

Corporate Governance, D&O and Audit Liabilities

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Corporate Governance and Disclosure Obligations

The Combined Code on Corporate Governance.

Based on Higgs' review of the role of Non-Executive Directors and Smith report on Audit Committees.

“Comply or explain” requirement.



The Operating and Financial Review (“OFR”)

- ❖ Regulations to be introduced under Section 257 Companies Act 1985
- ❖ Companies (Audit, Investigation and Community Enterprise Bill) introduced December 2003
- ❖ Government issued consultation paper including OFR regulations and guidance – the consultation period ends 6 August 2004
- ❖ Companies to prepare statutory OFRs for the first time for financial years beginning on or after 1 January 2005

Accounts Modernisation Directive

- ❖ Adopted by the EU in July 2003
- ❖ Directive must be implemented for financial years beginning on or after 1 January 2005

Compliance with Disclosure Obligations – New Offences

1. knowingly or recklessly approving an OFR that does not comply with the relevant provisions of the Companies Act;
2. knowingly or recklessly approving a defective directors' report;
3. parallels criminal offence of approving defective accounts.

Enforcement by Financial Reporting Review Panel.



Requirement to provide information to auditors

Companies (Audit, Investigations and Community Enterprise) Bill

Requires directors' report to contain a statement that the directors are not aware of relevant information which has not been disclosed to the company's auditors.

No boundaries on materiality.

The clause requires every director to take responsibility for disclosures by his fellow directors.

It will be difficult for a director to be sure he has disclosed all information.

Enhanced role of non-executive directors



Liability position of directors and auditors

- ❖ *Barings v Coopers & Lybrand and Deloitte & Touche, Singapore*
- ❖ *The Equitable Life Assurance Society v Roger Bowley & Others*
- ❖ *Section 727 Companies Act 1985*

DTI Consultation Document on Directors & Auditors Liability Reform

- ❖ Issued December 2003.
- ❖ Consultation ended March 2004



Auditors Reform - Proposals

1. Minimal law reform.
2. Allow auditors to limit their liability contractually.



Directors – possible reform

1. Maintain status quo.
2. Relaxation of Section 310 (in various ways) and broadening of Section 727 relief.



Transparency Directive

- ❖ Article 7(2) and Recital 10.
- ❖ House of Lords European Union Committee:

“It is not satisfied that the fears expressed [as to an extension of auditor and director liabilities] are without foundation. We note that whilst the Transparency Directive may not be intended to extend civil liability of the company directors and auditors to the investing public generally there remains legitimate uncertainty as to the effects of the directive if adopted in its present form. There also remains the so-called jurisdiction issue on which the government was unable, at this stage, to give a clear view.”

Transparency Directive (2)

“What is clear is that, if and when, the Directive is adopted, the European Court of Justice will have the final word on how the Directive is to be interpreted and whether member states have fully and correctly implemented it. Thus, although the UK might transpose the Directive into English law in such a way as to maintain the current position as regards the liability of directors and auditors following the House of Lords in Caparo, whether that will be compatible with the Directive would ultimately be up to the European Court of Justice to determine.”

Some Insurance Issues

1. Risk allocation – fundamental change or only marginal potential variation?
2. Section 310 reform and opportunities – representation costs, excesses and the like.
3. Overall impact of developments for auditors' risk profile.
4. Use of reform tools as a barometer of risk management competence?
5. The rise of regulatory and disciplinary investigations and prosecutions.
6. Jurisdictional issues.