Barriers to the adoption of independent reviews by non-public interest entities in South Africa : the current perceptions of South African professional accountants

A research report submitted by

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DECLARATION

I, Kudzinetsa Nyambuya (student number 1590692) declare that the work contained in this thesis is my own, except as indicated in the references and can be submitted in partial fulfilment for the degree of Masters of Commerce in Accounting for the School of Accountancy.

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Kudzinetsa Nyambuya

Signed at ______________________

Date__________________________

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ABSTRACT

Orientation: The South African Companies Act no. 71 of 2008 introduced independent reviews as an additional form of providing assurance for the non-public interest entities (non-PIEs) with the aim of reducing the reporting burden. Despite the Companies Act becoming effective on 1 May 2011, some companies which qualify for independent reviews still opt to have their annual financial statements (AFS) audited.

Research aim: The purpose of this study is to gain an understanding of the reasons that companies which qualify for independent reviews still select to have their AFS audited when there is a less burdensome option. The main research question is directed towards investigating why audits are still preferred to independent reviews and the barriers to the selection of independent reviews.

Motivation of the study: Small and medium-sized enterprises (SMEs) play a crucial role in the South African economy so it is critical to ascertain whether the independent review option is meeting its goal of reducing the reporting burden. The feedback provided assists the government in developing and updating strategies meant to support SMEs.

Research approach and method: The research follows a qualitative approach within an interpretive paradigm where the data were collected from a series of nineteen detailed semi-structured interviews with a sample of South African professional accountants with the relevant experience on the subject matter.

Main findings: The main findings indicate that audits are retained due to the need of small companies to reduce agency costs and appease the demands of various stakeholders, specifically lenders, lack of knowledge and guidance from practitioners regarding independent reviews, independent reviews being compared to audits, misconceptions and the resistance to change.

Contributions of the study: This study contributes to providing an understanding of the barriers to the successful adoption of independent reviews and also recommendations on how acceptance of independent reviews can be improved to meet the purpose of reducing reporting burden for non-PIEs in South Africa.

Keywords

Agency cost, assurance, audit, independent review, non-public interest entities, professional accountant

CONTENTS

ABREVIATIONS

ACCA	Association of Chartered Certified Accountants
AFS	Annual Financial Statements
APA	Auditing Professions Act
CA(SA)	Chartered Accountant (South Africa)
CIMA	Chartered Institute of Management Accountants
CIPC	Companies And Intellectual Property Commission
DTI	Department of Trade and Industry
IAASB	International Auditing and Assurance Standards Board
IAC	Institute of Accounting and Commerce
IAS	International Accounting Standard
IASB	International Accounting Standards Board
ICSA	Institute of Chartered Secretaries and Administrators
IFAC	International Federation of Accountants
IRBA	Independent Regulatory Board for Auditors
ISA	International Standard for Auditing
ISRE	International Standard on Review Engagements
MOI	Memorandum of Incorporation
non-PIEs	Non-Public Interest Entities
PIE	Public Interest Entity
PIS	Public Interest Score
RFT	Request for tenders
SAIBA	South African Institute of Business Accountants
SAICA	South African Institute of Chartered Accountants
SAIGA	South African Institute of Government Auditors
SAIPA	South African Institute of Professional Accountants

SAIT	South African Institute of Tax Practitioners
SMEs	Small and medium-sized enterprises

GLOSSARY

Analytical procedures	Evaluations of financial information through analysis of plausible relationships between financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships which are inconsistent with other relevant information or that differ from expected values by a significant amount.
Assurance engagement	An engagement in which a practitioner aims to obtain sufficient and appropriate evidence in order to express a conclusion designed to enhance the degree of confidence of the intended users, other than the responsible party about the subject matter information. Each assurance engagement is classified on two dimensions: Either a reasonable assurance engagement or a limited assurance engagement
Reasonable assurance engagement	An assurance engagement in which the practitioner reduces engagement risk to an acceptably low level in the circumstances of the engagement as the basis for the practitioner' conclusion. The practitioner's conclusion is expressed in a form which conveys the practitioner's opinion on the outcome of the measurement or evaluation of the underlying subject matter against criteria.
Limited assurance engagement	An assurance engagement in which the practitioner reduces engagement risk to a level acceptable in the circumstances of the engagement but where that risk is greater than for a reasonable assurance engagement as the basis for expressing a conclusion in a form that conveys whether, based on the procedures performed and evidence obtained, a matter(s) has come to the practitioner's attention to cause the practitioner to believe the subject matter information is materially misstated.
Practitioner	A professional accountant in public practice
Population	The entire set of data from which a sample is selected and about which the auditor wishes to draw conclusions.
Review engagement	The objective of a review engagement is to enable an auditor to state whether, on the basis of procedures which do not provide all

	the evidence required in an audit, anything has come to the auditor's attention which causes the auditor to believe that the financial statements are not prepared, in all material respects, in accordance with an applicable financial reporting framework.
Review procedures	The procedures deemed necessary to meet the objective of a review engagement, primarily inquiries of entity personnel and analytical procedures applied to financial data.
Independent reviewer	A person appointed to perform an independent review in terms of regulation 29 of the companies act.

1 INTRODUCTION

1.1 Background

The introduction of the Companies Act no. 71 of 2008 referred to as the “Companies Act” by the Department of Trade and Industry (DTI) in South Africa led to the exemption of the previously mandatory audit requirement for certain non-PIEs which meet the requirements for an independent review in terms of regulation 29 and the exemption requirement in terms of section 30 (2A) (Companies Act 71, 2011a). The Companies Act became effective on 1 May 2011, however, to date there are still some companies which qualify for independent reviews but still opt to have their AFS audited (CIPC, 2016). This inspired the study to obtain an understanding of the opinions of professional accountants in the post implementation phase of independent reviews. The period of more than seven years after the effective date allows for the understanding of the various factors at play in the implementation and acceptance of independent reviews.

The DTI replaced the Companies Act no. 61 of 1973 “the previous Act” which had been in existence for more than 30 years with the current Companies Act no. 71 of 2008 effective 1 May 2011 (Odendaal and De Jager, 2011a). In terms of the previous Act, all companies were required to appoint an auditor at every annual general meeting and have their AFS audited. This created a statutory duty on all companies to be audited, regardless of their size, the category of company i.e. private or public company, or whether it was in the best interest of the company or the needs of its stakeholders.

In most companies or organisations there are various corporate relationships either with owners, providers of funds or various levels of management. As a result, the agency theory predicts that whenever there is a corporate relationship involving the separation of ownership and control, the agent to whom the control decisions are delegated will make decisions in their best interest (Jensen and Meckling, 1976). The companies’ AFS are used as monitoring tools for the management’s activities while assurance provided by an independent party is important to enhance the credibility of the of the AFS (Odendaal and De Jager, 2010).

The overall objective of an audit is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error (IAASB, 2016). This enables the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework and to report on the financial statements, and communicate as required by the International

Standard for Auditing (ISAs), in accordance with the auditor's findings (IAASB, 2016). As a result, an audit provides a reasonable level of assurance which is a high form of assurance. While the objective of a review engagement is to enable an auditor to state whether, on the basis of procedures which do not provide all the evidence required in an audit, anything has come to the auditor's attention causing the auditor to believe that the financial statements are not prepared, in accordance with an applicable financial reporting framework (IAASB, 2016). An independent review, on the other hand, results in a limited level of assurance due to the fact that fewer procedures are performed. This result in less financial and time resources being demanded from companies compared to audits.

In as much as audits produce a higher level of assurance, it was argued that the imposition of compulsory audits on small companies made them bear unreasonably high reporting costs, especially if they did not have external users or that information is not of great use to external users (Seow, 2001). Additionally the costs borne by smaller companies on audits were disproportionately high as larger companies enjoy economies of scale (Keasey, Watson and Wynarczyk, 1988). As a result, there were calls for the government to support small companies by reducing their reporting burden and improve their survival aspects: this is also aligned with the audit deregulation requirement implemented in other jurisdictions e.g. the United Kingdom (UK), the United States of America (USA) and Canada. This led to the implementation of the Act, the primary objectives of which include: promoting the development of the economy by encouraging enterprise efficiency, aligning with international practices, promoting entrepreneurship development by reducing the regulatory burden for small companies by creating flexibility and simplicity in the maintenance of companies (DTI, 2011).

The Companies Act introduces the concept of protecting the public interest, so regulations determining which companies are audited or independently reviewed should meet this objective (Companies Act 71, 2011a, Odendaal and De Jager, 2011a). The change in the requirements was made to ensure that non-PIEs are not overburdened by compliance requirements which are more appropriate to the larger companies (Dedman, Kausar and Lennox, 2014, Seow, 2001, Van Wyk, 2009). This was due to the mandatory auditing requirement imposing costs especially on non-PIEs for which limited benefits were obtained (Dedman et al., 2014, Keasey et al., 1988, Van Wyk, 2009). In any case, the non-PIEs may voluntarily perform audits if it's in their best interest to do so (Dedman et al., 2014).

1.2 Purpose of study

The purpose of this study is to obtain an understanding of the reasons why some non-PIEs which qualify for an independent review may opt to have their financial statements audited, yet there are more costly and not compulsory in terms of the law. Limited research exists, even in other jurisdictions, on the reasons for the assurance choice; additionally studies performed in other jurisdictions do not cater for country specific factors including social, historical, cultural, legal and economic differences, thus providing limited usefulness (Collis, 2012).

An investigation was performed with selected South African professional accountants, who are registered members of the South African Institute of Professional Accountants (SAIPA) or the South African Institute of Chartered Accountants (SAICA) respectively, regarding the considerations taken into account by small companies when making the selection of either an audit or independent review. The cost of an audit is more than that of an independent review as such the fact that some entities still opt to be audited when they qualify for an independent review, inspired this research (Odendaal and De Jager, 2010).

The current legislation has been effective for more than 7 years, yet according to the results of a survey on a sample of practitioners published by the Companies and Intellectual Property Commission (CIPC) in December 2016, it was noted that about 24% of the practitioners' clients who qualified for an independent review opted to have their financial statements audited (CIPC, 2016). The period of 7 years allows the professional accountants to understand the factors affecting the continued retention of audits and scepticism about independent reviews.

The majority of the practitioners in the survey whose clients qualified for independent reviews were registered members of SAIPA (45.61%) while 27.41% were SAICA registered members as such the need to consider their views in this study. The rest of the participants belonged to the following professional bodies Chartered Association of Certified Accountants (1.1%), Chartered Secretaries Southern Africa (2.63%), Independent Regulatory Board for Auditors (18.42%), Chartered Institute of Management Accountants (0.44%), Chartered Institute for Business Management (0.22%), Institute of Accounting and Commerce (2.19%), South African Institute of Business Accountants (1.32%), South African Institute of Government Auditors.(0.66%)

Additionally, the views of SAIPA or SAICA registered accountants were considered in this study because they have experience in the reporting of the financial statements, they have insights regarding the reporting choice selection and will be able to provide useful and valuable information for this study. Furthermore, SAIPA and SAICA are the only International Federation of Accountants (IFAC) member organisations in South Africa hence the need to obtain their insight.

An empirical study was conducted before the implementation of independent reviews by Odendaal and De Jager (2011b) regarding the perceptions of South African Chartered Accountants CA (SA) and Registered Auditors (RA) on independent reviews (Odendaal and De Jager, 2011c). The results of their study indicated that the majority of the practitioners anticipated a significant demand for independent reviews in South Africa (Odendaal and De Jager, 2011b, Odendaal and De Jager, 2011c).

This research investigates the perceptions of professional accountants regarding reasons affecting the retention of audits, by covering the period after the implementation of independent reviews. As noted earlier, the objective of the DTI was to encourage economic participation so under the current legislation in addition to registered auditors, professional and chartered accountants are now eligible to perform independent reviews as opposed to previously when they were excluded from such activities. This study will obtain the views of professional accountants who are members of SAIPA or SAICA respectively as they are role players in the accounting industry, traditionally have small entities as their clients, are now eligible to perform independent reviews and are also experienced in the performing of accounting and assurance services.

1.3 Research question

What are the barriers to the adoption of independent reviews and reasons causing some non-PIEs to select audits when they meet the requirements for independent reviews?

1.4 Significance of study

The significance of this study will be shown based on the theoretical, methodological, and practical contributions (Regoniel, 2015). SMEs play a crucial role in the various sectors of countries' economies, most specifically by creating employment, social stability and the developing of skills (Carey, 2015, Ladzani and Van Vuuren, 2002, Lukács, 2005). They also contribute to the economic development and, to a great extent, they generate technical innovation (Rothwell and Zegveld, 1982, Savlovschi and Robu, 2011). However, these entities struggle for survival, so it is important for practical feedback to be obtained in order to ensure that relevant support is continually updated and provided to the SMEs sector.

Theoretical contributions

This study will expand on the existing literature on independent reviews as a form of assurance for non-PIEs as there is limited empirical research in this area (Rennie, Senkow, Rennie and Wong, 2003). Additionally, this study uses the agency theory to provide a detailed understanding of the retention of audits even in the face of independent reviews in a South African context. The use of the agency theory to explain the retention of audits in the face of deregulation has been performed in other jurisdictions (Chow, 1982, Collis, 2012, Dedman et al., 2014, Seow, 2001), but the social economic circumstances differ significantly providing a potential to identify specific factors to the South Africa environment.

Methodological contributions

The methodological contributions entail how the use of a different research design enhances and extends the existing body of knowledge (Kogut, 2009). Traditionally quantitative approaches have been used in the determination of reasons affecting the retention of audits (Collis, 2012, Dedman et al., 2014, Rennie et al., 2003, Senkow, Rennie, Rennie and Wong, 2001). This study introduces the use of a qualitative approach which involves interviews to obtain views of the participants and an in-depth understanding of the retention of audits in a South African context (Atkins and Maroun, 2015).

Practical contributions

This study contributes to the understanding of the reasons for the assurance choices made by some non-PIEs and the likely barriers or challenges of independent reviews. Independent reviews were introduced to ensure that small companies provide less rigorous, less burdensome, less onerous and less costly assurance to users than an audit (Odendaal and De Jager, 2011a). The findings of this study should contribute towards providing feedback on the DTI policy to determine whether the goal of trying to reduce the reporting burden is being realised. This is because the study allows for the identification of the operational challenges associated with the non-PIEs' assurance framework. The study also provides an opportunity to generate efficient and sustainable recommendations which can be applied in the assurance policy making decisions meant to assist and support small companies in South Africa.

1.5 Delimitations

The study only investigates the perceptions and views of South African professional accountants affiliated with either SAIPA or SAICA. Other South African professional accountants affiliated with the following bodies SAIBA, CIMA, ACCA, IAC, SAIGA, ICSA and SAIT were not invited to participate in the study. CIMA affiliated professional accountants were specifically excluded as they focus on management accounting for accountants working in industry while ICSA qualifies people who have roles as company secretaries, governance advisers, risk managers, compliance managers and SAIT focuses solely on taxation accountants working in industry (Accounting Weekly, 2014). SAIBA is an accounting and financial professional board, so in addition to providing accounting work to the public, it also caters for anyone in the accounting department including debtor clerks, creditor clerks, financial controllers, marketing and operations managers as a result the members were excluded from the study (Accounting Weekly, 2014). Additionally participants' selection focused on their affiliation with SAIPA or SAICA and not specifically on whether they owned or managed SMEs in their personal capacity. In instances where the participants were SME owners it was mere coincidence.

The views are also limited to considerations taken into account by non-PIEs which can either select between an independent reviews or an audit as such does not cater or provide explanations for those non-PIEs that qualify for an audit exemption. Additionally this paper considers the perceptions of professional accountants who operate in various sectors and does not focus on any specific industry or sector reporting requirements. Furthermore this paper does not measure the extent to which independent reviews have been adopted in South Africa but considers views on why independent reviews are not widely adopted by non-PIEs.

1.6 Assumptions

As an interpretive approach is followed, the study assumes that financial accounting and assurance is a social science as a result knowledge, reality and meaning are constructed by the human actors, their interactions with one another and the environment in which they operate in (Baker and Bettner, 1997). Accounting activities are, therefore, designed and constructed by human interventions which change over time (Coetsee, 2011). This results in what is considered to be true being different to different actors and also changing over time (Coetsee, 2011).

It is also assumed that the professional accountants due to their key role in the provision accounting services, significant level of experience in the accounting profession and direct involvement in the provision of accounting services to non-PIEs have adequate knowledge regarding the considerations taken into account by their clients in the independent review or audit decisions. In addition it is also assumed that the various respondents provide honest and truthful information regarding their general experience and observations because of the fact that they volunteered to participate and that their anonymity and confidentiality were protected. It is also assumed that the responses were not rehearsed as the interview agenda, not the interview questions, was send close to the interview days and not long in advance (Leedy and Ormrod, 2015).

1.7 Overview of the study

Building on the introduction provided in the current chapter, this report presents chapter 2 in the following section, which provides the literature review where a critical analysis of the existing body of knowledge regarding what has been done on the topic and the key issues identified was addressed (Hart, 2018). Chapter 3 then presents the research method section, outlining the systematic steps undertaken to solve the research problem (Kothari, 2004). This is then followed by chapter 4 which provides the analysis and interpretation of the information gathered from the respondents. Chapter 5 provides the conclusion of the study together with the recommendations and areas of future studies.

2 LITERATURE REVIEW

2.1 Introduction

The literature review was formulated using a systematic review which entailed the explicit and rigorous analysis of the existing body of knowledge (Engelbrecht, Yasseen and Omarjee, 2018, Greenhalgh, Robert, Macfarlane, Bate and Kyriakidou, 2004, Onwuegbuzie, Leech and Collins, 2012). This methodology allowed for the synthesis, evaluation and interpretation of knowledge from various sources to assist in the answering of the research question (Greenhalgh et al., 2004, Hart, 2018, Onwuegbuzie et al., 2012). The review of various sources enhanced the identification of variables relevant to the research topic and the identification of relationships between theoretical concepts and practice (Onwuegbuzie et al., 2012). The researcher performed meta-evaluation on whether to include or exclude sources and this enhanced the quality and legitimacy of the literature (Engelbrecht et al., 2018, Onwuegbuzie et al., 2012) in answering the question concerning why some companies still performed audits even though they are more costly and not required by law.

The literature review is structured as follows: section 2.2 introduces the agency theory as the theoretical framework which explains the demand of external assurance. This is followed by section 2.3 which provides the legislative requirements of the Companies Act to develop the context and background of this current study. Section 2.4 and 2.5 compare and contrast audits and independent reviews to identify potential factors influencing the choice selection, enabling the development of an interview agenda. Lastly section 2.6 provides some additional factors which significantly influence non-PIEs in their audit or independent review selection process.

2.2 Agency theory

An agency relationship exists when there is separation between ownership and control i.e. a principal contracts an agent to make decisions on his/her behalf (Jensen and Meckling, 1976, Wallace, 1980). The agency theory predicts that, as both parties are utility maximisers, the agent will not always make decisions which are in the best interest of the principal (Jensen and Meckling, 1976, Wallace, 1980). To attain optimal decisions for the principal, unavoidable agency costs made up of monitoring expenditure by the principal, bonding costs by the agent and residual loss will be incurred (Jensen and Meckling, 1976).

Agency cost can, as a result, be expanded to all organisations and any other relationships which involve cooperative effort, including various stakeholder relationships (Eisenhardt, 1989, Jensen et al., 1976, Wallace, 1980). Agency costs become higher as the separation of control and ownerships increases e.g. in large corporations between shareholders as the principal and directors as agents (Carey, Simnett and Tanewski, 2000, Collis, Jarvis and Skerratt, 2004). In addition, the agency costs also increase as the size and complexity of the organisations increase (Collis et al., 2004).

However, agency costs still exist even in smaller companies, despite the fact that the complexity or the separation of power and ownership may be less than in large organisations (Seow, 2001). In small organisations, the principals include mostly external shareholders, providers of credit i.e. anyone who is distant from management actions and cannot verify those actions directly (Collis et al., 2004).

The agency theory also states that in new and small organisations with limited resources available for weathering uncertainty, the likelihood of failure may be high so some risk averse owner-managers may transfer the risk to the supplier of funding (Eisenhardt, 1989). Agency based incentive problems may be reduced by independent and effective monitoring techniques (Baylis, Burnap, Clatworthy, Gad and Pong, 2017). The magnitude of the agency cost is limited by how well the stakeholders, such as banks, monitor the actions of owner-managers (Ang, Cole, and Lin, 2000). To maintain agency relationships, great reliance is placed on audited financial statements, even for small organisations (Collis et al., 2004).

Banks provide the main source of external funds for small business; as a result they play a pivotal role in their financing (Ang, Cole and Lin, 2000, Berry, Faulkner, Hughes and Jarvis, 1993). However they bear a significant risk when owner-managers utilise borrowed funds to engage in investment activities which promise high returns, with even lower success probabilities as the owner-managers stand to gain if success is achieved, yet the lenders' returns are fixed, while they stand to lose more if success is not attained (Chow, 1982, Eisenhardt, 1989, Jensen et al., 1976). There is also risk that the owner managers utilise the funds obtained for personal use or diverge from the agreed purpose (Carey et al., 2000). Lenders, therefore, make use of debt contracts which rely on accounting numbers; however, the preparation of these, is the responsibility of owner-managers, creating an incentive for them to distort the accounting figures (Baylis et al., 2017). Lenders will anticipate the incentive of owner-managers to transfer wealth or distort accounting figures and put monitoring techniques such as the verification of the financial information by independent parties in place to protect themselves (Dedman et al., 2014, Seow, 2001).

Despite audited accounts traditionally playing an agency role between the external shareholders and directors (Collis et al., 2004), audited financial statements also provide credible financial information which allows lenders to assess the risks of the entities requiring funding and determine whether the companies they have provided with funding will be able to meet their repayments obligations (Dedman et al., 2014, Senkow et al., 2001, Seow, 2001). In terms of the agency theory, lenders employ various monitoring activities, including requiring audited financial statements and covenants, to limit the owner-manager and protect their own interests (Jensen and Meckling, 1976, Senkow et al., 2001).

In small organisations, information asymmetry may also exist with internal shareholders or owners (Collis et al., 2004, Power, 1997). This can be attributed to owner-managers of small entities lacking the financial sophistication, being incapable of performing random audits or fully understanding the financial results (Ang et al., 2000, Collis et al., 2004). This leads to small entities typically having poor record keeping and owner-managers often exercising flexibility with certain cost items (Ang et al., 2000).

Auditing, formal control systems and budget restrictions are tools utilised to align the interests of the stakeholders and managers (Jensen and Meckling, 1976). Companies are more likely to be audited voluntarily when the agency costs are high (Dedman et al., 2014). The owner-manager is willing to expend resources by incurring bonding costs in the form of contractual guarantees to have the financial statements independently audited to assure the protection of stakeholders' interests, as long as these marginal costs are less than the additional benefits derived (Chow, 1982, Jensen et al., 1976).

Additionally the owner-managers agree to bear these agency costs as they already produce most of the information required by the lenders for internal decision making purposes and it is also in their best interest to have the accuracy of their reports verified by an independent auditor (Jensen et al., 1976, Seow, 2001, Wallace, 1980).

Conversely, to avoid these agency costs, the owner- manager will invest his own wealth into the firm before resorting to outside funding (Jensen and Meckling, 1976). Debt will then be used if the ability to exploit potentially favourable investment opportunities are limited by the resources of the owner (Jensen and Meckling, 1976).

Agency costs are expected to be lower for smaller companies in which a single family holds a controlling interest of more than half of the firm's equity (Ang et al., 2000). However, although there is a close link between ownership and control, agency costs still exist even in such entities because of conflicts of interest among family members or as non-family members start to participate in management or representation on boards of directors (Carey et al., 2000, Collis et al., 2004).This confirms the existence of agency cost in every corporate relationship and so the need to monitor such costs by demanding independent assurance.

2.3 Assurance requirements of the Act

The objective of general purpose financial reporting is to provide financial information about the reporting entity which is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity, as they cannot request reporting entities to provide information directly to them (IASB, 2018). Preparers have an obligation to the primary users who rely on the general purpose financial statements. However, there may be a conflict of interests between the information preparers and the users, resulting in biased information production and this hinders the usefulness of those AFS. This is due to the fact that AFS are used as a monitoring tool for management's performance, yet they are the preparers of the financial information, while the users do not have the ability to access directly or verify the quality of the information (Wallace, 1980). So it is for the protection of the users and the public at large that assurance provided by an independent party is required in terms of the Act.

The Companies Act compulsorily requires companies to be audited if it is in the public interest i.e. everyone with a direct or indirect interest in the company activities (Odendaal and De Jager, 2011a). The term 'public interest' is not defined by the Companies Act but quantitative measures of turnover, third party liability, size of workforce, and membership size or securities ownership play a role in the determination of the public interest score (PI Score) which then is used to assess whether a company is in the public interest (Companies Act 71, 2011a). Regulation 26 (2) provides for the calculation of the PI Score of a company for each year by summing points attributed to various aspects of the company which include the average number of employees, the level of third party liability, the amount of turnover for the year, in the case of profit companies, the number of individuals who have a beneficial interest in the company's issued securities and, in the case of a non-profit company, the number of individuals who are members of the company (Companies Act 71, 2011b). In as much as quantitative measures play a role in the determination of the public interest, significance is given to the economic or social significance of the company, the nature and extent of the company's operations (Companies Act 71, 2011a, Odendaal and De Jager, 2011a). (Please refer to Appendix B for guidance on the calculation of the PI score.)

The Companies Act requires AFS to be audited for all public companies, profit or non-profit companies where it is desirable in the public interest and companies whose Memorandum of Incorporation (MOI) or shareholders resolution requires it, regardless of their PI Score (Companies Act 71, 2011a). Audits are only compulsory for public companies, state owned companies, profit or non-profit companies holding assets in a fiduciary capacity in excess for R5 000 000 for unrelated parties, non-profit companies incorporated by the state to perform statutory functions, companies whose PI Score is 350 or more or whose public score is at least 100 but less than 350 and whose financial statements were internally compiled (Companies Act 71, 2011b).

Table 1: An illustration of companies mandatorily required to be audited

Company category	**Audit/ Independent review requirement**
State owned companies	Audit
Public companies (listed and non-listed)	Audit
Profit or non-profit companies which hold assets in excess of R5m in a fiduciary capacity for unrelated parties	Audit
Non-profit companies which are state of foreign controlled or perform a statutory or regulatory function.	Audit
Profit or non-profit companies the PI Score of which the particular financial year is at least 350	Audit
Profit companies or non-profit companies, for which their PI Score for the particular financial year is at least 100 but less than 350 and whose statements are internally compiled.	Audit

As an alternative, the Companies Act introduced independent reviews and audit exemptions for companies which are not in the public interest. As a result, on the other spectrum will be entities exempt from both audits and independent reviews in terms of section 30 (2A) unless if an audit is required by their MOI or they have opted for a voluntary audit (Companies Act 71, 2011b). Companies in which every holder of any securities issued by the company is also a director of the company and the company does not fall under classes of companies required to be audited as mentioned above (Companies Act 71, 2011a), qualify for exemptions. The exemption requirement also ensures that companies are only audited if it is in the public interest (Odendaal and De Jager, 2011a). Since the focus of this research is not such companies, no further details will be provided.
Therefore, profit or non-profit companies whose PI Score is less than 100 or whose PI Score is at least 100 but less than 350 with independently compiled AFS qualify for an independent review (Companies Act 71, 2011b, SAICA, 2008). It follows that companies with low PI scores will qualify for independent reviews which generally are small companies or companies which operate in the SMEs environment as the PI score is calculated based on the operational quantitative measures.

Relevant for this research would be non-PIEs whose PI score is less than 100 and those with a PI score of at least 100 but less than 350 if their AFS are independently complied. This is because these are the companies which qualify to have independent reviews, yet at the same time may voluntarily perform audits if they choose to do so. They fall into the category that enables us to understand the research question on why companies which qualify for independent reviews may still opt to be audited.

Table 2: An illustration of companies qualifying for independent reviews

Company category	**Manner in which financial statements are compiled**	**Qualification**
Profit companies or non-profit companies of which the PI Score for the particular financial year is at least 100 but less than 350.	Independently compiled.	Independent review.
Profit companies or non-profit companies of which the PI Score for the particular financial year is less than 100.	Independently compiled.	Independent review.
Profit companies or non-profit companies, of which the PI Score for the particular financial year is less than 100.	Internally compiled.	Independent review.

In accordance with regulation 29 of the Act, companies must have their AFS independently reviewed in terms of International Standards for Review Engagements (ISRE) 2400 (Companies Act 71, 2011b). An independent review may not be carried out by an accounting professional who has been involved in the preparation of the AFS, regardless of the professional accountant being independent of the entity (Companies Act 71, 2011b). Independent reviews must be carried out by either registered auditors, or members in good standing of a professional body which has been accredited in terms of section 33 of the Auditing Professions Act (Companies Act 71, 2011b). Qualified accounting officers of close corporations may also carry out independent reviews, but only for companies whose PI Score is less than 100 (Companies Act 71, 2011b). So the scope of who can perform independent reviews is wide compared to audits which can only be conducted by registered auditors. Accountants whether they are registered with professional bodies or not, can perform independent reviews. Additionally the bureaucracy regarding registration with IRBA is eliminated thus award accountants the opportunity of starting they own practices and performing independent reviews This is in line with the goal of the DTI to encourage entrepreneurship and encouraging economic growth.

2.4 Auditing

Audits existed in the development of business corporations and were in existence even before their requirement as legislation (Watts and Zimmerman, 1983). Audits where created by markets as a tool to address the agency problem which existed as corporations became bigger and members gave up governing powers to managers who faced conflict of interests between their own welfare and that of the members/owners. It can be noted that the purpose of audits originated from the needs of society or users to reduce the opportunistic behaviour cost borne by the manager (Watts and Zimmerman, 1983). Over time though audits evolved in response to changes in the organisational forms, professional and legislation requirements (Watts and Zimmerman, 1983).

Audits are an essential part of financial reporting and play a crucial role in enhancing the quality of financial reporting systems, increasing the credibility of reported financial statements by reducing bias and the conflict of interest between the information preparers and the users (Chen, He, Ma and Stice, 2016, Collis et al., 2004, Seow, 2001, Wallace, 1980). In order to strengthen the degree of confidence of the intended users in the financial statements, the auditor has a responsibility towards the intended users of the AFS (Baylis et al., 2017, Chen et al., 2016, IAASB, 2016).

Expertise is required for complex information preparation and verification (Wallace, 1980): specifically with smaller entities which may not be capable of hiring the required financial or accounting experts (Seow, 2001) leading to their relying heavily on the auditors to identity any discrepancies and to make the necessary recommendations. Additionally audits improve the financial data utilized by managers in decision models e.g. capital budgeting, inventory planning, and break-even analysis, possibly by finding errors or providing error checks which make the financial statements more reliable (Collis et al., 2004, Wallace, 1980). This enables the company preparing financial statements to provide assurance to its users that the information is carefully prepared and credible (Wallace, 1980). The testing of controls during audits also allows the identification of weaknesses and recommendations which may result in improvements of internal controls over the operations (Wallace, 1980).

Consequently, auditing provides signals about the reduced measurement error of financial reporting, implying superior reporting quality more specifically if a reputable auditor has been used (Hay and Davis, 2004, Wallace, 1980). Audited financial statements of small companies also provide positive signals to lenders that the business is well managed (Collis, 2012). Additionally, audits play a role of checking borrowers' compliance with covenants in lending agreements to mitigate conflict of interest between the lenders and the shareholders (Baylis et al., 2017, Senkow et al., 2001).

An agency relationship also exists between the employees and the owner-managers, employees being the agents (Senkow et al., 2001). As a result, the threat of discovery possibly prompts employees to avoid the illegal extraction of company resources, redistribution of creditors' claim to shareholders, abuses of financial reporting standards and also incentivises them to be more careful in preparing financial records in anticipation of an audit (Wallace, 1980).

Auditing provides compensation for loss of control and additional supervision, specifically in growing entities as it becomes more difficult for the owners or management to provide direct and physical supervision which may lead to opportunism (Abdel-Khalik, 1993, Carey et al., 2000, Hay and Davis, 2004, Senkow et al., 2001). In addition, Seow (2001) also observed that audits are likely to be demanded in cases where the shareholders are not directors or involved in the day-to-day operations of the entity (Seow, 2001). As noted earlier audits provides the monitoring function for agency costs (Carey et al., 2000, Senkow et al., 2001).

Auditing is considered a desirable public good (Rennie et al., 2003), however, despite all the benefits associated with audits in general, it is crucial to consider the cost-benefits and limitations of audits to small companies. This is because motivations of large and listed companies for the selection of audits significantly differ from those of smaller companies which are not in the public interest (Collis, 2012). Regardless of the cost, Wallace (1980) argues that audit services are greatly valued by companies; otherwise their consumers would demand competing services. Additionally it is argued that audits are valued and retained because of their benefits and not just to satisfy the regulatory requirements (Wallace, 1980).

2.5 Independent reviews

The Companies Act requires that the AFS be independently reviewed in accordance with ISRE 2400 (Companies Act 71, 2011b). The International Auditing and Assurance Standards Board (IAASB) issued the ISRE 2400 revised, effective 31 December 2013, with the aim of providing a cost effective and value adding alternative to audits, most specifically for instances where an audit is not mandatory (Cowperthwaite, 2014).

In as much as independent reviews consist mostly of enquiries and analysis, it is crucial that the professional accountants have detailed knowledge and understanding of the clients' business and environment so as to design and perform the appropriate procedures, resulting in value adding advice to the client (Cowperthwaite, 2014). The reviewer is required to be sceptical, to exercise professional judgement, to dig deeper always and to obtain additional evidence through performing further procedures, mostly in cases where they identify unexpected trends (Cowperthwaite, 2014).

Independent reviews add value by providing independent assurance, increasing confidence in the credibility of clients' financial statements to a wide range of stakeholders (Cowperthwaite, 2014, IFAC, 2013, McGeachy-Colby, 2014, Rennie et al., 2003). Therefore, independent reviews provided by an objective and independent professional accountant yield a meaningful level of assurance to clients and users (Cowperthwaite, 2014). Similarly, professional reviewers also add value by providing tailored business advice to clients due to their business experience and vast understanding (Cowperthwaite, 2014, McGeachy-Colby, 2014).

Additionally independent reviews provide a cost effective assurance in cases where an audit is not required and the operations of the entity are not complex (Cowperthwaite, 2014, IFAC, 2013, McGeachy-Colby, 2014). This is due to independent reviews being less time-consuming to clients (McGeachy-Colby, 2014) and fewer disruptions to company operations and management time, reducing the unnecessary burden of an audit which may be imposed on smaller companies (Seow, 2001).

Despite the perception that audits result in improved quality of financial statements information (Wallace, 1980), it has been argued that the perception of improved quality may not be as convincing in small company settings as these have fewer ownership structures (Chow, 1982). Incidentally, independent reviews also provide the preparation for growing business for the progression to audits (McGeachy-Colby, 2014). This is as a result of some of the procedures for independent reviews being similar to those of audits. For small and growing companies, this then provides them with the introduction to independent verification procedures and preparation for the audit process that becomes compulsory for entities in the public interest.

2.6 Other factors affecting the choice

2.6.1 The misunderstanding of level and type of assurance

Independent reviews provide limited assurance while audits provide reasonable assurance. A higher form of assurance obtained from an audit provides a greater level of confidence on the AFS as the procedures performed and evidence obtained are more, in-depth and rigorous. Concerns have been raised about whether users are able to differentiate between the level of assurance obtained from and independent review and from an audit (Gay, Schelluch and Baines, 1998). Even though a reasonable level of assurance is the highest form of assurance available, it is generally misinterpreted as an absolute level of assurance. An absolute level of assurance assumes that there is zero assurance risk so it is not attainable nor is it cost beneficial as auditing teams apply professional judgement and make use of persuasive, rather than conclusive evidence.

Incidentally, audits provide opinions in the form of positive assurance, yet with independent reviews there are no opinions expressed, rather negative assurance is provided by the reviewer (Odendaal and De Jager, 2011a). The negative assurance informs the reader that, as a result of the limited procedures performed by the reviewer, nothing has come to their attention which would cause them to believe that the financial statements are not presented fairly in accordance with the stated financial reporting framework (Abdel-Khalik, 1993, Gay et al., 1998). Once again concerns have been raised about the user’s ability to differentiate and understand the different types of assurance existing (Gay et al., 1998).

As audits have long been performed on all companies in South Africa, it is likely that users are quite familiar with the positive assurance, but it does not necessarily mean that they understand it. As independent reviews provide a negative assurance which is recent, the difference may not fully be understood. In addition, Watts and Zimmerman (1983) argued that an audit will be successful in reducing agency costs borne by the manager if the auditor is expected to report on any identified breaches of contract, but concerns arise about whether the negative form of an independent review allows the reporting of such breaches.

Table 3: Summary of the main differences between audits and independent reviews

Engagement	Audit	Independent review
Assurance level	Reasonable	Limited
Assurance type	Positive	Negative
Standards	ISAs	ISRE 2400
Procedures	Risk assessment procedures	Enquiries, observations and analytical procedures

2.6.2 The need to maintain the status quo

As audits are considered a public good, concern about their being under produced led to their being legislated in most jurisdictions (Rennie et al., 2003). However, it has been noted that, even under deregulation of audits, some companies continue to purchase audit services voluntarily. Consistency with previous years in an attempt of maintaining traditions of habits was identified as a factor influencing the audit retention decision (Collis, 2008). As audits have long been performed by companies, it is likely that they have been entrenched in the business culture and market participants are quite comfortable with what they entail and the level of assurance they provide. In accordance with prior research conducted in South Africa, some banks indicated that they would continue to require audits as they do not understand the level of assurance obtained from an independent review (Odendaal and De Jager, 2011a). This indicates the need to maintain the status quo and, to a greater extent, the element of resistance to change.

2.6.3 The stakeholders' influence in the decision selection

The objective of any assurance, be it an audit or an independent review, is to enhance the degree of user confidence (IAASB, 2016). Historically, AFS were prepared by managers and presented to shareholders or owners, and audits were used as a monitoring system between managers and equity holders (Carey et al., 2000, Watts and Zimmerman, 1983). Today a wider range of users i.e. stakeholders are interested in the analysis of AFS for purposes of determining e.g. the solvency, liquidity, profitability and success of entities so as to make informed economic decisions (Odendaal and De Jager, 2010).

Indirect evidence from the past also suggests that auditing was used to monitor debt instruments because of the inherent conflict of interests which exists between the equity holders and the debt holders (Watts and Zimmerman, 1983). Wallace (2004) identified lenders as the most significant stakeholders, whose requirements for audit influenced mostly the continuance of audited financial statements, followed by a parent company requirement for groups and then credibility of information as a final point (Wallace, 2004). In a study performed by Abdel-Khalik (1993), observations were made that lenders required audited financial statements from owner-managed companies as part of the lending agreements. This is also consistent with a study performed by Senkow et al (2001) in Canada which identified the most significant driver for voluntary audit demand as lending agreements. In addition the owners or parent company also played a significant role in the demand for audits due to their need for enhanced credibility (Senkow et al., 2001, Wallace, 2004).

As bank lending is the major source of funding for small business, banks rely mostly on financial information to make the lending decision (Berry et al., 1993, Collis, 2012). The credibility, quality and reliability of the financial information is of utmost importance, especially in smaller companies which may not have adequate security or existing relationships with the bankers (Berry et al., 1993). Berry (1993) argues that audited financial statements are preferred by bankers as they provide more reliable information than do management accounts or forecast as they would not have been verified by an independent party (Berry et al., 1993).

In light of this, companies will opt for voluntary audits to raise capital and if it’s in their best interest to do so (Dedman et al., 2014). They will consider the cost of elevated interest rates versus the cost of continuance of auditing where high interest rates are associated with non-audited financial statements (Senkow et al., 2001). Blackwell, Noland and Winters (1998) observe that companies which do not provide audited AFS to lenders tend to pay higher interest rates.

Additionally, small companies may still undertake audits to satisfy existing lender agreements or secure investment money from banks and other creditors (Dedman et al., 2014, Odendaal and De Jager, 2010). As an illustration, companies may already have existing debt covenants from before audit deregulation, requiring them to have audited financial statements so they would continue to be audited (Seow, 2001). It was noted that smaller companies continued to be audited even under deregulation because of the audit imposition placed on them by lenders and owners (Chow, 1982, Rennie et al., 2003).

2.6.4 The cost implications

There is a direct association between the level of assurance obtained and the cost of the audit to the company based on the tasks and time spent by the practitioner (Odendaal and De Jager, 2011a). Independent reviews result in lower expected costs as they involve fewer procedures comprising mostly of observations, enquires with the client personnel and analytical procedures applied to financial and non-financial information(Abdel-Khalik, 1993, Gay et al., 1998).

The results of prior research performed by Abdel-Khalik (1989) provided evidence that the cost of independent reviews was only one third, compared to that of an audit. One of the significant reasons for not retaining audits, according to a study performed by Senkow et al. (2001) in Canada was cost benefit assessments. This was also consistent with study by Rennie et al. (2003) which identified cost savings as the most important reason for the purchase of a lower level of assurance. It would seem that most companies prefer assurance on their financial statements at a low cost and independent reviews give rise to significant cost savings (Odendaal and De Jager, 2010, Wallace, 2004).

Conversely, it is important to note that auditing increases the value of the company, reduces the cost of capital for companies, increases market confidence and contributes to investor protection (Carey et al., 2000, Commission, 2010, Maroun and Solomon, 2014, Watts and Zimmerman, 1983). The owner-managers may still voluntarily opt for an audit and incur the higher cost if the benefits they anticipate are higher than the audit fees (Chow, 1982, Senkow et al., 2001). Cost benefit analysis is performed in order to determine the assurance choice.

Time saving was considered as another potential factor for the non-retention of audits (Seow, 2001). However, Wallace (2004) argues that, even for limited assurance, the accountant should thoroughly understand the client i.e. information infrastructure, and accounting systems so as to consider the inherent, control and detection risk (Wallace, 2004), and this may also require a significant amount of time.

2.6.5 Professional accountants' influence and advice

Previous research has identified external professional accountants as the most frequent source of business advice for the SMEs (Bennett and Robson, 1999). They also play a significant role in advising SMEs on regulation requirements (Collis, 2012). In some instances, the external accountants also submit the statutory documents on behalf of the small companies (Rennie et al., 2003). High levels of trust exist between the SMEs and the external accountants (Bennett and Robson, 1999). However despite the valued technical competency of accountants, it is very costly for small companies (Blackburn, Eadson, Lefebvre and Gans, 2006).

Carey (2015) also observed that the performance of SMEs is enhanced if business advice is purchased, together with auditing services. Kitching, Kasperova, Blackburn and Collis (2011) also identified the accountants' advice as being the primary reason for small businesses' financial reporting selections. In most instances, the accountants were responsible for informing the small companies about the reporting requirement options available and also advising them on the advantages and disadvantages of the options (Kitching et al., 2011). So the advice provided is based on what the external accountants think is appropriate, taking into account the cost-benefit analysis (Blackburn et al., 2006, Collis, 2012, Kitching et al., 2011).

On the other hand, the objective of auditors or reviewers of an assurance engagement, be it an audit or an independent review, is to reduce the engagement risk to an acceptably low level (IAASB, 2016). There is an association between the tasks and time required to obtain a certain level of assurance (Odendaal and De Jager, 2011a). Therefore, as the nature, extent and timing of procedures performed to obtain evidence under an independent review are less than that of an audit, the acceptable level of engagement risk is higher for the practitioner under an independent review than is an audit (Odendaal and De Jager, 2011a). Additionally, the fees obtained from audits are higher, based on the tasks and time required to obtain the required level of assurance. This provides the need to ascertain whether the advice provided by the auditors to their clients may be biased in favour of an audit so as to limit their engagement or litigation risk and increase their fees.

In addition, if the owner-managers are not well vested in accounting or lack proper training in business and management subjects then there is also a great reliance on auditors (Collis, 2012). Granted, in some jurisdictions auditors are prevented from providing other business advisory services (Carey, 2015), but Seow (2001) notes that if there is a high reliance on the auditor to provide other non-audit services then it is likely that the audit will be retained so as to maintain the good relationship (Seow, 2001).

The existence of a long standing relationship between the external auditors and a small company can also influence the decision by the smaller companies to voluntarily continue with audits (Seow, 2001). This is due to the fact that the retained accountant may have significant knowledge of the client's business and is in a strong position to discuss the costs and benefits of the various options and influence the decision.

2.6.6 Inconsistencies in the application of ISRE 2400

The guidance for the performance of independent reviews is provided in terms of ISRE 2400, but the approaches, nature, scope and extent of procedures under an independent review vary considerably (Odendaal and De Jager, 2011a). ISRE 2400 does not clearly distinguish whether it is a procedural standard or a risk standard. Some practitioners support a risk based approach while others advocate a procedure based approach (Odendaal and De Jager, 2010). This may affect the consistency of the procedures, tasks, timing, and level of judgement in determining the level of assurance provided. Differences in style and application between highly structured formal approaches and those allowing more professional judgement create practitioner concerns regarding optimal design of procedures (Power, 2003). This affects the consistency of procedures, comparability of various reports and may also increase the expectation gap between the reviewers and the users (Gay et al., 1998).

Reviewers may also end up performing too much or too little work as the guidance required in the performance of an independent review does not clearly distinguish a review from an audit

(Odendaal and De Jager, 2011a). If the reviewer performs too much work under an independence review because of the lack of proper guidance, it may end up costing the company too much for the lower level of assurance, defeating the purpose of reducing the reporting burden of smaller companies (Odendaal and De Jager, 2010). Professional competency in assurance skills, coupled with the use of automated technology, is important to ensure that reviews are performed effectively (Cowperthwaite, 2014).

2.6.7 The expectation gap

The expectation gap is a result of the differences between what the users expect from an audit and what the auditing profession defines the audit objectives to be (Sikka, Puxty, Willmott and Cooper, 1998). The users of financial reports expect auditors to detect and to report on material fraud and irregularities, while the auditing profession argues that the public misunderstands the role of the auditor as these are not major auditing objectives but are the responsibility of directors or management (Sikka et al., 1998). Nazri Fadzly and Ahmad (2004) observed that investors and brokers took the view that auditors were responsible for the preparation of financial statements, ensuring that the client's internal controls were designed and operating effectively, detecting and preventing all fraud. Their study indicated the existence of an expectation gap with some of the key users of AFS (Nazri Fadzly and Ahmad, 2004).

Corporate scandals and collapse of markets have contributed to the increase of the expectation gap (Hassink, Bollen, Meuwissen and De Vries, 2009), the lack of trust and confidence of the auditing profession and the work they (Gay et al., 1998, Hassink et al., 2009). The expectation gap may also potentially be increased because of the level of assurance perceived by users in audits or independent reviews being higher that the level of assurance provided by practitioners (Odendaal and De Jager, 2011b). In addition some inconsistencies in independent review approaches, nature, scope and extent of procedures may also increase the expectation gap between the reviewers and the users (Gay et al., 1998).

2.6.8 Clients' need for value add services

It has been argued that monitoring activities such as auditing and formal control systems increase the value of the entity (Jensen and Meckling, 1976). Robust audit has been identified as being a source of legitimacy for organisations, contributing to investor protection and reducing the cost of capital for companies (Commission, 2010, Maroun and Solomon, 2014).

In addition the auditors have the capacity to add value for their clients through the provision of business advice (Abdel-Khalik, 1993). Inherent and control risks are considered high in small business (Collis et al., 2004). This is as a result of their lack of skills and knowledge regarding internal or financial controls, their difficulty in hiring competent staff at competitive salaries so they rely on external accountants expertise for advice (Carey, 2015). Due to the accountants' expertise and economies of scale the practitioners may be able to perform certain tasks more effectively and efficiently than the client personnel.

Consequently, external accountants are in a better position to provide a wide scope of specialised services than the client personnel (Chow, 1982). External accountants are also able to advise their long-term clients because of the knowledge obtained from the clients over time, yet new clients also get to benefit from the accountant's industry experience (Carey, 2015, Collis, 2012). Additionally audits enable an in-depth understanding of the accounting records and systems of companies, as well as industry specific knowledge providing potential for the auditors to give business advice and to improve internal controls (Carey, 2015, Collis, 2008).

Carey (2015) observed that small business exhibit superior performance after purchasing business advice from external accountants and that the performance is further enhanced when business advice is jointly purchased with auditing. This then allows auditors to add value to their clients' businesses and to charge a nominal fee on the other non-audit services provided such as taxation, consulting or advisory services due to the existing understanding of the client business and operations (Seow, 2001).

2.7 Summary

The literature review section has identified the role agency relationships play in the demand for independent assurance as a tool of monitoring opportunistic behaviour by those entrusted with the control and decision making authority. This was followed by the background of how the Companies Act requires companies to provide assurance, either through audits or independent reviews, with the main purpose of enhancing financial accountability so as to protect the public interest. In the next sections, comparisons were provided between audits and independent reviews to identify the potential reasons for the selection made by companies. Eventually, additional factors and considerations on the retention of audits were provided, based on similar prior research to establish a background and provide a platform for answering the research question. The next section will discuss the methodology.

3 RESEARCH METHOD

3.1 Introduction

This section covers the approach, strategy, together with the various techniques and procedures, employed by the researcher in order to solve the research question. Sections 3.2 provides the research methodology which is the ideological foundation of the method (Wahyuni, 2012) and the systematic way in which the researcher answers the research question (Kothari, 2004). This is then followed by the research design in section 3.3 which connects the research methodology and the suitable methods and techniques implemented by the researcher in order to solve the research problem (Wahyuni, 2012). The rationale for methodology and the design is also provided to enhance the validity of the results. Section 3.4 provides the procedures followed by the research in selecting the relevant sample of interviewees to participate in answering the research question. Section 3.5 presents the procedural steps of how the data was collected by the researcher through semi structured interviews. This is then followed by section 3.6 which provides details on how a thematic analysis was used to systematically analyse and interpret the data. Section 3.7 provides the limitations of the study while section 3.8 discusses the measures put in place to enhance the validity and reliability of the study. This is then followed by section 3.9 which outlines the ethical considerations and safeguards to ensure that the data was produced morally.

3.2 Research methodology

A paradigm is explained as a whole system of thinking or fundamental beliefs affecting how social research is conducted, including the methodology choice (Neuman, 2013, Wahyuni, 2012). As the area of independent reviews is understudied with limited publications, a qualitative exploratory approach using detailed interviews was adopted, grounded in an interpretive (Alsaawi, 2014, Braun and Clarke, 2006, Friese et al., 2018, Rowley, 2012).

An epistemology paradigm is a philosophical dimension rooted in the belief that reality is based on social actors (Wahyuni, 2012). A positivism paradigm was considered inappropriate as it is based on the view that social reality is external and objective, as a result seeking to obtain law-like generalisations associated with quantitative approaches (Creswell and Clark, 2011, Neuman, 2013, Wahyuni, 2012). An interpretive paradigm assumes that knowledge is obtained through social constructions such as language, shared meanings, consciousness and people’s perceptions (Klein and Myers, 1999, Rowlands, 2005, Wahyuni, 2012). The interpretive paradigm aims to understand people by investigating opinions, perceptions and experience interpretation (Greener, 2008). In contrast to the positivism which assumes one objective reality, the interpretive researcher acknowledges that there are multiple perspectives of reality (Greener, 2008, Rowlands, 2005). As a result, the interpretive paradigm was selected as it allows the exploration of perceptions, views and experiences of accountants, regarding the opting for audits or independent reviews.

A qualitative approach enables the exploration and understanding of meanings which individuals ascribe to social problems based on their interpretation of the world they engage in (Creswell, 2014): it allows the capturing and studying of complex phenomena occurring in natural settings (Leedy and Ormrod, 2015). Qualitative data allows for the gaining of a deeper insight and understanding of a problem than a quantitative approach which provides mostly a general understanding of a problem (Creswell and Clark, 2011).

A qualitative approach was selected as it allowed the gaining of detailed understanding regarding the complexities around the considerations made in the audit or independent review selection decision (Creswell, 2003). The qualitative approach allows the iterative process by which the researcher moves back and forth between the data collection and analysis (Rowley, 2012, Wahyuni, 2012).

The researcher selected nineteen knowledgeable participants with practical experience and knowledge regarding either the financial reporting or assurance environment for SMEs and the considerations taken into account in the audit or independent review decision, instead of selecting a large sample to make generalisations (Leedy and Ormrod, 2015). The number of interviews performed follows the recommendation of twelve interviews made by Rowley (2012) for qualitative research (Rowley, 2012). A higher number of nineteen was selected to make the sample better (Leedy and Ormrod, 2015). Additionally the interview sample was consistent with the sample size selections from prior research (Engelbrecht et al., 2018, Pandya, 2016). The perceptions of the participants and the aims of the research make the interpretive approach subjective (Vosloo, 2014). However, Maroun (2012) argues that there is nothing wrong with subjectivity or the absence of complicated statistics in a research paper. An interpretive or critical approach may be conceptually superior to the quantitative styles as importance is placed on the social and cultural interconnections (Maroun, 2012).

The researcher’s involvement in the data collection and analysis process also makes the study subjective (Leedy and Ormrod, 2015). This is a feature of qualitative research and does not undermine the validity and reliability (Creswell, Hanson, Clark Plano and Morales, 2007). Qualitative designs are considered useful for addressing explanatory or interpretive research questions, enabling the identification of important variables which is crucial in this study as the research area is understudied (Creswell, 2003).

3.3 Research design

The research design focuses on all the procedures and steps relevant in answering the research problem. The research design provides a research framework and plan which guides and links the methodology and the research method (Wahyuni, 2012). The research design provides an overall plan, as well as the collection of data. In the current study, the researcher chose interviews to obtain the perceptions and opinions of the participants regarding the assurance choice selection.

Interviews are appropriate in collecting insights or understanding opinions, attitudes and experiences about a phenomenon (Alsaawi, 2014, Greener, 2008, Rowley, 2012). The data from prior literature was used in the development of the interview agenda so as to investigate the perceptions of professional accountants regarding the considerations taken into account in the independent review or audit selection (please refer to Appendix A for the agenda). Interviews also ensure that participants are able to gain clarity and to interpret and describe the matter under discussion in a manner with which they are comfortable.

Semi structured, open-ended questions developed from the literature were used to obtain an in-depth understanding of how these considerations affect the independent review or audit decision. Semi structured interviews are a hybrid type of interview which lies between structured and in-depth interviews, having the merit of predetermined questions while also allowing participants to talk freely (Rubin and Rubin, 2011, Wahyuni, 2012). This allowed a deep and thorough examination of the investigation (Alvesson, 2003, Creswell, 2003, Greener, 2008, Rubin and Rubin, 2011).

Open-ended questions were used to avoid rehearsed responses to gain information and perspectives not planned for, improving the validity and reliability (Rowley, 2012). Open-ended questions also allow the flexibility which is crucial for capturing various viewpoints and wide range of experiences (Creswell, 2014, Rowley, 2012). This also provides an opportunity for prompting and probing of perceptions to attain clarity, following up on interesting points and also addressing inconsistencies which may occur in the interviewees responses (Bryman and Bell, 2015, Rubin and Rubin, 2011).

The questions designed were broad and general enough to allow the interviewees to construct their own meanings and not be influenced by the researcher’s views (Creswell, 2014). This makes the comparison and integration of the interview transcripts complex (Rowley, 2012) but, because this is an understudied area in South Africa, it allowed the researcher to obtain a detailed insight of the perceptions.

Additionally, the use of semi structured, open-ended questions also allowed the participants to construct the meaning of the situation so as to express their views while retaining focus on the research question (Creswell, 2003). The study relies on the participants' views regarding their practical experience of the considerations made in the independent review or audit selection decision (Creswell, 2003). The researcher acknowledges and brackets the influence of their personal background to allow the interpretation of the views of others (Creswell, 2003).

Prior literature was used to develop and refine the themes and questions incorporated in the agenda for the semi structured interviews (Creswell and Clark, 2011, Rowley, 2012). A pilot study was performed with two colleagues before the actual interviews commenced to ensure that the questions were precise, clear, objective and relevant (Alsaawi, 2014, Rowley, 2012, Wahyuni, 2012). To enhance validity, the data obtained from the pilot study was used to refine the interview agenda developed from the literature review to ensure that the questions were appropriate and relevant in answering the research question, enabling appropriate modifications to be made before hand (Alsaawi, 2014, Rowley, 2012).

3.4 Selection of interviewees

The appropriate design of interviews and selection of participants allows the generation of insights and understanding regarding phenomena (Rowley, 2012). The targeted population for this exploratory study is made up IFAC registered member organisations, which includes registered professional members of SAIPA or SAICA. This particular population was selected as they hold a significant market base for the provision of accounting, independent review and auditing services to small business in South Africa. SAIPA affiliated members specialise in accounting and independent review services mostly for small entities while SAICA members provide auditing, independent reviews and accounting services

The objective was not to test a hypothesis or make generalisations about the entire populations (Leedy and Ormrod, 2015). A small sample which is an inherent feature of qualitative research was selected from this population to allow for a detailed account of the phenomena (Creswell, 2014). The respondents selected for this study had to be registered SAIPA or SAICA members with at least five years' experience in the accounting profession. Additionally, the respondents needed to have experience either in the SME sector or in providing accounting services to the SME sector. In this current study, the researcher selected a diverse group of participants based on their knowledge and experience of the subject matter. Due to the selection of a small sample the knowledge obtained cannot support generalisation (Rowley, 2012).

There is no specified number of participants required to be interviewed for qualitative research (Alsaawi, 2014). As a result, purposeful sampling ranging from twelve to twenty five professional accountants was the gain for the detailed interviews (Leedy and Ormrod, 2015, Rowley, 2012). Rowley (2012) advocates for the use of twelve interviewees while Leedy and Ormrod (2015) recommend twenty five interviews so the aim for nineteen interviews was considered appropriate in the current study. Furthermore the number was subsequently considered to be sufficient based on the saturation principle of diminishing returns. This implies that the sample size was considered sufficient when the same information, stories, themes, issues or topics were continuously expressed by the participants (Alsaawi, 2014, Boyce and Neale, 2006).

Purposive sampling cannot produce statistical inferences regarding the population (Alsaawi, 2014, Rowley, 2012). The purposeful selection of a small group of professional accountants can lead to bias (Rowley, 2012) but it was necessary to ensure that only participants with the required experience and knowledge to provide insight were selected (Wahyuni, 2012). This group was well vested in the provision of accounting services to small companies or directly involved in the performance of independent reviews and assumed to be information rich and knowledgeable in accounting and reporting needs of these small clients (Leedy and Ormrod, 2015, Van Wyk and Rossouw, 2009).

3.5 Data collection

Considering the purpose and the paradigm of the study, semi-structured interviews were used to collect the data. Based on referrals from colleagues in the academic or accounting profession, together with recommendations of previous interviewees, potential participants involved in the preparation of financial statements, independent reviewing or auditing process were identified. The intended participants were contacted in advance, either telephonically or through email, to request their involvement in the study (Rowley, 2012). The nature and purpose of the study, together with a detailed explanation regarding the participants, rights, guaranteed anonymity and confidentiality of their responses (Alsaawi, 2014, Boyce and Neale, 2006, Wahyuni, 2012). Ethics clearance for the interviews was obtained from the University of the Witwatersrand. Follow-ups were made to encourage involvement while invitations to make appointments on the interview dates were made with the participants who agreed to take part in the study (Rowley, 2012). Reminders of the request and the interview agenda were sent to the interviewees close to the interview date to enable them to obtain an understanding of the purpose of the study and its context (Boyce and Neale, 2006). Based on availability and preference of the participants, interviews were either performed in person or telephonically, mostly with participants in Durban or Cape Town. Nineteen interviews were conducted and took place from 16 April to 2 July 2018.

Before the interview commencement, permission to record the interview was obtained and the purpose of recording which was to ensure focus on the discussion without the disruption of taking detailed notes was explained to the participants (Alsaawi, 2014, Bryman and Bell, 2015). The interviewees were reminded that participation was voluntary, and of their right to withdraw from the study at any point (Leedy and Ormrod, 2015). Reassurance was provided regarding anonymity and that all the information would be kept private and confidential (Boyce and Neale, 2006). If direct quotes were used, they would be allocated codes and not be directly attributed to the individuals.

The researcher would ask the interviewees questions focused on obtaining a detailed understanding of the reasons for the continued demand of audits and the considerations taken into the audit or independent review selection decision. The topics in the agenda were used to guide the semi-structured interviews (Leedy and Ormrod, 2015). Precautions were put in place to avoid the preempting of responses, while making sure that the researcher restrained from providing reactions to the participants' answers. The open-ended questions allowed the prompting of participants in cases where their responses were unclear or inconsistent (Bryman and Bell, 2015, Rubin and Rubin, 2011).

Nineteen interviews were performed, based on the saturation principle, with interviews approximating 22 minutes to 80 mins to ensure that sufficient data were obtained (Rowley, 2012, Vosloo, 2014). In as much as there was a variation in the length of time taken for the interviews, the short interviews were also considered useful in obtaining insights so it should not be assumed that they are inferior to long ones (Bryman and Bell, 2015). The transcripts of the interviews were offered on request to the interviewees so that they could confirm the accuracy of the information (Leedy and Ormrod, 2015). The professional accountants were requested to provide consent to use the data obtained in the report (Boyce and Neale, 2006, Creswell and Clark, 2011, Rubin and Rubin, 2011, Wahyuni, 2012). Subsequently, the recordings and the contents from the interviews were stored under password protection to maintain confidentiality (Boeije, 2009, Wahyuni, 2012).

3.6 Data analysis and interpretation

A thematic analysis was followed, which is defined as the systematic method of identifying, organizing data and giving insight into patterns relevant in answering the research question (Braun and Clarke, 2006). The data analysis and interpretation was conducted using data analysis spiral and iterative process with the researcher analyzing data from interviews and reading of relevant literature (Braun and Clarke, 2006, Rowley, 2012, Wahyuni, 2012).

The first step of the data analysis spiral involved the organizing of the data. After the interviews, the researcher listened to the recordings and transcribed them into text form and also made notes of important points: this enabled familiarization (Alsaawi, 2014, Braun and Clarke, 2006, Friese et al., 2018, Rowley, 2012). The data from the recordings were converted into text in Microsoft word to enable easy analysis (Leedy and Ormrod, 2015). This step involved the researcher listening to the audio recordings more than once, then rereading the text and making relevant notes (Alsaawi, 2014, Braun and Clarke, 2006).

The second step involved revision of the data to allow the understanding of the content and the systematic development of codes (Alsaawi, 2014, Braun and Clarke, 2006). This once again required the rereading of the entire data in order to develop the various codes. In the initial phase, the researcher was open-minded in the identification of potential codes i.e. open codes resulting in a significant amount of codes (Boeije, 2009). Data items were read thoroughly and coded entirely before moving on to the next item where the process was repeated (Braun and Clarke, 2006). All the data relevant in answering the research question was coded (Braun and Clarke, 2006). Some codes were modified as additional data items were read and the systematic coding continued (Braun and Clarke, 2006).

The constant process of collecting, analyzing and interpretation of information was performed continuously. This was followed by the third step which involved the identification, categorising and grouping of emerging themes, referred to as open codes (Alsaawi, 2014, Boeije, 2009, Braun and Clarke, 2006). During this phase, the researcher started generating themes by shifting the codes to themes through the identification of similar and overlapping codes (Braun and Clarke, 2006). This allowed the identification of further themes arising from the interviews, requiring further reading of necessary literature (Leedy and Ormrod, 2015). Preliminary categories and sub-categories were identified during the re-reading of the text to enable the coding of the data (Leedy and Ormrod, 2015). To assist the tracking of the information provided and to protect anonymity and confidentiality, the participants were also allocated codes (Wahyuni, 2012). The themes identified from the transcribed data were used to group the contents of the data. A diligent and repetitive process was applied to identify themes so as to ensure completeness, eliminate vagueness and overlapping ideas.

To enhance the reliability of the coding, specific quotations obtained from the interviewees were included under the relevant codes and sub codes. Particular caution was applied to minimise researcher bias or contamination of analysis (Leedy and Ormrod, 2015).

After the transcribing, reading and coding of a sufficient number of transcripts, a degree of saturation was obtained (Leedy and Ormrod, 2015, Rowley, 2012, Vosloo, 2014). The purpose was to obtain such saturation on the subject and not to achieve statistical consensus (O'dwyer, Owen and Unerman, 2011). The data were grouped under headings and subheadings based on the themes identified from prior literature. As the process was iterative, axial codes were reviewed and revised where inconstancies and contradictions were identified, enabling necessary adjustment for subsequent interviews and follow-ups to previous interviews (Boeije, 2009, Braun and Clarke, 2006, Wahyuni, 2012). The reviewing of potential themes is crucial for quality checking (Braun and Clarke, 2006, Friese et al., 2018).

During this phase the unique and specific themes directly addressing the research question were defined and named (Braun and Clarke, 2006). The themes were assigned different codes to impose structure to the data set. In addition, the classification and codes were reviewed by another researcher to avoid bias (Long and Johnson, 2000, Rowley, 2012, Wahyuni, 2012). Lastly the final phase involved the integration and logical summary of the data (Leedy and Ormrod, 2015). A rigorous structuring of the data in line with the key themes arising from the analysis in conjunction with the prior literature data was conducted until saturation was achieved (O'Dwyer et al., 2011).

3.7 Limitations of the study

As the research was limited to the perceptions of a few purposefully selected professional accountants in South Africa, the results cannot be generalised as the information gathered from the small sample is not representative of the population (Boyce and Neale, 2006). The qualitative approach used involved the obtaining of individual opinions through interviews, this inherently resulted in a level of bias, subjectivity or rehearsed responses (Boyce and Neale, 2006, Creswell and Clark, 2007). The views may also be biased because of the stake various professional accountants have in the subject matter (Boyce and Neale, 2006).

Additionally, with interviews the researcher inherently becomes a part of the data collection instrument (Creswell and Clark, 2011). Validity and reliability where enhanced as they become important with such a methodological choice. The researcher also used effective interview techniques such as making the interviewees comfortable, being neutral, avoiding leading questions and keeping his/her own personal opinions uninvolved (Alsaawi, 2014, Boyce and Neale, 2006).

Lastly, there was no cost effective way of obtaining information from all the parties relevant reliance was placed on the information gathered from a sample.

3.8 Validity and reliability

Obtaining feedback and making necessary adjustments through performing pilot studies enhanced the validity and reliability of the research (Alsaawi, 2014, Leedy and Ormrod, 2015, Rowley, 2012). The design of the agenda from prior literature, in conjunction with performing detailed and lengthy interviews until a sense of saturation was achieved, enabled the continuous searching of sufficient collaborating evidence which contributed to the validity and reliability of the research (Rubin and Rubin, 2011). Additionally, the detailed description and documentation of the phenomena also enhanced the validity (Leedy and Ormrod, 2015).

Obtaining reviews from another researcher regarding coding and providing the interviewees the opportunity to correct and approve the transcripts also enhanced the validity of the research (Leedy and Ormrod, 2015, Rowley, 2012). Paying attention to the varying tone and gestures of the respondents and following up on contradictions or inconsistencies also enhanced validity and reliability (Bryman and Bell, 2015).

The selection of suitably qualified, knowledgeable and experienced professional accountants for the interviews and the use of open-ended questions which reduces the risk of rehearsed answers also added to the validity and reliability of the research (Leedy and Ormrod, 2015, Rowley, 2012). Furthermore, placing importance on the ethical considerations by explaining to the interviewees their rights and reassurance of the anonymity and confidentiality of the whole process aids the obtaining of honest responses (Greener, 2008) .

3.9 Ethical considerations

As the study requires the participation of human subjects it is crucial to protect their rights (Alsaawi, 2014, Creswell, 2014). Additionally the protection of the participants' confidentiality and anonymity will encourage them to answer freely (Greener, 2008). The use of interviews to obtain the participant's opinions created the potential to reveal sensitive information as such measures were put in place to protect the participants (Creswell, 2014). An application to the University of the Witwatersrand Ethics Committee prior to the interviews commencing was submitted and approved. The ethics clearance number obtained from the University is CACCN/1187. The participants were also provided with the objectives of the study and requested to give consent to participate in the study (Boyce and Neale, 2006, Creswell et al., 2007, Greener, 2008).

To avoid rehearsed answers, the participants were provided with the agenda and not the detailed interview questions close to the interview date. The participants were informed of their anonymity and confidential rights, together with their right to stop the interview at any time if they deemed fit (Greener, 2008). After the interviews the researcher continued to protect the confidentiality of the data collected and the details of the participants by storing the material under password protection. The researcher maintained objectivity throughout the data collection phase, data analysis and reporting phases (Alsaawi, 2014, Greener, 2008).

3.10 Summary

This section provided details on how an interpretive epistemology paradigm was followed, which then informed the methodology and the research method of the study (Wahyuni, 2012). It explained how the research design connected the research methodology and the research methods. Semi structured interviews were performed with selected interviewees to answer the research question. Detailed rationale was provided on the selection of the approach and techniques used for the data collection. This was followed by a detailed explanation on how thematic analysis was used in the interpretation and analysis of the data. A disclosure of the limitations of the study was also provided, together with the ethical consideration and safeguards implemented to enhance the validity and reliability of the study.

4 FINDINGS AND ANALYSIS

4.1 Introduction

The section provides the analysis of the interviews performed to obtain the perceptions of professional accountants who specialise in providing accounting services, independent reviews and or audit services for small entities. The study suggests that the main reason for small firms purchasing assurance services is to reduce the conflict of interests which exists among shareholders and bondholders. The agency theory was used to examine the reasons why non-PIEs are still purchasing audits despite audits no longer compulsory. Section 4.2 uses the literature in section 2.2 and 2.6.3, together with the response obtained from the interviewees, to describe the various agency relationships which exist and how the conflicts are monitored. The rest of section 4 provides a discussion of all the other reasons provided by the respondents for the selection of audits while linking to the prior literature in various parts of section 2. This includes section 4.3 which highlights the general lack of knowledge and understanding regarding what an independent review entails and the level of assurance it provides. This is followed by section 4.4 which provides details on how independent reviews are constantly compared to audits as a result negatively affecting their acceptability and adoption. Section 4.5 provides the effects which practitioner advice, competence and reputation play on the demand for various levels of assurance.

4.2 Satisfaction of stakeholders' requirements

Abdel-Khalik (1993) suggests that the choice of the type of assurances lies with the client in the absence of regulatory mandates (Abdel-Khalik, 1993). Although the study acknowledges that, ultimately, the decision will be made by the management of the client, it is maintained that there are other forces at play. In spite of the Companies Act providing options to management of non-PIEs, it is questionable whether the decision to be audited or independently reviewed lies entirely in the hands of the owner-managers. This is because external stakeholders can demand a specific assurance type and greatly influence the selection process.

4.2.1 Credit providers

Most of the respondents placed emphasis on the importance of credit providers in the survival and sustainability of small businesses, especially in a country like South Africa where small business struggle for support and lack funding (Anderson, 2017).The participants viewed the main purpose of the preparation of financial statements by small business as providing the existing or potential lenders with the information they need in making decisions about providing, maintaining and extending credit supply to the entities. Lenders consider the financial information important when used in combination with other non-financial information for lending due diligence. An agency relationship exists specifically between the providers of finance and the owner-managers, because the lenders rely on the financial information prepared by the owner-managers, which they cannot verify, to perform their assessments on the provision or extension of funds decisions.

Due to the conflicts of interest which exist, both parties are bound to act in their own best interests. To protect their interests, the credit providers will put in place monitoring techniques such as independent verification of the information communicated by the owner managers. The respondents unanimously identified credit providers as the most influential stakeholders in determining which type of assurance engagement the small companies would enter into, regardless of the management's preferences.

A range of responses were given with the majority of the respondents expressing the view that most credit providers required financial statements to be accompanied by an audit report for the application of credit facilities (R2, R4, R6, R7, R12, R13, R14, R15, R18 and R19). This is consistent with prior observations made by Rennie et al. (2003) who identified lender and owner requirements as the most important reason for the continuance of the audit decision even under deregulation (Rennie et al., 2003). Power (1997) also argues that, as long as an agency relationship exists, small business will continue to opt for audited financial statements to appease their lenders and reduce the information asymmetry (Power, 1997). The credibility, accuracy and reliability of information is crucial for lenders, more specifically in lending decision for small businesses which conversely struggle in meeting this requirement. As a consequence, lenders are stricter when it comes to lending requirements or extending credit facilities to smaller business and will demand for an audit (R14).

> "In some instances after providing clients with an independent report, they come back and say the bank wants audited financial statements for the previous reporting periods as well, going back as far as 3 prior years" (R3)

The importance of having audited financial statements was emphasized by some of the respondents indicating that, in some instances, clients would opt to be audited even when they could hardly afford it (R12) or when it would result in audit fees which may be higher than the funding obtained (R2). As established earlier, profitability and survival are significant challenges in small business, so they may not be in a position to provide guarantees or sufficient collateral to cover their debts. As a result they would be compelled to meet the credit providers' requirements, even if it comes at a costly price.

On the other hand, banks may impose certain liquidity or solvency requirements as part of their lending arrangements to keep track of their money and protect their interests. Owner-managers of small companies have less discretion in the audit decision as they depend greatly on lenders for their survival and will yield to the lender demands. This concurs with previous studies which indicated that, even in the absences of audit requirement regulation, owners would voluntarily opt to be audited in order to satisfy the credit providers requirements (Abdel-Khalik, 1993, Senkow et al., 2001).

> "What we have also discovered is that a lot of financial institutions when they have to fund entities they look for audited financial statements even though there is no legislative requirements to be audited, bankers still ask for audited financial statements. The challenge is at the counter phase where the client engages with the funder, at that level, there is a massive gap in understanding of the change in legislation" (R4).

Essentially, most of the respondents viewed the demand for audited financial statements by lenders as an unnecessary taxing requirement on the small companies and an indication of failure to update their requirements to align them with the Act. This concern rests on the assumption that the lenders are not aware of the independent review option for small companies or are sceptical about the sufficiency and credibility of independent reviews. The respondents, however, overlooked the fact that audits are used as a monitoring tool for the conflict of interest which exists between the lenders as the principal and owner-managers. In addition, they were not mindful of the fact that financial information of small companies is generally considered unreliable or incomplete so lenders require the highest form of assurance provided by audits. This is consistent with previous studies which showed that auditing is a monitoring tool related to high agency costs and high debt leverage (Carey et al., 2000, Hay and Davis, 2004).

Several respondents emphasised that the type of assurance required by the credit providers depends on other factors e.g. the amount of credit being extended or the complexity of the applicant business. The higher the credit facility becomes (R1, R8, R9, R10 and R17) and the more complex the operations of the applicant (R9 and R10), the more the credit providers will insist on audited financial statements. This implies that lenders implement more monitoring techniques in instances where the risk of loss or uncertainty is high. Consequently, this is an indication that lenders will protect their interests further by demanding the highest form of assurance obtained from an audit if their risk is higher. This then results in owner-managers being influenced to select audits rather than independent reviews.

Additionally some respondents agreed that it would also depend on whether clients are trying to obtain credit or extend credit terms with major international suppliers, in which case they are likely to insist on audited financial statements unless the suppliers have an understanding of what independent reviews entails (R5 and R7). This could be as a result of them not exposed to independent reviews in their own jurisdictions or countries.

On the other hand, a few respondents argued that the providers of credit facilities were indifferent to the level or type of assurance (R3 and R5) and what they required was any assurance, as long as it was provided by an independent party (R1 and R10). They went further to state that in as much as credit providers listed audited financial statements as supporting document for credit applications, they will still accept the lending applications if an independent review report is attached (R1). This was justified by the fact that lenders will perform their own assessments and due diligence in the lending decision and not rely entirely on the assurance provided by independent parties.

> "I think with the independent review, it's not so much for the users, it's much more for the providers of finance and all they want to see is an opinion expressed, whether it's a moderate opinion or a negative opinion or a real opinion, the opinion is primarily to protect themselves" (R1).

Eventually one of the respondents stated that the companies qualifying for independent reviews end up opting for audits so as to reduce their risk premium (R3). The understanding appeared to be based on the fact that risk assessment performed by financial institutions is very favourable towards companies which have audited financial statements. The less assurance provided on the financial statements, the lower the credibility of the financial information and the higher the risk so the banks cushion themselves from such risk by charging a higher interest rate on the borrower. This is consistent with observations made by Blackwell et al. (1998) indicating that companies which did not supply audited financial statements to the credit providers were charged premium interest rates

4.2.2 Other stakeholders

In addition to the credit providers, other significant stakeholders were also identified as being influential in the audit or independent review decision. The South African government has been implementing policies which encourage entrepreneurship and business development specifically for small business. The implementation of the White Paper on National Strategy for the Development and Promotion of Small Business significantly resulted in the promotion of SMEs development (Trade and Industry, 1995). Businesses receive support from the government, specifically SMEs with owners from previously disadvantaged backgrounds, however such support is considered insufficient (Anderson, 2017).

Despite these support structures available to small companies, it was noted that in most cases government policies or requirements for giving assistance still included the audit requirement. This could be as a result of updates not being made in time to align with the requirements of the Act, inefficiencies and red tape in government structures, the process being too costly and resulting in administration and coordination chaos due to the chain reaction (R2). In order to enter into business agreements with the governments, an audit would be required (R2 and R7).

> “I can tell you, I have never seen where they say give me the independently reviewed financial statements. All they talk about is audited financial statements” (R2).

If government is meant to provide support to the small business, why do they continue to place the audit requirements which is costly and burdensome most specifically on small business, yet small business are characterized by survival difficulties and failure? It is crucial to acknowledge that an agent relationship also exists between the government and the small business with the government being the principal. In as much as the government is meant to provide developmental support to these small businesses, it also needs to protect its resources and interests by obtaining assurance which verifies the credibility of the information provided to them. This then enables government to provide support and assistance to small companies which qualify for funding and, in other instances, to verify if the funds are utilised for the purpose agreed upon.

It was also noted that there are inconsistencies among the various government departments, various provinces, at the different government levels and for various purpose as well (R3 and R7). In some instances they demand audited financial statements while in other instances they accept an independent review report (R3). This is another indication of the coordination and decentralisation chaos which results in some small companies providing too much to be on the safe side while others provide less or just sufficient engagement assurance.

According to some of the respondents, the need for entities to enhance their chances of obtaining tenders may result in their opting to be audited (R2, R3, R5 and R12). It was noted that for tendering in the government space, most requests for tenders (RFT) listed audited financial statements as a requirement (R2, R3, R12 and R14) and audits were valued (R5) so clients opted for them to increase their business prospects. This once again brings to question whether the owner-managers have a say in the type of assurance or whether they just follow the demands of specific stakeholders.

> “For tenders basically they do their own due diligence on those companies but it’s better to have audited financials than independent reviews as it goes back again to whether the

> people sitting on those boards or procurement boards know exactly the difference between independent reviews and audits is. There is that knowledge gap between the two, so some end up opting for audits to be safe when applying for tenders" (R3).

Some respondents expressed the view that outside shareholders not involved in the day-to-day operations, possessing a substantial interest, would usually insist that an audit be performed (R7, R9). This is consistent with the observations made by Power (1997) that shareholders will continue to require audits to protect their interests due to information asymmetry. Finally a few respondents also noted that if the company is not doing well, the trade unions can also request audited financial statement (R2 and R6).

Respondents had conflicting opinions about the effect of independent reviews on stakeholder confidence and often respondents contradicted themselves. Some of the respondents commented that independent reviews improved stakeholder confidence (R1, R5, R7, R10, R11, R15 and R18) but the confidence was only recognised as being subordinate to that from audits (R1, R10 and R16). The confidence obtained from independent reviews could not be gauged on its own merits; it would either be compared with the confidence obtained from audits or confidence obtained from compilation. Firstly, this could be because audits have been in existence for long so subconsciously the effect of independent reviews will be seen in the shadow of audits. Secondly, it could be because not enough independent reviews have been performed by the right entities to set precedence on their sufficiency on stakeholder confidence. Considering this, other respondents felt that with time (R4, R7, R12 and R13) and significant adoption by clients (R2, R6, R7 and R12) the confidence would grow in the value of a service. This echoes the observations that over time when companies adapt to the relaxation of the regulated audit requirements, there is a gradual move away from the strong audit retention trend (Dedman et al., 2014).

Incidentally principals use external assurance as a monitoring tool for the agency costs, yet independent reviews were introduced by the government to reduce the reporting burden of small companies. There is a conflict between the purposes for which independent reviews were introduced and the needs of the principals. As small companies' financial information is associated with being out-of-date, incomplete or incorrect, the irony is that the principals will then demand a higher level of assurance which comes at a great cost to these small companies.

4.3 The lack of knowledge and understanding

In as much as audits are the most customary form of assurance globally, other external assurance alternatives also exist. In some instances, for example, SMEs it has been argued that audits may not be the best option depending of the organisations’ complexities (IFAC, 2013). In as much as the South African legislation provides assurance choices between independent reviews and audits, it is crucial that the clients and public are knowledgeable about the options available to them for them to make an informed decision.

4.3.1 Lack of knowledge about the purpose of independent reviews

The implementation of independent reviews can be assessed for fit if it meets the purpose for which it was established. As noted in the background section, independent reviews were introduced in South Africa as an option only for non-PIEs. A range of opinions regarding the objective of the introduction of the option for non-PIEs in South Africa were given. Most responses identified the reduction of cost or relieving the financial burden as an important driver for the introduction of independent reviews (R1, R2, R3, R5, R6, R8, R10, R12, R14, R15, and R19).

> “The reason that stipulated the legislation was that a lot of businesses could not afford audits, audits became costly therefore they instituted an independent review” (R1).

This, coupled with the fact that most of these companies are not of public interest (R1, R3, R14) and do not have as much accountability to a wide range of external parties (R8, R12) meaning that the potential for harm to the general public was mitigated (R6, R14). While it is true that the enhancement of transparency and the protection of the public interest were some of the key drivers of the introduction of the new Act, it does not necessarily follow that independent reviews obstruct that goal in as much as they provide less assurance. Rather companies are less scrutinised by the general public and are usually smaller so it follows that their reporting requirements need not be onerous.

It was also suggested that the independent reviews were introduced to simplify the requirements for smaller companies (R9, R15, R18) by reducing the audit burden (R3, R4, R6, R10, R12, R13, R14, R19). Because audits have broader scope i.e. in terms of resources, the work which needs to be done, the corroborative evidence required, as well as the time required for the planning and the execution, they demand a great deal of client’s time and resource in return. Independent reviews on the other hand, still provide assurance on the financial statements in a less demanding and cost effective manner.

One respondent went further to highlight that had the requirement not been relaxed; many these small companies would have been non-compliant with the audit requirement (R3). Based on the analysis of the information gathered from the interviews, it was noted that smaller companies failed to comply with the old reporting requirements and are still facing significant challenges to meet even the less burdensome requirements provided by the new Act.

Other respondents also identified the promotion of entrepreneurship and stimulation of growth as the purpose of the independent review introduction (R3, R5, and R19).

> "It was basically more on trying to promote entrepreneurship and also alleviating the new companies from that burden of being audited" (R3).
>
> "Independent reviews for smaller companies were meant to promote business for the SMEs so that's why they introduced a lesser and more effective way of adhering or complying with the Act that is more cost beneficial for the smaller business" (R19).

Survival in the various phases of the business cycle is a challenge, particularly for small business as they usually lack a solid capital base or operating funds to weather most uncertainties. So the reduction of costly reporting requirements assists small business to channel their limited operating funds to their core business and it encourages entrepreneurship.

According to one of the respondents, independent reviews were introduced as a means of trying to keep abreast with the global standards (R7). As noted in the literature review section, in some jurisdictions, particularly in developed countries e.g. the UK, USA, Canada, audits have been deregulated for smaller companies and this has led to a similar approach being followed in South Africa. Post the Apartheid regime, South Africa has been working to align its reporting requirements with international best practice.

In contrast with the views expressed above, one respondent raised concern that what the department had in mind when they introduced independent reviews is not public knowledge so the DTI and CIPC need to clarify what they were trying to achieve when independent reviews were introduced (R3). Even though the respondents expressed their views regarding the introduction of independent reviews, there seemed to be a gap regarding what the DTI was trying to achieve. This may be attributed to the adoptive nature of South Africa to international reporting regulations without a proper understanding of the history, transitions and context of those jurisdictions and the lack of adequate and specific transmission by the DTI regarding their goal in mind. There also seemed to be an internal conflict within the respondents regarding what they expected the purpose to be and the outcomes observed from their actual experiences since the implementation of independent reviews.

4.3.2 The lack of awareness regarding the independent review option

The independent review option which results in a limited assurance was a new concept in the South African environment when it was introduced and it would seem, even 7 years later, there is still lack of information regarding the option. The regulator is mandated to educate and inform the public about all laws and providing policy and legislative advice. This is questionable according to several respondents who stated that there was no general awareness of the independent review option and the criteria required to qualify for the option (R1, R2, R3, R4, R6, R7, R8, R9, R12, R14, R17 and R19). As a result the lack of awareness and information negatively affects the demand for independent reviews.

Some respondents went further to criticise the government and the regulator for the lack of awareness regarding the option (R2, R4, R5 and R6), stating that the regulator needs to promote awareness (R5, R6 and R7). Considering the fact that the public is acquainted with audits, incorrectly considering them compulsory because of the long standing previous Act and, therefore, assuming that it is the only form of assurance available, the selection of independent reviews will be adversely affected. This is a great indicator that the owner-managers of small entities are not well enlightened with the regulatory side of business.

> "There hasn't been a drive to raise awareness. So from that perspective I don't think there is a high awareness" (R6).

> "Some meet the criteria for the independent review but they don't do it because they are not aware that they can actually do an independent review" (R19).

The researcher is of the opinion that the accounting professionals also have a role to play in advising, educating and guiding their clients appropriately about the various reporting options available to them and demonstrating the differences. The lack of awareness is a possible factor affecting the demand for independent reviews, so the promotion of awareness is equally important to the stakeholders for they largely influence the assurance selection decision.

4.3.3 Differences between audits and independent reviews not understood

Considering the fact that the South African public has historically been exposed to audits as the only form of assurance, it raises concern as to whether the differentiation of the various types of assurance can be objectively understood. Essentially, the majority of the respondents expressed the view that the difference in the level of assurance was not clearly understood by the various groups in the market (R3, R4, R5, R6, R7, R8, R9, R10, R11, R13, R14, R16, R18 and R19).

> "You must remember that the change is still very fresh, still very new and a lot of companies that were specifically audited don't fully understand it" (R4).

While the audit which the public is acquainted with provides a reasonable assurance, it was identified that this assurance was incorrectly treated as indistinguishable to absolute assurance. The emphasis has always been that a reasonable assurance represents that the financial statements are sound. An unqualified opinion under the reasonable assurance was incorrectly treated in the same light as meaning that the financial statements were completely accurately and perfect. This is consistent with the observations made by Porter, Hógartaigh, and Baskerville (2012) according to which more weight was given to the audit report by the public compared to what the auditors will be communicating on the audit report (Porter et al., 2012). The existence of this misconception adversely affects the worth of a limited assurance which then is homogeneously treated as a poor quality of assurance.

Consequently in the small business environment it was noted that most of the entrepreneurs requiring assurance did not have an accounting background and did not understand the various types of engagements as their focus was on their core businesses (R4, R5, R8 and R14). Ladzani and Van Vuuren (2002) report that the downsizing by big companies and high levels of unemployment in South Africa have resulted in people establishing their own business for survival and wealth creation but some of these people would not have a business background (Ladzani and Van Vuuren, 2002). Another respondent agreed that there was no deep understanding of the various levels of assurance or types of opinions and noted that clients were more concerned with not getting a modified option, rather with than the level of assurance (R1).

> “I think they understand it to an extent, that they don’t want a qualified opinion because a qualified opinion is not a marketable tool to raise finance (R1)”.

It was also argued that the clients did not understand what is involved in conducting an independent review (R1, R2, R10, R12, R14 and R19) and what the opinion implies (R1, R2, R3, R6, R8, R14 and R16). It was also noted that considering the long history of the profession, the changes brought in by the Companies Act were fairly new, so there was no understanding of what the change accompanied (R4, R7 and R8). The difference between an audit and an independent review is understood only to the extent of what it cost them (R2, R3 and R10).

> “Awareness is lacking and they do not understand the differences so until the awareness issue is addressed and the line is clearly differentiated between the roles for the parties in an engagement we will not attain the result” (R3).

Based on the analysis of the information, it was determined that the clients do not understand the purpose and procedures performed under an independent review. Abdel-Khalik (1993) reports that, besides negotiating the fee, the client who enters into an external assurance engagement does not have any say in influencing or freedom to influence the assurance process and product. The mere fact that procedures were performed by an independent party, who, in most instances, is an external accountant or an auditor, subconsciously meant that a “mini audit” was being performed on their financial statements. This is equally risky, if the assurance level from an independent review is incorrectly thought to be equivalent to that obtained from an audit.

The lack of understandability of the level of assurance obtained from independent reviews creates a general disinclination towards their acceptance. The inherent lack of proper understanding of the reasonable assurances, coupled with entrenchment into the mindset of the public as audits being the only form of assurance creates challenges and reluctance to the implementation and acceptance of independent reviews. Principals for whom the external assurance is obtained will most likely demand the audit option, not only because it provides them with the highest level of assurance or monitoring available but because they believe they understand it better.

4.3.4 The expectation gap

The researcher detected mismatches in relation to the clients' perceived expectations from independent reviews, what the opinion from an independent review engagement implies and the practitioners' roles. As noted earlier independent reviews are new in South Africa and the differences between audits and independent reviews are greatly misunderstood.

Several respondents commented that there was an expectation gap (R6, R10 and R18); the clients expected more from independent reviews, in terms of the procedures to be performed (R2, R5, R8, R12 and R14), the responsibilities of the practitioners (R3 and R5) and the level of assurance to be delivered (R3, 14 and R16) than would be stipulated in an engagement letter as they lack understanding (R1, R8 and R14). They would expect more or less the same benefits as from an audit at a lower cost (R2, R3, R5 and R7).

The gap is expected to be greater for the clients who previously received audits than to clients who have never entered into an assurance engagement (R5 and R12). This is because of the lack of understanding of the scope and procedures involved in obtaining the different assurances. As an illustration, the accountant or auditor will still request documents from them, make observations, enquiries and follow-ups if necessary, so subconsciously in their minds they would still consider it the same as an audit.

Respondents expressed the fact that the clients do not go through the engagement letter in detail (R3, R9 and R14), while others went further to state that the engagement letter is long (R3) and written in jargon which people from a non-financial background may struggle with (R8). Indeed the blame for the lack of understanding cannot lie entirely at the client's feet; it is highly likely that the accountants or auditors are not deciphering the message they are trying to communicate to their clients in their reports. The researcher deduced the importance of providing clients with clarity regarding the various engagement types available, the assurance level they provide, as well as each party's responsibilities. The researcher agrees with Gray, Turner, Coram, and Mock (2011) on the need to educate the accountants or auditors on the objective of the audit or independent review and the intended messages communicated in the reports so that they provide clarity to the clients (Gray et al., 2011)

> "I had a misunderstanding with one of my clients because they felt including the limited assurance statement in the report implied that you could not stand up to the public with your opinion and also it's as if you are declaration to the public that you don't know whether the financial statements are fine or not. That indicates to me that there is lack of understanding: they expect that when you perform an independent review and you sign off on that opinion you can also sign off on the audit report as this is the same thing" (R3).

In as much as the clients expect more from what the independent review report communicates i.e. place an overstated value on the assurance provided, the irony is that, on the other side, the stakeholders perceive the value of the assurance to be negligible. This then creates tension as the principals who seek the highest form of assurance, which the independent review does not provide and, at the same time, the small business feels comfortable with its own financial statements.

4.3.5 The value of financial reporting and assurance

Financial reporting provides existing and potential investors, lenders and other creditors who have no direct access with useful information in making decisions about the entity. Bearing in mind that small businesses rely of debt for cash flow purposes and survival, the financial information allows lenders or any other providers of finance to make lending or investing decisions.

It was noted that the value of financial reporting was not understood and appreciated amongst the various groups in the South African market. Some respondents went further to state that generally smaller companies did not even prepare general purpose financial statements (R11, R14 and R19) unless they were required for funding purposes (R3, R5, R7 and R11), SARS (R5, R7 and R11) or tenders (R5). Consequently, small companies use financial statements as a key tool for raising funds.

> "The understanding is very thin on the ground and we have got to acknowledge that a lot of our people that goes into business fall into business unexpectedly so there is no teaching at school about entrepreneurship and what financial statements mean. Actually the curriculum around accounting in school and business economics and economics in

> school doesn't address a lot of the nitty gritty day-to-day things that a business would encounter and therein lies part of the problem" (R7).
>
> "I think some companies don't get audited at all if they don't have to present their financial statements to someone: if there is someone that may be relying on their financial statements they will probably go the audit route" (R6).

The researcher deduced that provision of assurance was mostly to comply with the regulations and avoid penalties, not for the benefit which financial statements provide.

On the other hand, it is crucial to acknowledge that the reporting needs of owner-managed entities are different from those which have shareholders who are not directors or are not involved. This is because owners are directly involved in the day-to-day operations of the business and have direct access to the management accounts or financial information. It was noted that small businesses generally tended to make great use of internal management accounts in making business decisions rather than general purpose financial statements. The preparing of financial statements and providing assurance is grudgingly to appease the users or comply with regulation.

> "You see you must also remember that if you are not a listed company, 99% of the shareholder and owners don't even look at the financial statements other than the page that they must sign" (R1).

Most interviewees agreed that the practitioners have a role to inform and advise their clients about the value of independent reviews (R4, R7, R8, R9 and R10). However, some respondents raised concern that there was a lack of holistic drive from the industry to inform on the sufficiency and value of independent reviews (R1, R3, R4 and R13). This is an indication that, besides the pros and cons for the clients there is conflict of interest also among the professionals providing the assurance services. The professional accountants also consider what is in their best interest which influences their approach.

The owners in small owner-managed businesses tend to have control and an understanding of the financial information. In such circumstances it was noted that they do not consider having audits or independent reviews a necessity. Due to legislation, they select the less costly option of independent reviews unless lenders demand audited financial statements (R9). The understanding of the value of independent reviews to clients appeared to be recognised only to the extent of their ability to provide assurance at a lower cost for the clients (R1, R2, R3 and R4). This creates a conflict of interest as the small business may be trying to provide assurance at a reduced cost but mismatching with the principals' need to obtain the highest form of assurance.

4.3.6 Compliance and regulation issues

There was a general consensus that in cases where clients opted for independent reviews the demand was driven by compliance rather than the value (R1, R4, R5 R6, R7, R11, R14, R15, R17, R18 and R19).

> "It's purely because the companies Act says I need to do it, and there is a perception that compliance to regulation improves transparency and ethical behaviour" (R1).

However, one respondent had a different view stating compliance with the Act was not prioritized by some of the smaller companies (R3) as they lack awareness of the requirements and also as there is no enforcement (R3).

> "People are not concerned with whether they are supposed to be audited or independently reviewed but rather what kind of opinion do they need to get this and currently the market is biased in favour of audit opinions" (R3).

Conversely some respondents accused the legislation of not being adequately supportive of independent reviews (R1). One respondent raised concern that the legislation was structured in a way which weakened the importance of independent reviews (R1) and it was not adequately regulated (R2, R4, R5, R8, R11, R13 and R16) making it difficult for the service to be valued. Concerns were raised about who the custodian of independent reviews was (R5, R6, R8 and R16) and whether the quality of independent reviews was being guarded sufficiently (R5 and R13).

> "There is no governance for independent reviews so the credibility of the position, the function, the qualification or the procedure has been rubbished" (R13).
>
> "Independent reviews have a value in the market, and we need to regulate them so as to serve the public and protect the public because whether, you are a small business or big business, you have an impact on the public" (R1).

Respondents had conflicting views with regards to the PI Score determination and often they contradicted themselves. Some accountants raised concerns regarding the determination of the PI Score, stating that the term 'non-public interest' should be defined more (R1, R3 and R7) and should also be re-examined (R11)and include additional features (R1, R5, R11, R12 and R18) such as risk. The thresholds may consequently then need to be revisited (R1 and R7) after clearly defining what the public entail (R1, R3 and R7). While others went on to state that even if it was a good starting point (R2) and a well though average (R3 and R4) encompassing many representative variables, it would need other adjustments.

> “The PI Score can indicate non-public interest but when you look at the risk related to the business and how people are being affected, you will realise that the score might not be enough so it's actually not a good indication” (R12).

Adversely some companies may have public interest yet not be required to be audited because of a low PI Score, while on the other hand; there may be some companies which are forced to be audited while they are not in the public interest (R5). The researcher deduced that the calculation of the PI Score should not be done as a tick box exercise. Based on the operations of an entity it should encompass transparency, accountability and governance by protecting all interested parties, including the secondary stakeholders.

It was also noted that some companies existing before the implementation of the Companies Act did not amend or convert their articles or memorandum of association to the new MOI. These sentiments were echoed by some of the respondents who commented that some entities were not in a position to be independently reviewed because their articles or memorandum of association dictated that an audit be performed (R1, R6, R7, R11 and R12).

> “The age of the company says we are a pre-2008 company, therefore, we have a relationship with our auditors; our articles of incorporation say we must get audited, therefore, it’s very much entrenched into the fibre of the company and your newer smaller companies would not have that requirement” (R6)

The Companies Act provided a transitional period of 2 years from the effective date for companies to amend their articles and memorandum of associations to the MOI free of charge, otherwise to follow the new process of amending the MOI and paying the relevant costs. The researcher deduced that the companies which did not amend their MOI would have maintained an audit as it would have been a requirement included in their articles and memorandum of associations. If the companies were not aware of the transitional period to amend the MOI or the independent review option, they would retain the audit requirement, even if it was not a conscious choice.

4.4 The comparison of independent reviews to audits

In South Africa audits have been entrenched in the economic and regulatory environment of business such that it has led to their gradual idealisation. It is inevitable that independent reviews will be viewed in comparison to audits.

4.4.1 The cost effect

Independent reviews were introduced as an additional form of assurance for non-PIEs to relieve them of the financial burden associated with reasonable assurance. This led to independent reviews being advocated to small business clients to reduce assurance costs.

The fees charged by the practitioners either from an audit or an independent review should reflect the amount of risk and effort, therefore, the riskier the client, the larger and more complex the operations of an entity are, the more effort required to obtain the required level of assurance. As independent reviews are less risky in terms of third party liability, they require less procedural effort and it is expected that the cost of obtaining the negative assurance will be lower than that of a positive assurance. However, it is also important to note that the larger a company is, the more likely is to benefit from economies of scale on the assurance obtained (Chow, 1982). Smaller companies are at a disadvantage and will bear a high cost in order to obtain assurance. This was illustrated by the observations made by Chow indicating that the variable costs of audit do not double for a firm twice its size (Chow, 1982).

Respondents had conflicting views about the cost of independent reviews for the smaller companies, and often the respondents contradicted themselves. This may stem from the variability of the knowledge embedded in them regarding what they expect independent reviews to cost, versus the reality from their experiences. Some respondents highlighted the fact that independent reviews resulted in significant cost saving for the clients (R1, R2, R3, R6, R8, R10, R14, R15, R16, R18 and R19). This was based on the premise that only limited procedures have to be performed under independent reviews, resulting in less time required, unless anything has come to the practitioners' attention which may require additional work. This is consistent with previous research performed by Rennie et al. (2003) which identified cost reduction as one of the significant reasons for the purchase of independent reviews or reduced level of assurance. While the respondents indicated that there is a cost saving, there was no consensus on the extent of cost saving and, in most cases, they could not elaborate on the percentage in saving.

Some respondents went further to state that the companies would do a cost benefit analysis (R5 and R15), and will select the independent review if they get something out of it or are able to avoid some form of penalty from non-compliance (R3, R5 and R7). This is in line with the observation that small companies understand the cost and benefits of audits (Dedman et al., 2014). Consequently, because of their heavy reliance on debt, they would opt for audits which are more costly in terms of fees, so as to satisfy the lender requirements and avoid jeopardizing their chances of obtaining funding (R2 and R13) or avoid high interest rates (R3). This is consistent with the observation made by Blackwell et al. (1998) that companies not performing audits gravitated towards high interest rates (Blackwell et al., 1998).

In as much as the financial impact of independent reviews is lower, it would also result in other diminishing benefits, specifically where the small businesses have agency relationships. This concurs with Jensen and Meckling (1976) argument that companies will voluntarily bear the audit cost in order to safisfy their agency relationships. Other respondents went further to state that the benefits from independent reviews were outweighed by the cost (R3, R4 and R13) because their value has not yet been fully realized (R1 and R4) and also the market or the users of financial statements might not understand or accept them (R3 and R13).

> "In other instances as well some of the clients will go for an independent review purely based on the fact that it will cost less but they also don't know the other costs associated with that decision as they do not know the differences between the two, they just think it's the same" (R3).

Some of the respondents answered in a hypothetical sense by indicating that independent reviews should be cheaper (R4) if they are done properly (R8). The hesitancy to commit to an opinion is an indication of the conflict which exists between what they learnt from formal education as the justification for independent reviews and what they have observed from practical experience. At the other extreme, some respondents qualified this by stating that independent reviews did not significantly cost less than audits because the type of work required and the procedures followed were almost the same (R2, R6, R7, R13 and R18). These results contradict prior studies which have indicated that independent reviews' result in the reduction of costs (Abdel-Khalik, 1993). Another respondent argued that risk has been built better into the pricing of audits than the independent review (R4).

> "Now if you look at what the standard requires you to do, it means you are now required to do more analytical analysis than procedural steps and that is where it becomes much more costly because you now need to look at the financial statements in the context of the business, business risks etc. and see whether the information reflects what transactions have happened through the year" (R1).

In as much as there is a reduction in litigation risk for the practitioner and the type of procedures to be performed, the respondents argued that it was the cheap, clerical work which was eliminated from independent reviews so they still put in almost the same amount of work as in an audit (13). As an illustration, similar planning procedures will need to be performed, obtaining an in-depth understanding of the client operations and their environment, together with completion procedures. In addition, as clients are charged based on time, the practitioner may then spend a similar amount of time performing detailed analytical procedures and enquiries with the clients, regardless of the fact that substantive procedures are not required for independent reviews.

This then creates frustrations and tensions with clients who are charged a fee slightly less than that of an audit yet the stakeholders' degree of confidence in the assurance is significantly reduced. Clients moving from a compilation to an independent domain also experience the steep changes in price. Some respondents expressed the view that the cost reduction obtained from receiving an independent review was not that significant, compared to auditing cost as many clients still opted to be audited (R13 and R18).

> "They try the independent review, and then they get the bill and they put the 2 together and see that it adds up to what an audit is anyway" (R13).
>
> "Because we are paying money, we would rather get the "better product" out of it. Because we are paying money, no matter what, rather pay extra and get that extra assurance out of it" (R5).

Some respondents highlighted that independent reviews save the clients some time (R2, R6, R8, R10 and R19). This is due to audits providing a disruption in the core activities of client personnel. On the other hand, with independent reviews the reviewer may come in for observations or enquires after they have done their analytics off site which provides fewer disruptions and saves time for the clients.

> "An audit has a lot of requests and requires a lot of time from the staff to actually provide the auditors with that number of responses or documentation so clients don't want to spent time trying to do an audit so they would adopt an independent review because it's much quicker to do" (R19).

4.4.2 Misperceptions and the lack of acceptance

Several of the respondents commented that the public had a perception that the only set of financial statements which could be relied upon or trusted is audited financial statements (R1, R2, R3, R4, R5, R6, R7, R8, R11, R12, R13 and R18). This could be because of the entrenchment of audits in the reporting environment and also the fact that the additional option created is not completely new but a less procedural option, resulting in the provision of a lower assurance. This is consistent with the observation that companies discontinuing audits face challenges in substantiating the accuracy of their financial statements, more specifically when audits are ingrained in society (Wallace, 1980). This also echoes a study performed in the United Kingdom which indicated that the director's perceptions regarding the value of audits in providing a high quality of information and internal records checks was most important (Collis et al., 2004).

Because audits provide reasonable assurance which is the highest level of assurance, this by default has contributed to the misperception that independent reviews are less reliable (R1), not good enough (R4 and R13) and associated with a lower quality (R8) because of fewer procedures being performed (R5). The public does not understand that audits and independent reviews fit the different needs of different business. Some respondents raised the issue that clients were concerned with how the stakeholders would perceive their companies if they opted for independent reviews (R5 and R6). This stems for the notion that if clients are opting for a lower degree of confidence, they may be cost cutting, struggling or trying to hide something.

Some respondents went further to explain that due to the lack of valuing (R6 and R10); independent reviews have not been embraced the way they ought to be (R4). Some clients will opt to have audits as they are generally acceptable and considered a safe option (R9). Perceptions are a key factor affecting the acceptability of independent reviews (R5, R8 and R13) and they are difficult to change (R4 and R5). Gold, Gronewold, and Pott, (2012) recommend that the profession needs to understand the opinions of users in the revision of standards to address the needs of users (Gold et al., 2012).

> “ Remember an audit is the highest form of assurance that you can get in terms of the law, in terms of what needs to happen, anything less than that, people still have a perception that it's just not good enough” (R4).

Granted these are misconceptions of participants regarding limited assurance but the respondents overlook the fact that principals demand a high level of assurance to monitor the agency cost that exist between them and the owner-managers. It is also important to acknowledge that the responsibility of faithful representation is the responsibility of the preparers of financial statements, not the practitioners providing assurance. The compliance of IRFS in the preparation of financial statements enhances the quality. The practitioners’ role is to express an opinion on the fairness of the financial statements i.e. that they are free from material misstatements.

4.4.3 Resistance to change

The respondents indicated that there was a general force of resistance to change because audits are considered to be the only source of acceptable assurance. It would appear the resistance is not limited only to those who internally drive the financial reports i.e. owner-managers, directors or audit committee but also extends to lenders, investors, some practitioners and other parties in the financial services space due to their education, experience and background.

This agrees with the argument of O’Donovan (2002) which states that, in order to continue operating successfully, businesses must act within the bounds of what society identifies as ‘socially acceptable behaviour’ (O’Donovan, 2002). Legitimacy is a subjective and abstract concept influenced by cultural and social variables (Maroun and Solomon, 2014, Tilling, 2004). Audits have been legitimised, despite their inherent complexities, criticism on small businesses. In as much as small businesses aim to reduce the agency cost, their hands are tied and they will retain audits, as independent reviews are not yet socially acceptable and could also ruin their chances of obtaining funding.

It was noted that the culture at a company or those driving the audit or independent review decisions will dictate what option to select (R5, R6 and R13). Most respondents were of the view that, in South Africa, there is a general motion to resist the change by the various groups of interest (R1, R2, R3, R4, R5, R7, R10, R11, R12 and R14) they would insist on an audit even when advised to consider an independent reviews (R2, R10 and R12). This could be to maintain consistency because they are only acquainted with audits so this is what they know to have worked in the past. Furthermore, some interviewees expressed concerns that independent reviews are viewed as an option but not yet established as a standard (R1, R2, R6 and R13).

> “Because it hasn’t been made a standard or a norm, it is legislative and made an option but not really made a norm” (R6).

In as much as an entity can qualify for an independent review, because of legacy driven mindsets, resistance, questions or suspicion are raised on why an audit have not been done (R2, R4, R5, R12 and R14). This is in line with Chow’s (1982) suggestion that business may continue to perform audits in order for them to satisfy political costs i.e. meet the institutional requirements (Chow, 1982).

> “Some people opt for the audit because they have always done audits in the previous years, so moving from an audit to an independent review is a very big transition for them, so they are not more open or comfortable to do a review” (R19).

The resistance to adopting independent reviews is stronger in organisations which are in highly regulated environments/ industries or entities of which the financial statements are consolidated into audited group financial statements, entities which have been in existence pre 2011 and have prepared audited financial statements. This is mainly because the businesses are obliged to engage in audits by other parties or stakeholders or boards because of to the entrenchment of audits.

Some respondents went further to highlight how the educational and training systems in the field of accountancy have and remain focused only on ISAs and auditing as a result influencing the general mindset (R1, R4, R6 and R12)

> "I think part of the problem is how people are schooled. You can go and speak to any of the auditing lecturers, they don't mention independent reviews, they don't mention compilation unless if it's a slip of the tongue. It's a 2 minute session on an independent review as a moderate opinion and that's it" (R1).
>
> "A review is not a big enough focus of the syllabus or the articles process. The syllabus test you on the full audits ISAs while ISRE comes out somewhere in there as one of the other engagements that you can perform and I don't think there is a full focus on saying this is what is sufficient" (R6).

4.4.4 The effect of value-add services

Traditionally, assurance services were demanded in order to enhance the credibility of financial statements. Over time, to enhance relevance and competitive advantage, the accounting profession started engaging in other value adding services, such as consulting, tax and advisory etc. Value add is enhanced if the assurance service is bundled with other services provided by the practitioner because of the detailed understanding of the client business operation and other industry expertise the practitioner may possess. As an illustration, during performing an audit, the practitioner may evaluate the quality, sufficiency and adequacy of the client's internal control and so be in a position to provide the client with advice and recommendations. Granted in South Africa to ensure independence and avoid threats to independence, the practitioner is required to follow the guidance in terms of the Code of Professional Conduct.

Some accountants emphasised that independent reviews also created value for the financial statements of the clients, but the value created was compared to audits of which the purpose, scope and objectives are not the same. Indeed to perform independent reviews the practitioner is required to obtain detailed knowledge regarding the client business operations and industry, as a result the clients can also benefit from the spill over knowledge. This is consistent with prior evidence, which supported the existence of efficiencies when clients obtained management advisory services and auditing services from the same firm (Simunic, 1984).

Some respondents emphasised that clients valued the identification of misstatements and checks on accounting records obtained from audits (R5, R6, R10 and R19). This provides clients with the satisfaction that information is double checked and this plays a significant role in building trust and professional relationships with practitioners. However, concern was raised that with independent reviews, clients may lose the misstatement and error checks as the procedures do not include detailed substantive procedures and the shorter time required to conduct them do not sufficiently provide the practitioners with the opportunity to detect any distortions (R2, R5, R8, R10 and R19).

The substantive procedures performed during audits award the auditor the opportunity to verify the amounts recorded by the entity. As it is the responsibility of management to identify misstatements due to fraud or error, the owners rely on audit work to identify additional misstatements. However, due to the nature of the procedures required under independent reviews, there is still concern that the analytical reviews, observations and enquiries do not allow the reviewer to reveal the intentional and concealed facts of the misstatement.

In practice the public also relies on the auditors to identify misstatements and this is usually noted when the auditors are blamed when companies fail or go bankrupt, particularly if the auditors had previously issued unmodified audit opinions. The reliance is more so for small companies that may not be capable of hiring expert staff to handle the complex transactions in their operations. Seow (2011) suggests that the audit will be retained if the client relies significantly on the auditor for non-audit services.

Management relies on internal controls to compensate for the lack of observability of transactions and events in their organisations, but these controls are not without flaws. Recommendations on accounting systems and internal controls were also identified as additional value add services provided by audits (R2, R3, R5, R6, R8, R10, R18 and, R19). This was elaborated by a respondent who stated that there is a need for testing of controls, to identify control deficiencies and make recommendations to the client but the same could not be said with independent reviews as they involve some of the lowest forms of testing (R2). This is consistent with the observations made by Woolf (1994) that the risk of bias and concealment is high with independent reviews as the main source of information and explanation is from the managers or owners (Woolf, 1994).

As the business grows, the owners of small entities lose the ability to observe directly and be involved in the supervisory and control functions. Agency costs also exist internally in organisations between various divisions, groups and hierarchical levels e.g. owners, management and other personnel. Paradoxically, the agency costs exist even in small entities but become higher as the organisations grow and develop longer chains of command and this result in the owners losing control, creating opportunistic behaviour amongst the various levels. In addition the functionality of complex technologically advanced systems and controls implemented to cater for the growing business needs may not be properly understood by the owners or management.

To ascertain whether they can rely on the information generated by these systems, auditors perform the testing of controls and will also provide recommendations to the client if they identify any problems. In as much as the testing of controls is not meant to provide any form of assurance on the systems or controls, small businesses rely on the test of controls performed during audits for recommendations to avoid incurring other additional assurance costs such as hiring experts to test the systems or, on the other hand, incurring significant costs of acquiring complex internal control systems.

On the other hand, organisations can only establish internal auditing as a monitoring response to safeguard assets, prevent opportunism or ascertain the proper functioning of controls. However, most small companies cannot afford the internal audit function as a result would rely on the external auditors to test the controls systems as part of their audit procedures while these procedures are not required on an independent review engagement. Unfortunately, even with the existence of an internal auditing function, its independence is usually questioned, especially by the principals who are external parties (Abdel-Khalik, 1993).

Conversely some respondents argued that independent reviews can add just as much value (R13 and R15), as long as there are conducted properly (R1, R7, R9 and R12), while another answered by suggesting that reviews should also add value (R4). This may be because the conducting of independent reviews is still finding its way and there is not a significant amount of practical experience reference. Others went further to state the benefits or value obtained from independent reviews has not yet been fully derived (R1 and R4).

4.5 Professional practitioners

Professional accountants in practice are looked upon as business advisors and trusted in this role because of their vast business experience and their knowledge of their clients' businesses (Bennett and Robson, 1999, Cowperthwaite, 2014). Clients value and trust the advice provided by their practitioners. While there was consensus amongst the respondents regarding professional practitioners' influence on clients, the motives regarding the choice of assurance advocated differed.

4.5.1 The effect of practitioner advice

One respondent identified a wider range of professionals to select from as a benefit of independent reviews for the smaller companies (R6).

> "You have a greater scope of professionals you can engage to do a review, as opposed to an audit where it has to be an RA. The access has increased" (R6).

However, several of the respondents commented that there is no incentive for most practitioners to promote independent reviews (R2, R5, R6, R7, R13 and R19) because of the fact that the fees obtained from independent reviews are much lower than the fees from providing accounting or auditing services (R1, R2, R3, R5, R6, R8, R11, R14 and R16).

This may be because South African regulation prohibits the professional accountants involved in the preparation of the financial statements from performing the independent review. Faced with the option of continuing to prepare the financial statements or continuing to audit the company, the practitioners may prefer the former. This also indicates that's an agency relationships also exist between the practitioners and their clients as there is a conflict of interest i.e. what may be in the best interest of the client may not be in the best interest of the professional practitioner.

Similarly, one respondent raised concern that due to the requirement for the separation of the compilation and review function, the external accountant/compiler may refer the client to an independent reviewer. There was a risk of losing the client to the reviewer or the demolishment of long-standing relationships with the client if they are dissatisfied with the referred reviewer (R7). This can be because the referred practitioner may not understand the nature of the client business sufficiently or lack of experience in the sector (R7).

Some respondents argue that, from a cost benefit analysis, it is more costly to perform independent reviews because even though limited procedures are performed, most of the planning and completion steps are still performed, requiring almost the same amount of resources (R2 and R3) yet a lower fee is charged. It would seem practitioners have not yet managed to effectively perform independent reviews profitably. It was deduced that the practitioners would advocate for the engagement which will be in their best interest and provides them with most benefit as they are also in business.

Some respondents stated that, in cases where the potential or existing clients are struggling financially, the practitioners would advise the clients to go for independent reviews. As a result the practitioners are able to obtain new clients or to maintain the existing client relations while earning some income in the process as they would not want to lose the clients completely (R2, R3 and R6). In addition, it was noted that due to the recession, clients are constantly embarking on cost-cutting measures and one of the areas targeted is professional accounting or assurance services (R2, R5, R10 and R19). The practitioners would also respond by ensuring that they implement cost effective strategies which include identifying areas with less risk or areas which are not significant, then advising clients to consider having independent reviews to be performed for those sections (R2 and R10) so as to save time and maintain or attract clients with a reasonable fee (R8).

In as much as only limited procedures have to be performed, the guidance on performing independent reviews requires the practitioner to have detailed knowledge and an in-depth understanding of the clients' business. The need for cost reduction then creates time and resources pressure on the practitioners as they charge clients based on time spent on the work done which might still significantly be more, resulting in the minimised incentive to promote independent reviews. It may put a strain on the practitioners' diligence, resulting in compromising the quality of the work and the value to be obtained from the service.

> "Technically speaking you will do more, because you should do analytical reviews, now the analytical reviews for an independent review is much higher because you now need to identify risk on the financial statements, and then do ratio analysis, or trend analysis or data mining to see whether the information which indicated risk actually has proved that there is a risk or whether it has not proved that there is a risk so it's much more work. Unfortunately, most of the people who do independent reviews are not competent to do it, but they do it because they apply audit procedures and not independent review procedures. " (R1)

> "Basically we do the same amount of work: in other words, I will not just accept somebody's set of financial statements and sign them off. I insist that we actually go into it and see that all the proper checks and balances are there and that everything ties up" (R9).

Some respondents raised concern that obtaining detailed knowledge about the client in the limited time available was a challenge (R2 and R14), leaving the reviewer with not enough knowledge of the business in some instances (R7). To effectively perform independent reviews, there might be the need to rely on the client's knowledge gathered from previous engagements (R2). However, such existing knowledge may not be available if the independent review engagement is new. Without existing client knowledge, the practitioner faces the risk of overruns during the first few years of new independent review engagements. In contrast, concerns were raised that a tick box or checklist exercise on the steps and procedures might be followed to ensure that practitioners meet budget requirements which would compromise on the value and quality of the engagement (R3 and R14).

Several of the respondents commented that the guidance provided for independent reviews in terms of ISRE 2400 was insufficient (R2, R7 and R8), leading to a gap on the reviewer side in terms of what procedures they are supposed to be doing and to what extent (R8, R14, R16 and R19). In as much as guidance is provided, there is still vagueness or uncertainty with regards to what is regarded as being enough.

> "Although they have those examples of procedures in the ISRE for what you do in the review, some of them here quite similar to an audit and then people were unsure when sufficient work had been performed. Depending on the particular partner and how much they are comfortable, some would realise that it is limited and wouldn't want to do as much work, while others would still feel a bit uncomfortable because they are used to auditing and they know they are signing off this set of financials so they are inclined to do more work" (R8).

> "Independent reviews have a lot of analytics so if things are not predictable it becomes very difficult to perform an independent review you then have to go into much detail and how much detail is always a grey area. Independent reviews are very grey in what to do" (R16).

This could lead to practitioners performing excessive procedures (R2, R6, R8, R9, R10 and R14) which would result in being over budget (R8). In some instance the practitioners feel uneasy about performing analytical procedures and the lack of testing thus end up performing some audit procedures.

> "The partner would come back and say I am not comfortable so why don't you also do these other tests by the end of it you would have done so much testing, it was basically like doing the audit. Work based on looking at trends and ratios didn't feel to the auditor as they are testing anything, so they would try and do more and go over budget and in essence they would have audited" (R8)

Several respondents further highlight that the rules are clearer for an audit making it easier to attain comfort on the work conducted (R6, R8, R13, R14 and R19). Through formal education, knowledge inherited from prior generations and practical experience developed over time, professional judgement and comfort is easily attained when conducting audits compared to independent reviews.

> "The focus even at the training level is full scale audit and so you have a proper appreciation of what is sufficient for a full scale audit but not so clear on whether you are going to over shoot or undershoot the mark if you are doing an independent review and therefore you most probably over shoot the mark" (R6).

> "Auditors prefer to perform audits because there is no clarity in terms of what you are actually supposed to do in terms of an independent review and whether you have done enough, because we never had this and most of the audit firms' tools were built specifically for audits and there is no clarity ito whether we have covered much in order for us to issue an IR opinion. So auditors would mostly go for an audit because they are more comfortable" (R19).

Some of the respondents go further to argue that the analytical procedures and enquiries do not allow the practitioner to verify the data provided by the clients (R2, R8 and R19). If the accounting is not being performed correctly and as transparently as it should be, together with highlighting the issues which exist, there is a risk that the reviewer may not pick it up (R7 and R19). Therefore, in addition to vagueness, for the analytical procedures to reach an acceptable level, concern was raised regarding the identification of misstatements and how to make recommendations (R16).

> "We need to acknowledge that if the bookkeeping is not done correctly, and the compilation is not done as correctly as possible the review becomes very difficult because you are using the wrong information to actually ensure the credibility of the review" (R7).

The need to obtain satisfaction on the sufficiency of work conducted could stem from the dread of third party liability or scrutiny the accounting profession has been facing lately, not just in South Africa but globally as well. The independent reviewer still faces the same third party liability risk even though fewer procedures are being performed. This is supported by prior studies which indicate that auditor liability is very important in some jurisdictions where suing professional accountants is significantly beneficial (Hay and Davis, 2004, Wallace, 1980).

Although the recovery of losses by the providers of funds to SMEs from auditors due to negligence is minimal in South Africa, especially for smaller companies where the legal costs will be higher compared to the financial loss, the reputational damage is equally detrimental. The auditors face a challenge to reduce the risk of third party liability or reputational damage with independent reviews as fewer procedures are required, yet if something goes wrong then their reputation is on the line.

Incidentally clients fluctuating between independent review and audit engagements based on their PI Score calculation could result in administrative burdens for the practitioner (R4) as a result lessen the choice of independent reviews. This is because the PI Score determination is made on an annual basis, for clients with PI Scores close to the thresholds it may fluctuate and they may fall into different reporting categories in different years.

> "Sometimes it would create operational issues for the practitioners because now they have budgeted for something to be independent reviewed and then when they get to the client they realise that it's supposed to be an audit and they haven't planned enough resources, so they now have to go and renegotiate the fees which takes time" (R8).

4.5.2 The effect of practitioner competence and training

ISRE 2400 lists enquiries, observation and analytical procedures as the main sources of information for independent reviews, but to obtain sufficient assurance form such procedures requires great skill and competence. Several interviewees expressed concerns stating that the practitioners were not being properly equipped or schooled to perform the independent reviews effectively (R1, R7, R12, R13 and R14). Some respondents further identified that the understanding of the distinction in the execution activities of an independent review and an audit as a challenge (R8, R11 and R14).

> “What is happening is that for each engagement you need a certain set of competences and skills, but when I look at how it is graded now, at the bottom you have got a compilation, independent review and then audit at the top. If I am entitled to an audit what does it imply, it implies that I have the skills and the competency to perform and independent review and a compilation, whether I have got it or not is irrelevant because I am at the top level” (R1).

It was highlighted that probably the education and training systems on independent reviews were not adequate (R2, R5, R6 and R12). This could be because the focus at tertiary education institution and training in practice is focused on accounting and auditing courses. The deficiency in graduates’ competence can also be attributed to varying expectations of educators and employers (Bui and Porter, 2010). The educators expect the students to obtain the skill in practice while the employers expect the education to be obtained in tertiary institutions.

> “And I think that is what is lacking in the industry in general because firstly we don't understand the standards which govern those engagements and secondly we don't understand the value which an opinion expresses” (R1).
>
> “You must remember professional competence to do an independent review is based on 3 pillars. Firstly the technical knowledge, now if it is not taught as part of your studies, which means by doing an independent review you may be lacking the understanding of the independent review processes. Secondly the practical experience, now if you look at practical experience in practice most of the independent reviews are mirrored to an audit, so they do the same procedures as an audit, yet the objectives are different. How can you add an audit objective into an independent review, you do the same procedures and hope to get different answers. Lastly the attitude of the practitioners towards the independent review, if it's a moderate decision the perception is they may not have to be as diligent as with an audit” (R1).

Some respondents suggested that more focus on independent reviews should be introduced at tertiary level. Proper training for practitioners should be combined with more frequency of performing independent reviews (R2, R5, R6, R8, R10 and R12).

4.5.3 The impact of practitioner scandals

The accounting profession has faced significant criticism and loss of credibility following corporate failures or scandals. As a result globally the audit function posts 2008 has been under great scrutiny. The South African auditing profession has not been spared that harsh fate because of scandals linked to Steinhoff, Linkway Trading, the South African Revenue Service (SARS) and VBS Mutual Bank. Trust is crucial between the auditors and the public as it is a foundation on which audit services are established. However, the public loses confidence and trust in the work of auditors, as they expect the auditors to have identified and foreseen the corporate scandals, failures or crisis.

Most respondents expressed concerns that the recent auditing scandals have brought disrepute to the profession (R1, R2, R3, R4, R8 and R9). However, the respondents clearly had different views about how the public perceived the various engagements. One respondent felt that the recent scandals could increase the independent review demand when clients start realizing that audits are not foolproof (R4). On the other hand, some respondents argued that because reasonable assurance from an audit is the highest form of assurance, clients and the public have been questioning its sufficiency and adequacy (R2, R6 and R7). With the recent scandals the demand for independent reviews would be negatively affected because of loss of stakeholder confidence (R3,) because if the highest form of assurance is being questioned, then a lesser form of assurance would be rejected (R6 and R8).

> "I think in the South African context, there's been so much in recent media about the Steinhoff of the world and such that there's so much scrutiny over any set of financial statements. I think it does matter, hopefully the professions' reputation perception changes a bit. But you see if you are saying I have reviewed the set of financial statements that's not enough anymore; I don't think it's enough" (R6).

The users of financial reports expect auditors to detect and to report on material fraud and irregularities by management (Sikka et al., 1998). Some prior studies also argues that society is of the view that without detection of fraud, there is no purpose for audits i.e. audits lose their relevance (Salehi and Azary, 2009). Clients may question the reason for paying more fees on audits, yet auditors' competency, image and credibility are being questioned.

4.6 Summary

This section provided the findings and analysis of the research question. The main reasons for the retention of audits by non-PIEs in South Africa were explained, using the agency theory. It was noted that credit providers were the most influential stakeholders and they played a significant role in the assurance choice made by non-PIEs. The stakeholders demanded the highest form of assurance in order to manage the agency costs. In addition, there is a general lack of knowledge and understanding of the limited assurance provided by independent reviews. Independent reviews are also compared to audits and found wanting because audits have been entrenched in the business environment and the independent reviews created as an alternative provide a lower level of assurance, yet the cost difference is not significant. Finally, the role of the practitioners was also identified as a significant factor as they play a crucial role in providing financial and assurance advice to their clients, so when their reputation is brought into disrepute, even the reasonable level of assurance is challenged for its adequacy.

5 CONCLUSIONS AND RECOMMENDATIONS

This chapter provides a summary of the key findings obtained from the interviews, concluding remarks and the recommendations section 5.1. This is then followed by section 5.2 which highlights the research contribution while also identifying opportunities for future studies.

5.1 Conclusions and recommendations

The purpose of this report was to obtain an understanding of the reasons why a significant number of non-PIEs still opted to perform audits, when they qualified for independent reviews which were introduced to lessen the reporting burden. The study aimed to determine the various forces and factors at play in the selection process.

Overall, the majority of the respondents indicated that the primary users of financial statements, specifically the lenders, played a significant role in the choice that the non-PIEs make regarding whether they obtain an audit or an independent review. Despite the fact that the decision for the selection of the options available lies with the management of the non-PIEs, it was noted that the pressure from the primary users would result in the selection of audits, regardless of the financial implications. This suggests that the managing of agency costs plays a significant role in the demand for audits, regardless of the reporting options provided by the Act. This research provides evidence consistent with prior literature regarding the retention of audits, even in the face of deregulation due to the monitoring of agency costs.

In as much as the government introduced independent reviews with the goal of reducing the financial reporting burden of the non-PIEs, this decision presented a conflict of interest with the needs of the primary users. Where the primary users seek to obtain as much assurance as possible on the information reported by the non-PIEs, independent reviews provide a limited assurance compared to an audit. In their bid to relieve the non-PIEs, the government should implement an effective alternative which caters for the contracting needs of the managers, shareholders and bondholders, not just the reduction of assurance costs (Chow, 1982).

Additionally it was also found that the smaller companies performed cost benefit analysis in the decision making process. In as much as independent reviews were introduced to reduce the financial burden of providing assurance, it was noted that there were other significant non-financial costs associated with their selection and, in some instances, the benefits associated with the decision are currently not being fully realised. Additionally independent reviews did not result in a significantly lower cost for the clients due to practitioners not having reaching efficiency levels in their performance.

A number of issues were also identified by respondents, including a general lack of; appreciation for financial reporting, awareness of independent reviews, knowledge on what a limited assurance entailed, clear guidance on the performance of independent reviews and application of professional judgement by the practitioners. The practitioners are also facing challenges in performing independent reviews so there is the lack of incentive in creating awareness or recommending the option to their clients. Additionally the research identified the challenges faced in the interpretation and application of the new regulation. The regulator needs to educate, inform and promote awareness regarding independent reviews to the general public, the purpose for their introduction and their role to non-PIEs.

Consequently, a significant amount of training, education is also required both at tertiary education level and on the job, to provide the practitioners with skills and techniques required to perform independent reviews efficiently and consistently. This will result in the imparting of a rich understanding of what the independent review opinion means so that they can provide the service efficiently and also provide informed guidance and education to their clients.

Lastly, legacy issues, the resistance to change issues and perceptions were revealed as significant forces resulting in the continued demand of audits by non-PIEs. In as much as these factors are difficult to change, there is a need for understanding the core objective and purpose for the introduction of independent reviews. Once again, the researcher recognised the importance of providing education and clarity to the general public regarding the varying needs of small non-PIEs and the role that independent review engagements play in meeting the needs of these users. Additionally the implementation of proper regulation and quality control of independent reviews would enhance the legitimacy and improve perceptions of the public.

5.2 Influence of study and areas of future research

This study is among the first to provide a detailed interpretive account of the forces affecting the selection of independent reviews for non-PIEs in a South African context. Although financial reporting for SMEs is extensively researched, there seems to be limited research performed on independent reviews, their role and purpose. The majority of the existing body of retention of audits in the face of deregulation is formulated in Europe, America and Asia. As noted earlier, the usefulness of studies in other jurisdictions may be limited as it does not cater for other socio-economic differences (Collis, 2012). The research explores the barriers to and some of the challenges of non-PIEs in South African experience when selecting the independent review option. The results obtained from this study provide feedback on the functionality of independent reviews and the assurance environment for non-PIEs. This feedback is important as it highlights that much still need to be done by the government in order to improve the support required by non-PIEs, reduce their reporting burden while not compromising on their ability to satisfy stakeholder requirements.

This study is amongst the first to provide a detailed qualitative account of the factors affecting the selection of independent reviews and the retention of audits. As a result, there is potential for further qualitative and quantitative research on the perceptions about independent reviews in South Africa in the post implementation phase. In addition, research can also be performed on the extent of cost reduction and reporting burden for the non-PIEs. Research can also be performed to obtain the perceptions of SME owners or management on the barriers to independent review adoption. Additionally, further research can also be performed on determining the cost benefit analysis of the selection of independent reviews as opposed to audits. Lastly, research can also be performed on the challenges faced by practitioners in performing independent reviews.

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Appendix A – Interview agenda

1) What is your understanding of the purpose of the introduction of independent reviews for non-PIEs in South Africa?
2) What is the extent of adoption of independent reviews by non-PIEs since the implementation?
3) Which significant considerations do non-PIEs take into account when deciding between obtaining an independent review or external audit?
4) Do you believe the stakeholders of non-PIEs are influential in the decision of whether the entity selects an audit or independent review?
    a) How acceptable are independent reviews by users?
5) What do you understand about the accountants' influence on or guidance in the type of engagement selected by the non-PIEs?
6) What do you believe the effects of the selection of independent review have been on the non-PIEs and their primary stakeholders?
7) In your opinion, do independent reviews cost significantly lower than audits?
8) Does the performance of independent reviews by non-PIEs add value to the entities?
9) What challenges do practitioners face in the performing of independent reviews?
    a) Are there significant differences between what the users expect from an independent review and the practitioners' objectives?

Appendix B – Public interest score (PI Score)

This appendix is provided as guidance on how the PI Score, used in determining companies which can be independently reviewed or audited is calculated.

The PI Score is calculated at the end of each financial year by adding the following:

a) a number of points equal to the average number of employees of the company during the financial year;
b) one point for every R 1 million (or portion thereof) in third party liability of the company at the financial year end;
c) one point for every R 1 million (or portion thereof) in turnover during the financial year and
d) one point for every individual who, at the end of the financial year, is known by the company –
    i. in the case of a profit company, to directly or indirectly have a beneficial interest in any of the company's issued securities or
    ii. in the case of a non-profit company, to be a member of the company or a member of an association which is a member of the company.

Appendix C – List of interviewees

Respondent number	Background	Length of interview (approx.)
Respondent 1	Executive Education, training, Chemical industry 36 years of experience in accounting profession.	44 mins
Respondent 2	Senior audit manager, 8 years of experience in accounting profession.	80 mins
Respondent 3	Audit manager, 6 years of experience in the accounting profession.	67 mins
Respondent 4	Practitioner and academic, more than 35 years of experience.	52 mins
Respondent 5	Education, 14 years of experience in the accounting profession.	34 mins
Respondent 6	Commercial manager, 7 years of experience in the accounting profession.	32 mins
Respondent 7	Sole practitioner, 20 years of experience in the accounting profession.	47 mins
Respondent 8	Education, 6 years of experience in the accounting profession.	34 mins
Respondent 9	Sole practitioner, more than 35 years of experience.	42 mins
Respondent 10	Project manager, 7 years of experience in the accounting profession.	45 mins
Respondent 11	Sole practitioner, 31 years of experience in the accounting profession.	38 mins
Respondent 12	Audit manager, 7 years of experience in the accounting profession.	38 mins
Respondent 13	Sole practitioner, 32 years of experience in the accounting profession.	53 mins
Respondent 14	Director client services, 7 years of experience in the accounting profession.	64 mins
Respondent 15	Financial and business consultant, 9 years of experience in the accounting profession.	27 mins

Respondent 16	Accounting manager, 5 years of experience in the accounting profession.	25 mins
Respondent 17	Sole practitioner, more than 15 years of experience.	42 mins
Respondent 18	Consultant, 5 years of experience in the accounting profession.	27 mins
Respondent 19	Audit manager, 7 years of experience in the accounting profession.	32 mins

Appendix D – List of tables