



Office of the Director
of Corporate Enforcement

*Oifig an Stiúirthóra um
Fhorfheidhmiú Corparáideach*

Decision Notice D/2002/1

*The Principal Duties and Powers of
Auditors*

under the Companies Acts 1963-2001

Decision Notice D/2002/1
Information Book 5

The Principal Duties and Powers of
Auditors
under the Companies Acts 1963-2001

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1.0 Introduction

The Companies Acts 1963-2001 contain extensive provisions detailing how the affairs of companies are to be conducted. These provisions describe how the various participants in companies should discharge their duties and obligations. In addition, participants are accorded substantial rights and powers in order to enable them to assert their rights and, if necessary, defend their personal and/or corporate interests.

The Director of Corporate Enforcement is of the view that the extensive requirements of the Companies Acts make it difficult for many non-professional participants in company affairs to be well informed of their rights and obligations under the law. This has, in part, contributed to an inadequate standard of compliance with company law in the past.

Section 12(1)(b) of the Company Law Enforcement Act 2001 specifies that a function of the Director is “*to encourage compliance with the Companies Acts*”. Consistent with this remit, the Director issued a Consultation Paper setting out the principal duties and powers of companies, company directors, company secretaries, members & shareholders, auditors, creditors, liquidators, receivers and examiners under the Companies Acts 1963-2001. The responses received in response to the Consultation Paper were reviewed in detail and, following that review, the comments and suggestions made by the various contributors were, as far as is practicable, taken into account.

The resulting guidance has been prepared in the form of a series of information books. There are information books on the following topics:

Information Book 1 – Companies

Information Book 2 – Company Directors

Information Book 3 – Company Secretaries

Information Book 4 – Members and Shareholders

Information Book 5 – Auditors

Information Book 6 – Creditors

Information Book 7 – Liquidators, Receivers and Examiners

In addition to information on the relevant duties and powers, each book contains information on the penalties for failure to comply with the requirements of the Companies Acts and useful addresses and contact points.

Each book has been prepared for use by a non-professional audience in order to make the main requirements of company law readily accessible and more easily understandable.

The Director of Corporate Enforcement considers it important that individuals who take the benefits and privileges of incorporation should be aware of the corresponding duties and responsibilities. These information books are designed to increase the awareness of individuals in relation to those duties and responsibilities.

The Director wishes to make clear that this guidance cannot be construed as a definitive legal interpretation of the relevant provisions. Moreover, it must be acknowledged that the law is open to different interpretations. Accordingly, readers should be aware that there are uncertainties in how the Courts will interpret the law, particularly when the law is applied to the specific circumstances of specific companies and individuals.

It is important to note that where readers have a doubt as to their legal obligations or rights, they should seek independent professional legal or accountancy advice as appropriate.

As changes are made to company law in the future, the Director intends to keep this guidance up to date. He also welcomes comment on its content, so that future editions can remain as informative as possible.

Office of the Director of Corporate Enforcement

November 2002

2.0 Principal Duties and Powers of Auditors

2.1 Companies' and Directors' Responsibilities for the Preparation of Annual Financial Statements

Before examining auditors' responsibilities and duties, it is helpful to first revisit companies' and company directors' responsibilities with regard to the preparation of annual financial statements.

Generally, companies and their directors are required to prepare accounts on an annual basis. The annual accounts are prepared from the information contained in the company's books of account and other relevant information. The contents of the financial statements are set out in Information Book 1 – Companies. The directors are also required to annex a report to the accounts (known as the directors' report¹). This is a report by the directors to the members of the company. It is required to address certain matters, details of which are set out in full in Information Book 2 – Company Directors.

In addition to maintaining proper books of account and preparing financial statements which give a true and fair view of the state of the company's affairs and of its profit (or loss) for the relevant period, the directors also have responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and for the prevention and detection of fraud and other irregularities.

¹ The Directors' Report is required by section 158 of the 1963 Act (as amended). Its contents are prescribed by section 158 of the 1963 Act and by sections 13 and 14 of the Companies (Amendment) Act, 1986.

2.2 What is an Auditor

An auditor is an independent professional person qualified to perform an audit. In practice, a firm of auditors will usually be appointed to act as auditors to a company.

2.3 What is an Audit

For the purposes of the Companies Acts, an audit is an examination of the financial statements of a company performed by an auditor or firm of auditors. The objective of performing an audit is to enable the auditor to provide the members of the company with an independent, professional and informed opinion on the financial statements prepared by the directors.

By reporting their opinion, the auditors of the company provide reasonable assurance to the members of the company that the financial statements give a true and fair view of the state of the company's affairs at a particular point in time (i.e. at the financial year end) and of its profit (or loss) for the period under review and that they have been prepared in accordance with the Companies Acts and applicable accounting standards.

In performing their audits, auditors are required to comply with professional standards as set down by the Auditing Practices Board, an independent standard setting body.

In carrying out an audit, auditors are required to:

- carry out procedures to obtain sufficient appropriate audit evidence to enable them to determine with reasonable confidence whether the financial statements give a true and fair view;
- evaluate the overall presentation of the financial statements in order to ascertain whether they have been

prepared in accordance with the Companies Acts (and any other relevant legislation) and accounting standards;

- issue a report to the members of the company containing a clear expression of their opinion on the financial statements.

2.4 What Does an Audit Involve

During the course of an audit, auditors will normally perform the following types of audit work:

- furnish the company with a 'letter of engagement', in which the auditor sets out the directors' and auditors' respective responsibilities and the scope of the audit;
- obtain a knowledge of the company's business and industry;
- plan the audit, with a view to, *inter alia*, identifying the areas of the financial statements most likely to be susceptible to the risk of error or misstatement;
- where one exists, evaluate the company's system of internal control (internal control systems are explained in summary in Appendix E to Information Book 1);
- examine, on a test basis, the evidence relevant to the amounts and disclosures contained in the financial statements;
- assess the significant estimates and judgements made by the directors in the preparation of the financial statements;
- determine whether the accounting policies are reasonable and have been adequately disclosed;
- review the overall presentation of the financial statements;
- examine any significant events in the post balance sheet period i.e. in the period between the date to which the financial statements are

made up and the date the audit is completed;

- on completion of the audit, provide the directors with a letter setting out any problems encountered (e.g. errors, weaknesses in internal controls etc.) during the course of the audit and making recommendations to address the problems encountered (this letter is referred to as a ‘management letter’);
- issue the auditors’ report to the members of the company (see below).

2.5 What does ‘True and Fair View’ Mean

Under the Companies Acts² companies’ financial statements are required to give a true and fair view of the state of the company’s affairs and of their profit (or loss) for the period in question.

However, the Acts do not define the term ‘true and fair view’. As a general rule, a set of financial statements will be considered to give a true and fair view where they have been prepared in accordance with:

- the Companies Acts, and;
- accounting standards.

In order for a set of financial statements to give a true and fair view, they would be expected to:

- fairly reflect the circumstances of the company’s business;
- reflect the commercial effect of the underlying transactions and balances and not merely their legal form;
- state the assets, liabilities and profits (or losses) of the company as arrived at in accordance with accounting policies required by company law and by the relevant accounting standards, and;
- consistently apply those accounting policies i.e. from year to year in order that the financial statements

from one year to the next are comparable.

Overall, the financial statements will not give a true and fair view unless the information contained in them is sufficient in quantity and quality to satisfy the reasonable expectations of the readers to whom they are addressed i.e. the members. The auditor’s opinion seeks to enhance the credibility of the financial statements by providing reasonable assurance from an independent source that they give a true and fair view.

2.6 When is an Audit Required

In general, every company must have its financial statements audited annually. However, certain companies can be exempted from the requirement to have an annual audit provided that they comply with certain conditions³. It should be noted however that where a company can avail of the exemption to have an audit performed, the requirements to maintain proper books of account and to prepare annual financial statements are unaffected.

2.7 Qualifications of an Auditor

In order to qualify to act as auditor to a company, a person must comply with a number of requirements. They must:

- be a member of a recognised body of accountants⁴ (or have an equivalent qualification), and;
- hold a valid practising certificate from a recognised body of accountants (a practising certificate will not normally be awarded until a person has completed a number of years post qualification experience of auditing).

A small number of individuals are, by virtue of a Ministerial authorisation obtained prior to 3 February 1983, and registered under the provisions of section 199(3) of the Companies Act,

² Section 149 Companies Act, 1963 and section 3 Companies (Amendment) Act, 1986

³ The criteria for small company audit exemption are dealt with in detail in Information Book 1 (section 2.10.3).

⁴ The following bodies of accountants are recognised by the Minister for Enterprise, Trade and Employment for auditing purposes under section 191 of the Companies Act, 1990:

The Institute of Chartered Accountants in Ireland (ICAI)

The Association of Chartered Certified Accountants (ACCA)

The Institute of Certified Public Accountants in Ireland (ICPAI)

The Institute of Chartered Accountants in England and Wales (ICAEW)

The Institute of Chartered Accountants in Scotland (ICAS)

The Institute of Incorporated Public Accountants (IIPA)

1990, authorised to continue as recognised auditors.

Certain parties, such as bodies corporate, those who have links with the company being audited (for example, officers and employees of the company and their near relations) and undischarged bankrupts are prohibited from acting as auditor to a company. Similarly, persons who are the subject of a disqualification order are precluded from acting as company auditors.

In addition to the legal prohibitions on certain persons acting as company auditors, the recognised accountancy bodies' Codes of Ethics impose further restrictions on their members and the circumstances under which they are permitted to act as a company's auditor. The purpose of these Codes of Ethics is to preserve the independence of the auditor.

2.8 Appointment of Auditors

The first auditors of a company may be appointed by the directors or by a general meeting of the company. After that, the auditors are appointed by the members of the company in annual general meeting and hold office until the next such meeting.

2.9 Remuneration of Auditors⁵

In the case of auditors appointed by the directors, the auditors' remuneration may be fixed by the directors. In all other cases, the auditors' remuneration is fixed by the company at the AGM.

2.10 Auditors' Duties

Auditors' principal duties are as follows:

2.10.1 Duty to Provide an Audit Report

The principal duty of the auditors to a company is to report to the members of the company on the financial statements examined by them⁶. The auditors' report must be read at the AGM and should be

made available to every member of the company.

The auditors' report must state whether, in their opinion:

- the company has maintained proper books of account;
- proper returns have been received from branches of the company not visited by the auditor (Where a company operates a number of branches, it may not have been possible for the auditor to visit all during the course of the audit. Where this is the case, the auditor will usually seek to visit all branches at least once over a number of annual audits);
- the financial statements have been properly prepared in accordance with the provisions of the Companies Acts and give a true and fair view of the company's affairs and of its profit (or loss);
- in the case of a group of companies, the group financial statements give a true and fair view of the state of affairs and profit (or loss) of the undertakings included so far as concerns the members in accordance with the provisions of the Companies Acts;
- there has been a serious loss of capital requiring the convening of an extraordinary general meeting;
- the information contained in the directors' report is consistent with the financial statements.

The auditors' report must also state whether:

- they have obtained all the information and explanations they considered necessary for the purposes of the audit, and;
- the company's balance sheet and profit and loss account are in agreement with the books of account.

By law, the directors are required to disclose certain information in the financial statements e.g. detailed particulars of directors' emoluments such as salaries, fees, taxable expenses, pension contributions and other benefits. Where the financial statements do not provide this information, the auditors are required to provide it in their report.

Where the auditors cannot report positively on any of the above matters, they may find it necessary to 'qualify' their audit report giving reasons for the qualification. A qualified audit report can take two forms, namely:

- a 'disclaimer of opinion', in which the auditors state that they are unable to form an opinion as to whether the financial statements give a true and fair view. A disclaimer of opinion will arise where the scope of the auditors' work has been limited in some way e.g. they have been unable to gain access to all of the books and records, or;
- an 'adverse opinion', in which the auditors state that the financial statements do not give a true and fair view. An adverse opinion will be given where the auditors are in disagreement with the financial statements and the directors are not prepared to amend them to reflect what the auditor considers to be a true and fair view.

2.10.2 Duty to Report Failure to Maintain Proper Books of Account⁷

Where auditors form the opinion that the company being audited is contravening, or has contravened, its obligations to maintain proper books of account, they are obliged to serve a notice on the company informing it of that opinion. If the necessary steps are not taken by the directors within seven days to ensure that proper books of

account are maintained, the auditors are required to notify this to the Registrar of Companies, who in turn will notify the Director of Corporate Enforcement.

Where the Director of Corporate Enforcement subsequently requests the auditors to do so, they are required to furnish the Director with such information, including an explanation of the reasons for their opinion and give the Director access to documents, including facilities for inspecting and copying them.

2.10.3 Duty to Report Indictable Offences⁸

As a result of the Company Law Enforcement Act, 2001, auditors are now required to make a report to the Director of Corporate Enforcement where during the course of, and by virtue of, carrying out an audit, information comes into their possession which leads them to form the opinion that the company, or an officer or agent of it, has committed an indictable offence under the Companies Acts.

In their report to the Director under this section, auditors are required to set out details of the grounds on which they have formed their opinion. The Director has, in conjunction with the Auditing Practices Board (APB) and the Consultative Committee of Accountancy Bodies – Ireland (CCAB-I) published detailed guidance to auditors on their responsibilities under this section⁹.

2.10.4 Duty to Exercise Professional Integrity¹⁰

Auditors are under a duty to carry out the audit with professional integrity. In preparing their report, auditors must exercise the skill, care and caution of a reasonably competent, careful and cautious auditor. Where auditors do not comply with their duty to exercise reasonable skill and care, they may be liable for damages:

⁷ Section 194 Companies Act, 1990 as amended by section 74 Company Law Enforcement Act, 2001

⁸ Section 194(5) Companies Act, 1990 as inserted by section 74 Company Law Enforcement Act, 2001

⁹ The guidance, which is contained in Decision Notice D/2002/2 'The Duty of Auditors to Report to the Director of Corporate Enforcement', is available on the ODCE website (address: www.odce.ie). As the guidance was issued jointly with the Auditing Practices Board (APB), the guidance has also been published in the form of an APB Audit Bulletin.

¹⁰ Section 193(6) Companies Act, 1990

- to the company under their contract; and/or;
- to those parties to whom they owe a duty of care for negligence, including the company, the members and, in certain limited circumstances, prospective shareholders.

Auditors cannot exclude their liability to the company, nor can auditors have a company indemnify (insure) them against any liability to third parties in respect of negligence.

2.10.5 Duty to Furnish Evidence of Qualifications¹¹

An auditor, or a person purporting to act as an auditor, is required to provide to the Director of Corporate Enforcement on request evidence of his or her qualifications to so act.

2.11 Auditors' Rights

Auditors of companies have the following rights:

2.11.1 Right of Access¹²

Auditors have the right of access at all reasonable times to the books, accounts and vouchers of the company. They can require from the company's officers and employees such information and explanations that are necessary for the performance of their duties¹³. A person who fails to comply with such a request within a reasonable time, or who knowingly gives false information, is in breach of the Companies Acts.

Subsidiary companies incorporated in the State and their auditors are also required to give the auditor of the holding company such information and explanations as that auditor may reasonably require for the purposes of their duties. Where the company has subsidiaries outside the State, the company itself is obliged to take all

reasonable steps to obtain such information and explanations for the auditors.

2.11.2 Right of Notification and Attendance at Company General Meetings¹⁴

Auditors are entitled to attend any general meeting of the company and to receive the same notices and communications relating to meetings as the members. They also have the right to be heard at all general meetings on any part of the meeting that concerns them.

2.11.3 Rights Regarding Removal and Non-reappointment¹⁵

Auditors may be removed by resolution of a general meeting or by way of resolution appointing someone else instead of them. Where such a course of action is proposed, auditors are entitled to contest their proposed removal and to explain the circumstances of their proposed removal to the members.

An auditor is permitted to resign from office before the expiry of his or her term of appointment by serving notice in writing on the company. Resigning auditors or auditors who are unwilling to be reappointed must state in their notice of resignation the circumstances connected with the resignation which they consider ought to be brought to the notice of the members and creditors or if there are none, that no such circumstances exist.

Where, at an annual general meeting, no auditors are appointed or reappointed, the company must inform the Minister for Enterprise, Trade and Employment of this within one week and the Minister may then appoint auditors to the company.

¹¹ Section 187(12)(a) Companies Act, 1990 as inserted by section 72 Company Law Enforcement Act, 2001

¹² Section 193 Companies Act, 1990

¹³ Section 197(3) Companies Act, 1990 states: "An officer of a company who fails to provide to the auditors of the company or of the holding company of the company, within two days of the making of the relevant request, any information or explanations that the auditors require as auditors of the company or of the holding company of the company and that is within the knowledge of or can be procured by the officer shall be guilty of an offence".

¹⁴ Section 193 Companies Act, 1990

¹⁵ Section 161 Companies Act, 1963 as amended by section 184 Companies Act, 1990

3.0 Penalties Under the Companies Acts

3.1 Penalties for Criminal Offences

Court Imposed Penalties

Under the Companies Acts, provision is made for two types of criminal offence, namely summary and indictable offences. A summary offence is generally of a less serious nature and is tried before a judge only in the District Court. Indictable offences are generally of a more serious nature. Indictable offences can, in the same way as summary offences, be tried in the District Court before a judge only. However, the distinction between a summary offence and an indictable offence is that, due to their more serious nature, indictable offences can also be tried in the Circuit Court i.e. before a judge and jury. Where this course is taken, the indictable offence is said to be prosecuted on indictment.

Where an offence is prosecuted on indictment, the penalties provided for by the law on conviction are generally considerably higher than had the offence been prosecuted summarily.

In general the maximum penalty on conviction:

- of a summary offence under the Companies Acts is €1,900 and/or 12 months imprisonment, and;
- of an indictable offence under the Companies Acts is €12,700 and/or 5 years imprisonment.

However, the Companies Acts also provide for considerably higher sanctions in respect of certain offences e.g. fraudulent trading (€63,000 and/or 7 years imprisonment on conviction on indictment) and insider dealing (€254,000 and/or 10 years imprisonment on conviction on indictment).

Administrative Fines

Under the provisions of the Company Law Enforcement Act, 2001, the Director of Corporate Enforcement also has the discretion to impose an administrative fine rather than initiating a summary prosecution. Where the Director chooses this course of action, provided that the fine is paid and the default in question is remedied within 21 days, no prosecution will ensue¹⁶.

3.2 Civil Penalties

Disqualification

In addition to fines and penalties, there are also provisions for other sanctions under the Acts. Persons convicted on indictment of an indictable offence relating to a company or involving fraud or dishonesty are automatically disqualified from acting as company directors/officers (see Appendix B to Information Book 2 – Company Directors).

The Director of Corporate Enforcement can also apply to the Courts seeking the disqualification of any person:

- guilty of two or more offences of failing to maintain proper books of account, or;
- guilty of three or more defaults under the Companies Acts.

Restriction

The provisions relating to the restriction of company directors apply to insolvent companies i.e. companies that are unable to pay their debts as they fall due. Where a company which goes into liquidation or receivership¹⁷ is insolvent, a director of the company who fails to satisfy the High Court that he or she has acted honestly and responsibly will be restricted for a period of up to five years.

¹⁶ Section 109 Company Law Enforcement Act, 2001

¹⁷ A liquidator's function is to collect and realise the assets of the company, to discharge the company's debts, to distribute any remaining surplus, investigate the company's affairs and to legally dissolve the company. The function of a receiver is to dispose of certain assets of the company in order to allow the repayment of a debt to a creditor e.g. a bank. See Information Book 7 for further information on liquidators and receivers.

Such a restriction prevents a person from being a director or secretary or being involved in the formation or promotion of any company unless it is adequately capitalised. In the case of a private company, the capital requirement is €63,487 (£50,000) in allotted paid up share capital, and in the case of a public company, €317,435 (£250,000). Such a company is also subject to stricter rules in relation to capital maintenance. The topic of restriction is dealt with in detail in Appendix B to Information Book 2.

Strike Off

Where a company defaults in performing certain of its legal obligations e.g. fails to file an annual return with the Registrar of Companies, the Registrar can strike the company off the register of companies.

If struck off the register, ownership of a company's assets automatically transfers to the State. Ownership will remain with the State until such time as the company is restored to the register. While struck off, the liability of every director, officer and member of the company continues and may be enforced as though the company had not been dissolved¹⁸.

The procedures required to have a company reinstated to the register are dealt with in Appendix A to Information Book 1.

4.0 Useful Addresses

Office of the Director of Corporate Enforcement,
16 Parnell Square,
Dublin 1.
Tel: 01 858 5800
Web: www.odce.ie

Companies Registration Office
14, Parnell Square,
Dublin 1.
Tel: 01 804 5200
Web: www.cro.ie

Department of Enterprise, Trade & Employment,
Kildare Street,
Dublin 2.
Tel: 01 631 2121
Web: www.entemp.ie

Company Law Review Group,
Earlsfort Centre,
Hatch Street Lower,
Dublin 2.
Tel: 01 631 2763
Web: www.clrg.org

Basis
Business Access to State Information & Services
Web: www.basis.ie