THE INSTITUTE OF
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IN IRELAND

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Mr. Arthur Levitt Jr.
Mr Donald Nicolaisen
Co. Chairmen
Advisory Committee on the Auditing Profession

21 August 2008

Dear Mr Levitt and Mr Nicolaisen

The Institute of Chartered Accountants in Ireland ('ICAI') is Ireland's largest professional accountancy body. It is currently responsible under the Irish companies acts for the approval and registration of those of its members who conduct statutory audit work. This includes Irish members of the so-called 'Big 4' audit firms and the mid-tier global networks. This regulatory role of ICAI is in turn overseen by the Irish Auditing and Accounting Supervisory Authority ('IAASA') – an independent audit oversight body established under statute.

ICAI has noted with interest the current second draft report of the Advisory Committee on the Auditing Profession'. As a small open economy on the western fringe of the European Union, Ireland has significant exposure to the United States economy. Ireland has enjoyed significant inward investment from U.S. corporates and a number of Irish public companies have U.S. listings. This has meant that a number of Irish audit firms have been required to register with the Public Company Accounting Oversight Board ('PCAOB').

ICAI therefore has an interest in developments and proposals that impact the auditing profession. We have noted the current second draft report of the Committee. We share the concern expressed in the report that '*the loss of one of the larger auditing firms would likely have a significant impact on the capital markets*'.

For that reason we support Recommendation #1 relating to 'Concentration and Competition' on the need to reduce barriers to growth of the smaller auditing firms. Concentration of the audit market has long been a concern of regulators, policy makers and the profession itself. This is indeed very much a public interest issue. ICAI has long considered that liability reform as it affects auditors must be a crucial component in any measures aimed at addressing successfully the issue of concentration and at securing the supply of audit services to the capital markets.

In this context, ICAI published a paper 'Auditor liability – the reform imperative' in February 2007 (http://www.icai.ie/Global/sub_documents/Auditor%20Liability%202007%20Feb%20final%20rep032007.pdf) on the need for reform of Ireland's auditor liability regime. In producing this document, we were encouraged by all of our member firms, including those mid-tier firms who were members of global networks, on the need for a multi-jurisdiction approach to this issue.

In Ireland, we were particularly pleased when this issue was recognized a priority by the Government minister responsible for company law in Ireland. During the Summer of 2007, the minister formally referred the issue of auditor liability and possible legislative reform to Ireland's Company Law Review Group ('CLRG') for deliberation. The CLRG report on the matter is expected imminently and it is anticipated that it will contain a formal Recommendation to Government that Ireland's auditor liability regime is in urgent need of reform.

Elsewhere, you may be aware that the issue of auditor liability has been receiving close attention at European level. Following an independent and comprehensive study carried out for the European Commission in 2006, the Commission issued a formal Recommendation to EU Member States on the need for action on auditor liability in June 2008. Significant reforms in this area are also underway in Australia.

In the current climate of concern for the sustainability of the auditing profession globally, ICAI believes that the final report of the Advisory Committee on the Auditing Profession provides an opportunity to highlight the continuing concerns that exist in this area and to encourage the need for continuing dialogue on the matter between all stakeholders. Any report that aims to consider and develop recommendations on the sustainability of the auditing profession is incomplete without detailed consideration of the need to reform auditor liability regimes. We would therefore encourage the Committee to give further consideration to this matter in finalizing its report.

Yours sincerely

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What is the key threat facing the audit profession?

Auditor Liability - the reform imperative
Representation 03/2007

February 2007

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Introduction

The issue of auditor liability has long been a source of considerable concern to the Institute, as well as the auditing profession globally. Over many years, we have encouraged Government to give this issue its urgent attention.

Indeed, recently auditor liability has been receiving close scrutiny from policy makers and governments around the world.

This has been due largely to the potential difficulties for capital markets that would arise from the collapse of another of the large audit firms. Shareholders depend on rigorous and high quality external audit as a means of providing assurance on the financial results delivered by companies in which they invest.

Measures aimed at delivering reform of the auditor liability regime have already been introduced in many other countries - for example, Australia, Belgium, and, significantly, the United Kingdom.

In Ireland the position is particularly sensitive. Uniquely in Europe, auditors of Irish companies are prohibited by law from incorporating. And the law requires Irish auditors to have unlimited liability in relation to audit work. When this is combined with our system of "joint and several liability" whereby auditors can be liable for the losses caused by others, the result is that the assets of audit firms are exposed to catastrophic loss and the personal assets of partners in audit firms are at risk on every audit. The situation is inequitable and now undermines the capacity of the Institute to sustain the profession as an attractive career choice.

More importantly, there are also public interest issues involved. Ireland's reputation and that of the IFSC, in particular, is heavily dependent on a secure and high quality auditing profession.

The degree of risk to which Irish audit firms are now exposed threatens their continued long term viability.

A number of significant developments have occurred recently which have served to focus closer attention on auditor liability;

- the publication by the European Commission in late 2006 of a comprehensive economic study on auditor liability;
- the referral by Minister Michael Ahern T.D. of the issue to the Company Law Review Group; and
- the launch of a public consultation on auditor liability by the European Commission.

For some months ICAI has had a working group examining the issues involved. It has produced this paper as part of our efforts to move forward with this important policy issue.

If you would like to comment on its content, please contact me at martin.wilson@icai.ie

Martin Wilson

Martin Wilson

The issue

At present, the law relating to the liability of statutory auditors in the Republic of Ireland places auditors in a unique and precarious position compared to other service providers to corporate entities. Increasingly, also, Irish based auditors are at a competitive disadvantage compared to auditors elsewhere as a result of recent measures aimed at implementing auditor liability reform in other jurisdictions.

Section 200 of the Companies Act, 1963 prohibits the statutory auditor from exempting himself, limiting his liability, or obtaining any indemnity from the Company in respect of such liability. Coupled with the ban on bodies corporate from acting as auditors contained in section 187 of the Companies Act, 1990, the effect of this is that individual auditors are exposed to unlimited liability. Moreover, due to the principle of joint and several liability which exists in Irish law, auditors are potentially accountable not only for losses caused by their own actions or failings but also for those who may have primary responsibility for such losses but have no resources to meet claims awarded against them.

So, for example, in an action arising as a result of a corporate collapse where the directors and other senior management of a company have been found to be principally at fault, and where the auditors' culpability has been relatively minor, the auditors may well still have to bear 100% of the loss arising due to the insignificant resources of the other defendants to the claim.

Furthermore, the prohibition on bodies corporate from acting as auditors means that the personal assets (including, for example, private residences) of all partners in audit firms are exposed in the event of a 'catastrophic loss', notwithstanding that most partners will have no involvement or culpability in the matter giving rise to that loss.

The current liability regime encourages plaintiffs to go after those defendants (in this case the auditors) with the 'deepest pockets', even though the auditors may be held to have been responsible for the loss to a much lesser extent than any other defendant.

While auditors' potential liability is unlimited, this liability is not and cannot be matched by unlimited resources. The ability of even the largest audit firms to meet massive claims is severely limited by the non-availability of adequate professional indemnity insurance. Rather, firms have to rely on their limited capital resources and their own in-house captive insurance vehicles which, by definition, are unable to spread the risk widely. Thus, the largest audit firms are now essentially self-insuring and, by default, are forced to act as the insurers of our capital markets. This situation is neither equitable nor sustainable.

Failure to implement reform results in auditor firms continuing to be faced with the threat of catastrophic loss with potential serious adverse consequences for Ireland's economy.

This short paper sets out arguments in favour of reform and suggests a mechanism for achieving this.

The Case for Reform

Understandably, the auditing profession has long been interested in achieving reform of the auditor liability regime. This interest is not aimed at seeking preferential treatment for auditors. Nor are auditors attempting to avoid liability for the consequences of their own negligence. Any reform should still result in auditors being accountable and financially responsible for their share of any loss arising from a corporate failure and should offer no relief for criminal or fraudulent activity by the auditor.

Arguments supporting liability reform are discussed below under the following headings;

- National interest considerations
- Competition considerations
- Equity considerations
- Professional Indemnity Insurance ('PII') considerations
- Reform in other jurisdictions
- Other considerations

National interest considerations

The continued and efficient operation of Ireland's capital markets is crucially dependent on a healthy, appropriately regulated and high quality auditing profession. In particular:

- The Irish stock exchange, Irish bankers, Irish investment managers and pension funds are critically dependent on auditors' reports on financial statements of their investee companies.

- A key driver of Ireland's economic development in the last ten to fifteen years has been Foreign Direct Investment which in turn, both locally and globally, is reliant on the availability of a high quality audit profession to underpin reporting of financial information.

- Similarly, Ireland has been extraordinarily successful in attracting much business from the highly mobile Funds Industry. This industry is widely recognised as being able to relocate between jurisdictions with relative ease. The favourable environment available for this industry in this country has included the existence of a pool of high quality professional services firms which includes the presence of globally recognised audit firms.

The failure, therefore, of one of the existing so called 'Big 4' auditing firms in Ireland would have a very significant and detrimental impact on the attractiveness of Ireland as a commercial market place. It would leave the audit market here in turmoil and would certainly have unforeseen consequences on Ireland's ability to support these significant economic activities which have been central to Ireland's economic success over the last 15 years.

While Ireland can be rightly very proud of the success of the IFSC, it must also be conscious that there are others, particularly in other jurisdictions, who have described it as a 'financial Wild West' and have questioned the appropriateness of certain of the activities which are carried on there. While this may be driven by envy, rather than fact, overseas perceptions of Ireland, and in particular the IFSC, as a place to do business, particularly on the part of

Regulators and investors, would be seriously damaged by the failure of a large Irish auditing firm.

2002 saw the global demise of Andersen and what was then the Big 5 auditing firms was reduced to the Big 4. At that time most of the former Andersen clients generally migrated to the remaining Big 4 firms while a smaller number moved their business to mid tier audit firms. To date, the remaining Big 4 firms have been able to manage these additional clients. However in the event of the failure of one of the Big 4, this scenario will not be repeated. Instead it is likely that each of the remaining Big 3 will look critically at their listed entities, particularly riskier companies and financial institutions and decide either to jettison those clients who they consider to carry an uneconomic level of risk or, alternatively, exit this sector of the audit market completely. This would leave many of the world's largest financial institutions, public companies and government bodies without an auditor. The consequential impact that would have on the capital markets can only be imagined.

Governments elsewhere have recognised the risk of the global impacts of the failure of a local auditor and are working at putting in place fairer regimes to mitigate against such an occurrence. Ireland also needs to be mindful of the potential global impact of a failure of an audit firm in Ireland. Ireland should seek to ensure that this does not happen here.

Furthermore, Government policy has rightly been to encourage entrepreneurship, research and development, innovation, and risk taking. By their nature, such activities carry a higher than normal risk of business failure. This is a natural and unavoidable consequence of the operation of the marketplace. However, Government must also ensure that there continues to exist a robust and high quality external audit market prepared to provide the necessary external assurance requirements for such activities without fear of 'catastrophic loss' arising from such failures.

Competitive considerations

Historically, the company law regime under which Irish auditors have operated has been aligned closely with that of our nearest neighbours, the United Kingdom. This similarity has facilitated the ability of business in general as well as auditors to operate in both jurisdictions with comparative ease and legal certainty. However, a number of years ago, recognising the particular risks faced by auditors, the UK implemented a number of measures that resulted in limited reform of the law relating to auditor liability. Since 1989, statutory audits in the UK can be carried out by incorporated entities. More recently, in 2000 the UK passed legislation providing for the establishment of Limited Liability Partnerships ('LLPs'). UK auditors may now also operate as LLPs.

While neither of these measures addresses the core issue associated with the liability of auditors, i.e. the absence of proportionality and the exposure of auditors to multi-billion euro lawsuits, they have provided a limited measure of relief by protecting the personal assets of innocent partners in any claim for losses against the audit firm.

In addition, recognising ongoing concerns about this issue, the UK Parliament has recently enacted measures, in the Companies Act, 2006, aimed at creating a regime that would allow for proportionality and limitation of liability through other means, for example by capping.

A recent and significant development impacting on the auditing profession in Ireland and throughout Europe has been the adoption of Directive 2006/43/EC by the European Union which addresses the statutory audits of annual accounts ('the 8th Directive'). This Directive includes provisions for requiring the recognition of statutory auditors from one Member State by other Member States. Thus any EU based firm of auditors, however structured, will be able to operate in Ireland, once it has passed certain requirements of the Irish regulator. The ability of audit firms in these jurisdictions to audit in Ireland while being subject to a very different liability regime in their home State is clearly unfair to Irish audit firms and is not a sustainable position.

The regime relating to auditor liability in Ireland is significantly different to that in most other countries. Now nearly half of the EU member states either permit limitation on auditor liability or provide for it on a statutory basis. As mentioned above, the UK has recently introduced proposals aimed at legislating for reform of the auditor liability regime. Belgium has also recently legislated for a liability cap in relation to company audits while Austria has recently passed legislation to provide for proportionate liability in relation to any losses caused by auditors.

Irish audit firms should be allowed to operate in an environment which is no less disadvantageous and equitable than in other EU States. Incorporation by audit firms is permitted in all other EU Member States with the exception of Ireland.

Empirical evidence suggests that one of the reasons the mid-tier firms do not compete directly with the larger firms in the market for audits of public companies and very large private companies is because of the higher risk considerations associated with such work. This inevitably leads to a restriction in choice in the market place which is generally considered unhealthy.

Reform of the auditor liability regime would assist in increasing competition in an area where, heretofore, dominance by the Big 4 auditing firms in the marketplace for public company audits has been a source of concern.

It is worth considering the statistics from certain other countries where there is a monetary cap on auditor liability and where the dominance of the Big 4 on the quoted company marketplace is significantly reduced. In Germany, where there is currently a liability cap of €4 million on auditor liability, 22% of quoted companies are not audited by Big 4 firms. In Austria, where the liability of all possible defendants who did not act intentionally is limited to €363,000 per audit, 20% of the top 50 companies are audited outside the Big 4. Similarly in Greece where the cap is set at five times the salary of the President of the Supreme Court, almost half of the top 50 companies are audited outside the Big 4. This contrasts with the situation in Ireland and, indeed, the UK, where substantially all of the major public companies are audited by Big 4 firms.

It is clear that a more equitable liability regime will encourage mid-tier audit firms to enter the market for public company audits over the longer term and will increase the choice of auditor for these companies.

This restriction in choice is made all the more severe by the impact of new independence rules which must be considered by auditors before providing other services to companies which, as a consequence, impact on the choice of auditor available for public companies. It is commonplace now for large companies to have another accounting firm, other than its auditor, as a preferred provider of non-audit services. The nature of the services provided by this other firm may effectively prohibit it from being eligible to act as the company's auditor. In the event of a decision to change company auditor, a public company could find itself restricted to a choice of two of the Big 4 firms who would be eligible for the appointment. This lack of choice is undesirable but is now the reality faced by many public companies.

The audit market will become more competitive by creating a sensible and realistic liability regime to make it attractive to those mid-tier firms who believe they can compete with the Big 4 already but who are unwilling to do so as they consider that the risks they are taking are unnecessarily high.

Equity considerations

As mentioned above, the principle of joint and several liability to which Irish auditors are subject, means that not alone are auditors liable for losses which arise directly as a result of their actions (or inactions) but are also potentially liable for the further losses which have been caused by others who have no means to make good those losses. In the vast majority of reported cases of corporate collapse, where audit failure has allegedly been involved, it is the actions of management and/or the directors that have been found to have been the primary cause. However, to the extent that the auditor is held to be in any way liable, it has generally been the case that those primarily responsible have no means to compensate for those losses, with the consequence that audit firms are sued for multi billion Euro amounts notwithstanding the fact that their culpability may be very small compared to those other defendants.

All audit firms in Ireland operate as partnerships or sole traders. The effect of this is that every auditor effectively has his personal assets, including his home, at risk. While it may be considered appropriate for an individual guilty partner's personal assets to be at risk for his own malpractice, it is patently unfair for the personal assets of other innocent partners to be so.

Recent years have seen significant changes to the legal framework governing the regulation of statutory auditors and the accounting profession in general. The creation of the Irish Auditing and Accounting Supervisory Authority ('IAASA') will contribute to the maintenance of a high degree of confidence in the profession.

Legal measures have also been put in place requiring auditors and accountants to undertake what is essentially a 'whistleblowing' role in respect of many suspected breaches of laws by their clients.

Examples include;

- Reporting suspected breaches of company law to the Office of the Director of Corporate Enforcement;
- Reporting suspected offences under the Criminal Justice (Theft and Fraud Offences) Act, 2001;
- Reporting suspected money laundering offences (including Revenue offences) to the Garda Siochana and Revenue.

The Financial Regulator has now significantly increased powers to require a wide range of information and reports from statutory auditors. Indeed the emergence of numerous regulatory agencies throughout the economy has spawned a plethora of new reporting/assurance requirements on the part of these regulators who have sought to impose additional reporting by auditors on aspects of the business of regulated entities.

While certain technical issues may exist with the nature and form of these additional obligations, auditors have accepted such additional obligations. However, it is fair to say that a consequence of this is that the risks in so doing have increased significantly. In the context of these significant additional undertakings it is reasonable for auditors to expect some level of additional protection than heretofore.

The auditor's role is quite unique in two key respects. Firstly, he is the only professional adviser to a company who is uniquely unable to do anything to put in place any limit whatsoever on his liability. Secondly, he is also the only adviser who has an obligation to report directly to the shareholders of the company rather than to the company itself. In addition the auditor's report is also available to other future investors who were not necessarily shareholders at the time of issue of the report.

Furthermore, while the auditor is generally paid on a time and materials basis, the risks to which he is exposed are linked directly to a company's market capitalisation; clearly, this is something entirely beyond his control. The interplay of these factors significantly increases the risks to which the auditor is subject, but yet he continues to be prohibited from doing anything to protect himself from infinite liability for loss.

Professional Indemnity Insurance ('PII') considerations

It has long been a common perception that auditing firms, and in particular the Big 4, have unlimited insurance and resources to cover losses arising from all corporate collapses. By extension there is a presumption that the global capital markets are effectively underwritten by the Big 4 auditing firms. This perception of 'deep pockets' has undoubtedly encouraged claimants to pursue the statutory auditor in the event of corporate collapses and has fuelled claims amounting to billions of Euro which, otherwise, would not be pursued at all. The reality, however, is somewhat different.

The Big 4 auditing firms have found it impossible in recent years to obtain commercial insurance at any price in the market that is sufficient to cover the risks to which they are exposed. This, of itself, is an indicator that the market generally perceives the risks which auditors carry to be uninsurable and as a result have exited the marketplace which they were very active in throughout the '80s and '90s. As a result, the Big 4 audit firms have had to rely on their own captive insurance vehicles, a form of self insurance, which have insufficient resources to meet the level of claims to which auditors are exposed. Similarly, the fact that audit firms are generally quite 'thinly' capitalised (again, contrary to common perception) means that resources available to firms, including the personal assets of partners, are extremely limited. As a result despite the fact that auditors are sued for billions of Euro, the level of reserves and capital available to cover losses can often amount to a fraction of this. For example, had the recent UK case involving Equitable Life and its auditor been successful, it would undoubtedly have bankrupted the audit firm.

The non-availability of insurance was a critical issue facing the accountancy profession in Australia in 2001. The collapse of Australia's largest insurer, HIH, put pressure on the capacity of the insurance market. The remaining insurers established limits and exclusions on their policy holders which meant that mid tier firms with audit, taxation financial planning or insolvency practices had to consider carefully the potential risks involved before offering such services at all.

The effect on the global insurance industry of the events of September 11, 2001 and this already tightening insurance market in Australia resulted in a sharp concentration in insurance capacity, increased premium costs and widespread unavailability of insurance cover. The accountancy profession, in particular, found it difficult to obtain comprehensive cover for basic accountancy services. As a consequence, the Australian government was obliged to reform the existing regime exposing auditors to unlimited liability in favour of a system of 'capped claims' and proportionate liability.

Australia has thus made considerable progress on liability reform. Currently all states and territories and the Federal Government have replaced joint and several liability with proportionate liability for economic loss to counter the tendency for claimants to pursue those with high levels of insurance cover regardless of how responsible that party was for the loss. In addition all levels of government have also committed to professional standards legislation. Essentially professional standards legislation allows professionals to limit their liability in exchange for risk management strategies, compulsory insurance and other consumer protection initiatives. Legislation has also been passed permitting incorporation of audit practices.

Reform elsewhere

Charlie McCreevy, as EU Commissioner for Internal Market, has frequently stressed the urgent need for reform of the liability regime for auditors across Europe. He recently stated "No one wants another corporate scandal that could reduce the Big 4 to the Big 3 - especially audit firms themselves who we know want to limit their liability for acts under their direct responsibility. Now that some EU countries already have limitations or are moving in that direction, we think the time is right for EU action".

This paper has commented already on certain measures elsewhere aimed at achieving reform of auditor liability, notably in Australia and the UK. The UK reforms have resulted from significant research and consultation with all relevant stakeholders undertaken by the Department of Trade and Industry and included Regulatory Impact Assessment.

Reform of the auditor liability regime has been recognised as a business imperative among many EU Member States. Most other EU Member States either have introduced some measure of reform to auditor liability or are in the process of so doing. The table below summarises the position in key EU Member States. Ireland lags behind these initiatives considerably, in particular, on the ability of audit firms to incorporate. Why should this be so? Why should Irish audit firms be treated any differently in this particular regard?

For the current position in Europe see the table in the Appendix at the end of this document.

Other considerations

The business community, investors and government are looking to the audit profession to help develop and deliver new types of financial and non financial reporting. We have referred to instances of this elsewhere in this document. A more equitable liability regime would facilitate the involvement by auditors in the development of new reporting techniques including development of better information for capital markets, new style assurance reports on matters that are objectively verifiable, disclosure by firms of their quality control processes etc.

The auditing profession in Ireland is currently held in very high regard and has an enviable reputation for quality and integrity. The availability of high quality individuals to support the capital markets and government investment activity is dependent entirely on a steady flow of bright, well qualified and ambitious individuals into the profession. An unfair liability regime is already having adverse consequences on the big accounting firms' ability to attract and retain the brightest individuals as alternative careers, providing greater certainty in terms of personal financial security, offer a safer alternative. In time, this inevitably will impact on audit quality.

Means of achieving reform

Permitting auditors to incorporate would remove an anachronism from Irish law which exposes the personal assets of partners in auditing firms to the claims of creditors arising from matters for which they have no personal responsibility. It is a necessary reform which can be achieved through a simple amendment to section 187 of the Companies Act, 1990. This necessary reform is insufficient however to ensure the continuity of supply of audit services to the market.

Continuity of supply of audit services is important to the smooth functioning of the Irish economy. This suggests a regime of auditors' liability which is within the capacity of auditors or their insurers to pay, unlike unlimited liability which cannot be. Broadly speaking there are three possible approaches to the problem, a statutory cap on auditors' liability, permitting auditors to limit their liability by contract or the adoption of a system of proportionate liability. We would welcome any of these, but we suggest that the adoption of a statutory cap may be the simplest to introduce.

The mechanism of a statutory cap has been adopted recently in Belgium where a statutory liability cap of €12 million has been established for audits of public companies and €3 million for private company audits.

A change in the law to allow auditors to limit their liability by contract with their clients could also be simply achieved by a straight forward amendment of section 200 of the Companies Act, 1963 to exempt auditors from the terms of section 200 generally. In the event of such a change it would be a matter for the contracting parties to agree on what should be the limit of the auditors' liability.

The adoption of proportionate liability would involve a change in the law to provide that, in the event of a claim against auditors, the courts would be required to measure damages on the principles of proportionate liability.

While a move to proportionate liability has much to commend it in terms of equity and a sustainable system of liability for auditors it would be more complex to legislate for than a statutory cap on auditors' liability or the amendment of section 200 which would permit auditors and their client to agree on the limit of the auditors' liability.

Concluding remarks

Section 200 of the Companies Act, 1963 prevents any limitation on auditor liability and was drafted primarily to prevent a company from giving protection to its "officers" who had acted against the company fraudulently or illegally. However, it was extended to include "persons employed by the company as auditor". While this linking of the directors and auditors as officers of the company may have been appropriate at the time, subsequent events have established very clear and separate responsibilities for both directors and auditors and independence requirements have further reinforced the very different responsibilities of each.

Reform of the current liability regime facing auditors would not amount to any element of preferential treatment for the profession. Any proposals amount to no more than an opportunity to avail of the same types of liability limitations that are currently available to all other professionals and businesses. Auditors would still be accountable and financially responsible for their share of any loss which could still amount to significant sums of money and they would correctly offer no release from potential criminal proceedings.

It is imperative that progress is made on this issue at the earliest possible opportunity.

Appendix

Country	Can auditor liability currently be limited?	Mechanisms used to limit liability (where appropriate)	Further details
Austria	There is a statutory liability cap. Incorporation of audit firms is also permitted	The cap varies from €2million to €8 million depending on the size of the company. The cap does not apply to intentional conduct.	In respect of listed companies a cap of €20 million applies. In respect of banks and insurance companies a cap of €30 million applies
Belgium	There is a statutory liability cap Incorporation of audit firms is also permitted.	A financial cap with an upper limit of €12 million for listed companies and €3 million for unlisted companies. The cap does not apply in the case of fraud or intentional conduct.	N/A
Denmark	Contractual limitations to the statutory auditor's liability do exist, as long as the audit complies with the generally accepted auditing principles Incorporation of audit firms is also permitted.	The auditor and the audited company may reduce the financial obligations of the statutory auditor by contract and introduce a liability cap. Such an agreement has no effect on third parties. The cap does not apply in the case of gross negligence or fraud.	N/A
Finland	There is no statutory liability cap and contractual limitations to the statutory auditor's liability do not exist. Incorporation of audit firms is permitted.	N/A	Company legislation differentiates between the roles of the Board of Directors and the statutory auditor. As such, an auditor will only be found liable for a breach of his responsibilities, not jointly and severally with the Board. This is a form of proportionality but not in the same spirit as the French system.
France	There is no legal liability cap and contractual limitations do not exist. Incorporation of audit firms is permitted	For liability to be established there has to be a direct link between an audit failure and the damage caused as a result.	In all cases liability is apportioned between the company management and the auditor depending on their respective role in the failure. In addition, a specific case of proportionate liability occurs in case of joint audits: the judge may assign a different responsibility for each audit firm based on the facts of the case.
Germany	There is a statutory liability cap. Incorporation of audit firms is also permitted	A financial upper limit (a cap)	The limit is EUR 4.000.000 for all listed companies, EUR 1.000.000 for all unlisted companies
Ireland	No.	N/A	N/A
Italy	There is no legal liability cap and contractual limitations do not exist. Incorporation of audit firms is permitted.	N/A	Note that the Parmalat Commission has proposed in a draft law that an auditor's liability should be limited to a multiple of audit fees. The current suggestion is for a multiple of 10.
Luxembourg	Liability cap allowed by contract but this does not apply in the case of gross negligence or fraud Incorporation of audit firms is permitted	N/A	N/A

Country	Can auditor liability currently be limited?	Mechanisms used to limit liability (where appropriate)	Further details
Netherlands	Liability cap allowed by contract but this does not apply in the case of gross negligence or fraud. Incorporation of audit firms is permitted	N/A	N/A
Portugal	There is no legal liability cap and contractual limitations do not exist. However incorporation of audit firms is permitted	N/A	N/A
Spain	Liability cap allowed by contract but this does not apply in the case of gross negligence or fraud. Incorporation of audit firms is permitted	N/A	N/A
Sweden	Liability cap allowed by contract provided shareholders holding 10% of shares do not vote against the agreement. Incorporation of audit firms is permitted	N/A	N/A
UK	There is no legal liability cap and contractual limitations do not exist. Incorporation of audit firms is permitted.	N/A	Joint and several liability. Section 310 of The Companies Act 1985 expressly forbids an auditor from limiting their liability. The scope of an auditor's duty of care is defined by the leading case of Caparo. The law currently gives investors and the company the right to seek redress from the auditors through the company. In addition, third parties may have a direct right of action against the auditors. Auditors are permitted to form Limited Liability Partnerships - but this does not protect a firm from collapse in the face of litigation. The Company Law Reform Bill 2006 proposes to allow auditors limit liability by contract.
Cyprus	There is no legal liability cap and contractual limitations do not exist.	N/A	N/A
Czech Republic	Limitation liability cap allowed by contract only after the damage causing event.	N/A	N/A
Estonia	There is no legal liability cap and contractual limitations do not exist.	N/A	N/A

Country	Can auditor liability currently be limited?	Mechanisms used to limit liability (where appropriate)	Further details
Greece	There is a statutory liability cap and this is set at five times the total of the annual emoluments of the President of the Supreme Court or the total of the fees of the liable Certified Auditor in the previous financial year provided that the latter exceeded the former limit.	N/A	The cap does not apply in the case of intentional conduct.
Hungary	There is no legal liability cap and contractual limitations do not exist.	N/A	N/A
Latvia	Contractual limitation of liability agreements exist in practice, although they are not regulated by law.	N/A	N/A
Lithuania	Contractual limitation of liability agreements exist in practice, although they are not regulated by law.	N/A	N/A
Malta	There is no legal liability cap and contractual limitations do not exist.	N/A	N/A
Poland	Limitation of liability by contract allowed, but with limitations.		N/A
Slovak Republic	There is no legal liability cap and contractual limitations do not exist.		
Slovenia	There exists a statutory cap of €150,000. Cap applicable only to audited company and shareholders.		In the case of intentional tort or gross negligence, the Court may disregard the cap.

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