

Auditor liability

The following suggestions relating to auditor liability were the most surprising part of the government's proposals:

12. The Government will amend the law to allow auditors to incorporate.
13. The Government will seek the agreement of the States to introduce proportionate liability.
 - The Government believes that the market for audit services will be improved if the arbitrary consequences of the present rules relating to joint and several liability in relation to economic loss and property damage are reformed.

Commentary

Currently auditors can be sued for the total loss resulting from their alleged negligence, and all partners in the audit firm are parties to the action. This is termed joint and several liability. The government proposal is to introduce proportionate liability, whereby only the partner involved in the audit is sued and the amount of damages payable is limited to the auditor's share of blame. The partner sued can be liable for total damages awarded; this liability extends to his or her personal assets.

The audit contract is between the company and the auditor. If litigation involving auditors occurs prior to liquidation, the company sues the auditor; if it occurs after liquidation proceedings start, the liquidator acting in the name of the company sues the auditor.

If proportionate liability is introduced to determine blame, evidence about the directors' and management's conduct will be admissible. Directors and management may be reluctant to sue the auditor knowing their own actions will be reviewed in court, thus making information available to the ASIC, who might later initiate their own proceedings against directors or management.

Conclusion

The government's discussion paper on auditor reform is another step in this continuing tale of an accounting/auditing crisis. The royal commission into the collapse of HIH Insurance has yet to present its findings, and the government has noted that these findings may influence the nature of the reforms adopted. The government's proposed reforms are based on a self-regulatory model. On the important issue of auditors' providing non-audit services to their audit clients, the reforms rely on the principles established in *Professional Statement F1: Professional Independence* and disclosure of relevant data in a company's financial statements. Whether this satisfies the critics of auditing remains to be seen. The one surprising suggestion is to allow auditors to incorporate and to change their liability from joint and several liability to proportionate liability. Obviously the auditing profession will welcome this reform.