



DAW/BPC-SUB/mb

Mr Arthur Levitt Jr
Mr Donald Nicolaisen
Co-Chairs
US Treasury Department Advisory Committee on the Auditing Profession
Department of the Treasury
1500 Pennsylvania Avenue, NW
WASHINGTON, DC 20220
USA

25 August 2008

Dear Messrs Levitt and Nicolaisen

AUDITOR LIABILITY

I am writing on behalf of The Institute of Chartered Accountants of Scotland in relation to your current enquiry into the audit profession and, in particular, in relation to auditor liability. We have consulted selected members in firms belonging to international networks of various sizes, in compiling this letter.

We note that in the draft report, 'Advisory Committee on the Auditing Profession, Second Draft Report' issued on July 22, 2008, a number of issues that affect the auditing profession in the US are considered, and proposed recommendations put forward. There is discussion in Chapter V of potentially catastrophic risks that public company audit firms face, however, we are surprised that auditor liability is not specifically addressed. In our opinion, this is a key risk especially to the larger firms. The risk has been recognised in the UK and the Companies Act 2006 permits a company and its auditor to agree an annual limitation of liability.

Whilst there can be some limitation of liability in the UK, our member firms that are part of an international network with US member firms continue to be exposed to significant and often unlimited liability via their network. This works against the extensive attempts of regulators on both sides of the Atlantic, which are being made to promote a wider choice of audit firms in an increasingly global market.

We believe that the ability to limit auditor liability is key to promoting a sustainable, quality audit market by helping to encourage the creation of an environment where there is an expectation of compensation proportionate to the causation of corporate loss, rather than one in which one single party (generally the auditor) is pursued for the whole amount of that loss on the basis of presumed ability to pay.

Companies need access to quality audits at a reasonable cost but there is a high risk attached to auditing multinational companies, due to the auditor being exposed to very high claims in comparison to the profits of the audit firm. This leads to insurance companies restricting the availability of insurance for auditors, increases in audit fees and auditors withdrawing from certain 'riskier' segments of the market.

We believe that a more realistic environment needs to be created where the direct financial penalties on auditors for negligence are significant but not so far reaching and disproportionate as to threaten the existence of the firm or its network of firms. We call upon you to address this issue in your report and to consider recommending the introduction of some form of liability limitation in the US.

Please do not hesitate to contact me should you wish us to expand on the above points.

Yours sincerely

A handwritten signature in black ink, appearing to read 'David A Wood', with a long horizontal flourish extending to the right.

DAVID A WOOD
Executive Director, Technical Policy