

A study on systems of civil liability of statutory auditors in the context of a Single Market for auditing services in the European Union

Carried out on behalf of the European Commission

TABLE OF CONTENTS

Introduction	p. 1
1. Description of the Different Systems of Civil Liability to which Statutory Auditors are Subjected in the Various Member States	p. 5
1.1 Main Features of Statutory Auditors' Liability	p. 6
1.1.1 Legal Basis	p. 6
1.1.2 Nature of Statutory Auditors' Liability	p. 7
1.1.3 Highlights of the Member States' Rules	p. 8
1.2 Parties to the Action	p. 20
1.2.1 Plaintiff(s)	p. 20
a) The Audited Company	p. 22
b) Third Parties	p. 22
c) Collective Actions	p. 26
d) Bankruptcy	p. 29
1.2.2 Defendant(s)	p. 31
a) Appointed Statutory Auditor	p. 33
b) Signing Person	p. 34
c) Associates	p. 34
d) Joint Auditors	p. 34
e) Parent Companies or Subsidiaries	p. 35
1.3 Events Leading to Liability	p. 37
1.3.1 Liability Arising out of the Appointment as Auditor	p. 39
a) Acceptance of the Mission	p. 39
b) Termination	p. 40
1.3.2 Liability Arising out of Exercise of Duties	p. 41
a) Degree of Duty	p. 41
b) Irregular or Misleading Opinion	p. 43
c) Non Disclosure	p. 44
d) Breach of Other Duties	p. 46
e) Parent Companies or Subsidiaries	p. 35

1.4	Fault, Remedies and Causation	p. 49
1.4.1	Fault	p. 49
	a) Definition	p. 51
	b) Proof	p. 51
	c) Absence of Fault	p. 55
1.4.2	Remedies	p. 56
	a) Types of Remedies	p. 58
	b) Assessment of Damages	p. 61
1.4.3	Causation	p. 64
	a) Various Tests for Causation	p. 66
	b) Faults of Third Parties or of the Plaintiff	p. 7
1.5	Limitations of Liability	p.70
1.5.1	Statutory Limitations	p. 72
	a) Time Limitations	p. 72
	b) Liability caps	p. 74
	c) Corporate Structure	p. 75
1.5.2	Contractual Limitations	p. 78
	a) Time Limitations	p. 79
	b) Liability caps	p. 79
	c) Obligations	p. 80
	d) Discharge	p. 80
1.6	Insurance	p. 81
1.6.1	Mandatory Insurance	p. 83
1.6.2	Scope of Insurance	p. 84
1.6.3	The Insured (firm and / or employees)	p. 85
1.6.4	Group Insurance	p. 86
1.6.5	Role of Insurance Companies in Litigation	p. 87
2.	Criminal Liability	p. 89
2.1	Criminal Offences	p. 91

2.2	Criminally Liable Persons	p. 93
2.3	Role of Public Prosecutor	p. 95
2.4	Interaction of Criminal and Civil Liability	p. 96
3.	Analysis of the Practical Effects of the Existence of the Various Statutory Auditors' Liability Systems from the Point of View of the Single Market	p. 99
3.1	Major Differences in the Civil Liability Regimes in the Member States	p. 101
	3.1.1 Standing to Sue	p. 101
	3.1.2 Limitation Periods	p. 102
	3.1.3 Limitations of liability	p. 102
	3.1.4 Mandatory Insurance	p. 102
	3.1.5 Impact of Criminal Prosecution	p. 103
3.2	Impact of the Current State of Achievement of the Internal Market	p. 104
	3.2.1 Establishment	p. 104
	3.2.2 Cross-Border Services	p. 104
	3.2.3 Auditing Firms : Establishment and Cross-Border Services	p. 105
3.3	Jurisdiction and Choice of Law, the Link Between the Differences and the Statutory Auditors' Decisions	p. 106
	3.3.1 Jurisdiction over Liability Actions Against Statutory Auditors	p. 106
	3.3.2 The law Applicable to the Statutory Auditors' Liability	p. 108
	<i>Conclusion</i>	p. 111
	<i>Notes</i>	p. 113

Introduction

1. Background. This study into the systems of civil liability for auditors is submitted within the framework of the European Commission's open invitation to tender n° XV/98/10/D. The purpose of the study, as stated by the Commission, is *«to determine to what extent the different systems of civil liability of auditors which exist in the Member States could constitute an obstacle to the development of a single market in the field of auditing services in the European Union.»*

Given the fact that the study must cover the legal systems of all of the fifteen Member States, we called upon our various colleagues and corresponding firms in twelve Member States. We also enlisted the services of a Scottish barrister to review the report of the United Kingdom in light of Scottish law. Thieffry & Associés completed the studies of France, Belgium and Luxembourg. This network is made up of practitioners who have significant experience in the Courts of their countries in the field of civil liability in general and often, more importantly, how the rules of civil liability apply to statutory auditors.

Our choice of practitioners to undertake the study was deliberate. The issues which arise in the context of liability of statutory auditors do not exist in a vacuum. Rather, they affect the business community in a variety of ways and call for pragmatic solutions which balance the needs of many different actors in the commercial arena. Moreover, a study which adopts a more practical perspective complements the existing works in the field which have undertaken an economic analysis of the issues.

2. Questionnaire. In order to achieve the Commission's objective, the first step was the formulation of a detailed questionnaire which was designed to elicit a detailed description of the civil liability system to which statutory auditors are confronted in the different Member States. A copy of the questionnaire is included as Annex 1.

The elaboration of the questionnaire took into consideration the important works which have already been accomplished on the present subject including studies in 1996 by the Maastricht Accounting and Auditing Research Centre (the “MARC Report”) and the *Fédération des Experts Comptables Européens* on the «Role, Position and Liability of the Statutory Auditors within the European Union», the Act of the Conference of 5 and 6 December 1996 on the Role, the Position and the Liability of the Statutory Auditor within the European Union (“1996 Conference”) and the Green Paper of 24 July 1996 (“Commission’s Green Paper”) on the same subject.

This questionnaire was submitted to the Commission for its approval and then sent to the network of corresponding firms to provide them with a framework for their portions of the study.

However, even the best-intentioned scholar brings along a certain amount of national «baggage» in the form of concepts and established rules. Therefore, the corresponding firms had some latitude to ask and answer questions which were not asked and to explain why certain questions we asked were not relevant to their particular situation.

Upon receiving the national reports, they were reviewed and complemented, when necessary, with additional questions and requests for clarifications.

These national reports have served as the basis of an interim report which contained, in accordance with the stipulations in the open invitation to tender, a «*detailed description of the various civil liability systems to which legal auditors are subject*» and «*a comparative analysis of the definition and practical application of legal concepts (damage, fault and causal link between fault and damage) which form the basis for the system of civil liability in the Member States*».

A draft interim report was submitted to our correspondents for their comments and then presented to the European Commission which made some observations which were taken into account in this final report.

Another questionnaire, which is attached as Annex 2, was sent to over thirty statutory auditing firms, in order to obtain a non-statistical, first approach of these interested parties’ current perception of the topic.

3. Scope of the Study. The subject of this study is the civil liability of statutory auditors in the national legal systems of the fifteen Member States of the European Union.¹

The term «*statutory auditors* » refers to auditors authorised to conduct statutory audits, i.e., audits required by EU directives.

The European legislation in question includes the fourth directive of 25 July 1978 (n° 78/660/EEC, OJEC of 14 August 1978) concerning the annual accounts of certain types of companies defined in Article 1, the seventh directive of 13 June 1983 (n° 83/349/EEC, OJEC n° L 193 of 18 July 1983) concerning consolidated accounts, the bank accounts directive of 8 December 1986 (n° 86/635/EEC OJEC n° L 372 of 31 December 1986), the insurance accounts directive of 19 December 1991 (n° 91/674/EEC, OJEC n° L 374 of 31 December 1991) and the UCITS directive of 20 December 1985 (n° 85/611/EEC, OJEC n° L 375 of 31 December 1985) which require banks, insurance companies and undertakings for collective investment in transferable securities to undergo statutory audits. Moreover, according to the partnership directive of 8 November 1990 modifying the fourth and the seventh directives (n° 90/605/EEC) Article 1, partnerships whose unlimited liability partners are either public or private limited liability companies are also subject to an audit requirement.

The types of auditors in the Member States who are permitted to perform the audits which fall within the requirements of the EU directives are as follows:

Austria:	Buchprüfer, Wirtschaftsprüfer ² .
Belgium:	Réviseur d'entreprise (Bedrijfsrevisor).
Denmark:	Registreret Revisor, Statsautoriseret Revisor ³ .
Finland	Kauppakamarin Hyväksymä Tilintarkastaja (HTM Auditor), Keskuskauppakamarin Hyväksymä Tilintarkastaja (KHT auditor) ⁴ .
France:	Commissaire aux comptes.
Germany:	Vereidigter Buchprüfer ⁵ , Wirtschaftsprüfer.
Greece:	Elenktis ⁶ .
Ireland:	Registered auditor.
Italy:	Revisore contabile. ⁷
Luxembourg:	Commissaire aux comptes, Réviseur d'entreprises ⁸ .
The Netherlands:	Accountants-Administratieconsulent, Registeraccountant ⁹ .
Portugal:	Revisor oficiais de contas.

Spain:	Auditor de cuentas.
Sweden:	Godkänd Revisorer ¹⁰ , Auktoriserad Revisorer.
United Kingdom:	Registered Auditor.

4. Structure of the Study. The questionnaire is divided into six sections. The interim report covered the first two sections of the questionnaire:

- 1) The description of the different systems of civil liability to which statutory auditors are subjected,
- 2) The definition and practical application of legal concepts (damages, fault, causal link between fault and damage) which form the basis of the civil liability systems.

The final report includes the contents of the interim report and describes the answers to the remaining sections of the questionnaire covering the practical application of the rules of civil (1.) and criminal (2.) liability, thus providing the basis for an analysis of the practical effects of the existence of the various statutory auditors' liability systems from the point of view of the Single Market (3.).

1. Description of the Different Systems of Civil Liability to which Statutory Auditors are subjected in the Various Member States

The rules of civil liability are part of the core of fundamental concepts in the legal systems of the Member States. The purpose of this section is to lay out these basic rules and explore their application with respect to statutory auditors.

Reference is made to the questionnaire which was submitted in the various Member States, item by item.

The section begins with a review of the laws and regulations which apply to statutory auditors and the nature of liability (1.1).

The study then proceeds with the examination of the parties to the action (1.2), Events leading to civil liability (1.3), the basic elements of Fault, Remedies and Causation (1.4), Limitations of Liability (1.5), and Insurance (1.6).

1.1 Main Features of Statutory Auditors' Liability

1.1.1 Legal Basis

Questionnaire reference:

Does liability arise from the general rules for civil liability or are there specific statutory provisions for statutory auditors? (Question 1.1)

Given the fundamental nature of civil liability rules, it is important, as a preliminary issue, to ascertain whether there is a special regime in place for the liability of statutory auditors or, on the contrary, if statutory auditors are subjected to the same rules of civil liability as other professionals or the public in general.

This question is of particular importance to the considered harmonisation of national laws. Indeed, if general rules of civil liability are applied to statutory auditors, then the implementation of uniform rules would require either a fundamental change to the Member States' civil liability regimes in general, or the creation of bodies of specific rules concerning statutory auditors. On the contrary, a regime of specific statutory rules for statutory auditor liability would tend to make harmonisation a less burdensome undertaking.

COUNTRY	GENERAL RULES	SPECIFIC RULES
Aus	Yes	Yes
Bel	Yes	Yes
Den	Yes	No
Fin	Yes	Yes
Fra	Yes	Yes
Ger	Yes	Yes
Gre	Yes	Yes
Ire	Yes	No
Ita	No	Yes
Lux	Yes	No
Ned	Yes	No
Por	Yes	Yes
Spa	Yes	Yes
Swe	Yes	Yes
UK	Yes	No

In five Member States (Den, Ire, Lux, Ned, UK) the liability of statutory auditors is not the subject matter of any specific legislation. In these countries, the general rules of civil liability are applied to statutory auditors. As a result, in common law countries, Court-made rules on negligence apply, while in civil law countries, the pertinent sections of the Civil Code govern the area.

A second group consists of nine Member States (Aus, Bel, Fin, Fra, Ger, Gre, Por, Spa, Swe), where general rules of civil liability are supplemented by specific statutory provisions pertaining to statutory auditors. In these countries, the specific provisions can be complemented by the general rules applicable to civil liability concerning, *inter alia*, fault, causation and damages.

Finally, in Italy, liability is based only on the specific provisions which govern statutory audits.

1.1.2 Nature of Auditors' Liability

Questionnaire reference:

What is the nature of the statutory auditor's liability, contractual or tortious? (Question 1.2)

Within the context of the statutory audit, an auditor's fault or negligence can have consequences which go beyond damages to the audited company. Indeed, individual shareholders, creditors and prospective purchasers of the audited company are all in a position to rely on the statutory auditor's report and, as a result, suffer damages.

As will be seen, the distinction between contractual liability and liability grounded in tort can have a significant impact on such issues as the statute of limitations, the amount and nature of the damages which can be recovered and even the extent of the auditor's duty of care.

This section explores the nature of the statutory auditor's liability to both the audited company and third parties who suffer damages in the context of the statutory audit, which appears as follows:

COUNTRY	Audited Firms	Third Party
Aus	Contractual	Contractual/Tort*
Bel	Contractual/Tort	Tort
Den	Contractual	Tort
Fin	Tort	Tort
Fra	Tort	Tort
Ger	Contractual/Tort	Contractual/Tort
Gre	Contractual	Tort
Ire	Contractual/Tort	Tort
Ita	Contractual	Tort
Lux	Contractual	Tort
Ned	Contractual	Tort
Por	Contractual/Tort	Contractual/Tort
Spa	Contractual	Tort
Swe	Contractual	Tort
UK	Contractual/Tort	Tort
* Tort liability to third parties is theoretically conceivable, for various reasons, however, it is of no practical relevance.		

Every country, except Finland and France, bases liability towards the audited company on the contract entered into between the auditor and the audited company. This situation is justified by the fact that the mission, though statutory in nature, arises from a contractual relationship between such parties.

French Law emphasises the public policy nature of the auditor's duty as the justification for basing the action by the audited company in tort. The mission undertaken by the statutory auditor, which is a public interest mission, is defined by laws and regulations and not by contract.

In Finland, there is, in principle, a contract for the performance of auditing tasks entered into between the company and the auditor and breach of this contract leads to liability even without negligence. However, since liability based in tort under the Act on Auditing (“TTL”) is very wide reaching, the additional liability under contract has very little practical significance. One exception remains: if the negligent auditor is appointed personally, but works within an auditing firm, the liability of the auditing firm cannot be based on TTL but must be based on breach of contract.

Moreover, in Germany, Ireland, Portugal and the United Kingdom, where the statutory auditor is negligent in carrying out the audit, he can and generally will be liable to the company both for breach of contract and in tort, whereas in Belgium the *Cour de Cassation* has established the rule allowing a contracting party to sue in tort, which is an exception to the general rule forbidding the plurality of liability (in both contract and tort), if he can show the existence of negligence beyond a mere breach of the contract, and damages which are different from those caused by the breach of contract.

On the contrary, the general trend vis-à-vis third parties is to ground the liability action in tort. The overall consensus is that, since there is no contractual relationship between the statutory auditor and the third party, the protection afforded must be of an extra-contractual origin.

Three Member States have set forth a “third kind of liability”:

- in Austria and Germany, if the injured third party can show that the auditing contract had “protective effects” towards third parties (*Vertrag mit Schutzwirkung für Dritte*, *infra* p. 25), he may bring an action on the contract;
- in Portugal, although most scholars would agree that statutory auditors’ liability towards third parties is tortious, some scholars assert that their liability is of another type (neither tortious nor contractual, but based on “*culpa in contrahenda*”, based on the assumption that certain third parties are compelled to rely on the audit to take a decision) and yet others tend to believe liability is contractual.

1.1.3 Highlights of the Member States’ Rules

The law concerning civil liability of statutory auditors in the various Member States may be summarised as follows:

Austria

a) Applicable Law and Regulations

Contractual liability is based on the general rules as modified by section 275 of the *Handelsgesetzbuch* (« HGB »)¹¹. Tortious liability is governed by the general rules.

b) Who is liable

Not only the statutory auditor (either an individual or an audit firm), but also all his assistants as well as the statutory representatives of the auditing firm are directly liable to the injured party, as will be explained hereafter. All liable parties are jointly and severally liable.

c) To whom may the auditor be liable

The plaintiff in a suit brought under HGB section 275 may be the audited company (i.e. the contracting party) or a company affiliated with the audited company as set forth in HGB section 228.3 (companies whose accounts have to be fully consolidated). Liability towards third parties, which is possible under restrictive conditions, is based in tort, unless the Court recognises the existence of an implied contract between the third party and the auditor, or of a contract with protective effects towards the third party.

d) Liability cap

Under this specific statutory provision of HGB section 275, liability cannot be waived nor limited. However, the liability of all possible defendants who did not act intentionally is limited to an amount of ATS 5 million (363,364 Euro) per audit.

e) Limitation period

The statute of limitations is five years from the occurrence of the damage, instead of three according to the general rules for civil liability applicable in case of tort liability.

Belgium

a) Applicable Law and Regulations

In addition to the general rules of civil liability, the liability of statutory auditors falls within a specific legal framework:

- Article 9 bis of the law of 22 July 1953 sets forth the general regime for statutory auditor's liability¹²;
- Article 64 octies of the *loi coordonnée sur les sociétés commerciales* (« LCSC ») describes the duties of the auditor and the conditions of his liability¹³.

b) Who is liable

The statutory auditor, whether an audit firm or an individual, may be liable. The signing persons and the associates may also be jointly and severally liable.

c) To whom may the auditor be liable

Auditors may be liable towards the audited company and third parties. The liability towards the audited company is based either on the contract between the company and the statutory auditor, or in tort; the liability towards third parties is based in tort.

d) Liability cap

There is no legal liability cap, and the parties cannot limit the amount of damages nor reduce the scope of auditor's liability in the contract or in a separate agreement.

e) Limitation period

The limitation period of both contractual and tortious actions is five years from the occurrence of the damage.

Denmark

a) Applicable Law and Regulations

The liability of auditors arises from the general rules of liability (to which reference is made in §141 of the Danish Companies Act) as developed by case law.

b) Who is liable

Both the individual statutory auditor in charge of the audit and the audit firm, if any, are liable. Associates who participated in the audit will not be liable under Danish law.

c) To whom may the auditor be liable

The statutory auditor's liability to the audited company arises in contract, and to any third parties from a breach of duty in tort.

d) Liability cap

There is no statutory liability cap, but the auditor and the audited company may reduce the obligations of the statutory auditor by contract and set a liability cap. Such an agreement has no effect on third parties.

e) Limitation period

The action can be brought within five years from the discovery of negligence. This period can be reduced by contract, which reduction is effective only between the statutory auditor and the audited company.

Finland

a) Applicable Law and Regulations

When a statutory auditor performs duties prescribed by law (e.g. auditing of accounts of a company or other tasks assigned to the auditor), only the specific liability provision of §44 of the Act on Auditing *Tilintarkastuslaki* (« TTL ») is applicable¹⁴. However it does not include any provisions on specific issues such as the calculation of damages, causation, level of breach of duty or contributory negligence of the plaintiff. In this regard, general principles of civil law are applied to damages caused in a contractual relationship and the regime of the Act on Liability is applied to damages caused to third parties.

b) Who is liable

An action in tort under TTL §44 can be brought against the statutory auditor, either an individual or an audit firm. In this case, the signing person is also liable. They are also liable for the damages caused by their employees, who cannot be liable under this section.

Nevertheless, the associates may be liable for the breach of a general provision of civil law. If the statutory auditor is an individual who works in an audit firm, the audit firm may be liable only in case of a breach of the contract.

c) To whom may the auditor be liable

The action in tort under TTL §44 is widely opened to the audited company, its shareholders and members, and to any third party. As a consequence, the action in contract is of lesser interest, except in the specific case described hereabove.

d) Liability cap

There is no statutory liability cap, and contractual limitations to the statutory auditor's liability do not exist in Finland, although they are possible in theory.

e) Limitation period

The limitation period depends on the plaintiff:

- three years from the signature of the report if the plaintiff is the audited company;
- ten years from the occurrence of the damage if the plaintiff is a third party.

France

a) Applicable Law and Regulations

Statutory auditors' liability is governed by a specific provision contained in Article 234 of the Company Law of 24 July 1966¹⁵. This provision is considered to be no more than an application of the general civil liability rules of Article 1382 of the Civil Code, the concepts of fault, damages and causation being the same (CNCC, *Encyclopédie des Etudes Juridiques, responsabilité civile du commissaire aux comptes*, n° 2 ; Hemard, Terre, Mabilat, Sociétés commerciales, Tome II, n° 1048).

b) Who is liable

The statutory auditor, meant as audit firm or individual, may be liable. If the appointed auditor is a firm, the signatory of the report is jointly and severally liable with the firm. The associates cannot be liable under the specific provision of the Company Law.

c) To whom may the auditor be liable

The auditor is liable towards the audited company, its shareholders and any third parties. The liability of the statutory auditor is tortious only, as his mission is considered as of public interest.

d) Liability cap

There is no legal liability cap, and the parties cannot limit the amount of damages nor reduce the scope of auditor's liability in the contract or in a separate agreement.

e) Limitation period

The action must be brought within three years from the damage causing event.

Germany

a) Applicable Law and Regulations

Statutory auditors' liability arises from the general rules for civil liability in tort¹⁶ as well as from specific statutory provisions for statutory auditors as contained in Article 323 of the HGB¹⁷, which provides for auditors' contractual liability. Some of the statutory provisions applicable to auditors' liability are also found in the professional rules contained in the Act on the Profession of Auditors (*Wirtschaftsprüferordnung*).

b) Who is liable

Under HGB section 323, not only the statutory auditor but also all his assistants as well as the statutory representatives of an auditing company participating in the audit are directly liable to the injured party. All liable parties are jointly and severally liable.

c) To whom may the auditor be liable

The plaintiff in a suit brought under HGB Article 323 may be the audited company or a company affiliated with the audited company. An action may not be brought by the audited company in tort if the auditor fails to meet his contractual obligations under Article 323 HGB. The liability towards third parties, which is possible under restrictive conditions, is based in tort, unless the Court recognises the existence of an implied contract between the third party and the auditor, or of a contract with protective effects towards the third parties.

d) Liability cap

Under the specific statutory provision of HGB Article 323, liability cannot be waived nor limited. The auditor's contractual liability is limited to DEM 2 Millions per examination, and DEM 8 Millions if the company issues stock with official rating.

e) Limitation period

Action in contract should be brought within five years from when all elements of claim exist. The statute of limitation for an action in tort is three years from discovery of damages and liable party.

Greece

a) Applicable Law and Regulations

Greek law distinguishes between common auditors and Chartered Auditors, who have specific professional capabilities.

Liability arises from general rules of law (Civil Code, Penal Code) and specific provisions which are mainly:

- Codified Law 2190/20, which sets forth civil liability of auditors towards the company¹⁸;
- Presidential Decree 226/1992 (G.G. 120 A) concerning the « Establishment, organisation and operation of the Corps of Chartered Auditors and Terms of inscription to the Special Registry and of the exercise of the profession of Chartered Auditor ». Article 19 of the Decree contains special provisions which limit the civil liability of Chartered Auditors¹⁹.

b) Who is liable

The appointed statutory auditor (firm or individual) is liable for the damages that he as well as his associates caused. If the appointed auditor is a firm, the signatory of the report is jointly and severally liable with the firm.

c) To whom may the auditor be liable

The statutory auditor's liability to the audited company arises in contract, and to any third parties from a breach of duty in tort.

d) Liability cap

The Chartered Auditors only benefit of a liability cap of either the quintuple of the annual salary of the President of the Supreme Court or the total amount of fees received by the Chartered Auditor during the previous fiscal year, whichever is higher. The parties cannot limit the legal liability of the auditor by contract.

e) Limitation period

For the audited company, the limitation period is two years and starts when all elements of claim exist. Third parties should sue the auditor within five years from the discovery of the damages and the liable party, and in any case within twenty years from the commission of the act.

Ireland

a) Applicable Law and Regulations

Liability arises from the general common law rules for civil liability (breach of contract, breach of statutory duty or tort) but claims would be based on the auditors' failure to meet their statutory obligations contained in the Companies Act 1963 (as amended) and 1990. Section 163 of the Companies Act 1963 and sections 193 and 194 of the Companies Act 1990 state the scope of the auditor's work and his main duties.

b) Who is liable

If the statutory auditor is an individual, the action will be brought against him. If the statutory auditor is a partnership, each partner is jointly and severally liable. The associates may also be liable, but there has not been any instance where this has occurred.

c) To whom may the auditor be liable

The audited company may bring an action in contract or in tort against the auditor, depending on the duty breached. Third parties may bring an action in tort under restrictive conditions.

d) Liability cap

There is no legal liability cap, and the parties cannot limit the amount of damages nor reduce the scope of auditor's liability in the contract or in a separate agreement.

e) Limitation period

The limitation period is six years for both contractual and tort actions, respectively from the breach of contract and from the occurrence of the damage.

Italy

a) Applicable Law and Regulations

Statutory auditors' liability is governed by specific provisions which set forth two different liability systems applicable respectively to the Board of Auditors or to the auditing firm:

- Article 2407 of the Civil Code provides for the liability for the Board of Auditors based on the duty of diligence of an agent²⁰;
- the liability of auditing firms is governed by Article 164 of the Legislative Decree of 24 February 1998 which refers to Article 2407 of the Civil Code²¹.

b) Who is liable

The appointed auditor (firm or individual) is liable. If the statutory auditor is a firm, the signatory of the report is also liable. The auditor member of the Board of Auditors is liable for the damages caused by his associates, whereas the associates of an auditing firm are jointly and severally liable with the firm.

c) To whom may the auditor be liable

The statutory auditor's liability to the audited company arises in contract, and to any third parties from a breach of duty in tort.

d) Liability cap

There is no legal liability cap, and the parties cannot limit the amount of damages nor reduce the scope of auditor's liability in the contract or in a separate agreement.

e) Limitation period

The action against the Board of Auditors should be brought within five years from discovery of the damage. The limitation period of the actions against auditing firms is either ten years (if the damage is suffered by the audited company) or five years (if the plaintiff is a third party).

Luxembourg

a) Applicable Law and Regulations

The general legal rules for liability set forth in Article 1142²² (contractual liability) as well as in Articles 1382 and 1383²³ (tortious liability) of the Civil Code govern the liability of statutory auditors.

b) Who is liable

In case of a breach of the contract, the appointed auditor only is liable, whether he be a firm or an individual person. In tort, he is liable together with the signing person and the associates for the damages they caused in the course of the audit.

c) To whom may the auditor be liable

The statutory auditor's liability to the audited company arises in contract, and to any third parties from a breach of duty in tort.

d) Liability cap

There is no legal liability cap. The audited company and the appointed auditor may set forth such a limitation by contract. It cannot affect the tortious liability of the auditor towards third parties.

e) Limitation period

The limitation period is five years from the signature of the report.

The Netherlands

a) Applicable Law and Regulations

There is no specific provision in the Dutch Civil Code which deals with the liability of statutory auditors. General rules of civil liability, as enforced by the Courts, are, thus, applicable.

b) Who is liable

In case of a breach of the contract, the appointed auditor only is liable, whether he be a firm or an individual person. In tort, he is liable together with the associates and the signing person, if any, for the damages they caused in the course of the audit.

c) To whom may the auditor be liable

The appointed auditor is liable towards the company for any breach of contract. Tortious liability towards third parties is not automatic, but requires specific circumstances showing the breach of a duty of care that the auditor owes to the third party.

d) Liability cap

There is no statutory liability cap, but the auditor and the audited company may reduce by contract the obligations of the statutory auditor and set a liability cap, with respect to “good morals” and to the assignment of the statutory auditor to approve the annual accounts. Such an agreement has no effect on third parties.

e) Limitation period

The action should be brought within five years from the discovery of the damage and the liable party, and in any case within twenty years from the event having caused the damage.

Portugal

a) Applicable Law and Regulations

The general rules of civil liability apply to statutory auditors. Tortious liability is governed by Article 483 et seq. of the Civil Code²⁴.

There are, however, specific statutory provisions, the main of which are:

- Articles 78, 81 and 82 of the *Codigo das Sociedades Comerciais* (CSC), which establishes the auditor’s liability towards the audited company, the shareholders and the creditors²⁵;
- Article 114 of *Decreto lei n° 487/99*, dated 16 November 1999, which extends the scope of these provisions to the auditing firms;
- Article 10 of the *Codigo de Mercado de Valores Mobiliarios*, which aims to protect investors and third parties through an extended liability of stock listed company’s auditors²⁶;
- Article 13 of the *Codigo de Processo Tributario*, which governs the liability of the auditor if the company cannot pay off its taxes²⁷.

Even where these specific provisions apply, the general rules of liability of the Civil Code provide the rules applicable for civil liability since these specific provisions do not include a complete regime.

b) Who is liable

The appointed auditor and, in case the auditor is a firm, the signatory of the report, are jointly and severally liable.

There are two qualifications to this general rule:

- the managers of the auditing company (usually the partners) may be liable towards the creditors of the audited company (see Articles 78 and 82 CSC);
- the partners of the audit firm appointed as auditor of a stock listed company may be jointly and severally liable (see Article 10 CMVM).

The associates who participated in the audit may be liable, but this has not occurred in practice.

c) To whom may the auditor be liable

The statutory auditor's liability to the audited company arises in contract or in tort, and to any third parties mainly from a breach of duty in tort, some of which are legally defined as stated hereabove.

d) Liability cap

There is no legal liability cap, and the parties cannot limit the amount of damages nor reduce the scope of auditor's liability in the contract or in a separate agreement.

e) Limitation period

The action should be brought within a period of five years from the discovery of negligence.

Spain

a) Applicable Law and Regulations

The civil liability of statutory auditors is provided for by Articles 11 and 12 of Law 19/1988 of 12 July 1988 on the Audit of Accounts (*Ley de Auditoria de Cuentas*)²⁸ and Articles 42 and 45 of Royal Decree 1636/1990 of 20 December 1990 approving the Regulation of the Audit of Accounts²⁹. There is also a specific reference to auditors' liability in Article 211 of the law of public companies (*Ley de Sociedades Anonimas*) approved by Royal Legislative Decree 1564/1989 of 22 December 1989.

However, these provisions do not contain a full and complete set of rules and it is generally acknowledged that they should be construed as a reference to the general provisions regulating civil liability under Spanish law, namely (i) Articles 1101 et seq. of the Civil Code for contractual liability, and (ii) Articles 1902 et seq. of the Civil Code for tortious liability.

b) Who is liable

The statutory auditor, either an individual or a firm, may be liable. The audit firm and the partner in charge of the work are jointly and severally liable. Once the remedies are exhausted against them, the other partners of the firm are also jointly and severally liable. Auditors are liable for the damages caused by their associates.

c) To whom may the auditor be liable

The statutory auditor's liability to the audited company arises in contract. Their tortious liability towards third parties is subject to restrictive conditions.

d) Liability cap

There is no statutory liability cap, but the auditor and the audited company may agree to a liability cap. Such an agreement has no effect on third parties.

e) Limitation period

The audited company should bring the action within fifteen years from when all elements of claim exist. The statute of limitation for an action in tort is one year from discovery of damages.

Sweden

a) Applicable Law and Regulations

Civil liability for statutory auditors is specifically regulated in Chapter 15, Section 2³⁰ of the Swedish Companies Act. A statutory auditor may also be liable under the general damage rules of the Tort Liability Act. The damage suffered by the company or third parties in consequence of the acts or omissions of a statutory auditor will, however, usually be deemed pure financial damage (i.e. damage incurred without connection to bodily injury or property damage), which is in principle recoverable only if it is the result of a criminal offence.

b) Who is liable

The appointed statutory auditor and, in case the auditor is an audit firm, the signatory of the report, are jointly and severally liable. The auditor is also liable for the damages caused by the associates.

c) To whom may the auditor be liable

The statutory auditor's liability to the audited company arises in contract, and to any third parties from a breach of duty in tort.

d) Liability cap

There is no legal liability cap, and the parties cannot limit the amount of damages nor reduce the scope of auditor's liability in the contract or in a separate agreement.

e) Limitation period

For the audited company, the limitation period is five years from the end of the fiscal year. The third parties should sue the auditor within ten years from the occurrence of the damage.

United Kingdom

a) Applicable Law and Regulations

In the absence of applicable statutory provisions, liability arises from general rules of common law for civil liability.

b) Who is liable

The statutory auditor (an individual or an audit firm) and, if the firm is a partnership, any or all of the partners, may be liable for the damages they as well as their associates caused. If the statutory auditor is an audit firm, the signatory of the report is also liable.

c) To whom may the auditor be liable

The statutory auditor's liability to the audited company arises concurrently in contract and in tort. The auditor may be liable to third parties under restrictive conditions.

d) Liability cap

There is no legal liability cap, and the parties cannot limit the amount of damages nor reduce the scope of auditor's liability in the contract or in a separate agreement.

e) Limitation period

In principle, the action must be brought within six years after the occurrence of the damage causing event (the breach of contract if the claim is based in contract, the date when damage is suffered if the action is based in tort).

1.2 Parties to the Action

Plaintiffs (1.2.1) and defendants (1.2.2) are considered in turn below.

1.2.1 Plaintiff(s)

In addition to the type of liability action which can be brought, the comparison of the parties who can bring liability actions provides an insight into the views that the national legal systems adopt with respect to the role of the statutory auditor.

This information allows a classification of statutory auditors as having either a commercial mandate, which means that auditing is considered as only, or principally, a contractual undertaking between the audited company and the statutory auditor, or rather a public interest purpose of protecting the public in general through the exercise of his regulated profession.

Questionnaire references:

- *Who can bring a liability action (the audited company, its officers, one or more shareholders, creditors, suppliers, employees, others)?
May third parties, such as shareholders organisations or trade or other associations sue a statutory auditor for damages suffered either by one or more of their members or collectively? If so, do the members of the group retain their individual standing? Is there the possibility of “class action” suits which allow an individual or legal entity to represent a group without having their express consent?
Do the answers to the above questions change if the audited company is in bankruptcy? (Question 1.3)
Must the injury be personal to the plaintiff or may he seek damages for collective damages for a group of which he is a member, most notably when the members of this group remain inactive (example: action brought by a shareholder for an injury to the corporation)? (Question 2.2.2)*

Traditionally, the issues involved must be explored in so far as they relate to the plaintiff's own injury or some collective injury.

This section will explore the injured parties who have standing to bring a liability claim, i.e. the audited company (a) and third parties (b), and the availability in the Member States of such mechanisms as class actions, derivative shareholders' action and access to justice of shareholder organisations to defend the rights of their members (c).

Special consideration must be given to the situation where the audited company is in bankruptcy (d).

SUMMARY : PLAINTIFF(S)

The audited company may bring an action against the statutory auditor in all countries, on the basis of contractual liability or tort liability. In Austria and Germany, linked companies have the same right to sue as the audited company.

An important difference concerns the standing of **third parties** to bring liability actions against the statutory auditor. In a majority of Member States (Belgium, Denmark, Finland, France, Greece, Italy, Luxembourg, Portugal and Sweden), the statutory audit is considered to be not only in the interest of the company, but also in that of the public. As a result, any third party may recover damages from the statutory auditor upon proving the elements of the liability claim, usually fault, damages and causation. However, in Common Law countries (Ireland and the United Kingdom) as well as Spain, the third party must prove that the statutory auditor owes him a duty of care. The statutory auditor will owe a duty of care to a person other than the audited company only if he assumes responsibility to that person for ensuring the substantial accuracy of the accounts with regard to the facts of the particular case. This entails that the auditor knew or should have known that claimant would rely upon his work and/or his report for a particular purpose. A similar reasoning applies in Austria and Germany with the concept of implied contracts and of contracts having protecting effects to third parties. In the Netherlands, the matter is not settled, but one part of the legal literature develops this proximity criteria.

The most common position regarding **collective actions** is to refuse them. Nevertheless, some are admitted in certain Member States, no general regime being able to be set out from the comparison:

- in France, certified shareholders associations may sue on behalf of investors, under restrictive conditions that make such actions very rare in practice;
- in Portugal, class actions may be brought in order to protect investors, but no claim involving an auditor has come before Courts until now;
- in five Member States, derivative actions (i.e. actions brought on behalf of the audited company) may be brought either by shareholders only (Portugal, Spain and United Kingdom) or by shareholders and/or creditors (Italy, Luxembourg).

While in **bankruptcy**, the audited company is represented by a liquidator or a receiver who acts on its behalf. In Austria, Denmark, Greece, Ireland, Portugal, Spain, Sweden and the United Kingdom, bankruptcy does not affect third parties' actions against the statutory auditor. In the other Member States (Bel, Fin, Fra, Ger, Ita, Lux, Ned), the receiver or his equivalent representing the creditors has standing to sue on their behalf. However, if the auditors' fault has resulted in damage suffered by the debtor or a third party (and not by the company), they may sue the auditor directly.

a) The Audited Company

The issue is undisputed: there is unanimous agreement that actions can be brought by the audited company on the basis of contractual liability or tort liability, depending on the country (see *supra* §1.1.2 p. 7).

b) Third Parties

This is an overall category excluding the audited company. Third parties may be injured parties to the extent that they are likely to be interested in reading and using the auditor's report. This includes the audited company's linked companies, its shareholders, creditors and employees.

The main question relates to privity. There are questions and variations in the Member States on liability in the absence of privity. Can an injured party, who is not in privity with the contracting parties, successfully bring a liability action against the statutory auditor?

According to the Commission's Green Paper, "there does not seem to be a reason to confine the liability of the auditor to the audited company – as the statutory audit has been required in the public interest." Green Paper, Section 5.1 et seq. The original draft of the proposal for a Fifth Company Law Directive reflected the position set forth in the Commission's Green Paper. However, this provision was later amended to eliminate all reference to liability to third parties, concentrating solely on the liability to the audited company.

The table hereafter shows that national systems can be divided into two general categories:

- countries where actions by third parties, including shareholders, are freely admitted;
- countries where restrictions are placed on such actions, making them more difficult.

COUNTRY	SHAREHOLDERS ON THEIR OWN BEHALF	OTHER THIRD PARTIES
Aus	Under restrictive conditions	Under restrictive conditions
Bel	Yes	Yes
Den	Yes	Yes
Fin	Yes	Yes
Fra	Yes	Yes
Ger	Under restrictive conditions	Under restrictive conditions
Gre	Yes	Yes
Ire	Under restrictive conditions	Under restrictive conditions
Ita	Yes	Yes
Lux	Yes	Yes
Ned	Not Clarified	Not Clarified
Por	Yes	Yes
Spa	Under restrictive conditions	Under restrictive conditions
Swe	Yes	Yes
UK	Under restrictive conditions	Under restrictive conditions

- ***Countries where actions by third parties are freely admitted (Bel, Den, Fin, Fra, Gre, Ita, Lux, Por, Swe)***

Such tortious actions may be brought by anyone who suffered a damage, provided the damage, the auditor's fault and the causal link are established.

The way these elements of liability are appreciated may differ from one Member State to another, as they refer to the core regime of tort liability. This section focuses on the existence of the action in principle, not on the chances of damages to be compensated. This will be examined in detail in sections 1.4.2 and 1.4.3 hereafter with regard to the extent of the auditor's liability.

The main difference between these countries is the legal ground of the admission of the auditor's liability towards third parties:

- In some countries, third parties' actions against auditors are provided for in the statute applicable to auditor's liability (see *supra* section 1.1.3):
 - Belgium: Article 64 octies of the LCSC;
 - France: Article 234 of the Company Law of 24 July 1966;
 - Finland: Section 44 of the TTL;
 - Italy: Article 64 of the Legislative Decree of 24 February 1998;
 - Portugal: Article 78 CSC (auditor's liability towards creditors), Article 82 CSC (auditor's liability towards shareholders) and Article 10 CMVM (extended liability of stock listed companies' auditors towards third parties);
 - Sweden: Chapter 15 Section 2 of the Swedish Companies Act.

These rules do not limit third parties' actions to specific categories, except in Portugal where the various statutes actually offer to a wide range of third parties the right to sue.
- In other Member States where third parties' actions are freely admitted, the general rules of tortious liability apply, without any specific provision for third parties' actions:
 - in Greece and Luxembourg, the Civil Code;
 - in Denmark, Courts grant compensation to a wide range of third parties, by considering the auditor as a "representative of the public".

- ***Countries with restrictions on actions by third parties (Aus, Ger, Ire, Ned, Spa, UK)***

In these countries, the action of the third party must fulfill the condition that the auditor owes a duty of care to this third party, i.e. the auditor knew or ought reasonably to have known that his work or report would be relied on by claimant for a particular purpose.

This concept of "foreseeability" has been mostly developed by English Courts. It is close to the Irish approach and may also apply in the Netherlands, where the issue is still disputed. In Austria and Germany, the auditor's liability towards third parties is governed by different rules depending on whether it is contractual or tortious. In Spain, Courts have laid down several conditions to third parties' actions stated in the law.

In the **United Kingdom**, any natural or corporate person may in principle sue a statutory auditor, but the auditor could generally be liable only if he owed that person a duty in tort to exercise reasonable care and skill in carrying out the audit. These duties have been defined by

several Court decisions. The auditor enters the scope defined in the case *Hedley Byrne v. Heller*³¹ in 1964, where the House of Lords held that a person who negligently makes a false statement which causes financial loss to another may be liable to that other person in the tort of negligence even if there is no contract between them, provided there is a “special relationship” between them³².

The scope of the auditor’s duty of care has been precised in the *Caparo* matter, a case involving auditors, by reference to the purpose for which the statutory audit is performed³³. The possibility for third parties to sue as it results from the case is rather restrictive: in ordinary circumstances, a statutory auditor in carrying out the audit owes a duty of care only to the company itself and to the shareholders of the company collectively in their capacity as members. The auditor does not, except in special cases, owe a duty of care to the officers of the company, to any shareholders in their individual capacity as investors, to potential purchasers of or investors in the company, nor to creditors, suppliers, employees or others.

Since this major decision, there have been a number of others in which the question of whether an auditor owed such a duty of care to someone other than the audited company has arisen³⁴. The House of Lords stated in *Al Saudi Banque v. Clark Pixley* ([1990] Ch 320), quoting the esteemed American Judge Benjamin Cardozo, that eliminating the “special relationship” criteria would lead to “liability in an indeterminate amount for an indeterminate time to an indeterminate class.”

In **Ireland**, the extent to which Courts will impose such a duty of care on auditors in favour of third parties has not yet been definitely ascertained. The decision in *Kelly v. Boland*³⁵ ([1989] IRLB 373) is in line with the approach of the English House of Lords in *Caparo v. Dickman*: the auditor may be liable if he owed persons such as the plaintiff a legal duty of care to avoid the sort of losses in fact experienced, and if there was a breach of that duty of care.

In **the Netherlands**, while the notion that statutory auditors may be held liable for their statement is more or less generally accepted³⁶, it is not completely clear which third parties may successfully recover damages from the statutory auditor and if there are additional requirements to be met before liability can be accepted. The question regards the interpretation of the interests protected by Article 6:162 Civil Code (liability based on tort [*onrechtmatige daad*]), in relation to the scope of the protection enjoyed by third parties with respect to the auditor's statement to the annual accounts. In the discussion, those who would require the application of the proximity criteria as defined by the English House of Lords in the *Caparo* case face those who consider that the auditor’s report is given for the benefit of, *inter alia*, the shareholders, and therefore no other conditions should be required. The Supreme Court has not taken a position with respect to this issue, and from the rare case law of lower Courts, it is not possible to extract any general principles or any development in case law.

In **Austria** and **Germany**, the liability of third parties can be based on the contract or in tort:

i) Linked companies: according to the statutes regulating the auditor’s liability (for Austria §275.1 HGB and for Germany §323 HGB, as presented *supra* §1.1.3 p. 9 and 12), linked companies may recover for damages caused by the auditor.

ii) Implied contracts: even if no contract has been formally concluded, the relationship between the auditor and a third party may be treated as such, and subject matter of the agreement is the provision of information by the auditor to a third party. In other words, if the auditor provided information to a third party and could not ignore that this information would be used and indeed this information determined the decision having caused damage, then this theory allows compensation.

In Austria, the existence of the contract would be deducted from the acts of the parties: for example, if the statutory auditor provides information directly to a bank that extends credit to a company, Austrian courts would probably treat the relationship between the bank and the auditor as such an agreement.

In Germany, the Supreme Court (*Bundesgerichtshof*) set forth the rule that an “information contract” between the auditor and a third party was tacitly concluded if information was given by the auditor which recognisably was of essential significance to the third party and if the latter considered this to be a basis for important decisions or measures³⁷. More recent decisions limit such liability for information and set strict conditions for a tacitly concluded information contract. Such a contract only exists if the circumstances allow the inference that the information should be subject to contractual rights and duties³⁸.

iii) Contracts having protective effects to third parties (*Vertrag mit Schutzwirkung zugunsten Dritter*): Courts apply this concept to auditor’s liability, and therefore impose a duty of care to third parties.

Austrian Courts would apply this theory under restrictive conditions. It is conceivable that, under very strict circumstances, such actions might be brought by a creditor or a third party that acquired stock of the company in reliance on the audit report if the statutory auditor knew that the buyer would rely upon the report. However, the mere general knowledge that the report is usually forwarded to banks extending credit to the audited company will probably not suffice for the establishment of such a duty.

In Germany, the contract may have protective effects with respect to a third party if the following conditions are met:

- the third party is close to the contracting party’s performance;
- the performing party is obliged to provide protection and care or, in his view, the performance shall also be to the benefit of the third party;
- the benefit to the third party of protection and care must be obvious to the statutory auditor.

This theory of contracts with protective effects enables third parties to recover damages for pure economic loss in cases of wrongful information, misrepresentation or false audit certificates when the law of torts would not allow compensation³⁹.

iv) Tort actions: they are conceivable in Austria, but irrelevant in practice, considering the general rules of civil liability. In Germany, third parties may base their action on the general rules for tort liability, as long as plaintiffs are within the protective ambit of a breached statute (under Article 823 II BGB), which may be the case with shareholders⁴⁰ or creditors, or they are intentionally harmed in a manner that is contrary to “good morals” (under Article 826 BGB).

In **Spain**, even if the availability of third parties' actions is stated by Article 11 of the *Ley de Auditoria de Cuentas* and Article 42 of the Royal Decree 1636/1990, it would be necessary to establish at least that the auditor had a duty of care to the third party.

c) Collective Actions

As shareholders of public companies are often individuals who do not have resources to undertake sufficient complex and costly litigation to protect their rights, such actions as those brought by shareholder organisations and class actions are two examples of actions which attempt to increase small investor's power.

Shareholder organisations are groups which represent the shareholders and attempt to advance the collective or individual interests of their members.

A "class action", a concept which originated in the American legal system, allows shareholders with a valid claim to join with other shareholders who suffered the same damage to prosecute their claims in the name of a small number of shareholders but on behalf of the entire group. The notice requirements for potential plaintiffs are usually less formal – targeted shareholders are included in the class unless they expressly request to be excluded.

Derivative actions differ from that of shareholders organisations and class actions in that the shareholders bring suit on behalf of the company for injuries that the company suffered. Any damages awarded are paid to the company.

As is clear from the chart below, the general trend in the Member States is that standing to sue remains with the injured party, whether this is the company or the individual shareholder. There are only a few notable exceptions to this general restrictiveness which are listed below:

COUNTRY	SHAREHOLDER ORGANIZATION	CLASS ACTION	DERIVATIVE ACTION
Aus	No	No	No
Bel	No	No	No
Den	No	No	No
Fin	No	No	No
Fra	Yes	No	No
Ger	No	No	No
Gre	No	No	No
Ire	No	No	No
Ita	No	No	Yes
Lux	No	No	Yes
Ned	No	No	No
Por	No	Yes	Yes
Spa	No	No	Yes
Swe	No	No	No
UK	No	No	Yes

Shareholders Organisations

France is the only Member State which grants standing to sue to shareholders' organisations. French decisions support the position that an association of shareholders may maintain an action to recover the damages sustained by each of its members individually. Moreover, the law of 5 January 1988, as modified by the laws of 23 June 1989 and 8 August 1994, grants associations certain powers to defend the rights of persons in the areas of investment in securities and in other financial products. Certified associations have the right to represent all investors⁴¹.

In practice, few associations have been certified and few, if any, actions have been introduced by them against statutory auditors.

Class Actions

Portugal is the only Member State which allows class actions.

Law n° 83/95 dated 31 August 1995 establishes the circumstances and terms under which a class action (*Acção Popular*) can be brought. It provides among others, for "the protection of consumers of goods and services" (Article 1 paragraph 2, of let n° 83/95). However, such a situation has never come before the Courts in the field of statutory auditing. The Securities Exchange Act, which was approved by Decree-Law n° 486-99 of 13 November 1999, deals with the rights of investors and completes Law n° 83/95⁴².

Every individual with a legitimate interest has standing to sue. Associations defending the interests protected by the class action law and whose articles of incorporation expressly provide for the defence of their members' rights, also have standing to sue. In the class action, the plaintiff represents all the potential injured parties, without their formal permission or a power of attorney. When the Court receives the class action petition, it notifies the injured parties who must take a formal position in the action, and state whether they accept or refuse to be represented in the case. Silence is deemed acceptance. If a potential plaintiff expressly refuses to be part of the group, he is said to be exercising his right to "self-exclusion" (*direito de auto-exclusao*).

Derivative Actions

As shown below, only five Member States allow shareholders, and sometimes creditors, to act against statutory auditors on behalf of the audited company.

COUNTRY	ALLOWED (YES / NO)	WHO CAN ACT	CONDITIONS
Aus	No	Not Applicable	Not Applicable
Bel	No	Not Applicable	Not Applicable
Den	No	Not Applicable	Not Applicable
Fin	No	Not Applicable	Not Applicable
Fra	No	Not Applicable	Not Applicable
Ger	No	Not Applicable	Not Applicable
Gre	No	Not Applicable	Not Applicable
Ire	No	Not Applicable	Not Applicable
Ita	Yes	Shareholders	Min. detention 5% for at least 6 months and only for publicly traded companies
		Creditors	When assets are not sufficient to cover the company's debts
Lux	Yes	Shareholders Creditors	Only for banks
Ned	No	Not Applicable	Not Applicable
Por	Yes	Shareholders	Min. detention 5% and company joined to the lawsuit
Spa	Yes	Shareholders	Min. detention 5% Specific procedures as detailed hereafter
Swe	No	Not Applicable	Not Applicable
UK	Yes	Minority shareholders	No conditions Specific procedures as detailed hereafter

In **Portugal**, collective actions, as defined by articles 77 par. 1 *in fine* and 4 of the CSC, require the company to be judicially called to the action.

In **Spain**, holders of 5% or more of the capital of the audited company (as a group or individually) are entitled to require the company's directors to convene a shareholders' meeting in order to decide whether or not to bring an action against the company's auditors. If the meeting is not convened, the shareholders decide not to bring the action or the claim is not filed within one month, then the minority shareholders may bring the action on behalf of the company.

In the **United Kingdom**, minority shareholders who could not show that the auditor owed them a duty of care as individuals and who could not persuade a majority of shareholders to compel the company to take action may attempt to persuade the Court that action should be taken in the company's name despite the refusal of the majority of shareholders to do so.

d) Bankruptcy

The impact of bankruptcy is potentially significant because the liability of statutory auditors is often raised when audited companies file for bankruptcy. Given the specific bankruptcy procedures of the Member States, neither their possible effects on the overall system of civil liability of statutory auditors nor the rules applicable in this situation can be ignored.

As a result, it is relevant to consider whether there are there specific rules regarding plaintiff when the company is in bankruptcy, and whether the liquidator or the receiver have the privilege of the action.

The receiver is the administrator of the company while in bankruptcy where the Company is allowed to keep operating. The liquidator is appointed to settle the company's debts and assets. As used with respect to the various Member States, the notions of Liquidator and Receiver include the following:

Aus	Liquidator:	<i>Masseverwalter</i>
Bel	Receiver:	<i>Curateur</i>
Den	Receiver:	<i>Bobestyrer</i>
Fin	Receiver / Liquidator:	<i>Pesänhoitaja</i>
Fra	Receiver:	<i>Administrateur judiciaire</i>
	Liquidator:	<i>Liquidateur</i>
	Creditors' Representative:	<i>Représentant des créanciers</i>
Ger	Receiver:	<i>Insolvenzverwalter</i>
Gre	Receiver:	<i>SúvdikoV</i>
	Liquidator:	<i>EkkaqaristhV</i>
Ire	Liquidator:	<i>Liquidator</i>
Lux	Receiver:	<i>Curateur</i>
	Liquidator:	<i>Liquidateur</i>
Ned	Receiver:	<i>Curator</i>
Por	Liquidator:	<i>Liquidatário Judicial</i>
Spa	Receiver:	<i>Depositario / Síndicos</i>
Swe	Receiver:	<i>Konkursförwaltare</i>
	Liquidator:	<i>Likwidator</i>
UK	Liquidator:	<i>Liquidator</i>

The chart below reveals a disparity among national laws:

COUNTRY	ACTIONS ON BEHALF OF THE COMPANY	ACTIONS ON BEHALF OF THIRD PARTIES
Aus	Liquidator	Third Parties
Bel	Receiver	Receiver / Third Parties
Den	Receiver	Third Parties
Fin	Receiver/Liquidator	Receiver / Third Parties
Fra	Receiver/Liquidator	Creditors' Representative / Third Parties
Ger	Receiver	Receiver / Third Parties
Gre	Receiver/Liquidator	Third Parties
Ire	Liquidator	Third Parties
Ita	Receiver	Receiver / Third Parties
Lux	Receiver/Liquidator	Receiver / Third Parties
Ned	Receiver	Receiver / Third Parties
Por	Liquidator	Third parties
Spa	Receiver	Third Parties
Swe	Receiver/Liquidator	Third Parties
UK	Liquidator	Third Parties

The receiver or the liquidator represents the company while in bankruptcy period. As a result, he has sole authority to sue the auditor on behalf of the company. This principle applies in all Member States⁴³, the position of the person acting on behalf of the company depending on local bankruptcy law specificities.

The rules regarding the availability of third parties' actions remain unchanged in most Member States when the company is in bankruptcy (Aus, Den, Gre, Ire, Por, Spa, Swe, UK).

In the other Member States (Bel, Fin, Fra, Ger, Ita, Lux, Ned), the person acting on behalf of the company also has standing to sue on behalf of third parties. However, injured parties may bring action on their own behalf as far as they suffered damage different from that suffered by other creditors and by the audited company. This rule applies with slight specificities in France, Finland and Germany:

- in Finland, if the third party's action is based on his status as creditor of the bankrupted company, all proceeds are first paid to the bankruptcy estate;
- in France, the person in charge of the protection of the creditors is a third person, the creditor's representative, who is different from the liquidator and the receiver;
- in Germany, this rule applies from the point in time when a procedure is formally opened, therefore an individual creditor may sue on his own behalf if the bankruptcy proceeding has not been formally opened (due to a lack of remaining assets).

1.2.2 Defendant(s)

The question of against whom may the liability action be brought is rather relevant for the plaintiffs, whose litigation must be brought against the right person or firm.

Questionnaire references:

- *In the case where an individual operates his own business, should separate litigation be brought against his or her associates who undertook the work. (Question 1.4.1)*
- *If the audit is undertaken by a legal entity and if the firm is the statutory auditor, can an action be brought against the firm? Against the individual in charge of the audit and who signed the reports (if such a signature was required)? Against the other partners of the firm, even if they did not participate in the audit in question? Against the associates of the individual who undertook the audit? (Question 1.4.2.1)*
- *If the audit is undertaken by a legal entity but the individual is the statutory auditor, can the action also be brought against the firm, under a respondent superior or some other theory? Against the other partners of the firm? Against the associates who participated in the audit? (Question 1.4.2.2)*
- *When several statutory auditors conduct a joint audit (if this is authorised or required by applicable laws or regulations), must they establish a common report? Are they jointly and severally liable or is liability apportioned according to the percentage of work undertaken or in some other way? (Question 1.4.3)*
- *Is the statutory auditor of a parent company liable with respect to inaccuracies in the accounts of its subsidiaries? Are the statutory auditors of both the parent company and subsidiaries jointly and severally liable? (Question 1.4.4)*

SUMMARY : DEFENDANT(S)

The most common situation regarding the party against whom the liability action may be brought is as follows.

The appointed statutory **auditor**, either an individual or a firm, is liable in all Member States. If the auditor is a firm, the individual **signing** the report is jointly and severally liable with the firm. The **associates** would not be successfully pursued: either they are not liable or it is more relevant to bring the action against the statutory auditor. The detailed study points out two exceptions: in Ireland, only a sole practitioner or a partnership may be appointed as a statutory auditor; in the Netherlands, it is not required that an individual signs the report on behalf of the firm.

The case of **joint audits** may arise in all the Member States: the liability between joint auditors is generally joint and several, but under specific conditions, it is possible to apportion the liability according to their actual individual involvement (Denmark, France, Ireland, and Sweden).

In the course of the **audit of consolidated accounts**, in some countries the parent's auditor may be different from the subsidiaries' auditors. Then he is liable for any breach of duty related to the consolidated accounts, including the control of the subsidiaries' audits, but he is not liable if he reasonably relied upon the work done by the subsidiaries' auditors (Bel, Fra, Gre, Ire, Ita, Lux, Ned, Por, Spa, UK), or if he checked that the subsidiaries have been audited according to the same principles as those applicable in the country (Austria) or by an EU statutory auditor (Germany). In this case, only the subsidiary's auditor may be liable. The parent's auditor and the subsidiaries' auditors are jointly liable if both have been negligent in their reviews. In three Member States (Finland, Denmark and Sweden), parent and subsidiary companies have the same statutory auditor who consequently may be liable for any breach related to the subsidiary's account.

The chart below presents the compared situation in the European Union as regard to the different defendants :

COUNTRY	Individual Auditor / Audit Firm	Signatory of Report	Associates*
Aus	Yes	Yes	Yes
Bel	Yes	Yes	Yes
Den	Yes	Yes	No
Fin	Yes	Yes	Yes ⁱ
Fra	Yes	Yes	No ⁱⁱ
Ger	Yes	Yes	Yes ⁱ
Gre	Yes	Yes	No
Ire	Individual / Partnership	Yes	Yes ⁱ
Ita	Yes	Yes	Yes/No
Lux	Yes	Yes	No
Ned	Yes	N/A	Yes
Por	Yes	Yes	Yes
Spa	Yes	Yes	No
Swe	Yes	Yes	No
UK	Yes	Yes	No
* The term “associates” refers to employees of the statutory auditor or the auditing firm. ⁱ This is rare in practice. ⁱⁱ Except if the associate acted outside the scope of his employment.			

a) Appointed Statutory Auditor

The appointed statutory auditor is the main liable person since he signed the audit contract with the audited company and therefore issued the report. He is either an individual person or an audit firm.

- In all fifteen Member States, the statutory auditor may be a natural person without being part of a legal entity. In such cases, he is obviously liable for his faults and negligence.
- If the appointed auditor is an audit firm, the firm is the liable person. In one Member State (Ire) a body corporate shall not be qualified for appointment as a statutory auditor. An audit must be undertaken by either a sole practitioner or a partnership. In this case, each partner is jointly and severally liable.

Though it rarely occurs in practice, in some Member States (Aus, Bel, Den, Fra, Fin, Ger, Gre, Ire, Ita, Lux, Ned, Swe, UK), the mandate can be given to an individual statutory auditor even if he works for an auditing firm, while in other Member States (Por, Spa) only the auditing firm may accept the auditing mission. When the mission is given to an individual statutory auditor within a firm, either the auditing firm is discharged from liability (Bel, Gre, Lux), or the firm is jointly liable with the individual in charge of the audit only if he is also a legal representative of the company (Aus, Ger), or the firm faces liability under a *respondiat*

superior theory (Fra, Swe) or on the basis of an implied contract (Den, Fin, Ire, Ita, Ned, Swe, UK).

b) Signing Person

When the auditing mission is undertaken by an auditing firm, in each Member State except the Netherlands, an individual is required to sign the audit report on behalf of the auditing firm. Thus, the signatory is jointly and severally liable with the auditing firm.

c) Associates

With respect to associates, two possibilities exist :

- either any action against them is impossible (Den, Gre, Spa, Swe, UK and Ita for the associates of the Board of Auditors) or difficult (Fra),
- or it is possible to bring such an action but it rarely occurs in practice since the fact that the auditor is responsible for their acts makes filing suit against an employee pointless (Aus, Bel, Fin, Ger, Ire, Lux, Ned, Por, Ita for the associates of an Auditing Firm).

d) Joint Auditors

The question of the liability of several auditors when they conducted a joint audit is all the more important as joint audits are allowed in all the fifteen Member States and even required in France in certain cases.

COUNTRY	Joint audits are	Must a joint report be issued?	How is liability allocated
Aus	Allowed	No ⁱ	Joint and several
Bel	Allowed	Yes	Joint and several
Den	Allowed	Not Clarified	Joint and several/proportional
Fin	Allowed	Yes	Joint and several
Fra	Required ⁱⁱ	Yes	Joint and several/proportional
Ger	Allowed ⁱⁱⁱ	Yes	Joint and several
Gre	Allowed	Yes	Joint and several
Ire	Allowed	No	Joint and several/proportional
Ita	Allowed ^{iv}	Yes	Joint and several
Lux	Allowed ⁱⁱⁱ	Yes	Joint and several
Ned	Allowed ⁱⁱⁱ	Not Clarified	Not Clarified
Por	Allowed	Yes	Joint and several
Spa	Allowed	Yes	Joint and several
Swe	Allowed	No ⁱ	Joint and several/proportional
UK	Allowed ⁱⁱⁱ	Yes	Joint and several

ⁱ However, it is current practice that the auditors submit a common report.

ⁱⁱ For *sociétés anonymes* required to publish consolidated financial statements and banks with more than 3.000 million FF in assets.

ⁱⁱⁱ Though joint audits are theoretically possible, they rarely (Ger, Lux, UK) or never (Ned) occur in practice.

^{iv} The audit by the Board of Auditors is considered a joint audit since it is carried out by three or five statutory auditors. However, joint audits carried out by two or more auditing firms are not permitted.

The chart above shows that where joint audits are a common practice (all Member States except Ger, Lux, Ned and UK), the liability of the auditors is principally joint and several even if they did not issue a joint report (this is the case in Ire, Aus and Swe).

In some cases, liability is proportional :

- in France, though a joint report must be issued, the statutory auditor may submit his dissenting opinion which may exonerate him from liability;
- in other Member States, the possibility of an apportionment of liability, if it exists, depends on the allocation of the work or on the circumstances of the joint audit :
 - in Denmark, auditors may divide the work between themselves in an agreement with the client: in such a case, when the client is aware of the scope of the work undertaken by each of the several auditors separately, the auditor who is not negligent may avoid liability; the limitation of liability does not apply, as the third party has no knowledge of the division of the work between the auditors;
 - in Sweden, it is acceptable that auditors divide the work between them, and consequently an error in the report may be the result of the negligence of one but not the other; if, however, both have been negligent, they will in principle be jointly and severally liable, although the Court could decide to apportion liability according to their respective degree of negligence;
 - in Ireland, theoretically, circumstances might arise where only one joint auditor is liable (i.e. the other is held to have acted with due skill and care in expressing his opinion). If both auditors were liable, liability could be apportioned between them, but, if one joint auditor is unable to discharge its share of the plaintiff's losses, the other liable joint auditor would be liable to make up the deficit;

In Finland, in the relationship between the defendants, the amount of damage payable has to be fairly divided, taking into account the negligence of each of the auditors, any benefit gained as a result of the action which caused the damage and other circumstances.

e) Parent Companies or Subsidiaries

The question arises in group audits: is the statutory auditor of a parent company liable with respect to inaccuracies in the accounts of its subsidiaries? Are the statutory auditors of both the parent company and subsidiaries jointly and severally liable?

In some Member States (Den, Fin, Swe), at least one of the statutory auditors of the parent company must also be an auditor of the subsidiary. As a result, he is liable for any breach related to the subsidiary's accounts.

In Austria and Germany, the statutory auditor responsible for the audit of the consolidated accounts is also required to audit the annual accounts of all subsidiaries whose accounts are consolidated. However, in both countries he may be dispensed from such duty: in Austria with regard to annual accounts of subsidiaries that were audited in accordance with the provisions of the Austrian Commercial Code or – with regard to non-Austrian subsidiaries – whose accounts were audited in accordance with the equivalent foreign provisions by an equally qualified auditor, and in Germany, if the accounts that are consolidated were audited

by an EU statutory auditor⁴⁴. In practice, the requirements of the law which discharge the auditor of the parent company from the obligation of auditing the accounts of the subsidiaries are usually fulfilled.

In other Member States (Bel, Fra, Gre, Ire, Ita, Lux, Ned, Por, Spa, UK), the parent company and the subsidiaries may have different statutory auditors. In this case, the statutory auditor of the parent company is not required to audit the accounts of the subsidiaries but does have an obligation to check the work done by the subsidiary's auditors. As a result, if the subsidiary's auditor was negligent and if a proper review by the parent's auditor should have revealed the deficiency, then both the subsidiary's auditor and the parent's auditor will be jointly and severally liable. On the contrary, if the subsidiary's auditor was negligent but the parent's auditor acted with due skill and care (meaning that he reasonably relied on work done by the auditor of the subsidiary), then the subsidiary's auditor would be solely liable. On the other hand, if the mistake was made in the course of the consolidation of the group accounts, the statutory auditor of the parent company will be solely liable.

1.3 Events Leading to Civil Liability

As will be seen below, the statutory auditor's exposure to liability begins upon the acceptance of the auditing mission and continues up and even after the submission of the auditing report.

This section will concentrate on the key events which could lead to liability, as may arise from the appointment of the statutory auditor (1.3.1) or the exercise of his duties (1.3.2).

SUMMARY: EVENTS LEADING TO LIABILITY

Some of the auditors' duties are related to the acceptance of the mission and its termination.

At the time of the acceptance of the mission, the existence of a conflict of interest obliges the auditor of all the Member States to give up pursuing the mission and may lead to his liability if this situation has caused a damage. Cases other than impediments leading to the statutory auditor's liability at this step may be the lack of the necessary human and material resources or the fact that a particular client provides a too large part of the auditor's total income, but in theory any wrongful acceptance causing damages may have this consequence.

Regarding the termination of the mission, nine Member States require that the auditor resigns for a good cause (Aus, Bel, Ger, Gre, Ita (auditing firms), Lux, Ned, Spa and Swe). In the other cases, the auditor may be held liable only if he resigns in bad faith.

The auditor's liability arising in the completion of his mission is considered through his duty of care (*obligation de moyens*): no bargained for result is to be achieved but the auditor promises to make every effort possible to achieve the result, except for some secondary missions for which the auditor is bound by a strict liability (*obligation de résultat*). Therefore, the auditor may be liable only if it can be proved that he caused a damage because he did not meet his duty of care in the completion of one of his duties.

Given this pre-requisite, the auditors' breach of duties leading to liability are substantially similar in all the Member States:

- irregular or misleading audit opinion: it may give rise to actions brought by third parties (banks, investors, suppliers) who made their decision upon the auditor's report expressing an erroneous audit opinion on the financial statements; the audited company may also sue the auditor if this false opinion caused a damage;
- non or late disclosure of fraud or irregularities : it is a ground for the auditor's liability if it led to a false audit opinion (as presented above), or if the plaintiff suffered a damage since by negligence the auditor did not detect the fraud, or once detected, did not disclose it, and if the damage could have been avoided in case of absence of fault or negligence;
- breach of other duties (e.g.: disclosure of events compromising the solvency of the company, duty of confidentiality, reporting on contracts between the company and its officers or between two companies having common directors, modifications of the company's articles of organisation, change in the capital, not interfering with the management, notification of shareholder's meeting in the case of directors' deficiency) may also give rise to auditor's liability.

1.3.1 Liability Arising out of the Appointment as Auditor

Questionnaire reference:

Liability arising out of the acceptance or of termination of the appointment as auditor (e.g.: conflict of interest, resignation in bad faith or untimely). (Question 3.1.1)

a) Acceptance of the Mission

In each of the fifteen Member States, the existence of a conflict of interest prevents a statutory auditor from accepting a mission. Moreover, if the conflict arises during the audit, the statutory auditor must withdraw from the mission.

The proscription in case of conflict of interest is usually included in the legislation governing statutory auditors, while in common law countries the rule has been developed by the Courts. The ethical rules adopted by the various certifying boards and professional organisations provide guidance to the statutory auditor concerning the existence of a conflict of interest and usually set forth the disciplinary measure which would be taken in case of violation.

As a general rule, a statutory auditor is liable for any damages caused by the existence of a conflict of interest. Though there is little case law on this subject, an analogy can be made, in general, to the conflict of interest rules that have developed for other professions where a fiduciary relationship exists, e.g. accountants, lawyers.

Generally speaking, there are few other cases foreseen by law or professional rules, except impediments, giving rise to auditors' liability at this step, but the common rule is that any damage caused by a wrongful acceptance may lead to the auditor's liability. The most common examples of such situations refer to circumstances showing a lack of independence, such as the fact that the income received from the audited company represents a certain part of the total income of the statutory auditor (Bel, Fra, Ned, Spa). Insufficiency of staff or of skills compared to what is required to perform the statutory auditor's duty are other grounds for the auditor's liability, if they caused a damage (Bel, Ger, Gre, Ned, Spa, Swe). The cases leading to statutory auditor's liability out of his appointment are illimited in theory, but, except for the aforementioned conflict of interests, rare in practice.

b) Termination

The fact that there is a fiduciary relationship between the statutory auditor and the audited company removes the audit mission from the class of services that are provided in an employer-employee or business-client situation. Thus, in light of this special relationship, some limitations have been placed on the statutory auditor's ability to resign from his mission.

COUNTRY	Must the auditor show good cause to resign?	Can this lead to liability?	Court Decisions
Aus	Yes	Yes	No
Bel	Yes	Yes	No
Den	No	Yes	No
Fin	No	Yes	No
Fra	No	Yes	Yes
Ger	Yes	Yes	No
Gre	Yes	Yes	No
Ire	No	No ⁱ	No
Ita	No ⁱⁱ	Yes	No
Lux	Yes	Yes	No
Ned	Yes	Yes	No
Por	No	Yes	No
Spa	Yes	Yes	No
Swe	Yes	Yes	No
UK	No	Yes	No

ⁱ The Irish Courts have not yet been called upon to determine the extent to which, if at all, it is possible to bring a claim against a former auditor on the basis of wrongful resignation. Although possible, any such claim appears unlikely and could face significant legal and factual difficulties.

ⁱⁱ Regulated auditing firms only are required to provide serious motives for resignation. This is confirmed by the absence of provisions on this subject in the TU.

In nine Member States (Aus, Bel, Ger, Gre, Ita (auditing firms), Lux, Ned, Spa and Swe), the auditor must show cause to resign from his mission.

In the remaining cases (Den, Fin, Fra, Ire, Ita (Board of Auditors' members), Por, UK) no showing of cause is necessary. Nevertheless, in these countries any resignation which is untimely or in bad faith could also provide the audited company or a third party with a cause of action for damages⁴⁵. It should be noted that though no duty of showing good cause weighs upon the auditor, he would logically not be allowed to resign for the purpose of avoiding his contractual or statutory obligations. This rule diminishes the importance of the dichotomy that exists among the Member States with respect to this question.

1.3.2 Liability Arising out of Exercise of Duties

As the Commission's Green Paper pointed out, the principal expectations of the public are as follows: the accuracy of financial statements, the going concern status, fraud, and compliance with corporate legal obligations. This section explores the statutory auditor's liability in the Member States with regard to these expectations and duties.

After discussing the duty of care (a), the following issues will be explored: irregular certification (b), non-disclosure of fraud or of violations of company law (c) and other events which may occur in the course of the statutory audit (d).

a) Degree of Duty

Questionnaire reference:

Does the liability arise from the bargained-for result not being achieved or solely from a breach of duty? Do the answers to these questions vary according to the nature of the statutory auditor's duties? (Question 2.1.3)

This concept encompasses the criteria applied to determine the conditions under which an event can lead to liability, where the statutory auditor's duties consist in a duty of care (*obligation de moyens*), as opposed to a bargained-for result to obtain, failing what the statutory auditor is strictly liable (*obligation de résultat*).

In case of an *obligation de résultat*, liability arises automatically from the fact that a bargained-for result is not reached. The plaintiff does not need to prove defendant's fault. The only way for the defendant to be exempted is to show that the failure to reach the result is due to *force majeure*. The absence of fault or negligence is no defence to such a claim. This concept could also be referred to as strict liability. In case of an *obligation de moyens*, the defendant does not promise to obtain the desired result but to make every effort possible to achieve the result. Therefore, the defendant is exposed to liability only if the plaintiff proves that the non-achievement of the result is due to defendant's breach.

The question of whether the statutory auditor is bound by more than his fault gave rise to the following results:

COUNTRY	A duty of care (<i>obligation de moyens</i>)	Strict liability (<i>obligation de résultat</i>)
Aus	Yes	No
Bel	Yes	No
Den	Yes	No
Fin	Yes	No
Fra	Yes	Yes
Ger	Yes	No
Gre	Yes	No
Ire	Yes	No
Ita	Yes	Yes
Lux	Yes	Yes
Ned	Yes	Yes
Por	Yes	Yes
Spa	Yes	Yes
Swe	Yes	No
UK	Yes	No

In a minority of Member States, the statutory auditor is liable only if he breached his duty in the completion of his mission.

This solution may be justified by the fact that certification of accounts, the statutory auditor's main mission, involves a part of uncertainty, since the applicable statutes, regulations and professional standards prescribe the use of tests as opposed to a full audit, and the statutory auditor is not in charge of the permanent control of the audited company.

Even an appropriate audit complying with legal, regulatory and professional requirements, may not allow a statutory auditor to detect certain inaccuracies in the accounts or the existence of fraud. In such a case, the statutory auditor will not be held liable. A claim will be successfully brought against a statutory auditor only if it can be proved that he did not meet his duty of care in carrying out his mission, which would have allowed him to discover accounting irregularities. The majority of cases involving auditors deal with this issue. Moreover, even if the statutory auditor did undertake the necessary activities, he can still be found liable if he did not draw the proper conclusions from his work, for example by not refusing to certify the accounts, by not issuing his report with the requisite reservations, or by not informing the board of directors, the shareholders and the public authorities of the irregularities.

At the same time, in certain countries and for certain missions which have no element of uncertainty, the auditor is strictly liable or held to a standard of *obligation de résultat*.

In France, some secondary missions of the statutory auditor do not include any uncertainty and, therefore, he is bound by an *obligation de résultat* with respect to such duties. This is the case, for example, when the statutory auditor:

- certifies the accuracy of the amount of the largest remuneration paid by the audited company;

- verifies that the directors of the company comply with Article 95§1 of the Company Law which requires them to own at least the number of shares indicated in the Articles of Association.

In Luxembourg, the Netherlands and Spain, the statutory auditor would be strictly liable if he did not file his report before the statutorily prescribed deadline.

In Italy and Portugal, straightforward verifications, such as the cash on hand and the stock portfolio of the audited company, are subject to an *obligation de résultat*.

b) Irregular or Misleading Opinion

Questionnaire reference:

Irregular or misleading certification of accounts giving an inaccurate image of the company or certification of information tendered to shareholders. (Question 3.1.2.1)

COUNTRY	Does irregular certification lead to liability?	Court Decisions
Aus	Yes	No
Bel	Yes	Yes
Den	Yes	Yes
Fin	Yes	No
Fra	Yes	Yes
Ger	Yes	Yes
Gre	Yes	No
Ire	Yes	No
Ita	Yes	No
Lux	Yes	No
Ned	Yes	Yes
Por	Yes	No
Spa	Yes	No ⁱ
Swe	Yes	Yes
UK	Yes	Yes
ⁱ There is no direct pronouncement by the Courts on this subject. However, auditor's liability has been mentioned, <i>obiter dictum</i> . ⁴⁶		

Certification of the company's accounts is the primary mission of the statutory auditor. It is supported by the written Audit Report, which materialises the conclusions of the auditor's controls and investigations. As a result, an irregular certification can lead to liability if the elements of a civil liability action in contract or in tort are satisfied (see *infra* section 1.4).

While in seven Member States Courts have not been called upon to deal with these issues, in the remaining countries, they have rendered decisions where the issue of liability arising out of irregular or misleading certification was in question.

An Audit Report is issued for the purpose of being relied upon by third parties. Thus, in case of accounting irregularities and a false audit opinion (in the absence of misappropriation),

third parties are more likely to suffer damages than the audited company and, as a result, liability actions against statutory auditors are more often brought by them.

Typical scenarios are as follows:

- a company purchases shares of another company or subscribes to an increase in the capital of another company: Courts have actually granted damages to investors in Finland⁴⁷, France⁴⁸, Sweden⁴⁹, and the United Kingdom⁵⁰; a similar case occurred in the Netherlands⁵¹;
- a bank grants a loan to the audited company: such a case has led to Court decisions in France⁵² and in Sweden⁵³;
- a supplier contracts with the audited company : the auditor has been held liable towards the creditor in Belgium⁵⁴ and in Denmark⁵⁵;
- the bankruptcy proceedings reveals the inappropriate opinion of the auditor on the financial statements of the bankrupted company and the Court holds the statutory auditor liable towards the creditors of the company: Court decisions have found the auditor liable towards the bankruptcy estate in Denmark⁵⁶, in France⁵⁷ and in Italy⁵⁸.

In these scenarios, the above mentioned parties allege to have relied on the certified accounts in making their decisions. They claim to have suffered damages as a result of the statutory auditors' fault or negligence in certifying the company's financial statements, which led them to make a decision (to acquire shares, to grant a loan, to supply goods...) that they would not have made if the financial statements had not been certified.

In addition, the company itself may suffer a damage as a result of a statutory auditor's fault. Such claims have been settled in France, Germany and Italy. In France, the Court recognised the existence of a damage on the ground of a lost opportunity of reducing tax payment⁵⁹. In Germany, if a statutory auditor breaches one of his duties, for example by signing an irregular or misleading certification of accounts, thus giving an inaccurate image of the company or certification of information tendered to shareholders, this can lead to liability for the damages sustained by the company itself⁶⁰. In Italy, Courts have developed the conditions of the statutory auditors' liability during the first phase of their mission, related to the compliance with the legal and fiscal rules⁶¹, and have held an auditor liable because he did not take into account the particular situation of the audited company⁶².

c) Non Disclosure

Questionnaire reference:

Non-disclosure of fraud or of infringements of Company Law to directors, shareholders, public officers or competent authorities. (Question 3.1.2.2)

The Commission's Green Paper made reference to a survey conducted in the United Kingdom which showed that 75% of the persons surveyed believe that it is the statutory auditor's duty to detect all types of fraud. The same survey found that 61% of the general public thinks that it is the responsibility of the auditor to actively search for fraud. As a speaker at the 1996 Conference pointed out, « *the so-called 'expectation gap' is at its greatest in the area of fraud. . . . The public rightly demands that we should do more in this area. But greater responsibility would bring even greater risk. The prevention and detection of collusive fraud, often involving people in the most senior positions of trust, is a major challenge.*»⁶³

A fraud, for example a misappropriation, may lead to inaccuracies in annual accounts and to a false audit opinion. The damages caused by such false audit opinion are the same as described under §1.3.2 b). Dutch Court has judged that the financial statements must properly reflect the impact of such fraudulent action⁶⁴. Here, the liability of the auditor depends on the impact of the fraud on the financial statements and of the subsequent opinion of the auditor on the accounts.

There may be additional damages, principally to the audited company, if the statutory auditor does not timely disclose the fraud. However, this is a different issue, not related to the audit opinion as such.

COUNTRY	Does non-disclosure of fraud lead to liability?	Court Decisions
Aus	Yes	No
Bel	Yes	Yes
Den	Yes	No
Fin	Yes	Yes
Fra	Yes	Yes
Ger	Yes	No
Gre	Yes	No
Ire	Yes	No
Ita	Yes	Yes
Lux	Yes	No
Ned	Yes	Yes
Por	Yes	No
Spa	Yes	No
Swe	Yes	No
UK	Yes	Yes

In all the Member States, non-disclosure of fraud or of infringements of company law is a ground for liability if the statutory auditor's actions meet the various elements for a finding of liability.

In many of the Member States, the Courts have yet to be called upon to deal with this particular issue. There is, however, case law coming out from the United Kingdom showing the common law approach and out of Finland, France and Italy as examples of civil law treatment of the issues in question.

These cases help defining the statutory auditors' duties regarding the disclosure of fraud.

The available case law points out two types of cases:

- the auditor is liable if his negligent conduct prevented him from detecting the fraud:
 - because he wrongfully relied on the declarations or work of the accountants (France⁶⁵);

- more generally, because of an insufficient work, where in the absence of negligence, he might have prevented the fraud, whoever committed the fraudulent act (Finland⁶⁶, France⁶⁷, United Kingdom⁶⁸, Italy⁶⁹);
- the auditor is liable if he detected the fraud but did not disclose it, and if non-disclosure caused a damage (Finland⁷⁰, United Kingdom⁷¹).

In all cases, the statutory auditor is ordered to pay damages to the company if his negligent failure to disclose the fraud contributed to the continuation of such fraud and the resulting losses. Liability requires a showing that if the statutory auditor had met his duty of care, the company could have avoided at least part of the damage.

d) Breach of Other Duties

Questionnaire references:

- *Non-disclosure, late disclosure of events compromising the solvency, premature disclosure or erroneous disclosure. (Question 3.1.2.3)*
- *Breaches relating to other duties (Question 3.1.2.4)*

A first question that may be considered is whether the statutory audit should be regarded as a guarantee of the financial soundness of the audited company. The Commission's Green Paper pointed out that the role of the statutory auditor in this respect is vital and that he must be alert to factors which would affect the going concern basis of the audited company. On the other hand, the Commission indicated that « *auditors need to be cautious in the way they report publicly any concerns that they may have* » which raises the question of the statutory auditor's liability for premature or unjustified disclosure of events compromising the going concern basis.

In addition to duties arising out of certification of the accounts and compliance with company law, the statutory auditor, in many cases, has obligations relating to corporate governance of the audited company. These obligations deal with the disclosure of events such as contracts between the company and interested parties, modification of the corporate structure and the duty of confidentiality.

	Aus	Bel	Den	Fin	Fra	Ger	Gre	Ire	Ita	Lux	Ned	Por	Spa	Swe	UK
Non disclosure, late disclosure of events compromising solvency, premature disclosure or erroneous disclosure	Yes	Yes	Yes	Yes	Yes ⁱ	Yes	Yes / NC ⁱⁱ	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Reporting on contracts between the company and its officers or between two companies having common directors	NC	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	No ⁱⁱⁱ	Yes	Yes	Yes ^{iv}	Yes ^v
Modifications in the company's articles of organisation	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes	No	Yes	Yes	Yes	No	Yes
Increase or decrease of capital, modification of the legal entity, mergers, etc.	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes	Yes	No	Yes	Yes	Yes	Yes
Interference with the management	Yes	Yes ^{vi}	Yes	Yes	Yes	Yes	Yes	Yes	Yes	NC	NA ^{vii}	Yes	Yes	No	Yes
Absence of notification of Shareholder's meeting in the case of directors' deficiency, etc.	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes	No	No	NC	Yes	No	Yes
Breach of confidentiality	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

ⁱ This type of action would have its legal basis in the “*procédure d’alerte*” set forth in Article 230-1 of the law of 24 July 1966 introduced by the law of 1 March 1984⁷².

ⁱⁱ The liability of the statutory auditor in case of premature disclosure has not been stated in Greece, but he is liable in case of non- or late disclosure.

ⁱⁱⁱ Under Dutch law there is in general no duty to disclose the existence of agreements between the company and its directors or between two companies having common directors. An exception thereto concerns the aggregate of remuneration for the board of directors of a listed company which should be reflected in the annual accounts according to regulations of the Amsterdam Stock Exchange.

^{iv} In Sweden, such an obligation exists only if the two companies are a parent and subsidiary.

^v If the statutory auditor agreed to carry out these duties.

^{vi} The Belgian rule is that the statutory auditor may not substitute himself for the management of the company. «*A clear distinction must be made between the responsibility of the directors who participate in the management of the company and that of a statutory auditor whose tasks are completely different: the statutory auditor has only a mission of verification and no managerial competence.*» (Comm. Bruges, 13 February 1984, R.P.S. 1984, p. 198).

^{vii} This issue is not applicable in the Netherlands.

In general, breaches of the duties listed above may lead to liability in all the Member States. This is especially true with regard to disclosure of events compromising solvency and to breaches of confidentiality.

Regarding other duties, all the Member States recognise these obligations to the statutory auditors, except four countries where some of them do not exist: Ireland, Luxembourg, the Netherlands and Sweden.

There are several Court decisions dealing with the application of these rules, mostly in France on the following fact settings:

- non disclosure of events compromising solvency⁷³;
- erroneous disclosure of events leading to insolvency⁷⁴;
- disclosure of contracts between the company and interested shareholders or officers⁷⁵;
- interference with the management of the audited company⁷⁶;
- report concerning an increase in capital⁷⁷.

1.4 Fault, Remedies and Causation

As general rules of civil liability are applicable in case of negligence or wrongful acts, it is necessary to review them as regards specific issues involving statutory auditors. These issues have been structured according to the traditional approach to liability, considering, in turn, fault (1.4.1), damage (1.4.2), and causation (1.4.3).

1.4.1 Fault

This section will begin with a definition of the statutory auditor's fault, with regard to its different degrees and to the question of vicarious liability (*respondiat superior*) for the actions of the statutory auditor's employees or agents (a). The proof of fault will be discussed in view of the standards that are used in considering the statutory auditor's conduct and the question of confidentiality during the lawsuit (b). Finally, absence of fault as a defence will be discussed (c).

SUMMARY : FAULT

The statutory auditor may be liable if his negligence or intentional conduct caused a damage.

He may also be liable for faults committed by:

- his employees and associates (in every Member State);
- experts he appointed (except in the United Kingdom);
- the audited company's officers (not for their fault in itself, but possibly for having not detected such fault).

The negligence giving rise to the statutory auditor's liability needs to be defined by reference to a model. The conduct of the auditor in the completion of his mission is appreciated by comparison with a standard. All the Member States apply an objective standard based on the conduct expected from an average prudent and diligent auditor, a reasonably competent member of his profession.

Such standard is defined by Courts as well as professional regulatory bodies, though their rules do not bind Courts unless they have been adopted by law. According to available case law, Courts in Belgium, France, Italy, Ireland and UK, have adapted the standard to the circumstances of fact.

To prove that his behaviour was in accordance with such standard, an auditor may disregard his duty of confidentiality in all the Member States, except in Greece and Denmark. In Portugal, the Court's agreement to such a disclosure is necessary. Similarly, a statutory auditor is not allowed to raise a privilege in order to prevent the introduction of evidence, except in Portugal where the Court only may permit the disclosure.

If the auditor proves that he committed no fault as regard to these criteria, he cannot be held liable.

a) Definition

Questionnaire references:

- *What is the level of breach giving rise to liability? (Question 2.1.1)*
- *Does the statutory auditor's faults have to be personal or is he liable for the faults of his associates or of any experts that he called upon? Can the statutory auditor be held liable for the faults of the officers of the audited company? (Question 2.1.2)*

In every Member State, the statutory auditor is liable for his intentional conduct as well as in case of negligence in any degree. As a result, even a slight negligence in the performance of his duties may lead to liability.

In addition, the auditor is liable for the actions of his employees and associates. Even if they may be personally liable in tort, the auditor is liable under the principle of the employer's liability for the faults of his employees in the course of their employment.

With respect to experts and consultants, the analysis of the situation in the Member States shows that there are three distinct groups:

- countries where the auditor is strictly liable for the experts he called upon (Aus, Bel, Den, Fra, Gre, Ita, Lux, Ned, Por, Spa); in the Netherlands such liability can be excluded by contract;
- countries where the auditor's own liability is for fault only; the auditor can show, for example, that he was not negligent in selecting the expert (Fin, Ger, Ire, Swe);
- a single country where there is no liability for the actions of experts (UK).

Finally, in all the Member States, a statutory auditor is not liable for faults committed by the officers of the audited company, but he may be liable for a distinct fault consisting of not detecting the irregularity or fault committed by the management that his auditing work should have allowed him to detect.

b) Proof

Two very different questions arise with respect to proving fault. The first issue relates to the determination of the standard of fault; the second one to the way adversarial Court proceedings may carry out with respect due to confidentiality.

Questionnaire reference:

Standard for determining fault or negligence: do the Courts use a subjective test or an objective, "reasonable person" standard? Is any consideration given to the level of knowledge and skill of an ordinary member of the profession? How is this level of knowledge and skill defined (auditing standards, case law, etc.)? (Question 2.1.4)

As previously exposed, the statutory auditor's breach of a duty of care is the necessary and sufficient condition to his fault in the exercise of his mission. As any negligence in the completion of his duty of care may lead to liability, it is necessary to determine such duty of care and to what extent it differs from a Member State to another.

As a general rule, statutory auditors are not required to check all the corporate transactions, but to audit the financial statements using a risk approach in order to form their opinion regarding the substantial – or material – inaccuracies that could hinder the “true and fair view” qualification of the financial statements. The question of the required competence of a statutory auditor is also of high importance considering that the auditor is a professional of accounting, and not a professional of every audited company’s activity.

As a result, there is a substantial part of judgement in the choice of the audit tests as well as in his opinion. Providing guidelines for the statutory auditor’s conduct therefore allows determining the scope of his duties and consequently the scope of his breach of duty.

Subject to the slight differences noted below, in all the Member States, the standard applied to determine fault or negligence is primarily an objective “reasonable person” standard. The test is whether the statutory auditor has exercised the care and skill reasonably to be expected of a normally diligent and prudent statutory auditor.

A general description of this objective standard may be as follows: he is an ordinary member of the profession, an average, prudent and diligent auditor, who follows good auditing practices as any reasonable person would, and who has the professional skills and knowledge that allow him to be referred to as a reasonably competent member of his profession.

In some Member States, this model may be adapted to circumstances of fact:

- in Belgium and in France, the standard depends on the situation in which the auditor was placed, meaning that one must consider an ordinarily diligent man placed in the same circumstances⁷⁸;
- in Italy, a Court decided that the duty of care of the auditor varies in relation to the particular situation that he has to take into account, and the auditor must be more diligent where there is clear “evidence of risks”⁷⁹.

In addition to this objective standard, some Member States may refer to subjective elements:

- in Belgium: the level of diligence changes, based on the qualifications of the auditor;
- in the Netherlands: the reasonable standard includes subjective elements regarding the party which gave the assignments at stake, and the elements of the specific assignments;
- in Spain: subjective tests, such as the degree of sophistication or the fees of the auditor, may be used;
- in Sweden, such subjective elements would not help to determine the fault, but may have some importance on the amount of damages to be awarded.

The behaviour of this “normally diligent and prudent auditor” may in some respect be defined by standards issued by professional regulatory bodies. While these standards are never binding on the Courts, they often refer to them.

In addition, in Belgium, professional rules bind Courts as some rules of the Institut de Réviseurs d’Entreprises have been implemented by statute. Likewise, in Spain, the Technical Rules on Audit are legal rules that the judge is obliged to follow and reference to other professional standards is made only where legal rules and contractual requirements are not sufficient.

In common law countries, Courts have significantly contributed to the definition of the standard, together with the professional bodies for statutory auditors:

- in Ireland, Justice O’Flaherty of the Irish Supreme Court stated that the auditors’ duty entails « *bringing reasonable skill and competence to their task. But they are not required to act as super-humans; nor are they to be faulted simply because an expert witness is produced who says that, if he had been in charge of things, affairs might have been ordered better* »⁸⁰;
- in the United Kingdom, if the auditor can show that he acted in accordance with a practice or opinion shared by a substantial body within the profession, a Court will usually find that the required standard has been satisfied, although it is still possible for the Court to conclude that the practice or opinion is unreasonable.

Questionnaire references:

Proof of fault or negligence: can the statutory auditor produce confidential documents in his defence in a liability action? Conversely, can the statutory auditor invoke a privilege in order to prevent the introduction of evidence related to his work? (Questions 2.1.5.1 – 2.1.5.2)

In every Member State, the statutory auditor is bound by a duty not to disclose confidential information which he learned during the completion of his mission. This duty can come into conflict with the Court’s role of considering the facts surrounding a matter in dispute.

The chart below shows distortions between the various Member States .

COUNTRY	Can the statutory auditor produce confidential documents in his own defence?	Can the statutory auditor invoke a privilege in order to prevent the introduction of evidence?
Aus	Yes	No
Bel	Yes	No
Den	No	No ⁱ
Fin	Yes ⁱⁱ	No
Fra	Yes	No
Ger	Yes ⁱⁱⁱ	No
Gre	No	No
Ire	Yes	No
Ita	Yes	No
Lux	Yes	No
Ned	Yes	No
Por	Yes ^{iv}	Yes ^v
Spa	Yes ^{iv}	No
Swe	Yes	No
UK	Yes	No

ⁱ Auditors have no automatic professional privilege and are under a duty to give evidence in Court. However, according to section 170 (3) of the Rules of the Legal Procedure Act, the Court can decide that auditors are granted a privilege regarding “secrets of essential importance”.

ⁱⁱ However, in some cases such information could be declared confidential by the Court.

ⁱⁱⁱ Although no legal rule expressly states that the statutory auditor can produce confidential documents in his defence in a liability action, he would probably be allowed to breach his duty of confidentiality to protect his own interest (WP Handbuch 1996).

^{iv} With the Court’s permission.

^v But the Court can order the disclosure of the facts and documents subject to professional privilege, whenever and within the limits it believes the breach of the professional privilege is justified, based on the interest at stake and on the principles of the law.

In a first group of countries, which represents the majority approach, a statutory auditor can introduce any document which is necessary for his defence; however, he cannot invoke his professional privilege in order to prevent the disclosure of evidence which would tend to show his own negligence (Aus, Bel, Fin, Fra, Ger, Ire, Ita, Lux, Ned, Spa, Swe, UK)

In Greece and Denmark, the statutory auditor cannot produce confidential documents in his own defence but he can be forced to do so by Court order.

c) Absence of Fault

Questionnaire reference:

Is the absence of fault a defence? (Question 3.2.2)

COUNTRY	Is absence of fault a defence?	Court decisions
Aus	Yes	No
Bel	Yes	No
Den	Yes	Yes
Fin	Yes	No
Fra	Yes	Yes
Ger	Yes	No
Gre	Yes	No
Ire	Yes	No
Ita	Yes	No
Lux	Yes	No
Ned	Yes	No
Por	Yes	No
Spa	Yes	No
Swe	Yes	No
UK	Yes	No

Fault is one of the elements of the cause of action against the auditor. As a result, the auditor may defend by showing the absence of fault, which usually requires showing that he acted in accordance with auditing standards or meeting some form of objective test of compliance with his duty of care (See *supra* 1.4.1 b).

These issues have been the subject of Court decisions in Denmark and France:

- Danish Courts have ruled in favour statutory auditors on at least two occasions based on an absence of fault⁸¹;
- in France, it appears from numerous Court decisions that the statutory auditor's fault is required to be inferred from circumstantial evidence. The absence of such fault may be deducted from a comparison between the standard of the "normally prudent and diligent auditor" and his actual behaviour⁸².

1.4.2 Remedies

The fault of the statutory auditor gives rise to injuries which are not just economic in nature. For this reason, it is important to explore the types of injuries which may result from the statutory auditor's negligence as well as the remedies available to injured parties.

This section begins with a description of the remedies that are available to injured parties (a).

The focus will then shift to manner in which damages are evaluated (b), taking into account such issues as the "loss of chance".

SUMMARY: REMEDIES

When successful, the result of the liability action is mainly the award of damages, but Courts may also order the termination of the contract in Austria, Belgium, France, Germany, Luxembourg, the Netherlands, Portugal, Spain and Italy (Board of Auditors).

Non material damages are in theory recoverable in Belgium, Finland, France, Greece, Ireland, Luxembourg, the Netherlands, Portugal, Spain, and the United Kingdom, but in practice, as a general rule, they do not exist in the field of the statutory auditor's liability.

While Courts enjoy a wide discretion regarding damages to be awarded, there seems to be some general trends as follows:

- Indirect injuries (such as the decrease of the value of stock): in Belgium, Denmark, Finland, Germany, Greece, Ireland, Luxembourg, the Netherlands, Portugal, Spain and the United Kingdom, a shareholder may be compensated for the decrease of the value of his stock, provided that he shows that his damage is due to the statutory auditor's breach of duty. The remaining Member States (Aus, Fra, Ita, and Swe) consider that such damage is suffered primarily by the company, unless the shareholder shows that his investment was based on the statutory auditor's report on the financial statements.
- Future injuries: Courts of some Member States (Fin, Gre, Ita, Spa) do not grant compensation. But if foreseeable (Fra, Ire, Ned, Por, UK) or ascertained (Aus, Bel, Den, Ger, Lux, Swe), the future damage caused by a statutory auditor's breach of duty may be recoverable. There are two methods for the calculation of damages: either the assessment is postponed until the losses have actually occurred (Aus, Ger, exceptionally UK), or it is based on the current value of the future losses (other Member States who grant future injuries' compensation).
- Court costs: they are borne by the losing party as a general rule. In all Member States except in Belgium and Luxembourg, the losing party also may have to contribute to some extent to the winning party's legal fees, but in practice, the amount awarded is determined by the Court, at a sometimes significantly lower level than the actual costs incurred, except in Austria.

In all the Member States, damages are awarded so as to place the victim in the same situation he would have been in if the breach had not taken place. The victim's situation is considered at various times, depending on the Member State: at the time of the last steps of the lawsuit, usually judgement (Aus, Bel, Den, Fra, Ger, Gre, Lux, Por, Spa, Swe, UK), at the time of the occurrence of the damage (Fin, Ire, Ita, Ned) or at the time of the breach of contract (Ire). In France, Belgium and the United Kingdom, Courts use the concept of "loss of chance" to allow compensation when the statutory auditor's fault contributed only in part to the injury; damages are decreased on a prorata basis of the probability that the injury would not have occurred had the statutory auditor committed no fault.

a) Types of Remedies

- *Questionnaire reference:*

Describe the possible results of the liability action. Is it possible to obtain the termination of the statutory auditor's duties, receive an award of damages or any other result? (Question 2.2.1)

While the principal purpose of a liability action is, by definition, the recovery of damages, there may be other remedies available, including termination of the contract.

COUNTRY	Termination	Damages
Aus	Yes	Yes
Bel	Yes	Yes
Den	No	Yes
Fin	No	Yes
Fra	Yes	Yes
Ger	Yes	Yes
Gre	No	Yes
Ire	No	Yes
Ita	Yes	Yes
Lux	Yes	Yes
Ned	Yes	Yes
Por	Yes	Yes
Spa	Yes	Yes
Swe	No	Yes
UK	No	Yes

In a majority of countries (Aus, Bel, Fra, Ger, Lux, Ned, Por, Spa, Ita (Board of Auditors)), the audited company may also seek termination of the mission.

In several countries (Fin, Den, Gre, Ire, Swe, UK, Ita (Auditing Firm)), Court action is not necessary in order to terminate the mission of the statutory auditor, as a decision of the audited company's managers or shareholders is sufficient. In the Netherlands, it is also possible for the representatives of the company to terminate the employment but, in such a case, a Court may find the termination unlawful.

Various cases give rise to the award of damages. The table hereafter presents the types of compensation which may be awarded.

COUNTRY	Non-material damages	Decrease in the value of the stock	Future injury	Court Costs	Attorney's fees
Aus	No	No	Yes	Yes	Yes
Bel	Yes	Yes	Yes	Yes	No
Den	No	Yes	Yes	Yes	Yes
Fin	Yes	Yes	No	Yes	Yes
Fra	Yes	No	Yes	Yes	Yes
Ger	No	No	Yes	Yes	Yes
Gre	Yes	Yes	No	Yes	Yes
Ire	Yes	Yes	Yes	Yes	Yes
Ita	No	No	No	Yes	Yes
Lux	Yes	Yes	Yes	Yes	No
Ned	Yes	Yes	Yes	Yes	Yes
Por	Yes	Yes	Yes	Yes	Yes
Spa	Yes	Yes	No	Yes	Yes
Swe	No	No	Yes	Yes	Yes
UK	Yes	Yes	Yes	Yes	Yes

- *Questionnaire reference:*

Are non-material damages recoverable? (Question 2.2.4)

Other than financial or pure economic damages may sometimes be awarded.

In a majority of Member States (Bel, Fin, Fra, Gre, Ire, Lux, Ned, Por, Spa, UK), the possibility of recovering damages for non-material injury exists, but so far remains purely theoretical in the area of liability of statutory auditors. One example would be if the statutory auditor reported non-existing irregularities to the shareholders, thus injuring the reputation of the officers or the company itself.

In Austria, Denmark, Germany, Italy and Sweden, non-material damages are not recoverable.

Thus, the most common case is that Courts only compensate economic losses.

- *Questionnaire reference:*

Can a plaintiff who suffered indirect injury recover damages, for example a decrease in the value of the stock? (Question 2.2.3)

Where the statutory auditor's fault or negligence caused a damage suffered directly by the audited company, which generated a loss for shareholders, e.g. a decrease of the value of their stock, they also may sometimes recover.

In several Member States (Bel, Den, Fin, Gre, Ire, Lux, Ned, Por, Spa, UK) the shareholder may base his claim on the decrease in value of the shares or derivatives due to a statutory auditor's breach. In Ireland and the United Kingdom, it is necessary for the plaintiff to show that circumstances give rise to a legal duty on the part of the auditor to take all reasonable

skill and care to prevent the plaintiff from sustaining that type of loss. In the Netherlands and Spain, no such indirect injury can be recovered in principle, but the injury suffered by a shareholder whose stock lost value may be deemed a direct consequence of a breach of the statutory auditor's duty.

In the remaining Member States, when a shareholder seeks recovery for a decrease in the value of the stock or derivatives, Courts consider that the decrease is only a consequence of the company's injury and that only the company has standing to bring an action. This principle was applied in France⁸³ and in Italy⁸⁴. In Austria and in Germany, where no case law subject to the recovery of a decrease in the value of the stock was found, the shareholder cannot, in principle, recover such an indirect damage, except if he can argue that the requirements for a contract with protective effects in favour of third parties are fulfilled (see *supra* p. 25).

However, in this second group of countries, the solution differs if a plaintiff based the decision to purchase shares on the basis of the certified accounts provided by the statutory auditor and later learned that the actual situation of the company was different from what then appeared. In such a situation, the shareholder may successfully bring an action for the damages he personally suffered, arguing that had he been better informed, he would not have bought the shares or would have bought them at a lower price. As a result, in Sweden⁸⁵, in France⁸⁶ and in Italy⁸⁷, Courts awarded damages to investors who purchased shares in a company on the basis of inaccurate accounts certified by the statutory auditor.

- *Questionnaire reference:*

Can future injury give rise to recovery and under what circumstances? (Question 2.2.5)

Courts often have to rule at a time when the statutory auditor's fault has already arisen and an injury to the defendant has occurred but cannot be evaluated at the time their compensation is sought because all the consequences have not occurred yet.

Some Member States allow recovery for future damages, although the rules applicable are expressed in slightly different ways, regarding specifically the assessment of the future losses to be recovered and their calculation.

The level of certainty of the future losses required in order that they be recovered slightly differs from a Member State to another. In France, Ireland, the Netherlands, Portugal and United Kingdom, the injury may give rise to recovery if foreseeable, meaning that it should naturally flow from the statutory auditor's breach of contract or violation of duty. In Austria, Belgium, Denmark, Germany, Luxembourg and Sweden, such damages may be awarded, provided that they may be ascertained, sometimes even calculated at an exact figure (Den, Swe).

Concerning the calculation of future damages, in Austria and Germany, Courts initially rule on liability (in Austria, the Court issues a "declaratory judgement"), and the compensation is fixed later on. This possibility to postpone the assessment of damages exists also in the United Kingdom, but it is exceptional. The other Member States evaluate the present value of the future damages.

In Finland, Greece, Italy and Spain, there is no recovery of future losses.

- *Questionnaire reference:*

In case of judgement against the statutory auditor, which party bears Court costs and legal fees? (Question 2.2.9)

In all Member States, the losing party is ordered to pay the Court costs associated with the litigation.

With respect to legal fees, including attorney's fees as well as cost involved in securing expert testimony, the rule, in all countries except Belgium and Luxembourg, is that the losing party may have to contribute to some extent to the fees of the winning party. In some countries, Courts set the attorney's fees based on a fee scale (Aus, Ger, Ned, Por, Spa). In other countries, the Courts decide what the reasonable level of fees should be (Den, Fin, Gre, Ita, Swe, UK).

In France, the general rule is that the Court, taking into account equity and the economic situation of the losing party, may decide whether or not each party will bear its own costs.

In all the above Member States, as a general rule, whatever award made is significantly lower than the actual costs incurred, except in Austria where full fees are usually recovered.

In Belgium and Luxembourg, each party bears its lawyer's fees.

b) Assessment of Damages

Questionnaire reference:

How are damages calculated? Is the goal of the recovery to make the plaintiff whole? From what moment are the damages calculated? (Question 2.2.8)

In all the Member States, the compensation awarded must place the victim in the situation he would have been in if the breach did not take place. Thus, Courts set the damages on the basis of their injury as it existed at a given point in time, which point should be determined in order that the award may cover any possible modification of the injury.

COUNTRY	Time when injury is considered
Aus	Closing of the oral arguments at the first instance level
Bel	Judgement
Den	Judgement
Fin	Occurrence of the damages ⁱ
Fra	Judgement
Ger	Last Court hearing
Gre	Filing of the lawsuit
Ire	Breach of contract or occurrence of injury to the plaintiff
Ita	Occurrence of the damages ⁱⁱ
Lux	Judgement
Ned	Occurrence of the damages
Por	Judgement
Spa	Judgement
Swe	Thirty days after presentation of claim
UK	Judgement
ⁱ However, if the amount of damages is decreased or increased and sufficient causal links exist, in the latter case, damages are taken into account as from the date of the Court's decision.	
ⁱⁱ However, the quantification takes into account any monetary devaluation which occurred from the time of the injury until the Court decision.	

Questionnaire reference:

Can the plaintiff recover for a lost opportunity and under what circumstances? (Question 2.2.6)

The concept of “loss of chance” provides a formula to calculate damages when the existence of a causal link between fault and damages is not fully established, i.e. in circumstances where it is uncertain whether a loss would have been suffered if there had been no fault. As a consequence, the amount of damages is based on the likelihood that the lost chance would have come about.

This concept differs from the “lost profits”, that are frustrated economic gains. Such a *negative* damage caused by the statutory auditor’s negligence may have to be compensated to the same extent as a loss.

At least three Member States refer to the theory of “loss of chance” when assessing damages:

- French Courts hold that, inter alia, in case of diversion of funds, the statutory auditor is not liable for the entire amount of diverted funds. Courts consider that the statutory auditor’s fault only deprived the company of a chance to discover the misappropriation and put an end to it, because even if the statutory auditor had completed his mission with the required prudence and diligence, the fraud might not have been discovered⁸⁸. The lost opportunity must be real and serious. For example, if the bankruptcy of the company could not have been avoided even in the absence of breach by the statutory auditor, then no compensation is due. In practice, the amount of compensation is that of the entire damages multiplied by the probability that the negligence caused the injury. For example, if the probability that the plaintiff would not have purchased the stock if he had been better informed is 1:2, then damages will equal 50% of the loss suffered by the plaintiff.

- In United Kingdom, a distinction is drawn between cases in which the uncertainty relates to what the plaintiff would have done himself in the hypothetical situation and cases in which it relates to what an independent third party would have done. In the former category of cases – e.g. where the plaintiff alleges that, if the auditor had discovered a fraud, the plaintiff would have taken steps which would have prevented further misappropriations – the plaintiff must prove on a balance of probability that he would have acted as he claims, and if this test is satisfied, the plaintiff will recover the whole of the losses that would (probably) have been avoided. Where, however, the relevant acts are those of a third party – e.g. where the plaintiff alleges that, if the auditor had reported as he should have done, a third party would have taken steps which would have prevented further misappropriations – the position is different. In such a case, provided it is shown that there was a “substantial” and not merely “speculative” chance that the third party would have acted as alleged, the Court will award damages based on the lost chance. Such damages are calculated by applying a percentage chance to the total loss in fact suffered.
- In Belgium, the Courts have already used the concept⁸⁹.

In the Netherlands and in Portugal, some authors are favourable to recovery under the theory of the loss of chance, but it has not been recognised yet by law nor by the Courts. In Ireland, Courts have never been called upon to determine this issue, therefore their position may be to adopt this concept.

In the other Member States (Aus, Den, Fin, Ger, Gre, Ita, Lux, Spa, Swe), the requirement of actual and certain causation remains a hindrance of the concept of “loss of chance” as described hereabove.

1.4.3 Causation

The causal link is one of the fundamental requirements of civil liability in all the Member States' legal systems.

This study presents the different theories used by the Member States to determine its existence (a), and the possibility for the defendant to invoke the third party's or the plaintiff's fault as a defence (b).

SUMMARY: CAUSATION

The causal link is one of the fundamental conditions of civil liability in all the Member States' legal systems. Various tests have been elaborated to determine whether the link between the damage and the statutory auditor's breach exists or not. The Member States have adopted one or several of these methods.

In some Member States, it is sufficient to show that damages would not have arisen, absent the statutory auditor's breach: this "sine qua non" condition generally applies in France as well as in Spain, but only with respect to events of wilful misconduct, and in Luxembourg and Belgium in case of claims brought in tort or where there is an intentional wrongdoing.

In addition to the above condition, most of the Member States require that the damage was foreseeable in the normal course of events. Irrespective of slight differences, this "adequate condition" theory is applied in Austria, Denmark, Finland, Germany, Italy, the Netherlands, Portugal, Sweden; in Luxembourg and Belgium in case of contractual liability except when there is an intentional wrongdoing, and in Spain except in case of wilful misconduct.

Some countries (Gre, Aus, Por) consider the causal link through the theory of the "purpose of the law": the statutory auditor is only liable for the damages suffered that the duty of care violated by him is intended to protect. Austria and Portugal use both this criteria and the "adequate causation" test, depending on the circumstances.

UK and Ireland have not adopted any specific test for causation, describing the issue as "a matter of common sense". Depending upon the circumstances of fact, Courts have used the foreseeability criteria in different ways.

The plaintiff's or a third party's fault may weaken the causal link between the damage and the statutory auditor's breach, and consequently may exempt the auditor from liability or reduce it. The plaintiff's fault can be a successful defence for the statutory auditor in all the Member States, except in Austria when the plaintiff is the audited company. In case of multiple defendants, liability is "joint and several", except in some cases in Portugal. This "pro-plaintiff" approach means that full compensation may be sought from any of a number of the liable parties, the paying party seeking contribution from the co-defendants. The appreciation of the causal potency of each of the faults is useful in the determination of the sharing of compensation.

a) Various Tests for Causation

Questionnaire references:

- *What type of causal link must be established? (Question 2.3)*
- *Are damages recoverable only to the extent they were foreseeable by the statutory auditor? (Question 2.2.7)*

Many theories have been elaborated to provide criteria to resolve the issue of causation, the main of which are:

- The theory generally known as that of a “sine qua non condition”, or “but for condition”, requires only a showing that, but for the breach of contract or tort, the claimant would not have suffered the loss. Causation exists if the damage would not have occurred, had the fault or negligence not been committed. When the damage was allegedly caused by an act, the test is whether there would be no such damage if the specific act did not happen. In case the damage was allegedly caused by an omission, the test is whether the damage would have arisen if the defendant had acted in accordance with his duties. The fault or negligence need not be the exclusive cause of the damage, but only its necessary cause.
- The theory of “adequate causation” or “foreseeability”: damages cannot be recovered unless they were reasonably foreseeable. Where the chain of causation is so long or tenuous that the losses were not reasonably foreseeable, the losses are described as too “remote” to be recoverable. The act committed, in addition to having materially caused the damage in question, must be capable of causing this type of damage when considered irrespective of the surrounding circumstances. Damages, which are unforeseeable according to normal experience, are not recoverable.
- The theory of the purpose of the law (*Normzwecklehre*): the statutory auditor is only liable for damages suffered that the duty of care he breached is intended to protect. One must consider the purpose of the rule which provides for the liability, the scope of protection afforded by such rule and whether the harmed interest falls within the scope of protection or not.

The Member States apply one or several of these tests for causation.

In France⁹⁰, the fault or negligence needs only to be the necessary cause of the damage (sine qua non condition). In some Member States, this condition is also sufficient in specific cases. In Luxembourg and in Belgium, it is sufficient in case of claims brought in tort or when there is an intentional wrongdoing. In Spain, in events of wilful misconduct, the auditor shall be liable for all the damages which are known to be a consequence of its breach, whether or not foreseen or foreseeable.

The foreseeability or adequate causation test is the most commonly used by the Member States’ Courts, but it may be used in slightly different terms:

- in Denmark, Finland⁹¹, Germany, the Netherlands, Sweden⁹², the auditor is only liable to compensate the foreseeable part of the damage; if the loss is so unusual that nobody could foresee the damage in the ordinary course of events, then there is no liability;

- in Luxembourg and Belgium, the solution is the same in case of contractual liability except where there is an intentional wrongdoing;
- in Italy, causation exists when, according to common experience, the damage appears to be the direct and immediate consequence of the fault or negligence⁹³;
- in Spain, the statutory auditor is only liable for the damages he could have foreseen, except in case of wilful misconduct;
- Austria and Portugal apply either this test or the theory of the purpose of the law.

In Greece, the theory of the purpose of the law is currently predominant.

In the United Kingdom and Ireland, Courts have avoided the adoption of a single test for causation, preferring to deal with the matter as a question of judicial “*common sense*” at the Court’s discretion. In Ireland, it is necessary, but probably not sufficient, for the plaintiff to establish “but for” causation. In England, firstly, damages cannot be recovered unless they were reasonably foreseeable by the statutory auditor. If not, the losses are described as “too remote” to be recoverable. Secondly, not all losses are recoverable, even if the “but for” causation test is met and the damages were foreseeable⁹⁴. Finally, there is a further refinement in cases where the victim is not the company but a third party who has relied on a negligent audit report in circumstances where the statutory auditor owed him a duty of care in tort⁹⁵.

b) Faults of Third Parties or of the Plaintiff

Questionnaire references:

- *Does the fault of a third party or of the audited company provide a defence? (Question 3.2.4)*
- *Is liability apportioned between the other liable party and the statutory auditor in accordance with the seriousness of their fault and/or their contribution to the damage? Are they jointly and severally liable and, if so, is there the possibility of contribution? (Question 3.2.5)*

The fact that the statutory auditor proceeds by random surveys when certifying the accounts of a company and uses the company’s accounting documents leaves significant room for inaccuracies having their origins in the actions of the company and third parties not being identified by the statutory auditor. Such acts or omissions committed by companies or third parties may make it more difficult for the plaintiff to prove causation as required.

The extent to which the third party’s or the victim’s behaviour provide the statutory auditor with a defence in a liability action should therefore be considered.

In addition, one must determine whether, in case of faults or negligence of a third party, the resulting liability is joint and several or proportional to each defendant’s degree of fault.

- Plaintiff's own fault

COUNTRY	Fault of the plaintiff as a defence	Court Decisions
Aus	Yes ¹	No
Bel	Yes	No
Den	Yes	No
Fin	Yes	Yes
Fra	Yes	Yes
Ger	Yes	No
Gre	Yes	No
Ire	Yes	Yes
Ita	Yes	No
Lux	Yes	No
Ned	Yes	No
Por	Yes	No
Spa	Yes	No
Swe	Yes	No
UK	Yes	Yes

¹ Except if the plaintiff is the audited company.

In all the Member States, except Austria, the statutory auditor may raise the plaintiff's own fault as a defence. In Austria, such a defence is only possible against the plaintiff who is a third party and not the audited company.

This rule is well developed in France and the subject of numerous Court decisions, as it is an established principle of civil liability that the victim's negligence relieves the defendant of liability. This relief can be total⁹⁶ or partial⁹⁷.

In Finland, a Court ruled in favour of a statutory auditor, based on the negligence of the plaintiff, which did not remove the negligence of the auditor with regard to the false auditing report, but broke the causal link between the negligence of the auditor and the damage suffered by the third party⁹⁸.

Finally, in Ireland and the United Kingdom, wrongful acts or omissions on the part of the officers or employees of the plaintiff could justify a reduction in any award of damages on the basis of contributory negligence on the part of the plaintiff or its officers or employees. For example, in the United Kingdom, if the negligence of the auditor and the plaintiff both contribute to the damage, liability is apportioned between them as the Court thinks just in accordance with the seriousness of their fault and the causal potency of their contributions to the damage.

- Third Party Liability

The fault of a third party may be considered in determining whether there was a fault of the statutory auditor himself: as a common principle, the statutory auditor should not negligently rely on information he may receive from third parties, e.g. subsidiaries' auditors, chartered

accountants, etc. The fault committed by an expert appointed by the statutory auditor has been treated above (see *supra* section 1.4.1 a.).

This subject raises fundamental questions of justice and how society has chosen to apportion the risk of loss. In the joint and several liability system, the plaintiff has the advantage of seeking full restitution from any of a number of defendants. The tortfeasors can then resolve the issue of apportionment between themselves. This “pro-plaintiff” approach can have important repercussions in the field of statutory audits since the injured parties (for example, the shareholders of a company which has gone bankrupt) may obtain full compensation from a party with “deep pockets” which is also often the only defendant with insurance available, i.e. the auditing firm.

The proportional approach allows the plaintiff to recover only the percentage of damages which can be imputed to the party in question. This system tends to be more fair to defendants, but has the disadvantage of not assuring the injured party of full restitution and making the determination of fault more important.

On this point, the Commission’s Green Paper, the MARC Report and the 1996 Conference all addressed the issue of apportionment of liability and suggested that liability regimes be more favourable to the statutory auditor.

The general rule applicable in the Member States is one of joint and several liability. Generally, if a defendant pays more than his fair share of the damages, he can seek contribution from other defendants.

The only exception to this rule is the Portuguese system, which provides for both proportional and joint and several liability: joint tortfeasors are jointly and severally liable to the injured party⁹⁹, while contractual liability is only joint, meaning that each party is liable for a proportional part of the damages, except the Audit Board (*Conselho Fiscal*), whose liability is joint and several. Various Portuguese legal provisions add specific rules dealing with this sort of liability¹⁰⁰.

In all the Member States which have a system of joint and several liability, a defendant who pays more than his share may seek contribution from his co-defendants. The appreciation of the causal link helps in determining the part of each of them.

In the United Kingdom, for example, if a third party is ordered to pay contribution to the auditor, the amount of such contribution will also be such as the Court deems fair, determined in accordance with the seriousness of their fault and the causal potency of their contributions to the damage. Another example of this practice of allowing a contribution to a co-defendant comes from a Finnish case¹⁰¹. In France, if the statutory auditor has paid the totality of the damages, he can seek contribution from the co-defendants. To determine the amount of contribution, Courts take into account either the comparative impacts of the various faults on the damages¹⁰² or the seriousness of the fault of each party¹⁰³. In Austria, the persons having caused the injury must pay damages in equal proportions unless one party’s liability for the damages or the seriousness of his fault is considerably higher than the other parties, in which case the allocation of the damages will be based on the level of fault.

1.5 Limitations of Liability

Statutory auditors' liability is not limitless. The work already completed in this area (MARC Report, Green Paper) explored the various possibilities for limiting a statutory auditor's liability. The two methods of limiting the liability of the statutory auditor are legislation placing statutory limits on the amount of liability and agreements between the parties to the audit contract setting forth a liability cap.

Both of these methods raise the question of whether the liability caps should apply to third parties who are not in privity with the statutory auditor and the audited company. The MARC report recommended that there be "no legally determined liability cap" and that auditors should have the freedom to agree to contractual liability caps with their clients.

This section will describe both legal limitations (1.5.1) and those provided for by contract (1.5.2).

SUMMARY: LIMITATIONS OF LIABILITY

Statutory auditors may benefit of several legal limitations to their liability exposure:

- time limits: there are almost as many rules regarding the limitation period and its starting point as Member States. For contract actions against statutory auditors, the statute of limitations vary from 2 years (Gre) to 15 years (Spa) and, as a general rule, they start running when the damage occurred or has been discovered. Tort actions must be brought within a period that may be as short as 1 year from discovery of the damage (Spa) and as long as 10 years from its occurrence (Fin, Swe), or even 20 years after the act (Gre);
- legal caps: three Member States' legal systems (Aus, Ger, Gre) include a legal liability cap. In Austria and Germany, it does not apply to the auditor who acted intentionally. In Greece and Austria, it concerns both liability to the audited company and liability to third parties;
- corporate structure: in every Member States except Ireland, statutory auditors are allowed to incorporate in limited liability companies. This is a way for the members of an audit firm who did not participate to the audit to limit their exposure where the audit firm is held liable. However, in Austria, the legal representative of the auditing firm is personally liable even if he did not participate in the audit, and in Portugal and Spain, partners who did not sign the audit report may be jointly and severally liable under certain conditions;

In addition, in a few cases, they may agree with the audited company to limit their liability:

- time limitations may be agreed by contract in Denmark, the Netherlands and Spain;
- contractual caps may exclude or limit the right to recovery (Den, Lux, Ned, Spa), except in case of wilful misconduct (Ned, Spa), gross negligence (Den, Lux, Ned), or fraud (Den, Lux);
- certain obligations of the statutory auditor may be suppressed by contract with the audited company in Denmark and the Netherlands;
- discharge: the audited company may relieve the statutory auditor from liability in Belgium and Luxembourg under certain circumstances, and in Ireland, also in theory.

1.5.1 Statutory Limitations

Time limitations (a), liability caps (b) and the impact of the auditor's corporate structure (c) are discussed below.

a) Time Limitations

Questionnaire reference:

What is the statute of limitations for such a liability action? When does the statute of limitations begin to run? How is the statute of limitations tolled or interrupted? Is there a shorter foreclosure deadline? (Question 3.2.1)

There are significant distortions between the rules governing the statutory limitation period.

First, in certain countries (Fin, Ger, Gre, Spa, Swe, UK) a distinction is made between contractual actions and tort actions. The tables hereafter present the main rules applied in the Member States for both types of action.

Statute of Limitations for Contract Actions

COUNTRY	STATUTE OF LIMITATIONS	STARTING POINT
Aus	5 years	When damages occur
Bel	5 years	When damage causing event occurs
Den	5 years	Upon discovery of negligence
Fin	3 years	Upon signature of report
Fra	3 years	When damage causing event occurs
Ger	5 years	When all elements of claim exist
Gre	2 years	When all elements of claim exist ⁱ
Ire	6 years	When damage causing event occurs
Ita	5 years/10 years ⁱⁱ	Upon discovery of damages
Lux	5 years	Upon signature of report
Ned	5 years	Upon discovery of damages and liable party ⁱⁱⁱ
Por	5 years	Upon discovery of negligence
Spa	15 years	When all elements of claim exist
Swe	5 years	At the end of the fiscal year
UK	6 years	When damage causing event occurs

ⁱ In the case of faulty acts or omissions concerning the audit of the annual financial statements, the time begins running with the submission of the audit report to the general meeting of the shareholders. In case of other illegal actions, e.g. the violation of confidentiality, the time begins from the time when the violation is committed.

ⁱⁱ With respect to the auditing firm, the Supreme Court has held that this firm is not a part of the audited company but rather an autonomous legal entity which undertakes an external verification. Cass. 9 March 1982, n° 1475, in Mass. Giur. It., 1984, p. 369. Such an action would have a ten-year statutory limit.

ⁱⁱⁱ This period is limited by the fact that the maximum period after which proceedings can be instituted is twenty years after the event which caused the damage.

Statute of Limitations for Tort Actions

COUNTRY	STATUTE OF LIMITATIONS	STARTING POINT
Aus	3 years	Upon discovery of damages
Bel	5 years	When damage causing event occurs
Den	5 years	Upon discovery of negligence
Fin	10 years	When damages occur
Fra	3 years	When damage causing event occurs
Ger	3 years	Upon discovery of damages and liable party
Gre	5 years/20 years ⁱ	Upon discovery of damages and liable party
Ire	6 years	When damages occur
Ita	5 years/10 years ⁱⁱ	Upon discovery of damages
Lux	5 years	Upon signature of report
Ned	5 years ⁱ	Upon discovery of damages and liable party
Por	5 years	Upon discovery of negligence
Spa	1 year	Upon discovery of damages
Swe	10 years	When damages occur
UK	6 years	When damages occur
ⁱ Without regard to the discovery of damages, the period is twenty years from the commission of the act.		
ⁱⁱ The general rule is that the statute of limitation is 5 years for actions against the statutory auditor. With respect to the auditing firm, the Supreme Court has held that this firm is not a part of the audited company but rather an autonomous legal entity which undertakes an external verification. Cass. 9 March 1982, n° 1475, in Mass. Giur. It., 1984, p. 369. Such an action would have a ten-year statutory limit.		

The limitation periods vary from 1 to 20 years, although in most cases they are between 3 and 6 years.

The starting point is not the same in all Member States. The starting point which is the most favourable to the statutory auditor is the time of the signature of the report (Fin (contract), Lux). Other Member States refer to the time when the damage causing event occurs (Bel, Fra, Ire and UK (contract)) or when damages occur (Aus (contract); Fin, Ire, Swe and UK (tort)).

In some Member States (Bel, Fra, Ire, Lux, UK), if the defendant is found to have concealed the tortious event, the statute of limitations begins to run upon discovery of the event in question. Even in the absence of concealment by the defendant, it is possible to extend the limitation period in the United Kingdom if the injured party suffers “latent damages”, in which case he may bring an action in negligence within three years from the earliest date on which he first had both the knowledge required for bringing such an action in respect of the relevant damage and a right to bring such an action.

In other Member States (Ger, Gre, Spa), all of the elements of claim have to exist for the limitation period of contractual actions to begin running.

Finally, the rule which is the least favourable to the statutory auditor is the rule according to which the limitation period starts to run only upon discovery of the negligence (Den, Por), discovery of the damages (Aus and Spa for tort actions, Ita) or, in some countries, discovery of both the damages and the person responsible (Ger and Gre for tort actions, Ned).

In four Member States (Bel, Fin, Gre, Swe), if the act in question is also a criminal act, the civil statute of limitations is extended to cover the limitations period for the criminal act.

In all the Member States, the limitation period is interrupted by the defendant's acknowledgement of the plaintiff's claim or by the commencement of legal proceedings.

b) Liability caps

Questionnaire reference:

If there is a maximum amount or a fixed rate for damages:

- *What are the basis and the conditions for their application, is the cap (or fixed rate) calculated per victim or per breach?*
- *May the parties waive the cap or fixed rate? May the Court disregard the cap or fixed rate in view of the degree of breach (e.g. intentional tort, gross negligence, etc.)?*
- *Do they apply to claims by the audited company or to third parties? (Question 3.2.6.1)*

The study hereafter focuses on legal caps only. Contractual caps will be presented later on, within the scope of contractual agreements. Both of devices raise the further question of whether liability caps should apply to third parties who are not in privity with the statutory auditor and the audited company.

COUNTRY	Statutory liability cap	Impact on third parties?
Aus	Yes	Yes
Bel	No	N/A
Den	No	N/A
Fin	No	N/A
Fra	No	N/A
Ger	Yes	No ¹
Gre	Yes	Yes
Ire	No	N/A
Ita	No	N/A
Lux	No	N/A
Ned	No	N/A
Por	No	N/A
Spa	No	N/A
Swe	No	N/A
UK	No	N/A
¹ Except for contractual actions under the conditions described below.		

Statutory limitations on the amount of damages exist in only three countries (Aus, Ger, Gre):

- in **Austria**: the legal cap is set at ATS 5 million¹⁰⁴ (approximately 363,400 Euro) per audit, regardless of the number of persons conducting the audit and the number of acts or omissions causing the damage, as long as the damage was caused negligently. The cap does not apply to intentional conduct and the statutory auditor may waive the cap. The cap applies to claims by the audited company as well as to claims of third parties.

- in **Germany**: the cap on damages stands at DM 2 million¹⁰⁵ (approximately 1 million Euro) per examination. In case of the examination of a stock corporation with issued stock with official rating (*Notierung*), liability for negligence is limited to DM 8 million (approximately 4 million Euro) per audit. The cap applies regardless of whether several persons participated in the examination and whether one or several of them acted intentionally, but those who acted intentionally do not enjoy the liability cap. This statute cannot be waived by the parties¹⁰⁶.

Statutory auditors whose activities are governed by Article 323 HGB which provides for this cap are generally not liable to third parties for breach of contract, except where a claim is made on the basis of a contract with protective effects with respect to a third party (see p. 25). In such a case, the question of the application of the liability cap has not been settled¹⁰⁷.

To the extent the breach of a contractual duty would generally also give rise to liability towards the audited company in tort, the liability cap does not apply to torts committed outside the scope of contractual obligations.

- in **Greece**: the statutory auditor's liability cannot exceed an amount equal to five times the annual salary of the President of the Supreme Court or the total amount of fees received by the chartered accountant during the previous fiscal year, whichever is higher¹⁰⁸. The cap is calculated per breach and it concerns liability vis-a-vis the audited company and third parties. The parties may agree to waive the cap.

It is interesting to note that a liability cap was proposed to the Belgian legislature but was rejected as a result of the difficulty to create an exception to the general rules of civil liability.

Apart from statutory limitations on liability, some Member States give Courts the power to reduce the amount of damages that the statutory auditor is ordered to pay. This led to cases in the United Kingdom¹⁰⁹ and Finland¹¹⁰.

c) Corporate Structure

Questionnaire reference:

If the audit is undertaken by a legal entity and if the firm is the statutory auditor, can an action be brought against the firm? Against the individual in charge of the audit and who signed the reports (if such a signature was required)? Against the other partners of the firm, even if they did not participate in the audit in question? Against the associates of the individual who undertook the audit? (Question 1.4.2.1)

In every Member State except Ireland, statutory auditors may structure their business as limited liability firms which shield them from liability. The MARC report recommended an unrestricted freedom for auditing firms to adopt any legal form (See, MARC Report, p. 154).

COUNTRY	Form of business organisation performing statutory audits	Partners' liability
Aus	<i>Aktiengesellschaft</i> (public limited liability company)	Limited ⁱ
	<i>Gesellschaft mit beschränkter Haftung</i> (limited liability company)	Limited ⁱ
	<i>Kommanditgesellschaft</i> (limited partnership) ⁱⁱ	Limited/Unlimited ^{iv}
	<i>Kommanditerwerbsgesellschaft</i> (non-commercial limited partnership)	Limited/Unlimited ^{iv}
	<i>Offene Erwerbsgesellschaft</i> (non-commercial partnership)	Unlimited
	<i>Offene Handelsgesellschaft</i> (general partnership) ⁱⁱ	Unlimited
Bel ⁱⁱⁱ	<i>Société en nom collectif</i> (general partnership)	Unlimited
	<i>Société privée à responsabilité limitée</i> (limited liability company)	Limited
	<i>Société coopérative</i> (cooperative company)	Limited/Unlimited
Den	<i>Interessentskab</i> (general partnership)	Unlimited
	<i>Aktieselskab</i> (public limited liability company)	Limited
	<i>Anpartsselskab</i> (private limited company)	Limited
Fin ^v	<i>Avoin yhtiö</i> (general partnership)	Unlimited
	<i>Kommandiittiyhtiö</i> (limited partnership)	Limited/Unlimited ^{iv}
	<i>Osaakeyhtiö</i> (limited liability company)	Limited
Fra ^{vi}	<i>Société civile professionnelle</i> or <i>société d'exercice libéral</i> (professional corporation)	Unlimited
	<i>Société anonyme</i> or <i>"société à responsabilité limitée"</i> (limited liability company, limited liability company)	Limited
Ger	<i>Aktiengesellschaft</i> (public limited liability company)	Limited
	<i>Kommanditgesellschaft auf Aktien</i> (incorporated partnership)	Limited/Unlimited ^{iv}
	<i>Gesellschaft mit beschränkter Haftung</i> (limited liability company)	Limited
	<i>Offene Handelsgesellschaft</i> (general partnership)	Unlimited
	<i>Kommanditgesellschaft</i> (limited partnership)	Unlimited
	<i>Partnerschaftsgesellschaft</i> (partnership companies)	Unlimited
Gre	<i>Omorrythmos Etairia</i> (general partnership)	Unlimited
	<i>Eterorrythmos Etairia</i> (limited partnership)	Limited/Unlimited ^{iv}
	<i>Etaireia Periorismenis Euthinis</i> (limited liability company)	Limited
	<i>Anonymi Etairia</i> (public limited liability company)	Limited
Ire	Partnership	Unlimited
Ita ^{vii}	<i>Società Semplice</i> (non-commercial partnership)	Unlimited
	<i>Società in Nome Collettivo</i> (general partnership)	Unlimited
	<i>Società in Accomandita Semplice</i> (limited partnership)	Limited/Unlimited ^{iv}
	<i>Società per Azioni</i> (société par actions)	Unlimited
	<i>Società in Accomandita per Azioni</i> (incorporated partnership)	Limited/Unlimited ^{iv}
	<i>Società a Responsabilità Limitata</i> (limited liability company)	Limited
Lux ^{viii}	<i>Société anonyme</i> (public limited liability company)	Limited
	<i>Société à responsabilité limitée</i> (private limited liability company)	Limited
	<i>Société civile</i> (non-commercial company)	Unlimited
Ned	<i>Maatschap</i> ^{ix} (general partnership)	Unlimited
	<i>Besloten Vennootschap met beperkte aansprakelijkheid</i> (private limited liability company)	Limited
	<i>Naamloze Vennootschap</i> (public limited liability company)	Limited

Por ^x	<i>Sociedades Civis Profissionais</i> (professional corporation)	Limited
	<i>Sociedades Anonimas</i> (public limited liability company)	Limited
	<i>Sociedades em Nome Colectivo</i> (general partnership)	Unlimited
	<i>Sociedades em Comandita</i> (limited partnership)	Limited/Unlimited ^{iv}
Spa	<i>Sociedad civil</i> (non-commercial company)	Unlimited
	<i>Sociedad colectiva</i> (general partnership)	Unlimited
	<i>Sociedad comanditaria</i> (limited partnership)	Limited/Unlimited ^{iv}
	<i>Sociedad comanditaria por acciones</i> (incorporated partnership)	Limited/Unlimited ^{iv}
	<i>Sociedad de responsabilidad limitada</i> (limited liability company)	Limited
	<i>Sociedad anonima</i> (limited liability company)	Limited
	<i>Sociedad cooperativa</i> (cooperative company)	Limited
Swe	<i>Kommanditbolag</i> (limited partnership)	Limited/Unlimited ^{iv}
	<i>Handelsbolag</i> (partnership)	Unlimited
	<i>Aktiebolag</i> (limited liability company)	Limited
UK	Partnership	Unlimited
	Limited Partnership	Limited/Unlimited ^{iv}
	Public Limited Liability Company	Limited
	Private Limited Liability Company	Limited

ⁱ However, if the partner is also a legal representative of the company, his liability is unlimited.

ⁱⁱ As of 7 July 1999, auditing firms may no longer be set up in this legal form. Existing general and limited partnerships have been granted a transition period until 31 December 2005.

ⁱⁱⁱ In Belgium, there are no auditing firms which operate as partnerships. There are 258 auditing firms which have adopted the form of the SPRL. The liability of cooperatives depends upon whether the entity is a limited liability cooperative (*société coopérative à responsabilité limitée*) or an unlimited liability cooperative (*société coopérative à responsabilité illimitée*). In the overwhelming majority of cases, the former entity is adopted. There are currently 46 such entities undertaking statutory auditing in Belgium.

^{iv} The full partners have unlimited liability, the silent or "investing" partners have limited liability.

^v Companies or partnerships which are capable of acting as an independent auditing firm can be approved either as a KHT Firm of Auditors or a HTM Firm of Auditors. There are 21 KHT Firms of Auditors (all of which are limited liability companies) and 26 HTM Firms of Auditors (20 limited liability companies and 6 limited or general partnerships).

^{vi} The issue of whether an incorporated partnership (*société en commandite par actions*), a limited partnership (*société en commandite simple*) and a general partnership (*société en nom collectif*) may undertake statutory audits has been considered but, in practice, this kind of structure is never adopted since partners' liability is unlimited.

^{vii} This is only relevant to the auditing firm.

^{viii} The law does not provide a list of business organisations which have the status of *réviseur d'entreprises*. Consequently, all forms of business organisations may, in theory, become a members of the IRE. Currently, all the members of the IRE are one of the three types of entities listed above.

^{ix} Until recently, practically all statutory auditors were organised as *maatschap*.

^x Decree-Law n° 487/99 which was adopted in November 1999 foresees new forms of business organisations that may be used by Statutory Auditors and is more in line with the rest of the European Union. Each of these new forms must maintain their civil nature (i.e. they cannot perform commercial acts).

In one Member State (Ire), the option of operating under a business form which limits personal liability does not exist and, consequently, all the partners (whether they participated in the audit or not) are jointly and severally liable.

In the fourteen other Member States, statutory auditors are allowed to adopt the structure of a limited liability company. This allows partners who did not participate in the audit to shield themselves from civil liability.

There are three qualifications to this rule:

- in Austria, the legal representative of the auditing firm is liable even if he did not personally participate in the audit in question¹¹¹;
- in Spain, partners who have not signed the audit report are subsidiarily liable, jointly and severally amongst themselves¹¹². No action may be brought against them until the plaintiff has exhausted its remedies against the firm and the partner in charge of the work, but once such remedies have been exhausted, the plaintiff may sue all or part of the remaining partners;
- in Portugal, unless its Articles of Incorporation provide otherwise¹¹³, the managers of the statutory auditors' firm are liable towards its creditors only where, due to their intentional or negligent conduct, disregard of the legal or contractual provisions aiming to protect creditors, the firm's assets have become insufficient¹¹⁴. Moreover, the *Comissario de Mercado de Valores Mobiliarios* ruled that whenever auditors' firms listed at the *Comisario de Valores Mobiliarios* intentionally or negligently cause damages to entities that issue shares to investors and to third parties, the auditing firm and its partners are jointly, severally and unlimitedly liable for the damages¹¹⁵.

1.5.2 Contractual Limitations

In the absence of a statutory cap on liability or in addition thereto, the statutory auditor and the audited company may sometimes agree to setting a liability cap (b), limiting certain obligations (c) or shortening the statutory limitations period (a). Such arrangements have the advantage of flexibility as they allow the parties to adopt an estimate of possible damages which is the result of an arm's length agreement. Discharge by management may also affect the liability action (d).

In a vast majority of Member States, it is not possible to eliminate or lessen the auditor's obligations, shorten the limitation period or agree to a cap on liability. The rationale behind these restrictions is that the parties cannot alter by contract what has been set forth by law with the purpose of protecting the interests of third parties and the public in general.

However, the table hereafter shows that there are exceptions to this rule.

May the statutory auditor contract with the audited company for:

Country	Shortening the statutory or legal period	Setting a Liability Cap	Suppression of certain obligations
Aus	No	No	No
Bel	No	No	No
Den	Yes	Yes	Yes
Fin	No	No	No
Fra	No	No	No
Ger	No	No	No
Gre	No	No	No
Ire	No	No	No
Ita	No	No	No
Lux	No	Yes	No
Ned	Yes	Yes	Yes
Por	No	No	No
Spa	Yes	Yes	No
Swe	No	No	No
UK	No	No	No

a) Time Limitations

Questionnaire references:

- *May the statutory auditor contract with the audited company:*
 - *to shorten the statutory or legal period in which to bring an action? (Question 3.2.6.2)*
- *In the above situations:*
 - *to what extent may the defendant rely on such a clause with respect to third parties to the contract*
 - *may such provisions be agreed upon with a party other than the audited company? (Question 3.2.6.3)*

In Denmark, the Netherlands and Spain only, it is possible to reduce the statute of limitation by contract.

b) Liability caps

Questionnaire references:

- *May the statutory auditor contract with the audited company:*
 - *to exclude or limit the right to recover damages (e.g. by limiting the amount of damages) If so, to what extent can the defendant rely on such agreements (such as in case of fraud or gross negligence of the statutory auditor)? (Question 3.2.6.2)?*
- *In the above situations:*
 - *to what extent may the defendant rely on such a clause with respect to third parties to the contract*
 - *may such provisions be agreed upon with a party other than the audited company? (Question 3.2.6.3)*

Only four Member States (Den, Lux, Ned, Spa) allow parties to agree to a liability cap. But such limitation of liability will have no effect in case of wilful misconduct (Ned, Spa), gross

negligence (Den, Lux, Ned), or fraud (Den, Lux). In Austria and Germany, it is possible to raise the legal cap, but not to reduce it.

c) Obligations

Questionnaire references:

- *May the statutory auditor contract with the audited company:*
 - *to suppress or increase certain obligations normally required of a statutory auditor? (Question 3.2.6.2)*
- *In the above situations:*
 - *to what extent may the defendant rely on such a clause with respect to third parties to the contract*
 - *may such provisions be agreed upon with a party other than the audited company? (Question 3.2.6.3)*

In Denmark and the Netherlands, the statutory auditor may contract with the audited company to suppress certain obligations. This does not impact, however, on the statutory auditor's liability to third parties. In the Netherlands, parties to a contract are free to limit their liability in case of breach of contract, to the extent that such a limitation is not contrary to "good morals"¹¹⁶.

d) Discharge

Questionnaire reference:

May the statutory auditor be, wholly or in part, immune from liability on the basis of certain circumstances such as shareholders ratification/discharge, difficulties encountered while performing the audit, lack of time, insufficiency of fees, intervention of another accounting specialist, mistake in law, force majeure? (Question 3.2.3)

Because liability depends, in general, on the diligence with which the auditor has carried out his work, it is independent from external circumstances such as the insufficiency of fees or the intervention of other accountants. Similarly, in most cases, the behaviour of the audited company's management towards the auditor is less relevant for the determination of the auditor's liability than the behaviour of the auditor himself.

Nevertheless, there are three countries (Bel, Ire, Lux) where it is possible for the statutory auditor to obtain a discharge from the shareholders.

In Belgium, the audited company may discharge the statutory auditor from both contractual and tort liability. Such a discharge will be strictly interpreted and must have been given with full knowledge of the circumstances. The discharge is effective only if "the annual accounts contain no omission or false indication hiding the true situation of the company." Moreover, according to Article 79 of the L.C.S.C., the discharge does not impact on the right of individual shareholders who did not approve the discharge to recover their personal damages which are distinct from those of the company. A similar rule exists in Luxembourg.

In Ireland, such a discharge is theoretically possible but the situation has apparently never arisen with respect to a statutory auditor.

1.6 Insurance

The ability to acquire and maintain liability insurance is an important concern of the auditing industry in the European Union. Increases in the number of civil liability actions and the damages awarded have placed a strain on the coverage of liability risks.

As a result, coverage is becoming more difficult to acquire and both premiums and deductibles are rising. Since few countries allow limitations on liability (*supra* question 3.2.6 p. 74), this trend will continue to develop.

The MARC Report recommended a “mandated professional indemnity insurance for auditors.” On the other hand, one speaker at the 1996 Conference indicated that the level of insurance has “undoubtedly resulted in what we now recognise as ‘deep pocket litigation’.”¹¹⁷ Another speaker said, “if a claim does result in litigation, the Court will first find out to what extent it is covered by insurance. The Court will then award the claim for the amount insured plus a surcharge, since the auditor must, after all, be punished for his professional error.”¹¹⁸

Finally, the Commission’s Green Paper pointed out that “insurance premiums throughout the EU might become more expensive as a result of litigation in some Member States. This might lead to a further concentration of the audit market in the hands of a limited number of audit firms.”

This section will explore the requirements in the Member States to have coverage (1.6.1), the levels of minimum coverage and maximum deductible (1.6.2), insurance coverage for individual auditors working within an auditing firm (1.6.3), the availability of group insurance plans (1.6.4) and the involvement of insurance companies in litigation of liability claims against statutory auditors (1.6.5).

SUMMARY : INSURANCE

The increase of civil liability actions makes the insurance coverage an issue of great importance. In most countries, insurance coverage is required by law (Aus, Den, Fra, Ger, Gre, Ita – auditing firms, Ned, Por, Spa, Swe), or by the professional organisations (Bel, Ire, UK). In the other Member States, statutory auditors usually obtain such professional insurance.

Except Ireland and Italy, all the Member States where insurance is mandatory require a minimum coverage, the amounts of which vary significantly. In France, Germany, Greece and United Kingdom, a maximum deductible is also imposed by law.

The obligation of obtaining a professional insurance rests either with the firm (Aus, Ger, Gre, Ire, Ita, Por, Spa), with the individual (Fra, UK), with both of them (Den, Swe), or with any of them (Bel). In Finland, Luxembourg and the Netherlands, there is no general rule.

Most of the Member States' professional organisations have underwritten group insurance policies. Five of them have not (Ger, Gre, Ire, Ita, UK). These group policies set up specific conditions such as minimum coverage, maximum deductible and the basis for the premiums' calculation.

The intervention of the insurance company in litigation usually depends on the terms of the insurance policy. Three Member States (Gre, Por, Spa) have made this intervention mandatory.

1.6.1 Mandatory Insurance

Questionnaire reference:

Is the statutory auditor required to obtain insurance covering his civil or criminal liability? (Question 4.1.1)

COUNTRY	Is Insurance Mandatory?
Aus	Yes
Bel	Yes ¹
Den	Yes
Fin	No
Fra	Yes
Ger	Yes
Gre	Yes
Ire	Yes ¹
Ita	Yes/No ²
Lux	No
Ned	No
Por	Yes
Spa	Yes
Swe	Yes
UK	Yes ¹
¹ Required by the professional supervisory body. ² For auditing firms (<i>società di revisione contabile</i>) insurance is mandatory under Article 161, para. 4 of the T.U. There is no insurance requirement for the board of auditors (<i>collegio sindacale</i>). Since the members of the board are professionals who practice law or accounting, they have insurance which covers all of their professional activity.	

In most countries, statutory auditors are required by law to obtain and maintain insurance covering their professional liability (Aus, Den, Fra, Ger, Gre, Ita – auditing firms, Por, Spa, Swe).

In countries where compulsory insurance coverage is not mandated by law, it is either required by the main professional organisations (Bel, Ire, UK) or it is a common practice or it is recommended to maintain such coverage (Fin, Ned, Lux).

1.6.2 Scope of Insurance

Questionnaire references:

Is there a minimum coverage per year or per claim? Is there any maximum deductible? (Question 4.1.4)

Does the law provide a list of risks which are or are not covered? (Question 4.1.5)

In every Member State, the insurance available to statutory auditors only covers their civil liability and not criminal liability which arises from intentional or grossly negligent conduct.

The table hereafter presents the minimum amounts to be covered and the maximum amounts that can be deducted.

COUNTRY	Amount of Minimum Coverage	Maximum Deductible
Aus	72 673 Euro	None
Bel	635 000 Euro	None
Den	268 000 Euro	None
Fin	None	None
Fra	76 224 Euro	10% of claim
Ger	1 022 583 to 4 090 335 Euro	1% of minimum coverage
Gre	150% of turnover	4 500 Euro
Ire	None	None
Ita	None	None
Lux	None	None
Ned	None	None
Por	500 000 Euro	None
Spa	300 506 Euro	None
Swe	887 600 Euro	None
UK	Varies ¹	Varies ¹
¹ Set by the recognised supervisory body to which the auditor is a member.		

- Minimum Coverage

In countries where a minimum coverage is required (Aus, Bel, Den, Fra, Ger, Gre, Por, Spa, Swe, UK), the required minima vary significantly. In France and Austria, the minimum coverage required by law is approximately 70,000 Euro, while in Belgium it is 635,000 Euro and in Germany from 1,022,583 Euro to 4,090,335 Euro. In Denmark, the insurance policy subscribed by firms employing more than 10 auditors must cover DKK 20 million (2.7 million Euro) per year at least.

In practice, in countries where insurance is not mandatory, minimum amounts are not specified but directly negotiated in group insurance policies.

- Deductibles

In some Member States, maximum deductibles are imposed by law (Fra, Ger, Gre) or by rules of the relevant professional institutes (UK).

The method for calculating the amount of the maximum deductible differs from one country to the other. In Germany, the maximum deductible is 1% of the minimum coverage. French law limits the deductible to 10% of the claim and, in the group insurance policy, the deductible is lowered to 1,524 Euro. In the United Kingdom, the maximum deductible for the Institute of Chartered Accountants of England and Wales varies with the size of the firm.

In other Member States, there is no maximum deductible. Such a solution leads to significant variation between lower and upper amounts negotiated in insurance policies within the same Member State.

1.6.3 The Insured (firm and / or employees)

Questionnaire reference:

If the statutory auditor practices as the employee/partner of a firm, does the obligation rest with the individual or with the firm? (Question 4.1.2)

COUNTRY	Who must maintain the insurance?
Aus	Firm
Bel	Auditor or firm
Den	Auditor and firm
Fin	Not required
Fra	Auditor
Ger	Firm
Gre	Firm
Ire	Firm
Ita	Firm
Lux	Not required
Ned	Not required
Por	Firm
Spa	Firm
Swe	Auditor and firm
UK	Auditor

A distinction can be made between five types of countries. Countries where the obligation rests with the auditor, those where it rests with the firm, those where both have to take out an insurance policy, those where a choice exists and, finally, those where there is no obligation to obtain an insurance.

In a first group of Member States, the insurance obligation rests with the individual (Fra, UK). In the United Kingdom, this obligation is invariably satisfied by the professional indemnity insurance of any firm in which the individual is a partner.

In the second group of countries (Aus, Ger, Gre, Ire, Ita, Por, Spa), the obligation rests with the firm, even if some variations exist in its formal application. In Austria, the obligation rests with the party to the contract with the client. In Germany, while the responsibility to take out the mandatory insurance lies with the firm, a statutory auditor who practices as a partner in a civil law association (OHG, KG) must obtain separate insurance coverage (Art. 44b IV, Act on the profession of Auditors). In Ireland, while there is no such requirement imposed by law, the Institute of Chartered Accountants requires professional indemnity insurance to cover all of the individuals practising in the firm. In Portugal, the obligation rests with the firm, but if all the partners of the firm have a personal insurance in compliance with the law, the firm is not required to have insurance.

In the third group of countries (Den, Swe), the obligation rests with the auditor individually as well as with the firm.

In Belgium, there is a choice.

In Finland, Luxembourg and the Netherlands, since there is no obligation to obtain liability insurance, the issue is dealt with on a case by case basis. For example, in Finland, group insurance policies are only available to natural persons but firms may negotiate a separate liability insurance to cover their risk as employers of auditors.

1.6.4 Group Insurance

Questionnaire reference:

Is there a group insurance policy available in general to members of the profession? (Question 4.1.3)

COUNTRY	Availability of a group policy
Aus	Yes
Bel	Yes
Den	Yes
Fin	Yes
Fra	Yes
Ger	No
Gre	No
Ire	No
Ita	No
Lux	Yes
Ned	Yes
Por	Yes
Spa	Yes
Swe	Yes
UK	No

In five Member States, there is no group insurance policy available (Ger, Gre, Ire, Ita, UK).

In the Netherlands, there is no group insurance policy available for *Registeraccountant*. For *Accountants-Administratieconsulent* (AA), a group policy was recently underwritten. Additional conditions may be required by the insurers, and insurers remain free to refuse AAs who apply for coverage.

In other Member States (Aus, Bel, Den, Fin, Fra, Lux, Por, Spa, Swe), professional organisations have negotiated group insurance policies with insurance companies:

- in Austria, there is joint professional indemnity insurance for damages exceeding coverage obtained by the individual members of the profession. The sum insured under the joint professional indemnity insurance equals nine times the sum insured under the member's policy, within the limits of a minimum amount of 654,055 Euro and a maximum of 2,180,185 Euro;
- in Belgium, the IRE subscribed a policy through the insurance brokerage firm Marsh and underwritten by AGF Belgium, which is available to individual auditors and auditing firms. Similar coverage has been taken out by the *Institut des réviseurs d'entreprises* of Luxembourg and covers 1.25 million Euro per claim and a deductible of 10% of the claim within the limits of 250 and 2,500 Euro;
- in Finland, both the association for certified KHT auditors and the association for HTM auditors have negotiated a group insurance policy with insurance company *Pohjola*, which is available to their individual members. For members of the KHT auditors association, the insurance is voluntary, while for members of HTM Auditors association, the insurance is included in the membership fee (voluntary membership). Coverage can reach up to 3,5 to 7 million Euro with a negotiated deductible from 336 Euro to 16,800 Euro;
- in France, the *Compagnie nationale des commissaires aux comptes* has taken out a policy with *Mutuelles du Mans* which is available to individual auditors and auditing firms and provides a maximum annual coverage of 840,000 Euro per claim and 1.67 million for all claims;
- in Portugal, the *Camara de Revisores Oficias de Contas* has taken out a policy with insurance company *Lusitania-Companhia de Seguros*;
- in Sweden, a group insurance organised by *FAR* is available to all members of the profession. The policy is underwritten by *AIG Europe*. The minimum coverage is 200 "base amounts" per claim (currently approximately 900,000 Euro).

1.6.5 Role of Insurance Companies in Litigation

Questionnaire reference:

How do insurance companies intervene in pending litigation? Is the intervention voluntary or forced? Are they in charge of the litigation? (Question 4.2.1)

Generally, Member States laws do not include provisions on the involvement of the insurance company in litigation because it is a general principle that parties who have an interest in litigation have the right to intervene.

In most Member States, the involvement of the insurance company is left to the discretion of the parties to the insurance policy (Aus, Bel, Den, Fin, Fra, Ger, Ire, Ita, Lux, Ned, Swe, UK). In practice, the policy generally provides that the insurer is in charge of the litigation management, but there may be also specificities:

- in Denmark, the auditor may involve his insurance company if he wishes;
- in France and Italy, although insurance policies often provide that the insurer has the right or obligation to intervene, the insured party also has the power to call in the insurer to intervene;
- in Finland, the insurance company can always take over the litigation on behalf of the insured; but the insured cannot force the insurance company to take part in the litigation;
- in Germany, insurance companies cannot intervene directly. However, they usually fix their influence in the insurance contract and, in practice, they usually determine the course of defence.

In other Member States, the intervention of the insurance company is mandatory (Gre, Por, Spa):

- in Greece, insurance companies are forced parties in litigation concerning the occurrence of an insured event;
- in Portugal, the action must be brought against the insurance company when the amount of the claim is less than 25 million escudos or, in the special case of auditing firms registered in the capital market commission, 500 million escudos. Above these amounts, the action must be brought against both the insurance company and the statutory auditor;
- in Spain, the insurer is required to be involved in litigation, unless the parties have previously agreed otherwise.

2. Criminal Liability

As a result of the public interest aspect of the statutory auditor's duties, he is in an increasing number of cases exposed to criminal liability. In addition, criminal proceedings can have an effect on the injured party's ability to seek civil remedies. It is thus necessary to consider the scope of the criminal sanctions that are applicable to the statutory auditor in the performance of his mission.

This section will explore the various criminal statutes which apply to statutory auditors in the Member States as regards the types of criminal offences (2.1), the defendant (2.2), and the main elements of procedure (2.3). Then the study will consider the possible interaction of criminal and civil liability regimes (2.4).

SUMMARY : CRIMINAL LIABILITY

In the scope of the auditor's work, in addition to general criminal offences, the main of which are fraud, misappropriation and breach of confidentiality, statutory auditors may be punished for offences relating specifically to their mission:

- submitting a materially false report;
- failure to report violations to public authorities (in France, Germany and Ireland);
- violation of rules on conflict of interests (in France and Greece).

The individual statutory auditor and the audit firm, if it is appointed as statutory auditor, may be liable in Belgium, Finland, France, Netherlands, Portugal and United Kingdom. In Finland, France and United Kingdom, they may be held liable together. In the other Member States, only physical persons may be criminally liable.

The statutory auditor is prosecuted in Criminal Court, by the public prosecutor. In some countries, the victim also has the right to start the criminal proceedings, independently from the Public Prosecutor's decision (Bel, Fra, Gre, Ire, Ita, Lux, Spa, Por, UK). In some other Member States, this is only possible if the public prosecutor refuses to prosecute (Fin, Swe), or by asking the Court to review his decision (Aus, Ger, Ned). In some cases, the victim's prior consent may be required, as far as certain criminal offences are concerned, mainly the breach of confidentiality (Fin, Ger, Gre, Ita, Por, Spa, Swe).

The victim may claim for damages in the criminal lawsuit. The victim is also allowed to change Courts subsequently in all the Member States, except in Ireland. In France and Luxembourg, it is only allowed to change a criminal prosecution into a civil lawsuit. Thus, a choice between civil and criminal proceedings arises. In some countries, considerations dealing with calculation of damages and standard of proof lead victims to prefer civil lawsuits. However, criminal action may be more favourable to victims in matters where they lack sufficient evidence to make their case, which evidence may be collected by the public prosecutor.

If both civil and criminal procedures have been started, the Civil Court is required to wait for the Criminal Court's decision in Belgium, Denmark, Finland, France, Greece, Italy, Luxembourg and Spain. In Austria and in these Member States except Denmark, the civil decision depends on the outcome of the criminal lawsuit.

2.1 Criminal Offences

Questionnaire reference:

Briefly describe the different criminal offences for which statutory auditors may be prosecuted. (Question 6.1.1)

As a preliminary matter, it is important to ascertain whether statutory auditors' criminal liability may be based on general criminal law statutes or only falls within the ambit of specific legislation. The table hereafter shows that statutory auditors may be held criminally liable under both general criminal provisions (e.g. fraud) and specific statutes.

Country	General Provisions	Provisions dealing specifically with auditors
Aus	Yes	No
Bel	Yes	Yes
Den	Yes	No
Fin	Yes	Yes
Fra	Yes	Yes
Ger	Yes	Yes
Gre	Yes	Yes
Ire	Yes	Yes
Ita	Yes	Yes
Lux	Yes	Yes
Ned	Yes	No
Por	Yes	No
Spa	Yes	No
Swe	Yes	No
UK	Yes	No

In all Member States, the auditors are subject to criminal penalties for violations of the general provisions of the criminal codes such as fraud or misappropriation and disclosure of confidential information on the company. The auditors may be perpetrators or accomplices with respect to all offences relating to business law and the activities of a company.

In addition to these general rules, there are, in several Member States, specific criminal law provisions dealing with the activities of statutory auditors.

In all Member States, the conduct of the auditor must be intentional and with knowledge of the inaccuracy.

Criminal offences may be divided into various categories:

a) Inaccurate Report

In every Member State, it is a criminal offence for the statutory auditor to give or confirm false information on the situation of the company, whether it is stated in the general criminal law or in specific provisions applicable to statutory auditors. However, the issuance of an inaccurate report does not constitute such a criminal offence. Two conditions must be met, even if they are expressed in slightly different terms throughout the Member States:

- the opinion must be materially inaccurate (Fin, Ger, Gre, Ire, Ita, Lux, Swe, UK): the most common situation is that the statutory auditor certified financial statements as providing “a true and fair view” of the situation of the company, whilst there were significant errors in the financial statements;
- fraudulent intent (Aus, Fin, Ire, Ita, Lux, Ned, Spa, UK), meant as the intent to deceive, may be required. In the other countries, the auditor should at least have known that his report expressed an inaccurate opinion.

b) Failure to Report Violations

In France and Ireland, the statutory auditor has a duty to inform the public authorities of violations of the law and is subject to criminal penalties for their concealment.

In the remaining Member States (Aus, Bel, Den, Fin, Ger, Gre, Ita, Lux, Ned, Por, Spa, Swe, UK), such a duty may arise from the general provisions of criminal law, providing that any illegal action should be reported to public authorities, but they do not focus on the auditors' liability in the scope of their work.

The duty to report violations to shareholders or to the company flows from the requirement of accuracy. In cases where violations materially affect the financial statements, the auditor may be punished if he did not take them into account in his report.

c) Conflict of Interests

Concealment of a conflict of interest is a crime in France and in Greece only. In the other Member States, it may lead to disciplinary measures and to civil liability under the conditions presented in the first part of the report.

d) Others

The Member States consider other acts as criminal offences, but there is no common practice regarding these other criminal offences:

- in Belgium and Italy, the violation of the duty to call a general shareholder meeting is a criminal offence;
- in Belgium, receiving fees beyond those set by the board of directors is a criminal offence;

- in Finland, the wilful violation of the duty to submit an auditor's report in violation of the Auditing Act (TTL) is a criminal offence;
- in Ireland, specific provisions provide criminal sanctions for continuing to act after having been disqualified and for failure to supply information to a parent company.

2.2 Criminally Liable Persons

Questionnaire reference:

Who is responsible (the individual or the firm)? (Question 6.1.1)

Country	Individual	Firm
Aus	Yes	No
Bel	Yes	Yes
Den	Yes	No
Fin	Yes	Yes
Fra	Yes	Yes
Ger	Yes	No
Gre	Yes	No
Ire	Yes	No
Ita	Yes	No
Lux	Yes	No
Ned	Yes	Yes
Por	Yes	Yes
Spa	Yes	No
Swe	Yes	No
UK	Yes	Yes

a) Natural Persons

In all the Member States, the individual who has committed the offence is responsible, in application of the principle of criminal liability of the natural person.

b) Legal Persons

The differences between the Member States' laws concerning the criminal liability of legal entities are significant.

- In a first group of Member States (Aus, Den, Ger, Gre, Ire, Ita, Lux, Spa, Swe), the principle *societas delinquere non potest* applies, thus only physical persons may be held criminally liable.

In Italy, the application of that principle is very strict and, therefore, only an individual who has actually committed an offence may be prosecuted. In other countries (Ger, Gre, Lux, Spa), if the firm is involved in a criminal offence, the criminal liability of its agents may be

pursued. The list of possible defendants includes the legal representatives, the managers, the directors or any other representatives.

- Some other Member States (Bel, Fin, Fra, Ned, Por, UK) allow that a firm, or any corporate body, be held criminally liable. The conditions imposed for such prosecution are, however, strict and vary from one Member State to another.

In the Netherlands, a legal entity may be held criminally liable if (i) the responsible person or persons within the firm had knowledge of the way in which a statutory auditor acted, (ii) instructions were given to the concerned statutory auditor by persons with authority to do so, and (iii) the supervisor involved approved the conduct of the statutory auditor or failed to prevent the statutory auditor from acting.

In Belgium, as a general principle of criminal liability, a legal entity is responsible for offences which are closely linked to the accomplishment of its stated purpose or the defence of its interests or for those activities which can be shown to have been undertaken for the benefit of the company.

In France, Portugal and Finland, companies are liable only for offences where such corporate liability is specifically provided by law. Thus, in Finland, a legal entity can be charged with misuse of business secrets, a rather theoretical case of criminal liability for auditing companies. The French Criminal Code provides that *“legal entities are criminally responsible ... for the offences which provide for such a liability”*. While there is no specific offence in French law concerning auditors' liability that does provide criminal responsibility for the firm, such a prosecution would be possible under general provisions such as theft or embezzlement, should their requirements be met. Both in France and Finland, corporate liability is additional to that of the concerned individual who can always be prosecuted. In the United Kingdom, if the auditor is a company, both the company and the individual will be responsible in many cases.

2.3 Role of Public Prosecutor

Questionnaire reference:

Who can start a criminal lawsuit? (Question 6.1.3)

COUNTRY	PUBLIC PROSECUTOR	VICTIM
Aus	Yes	No
Bel	Yes	Yes
Den	Yes	No
Fin	Yes	No ⁱ
Fra	Yes	Yes
Ger	Yes	No
Gre	Yes	Yes
Ire	Yes	Yes
Ita	Yes	Yes
Lux	Yes	Yes
Ned	Yes	No
Por	Yes	Yes
Spa	Yes	Yes
Swe	Yes	No ¹
UK	Yes	Yes
¹ Except if the Public Prosecutor has decided not to prosecute.		

In all the Member States, the public prosecutor has authority to start a criminal action against a statutory auditor who has committed criminal offences.

Differences mainly concern the rights of the victim in criminal proceedings. The victim may be entitled either to start a criminal lawsuit (a) or to consent to the prosecution of specific offences (b).

a) Right to Start a Criminal Lawsuit

In some countries (Aus, Den, Fin, Ger, Ned, Swe), only the public prosecutor is vested with the power to bring criminal charges. There are, however, exceptions to this general rule:

- in Sweden, some crimes may be only prosecuted by the victim, but not the main criminal offences susceptible of being committed by a statutory auditor;
- in Austria, Germany and the Netherlands, victims do not have the right to prosecute by themselves, nor to compel the Prosecutor to start the criminal lawsuit. But they may inform him of wrongful acts which may constitute criminal offences and, if he refuses to commence criminal proceedings, the victim may ask the Court to review his decision;
- in Finland and Sweden, if the public prosecutor refuses to prosecute, the victim may then bring a criminal lawsuit.

In Common Law jurisdictions, it is common practice that victims report criminal acts to the public prosecutor, who decides whether to start a criminal proceeding or not.

In other countries (Bel, Fra, Gre, Ire, Ita, Lux, Por, Spa, UK), the victim can start a criminal lawsuit on its own, without waiting a decision of the public prosecutor.

b) Prior Consent

In many countries (Fin, Ger, Gre, Ita, Port, Spa and Swe), and with respect to specific offences, the victim's prior consent to the public action is required. Thus, although such an action belongs to the public prosecutor, the victim's involvement is in fact required to start a criminal lawsuit for these offences:

- offences for which the consent of the victim is required generally concern the disclosure and/or the use of confidential or business information (Fin, Ger, Gre, Ita, Spa):
- Portugal distinguishes between public, semi-public and private offences; for «private crimes », only the victim may initiate the process and the public indictment depends of and is subject to the terms of the charges presented by the victim;
- in Finland, the prior consent of the victim is required except if a strong public interest so demands, in which case the public prosecutor may act without the victim's consent;
- in Germany, some offences concerning the auditor require an application for prosecution by the victim (e.g. the company concerned) and the public prosecutor will not start any procedure absent such an application or special public interest;
- in Sweden, some crimes may be prosecuted only upon request of the victim.

2.4 Interaction of Criminal and Civil Liability

As a result of the possible existence of both criminal and civil liability for a same conduct, the outcome of litigation is affected by such consideration as the role of the plaintiff in criminal proceedings and the choices which the plaintiff has in bringing his action (a), the possible interaction itself of civil and criminal proceedings (b), and the legal importance of judgements rendered in one forum which are presented in the other (c).

a) Victim's Involvement in Criminal Action

Questionnaire references:

- *May the victim be a party in the criminal case ? May the victim seek damages before the Criminal Court ? If so, under what conditions and how ? (Question 6.2.1)*
- *May the plaintiff choose between the different types of Courts (Civil and Criminal) ? May the plaintiff subsequently change Courts ? Is the plaintiff limited to one Court ? Practically, what are the elements guiding his choice ? (Question 6.2.2)*

The victim may generally become a party to the criminal trial and seek damages. As a common condition for a victim to seek damages based on civil liability in criminal proceedings, damages must relate to the same acts or omissions which are at issue in the criminal charge. In the United Kingdom, it would be possible for a victim to institute a criminal prosecution, but this would be unusual.

In most countries (Aus, Bel, Den, Fin, Ger, Gre, Ita, Ned, Por, Spa, Swe, UK), the plaintiff is entitled to change Courts subsequently to the filing of the criminal action, even if this cannot stop the proceedings started by the public prosecutor. In Ireland, however, the plaintiff is not allowed to change Courts once civil or criminal proceedings have started. In France and Luxembourg, the plaintiff may not change civil proceedings into a criminal prosecution, but can change a criminal lawsuit into a civil lawsuit.

In several countries, plaintiffs would more likely commence civil proceedings because Criminal Courts ultimately refer the victim to the Civil Courts to set the exact amount of damages if the determination of such damages is of any complexity (Aus, Den, Fin, Swe). Also, in Germany, although there is a procedure to seek damages in Criminal Court, hardly anyone uses this possibility since the judge can refrain from deciding upon the civil claim if he considers that it is not appropriate for the Criminal Court to do so and could cause a delay in the procedure.

In some countries, the fact that the plaintiff must prove criminal intent (Ire, UK), which increases the cost, the duration and the complexity of criminal proceedings, leads plaintiffs to bring civil suits. Moreover, in Ireland, damages are not normally awarded in criminal proceedings.

However, in other countries (Bel, Fra, Gre, Lux, Ned, Spa), the authority given to the police, the public prosecutor or judges to collect and secure evidence leads victims to prefer criminal proceedings. Moreover, since the public prosecutor must build up the case, the victim may save costs compared to a civil case. Therefore, in these countries, the complexity of operations certified by the auditor could be a reason to prefer criminal lawsuits.

b) Criminal Courts and Civil Courts

Questionnaire reference:

If the facts are submitted to the Criminal Court (or Civil) must (or may) the Civil (or Criminal) Court postpone its decision ? (Question 6.2.3)

In approximately half the Member States, if a civil lawsuit is running at the same time as a criminal lawsuit, the Civil Court is required to postpone the civil matter until the criminal judgement (Bel, Den, Fin, Fra, Gre, Ita, Lux, Spa).

In the other half Member States (Aus, Ger, Ire, Ned, Por, Swe, UK), civil and criminal litigation and judgements are independent. In those states, no rule of law requires that the criminal trial takes place first. Nevertheless, the Civil Court may postpone the civil lawsuit until a decision has been handed down in Criminal Court.

c) Res Judicata and Authority of the Adjudicated Issue

Questionnaire reference:

Has the decision rendered by a Civil (or Criminal) Court any bearing on the Criminal (or Civil) Court which is adjudicating the same issues (res judicata, authority of the adjudicated issue, etc..)? (Question 6.2.4)

In some Member States (Den, Ger, Ire, Ned, Por, Swe, UK), even where criminal and civil litigation concern the same subject matter, the doctrine of *res judicata* would not arise because civil and criminal Courts would apply different legal tests, different standards of proof and grant different remedies. However, in practice, even though the outcome of a criminal prosecution would not automatically determine the outcome of a civil action and vice versa, if the criminal lawsuit results in a conviction, the conviction can be relied on in the civil litigation as evidence of the facts on which it was based, and the defendant has the burden of disproving those facts, which in practice is likely to prove insurmountable.

Other Member States allow a strong link between civil and criminal judgements. In these Member States, the principle of *res judicata* applies (Aus, Bel, Fin, Fra, Gre, Ita, Lux, Spa) in consideration of the fact on which the criminal or civil liability is based. This means that the outcome of criminal litigation will be controlling in civil Court. Nevertheless, as criminal liability requires proof of wilfulness, whilst civil liability does not, the latter may arise even in the absence of criminal liability.

3. Analysis of the Practical Effects of the Existence of the Various Statutory Auditors' Liability Systems from the Point of View of the Single Market

As set forth in Article 3 of the EC Treaty, «the activities of the Community shall include . . . an internal market characterised by the abolition, as between Member States, of obstacles to the free movement of . . . persons, services. » The internal market for auditing services would fall within the ambit of Treaty provisions dealing with the free movement of workers (Article 39) and, most notably, freedom of establishment (Article 43) and freedom to provide services (Article 49).

In practice, few statutory auditors appear to have taken advantage of the internal market. While firms of statutory auditors are often involved in international networks, the largest of which are the well-known “Big Five”, other firms scarcely have branches in other countries. Indeed, one might even question whether the apparent lack of interest of statutory auditors for moving their place of business in another Member State where the rules of civil liability are less severe is not a result of belief that such a move is not possible because of legal requirements with respect to establishment and the provision of services in other Member States, or at least not practical as a result of cultural and language differences, as well as differences in the accounting practices and company laws applicable to the audited companies and which the statutory auditors must take into account.

For this reason, the level of achievement of the internal market with respect to auditing services must be taken into consideration when trying to assess the impact of differences in the Member States' liability regimes. The actual means by which auditors may benefit from freedoms of establishment and/or services should also be expected to be determinant as to the effective way in which differences in liability regimes themselves may impact on the statutory auditors' benefiting or not from such freedoms.

In any event, it is necessary to identify at least some of these establishment and/or distance services situations likely to occur in order to consider the corresponding fact patterns against which jurisdiction and applicable law will be determined. This is because differences in liability regimes should logically only influence the statutory auditors' decisions as to their establishment or rendition of services in another Member State in light of whether Courts with jurisdiction will choose the applicable law among, *inter alia*, the law of the forum, that of the Member State of origin of the statutory auditor, or that of the Member State of the audited company.

Indeed, not only do statutory auditors not seem to presently take full advantage of the internal market, they do not appear conscious of the discrepancies between the various liability regimes. At this stage, their reaction vis-à-vis potential liability exposure appears limited to leading them to agree with audited companies on choice of law clauses or to contemplate refusing “high risk” clients, but barely impacting on their fees.

Thus, while this study confirms that quite significant differences exist among the Member States' legal regimes applicable to the civil liability of statutory auditors, the main differences being summarised below (3.1), their likely impact on the decisions of the interested professionals and firms should be considered in view of the legal background pertaining to the actual achievement of the internal market (3.2), on the one hand, and principles of jurisdiction and conflicts of laws (3.3), on the other.

3.1 Major Differences in the Civil Liability Regimes in the Member States

Though there are significant differences in the civil liability systems in the Member States, they must not be overstated.

First, in every Member State, a plaintiff in a civil liability action against a statutory auditor will have to prove that the statutory auditor did not meet the duty of care of a normally diligent auditor, having regard to professional regulations and norms established by the various professional organisations, and that such fault actually caused the injury reparation of which is sought. It even appears that, in all countries (except one in some specific instances), the rule is one of joint and several liability, meaning that each one of several defendants may be ordered to pay the whole amount of damages and that if a defendant pays more than his fair share of the damages, he can seek contribution from the other defendants.

Second, there does not seem to be a correlation between the harshness of the national civil liability systems and the number of actual lawsuits involving statutory auditors' liability. In many countries where the liability exposure of statutory auditors is significant (e.g., because there is no restriction on actions by third parties or no legal or contractual liability caps, or because statutes of limitations are relatively long), Courts have not, as of yet, been called upon to settle such claims or have only done so on limited occasions. On the contrary, in the United Kingdom, where limits on liability actions against statutory auditors are above average (the requirement of a « special relationship » vis-à-vis third parties, judicial prerogative to relieve the statutory auditor either wholly or partly from his liability based on equity, etc.), the examples of Court decisions imposing liability on statutory auditors are numerous and the amounts involved are often quite significant.

Subject to these important qualifications, major practical differences bear upon the issues of standing to sue, limitation periods and recovery. Insurance coverage and the interface with possible criminal prosecution must also be taken into account.

3.1.1 Standing to Sue

An important difference concerns the standing of third parties to bring liability actions against the statutory auditor. In a majority of Member States, the statutory audit is considered to be not only in the interest of the company, but also a question of public interest. As a result, any third party may recover damages from the statutory auditor upon proving the elements of the liability claim, usually fault, damages and causation.

However, in Common Law countries (Ireland and the United Kingdom) as well as Austria, Germany and Spain, the statutory auditor only owes a duty of care to the audited company itself and to the shareholders collectively in their capacity as members of the audited company. The statutory auditor will owe a duty of care to a person other than the audited company only if he assumes responsibility to that person for insuring the substantial accuracy of the accounts with regard to the facts of the particular case. This entails that the auditor knew or should have known that the claimant would rely upon his work and/or his report for a particular purpose.

3.1.2 Limitation Periods

Statutory limitation periods vary considerably from one Member State to another, from one to twenty years in length. In certain countries, a distinction is made between contractual actions and tort actions.

The statute of limitation starts running at different times depending on the Member State. Placed in order from the most favourable to the statutory auditor to the least favourable, the starting points are as follows: 1) signature of the report, 2) occurrence of the damage causing events, 3) occurrence of the damage, 4) occurrence of all the elements of the claim, 5) discovery of breach, 6) discovery of the damages and the liable person.

In some Member States, the starting point changes if the statutory auditor attempted to conceal the fault.

3.1.3 Limitations of Liability

Important differences also exist with regard to the possibilities of limiting liability: legal liability caps, contractual liability caps, forms of legal entities allowed to conduct statutory audits.

In three countries (Austria, Germany and Greece), a legal liability cap has been established. In Austria and Greece, the cap applies to claims by the audited company as well as by third parties. On the contrary, in Germany, the liability cap does not affect actions by third parties, except if damages are sought on the basis of a contract with protective effects.

In addition, the United Kingdom and Finland give Courts the power to reduce the amount of damages; in the United Kingdom, this power has never been used in practice.

In some countries, the statutory auditor may contract with the audited company to suppress certain obligations, to shorten the statutory limitations period and to establish a liability cap.

In all countries except Ireland, statutory auditors are allowed to adopt the structure of a limited liability company which protects the individual members from liability beyond their contribution to the capital. This allows partners who do not participate in the audit to shield themselves from civil liability. However, the effect of this rule is limited by the fact that in all Member States, except the Netherlands, an individual statutory auditor must sign the report of behalf of the auditing firm and is jointly and severally liable with the auditing firm.

3.1.4 Mandatory Insurance

In most Member States, statutory auditors are legally required to obtain and maintain insurance covering their professional activities. In three countries, where insurance coverage is not mandated by law, such coverage is nevertheless required by the professional supervisory bodies (Belgium, Ireland, United Kingdom). In the three remaining countries (Finland, Luxembourg, the Netherlands) it is common practice or it is recommended to maintain such coverage.

In countries where minimum coverage is required, such minimum coverage varies significantly. Nevertheless, the practical impact of this difference is somewhat limited by group insurance coverage available to members of the profession in amounts substantially higher than the minimum coverage in ten Member States.

3.1.5 Impact of Criminal Prosecution

Eight countries have specific criminal law offences pertaining to the activities of statutory auditors (including, *inter alia*, issuance of an inaccurate certification, failure to report violations of law and conflict of interest).

In all countries, the criminal offence requires that the conduct of the auditor be intentional and with knowledge of the inaccuracy, which distinguishes criminal liability from civil liability.

In nine Member States, the criminal action may be started not only by the public prosecutor, but also by the victim. Moreover, in two countries, the victim may commence proceedings if the public prosecutor refuses. The victim has the choice either to bring a civil suit or commence criminal proceedings. In certain countries, the victim may have an interest in opting for the criminal suit in order to take advantage of the public authorities' greater ability to investigate and collect evidence which would establish the fault of the statutory auditor. This takes on even more importance when it is considered in light of the fact that the criminal judgement has *res judicata* effect in the civil proceedings.

3.2 Impact of the Current State of Achievement of the Internal Market

The underlying query to this study is not limited to the impact of the differences in the civil liability regimes applicable to statutory auditors on any specific form of possible exercise of their freedoms on the Internal Market. Thus, all such forms are equally relevant, irrespective of whether they involve establishment or distance services, by individual auditors or auditing firms. A short reminder of the current situation will be helpful in analysing the impact of those differences.

3.2.1 Establishment

At this time, there is no specific European legislation harmonising the conditions for the establishment of statutory auditors within the European Union. Nevertheless, the Eighth Directive of April 10, 1984, concerning the professional qualifications of persons undertaking statutory auditing activities (OJEC 1984 L 126), which harmonises provisions concerning the education and training of statutory auditors, has considerably reduced the differences between the systems in the Member States.

In this context, Directive 89/48/CEE of September 21, 1988 (OJEC 1989 L 19), concerning the recognition of higher education diplomas, implements the principle of mutual recognition by allowing an individual with a professional title in one Member State to obtain an equivalent title in another Member State, which may set an aptitude test to be passed as a prerequisite. With regard to statutory auditors, it appears that all the Member States recognise the equivalence of diplomas, subject to successfully passing such an aptitude test, which generally covers the topics which present the most significant differences between the Member States' legislation.

In *Ramrath*, (CJEC, May 20, 1992, case 106-91, p. 3351), the Court of Justice held that a decision by Luxembourg to deny access to the profession to a statutory auditor certified in another Member State was contrary to freedom of establishment because this right includes the possibility of creating or maintaining more than one centre of activity within the European Union. CJEC, July 12, 1984, *Klopp*, case 107/83, p. 3877.

Thus, a statutory auditor of a Member State may create an establishment in another Member State where he qualifies, which can be achieved by successfully passing a simple professional aptitude test.

3.2.2 Cross-Border Services

Given the nature of certain activities, restrictions to the provision of services in a Member State are allowed if they are objectively necessary, justified by public interest and applicable to all individuals undertaking the same activity, provided that the interest is not protected by regulations which apply to the service provider in his Member State of origin. CJEC, February 26, 1991, *Commission v. Italy*, case 180/89, p. 709.

In this regard, the Eighth Directive allows Member States to determine the respectability and the independence of statutory auditors providing services in their territory, and the Court of Justice held that a Member State may, to this end, subject the rendition of auditing services by a statutory auditor from another Member State to prior certification, require that the statutory auditor have a permanent infrastructure for the completion of the work and an effective presence, and adhere to the professional ethical rules of the Member State. However, such requirements are not objectively necessary when the statutory auditor, being established and certified in another Member State, temporarily provides services under cover of a statutory auditor of the Member State where the audit is taking place, because compliance with local regulations may be through the individual or legal entity which is subject to its laws. CJEC, May 20, 1992, *supra* p. 104.

As a result, a statutory auditor who is certified in one Member State must be able to provide his services in another Member State, either with a certification subject to requirements of a permanent infrastructure and an effective presence, or under the control and responsibility of a statutory auditor of the other Member State.

3.2.3 Auditing Firms : Establishment and Cross-Border Services

The freedom of establishment includes the right for an auditing firm to establish a branch or subsidiary in another Member State. As is the case for individuals, such an auditing firm must be certified, which implies that its members have the professional qualifications required by the Member State. According to *Ramrath*, auditing firms may establish in other Member States by creating a local auditing firm made up of certified statutory auditors in the Member State in question, and for which foreign statutory auditors could work. However, problems may arise from national requirements of capital ownership, management and control.

Likewise, problems similar to those encountered by individual auditors would seem to arise for firms of one Member State who send a statutory auditor of their Member State to another Member State where they have no establishment. As the Court of Justice stated in *Ramrath*, even when providing services, the conditions of a sufficient permanent infrastructure and an effective presence are justified by the necessity to protect the public interest concerning the respectability and independence of statutory auditors.

At this stage, the internal market for statutory auditing services is, therefore, rather compartmentalised and consists largely of national markets supervised by national legal structures making the mobility of statutory auditors very limited.

3.3 Jurisdiction and Choice of Law, the Link Between the Differences and the Statutory Auditors' Decisions

One should not infer from the existence of significant differences between the liability regimes applicable to statutory auditors in the various Member States that the statutory auditors themselves would enjoy the more favourable such regimes automatically as a result of moving their headquarters into the Member States where favourable regimes are in force or by rendering their auditing services from an establishment in such Member States. Just as hasty would be the conclusion that they would benefit from such Member States' less stringent laws when auditing companies based therein. Any other similar guess or belief must be equally questioned.

Which Member State's law applies is a legal question to be resolved by rules of conflicts of laws, most of which themselves depend on the country where a lawsuit is brought. Thus, choice of Court considerations must be taken into account before the law applicable to a given situation can be ascertained.

3.3.1 Jurisdiction over Liability Actions Against Statutory Auditors

As is the case with any cross border provision of services, the statutory audit in the context of the Internal Market presents jurisdictional issues which would arise in the case of an auditing firm domiciled in one Member State while the audited company or an injured third party is located in another Member State.

In such a case, the audited company or the injured third party should be expected to bring its claim in a forum likely to entail the application of a law providing the possibility of recovering a maximum amount of damages. The statutory auditor, on the other hand, would look to apply a law favourable to any defence he may have, e.g. which provides for a cap on liability or places a heavier burden on the plaintiff with regard to proving the elements of his claim, so that if the rules of conflict of laws of the forum lead to the application of a law unfavourable to his interests, the statutory auditor will attempt to challenge the jurisdiction of the Court in which the litigation was brought.

The relevant rules of jurisdiction of the national Courts in the European Union, at least when the defendant to a lawsuit is domiciled in a Member State, are mostly set forth in the Brussels Convention of 28 September 1968 on Jurisdiction and the Enforcement of Foreign Judgements, as modified («Brussels Convention»). However, it must be noted that a proposal for a Council regulation was submitted on 14 July 1999, whose goal is to «uniformise the rules of private international law in the Member States relating to jurisdiction.... ». This regulation would substitute the Brussels Convention and modify certain of its aspects, although it would not have a significant impact on the analysis below.

Article 5.2 of the Brussels Convention provides that the Member State in which a company or legal entity has its seat has exclusive jurisdiction over issues concerning the «validity of the constitution, the nullity or the dissolution of companies ... or the decisions of their organs ». This article does not provide a definition of the «seat » of the company (either the principal place of business or the registered office), the determination of which is left to the decision of

the Court before which the case is brought, according to its conflict of law rules. H. GAUDEMET-TALLON, *Les conventions de Bruxelles et de Lugano*, 1996, 2nd edition, n° 93, and Article 22.2 of the proposed regulation. Since exclusive jurisdiction on this basis only covers the creation and governance of the legal person, it does not appear to be applicable to issues involving the civil liability of its statutory auditor. It may, however, apply to decisions of the company related to his mission (e.g. nomination, termination).

Except in the case of exclusive jurisdiction, the parties may enter into a choice of Court agreement, which is given effect by Article 17.1, subject to certain conditions as to the form of the agreement.

In other relevant instances, the Courts of the Member State in which the defendant is domiciled have jurisdiction over actions brought against the defendant under Article 2 of the Brussels Convention. In the case of an incorporated auditing firm, the domicile would be its seat. Therefore, a liability action may always be filed in the Courts of the Member State of the domicile of the individual statutory auditor or of the seat of the auditing firm.

As an alternative to the jurisdiction of the Courts of the Member State where the statutory auditor has his domicile, Article 5 of the Brussels Convention provides for certain specific bases for jurisdiction in given situations, upon which the plaintiff may choose to rely, such as where the action is based in *contract* or in *tort*, or arises in *criminal proceedings*.

Article 5.1 provides the rule for jurisdiction over *contractual* matters. The Court of Justice has ruled that the term «contractual matters» has a meaning which is independent of any similar notion in the law of the Member States. CJEC, March 22, 1983, *Martin Peters*, case 34-82. The Court has not provided a specific definition, but has identified certain factors to be considered, such as whether the basis of the complaint is the contract itself and, consequently the breach thereof. CJEC, June 17, 1992, *Jacob Handte*, case 26/91. Liability incurred towards the audited company in the performance of the statutory auditor's mission could fall within this category. The rule under Article 5.1 is that jurisdiction lies with the «Courts for the place of performance of the obligation in question.» If the parties have specified no place of performance, the Court before whom the case is brought according to its conflict rules determines it. CJEC, October 6, 1976, *Tessili*, case 12/76. The proposed regulation attempts to unify the definition of the place of performance and, thereby, avoid the inconsistencies that the *Tessili* decision triggered, by providing that the place of performance is «the place in a Member State where under the contract the services were provided or should have been provided.» Since the statutory auditor's services involve the review of the audited company's accounts which are held in the country of the company and are provided to its governing body, it would appear that an appropriate forum would be the Courts of the principal place of business or registered office of the audited company.

For claims grounded in *tort* (including in delict or quasi-delict), the appropriate forum is in the Courts of the place «where the harmful event occurred or there is a risk of occurring.», under Article 5.3 of the Brussels Convention. The Court of Justice has held that the plaintiff in tort may bring an action in the Courts of the place where the event took place or those of the place where the injuries occurred. CJEC, 30 November 1976, *Mines de Potasse d'Alsace*, case 21/76. However, the plaintiff who suffers injuries as a result of a tortious event in one Member State and subsequent damages in another Member State can only sue in the forum where the event or the initial injuries occurred. CJEC, 19 September 1995, *Antonio Marinari v. Lloyd's Bank plc and Zubaidi Trading Company*, case C 364/93 ; see, in general, H.

GAUDEMET-TALLON, *supra*, n° 191. In addition, the plaintiff who suffers injuries as a result of those suffered by another victim can only sue in the Member State where such other, direct victim, suffered its own loss. CJEC, 11 January 1990, *Dumez France v. Hessische Landesbank*, case C 200/88 ; H. GAUDEMET-TALLON, *supra*, n° 192. Thus, in the situation where a plaintiff claims some financial loss, he would be able to litigate in the Member State where he has his domicile only if his financial loss is not the result of some other, direct injury that occurred in the Member State of the company, e.g. not in the case of a shareholder's loss resulting from injury occurred in the corporate accounts.

In the case of a *criminal action*, Article 5.4 provides that the defendant domiciled in one Member State may be sued « as regards a civil claim for damages or restitution which is based on an act giving rise to criminal proceedings, in the Court seized of those proceedings. » This jurisdictional basis is limited, however, « to the extent that that Court has jurisdiction under its own law to entertain civil proceedings. » Jurisdiction under this Article could play an important role in litigation of claims involving statutory auditors as a result of the large variety of criminal actions to which statutory auditors are subject. However, jurisdiction over criminal actions themselves is not governed by the Brussels Convention, but by Member States' specific rules. These would apply where a collateral claim for damages is brought in the criminal Court.

It is also worth noting that, under Article 8 of the Brussels Convention, an insurer can be sued in the Courts of his domicile or of the domicile of the policyholder. In addition, Article 9 extends the rule with respect to liability insurance to the place where the harmful event occurred.

3.3.2 The Law Applicable to the Statutory Auditors' Liability

The law applicable to the statutory auditor's liability is determined in quite different ways in *contract* matters, on the one hand, and in *tort*, including delict or quasi delict, on the other hand. Indeed, while rules of conflicts may seem simpler in the latter case, the outcome does not appear to be more predictable.

The general rule for actions brought in *tort* by either third parties or, in some Member States, by the audited company, is that the applicable law would be the law of the place of the tort (*lex loci delicti*). This rule would, in most cases, give rise to the application of the law of the audited company, as that of the country where the accounts are held and reviewed in performance of the statutory audit. The injury would also most frequently be sustained in the same country. However, there is an important issue as to whether the *lex loci delicti* is that of the place where the fact that led to the damage occurred, or that of the place where the injury was sustained, when they are different. In the latter case, it could exceptionally lead to the application of a foreign law, e.g. with respect to the audit of consolidated accounts.

Where a financial loss is sustained in a different country from that of the audited company, the question therefore arises of whether the Court may apply the law of the country where the loss is sustained rather than that of the country where the audit took place, just as with respect to jurisdiction. There is no settled case law on this issue in many Member States, and scholars present arguments both ways. Should the application of some other law than that where the act occurred be considered, it is sometimes believed that it should be that of the country where the injury is sustained (see, e.g., Pierre MAYER, *Droit International Privé*, Editions

MONTCHRESTIEN, 6è éd., Paris, 1998, n° 685), but more probably that it should be the proper law of the tort, i.e. that of the country with which the situation has the closest relation, (See, e.g. Bernard AUDIT, *Droit International Privé*, ECONOMICA, Paris, 1991, Nrs. 185 et seq.), which would likely again lead to the law of the company.

The situation with respect to the law applicable to a liability action against a statutory auditor based in *contract* is perhaps even more complex.

The Rome Convention of June 19, 1980 has progressively replaced the Member States' conflict of law rules with respect to contracts within the European Union. However, certain conflict issues do not fall within its scope. Article 1 (2)(e) provides that the Convention does not apply to «questions governed by the law of companies and other bodies corporate or unincorporated such as the creation, by registration or otherwise, legal capacity, internal organisation or winding up of companies and other bodies corporate or unincorporate and the personal liability of officers and members as such for the obligations of the company or body. »¹¹⁹ According to a report by Professors Giulano and Lagarde (OJEC C 182, 31 October 1980), this exception «covers all complex acts (contractual, administrative, registering) required for the creation of a company or regulating its governance or its dissolution, in other words, acts having their origin in company law. » With respect to governance issues, this exception covers «the general meeting of shareholders, voting rights, quorum, the nomination of the company's directors and officers. »

Since the nomination and the mission of the statutory auditor are covered within the company law of each Member State, the application of the Rome Convention to the liability of a statutory auditor is probably not possible. Indeed, it is the law of the country where the company has its headquarters, or where it was incorporated, which would generally apply to these issues.

In the unlikely event that the Rome Convention would nevertheless be held applicable, there would seem to be possibilities that the law of the company not be deemed applicable to the statutory auditor's liability:

- Article 3 of the Rome Convention sets forth the fundamental rule, which is a principle of conflicts of law in every Member State of the European Union and most other countries¹²⁰, that a «contract is governed by the law chosen by the parties. » In light of this rule, it is interesting to consider the possibility of the statutory auditor agreeing with the audited company to make the law of his or a third country applicable to the contract, as opposed to that of the country of the company ;
- likewise, in cases where the parties have not chosen an applicable law, the general rule set forth in Article 4 of the Rome Convention, is that the applicable law is that of « the country with which [the contract] is most closely connected », which is deemed to be the law of the principal place of business of the debtor of the characteristic prestation. Under such a rule, in a contract for the performance of auditing services, the law of the statutory auditor would apply.

Yet, it may appear difficult to apply another law than the audited company's to the statutory auditor's mission, given the fact that the requirement to have a statutory audit is a matter of the audited company's law and that the scope of the mission depends on the national law relating to the creation, the operation and the dissolution of the audited company. Though this

question has never been addressed by Courts in at least several Member States, probably because the markets for auditing services are still very much national in nature at this stage, from this point of view, it would seem more logical to apply the *lex societatis* to the scope of the auditor's mission and his obligations. Indeed, such analysis would corroborate that under which the Rome Convention would not apply to the issues pertaining to the liability of statutory auditors. Indeed, even where the action is brought by the audited company, and where such action is of a contractual nature, there are rules of conflict of law which may lead to the application of the *lex societatis*, e.g. as the result of the nature of the law in question (e.g. public interest) or of the national rules of conflicts which give jurisdiction over questions concerning companies to the forum of the principal place of business of the company (e.g. Article 1837 of the French Civil Code which provides that «every company having its principal place of business situated in the French territory is subject to the provisions of French law. »)

Conclusion

This study confirms, to a large extent, the results of prior works with respect to differences among the Member States' civil liability regimes for statutory auditors.

Differences are indeed significant, and bear upon the most diverse and profound features of such legal regimes, to the extent that their very underlying policies may in some respects appear dissimilar, or at least, not equally intense. A clear example of such significant differences lies in the legal nature of the liability action brought by the audited company itself against the statutory auditor, which may be either in contract or in tort. Another important difference concerns the standing of third parties to bring liability actions against the statutory auditor. At the other end of the legal reasoning, statutes of limitation vary not only by the length of the limitation period, as one might expect, but also by the starting point, with remarkable practical consequences. Differences with regard to the possibilities of limiting liability cannot be ignored, whether they concern legal or contractual liability caps, or forms of legal entities allowed to conduct statutory audits.

The overall practical impact of differences in such legal regimes should not be overemphasised, as they all require a showing that the statutory auditor somehow failed to carry his duties as required. In addition, at this stage at least, the frequency of actual court cases does not seem to correlate with the harshness of the applicable legal regime.

Likewise, civil liability regimes are an increasing concern for statutory auditors, at least in some Member States where litigation underway involves very large claims for damages, in the millions, and even in the billions, of euros. However, statutory auditors do not seem ready to take drastic steps to modify their practices as a response to this increasing threat, at least by somehow changing the location of such practices. At this stage, their reaction vis-à-vis potential liability exposure appears limited to leading them to agree with audited companies on choice of law clauses or to contemplate refusing "high risk" clients, but it barely impacts on their fees.

In addition, few statutory auditors appear to have actually taken advantage of the internal market. International networks, such as the "Big Five", do not rely on the internal market *per se*: rather, they are structured as associations of local firms. Other firms scarcely have branches in other countries. Indeed, it may be that the apparent lack of interest of statutory auditors for moving their place of business in another Member State where the rules of civil liability are less severe is a result of their belief that such a move is not possible because of legal requirements with respect to establishment and the provision of services in other Member States. Cultural and substantive legal differences in accounting and company law further frustrate any such plans.

Another perplexing factor lies in the fact that differences in liability regimes should logically only influence the statutory auditors' decisions as to their establishment or rendition of cross-border services in light of the applicable law that Courts with jurisdiction will choose among, *inter alia*, the law of their Member State of origin or that of the Member State of the audited company. However, the rules on jurisdiction and applicable law with respect to statutory auditors' liability are all but settled. In addition, such legal issues are traditionally of limited visibility for businesses. Thus, statutory auditors are unlikely to take enlightened decisions, should they consider taking advantage of the internal market for liability purposes.

In a majority of situations at least, not surprisingly, the law of the audited company seems to have the best chances of being applied, irrespective of other factors. Thus, there would seem to be little advantage for statutory auditors in moving their practice or establishing it in some location rather than another.

The cross-border auditing of companies may raise more interesting questions. Audited companies might seek competitive offers from statutory auditors based in various Member States in an effort to obtain lower prices for audited services by reason of the liability regimes being different. However, prices may not be very different, since the same liability regime has the greatest likelihood of being applicable, that of the audited company itself. Thus, differences in liability regimes would not be a significant source of competitive disadvantage between statutory auditors of different Member States. Any competitive advantage or disadvantage would have at most indirect and minimal effect, such as through differences in insurance premiums based on the statutory auditors' exposure to liability being mostly under the liability regime in force on his home market, assuming a major part of his practice is in such home market.

More likely is a competitive disadvantage suffered by audited companies themselves as a result of being governed by national laws whose liability regimes are unfavourable to statutory auditors. In other words, a company that is located in a Member State where such a harsh liability regime applies may be charged more for auditing services than its competitor from a Member State whose legal environment is more favourable.

Obviously, the position should be reconsidered if rules of jurisdiction and applicable law become more favourable to the application of a liability regime other than that of the Member State where the audited company has its seat or was incorporated, and even more if such favour becomes visible to statutory auditors, so that they do take it into account in making strategic decisions as to the location of their practice. Also, the progressive achievement of the internal market for statutory auditors through the improvement of relevant European legislation should trigger more cases likely to give rise to situations where differences in liability regimes become more crucial.

In the meanwhile, the differences between liability regimes appear to produce most of their effects, if any, on another market than that of auditing services, namely at the level of audited companies.

Notes

¹ For the purposes of this study we will use the following abbreviations for the Member States :

Austria :	Aus	Italy :	Ita
Belgium :	Bel	Luxembourg :	Lux
Denmark :	Den	The Netherlands :	Ned
Finland :	Fin	Portugal :	Por
France :	Fra	Spain :	Spa
Germany :	Ger	Sweden :	Swe
Greece :	Gre	United Kingdom :	UK
Ireland :	Ire		

² Buchprüfer are limited to statutory audits of private limited liability companies and general and limited partnerships when all of the unlimited liability members are private limited liability companies. Wirtschaftsprüfer may undertake any statutory audit.

³ Registrerede Revisorer must be registered with the Danish Commerce and Companies Agency and may perform statutory audits of small and medium sized private limited liability companies, incorporated partnerships, general and limited partnerships when all the members are either public or private limited liability companies and small and medium sized non listed public limited liability companies. « Small and medium-sized » is defined as not exceeding two of the following for two consecutive years: turnover of 100 million DKK (approximately 13.4 million euros), assets of 50 million DKK (approximately 6.7 million euros), more than 250 employees. Statsautoriserede Revisorer must be licensed and registered with the Danish Commerce and Companies Agency and may conduct any type of statutory audit. The rules governing statutory auditors apply to both Registrerede Revisorer and Statsautoriserede Revisorer.

⁴ KHT auditors may conduct any statutory audit. HTM auditors may only undertake statutory audits of small and medium-sized non-listed entities requiring a statutory audit. They may also participate in statutory audits of larger entities in cooperation with a KHT auditor. « Small and medium-sized entities » cannot exceed for two consecutive years two of the three following criteria : assets over 150 million FIM (approximately 25 million euros), more than 300 employees, Total turnover of more than 300 million FIM (approximately 150 million euros). The rules governing statutory auditors apply to both HTM and KHT auditors.

⁵ Wirtschaftsprüfer may conduct any statutory audit. Vereidigte Buchprüfer are limited to statutory audits of medium-sized private limited liability companies. « Medium-sized » companies exceed at least two of the following criteria : balance sheet total of at least 5,310,000DM (approximately 2.7 million euros), total turnover of at least 10,620,000DM (approximately 5.4 million euros), an average of 50 employees during the year. Further «medium-sized » companies cannot exceed two of the following three criteria : balance sheet total of 21,240,000DM (approximately 10.8 million euros), 42,480,000DM (approximately 21.6 million euros) in total turnover, an average of 250 employees during the year. The rules governing statutory auditors apply to both Wirtschaftsprüfer and Vereidigte Buchprüfer.

⁶ Statutory auditors are elected annually at the general meeting of the shareholders of the company and are either Common Auditors or Chartered Auditors. Common Auditors must be at least 30 years old, have a university degree and have five years experience. Chartered Auditors are members of the Corps of Chartered Auditors established by Presidential Decree n°226/1992 and must be a Greek or EU national with their permanent residence in Greece, have a university degree in economics, commercial or industrial studies by a Greek or recognized foreign university and be persons of «impeccable morality and virtue. ». Public limited liability companies and private limited liability companies can be audited either by four common auditors (two regular and two alternate) or by two chartered auditors

(one regular and one alternate). However, the law provides for specific categories of companies that must be audited by chartered auditors.

⁷ In Italy, the statutory audit requires the participation of two different auditing bodies : the Board of Auditors (*collegio sindacale*) and the Auditing Firm (*società di revisione contabile*). The Board of Auditors is a requirement in all companies where auditing is mandatory (joint-stock companies and limited partnerships with share capital with a minimum registered capital of 200 million lire (approximately 103,000 euros) or as low as 20 million (approximately 10,300 euros) if the appointment of a board is required under law or if the company has exceeded two of the limits specified in Article 11 of the Fourth Directive (Article 2435b Civil Code)). The Auditing Firm undertakes the certification of the balance sheet of companies listed on regulated markets.

⁸ The Réviseurs d'entreprises' scope of work are companies filling two of the three following conditions : total balance sheet exceeding 93 million LUF (approximately 2,3 million euros), turnover of minimum 186 million LUF (approximately 4,6 million euros), or more than 50 employees. The remaining companies are audited by a commissaire aux comptes.

⁹ Until 1993, only registeraccountants (« RA ») were qualified to audit the annual accounts of companies. Now, administratieconsulenten (« AA ») may also conduct such audits if they meet various specific professional qualifications. In practice, not many AAs audit annual accounts and when they do it is limited to smaller companies.

¹⁰ Auktoriserade Revisorer may conduct any statutory audit. Godkända Revisorer are only allowed to carry out statutory audits of small and medium-sized non-listed limited liability companies and small and medium-sized general and limited partnerships when all of the unlimited liability members are limited liability companies. « Small or medium-sized » is defined as not exceeding one of the following two criteria : assets of 35 million SEK (approximately 4.2 million euros), over 200 employees.

¹¹ Section 275 of the HGB provides as follows :

« (1) The auditor, his assistants and the auditing company's legal representatives, who participate in an audit, are obliged to conduct a conscientious and impartial audit and are bound to observe confidentiality. They must not make use of business or operating secrets that they encountered in the course of their activity, without authorisation. Who intentionally or negligently breaches his duties is liable towards the company and, if an affiliated company is harmed, he is also liable towards this company for the damage resulting therefrom. Several persons are jointly liable.

(2) The liability for damages caused by persons who acted negligently is restricted to ATS 5 million, per audit. This applies also when several persons participated in an audit or several acts were committed that result in liability for damages, this is irrespective of whether other participants acted intentionally.

(3) If the auditor is an auditing company the confidentiality obligation exists also towards the supervisory **board** of the auditing company as well as its members.

(4) The liability under these provisions can neither be excluded nor limited by means of a contract.

(5) Claims arising under these provisions are subject to a limitation period of 5 years. »

¹² Article 9bis of the law of 22 July 1953 provides as follows :

« Statutory auditors are responsible for completing their mission in accordance with the general principles of law. »

¹³ Article 64 octies of the LCSC provides as follows :

« Auditors are liable to the company for all faults committed in the exercise of their activity. They are jointly and severally liable to the company and to third parties for all damages resulting from violations of the provisions of the [various company laws] or the corporate articles or by-laws. They can only be discharged from liability for faults in which they did not participate if they prove that they

completed their mission with the normal diligence of their position and that they reported the faults in question to the board of directors and, if no adequate action was taken by the board of directors, at the next shareholders' meeting after learning of the fault. »

¹⁴ Section 44 of the TTL provides:

« If in the course of performing his duties the auditor has wilfully or negligently caused damage to the company or trust, the auditor is liable to compensate such damage. The same applies to damages which have been caused to a shareholder, a partner or a member of the company or trust or to any third person by violation of this law, violation of law applicable to the company or trust or violation of statutes or rules of the company or trust. The auditor is also liable for damages caused by his assistant wilfully or negligently.

If the auditor is a certified firm of auditors, both such firm and the auditor, who has the main responsibility of performing the audit, are liable for damages.

As to making liability equitable and the division of liability between one or more defendants, the Act on Liability, Chapters 2 and 6 apply. »

¹⁵ Article 234 of the Company Law of 24 July 1966 provides:

« Auditors are liable to both the company and third parties for damages which are caused by their faults or negligence in the performance of their duties. However, auditors are not liable for information or facts disclosed in furtherance of their mission as defined in Articles 230-1 and 230-2 of this law.

Auditors are not liable for the criminal offences of any directors of the company unless, having knowledge of the criminal offences, the auditors did not disclose them to the shareholders in their report. »

¹⁶ Under §823 II BGB a person who infringes a statutory provision intended for the protection of others is liable for any damage arising from the infringement. Whether or not the particular plaintiff is included within the protective ambit of the violated statute depends upon its interpretation in the light of the legislative intent. The statute was designed to protect the victim as an individual or as part of certain groups of individuals rather than a member of the public at large. The Courts have recognised that some statutes defining the auditor's duties are statutory provisions intended for the protection of others, such as certain provisions in the HGB (§§ 332, 333), in the Stock Corporation Act (§§ 403, 404) and also in the Criminal Code (§§ 263, 264a, 266 283 et seq. StGB).

In addition, an auditor can be liable under § 826 BGB for intentional and immoral harm. Under this statute, liability arises from intentionally causing harm to another in a manner that is contrary to "good morals".

¹⁷ Article 323 HGB states in pertinent part:

« (1)The auditor, his assistants and the auditing company's legal representatives, who participate in an audit, are obliged to conduct a conscientious and impartial audit and are bound to observe confidentiality. They must not make use of business or operating secrets that they encountered in the course of their activity, without authorisation. Who intentionally or negligently breaches his duties is liable towards the company and, if an affiliated company is harmed, he is also liable towards this company for the damage resulting therefrom. Several persons are jointly liable.

(2)The liability for damages caused by persons who acted only negligently is restricted to 2,000,000 German Marks, per audit. In case of an **audit** of a Stock Corporation which issued stocks with an official quotation, the liability of persons who acted negligently is, deviating from **phrase 1**, limited to 8,000,000 German Marks. This applies also when several persons participated in an audit or several acts were committed that result in liability for damages, this is irrespective of whether other participants acted intentionally.

(3)If the auditor is an auditing company the confidentiality obligation exists also towards the supervisory **board** of the auditing company as well as its members.

(4) **The liability under these provisions can neither be excluded nor limited by means of a contract.**

(5) **Claims arising under these provisions are subject to a limitation period of 5 years. »**

¹⁸ Codified Law 2190/20 provides :

« In discharging their duties, auditors shall be held responsible for any fault, being liable for the payment of damages to the company. The liability referred to in this paragraph may not be excluded or modified. Any claim of the company due to such liability shall have a statute of limitations of two years. »

¹⁹ Article 19 of the Presidential Decree provides :

« The Chartered Auditor is liable for any damage resulting from his actions or omissions during the audit and the issue of the audit certificate, if such damage is due to wilful misconduct or gross negligence of the auditor and it is caused by the use of the audit certificate.

The Chartered Auditors liability cannot exceed an amount equal to the quintuple of the annual salary of the President of the Supreme Court or the total amount of fees received by the statutory auditor during the previous fiscal year, whichever is higher. For auditing companies and joint ventures, the above limitation of liability concerns each partner or shareholder individually. Such auditing companies shall always be held jointly and severally liable with the partner or shareholder who caused the damage. »

²⁰ Article 2407 Civil Code provides :

« Auditors shall perform their duty with the diligence of an agent, they are responsible for the truth of their declarations and shall not reveal any information which they learn while performing the audit. They are jointly and severally liable with the directors for all acts and omissions by the directors if the damages suffered would not have arisen if they had not breached their duty of care. »

Under Italian law, two standards of diligence in performing obligations are generally referred to: an ordinary standard of diligence (*bonus pater familias*) and a professional standard of diligence (“*mandatario*” or agent).

²¹ Article 164 of the legislative decree of 24 February 1998 provides :

« The provisions of Article 2407, para. 1 of the Civil Code are applicable to auditing firms.

The person responsible for the audit as well as the employees who undertook the mission are jointly and severally liable with the auditing firm for damages suffered as a result of their breach of duty or for any offences towards the audited company or any third party who suffered damages. »

²² Article 1142 provides:

« Every obligation to do or refrain from doing an act shall be compensated by damages in case of breach. »

²³ Article 1382 sets forth the classic Civil Law rule on tort liability:

« A person shall remedy any damage to another person caused by his actions. »

Finally, Article 1383 provides:

« Each person is liable for all damage caused not only by his actions, but also by his negligence or imprudence. »

²⁴ Article 483 §1 of the Civil Code provides :

« Whosoever that, intentionally or negligently, violates the rights of another person [“*direito subjectivo*” or “*absolute right*”] or legal provisions designed to protect the interests of others, must compensate the injured party for the damages arising from the violation. »

²⁵ Article 78 CSC states that statutory auditors are liable to creditors of the company when, as a result of non-observance of legal or contractual provisions aiming to protect creditors, the company’s assets become insufficient.

Article 81 CSC establishes that the members of the statutory auditing committee (a committee, called *Conselho Fiscal*, composed of at least two statutory auditors or auditing firms which is, in some cases

required by law) have joint and several liability with the managers and directors of the company for breaches of duty.

Article 82 CSC states that statutory auditors are liable towards the company and its shareholders for the damages caused by their intentional or negligent behaviour. They are jointly and severally liable with the managers or directors of the company. Article 82 CSC Par. 2 states that Statutory Auditors are liable towards creditors under the terms of Article 78.

²⁶ Article 10 of the *Codigo de Mercado de Valores Mobiliarios* mentions that, whenever independent auditors intentionally or negligently cause damages to entities that issue shares, to investors and to third parties, they are all (the auditing firm, its respective partners and the associates who have signed the reports) “ jointly and severally ” and unlimitedly liable for the damages.

²⁷ Article 13 of the *Codigo de Proceso Tributario* states that whenever the assets of a company are not sufficient to pay off its taxes, the members of the Statutory Committee and statutory auditors are subsidiarily liable. Their subsidiary liability is “joint and several” with the directors and managers of the company. However, statutory auditors and members of the statutory committee are only liable if the tax authorities prove that the breach of tax duties by the company resulted from the non-fulfilment of their legal audit duties.

²⁸ Article 11:

« 1) The auditors shall be directly, jointly and severally liable with regard to the audited companies or entities and to third parties, for the damages caused by the breach of their duties.

2) When the audit is carried out by an auditor belonging to an auditing company, both the auditor and the company shall be liable in accordance with paragraph 1. The remaining auditing partners that have not signed the audit report shall be subsidiarily liable for the said damages, jointly and severally among themselves. »

Article 12 :

« Without prejudice to the unlimited civil liability for the damages they may cause when carrying out their activity, the auditors and the auditing companies shall have to post a bond (...).»

²⁹ Article 42 :

« 1) The auditors shall be directly, jointly and severally, and unlimitedly liable with regard to the audited companies or entities and to third parties, for the damages caused by the breach of their duties.

2° When the audit is carried out by an auditor belonging to an auditing company, both the auditor and the company shall be liable in accordance with paragraph 1. The remaining auditing partners that have not signed the audit report shall be subsidiarily liable for the said damages, jointly and severally among themselves. »

Article 45 :

« Civil and criminal liability-

The civil or criminal liability in which the auditors and the auditing companies may incur, if any, shall be enforceable in accordance with laws. »

³⁰ Chapter 15 Section 2 of the Swedish Companies Act provides :

« An auditor ... is liable in damages on the grounds mentioned in Section 1. He is also liable for damages caused intentionally or negligently by his assistants... If a registered auditing company is auditor...this company and the individual in charge of the audit are liable. »

Section 1 to which it refers, provides:

« An incorporator, board member or managing director who, when carrying out his assignment, intentionally or negligently damages the company shall be liable for the damage.

The same applies when damage is caused to a shareholder or someone else through the infringement of this Act, applicable annual accounts legislation or the articles of association. »

³¹ In the case of *Hedley Byrne v. Heller* ([1964] AC 465 House of Lords), Lord Hodson stated: « if in a sphere where a person is so placed that others could reasonably rely upon his judgment or his skill or upon his ability to make careful inquiry such person takes it upon himself to give information or advice to, or allow his information or advice to be passed on to another person who, as he knows or should know, will place reliance upon it, then a duty of care will arise. » ([1964] AC 514).

³² Recent decisions of the House of Lords (*Henderson v. Merrett Syndicates Ltd* [1995] 2 AC 145, *Williams v Natural Life Health Foods* [1998] 1 WLR 830) have shed light on the principle of the « special relationship ». The theoretical features of the concept have been further precised by the House of Lords as follows : (i) the theoretical basis of the principle recognised in the *Hedley Byrne* case is one of “assumption of responsibility”; (ii) it must be appreciated through an objective test, whether the defendant by what he said and did reasonably conveyed (directly or indirectly) to the claimant that he assumed responsibility to the claimant for the relevant statement or service; (iii) it applies to any assumption of responsibility for the provision of services whether or not they involve financial loss.

³³ *Caparo Industries Plc v. Dickman* ([1990] AC 605, House of Lords): the claimant in that case bought shares in the audited company shortly before the publication of its annual accounts and then bought further shares allegedly in reliance on the audited accounts. The claimant argued that because the auditors should have foreseen that a potential investor might rely on their report in deciding to buy shares in the company, especially since the company’s affairs were such as made it highly likely to attract a take-over bid, and because the claimant was already a shareholder in the company when it bought the further shares, there was the necessary “special relationship” whereby the auditors owed it a duty of care.

The House of Lords rejected this argument. They held that the extent of the duty of care which the auditor owes simply by reason of carrying out the audit and making his report is limited by reference to the purpose for which the statutory audit is performed. The purpose for which the Companies Act requires the auditor’s report to be provided to shareholders is to assist them in the proper management of the company; it is not to assist them in making individual decisions as to future investment in the company.

The effect of *Caparo* is that the auditor does not owe a duty of care, except in special cases, to shareholders in their individual capacity as investors in the company and even less to non shareholders contemplating investment in the company (for example lenders, trade creditors, employees, guarantors,...). The House of Lords applied the rule in *Al Saudi Banque v. Clarke Pixley* [1990] Ch 313, where it was held that the auditor owed no duty of care to a bank which lent money to the audited company.

³⁴ In *Barings plc v. Coopers & Lybrand*, it was held that a holding company may recover damages for loss in the value of its subsidiary resulting directly from a breach of duty owed to the company itself, as distinct from a duty owed to the subsidiary. In *Peach Publishing Ltd. v. Slater & Co.* (1999), the Court of Appeals allowed an appeal of an order by the Trial Court holding that the statutory auditor owed a duty of care in making assurances as to the soundness of the accounts to a prospective buyer of the company’s (statutory auditor’s client) accounts.

In *Yorkshire Enterprise Ltd. et al. v. Robson Rhodes*, ([1998] QB, High Court), the High Court held the statutory auditors liable for negligently misinforming a company which was considering investing in the audited company. The “special relationship” arose from the fact that the statutory auditors were aware of the purpose of the request for information and that reliance on the information was foreseeable.

Finally, in *Electra Private Equity Partners v. KPMG Peat Marwick* (1999), the *Caparo* rule was applied by the Court of Appeals. This case involved a plaintiff who hired an auditing firm to perform due diligence work and to investigate the target company. The auditing firm contacted its associate firm (the defendant) which acted as the statutory auditor of the target company to obtain information about the company. The associated firm knew why and by whom the information was requested and that the plaintiff would rely on the information in making its decision whether to purchase a majority

interest in the target company. The trial Court dismissed the claim as stating no cause of action. The Court of Appeals overturned this ruling holding that there was a « *triable issue, not just as to whether [the defendant] knew or foresaw the purpose for which the [plaintiff] required the accounts, but whether it assumed responsibility for their accuracy in providing them to the [plaintiff] in the circumstances alleged.* »

³⁵ In *Kelly v. Boland* ([1989] IRLN 373), the Court held that a statutory auditor owed a duty of care to the purchaser of the audited company because the auditor had been made aware that there were potential purchasers including the Plaintiff. In two previous years, the auditor was not aware of any potential purchasers and therefore not liable; however, in the third year he knew or ought reasonably have known that his report would be relied upon by a purchaser.

³⁶ Such was recently confirmed by the Rotterdam District Court. Rb Rotterdam, 19 November 1998, JOR 1999, 31.

³⁷ Such an “information contract” was especially concluded if the person obtaining the information placed specific trust in the auditor as a person of special competence. BGH VI ZR 184/70, judgement of 18 January 1972, WM 1972, pp. 466-468; BGH VII ZR 259/77, judgement of 22 March 1979, WM 1979, pp. 530-533.

³⁸ BGH VI ZR 73/84, judgement of 17 September 1985, WM 1985, pp. 1531-1533. For example, in a recent case the Court ruled that there was no claim against the tax consultant on the basis of an information contract when the tax consultant provided a balance sheet showing a profit to an investor who had the intention of acquiring the company. One month later the company went bankrupt. The Court reasoned that an “information contract” existed only if it was recognisable that the information was of essential significance to the recipient. This was especially the case if the party providing the information was particularly competent and he was an interested party with respect to the information. The tax consultant was not found to be liable because he did not act as an impartial trustee but as a dependent assistant without personal economic interest in the deal.

³⁹ Recently, the *Bundesgerichtshof* (Supreme Court) stated that, though Art. 323 I Commercial Code does not stipulate any rights for third parties against statutory auditors in principle, the contract of examination between the audited company and the auditors also had protective effects with respect to third parties. (1998, 1059). In this case, it was clear that a facsimile sent by the auditors was also destined to be used by a third party and that the auditors could expect that their facsimile would be of significance for economic decisions. As the decision is quite recent, it is not yet known how and to what extent it could be relied upon by third parties in practice.

⁴⁰ For example, in a judgment dated 5/2/1985, the OLG Karlsruhe decided that article 332 BGB which punishes the violation of the auditor’s obligations to report was intended to the protection of others under article 823 II BGB (OLG Karlsruhe 12 U 132/82, ZIP, 6 (Jg) 1985, 409-415).

⁴¹ If an association has been certified it can:

- bring suit before any Court in cases involving conduct which caused damages either directly or indirectly to all investors or to all members of certain categories of investors.
- seek damages before any Court on behalf of individual investors who have suffered individual damages having a common origin and caused by the actions of a single person. The association cannot proceed in this regard without the written approval of each investor, which makes the action different from the *classe action* under American or Portuguese law.

⁴² This law makes a distinction between institutional investors (*investidores institucionais*) and non-institutional investors (*investidores nao institucionais*). Institutional investors are Investment companies, banks, insurance companies, companies managing funds and pensions and they do not benefit from the same rights as non institutional investors. Non institutional investors (individuals,

stock market investors' associations and foundations whose goal is to protect stock market investors) have legal capacity to sue in order to protect "*interesses difusos*" (collective interests) and "*interesses individuais homogêneos*" (plurality of individual interests held by a plurality of individuals, members of a class, but which depend on a single matter of law or of fact and on a Court decision with an identical content).

⁴³ In Italy, the *Testo Unico* makes no mention of liability actions against auditing firms within the framework of the bankruptcy procedure. It is, therefore, unclear whether the company itself or the receiver is the proper plaintiff in such an action. The Court of Turin held on 18 September 1993 that the liquidator had standing to sue the auditing firm on behalf of the creditors.

⁴⁴ §317 par 3. HGB.

⁴⁵ This issue was explored in France by the Court of Appeals of Nîmes which held that a statutory auditor could be liable for damages if he resigns his mission « *in a way (in bad faith or by simple negligence) which injures to the company.* » Court of Appeals of Nîmes, JCP 1974 IV, 311.

⁴⁶ In a case before the Supreme Court (10 December 1998), the plaintiff requested that the resolutions agreed by the general meeting of the defendant, a traders' association, be declared void and that therefore a new auditor be appointed. The three rules that auditor must follow when carrying out an audit are transparency, reliability and fidelity. In a case before the *Audiencia Provincial de Ciudad Real*, the audited company requested the dismissal of an auditor appointed by the Commercial Registry. The request was based on Article 206 of the Spanish Corporations Act which provides that the company is entitled to request from the Courts of first Instance the dismissal of the auditor and the appointment of a new auditor when there is just cause (*justa causa*).

⁴⁷ In a case before the Supreme Court (S 96/419, 20 November 1997), a statutory auditor was found liable to the buyer of a company who had relied on the last audited accounts of the company and the auditing report given by a KHT auditor when guarantee liabilities were not shown in the accounts of the company, due to an accidental mistake of the bookkeeping and due to fraudulent criminal actions of the managing director. The buyer had not tried to do further research on the financial condition of the company, i.e. his due diligence did not go beyond the audited accounts and the auditing report. Regardless of the buyer's conduct, the statutory auditor was held liable for the damages, **only because he provided a misleading audit opinion.**

⁴⁸ Courts judged, for example, that :

- the purchaser could reasonably accept a balance sheet certified by the statutory auditor « *as a serious description of the company's situation.* » The statutory auditor was ordered to pay 300,000 euros: Court of Appeals of Paris, February 1984, Rev. Sociétés 1984, 779;
- the purchaser could « *legitimately rely on the work of the statutory auditor* » who was ordered to pay 500,000 euros: *Cour de Cassation*, 21 January 1997, BNCC 1997, n° 107, p. 40;
- the auditor was liable since the certified account were « without a doubt, the deciding factor in determining whether to invest in the company. » Court of Appeals of Paris, 8 September 1999, op. cit..

⁴⁹ In the *Gusum Case*, Gusum Bruk AB was declared bankrupt with a shortage of twelve million euros in April 1988. It was discovered that extensive manipulation of the company's books had taken place for over 10 years. In 1987 a group of investors acquired shares in Gusum for a total price of more than 3.5 million euros. The investors claimed that they bought the shares relying on, inter alia, the annual report for the financial year 1985/86 and the audit report for the same year, signed by the auditor. When the shares lost their value, the investors sued the auditor for damages. The Court began by establishing that the auditor had, through negligence, contributed to the distribution of an audited annual report containing incorrect information. Using the theory of protective norms which arise out of Swedish statutory law, the Court found that auditors should take the interests of the share-

purchasing public into consideration when establishing their report. With respect to the causal link, the Court stated that there must be some connection between the defendant auditor and investors. Thus, all investors do not necessarily have the right to damages. In this case, however, it was not a question of a small individual share purchase but of an acquisition of a very substantial block of shares, with the purpose of taking over the control of the acquired company. As the investors must have had a particular interest in the accuracy of the financial information regarding the company, the Court found that there was a sufficient causal link between the annual report and the losses of the investors. The investors were awarded 1/6th of their total claim in damages.

⁵⁰ In *ADT Ltd. v. BDO Binder Hamlyn* [1996] BCC 808, the Court awarded the plaintiff 39 million euros, the largest award in a case involving auditors, for a negligent misrepresentation in the audited accounts of the company. The plaintiff in this case sought to acquire the audited company and entered into negotiations with the company. When the deal was made, the president of the plaintiff company made the final agreement contingent on a discussion with the company's auditors. The plaintiff met with a partner of the defendant who answered questions related to the audited company's accounts. The partner was aware that the plaintiff was relying on the accounts to conclude the transaction and when asked, confirmed that the audited accounts presented a true picture of the company. The plaintiffs completed the acquisition of the target company in reliance on the statutory auditor's representations. The main issue in the case was whether the defendant assumed responsibility towards the plaintiff at the meeting to discuss the company's accounts. The defendant had conceded the issue of negligence. The duty of care owed to the acquiring company is based on the responsibility that the statutory auditor assumed which would be the basis of the "special relationship" test set forth in *Caparo* (*supra* p. 24). In this case, the partner in charge of the audit orally confirmed the statements made in the certification of the account to the acquiring company and, therefore, assumed responsibility toward the plaintiff for the accuracy of the accounts. Damages were calculated based on the amount paid for the company (63 million euros) less the amount a willing purchaser would have paid based on the true situation of the target company (24 million euros). In *Yorkshire Enterprise Ltd. et al. v. Robson Rhodes*, (*supra* note 34) the "special relationship" set forth in *Caparo* was held to exist in a case involving a plaintiff who requested that the statutory auditors provide a report on the financial condition of a company in which the plaintiff was investing. The investing company made it clear to the audited company and the statutory auditors that their final decision to invest in the company would be based on the report of the statutory auditors. The statutory auditors gave a favourable report of the company's accounts and, as a result, the plaintiff invested £250,000. Faced with a deteriorating financial situation, the audited company requested further investments from the plaintiff who provided an additional £125,000 continuing to rely on the statutory auditors' report. The audited company filed for bankruptcy and the plaintiff brought suit against the statutory auditors. After finding that the statutory auditors' were negligent in the elaboration of their report, the issue of duty of care was addressed. The High Court held that the statutory auditors were fully liable for the loss of the initial investment and the subsequent loan. According to the Court, the "special relationship" required by *Caparo* existed since the statutory auditors were fully aware of the reasons for the report to the investing company and that it was highly foreseeable that the investing company would rely on the report in making its investment decision without any further independent inquiry. Damages were set at £198,000 which represented the total amount of damages suffered by the plaintiff.

⁵¹ In the Netherlands, a 1998 case coming out of the District Court of Rotterdam confirmed the principle that the statutory auditor may be held liable for his statement. According to the District Court of Rotterdam, the statutory auditor has a general duty to carefully check all data provided to him to ensure that the company and third parties have an accurate view of the financial position of the company. In this case, the plaintiff had sold his shares in a company to a third party. The purchaser later brought suit claiming that the recoverable tax losses of the company in question as specified in the annual accounts did not accurately reflect the situation. The purchaser received an award of approximately 136,000 euros. The plaintiff then sued the statutory auditor who had certified the accounts. The Court held that the auditor was held to a higher duty of care since he knew that the

annual accounts were to be used by the purchaser in connection with the purchase of the shares in the company.

⁵² The Court of Appeals of Poitiers found a statutory auditor and the certified accountant two-thirds liable for having approved financial statements showing inventory enumerated in the certified balance sheet much overstated. The victim bank was held one-third liable: its fault was based on its loan approval upon an incomplete inspection of the financial statement and without taking the economic situation of the company into account. 20 October 1998 (BNCC n°113, page 28).

⁵³ In Sweden, in a 1996 case (NJA 1996:224), the defendant auditor was the accountant for two companies. During the period at issue, a certain amount of one of the companies' assets were transferred to the another company for a total price of 300,000 euros. The assets were valued at 292,000 euros in the balance sheet established by the auditor. It was later discovered that the actual value of the assets was only 35,600 euros. Before this discovery, a bank had granted credit in the amount of 142,300 euros to the company receiving the assets. The auditor had taken part in the discussion with the bank which preceded the granting of the credit. The bank's decision was based on the figures in the balance sheet and on information provided by the auditor in his capacity as accountant. The bank sued the auditor for the expected loss as a result of the debtor's default. The Supreme Court found that the damage to the bank was a direct result of the granting of the credit to the company and that the auditor had contributed to the incorrect picture of the value of the assets in question, and that he thereby had acted in conflict with generally accepted auditing standards.

⁵⁴ The Court of Appeals of Ghent ruled that a statutory auditor was jointly and severally liable with the directors who have let a supplier be convinced to sell a great deal of goods to the soon bankrupted company. The statutory auditor was held liable for not making his bi-annual verification, allowing a certified accountant to assume auditing duties and not being aware that the company was in bankruptcy. The total amount awarded was 350,000 euros. Court of Appeals of Ghent, 13 January 1995.

⁵⁵ In UfR 1982.585 H, an auditor was held liable to a supplier who had delivered goods to the audited company based on the public corporate accounts wherein the works in progress had an estimated value which included a profit of DKK 1.3 million (approximately 175,000 euros), which was held to have been exaggerated by an amount of DKK 826,000 (approximately 110,000 euros). Nevertheless, Court decisions do not have the same importance in Denmark as in common law countries and continental legal systems: the few decisions in this area cannot be considered representative.

⁵⁶ In UfR (Weekly Journal of the Courts) 1982.1062 OLD, the Danish Court found an auditor liable for certifying the accounts because the receivables and works in progress should have been evaluated at a much lower value. The auditor was held liable to the bankruptcy estate of his client.

⁵⁷ Two Court decisions may be quoted :

- by not reporting to the management the disorder in the company's accounting and errors in the balance sheet, the statutory auditor deprived the management of a chance to correct their behaviour and, as a result, prevented the company's creditors from the possibility of reducing their loss. In this case, the statutory auditor was held liable towards the body of creditors. Court of Appeals of Aix en Provence, 29 May 1981, Dalloz 1982, Ir 66;
- a proper verification of the accounts would have allowed the company to have a correct view of its financial situation and to take remedial measures. On the question of damages, the Court limited the amount of damages which were the result of the statutory auditor's negligence to 5% of the total, payable to the liquidator. Court of Appeals of Rouen, 27 April 1982, BNCC, p. 289.

⁵⁸ Statutory auditors' liability is also an issue when, as a result of the non-detection of accounting irregularities, the company continues its activity despite the fact that the shareholders' equity fell below the legal minimums (which is a cause for dissolution of the company). In this situation, the

Italian Courts has adopted two different solutions; either the statutory auditor is ordered to pay all the damages, or he is ordered to pay only the difference between the debts which arose after the shareholders' equity went below the legal minimum and any credit which accrued during the same period.

⁵⁹ In a 1996 case (26 January 1996, Bull. Joly, 1996, p. 289), the Court of Appeals of Paris held that a statutory auditor was liable for verifying only 1% of an area which represented 70% of the company's activity and which included patent irregularities. The statutory auditor was ordered to pay damages to the audited company which resulted from his breach of duty. The damages in this case were assessed on the basis of the lost opportunity to avoid paying excess taxes in error (approximately 76,000 euros).

⁶⁰ BGH NJW 1998, p. 1948, LG Hamburg, WM 1999, 139; LG Monchengladbach NJW-RR 1991, 415.

⁶¹ The first phase is the ongoing oversight of the company's accounting which takes place during the entire fiscal year. There is a doctrinal dispute as to whether the statutory auditor's negligence during this initial phase can result in liability to an injured party as a result of there being a sufficient causal connection between the statutory auditor's negligence and the damage to the party in question. One court has held that certain irregularities in the ongoing accounting certification, particularly with respect to non-compliance with legal and fiscal rules concerning the company's accounting, does not, by itself, cause a decrease in value of the company; it only facilitates the directors' violation of their duty. Tribunal of Milan, 3 June 1988, *Giur.comm.*, 1989, II, 945.

⁶² In this regard, the Court of Palermo found a statutory auditor liable for not reporting that a partner of the audited entity who was effectively running the business, brought considerable debts to the audited entity which caused it to go into bankruptcy. The Court reasoned that the statutory auditor should have been more vigilant, given the fact that the company was owned and operated by a family.

⁶³ Mr. Ian Brindle, p. 205.

⁶⁴ If the existence of fraud leads to the conclusion that the annual accounts are not in conformity with the statutory requirements and/or generally accepted accountancy principles, the statutory auditor may be liable for his statement if he did not meet his professional duty of care of a "good assignee". The District Court of Breda ruled that rendering a statement as to the annual accounts which does not reflect the relevant fraudulent circumstances, either in the statement or in a qualification thereto, may be characterised as a fault. 20 June 1995, 1997, 712.

⁶⁵ The Court of Appeals of Orléans found a statutory auditor liable for accepting information from an accountant who was employed by the audited company without taking further action when even a superficial survey would have shown the illicit acts of the accountant and allowed the statutory auditor to inform the managers of the association. The auditor was ordered to pay 718,000 euros corresponding to the misappropriations occurred after the submission of the certified report. The Court considered that, if the statutory auditor had met his duty of care towards the audited company, the company could have avoided the damages which occurred after his verifications (i.e. his report) but not those that occurred during the year for which he made his verifications. Court of Appeals of Orléans, 19 April 1995, BNCC n° 99, p. 332.

The Supreme Court also dealt with such an issue: the Court of Appeals of Reims held that the statutory auditor was negligent in the undertaking of his mission by accepting the work of the company accountant without verifying its reliability, making only summary verifications of the VAT tax without going sufficiently in detail into the client and supplier accounts, not analysing the internal control mechanism when misappropriations with respect to the VAT perpetrated by the accountant between 7 November 1986 and 23 February 1989, were possible because of the weak internal verifications. The Court found that standard auditing practices would have detected the fraud and,

therefore, the fraud continued as a result of the statutory auditor's negligence. However, the Court found that the damages that the company suffered were essentially the result of the company's negligence (unusual organisation in case of director's absence and the fact that the director signed blank checks which the accountant presented him) and set the statutory auditor's fault at 20%. Finally, the Court held that the statutory auditor was responsible only for the misappropriations which occurred after he had submitted his report since the verifications occurred "after the facts in question." The *Cour de Cassation* overturned the decision on this last ground ruling that the « *statutory auditor's mission is not limited to a verification a posteriori, but rather is a permanent mission of verification.* » *Cour de Cassation*, 19 October 1999.

⁶⁶ A case involved the main shareholder of a limited liability company who for many years had been paid sums for "company expenses" when in reality these payments had to be considered as being a shareholder's loan from the company. The loan had been given in violation of the Companies Act. The two statutory auditors were negligent in failing to remark the violations in their auditing report and this had contributed to the continuing of these violations and losses to the company. The managing director had a primary liability to pay for the whole damage and the two auditors were each half responsible for any amount they could not recover from the managing director. Supreme Court, 31 July 1992 KKO 1992:98.

⁶⁷ The Court of Appeals of Paris found a statutory auditor liable for not undertaking any verifications of the company's accounts during nine months of the fiscal year. The Court reasoned that losses which occurred after the submission of the auditor's report could have been avoided if the auditor had respected his duty of care to the company and ordered the statutory auditor to pay 305,000 euros in damages which represented the amount of the misappropriation after the submission of the certified report. 16 October 1979, JCP ed. G 1980 II-1932, confirmed by the *Cour de Cassation*, 16 November 1981, BNCC p. 66.

The *Cour de Cassation* on 19 October 1999 affirmed a decision by the Court of Appeals of Paris finding a statutory auditor liable for 103,000 euros in damages as a result of misappropriations from the client account which represented one of the largest items on the balance sheet and was not verified by the statutory auditor in accordance with the procedures recommended by the *Conseil National des Commissaires aux Comptes*. The Court of Appeals also stated that the existence of an accounting irregularity should have caused the statutory auditor to undertake a more precise verification. In the words of the *Cour de Cassation*:

« *by certifying the accounts in a hasty and negligent manner, when a serious examination in accordance with the general professional practices would have allowed the statutory auditor to issue reservations, the statutory auditor deprived the company of the opportunity of putting an end to the managers' illicit activity and avoid further instances of misappropriation.* »

The causation element was, thus, satisfied by the fact that the statutory auditor's non-disclosure in his certification report deprived the company of an opportunity to avoid further losses. The statutory auditor was ordered to pay a percentage of the losses which occurred after the issuance of his report.

⁶⁸ Many cases of alleged negligence of statutory auditors involve failure to discover fraud. *In Re Kingston Cotton Mill Company* (n° 2) elaborates on the definition of "misfeasance" which, according to the Court, includes the case of an auditor who, either « *knowingly or through failure to use reasonable skill and care, certifies accounts which ought not to have been certified, provided the direct result is pecuniary damage to the company.* » This case involved a inclusion of figures in the balance sheet relating to the stock-in-trade of the company based on a certification by the manager which proved to be false. The Court reasoned that the auditor was not « *entitled to rely upon the manager's certificate if an ordinary careful examination of the books ought to have made them suspect that statement.* » The auditor should have tested the « *accuracy of the manager's certificate by a comparison of the figures in the books that require auditing.* » This position is summed up in Lord Justice Lopes' maxim that the auditor is "a watch dog, but not a bloodhound." The other case is mentioned hereafter.

⁶⁹ The Cour de Cassation held that the auditor's vigilance must be even greater when there is "evidence of risk". In the case in question, the Court found that the high price for the purchase of a building especially in light of a much lower price agreed to in a precontractual document constituted such evidence. Supreme Court, 7 May 1993, op. cit. p. 45.

⁷⁰ Two cases are relevant to the non disclosure of a detected fraud :

- In a 1981 case, the managing director of a company had widely misused funds of the company so that he had received money to pay invoices which, in reality, had already been paid. The KHT auditor who had conducted a continuous, controlling audit upon appointment of the board of directors had noticed several irregularities in the book-keeping of the company and failures in the system of handling invoices and had drawn the attention of the board of directors. However, he failed to properly stress the importance of developing the company's bookkeeping system and internal verification system to such a level that the double payment of the same invoice would be prevented. The two other auditors responsible for the yearly audit should have noticed the irregularities in the bookkeeping as well as the fact that the board of directors had failed to take any action in the matter. Despite this, the auditors had given a clean auditing report and recommended the approval of the final accounts and actions of the board of directors. All three auditors were found negligent. The negligence of the KHT auditor responsible for the control auditing was deemed to be greater than the negligence of the two non-professional auditors who only did the yearly audit. They did not have to pay for the whole amount of damages, but only an amount deemed equitable of 17,000 euros. Supreme Court 14 April 1981, KKO 1981:48.

- More recently, the Helsinki Court of Appeals found a statutory auditor liable for damages which arose from the fact that he had warned in his report for 1989 but not in subsequent years that a board member had taken out company funds for his personal use in violation of the Companies Act. Helsinki Court of Appeals, 14 October 1997 (S 97/35). **But the Supreme Court has excluded the statutory auditor's liability because there was no causal link between the auditor's fault and the damage, as the shareholder in question was already without means of payment in 1992 (Supreme Court 12/11/99).**

⁷¹ In *In Re London and General Bank* (N° 2), an auditor presented a confidential report to the directors calling their attention to the insufficiency of the securities in which the capital of the company was invested, and the difficulty of realising them, but in his report to the shareholders merely stated that the value of the assets was dependent on realisation. The shareholders were deceived as to the condition of the company, and a dividend was declared out of capital and not out of income. The Court held that the auditor was guilty of misfeasance as set forth under section 10 of the Companies Act of 1890 and was ordered to pay damages in the amount of the dividend paid.

⁷² Article 230-1 of the law of 24 juillet 1966 provides:

« *When the statutory auditor of a company discovers, in the execution of his mission, evidence of activity which compromises the ongoing nature of the business, he shall inform the chairman of the board of directors of the company according to the procedure set forth in the decree of the Conseil d'Etat.* »

With regard to premature or erroneous disclosure, Article 234 of the law of 24 July 1966 provides that the statutory auditor cannot be held liable for information disclosure in the context of his *devoir d'alerte*. Nevertheless, legal scholars are of the opinion that the statutory auditor would be liable in such circumstances if he acted in bad faith.

⁷³ In the *Primor* case (Supreme Court, 19/12/95), it was alleged that over a period of many years, the auditors fail to detect serious under provisions in the claims reserves which compromised the company's solvency : although the case was ultimately dismissed on the basis of the plaintiff's delay in the litigation, it demonstrates that the auditors will be liable for such circumstances where they acted negligently, i.e. without due skill and care.

⁷⁴ The french *Cour de Cassation* held that the termination of the mission of the statutory auditor was justified when the statutory auditor undertook, in bad faith, the alert procedure when there were no

facts which threatened the ongoing nature of the business, sent nineteen letters to public authorities mentioning alleged illicit practices which did not occur and refused to establish a required report. *Cour de Cassation*, 14 November 1995, rev. Soc. 1996, p. 279. More recently, the Court of Appeals of Paris approved the termination of the statutory auditor's mission where the statutory auditor commenced the alert procedure based only on rumours discrediting the president of the company. Court of Appeals of Paris, 25 February 1998, RTD Com. 1998, p. 360. Though these cases involved the termination of the statutory auditor's mission, commentators are of the opinion that the same actions on the part of the statutory auditor could lead to liability for damages to the company in question. Moneger & Granier, *Le commissaire aux comptes* n° 549; Viandier, *Droit comptable* n° 55.

⁷⁵ The *Cour de Cassation* in France held that the statutory auditor has an obligation to report all contracts between the company and its directors or between two companies having the same directors. The case involved a statutory auditor who was informed of the existence of such a contract (an employment contract between a director and the company) and did not report it. The contract was cancelled as a result of the statutory auditor's oversight and the Court ordered the statutory auditor to pay damages to the director in question. 2 July 1973 D 1973, p. 674. The Court of Appeals of Bordeaux held that the certification of the largest salaries which the company pays is of such an importance that any error on the part of the statutory auditor will lead to strict liability (*obligation de résultat*). 7 March 1990, *Droit des Sociétés* 1991, n° 225.

⁷⁶ The *Cour de Cassation* in France has upheld a decision discharging a statutory auditor for interfering in the management of the company. 18 October 1994, *Les Petites Affiches*, 21 June 1995, n° 74. Liability would presumably arise under the same circumstances.

⁷⁷ In France, under the Company Law, the statutory auditor must issue a report in case of a capital increase without a preemptive right for the existing shareholders. In the case in question, the statutory auditor only approved the information given him by the directors without verifying its accuracy. He was ordered to pay damages which corresponded to the amount that the new shareholders lost as a result of his negligence. Court of Appeals of Dijon, 17 January 1996 RJDA 12/96 n° 1486.

⁷⁸ Concerning the fault, French Courts have held that:

- the statutory auditor does not have to « *verify all of the accounting operations of the company or search for all errors or irregularities, but rather undertake the verifications which are necessary in order to have a reasonable degree of assurance by verifying the regularity of the accounting procedures, investigating by survey and intensifying the investigation in case of evidence of irregularities.* » Court of Appeals of Bordeaux, 4 November 1997, BNCC n° 110, p. 311.
- The fact that the auditor had experienced resistance from the company when attempting to obtain information should have led him to be more vigilant and the fact that a summary examination of the accounts revealed the irregularities tended to show that the auditor did not meet the standard of care of a reasonably diligent professional. *Cour de Cassation*, 9 February 1988, Bull Civ. IV n° 68.
- The statutory auditor was negligent in the exercise of his mission by not providing the requisite level of supervision of his associates and not checking oral representations that were made to him and by not taking sufficiently into account the specificities of that particular company. Court of Appeals of Paris, 8 September 1999, *Albin Michel v. KPMG*.

⁷⁹ Supreme Court, Decision of May 1993, n°5263, In *foro italiano*, 1994, I, 130 : the case dealt with the acquisition of a building at an usually high price for the company when the price was raised after a preliminary agreement was signed.

⁸⁰ *Primor plc v. Stokes Kennedy Crowley*, [1995] IRLN 459, 502.

⁸¹ In UfR 1987.811 OLD and UfR 1988.653 H, the auditors were not found liable even though they had not discovered that their client had given a surety to his bank covering debt of another company

belonging to the same group. The case was decided by a majority of nine Supreme Court judges but two voted in favour of liability.

⁸² With respect to misappropriations, the following decisions by the French Courts are examples of rulings in favour of statutory auditors based on the absence of fault:

- the statutory auditor's mission is not to « *recreate accounts that have already been established, set up a system of continual, in-depth inspection...* » or « *undertake a systematic examination of the fundamental accounting documents* » but rather to proceed by random testing;
- the statutory auditor is only required to investigate more closely if there is « *serious evidence which would reasonably raise doubts* » as to the accounts;
- the statutory auditor was not responsible for illicit acts which were « *carefully hidden* » or if the fraud was « *very elaborate* »;
- the statutory auditor was not liable when the illicit acts were only discovered after an «in-depth investigation» or a «detailed and minute verification »;
- the fact that fraud was only subsequently uncovered by a firm retained expressly for investigating for such fraud is not sufficient to show the statutory auditor's negligence.

(CA Rennes, 27 May 1975; TGI Paris, 13 December 1982; TGI Nanterre, 17 May 1984; Cass. Civ., 19 May 1987; CA Grenoble, 7 March 1989; TGI Dijon, 6 July 1998; TGI Nanterre, 4 November 1998, BNCC n° 113°).

With respect to irregularities in the accounts, the Court of Appeals of Paris found in favour of a statutory auditor who brought the irregularities to the attention of the board of directors, proposed certain improvements and included the irregularities in his report to the shareholders which ultimately led to their rectification. CA Paris, 24 April 1989, BNCC n° 77, p. 94.

⁸³ *Cour de Cassation*, 1 April 1997, *Dalloz* 1998, somm. com. 180, not concerning an officer but the solution should be applicable to the auditor.

⁸⁴ 7 September 1993, n° 9885 in *il fallimento* 1994, n° 1, p. 44.

⁸⁵ This rule was the basis of the *Gusum* case (see note 49), where the plaintiffs had acquired stock in reliance on an audited annual report which turned out to be incorrect.

⁸⁶ *Cour de Cassation*, 9 February 1988, Bull. civ., 1988, IV, n° 68 (see note 78); *Cour de Cassation*, 21 January 1997, BNCC n° 107, p. 40 (see note 48).

⁸⁷ This solution was adopted by the Court of Milan (in decisions of 17 July 1997, in *Foro Padano* 1998, I, 139 and 18 September 1993 in *Giur. It.* 1994, I, 2, p. 657).

⁸⁸ *Cour de Cassation*, 19 October 1999, RJDA 1/00, n° 36; Lyon Court of Appeals, 6 November 1997, BNCC n° 108, p. 208.

⁸⁹ Olivier RALLET, *Responsabilité des dirigeants de sociétés*, Larcier, Bruxelles, 1996, n°56.

⁹⁰ The auditor is liable when the use of normal diligence would have prevented the damage.

- the normal supervision of the statutory auditor would have allowed him to discover and put an end to misappropriations by an employee or director of the company. *Cour de Cassation*, 16 November 1981, BNCC 1982, p. 66; Court of Appeals of Lyon, 6 November 1997, *supra* note 88.
- the plaintiff purchased stock in the company in reliance on the statutory auditor's erroneous certification. *Cour de Cassation*, 9 February 1988, Bull. Civ. IV, n° 68; 21 January 1997, BNCC n° 116, p. 40.
- the fact that the purchaser had not made any audit of the company prior to purchasing the shares was not a defence for the statutory auditor. *Cour de Cassation*, 21 January 1997, BNCC 1997, n° 107, p. 40.

On the other hand, the causal connection is not established and the statutory auditor is, therefore, not liable when:

- the cause of the damage occurred before the statutory auditor's breach, for example when the plaintiff acquired shares of the company or signed an employment contract before the disclosure of the statutory auditor's report. Civil Tribunal of Paris, 14 April 1986, BNCC n° 63, p. 299; *Cour de Cassation*, 15 June 1993, Bull. Joly 1993, p. 1130.
- an in-depth verification in conformity with established standards would not have allowed the statutory auditor to discover the illicit activity of a director or employee of the company. *Cour de Cassation*, 19 May 1987, BNCC n° 67, p. 334.
- the plaintiff purchased shares of the company knowing that the accounting report did not present the actual financial condition of the company and being familiar with the difficulties faced by the company. Court of Appeals of Amiens, 23 June 1988, BNCC n° 71, p. 317.

⁹¹ The Supreme Court decided that there was no causal link between the damage and the failure of the statutory auditor who failed to remark in his 1992 report a fraudulent shareholder's loan that he noticed in a previous report, because in 1992 the shareholder in question was already without means of payment (Supreme Court 12/11/1999, see note 70).

⁹² In NJA 1979:157 the Supreme Court concluded that liability for the auditor against a creditor of the company did not follow already from the fact that the auditor had failed to react against a particular transfer (undertaken while the debt to the creditor was outstanding) which unlawfully drained the company of money, it was required that the transfer had had a direct effect on the creditor's possibility to collect. This was not the case, according to the Supreme Court, if either the company remained solvent even after the transfer or the company's standing at the time of the transfer was already such that the creditor could expect to receive nothing in the coming bankruptcy.

In NJA 1996:224 the auditor had failed to react against an obvious overvaluation of a doubtful asset. A bank had lent money to the company in reliance upon this valuation. The Court of Appeals dismissed the claim by the bank against the auditor on the basis that it had not been demonstrated that the company was not solvent when it received the loan. The Supreme Court found, however, that in these circumstances, and in contradiction to NJA 1979:157, there was sufficient connection between the auditor's negligence relative to the evaluation and the subsequent loss of the bank, irrespective of whether the company was insolvent at the time of the loan. The reason was that there would irrespective of the solvency have been no credit at all, had the auditor not committed the fault.

⁹³ Article 1223 Civil Code.

⁹⁴ In *Galoo v. Grahame Murray* ([1994] 1 WLR 1360, Court of Appeals), the company alleged that the auditors should have reported that the company was insolvent at the date of their report. It further alleged that, if the auditors had so reported, the company would have ceased trading immediately and as a result would not have suffered subsequent trading losses. The "but for" test was clearly satisfied, but the claim was struck out and an appeal filed. The Court of Appeals held that the "cause" of the subsequent losses was not the auditor's negligence but the company's unprofitable trading. A negligent failure to report the company's insolvency could provide the opportunity for such losses to be suffered, but it could not "cause" them in the sense required by the law.

In *Yorkshire Enterprise Ltd. et al. v. Robson Rhodes* [1998] (*supra* note 34), the damage award included not only the investment made as a result of the statutory auditors' report, but also the subsequent loan despite the fact that the investing company did not expressly inform the statutory auditors that it was continuing its reliance on the report. Nevertheless, the auditors did have knowledge of this subsequent investment. The Court ruled that the auditors' liability extended to the subsequent loan because the further damages were directly attributable to the negligent misinformation in the report. This aspect of the ruling expands the scope of the potential liability of a statutory auditor. In *Caparo*, the House of Lords had limited the scope of liability to only the foreseeable consequences of the negligence and not for subsequent courses of action taken by the plaintiff.

⁹⁵ In *South Australia Asset Management Co v. York Montague Ltd.*, the House of Lords decided that, even where the investor establishes that he would not have made the investment but for the negligence of a professional adviser in giving him inaccurate information, his recovery is limited to that part of his loss that was caused by the information being wrong. This is a difficult test to apply. Another way of looking at it is that the investor cannot recover damages for losses caused by risks that he was willing to take whatever advice he received. The Court will seek to identify the risks of loss against which the auditor had a duty to use reasonable care to protect the investor.

⁹⁶ The Court of Appeals of Versailles completely cleared a statutory auditor of liability because he had drawn the board of director's attention to certain irregularities to which the board did not respond or take action. The Court ruled in favour of the statutory auditor even though he had not submitted his informational report to the shareholders for two years. 28 March 1991, Bull. Joly, 1991, p. 723.

⁹⁷ With regard to misappropriation, the Court of Appeals of Orléans, in a case cited above, ruled that the victim, an association, by not in any way overseeing its accounts and relying totally on its accountant, participated in the damage to the association. Liability was, therefore, equally apportioned to the statutory auditor and the association. 19 April 1995, *supra* note 65.

In a similar case, the Court of Appeals of Reims, ruled that the damages suffered by the audited company were the result of its unusual organisation during the director's absence and the negligence of the director who signed blank checks upon the accountant's request. The statutory auditor's liability arose from the fact that he made no comment as to the deficiencies in the company and, thus, was partially liable for the misappropriations.

The Court found the company to be 80% liable and the statutory auditor 20% liable for the damages. 31 July 1996.

The Court of Appeals of Poitiers found a statutory auditor and the certified accountant two-thirds liable and the victim bank one-third liable for approving a loan based on the evaluation of inventory enumerated in the certified balance sheet which turned out to be false. The bank's fault was based on its loan approval upon an incomplete inspection of the financial statement and without taking the economic situation of the company into account. 20 October 1998.

However in another case, the Paris Court of Appeals has held that « *despite the company's accounting shortcomings which contributed to its ultimate damages, the company may demand reparation of the damages which consisted of overpayment of taxes* ». 26 January 1996, Bull. Joly 1996, p. 289.

⁹⁸ The failure of the auditor to remark that the Board of directors of a company had failed to take action to place the company in liquidation, had no causal link to the credit loss suffered by a supplier of the company, since the supplier had not attempted to familiarize himself with the public auditing report of the company. Supreme court 23 January 1991 (KKO 1991:13).

Nevertheless, it should be noted that the reader of an auditing report must be able to rely on and does not need to check information contained in the auditing reports from other sources. Therefore, even if a buyer of a company would have been able to find the mistake by conducting a more careful due diligence, he was not obliged to do so from the point of view of liability of the statutory auditor. Supreme Court, 20 November 1997.

⁹⁹ Articles 490, 497(1) and 507 of the Civil Code.

¹⁰⁰ Article 73 CSC provides that the statutory auditors and members of the Audit Board (*Conselho fiscal*) are jointly and severally liable with the founding members, managers and directors of the company; within the framework of stock issuance, Article 163 of the CMVM defines the liability of statutory auditors and members of the audit board as jointly liable.

¹⁰¹ The managing director and main shareholder of a limited liability company had been paid sums for "company expenses" for many years, when in reality these payments had to be considered as being a shareholder's loan from the company. The loan had been given in violation of the Companies Act. The two statutory auditors had negligently failed to remark the violation in their auditing report and this

had contributed to the continuing of these violations and losses to the company. The managing director and the two statutory auditors were found to be jointly and severally liable to the plaintiff. Between the defendants, the managing director had a primary liability to pay for the whole damage and the two auditors were each half responsible for any amount they could not recover from the managing director. Supreme Court, 31 July 1992 KKO 1992:98.

¹⁰² Court of Appeals of Bordeaux, 17 October 1990.

¹⁰³ Court of Appeals of Paris, 29 September 1983.

¹⁰⁴ Section 275.2 HGB.

¹⁰⁵ Article 323 II HGB.

¹⁰⁶ Article 323 §4 HGB.

¹⁰⁷ In its decision of 2 April 1998 (NJW 1998, p. 1948) the Supreme Court stated that Article 323 HGB does not exclude possible liability of statutory auditors under a contract with protective effects to third parties. *supra* p. 25. At the same time the Court considered that the limitation of liability in Article 323 HGB must be taken into consideration in the relationship between the auditors and the third party. Some authors conclude that the limitation is generally applicable. Sieger/Gätsch, BB 1998, p. 1408. A good reason for such application seems to be that, otherwise, the third party would profit by a higher amount than the audited company itself, which paid for the audit. However, the District Court of Passau expressed the contrary opinion in a recent decision. The Court reasoned that the cap from Article 323 HGB is not applicable to contractual liability towards third parties. LG Passau, 28 May 1998, not final, BB 1998, 2052.

¹⁰⁸ Article 19 of the PD 226/92.

¹⁰⁹ The Companies Act provides the Courts with discretion to reduce the amount of damages awarded in case of auditor's liability. If the auditor is found liable for negligence or other breach of duty in proceedings brought by or for the benefit of the company, there is a discretionary power conferred by section 727 of the Companies Act 1985 whereby the Court may relieve the statutory auditor, either wholly or partly, from his liability on such terms as it thinks fit. The criteria which must be satisfied are (i) that the auditor has acted honestly and reasonably and (ii) that, having regard to all the circumstances of the case (including those connected with his appointment), he ought fairly to be excused. This provision has, in practice, never been used by the Courts to reduce a statutory auditor's liability.

¹¹⁰ A similar solution was applied by the Supreme Court of Finland in a case (20 November 1997, *supra* note 47) where the Court of Appeals had lowered the amount of damages that the statutory auditor was ordered to pay stating that it would be unreasonable to order the statutory auditor to pay total amount of damages. The amount was lowered from 1.3 million euros to 250,000 euros by the Court of Appeals and then further reduced by the Supreme Court to 180,000 euros. In a 1981 case, the Finnish Supreme Court ordered the co-defendants of a KHT auditor to pay less than the total amount of damages based on equity. 14 April 1981, *supra* note 70.

¹¹¹ Section 275 HGB, *supra* note 11.

¹¹² Article 11 of the Law 19/1988 of 17 July 1988, *supra* note 28.

¹¹³ *Decreto-Lei* n° 487/99 of 16 November 1999.

¹¹⁴ Art. 78 CSC, *supra* note 25.

¹¹⁵ Article 10 of the CMVM., *supra* note 26.

¹¹⁶ Article 3:40 CC.

¹¹⁷ Mr. Ian Brindle, p. 203.

¹¹⁸ Mr. André Bindenga, p. 210.

¹¹⁹ The justification for this exception is that at the time of the drafting of the Rome Convention there was significant work in progress concerning the harmonization of company law which resulted in the 1984 directive concerning the minimal qualifications of persons undertaking statutory audits of public companies which was in the form of a proposed directive at the time of the adoption of the Rome Convention (OJEC C 12, May 13, 1978).

¹²⁰ For example, Belgium, Cass. February 24, 1938 *SA Antwerpia* ; Denmark, *Baltica*, 1957 ; France, Cass. Civ. December 1910, *American Trading Company* ; Italy, article 25.1 disp. Pre. Civil Code ; the Netherlands, Hoge raad, May 13, 1966, *Alnati* ; United Kingdom, *Vita Food Products*, 1939 AC 277.