Chapter 3

AUDITORS' RIGHTS, APPOINTMENT, REMOVAL, RESIGNATION AND REGULATION

1. Auditors' rights and duties

So that they can carry out their duties properly, auditors have very powerful rights. For example:

- They have access to all records they require.
- They have a right to receive information and explanations of all transactions.
- They have a right to attend and receive notice about general meetings and they have right to speak at general meetings on relevant matters.

A general meeting is where the shareholders of the company come together, and the annual general meeting ensures that there should be at least one of these meetings every year. The auditors have the right to receive in advance information about any resolutions that are proposed to be put at these general meetings. And finally they have the right to require that the company's financial statements should be presented at the general meeting, otherwise of course if the financial statements contained information which the directors wanted to keep secret, the directors could delay presenting those.

Their right to be informed about, attend and speak at general meetings gives the auditors an opportunity to communicate directly with the shareholders – by whom they have been appointed and for whom they are acting.

Typical duties:

- To issue an audit report, giving opinions on:
- truth and fairness of the Financial Statements
- whether the Financial Statements are properly prepared
- any other opinions required.
- When leaving a client, to issue a Statement of Circumstances
- After resignation, to supply information to the new auditors.

An auditor:

- Must pass an approved set of professional examinations, set by a **Recognised Qualifying Body (RQB)** eg the **ACCA**
- Must become a member (and stay a member!) of a **Recognised Supervisory Body (RSB)** eg the ACCA
- The auditor must not be a **director or employee** of the company, or of any associated companies

The auditor must not be an **employee or business partner** of a director or employee of the company, or of any associated companies.

2. Appointment of auditors

Auditors have to be reappointed by resolution at every annual general meeting. Note that reappointment is not automatic. This is to prevent the incumbent auditors from simply staying in office. The requirement for a resolution means that the members have to take positive action to get auditors appointed.

Prior to the first annual general meeting the directors can appoint the first auditors or if an auditor resigns, for example, because he or she falls ill, the directors can appoint another auditor to fill a casual vacancy. This appointment will only last till next AGM.

If all else fails, in the UK, the Secretary of State, in other words the government, will ensure that all companies have an auditor.

The actions that the auditor should take when approached by a potential client are explained later.

3. Resignation of auditors

Auditors can resign by giving written notice and a statement of circumstances to the company.

A statement of circumstances explains why they have resigned. Written notice must also be sent to the regulatory authority and the members by the company by the company.

The thinking behind the statement of circumstance is that auditors may have resigned because they are deeply concerned about some aspect of the company's activities. So the statement of circumstances explains why the auditor has resigned, which could, of course, have been caused by perfectly innocent reasons, for example that the auditor wishes to cut back on work, or the auditor feels that the company is now too large for the auditing firm to deal with.

If the auditors are really concerned about the company and that's why they have resigned, they could also require the directors to call an extraordinary general meeting. The auditors can speak at these meetings, and therefore they can address the members and explain their concerns and why they have resigned.

4. Removal of auditors

Auditors can be removed from office. This would normally be at instigation of the directors, but does have to be ratified by the shareholders. They could be removed from office for perfectly legitimate reasons. Perhaps the auditors failed to the find a material fraud in the company and the directors have lost faith in them, or perhaps the company has now become international and a larger firm of auditors is needed.

However, the big fear is that the auditors were, perhaps, too good, too strict on insisting that certain aspects of the financial statements should be changed, or perhaps they issued a critical audit report that the directors didn' the accounts.

This is why the auditors are given the right to make representations about why they should stay in office. They have to deposit a statement of circumstance at company's office and this should be sent to the regulatory authority. The auditors can also receive notices, speak at a general meeting at which the term of their appointment would have expired. This allows the auditors, if necessary, to explain to shareholders what has happened and that they may have been removed without due cause.

5. Regulation

Auditors are regulated by:

- Professional bodies (eg ACCA)
- International bodies (eg IFAC, the International Federation of Accountants)
- National bodies (in the UK the FRC, Financial Reporting Council)

The purposes of IFAC are to serve public interest, strengthen the worldwide accountancy profession, establishing and promoting adherence to high-quality professional standards.

- **IAASB** (International Auditing and Assurance Standards Board): ISAs and other assurance standards
- **The International Ethics Standards Board for Accountants (IESBA)**: IFAC Code of Ethics.
- **TAC** (Transnational Auditors Committee): international dimension of audits.

IFAC ISAs are adopted by the FRC in the UK which has local regulatory power.

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