An Analysis of the Auditors’ Liability to Third Parties in Australia

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Abstract The purpose of this research paper is to provide a comprehensive analysis of the scope of auditors’ liability to third parties in Australia. In addition to examining the current legal position in Australia, the law on auditors’ liability in other jurisdictions, including the United Kingdom, United States, Canada and New Zealand, will be examined and compared to the extent of their influence on Australian laws. It is argued that auditors in Australia are subject to a greater scope of liability than in other countries. As a result, there is a need for reform of audit laws in Australia to limit the extent of auditors’ liability. Further, it is submitted that the development of future auditing laws in Australia should allow for the appropriate consideration of international trends in limiting liability. It is also anticipated that the proposed reforms will adequately safeguard auditors from the threat of litigation by third parties, and ultimately ensure that the floodgates for liability in Australia are not opened to an indeterminate level.

Keywords: Expectation Gap Theory, Deep Pockets Theory, proximity and reliance, disclaimers, contributory negligence, indeterminate liability, misleading and deceptive conduct, proportionate liability

I. Introduction

In recent decades, there has been a global upsurge in the number of corporate collapses and litigation claims by third parties, which have partly been explained by the economic recession occurring in the late 1980s.1 However, auditing professions in both Australia and around the world have encountered many difficulties and criticisms in recent years, as a result of corporate collapses being linked to allegations of

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professional negligence and the breach of statutory duties. Examples of high profile collapses occurring in Australia include the failures of HIH Insurance, Ansett and One Tel. In addition, overseas collapses include Enron Corporation and WorldCom in the United States. These allegations illustrate the seriousness of the current legal environment for the auditing profession, government and third parties. Thus, there is a continuing interest in understanding the law regarding auditors’ liability, given the large litigation claims brought by third parties ‘and the escalation costs of indemnity insurance cover in North America, Europe and Australia’.

**i. Auditors’ Liability in Australia**

The liability of auditors is an area of increasing significance, particularly in light of the changing and widening of auditor obligations in Australia. At present, auditors are subject to a vast regime of laws ranging from contract law to common law and statute. Various professional bodies including the Institute of Chartered Accountants in Australia (ICAA) and CPA Australia (CPA) regulate the conduct of accountants and auditors through the provision of standards and guidelines. Governmental agencies such as the Australian Securities and Investments Commission (ASIC) and the Australian Competition and Consumer Commission (ACCC) also govern the auditing profession.

Due to the many laws which have been imposed on the auditing profession in Australia, it is argued that auditors in this country are exposed to a greater level of liability than in other countries, such as the United Kingdom, United States, Canada and New Zealand. This is evidenced from the application of statutes such as the Corporations Act 2001 (Cth) and the Trade Practices Act 1974 (Cth), which effectively extend the liability of auditors to third parties. Therefore, reform of the law is necessary in order to limit auditors’ liability in Australia, by introducing systems of proportionate liability and statutory capping in line with international trends. The outcomes of this research will hopefully generate more knowledge and awareness about the current legal position of auditors in Australia.

**ii. Recent Cases Against Auditors**

In order to understand the impacts which litigation claims have had on the auditing profession, it is important to examine the cases brought against auditors in the past decade. The grounds for these

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3 G. Gill et al., Modern Auditing in Australia, 6th edn (John Wiley and Sons: Brisbane, 2001) 94.

4 See Free, above n. 1.
claims have often related to breaches of contract, professional negligence, and the contravention of statutory duties, as a result of the failure of auditors to give a true and fair view of a company's financial position. Some examples of recent cases involving auditors in Australia include an action under the trade practices legislation by the Linter Group against Price Waterhouse, which settled for an estimated $320 million. In 1996, the Australian Securities and Investments Commission (ASIC) initiated proceedings on behalf of Adelaide Steamship against Deloitte for the faulty audit of financial statements, an action totalling $340 million. Another case involving the Victorian Government and Peat Marwick Hungerfords in relation to the audit of the Tricontinental Bank settled for $136 million. All of these cases clearly highlight the excessive legal costs to which auditors are increasingly exposed. Thus, it is argued that any further extension of the scope of liability of auditors will detrimentally impact upon the provision of future audit services in Australia.

**iii. Structure of the Paper**

This paper is divided into eight main sections, each of which will detail various topics regarding auditors' liability. Section I highlights the significance of research and any anticipated outcomes. Section II deals with the definition of 'auditing', the role and functions of the auditor, and the types of users of audited financial reports. This will be followed by a review of the theoretical background surrounding auditors' liability, including the 'Expectation Gap' and 'Deep Pockets' theories. Next, section III will provide a comprehensive overview of the current legal position of auditors' liability in Australia and outline the professional bodies which regulate the auditing profession. There will be a detailed analysis of the auditor's duties and obligations to third parties under common law (section IV) and statute (section VI). Section V focuses on examining the case authorities regarding auditors' liability in various countries including the United Kingdom, United States, Canada and New Zealand. Section VII states several recommendations for reform of audit laws in Australia. Finally, the paper will close with a summary of the main findings in section VIII.

**iv. Scope and Limitations**

Due to the various limitations inherent in this paper, in terms of the scope of analysis and word length, there are a number of issues which will not be discussed in great detail. First, the main focus of this paper is on the roles, duties and liabilities of auditors in relation to companies and third parties. Thus, there will not be a detailed examination

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6 See Free, above n. 1 at 123.
7 See Anderson, above n. 5 at 357.
of the duties and responsibilities of directors or management, nor any associated corporate governance or agency issues. Secondly, the arguments presented in this paper are based from the perspective of the auditing profession; however, some attention will be given to highlighting the interests of third parties (including shareholders, investors, governmental bodies and insurance companies). Thirdly, a general overview of each country’s position in regard to auditors’ liability will be discussed only to the extent in which they influence Australian laws. Consequently, this paper does not intend to provide a comprehensive examination of the legal frameworks of the United Kingdom, United States, Canada or New Zealand. Further, any international data is predominantly sourced from case law authorities as these provide a more informative and comparable account of the scope of auditors’ liability. On the whole, these limitations should ensure that the focus of the paper remains purely on examining the current position regarding auditors’ liability in relation to third parties in Australia, and the potential for reform.

II. The Definition and Theory behind Auditing

i. Introduction

Auditing is now regarded as a sophisticated professional assurance service performed in the interests of a wide variety of parties including companies, shareholders and investors. The following parts of section II will discuss the meaning of the term ‘auditing’, as distinguished from ‘accounting’. The general role and functions of the auditor will then be outlined, followed by the different parties who rely on audited financial reports. Finally, the theories surrounding auditors’ liability will be presented, including the Expectation Gap Theory and the Deep Pockets Theory.

ii. The Definition of ‘Auditing’

The practice of auditing has become increasingly important in the corporate marketplace. The term ‘auditing’ is described as the accumulation and evaluation of information to determine whether a company’s financial report is in compliance with the established criteria and legislative requirements. By conducting an audit, an opinion is formed by the auditor as to the credibility of information contained in a company’s financial statements. Thus, the auditing process ensures

that figures in the financial statements are materially correct, which in turn adds value to such information.\textsuperscript{11}

(a) Auditing and Accounting Distinguished

It is important to distinguish ‘auditing’ from ‘accounting’, as the latter involves the ‘recording, classifying and summarising of economic events in a logical manner’.\textsuperscript{12} A public accountant provides non-attestation services including accounting, tax, banking and management consulting services.\textsuperscript{13} In contrast, an auditor provides assurance services and has a duty to determine the reliability and relevance of accounting information.\textsuperscript{14} This distinction is significant due to the inherent legal liability attached to the auditing profession.

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iii. Roles and Functions of the Auditor

Auditors play a critical role in the contemporary corporate marketplace and are often regarded as ‘watchdogs’ in overseeing a company’s affairs.\textsuperscript{15} The main role of the auditor is to develop a qualified audit system with effective controls to guard against mistakes and fraud (all of which have the potential to cause corporate collapses).\textsuperscript{16} Hence, auditors have a duty to warn management of any irregularities contained in a company’s financial reports.\textsuperscript{17} In terms of the common law, Moffitt J in \textit{Pacific Acceptance Corporation Ltd v Forsyth}\textsuperscript{18} stated that the function of an auditor is to provide an opinion regarding the compliance of the financial reports with the relevant accounting standards and the common law. In addition, auditors must possess the relevant skill and expertise to accumulate audit evidence, interpret findings, and form an independent opinion on the truth and fairness of financial statements in accordance with legislative requirements.\textsuperscript{19} Auditors must also perform their duties with reasonable skill and care, as established in \textit{Kingston Cotton Mill Co.}\textsuperscript{20} Therefore, auditors perform a very important function in the marketplace and are subject to a wide range of obligations.
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iv. Users of Assurance Services

There are many types of users who rely on audited financial statements in order to make business and investment decisions. One type
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\textsuperscript{11} Ibid.
\textsuperscript{12} See Arens et al., above n. 9 at 14.
\textsuperscript{13} Ibid. at 7.
\textsuperscript{14} Ibid. at 14.
\textsuperscript{17} See Latimer, above n. 15 at 666.
\textsuperscript{18} (1970) 92 WN (NSW) 29. As cited in Rajacic et al., above n. 10 at 207.
\textsuperscript{19} See Arens et al., above n. 9 at 14.
\textsuperscript{20} (No. 2) (1896) 2 Ch 279.
of user is the company which engages the auditors’ professional services. Auditors are directly liable to a company, due to the nature and privity of the relationship under contract law. This principle is supported in *Simonious Vischer & Co v Holt & Thompson* where Sheppard J stated that ‘an auditor is bound by contract, in consideration of the fee which his client agrees to pay him, to carry out the obligations imposed on him’. Further, it was stated by Lord Bridge in *Caparo Industries plc v Dickman* that, in advising the client, an auditor owes a duty to ‘exercise the standards of skill and care appropriate . . . and will be liable in both contract and tort’ for any losses caused by the breach of duty. Thus, the auditors’ contractual liability clearly extends to the client company.

Auditors may be liable to other external users including shareholders, investors, creditors and other third parties who rely on audited information. Users often rely on audited statements to provide an unbiased and independent opinion on a company’s financial position. Shareholders rely on audited reports presented in a company’s prospectus in order to make decisions regarding the purchase of securities. Investors require assurances as to the correctness of a company’s reports for the purposes of gaining access to capital resources, and for making decisions regarding mergers and business acquisitions. Further, financial institutions often examine the audited statements of a company before approving loan transactions to relevant parties. For these reasons, it is necessary for auditors to be aware of the different types of users to whom they are potentially liable.

**v. Theoretical Background behind Auditors’ Liability**

(a) Expectation Gap Theory
In many circumstances, particularly in the case of corporate collapses, investors and lenders wrongly treat business failures as audit failures. There is a tendency for third parties to blame auditors for the failures of directors and senior management in supervising the business and its operations. The difference in perceptions of the auditors’ role between users and auditors is explained by the ‘Expectation Gap Theory’. This theory suggests that the users of financial statements expect auditors to provide assurances concerning ‘material

21 See Free, above n. 1.
23 [1990] 1 All ER 568.
24 See Free, above n. 1 at 121.
25 See Rajacic *et al.*, above n. 10 at 208.
26 See Arens *et al.*, above n. 9 at 4.
27 See Free, above n. 1 at 121.
fraud, irregularities and the viability of the business and its manage-
ment'. In reality, the auditor has a duty to give a 'reasonable assur-
ance' as to whether or not financial reports are free from material
misstatement, and should not be perceived as providing an absolute
guarantee on the accuracy of financial statements. Therefore, it is
the directors' and management's responsibility to maintain proper
financial records and internal controls.

(b) Deep Pockets Theory
Third parties will often look towards the auditor 'when searching for a
solvent party from whom losses may be recovered', even though aud-
itors do not provide a guarantee as to the viability of a company.
This is referred to as the 'Deep Pockets Theory' whereby shareholders
and creditors tend to sue auditors for breach of common law and
statutory duties. The reason auditors are regarded as having 'deep
pockets' is because they are required by law to carry professional
indemnity insurance. Auditors are targeted by third parties because
there is little advantage in bringing proceedings against a company
that is insolvent, or whose assets are difficult to locate or realize.
This is despite the fact that there may be good arguable claims against
a company, especially where the directors and management are
clearly at fault. Overall, these theories provide an explanation for the
high instances of litigation against auditors by third parties seeking
compensation.

III. Professional Accounting and Auditing Bodies

i. Introduction
This section identifies the various professional bodies which govern
and regulate the auditing profession in Australia. These bodies are
also responsible for initiating disciplinary procedures against member
auditors involved in breach of duties. There will be a general discus-
sion on the auditing standards and guidelines, followed by an argu-
ment as to whether such standards should be legally enforceable by
the courts.

29 See Gill et al., above n. 3 at 75.
30 See Arens et al., above n. 9 at 113.
31 In addition, the legislative requirements under the Corporations Act 2001 (Cth),
s. 296 impose a duty on directors to ensure that financial records comply with
accounting standards.
32 See Free, above n. 1 at 121.
33 Ibid. at 133.
34 Ibid.
35 M. Duffy, 'Proportionate Liability: A Disproportionate and Problematic Reform'
(2003) 60 Plaintiff 8 at 11.
36 Ibid.
ii. Professional Bodies

There are a number of self-regulatory professional bodies which govern the auditing profession in Australia. These bodies include the Institute of Chartered Accountants in Australia (ICAA) and CPA Australia (CPA), both of which exert an important influence on accountants and auditors. These associations impose various standards and rules of conduct on members in regard to the provision of accounting and audit services. Another important body is the Australian Accounting Standards Board (AASB), which has the power to issue accounting standards for the purposes of the Corporations Act 2001 (Cth). The types of standards which auditors are expected to follow include the Statement of Accounting Standards, Auditing Guidance Statements, Generally Accepted Auditing Standards and the Statement of Auditing Standards (AUS) which is the most authoritative reference available to auditors. Hence, these professional associations perform a vital role in developing standards to ensure that auditors provide an independent and appropriate examination of a company’s financial statements.

(a) Disciplinary Bodies

Professional accounting bodies in Australia have established disciplinary committees similar to those of other professions. Disciplinary proceedings are initiated by the ICAA under the National Disciplinary Committee, and by the CPA under the Disciplinary Committee in each state. These committees have the power to impose penalties and sanctions on auditors where there is a breach of the professional standards of care and skill. Penalties which may be imposed include the forfeiture or suspension of membership, fines (maximum $100,000), reprimands, orders for the payment of costs, and requiring members to attend professional development courses. On the whole, there is not much evidence as to whether these committees are active in imposing sanctions on members, as most actions against auditors are either brought before the courts or government administrative agencies.

37 In addition, the Financial Reporting Council (established under the Australian Securities and Investments Commission Act 2001 (Cth), s. 1) is responsible for overseeing the setting of accounting standards by the AASB. See Latimer, above n. 15 at 649.
38 See Arens et al., above n. 9 at 22.
39 For example, the legal profession in Queensland has its own disciplinary body known as the Legal Ombudsman (established under Part 2B of the Queensland Law Society Act 1952), which has power to impose sanctions on solicitors who engage in professional misconduct.
40 See Gill et al., above n. 3 at 79.
41 Ibid.
42 Ibid.
iii. Auditing Standards and Guidelines

(a) Significance of the Audit Opinion
The main objective of providing auditing standards is 'to enable the auditor to express an opinion whether the financial report is prepared, in all material aspects, in accordance with an identified financial reporting framework'. The types of financial statements which are subject to an audit include a company's Statement of Financial Position, Statement of Financial Performance, Cash Flow Statement and so forth. The standards provided in the AUS refer to the objectives of the audit, terms of engagement, level of quality control and methods of detecting irregularities. The standards require auditors to 'accumulate sufficient appropriate audit evidence to express the audit opinion' as to the credibility of financial reports. Professional standards have the effect of improving auditing services by providing 'a measure of quality against which all completed audits are judged'. Therefore, auditing standards assist auditors in fulfilling their professional responsibilities to the company as well as third parties.

(b) Nature of Auditing Standards
Professional standards and guidelines are voluntarily imposed upon auditors; therefore they are not legally enforceable under the law. The reason is that most standards are vague, broadly interpreted and merely 'guide' the auditor in conducting an audit of financial statements. However, the courts will have regard to the practices and standards of the profession in establishing whether auditors have acted within the reasonable standard of care. Further, as standards are susceptible to change, Moffitt J in Pacific Acceptance Corporation Ltd v Forsyth stated that 'it was not a question of the court requiring higher standards because the profession had adopted higher standards'. It is thus left to the courts to apply the law based on 'such reasonable standards as would meet the circumstances of today, including modern conditions of business and knowledge concerning them'. Therefore, although professional standards are considered, the courts have formulated their own common law and statutory tests in determining whether auditors are liable to companies and third parties. An interesting development in the law at present is that the Commonwealth Government's Corporate Law Economic Reform Program (CLERP) 9 Bill proposes to give legal force to auditing standards.

43 AUS 202. See Appendix A to this paper: Statement of Auditing Standards.
44 Ibid.
45 Ibid.
46 See Rajacic et al., above n. 10 at 209.
47 See Gill et al., above n. 3 at 22.
48 See Free, above n. 1 at 124.
50 See Latimer, above n. 15 at 202.
51 Ibid.
The effect of this proposal is likely to be an increase in the duties to which auditors are subject, which consequently expands the scope of auditors' liability in Australia.

IV. Auditors' Liability under Common Law in Australia

i. Introduction

Over the years, there have been many common law developments regarding the scope of auditors' liability in Australia. Generally, the common law tort of negligence requires that there be (1) a duty of care, (2) a breach of the duty, and (3) that damage was caused by the breach. Thus, some of the following cases have found that auditors owe a duty of care to third parties for loss or damage suffered as a result of the negligent misstatement of financial reports. Several principles used in establishing auditors' liability will be discussed, including tests of reasonable foreseeability, proximity, reliance and causation.

ii. Standard of Care

A duty is imposed on auditors to exercise reasonable skill and care in auditing a company's financial statements. This duty was established in Pacific Acceptance Corporation Limited v Forsyth where the defendant auditors were held to be negligent in failing to inform the plaintiff of the existence of fraud and irregularities relating to certain loans. Therefore, in order for a plaintiff to make a successful claim in negligence, it must be proven that an auditor has acted carelessly in failing to meet the sufficient standard of care.

iii. The Tests of Proximity and Reliance

The Australian courts initially restricted the finding of auditors' liability in relation to third parties by using the test of proximity formulated by Barwick CJ in Mutual Life and Citizens' Assurance Co Ltd v Evatt to establish the existence of a duty of care. A proximate relationship was held to exist where an auditor knows or ought to have known that the plaintiff intended to use the information or advice for a particular purpose. Further tests of reliance were also developed in San

53 Ibid.
54 See Rajacic et al., above n. 10 at 207.
56 See Arens et al., above n. 9 at 118.
57 See Anderson, above n. 5 at 358.
58 (1968) 122 CLR 556.
Sebastian Pty Ltd v The Minister\(^{60}\) which was authority for the principle that auditors owe a duty of care to third parties where ‘a statement was made to the plaintiff, or a class of persons which included the plaintiff, with the intention of inducing them to act in reliance thereon’.\(^{61}\) This view was supported in *R Lowe Lippman Figdor and Franck v AGC (Advances) Ltd*,\(^{62}\) in which the courts found in favour of the auditors in limiting the scope of liability.

In contrast, the Supreme Court of New South Wales in the case of *Columbia Coffee & Tea Pty Ltd v Churchill*,\(^{63}\) invoked uncertainty in the law by holding auditors liable to third parties where there is an assumption of responsibility. The facts involve a plaintiff investor who brought an action against the auditors for losses suffered as a result of relying on audited financial reports, which had the effect of understating the company’s debts. In terms of liability to third parties, the courts held that auditors owe a duty of care to a plaintiff corporation as a potential purchaser of shares.\(^{64}\) Further, in applying a broad test of reasonable foreseeability, the duty of care is owed to a class of persons wider than the company and its shareholders only when it expressly assumes responsibility.\(^{65}\) In this case, the facts indicated that an assumption of responsibility was contained in the auditor’s audit manual. This amounted to an acknowledgement of liability by the auditor to parties who relied on the reports, clearly extending liability beyond the company which engaged the auditor’s services.\(^{66}\) Although the plaintiff failed to establish causation between the auditor’s breach of duty and the losses suffered, the principles of reasonable foreseeability and assumption of responsibility had the effect of increasing the scope of auditors’ liability to third parties.\(^{67}\)

**iv. The Current Position Regarding Liability**

The case of *Esanda Finance Corp Ltd v Peat Marwick Hungerfords (reg)*\(^{68}\) (*Esanda Finance*) illustrates the current stance in Australia regarding auditors’ liability and has clarified previous disparities in the law. The High Court effectively narrowed the scope of liability of auditors by denying third parties success in their claim against the

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60 (1986) 162 CLR 340.
61 See Hogg, above n. 59 at 81.
62 [1992] VR 671. The decisions of this case were also in line with the House of Lords judgment in *Caparo Industries plc v Dickman* [1990] 2 WLR 358. In *Caparo*, the plaintiff financiers suffered loss as a result of relying on the auditor’s unqualified report before providing further finance to a company, which subsequently became insolvent. The courts ruled that no duty of care arose between the auditors and the plaintiff. G. Goldman, ‘Where Do Auditors Stand?’ (1993) 63(3) *Australian Accountant* 60.
64 See Rajacic et al., above n. 10 at 219.
65 See Goldman, above n. 62 at 61.
66 Ibid.
68 (1997) 142 ALR 750.
auditors for negligent misstatement. The facts involved a plaintiff finance company which suffered loss as a result of relying on the audited reports prepared by the defendant, in approving loans to the defendant’s client company. In finding in favour of the defendant, the courts held that the auditors were ‘merely reporting in the ordinary course to members of the company and had not intended the financier to act on the audited accounts’. Thus, although the auditors had knowledge that the reports did not indicate the company’s true financial position, the reports were not prepared for the purposes of the finance company.

Additionally, in response to the findings in Columbia Coffee & Tea Pty Ltd v Churchill, the judges in Esanda Finance stated that an audit manual does not amount to an auditor’s assumption of responsibility to third parties. In terms of proving reasonable reliance, Brennan CJ stated that the report must have been prepared with the knowledge that it would be conveyed to a third party to rely upon, and that the third party suffered loss as a result of placing reliance on the audited information. In applying the tests to the case, the courts found that the plaintiff financier unreasonably relied on the audited information, and should have made further enquiries to obtain the true position of the company before lending finance. Therefore, the auditors did not owe a duty of care to the plaintiffs for the audited financial statements, because the tests of proximity, reliance and causation were not satisfied. Overall, the findings in Esanda Finance should comfort auditors in relation to their liability to third parties, as the case has established a number of strict tests which must be satisfied in determining cases of negligent misstatement.

**v. Effectiveness of Disclaimers**

Auditors often use disclaimer clauses in order to limit liability in relation to audited financial reports supplied to companies and third parties. The position in Australia is illustrated by the adoption of the principles in the English judgment of Hedley Byrne v Heller which involved the existence of a disclaimer in the audited financial statements. Based on the facts, the plaintiffs satisfied the requisite tests of proximity, reasonable reliance and causation in establishing negligence against the auditors. However, the courts eventually found in favour of the defendants due to the existence of an effective disclaimer provision. Thus, disclaimers are effective in Australia provided they

69 Ibid.
70 See Goldman, above n. 62.
71 Ibid.
73 See Gill et al., above n. 3 at 115.
74 The finding in Esanda Finance was consistent with the English decision in Caparo Industries plc v Dickman (1990) 2 WLR 358. See Goldman, above n. 62.
75 See Free, above n. 1 at 121.
are in compliance with the statutory obligations under the Corporations Act 2001 (Cth) and the Trade Practices Act 1974 (Cth).

**vi. Contributory Negligence**

The defence of contributory negligence is available to auditors under the common law. The relevant authority is *AWA Ltd v Daniels T/A Deloitte Haskins & Sells & Ors*\(^{77}\) in which the Supreme Court of New South Wales held that the plaintiff company failed to meet the standard of care required for its own protection and was thus proportionately liable along with the auditors. This judgment overruled the decision in *Pacific Acceptance Corporation v Forsyth*\(^{78}\) where Moffitt J stated that ‘auditors may not be excused from negligence on the grounds that the client’s directors or employees were also negligent’.\(^{79}\) Thus, the existence of the defence is a positive move towards proportioning liability and is in accordance with the policy reasons set out in *Brown & Hatton v National Australia Bank*,\(^{80}\) in which Rogers J stated that ‘directors should bear their proper share of responsibility with respect to the losses suffered by their company’. This is because it would be unjust and inappropriate for directors to escape liability completely, especially where the full burden falls on auditors to compensate aggrieved parties.\(^{81}\) Overall, the defence of contributory negligence attempts to apportion blame fairly amongst those parties responsible, particularly where financial losses are attributable to a third party’s own commercial misjudgment.\(^{82}\)

**vii. Common Law Remedies**

Damages under the tort of negligence for pure economic loss aim to restore the plaintiff to the position they would have been in if not for the tort.\(^{83}\) Therefore, once a defendant auditor is found liable under negligence, the plaintiff is then entitled to recover losses based on the law of restitution. Where there is more than one defendant, ‘all wrongdoing defendants will be both jointly and severally liable for the damage caused’.\(^{84}\) Consequently, if one of the defendants is found liable, the plaintiff has the opportunity to recover the full amount of compensation from that defendant.\(^{85}\) Finally, in cases involving contributory negligence of directors of a company or third parties, the outcome will be a reduction in the plaintiff’s damages entitlement.\(^{86}\)

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77 (1992) 10 ACLC 933.
79 See Gill *et al.*, above n. 3 at 21.
80 1987, unreported, Supreme Court of New South Wales. As cited in Free, above n. 1 at 129.
82 See Rajacic *et al.*, above n. 10 at 209.
83 See Free, above n. 1 at 124.
84 See Duffy, above n. 35 at 11.
86 See Free, above n. 1 at 124.
V. Auditors' Liability in Other Countries

i. Introduction

Section V aims to compare the current common law position in Australia in regard to auditors’ liability with the various case law authorities of other countries including the United Kingdom, United States, Canada and New Zealand. It is submitted that some of these overseas judgments and policy arguments have influenced the development of auditors’ liability in Australia. Further, it appears that there is an international trend in limiting auditors’ liability by denying third parties from seeking compensation.

ii. United Kingdom

The Australian common law system stems from English origins and hence there are many similarities between the two countries in determining the existence of negligence. The following precedents indicate that the English courts have taken a more cautious approach to auditors’ liability since the decision in Hedley Byrne.87

(a) Negligent Misstatement and Proximity of Relationship

In Hedley Byrne and Company Limited v Heller and Partners Limited88 (Hedley) the English courts overturned the decision in Candler v Crane, Christmas & Co89 by which auditors were originally protected from making negligent misstatements. The obiter judgment in Hedley effectively extended the liability for economic loss beyond the strict rules of contract and was authority for the principle that auditors owe a duty of care to third parties provided there is a relationship of sufficient proximity.90 The courts established a ‘special relationship’ test which was restricted to circumstances where the parties providing statements or advice were experts, persons with special skill or where it was foreseeable that a third party might reasonably rely on such skill.91 Overall, the defendant auditors in this case would have been found liable if not for the presence of an effective disclaimer clause.

(b) Reasonable Reliance and Causation Reinforced

Nearly 20 years later, the courts in JEB Fasteners Ltd v Mark Bloom & Co92 reinforced the principles of proximity and reasonable reliance, in

89 [1951] 2 KB 164.
90 See Rajacic et al., above n. 10 at 214.
91 The principles of reasonable reliance and special skill were later supported in the Australian decision, L Shaddock & Associates Pty Ltd v Parramatta City Council (No.1) (1981) 150 CLR 225. See Arens et al., above n. 9 at 118.
92 [1981] 3 All ER 269.
which third parties could successfully sue auditors for negligent misstatement. The facts of this case involved a plaintiff who sued the auditors for losses suffered as a result of relying on negligently prepared financial accounts. Although the plaintiffs were unsuccessful in their action against the auditors, the courts emphasized that the principal tests of reliance and causation must be satisfied in determining the existence of negligence.\(^93\)

**(c) Liability to Third Parties**

The decision in *Caparo Industries plc v Dickman*\(^94\) is now regarded as the landmark case in redefining the concept of proximity used to limit the auditor’s liability ‘for economic loss suffered by potential investors and individual shareholders’.\(^95\) The facts involved the audit of a company in which the plaintiff was a shareholder. The plaintiff relied on the audited financial statements prepared by the defendant and subsequently sought to take over the company.\(^96\) However, it was later disclosed that the corporation was in fact operating at a significant loss.\(^97\) This case is authority for the principle that auditors owe a duty of care to existing shareholders whom the auditor knew would rely on audited reports.\(^98\) The court took a narrow approach to liability, whereby the auditor must have actual knowledge of the purpose for which the plaintiff relies on the statement, at the time of making the statement.\(^99\)

Additionally, the courts held that the shareholders’ interest in audited financial statements is a collective one, therefore auditors owe a duty to the shareholders as a whole and not to any individual member.\(^100\) Therefore, as the auditors had no knowledge that the audited accounts would be relied upon for the purposes of investment, ‘the plaintiff was unable to recover the loss suffered when it increased its shareholding in the client company in reliance upon the accounts which contained an overstatement of the value of the shares’.\(^101\) This decision found in favour of the auditors and has since been supported by the Australian courts in *R Lowe Lippman Figdor and Franck v AGC (Advances) Ltd*\(^102\) and *Esanda Finance Corp Ltd v Peat Marwick Hungerfords (reg).*\(^103\)

\(^93\) M. Mills, ‘The Expectation Gap and Auditors’ Responsibilities’ (1990) 20 *University of Western Australia Law Review* 538 at 556.

\(^94\) [1990] 1 All ER 568.

\(^95\) See Gill *et al.*, above n. 3 at 21.

\(^96\) See Rajacic *et al.*, above n. 10 at 216.

\(^97\) Ibid.

\(^98\) See Arens *et al.*, above n. 9 at 110.

\(^99\) See Hogg, above n. 59 at 80.

\(^100\) [1990] 2 WLR 358. As cited in Chan, above n. 2 at 30.

\(^101\) See Hogg, above n. 59 at 80.


\(^103\) (1997) 142 ALR 750.
iii. United States

In the United States (US), there are several principles used in determining whether auditors are liable to third parties. The US courts have been cautious not to expand auditors’ liability to an indeterminate level.

(a) Liability under Contract
In America, the doctrine of privity established in *Landell v Lybrand*104 restricts the liability of auditors to those parties with whom there is a contractual relationship.105 This means that auditors are only liable to the client who ‘contracts for or engages in the audit services’. The case of *Credit Alliance v Arthur Andersen and Co*106 developed a test for determining the existence of a contractual relationship.107 First, the auditor must have known that the financial reports were to be used for a particular purpose. Secondly, the plaintiff relied on the audited reports and thirdly, the auditor knew the plaintiff would rely on such reports.108 Thus, there is a tendency for the US courts to limit auditors’ liability to instances where privity of contract is established. Further, liability will only extend the relationship of privity cases where auditors are found guilty of gross negligence amounting to fraud.109

(b) Test of Reasonable Foreseeability
The judicial trend in the US appears to apply a test of foreseeability per se.110 The Californian Supreme Court in *Billy v Arthur Young & Co*111 held that ‘accountants do not owe a duty of care to all persons who reasonably and foreseeably rely on accountants’ professional opinions’. In contrast, the Supreme Court at Ohio in *Haddon View Investment Co v Coopers & Lybrand*112 held that ‘an accountant may be liable to a third party for professional negligence where the third party is a member of a limited class whose reliance on the accountant’s representation is specifically foreseen’.113 In regard to establishing auditors’ liability in Australia, the principles in *Esanda Finance Corp Ltd v Peat Marwick Hungerfords (reg)*114 require that further tests

104 107 A 783 (Pa 1919).
107 See Anderson, above n. 105 at 21.
108 Ibid.
109 Ibid.
110 See Livanes, above n. 67.
112 436 NE 2d 212 (Ohio 1982).
113 See Anderson, above n. 105 at 23.
114 (1997) 142 ALR 750.
of proximity and causation be satisfied, in addition to the test of reasonable foreseeability.

(c) Liability of Professional Bodies
It was reinforced in Waters v Autotri\textsuperscript{115} that unless there is evidence of privity of contract or a statutory duty which holds auditors liable to third parties, the courts are reluctant to establish a duty of care. Interestingly, the plaintiff in this case attempted to sue the American Institute of Certified Practicing Accountants (AICPA) for the 'negligent promulgation of professional accounting standards'.\textsuperscript{116} However, it was held that such standards could not be interpreted as an assumption of responsibility by the AICPA of a duty of care to third parties.\textsuperscript{117} At present, there are no statutory provisions under Australian laws which extend liability to professional accounting bodies. Further, any claims made against the professional bodies by third parties would most likely fail to satisfy the tests of foreseeability, proximity and causation.

(d) Indeterminate Liability to Third Parties
In the much quoted case of Ultramarines Corporation v Touche,\textsuperscript{118} Cardozo J warned of the potential consequences associated with expanding auditors' liability. Doing so would result in auditors being liable 'for an indeterminate amount, for an indeterminate time, to an indeterminate class'.\textsuperscript{119} Other detrimental effects which may be caused by increasing the scope of liability are illustrated in H Rosenblum Inc v Adler.\textsuperscript{120} In this case, the Supreme Court of New Jersey stated that 'extra costs placed on auditors from a widening duty of care, either due to more careful auditing or from additional professional liability insurance, could be passed on by the client to its shareholders and customers'.\textsuperscript{121} Thus, Australian courts have considered these US policy arguments in being careful not to open the floodgates for litigation by third parties.

\textit{iv. Canada}

Previously, the Canadian courts have tended to award the plaintiff for losses caused by the negligent audit of a company's financial reports. However, the courts have now applied a stricter approach to determining auditors' liability in line with other countries.

\textsuperscript{116} \textit{Ibid.}
\textsuperscript{117} \textit{Ibid.}
\textsuperscript{118} 174 NE 441 at 444 (1931).
\textsuperscript{119} See Anderson, above n. 105 at 19.
\textsuperscript{120} 461 A 2d 13 (NJ 1983).
\textsuperscript{121} See Anderson, above n. 105 at 24.
(a) Liability to Third Parties
In *Haig v Bamford*,122 the Supreme Court of Canada ‘upheld a finding of liability against accountants in negligence causing economic loss to persons not their clients’.123 In this case, the accountants were aware that the primary purpose of preparing the financial statements was for the use of third parties in securing additional finance.124 Further, the Canadian courts exercised caution in limiting liability to a known class of investors by referring to the purposes for which the financial statement was prepared.125 In another case regarding negligent advice, the courts in *327973 British Columbia Ltd v HBT Agra Ltd*126 held that auditors may be liable if they are aware that third parties would be relying on the advice for a particular purpose, which was known to the adviser at the time the statement was made.127

(b) The Test of Proximity
In the case of *Dixon v Deacon Morgan McEwan Easson*,128 the Supreme Court of British Columbia held that a duty of care could not be imposed on the auditors because ‘no relevant degree of proximity between the parties existed’.129 The facts of this case involved a plaintiff who invested in a company after relying on audited financial statements, which severely overstated the company’s profit. As a result, the plaintiff suffered loss due to the decline in value of shares. The Canadian judges considered various issues in determining whether a duty of care existed including the test of reasonable foreseeability, the degree of proximity of relationship and whether it was ‘just and reasonable’ to impose a duty of care upon the defendant auditor.130 Overall, the courts found in favour of the auditors, as the requisite tests for establishing a duty of care were not satisfied.

(c) Current Position in Canada
The courts in *Hercules Management Pty Ltd v Ernst & Young*131 examined whether the auditor’s duty of care extended to shareholders. In this case, the defendant auditors were sued by the plaintiff for the negligent preparation of financial reports. The plaintiff suffered significant losses as a result of relying on financial reports when the corporation went into receivership.132 In determining whether a duty of care existed, the Canadian courts cited the English judgment in

123 See Livanes, above n. 67.
124 Ibid.
126 (1994) 120 DLR (4th) 726.
127 See Rajacic et al., above n. 10 at 215.
128 (1990) 64 DLR (4th) 441.
129 See Livanes, above n. 67.
130 Ibid.
132 See Rajacic et al., above n. 10 at 215.
Caparo Industries plc v Dickman\textsuperscript{133} where it was held that auditors' liability extends to audited reports when they are prepared for use by the corporation and shareholders as a whole.\textsuperscript{134} Further, there was no evidence that the auditors knew that the plaintiff would rely on the financial reports for any specific purpose.\textsuperscript{135} Consequently, the auditors' liability did not extend to the preparation of financial reports for the purpose of private business transactions by individual shareholders and thus the plaintiff was denied damages for the loss of the shareholding value.\textsuperscript{136} On the whole, this case represents the current position regarding auditors' liability in Canada, whereby auditors are protected against third party claims.

\textit{v. New Zealand}

New Zealand has followed similar trends to the United Kingdom and other countries in moving towards a narrower approach in limiting auditors' liability.

(a) Liberal Approach to Auditors' Liability

Initially, it appeared that the New Zealand courts treated third parties more favourably than auditors, as illustrated in the case of Scott Group Ltd v McFarlane.\textsuperscript{137} The facts of this case involved the preparation of financial statements by the defendant auditor, which significantly overstated the amount of assets owned by the company. The plaintiff subsequently suffered loss as a result of relying on the audited information when it undertook a takeover of the company. A court majority of two to one held that the auditors owed a duty of care to the plaintiff, even though they had no knowledge that the company would be subject to a takeover bid.\textsuperscript{138} In addition, the court stated that it was reasonably foreseeable that the plaintiff, as a member of a class, may rely on audited accounts in relation to a company's assets and business.\textsuperscript{139} Overall, this case highlights the dangers involved in adopting such a wide test of foreseeability, which would have resulted in the potential liability 'to all individuals the auditor could reasonably foresee would rely on the accounts'.\textsuperscript{140}

(b) Policy Arguments Raised in Scott Group v McFarlane

The court's rationale in finding for the plaintiff in Scott was explained by the fact that third parties often have limited or no opportunity to

\begin{itemize}
  \item [133] [1990] 1 All ER 568.
  \item [134] See Rajacic et al., above n. 10 at 215.
  \item [135] See Deturbide, above n. 125 at 261.
  \item [136] See Rajacic et al., above n. 10 at 216.
  \item [137] [1978] 1 NZLR 553.
  \item [138] See Hogg, above n. 59 at 80.
  \item [139] See Rajacic et al., above n. 10 at 217.
\end{itemize}
make independent examinations of a company’s financial statements.\textsuperscript{141} Therefore, the only option available to third parties is to rely on financial statements prepared by the auditor. In contrast, some judges were cautious in their decision not to increase liability further, despite finding the defendant auditors liable. Woodhouse J acknowledged that auditors owed a \textit{prima facie} duty of care to third parties; however, it must be proven that the plaintiff reasonably relied on the information and suffered actual loss as a result of such reliance.\textsuperscript{142}

(c) A Narrower Approach to Auditors’ Liability
The recent judgment of \textit{Purdue v Boyd Knight}\textsuperscript{143} has changed the legal position of auditors in New Zealand in relation to negligent misstatement. In this case, the High Court took a ‘narrower approach to auditors’ liability to third parties set out in the House of Lords decision in \textit{Caparo Industries plc v Dickman}.\textsuperscript{144} The facts involved an action brought by investors against the defendant auditors of the company. The auditors did not take reasonable care in preparing the audited financial statements and therefore failed to detect the overstatement of shareholders’ funds (which were the result of fictitious loans created by the directors of the company).\textsuperscript{145} Consequently, the plaintiff relied on the fraudulent statements and suffered economic loss.

(d) Additional Tests of Reliance and Causation
In defining the tests for negligent misstatement, the New Zealand courts in \textit{Purdue v Boyd Knight}\textsuperscript{146} examined several case authorities from various jurisdictions.\textsuperscript{147} In view of those cases, Chisholm J stated that it was necessary to determine whether the auditor assumed responsibility for the information, and whether the plaintiff relied on the information for the purpose for which it was produced.\textsuperscript{148} Accordingly, it must also be proven that the auditor knew the purpose for which the audited statements were prepared. Further, for a duty of care to exist, the plaintiff must have been within ‘an identified class that could be expected to rely on the information’.\textsuperscript{149} Overall, the High Court of New Zealand imposed a duty of care on the auditors as the plaintiff’s reliance on the audit report was the actual cause of the

\textsuperscript{141} See Rajacic \textit{et al.}, above n. 10 at 217.
\textsuperscript{142} Ibid.
\textsuperscript{143} 1998, unreported; HC Christchurch.
\textsuperscript{144} See Watson, above n. 140 at 52.
\textsuperscript{145} Ibid.
\textsuperscript{146} 1998, unreported; HC Christchurch.
\textsuperscript{147} Including \textit{Hercules Management Pty Ltd v Ernst & Young} [1997] 2 SCR 165; \textit{Caparo Industries plc v Dickman} [1990] 1 All ER 568; \textit{Esanda Finance Corporation Ltd v Peat Marwick Hungerfords (reg)} [1997] 142 ALR 750; and \textit{Scott Group Ltd v McFarlane} [1978] 1 NZLR 553.
\textsuperscript{148} See Watson, above n. 140 at 53.
\textsuperscript{149} Ibid.
loss.\textsuperscript{150} Despite the finding against the auditors, the case has effectively limited the liability of auditors due to imposition of the tests such as reliance and causation. Thus, the decision in \textit{Purdue v Boyd Knight} has laid to rest the ‘spectre of indeterminate liability’ which has existed in New Zealand since the findings in \textit{Scott Group}.\textsuperscript{151}

\textbf{VI. Auditors’ Liability under Statute Law in Australia}

\textit{i. Introduction}

Auditors in Australia are subject to a high level of liability to companies and third parties due to the wide scope of statutory obligations. Section VI examines the governmental regulatory bodies governing the auditing profession, which have been established under the Corporations Act 2001 (Cth) and the Trade Practices Act 1974 (Cth) (TPA). More specifically, several provisions under the Corporations Act relating to auditors’ duties in the preparation of financial statements will be examined. Next, the TPA will be discussed in terms of the misleading and deceptive conduct provisions under s. 52, implied warranties under s. 74, and disclaimers under s. 68. These findings will hopefully highlight the need for reform of the law in order to limit auditors’ liability to third parties.

\textit{ii. Corporations Act 2001 (Cth)}

\textbf{(a) Australian Securities and Investments Commission}

The Commonwealth authority responsible for administering the Corporations Act 2001 (Cth) (‘the Act’) is the Australian Securities and Investments Commission (ASIC). The purpose of having corporate regulation is to ensure that the economy operates efficiently to maintain confidence and ensure the adequate protection of investors.\textsuperscript{152} For this reason, any companies planning to issue new securities to the public are required to register with ASIC and conduct regular audits of financial statements under s. 301. The Act imposes a duty upon companies to give continual disclosure of financial statements for public access under s. 314. More specifically, the Act requires financial statements to be produced and accompanied by an auditor’s report, as part of the prospectus and subsequent reports.\textsuperscript{153} The Act also deals with several matters such as including the ‘qualifications, appointments, removal, powers and duties of auditors’.\textsuperscript{154} In circumstances where auditors have engaged in any conduct which breaches

\textsuperscript{150} Brownie Wills v Shrimpton [1998] 2 NZLR 320. As cited in Watson, above n. 140 at 54.

\textsuperscript{151} Ibid. at 56.

\textsuperscript{152} Other objectives of ASIC are contained in s. 1 of the Australian Securities and Investments Commission Act 2001 (Cth). See P. Latimer, \textit{Australian Business Law}, 22nd edn (CCH Australia Ltd: Sydney, 2003), 749.

\textsuperscript{153} See Arens et al., above n. 9 at 29.

\textsuperscript{154} Ibid.
the provisions of the Act, the Commission has the power to initiate proceedings against the auditor and impose penalties.

(b) Duties under the Corporations Act 2001 (Cth)
Provisions relating to audit and auditors' reports are contained under Part 2M.3, Division 3, Chapter 2M of the Act. Auditors are appointed by the company's shareholders in the general meeting under s. 327. Reports must include a statement of opinion about whether the financial report gives a true and fair view of the financial position and performance of the company.\textsuperscript{155} In addition, the auditor must also state whether the report is in compliance with the relevant accounting standards and the Act.\textsuperscript{156}

Another important provision to note is s. 311, which requires auditors to notify ASIC where there are reasonable grounds to suspect that a company has contravened any part of the Act. Further, under s. 1308, it is an 'offence for an auditor to knowingly lodge a statement with ASIC that is known to be false or misleading'. Thus, these are the main provisions which define the scope of liability of auditors in Australia. Thus, these are the main provisions which define the scope of liability of auditors in Australia. (For details of these provisions, see Appendix B to this paper.)

(c) Auditors' Liability in Relation to Securities
The Corporations Act provides certain sections relating to the issue of securities. Section 728 relates to any false or misleading statements contained in a company's prospectus. It appears that auditors could be rendered liable for contravention of these sections \textit{prima facie}. However, it is argued by some commentators that these provisions are not applicable to auditors because their work does not relate directly to the issuing of securities (which is defined as a 'financial product').\textsuperscript{157}

(d) Disclaiming Liability
In terms of disclaimers, s. 199A(1) is applicable to auditors and provides that 'a company must not exempt a person from a liability to the company incurred as an officer or auditor of the company'. Thus, these provisions make it difficult for auditors to avoid contractual liability under the Act.

(e) Disciplinary Proceedings for Contravention of the Corporations Act
In terms of actions brought against auditors for contravention of the Act, the Companies Auditors and Liquidators Disciplinary Board

\textsuperscript{155} Corporations Act 2001 (Cth), s. 307.
\textsuperscript{156} \textit{Ibid.}, s. 296.
\textsuperscript{157} See Rajacic \textit{et al.}, above n. 10 at 231.
(CALDB) is the Commonwealth statutory body responsible for hearing applications regarding breaches under the Act by auditors and liquidators.\textsuperscript{158} If there is evidence of a breach by an auditor, the CALDB has power to impose penalties including the cancellation or suspension of registration,\textsuperscript{159} and the imposition of restrictions on conduct or an admonition.\textsuperscript{160} Note that the decisions of the CALDB may be appealed to the Administrative Appeals Tribunal. The CALDB also allows the accounting profession to play a role in its own self-regulation; however, this role remains unclear.\textsuperscript{161}

\textbf{(f) Actions under the CALDB}

In recent years, actions have been brought against auditors following an application by ASIC to the CALDB. An example of one case in November 2001 involved a company (NSX Limited) and its auditor (Philip Charles Anderson), in which the CALDB held that the auditor breached s. 308 of the Act by failing to qualify audit reports (which did not provide a true and fair view of the company).\textsuperscript{162} Consequently, the CALDB suspended the auditor from practice and imposed various penalties including costs orders, and agreements to attend professional education courses in audit practice and procedure (in addition to the requirements of the Institute of Chartered Accountants in Australia).\textsuperscript{163} An action in May 2002 resulted in the CALDB bringing disciplinary action against nine auditors and a liquidator involved in contravention of the Act.\textsuperscript{164} Following ASIC’s applications, the CALDB imposed various penalties including the cancellation and suspension of registration.

\textbf{(g) Liability under the Corporations Act to Third Parties}

There is a requirement imposed on companies under s. 314 of the Act, to lodge financial statements with ASIC for the purpose of providing public access to such information. However, concerns arise as to whether this requirement exposes auditors to liability to unidentified members of the public. Currently, the position under the Act supports

\begin{itemize}
\item\textsuperscript{158} The CALDB was established under the Australian Securities and Investments Commission Act 2001 (Cth) and operates in conjunction with ASIC. See Gill \textit{et al.}, above n. 3 at 27.
\item\textsuperscript{159} The CALDB may cancel or suspend the registration of an auditor if they are ‘not a fit and proper person to remain registered as an auditor’: Corporations Act 2001 (Cth), s. 1292(1).
\item\textsuperscript{160} \textit{Ibid.}
\item\textsuperscript{161} See Latimer, above n. 15 at 649.
\item\textsuperscript{162} Sourced on 14 November 2001 from: ‘01/400 CALDB disciplines former auditor of NSX Limited’; see http://www.asic.gov.au/asic/ASIC_PUB.NSF/byid/E7DEF42F7524D05ACAA256B1000294E03?openDocument.
\item\textsuperscript{163} \textit{Ibid.}
\item\textsuperscript{164} Sourced on 9 May 2002 from: ‘02/161 ASIC successful in disciplinary actions against nine auditors and a liquidator’; see http://www.asic.gov.au/asic/ASIC_PUB.NSF/byheadline/02%2F161+ASIC+successful+in+disciplinary+actions+against+nine+auditors+and+a+liquidator?openDocument.
\end{itemize}
the principle in *Hedley Byrne & Co v Heller.* The reason is that because financial reports are required to be audited under the Act, and are listed on ASIC’s public register, a duty of care is owed to the public. The rationale is that audited financial statements would have no benefit if they were unable to be relied upon by third parties such as investors or creditors. Thus, this provision has the potential to increase auditors’ liability to third parties indefinitely and should therefore be curbed.

**iii. Trade Practices Act 1974 (Cth)**

(a) Australian Competition and Consumer Commission
The Australian Competition and Consumer Commission (ACCC) is the Federal Government body in Australia which has authority to administer the Trade Practices Act 1974 (Cth) (TPA). The ACCC also has power to initiate legal proceedings on behalf of aggrieved consumers, and enforce orders against parties who breach provisions of the TPA. It will be argued that auditors now fall within the scope of the TPA, which will affect the ACCC in terms of the legal actions brought against auditors by third parties.

(b) Scope of the Trade Practices Act 1974 (Cth)
In terms of scope, the TPA specifically applies to ‘corporations’ (as opposed to ‘natural persons’) due to strict constitutional limitations. For this reason, it appears that the auditing profession does not fall within the operation of the TPA, because auditing firms are prohibited from incorporation. However, it is argued that the TPA does apply to services provided by auditors, as s. 6 of the TPA specifically refers to ‘the conduct of individuals in trade or commerce’. The TPA also applies to natural persons where the conduct engaged in involves the use of postal or telephonic services. Therefore, the TPA is applicable where an auditor supplies reports to the company and its shareholders. In addition, certain provisions of the State and Territory Fair Trading Acts (FTA) extend the scope of the TPA to all legal ‘persons’ engaging in professional services. Other requirements necessary for the TPA to apply include s. 4B, whereby services are provided to a ‘consumer’ to the value of $40,000 or less. Further, auditing services clearly fall within the definition of ‘services’ provided to a consumer.

166 Ibid.
167 See Latimer, above n. 152 at 7.
168 Corporations Act 2001 (Cth), s. 1279(1).
169 See Rajacic et al., above n. 10 at 210.
170 See Anderson, above n. 5 at 351.
171 Consumer Affairs and Fair Trading Act 1990 (NT), s. 42; Fair Trading Act 1992 (ACT), s. 12; Fair Trading Act 1987 (NSW), s. 42; Fair Trading Act 1989 (Qld), s. 38; Fair Trading Act 1987 (SA), s. 56; Fair Trading Act 1990 (Tas), s. 14; Fair Trading Act 1985 (Vic), ss. 11, 12; Fair Trading Act 1987 (WA), s. 10.
and constitute 'work of a professional nature'. Therefore, the TPA applies to the auditing profession and has the effect of widening the scope of auditors' liability to third parties in Australia.

(c) Section 52

Requirements
Section 52 of the TPA provides a statutory duty allowing third parties to bring civil actions for damages against auditors for misleading and deceptive conduct. There are various requirements for succeeding in a claim for misleading and deceptive conduct under s. 52 of the TPA. Firstly, it must be proven that an auditor engaged in conduct that was 'misleading or deceptive, or likely to be misleading or deceptive'. Next, the test of causation must be satisfied under s. 82(1), in which the plaintiff must prove that loss or damage was in part or wholly a result of the auditor's breach. The section therefore applies to audited financial reports which are 'incorrect or inappropriately worded so as to mislead or deceive' users. In terms of the number of actions brought under s. 52 of the TPA against auditors, cases have been limited; however, as third parties become more aware of the provisions, there will be significant legal ramifications for the auditing profession.

Relevance of Common Law Tests
The benefit of initiating a claim under s. 52 of the TPA is that the plaintiff does not have to establish a duty of care and proximity of relationship, as required under the common law. This view was supported in Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd in which the court stated that 'misleading or deceptive conduct does not require proof of a breach of a duty of care, as negligence does'. Consequently, there is a smaller burden of evidence placed on third parties in establishing a breach of statutory duty. Therefore, the difficulties encountered by a third party in establishing duty of care

172 See Rajacic et al., above n. 10 at 232.
173 See Appendix C to this paper.
174 See Arens et al., above n. 9 at 130.
175 Ibid. at 132.
176 See Rajacic et al., above n. 10 at 210.
177 Note that accountants have been found liable under s. 52 in Mackman v Stengold Pty Ltd (1991) 13 ATPR ¶41–105, for reproducing financial reports without verifying the accuracy of figures; and Sweetman v Bradfield Management Services Pty Ltd (1994) 16 ATPR ¶41–290, for giving misleading advice to clients on tax minimization schemes. As cited in Anderson, above n. 5 at 351.
180 See Arens et al., above n. 9 at 132.
have effectively been removed by the TPA, which subsequently increases the scope of auditors’ liability.\textsuperscript{181}

(d) Section 51A and Misleading Representations
Auditors may also be liable for future representations under s. 51A(1) of the TPA if they are misleading in nature. Some examples of future representations made by auditors may include the preparation of ‘profit forecasts, cash flows forecasts, budget, net present valuations, and advice concerning intended acquisitions or disposals’.\textsuperscript{182} Further, the burden of proof lies on the defendant to prove that there were reasonable grounds for making the representation.\textsuperscript{183} This section has been interpreted strictly by the courts and therefore auditors must accompany any representations with appropriate evidence and qualifications to support their statements.\textsuperscript{184} At present, there has not yet been a definitive case brought under s. 51A against an auditor for misleading future representations; however, the potential for liability still remains at large.

(e) Implied Warranties under Section 74
In determining the scope of auditors’ liability, another important section to note is s. 74 of the TPA and it relates to consumer transactions for the supply of services.\textsuperscript{185} This provision effectively implies a warranty into all contracts between an auditor and the company engaging in its services. Therefore, a statutory duty is imposed upon the auditor to perform services with ‘due care and skill’ under s. 74(1) of the TPA. In addition, a further warranty is implied in relation to the provision of auditing services under s. 74(2), which states that any materials supplied in connection with the services must be ‘fit for the purpose for which they are carried out’. As a consequence, any audited financial statements must be reasonably fit for the purpose for which they are prepared. Thus, auditors will only be able to escape liability under this provision if it is proven that a consumer unreasonably relied on the auditor’s skill or judgment.\textsuperscript{186}

(f) Legality of Disclaimers under Section 68
In the course of providing assurance services, auditors have the right to use disclaimers at the end of the audited financial report in order to limit their exposure to liability. However, disclaimers must not be worded in a manner which contravenes sections of the TPA. The

\textsuperscript{181} Ibid.
\textsuperscript{182} See Rajacic et al., above n. 10 at 230.
\textsuperscript{183} Trade Practices Act 1974 (Cth), s. 51A(2).
\textsuperscript{184} See Wheeler Grace & Piericci v Wright (1989) ATPR ¶40-990, per Lee J. As cited in Rajacic et al., above n. 10 at 230.
\textsuperscript{185} Under the Trade Practices Act 1974 (Cth), s. 4, the term ‘services’ includes ‘work of a professional nature’, which effectively applies to the type of work performed by auditors.
\textsuperscript{186} See Rajacic et al., above n. 10 at 232.
relevant section is s. 68, which provides that 'any term of a contract . . . that purports to exclude, restrict or modify' the operation of s. 74 and its implied warranties is void. A breach of this provision will amount to a breach of contract, for which damages are assessable under the law of contract.187 Auditors still retain the ability to delineate their scope of duties by providing 'appropriate, clear and prominent warnings, qualifications and the like'.188 However, auditors cannot wholly exclude their liability from performing services with due care and skill under s. 74, or for future representations and misleading conduct under s. 51A and s. 52 of the TPA.189 Thus, many audited reports are provided with disclaimers attached; however, clauses will not be effective unless they are in compliance with the statutory requirements under the TPA.

(g) Availability of Contributory Negligence
Currently, no provision exists under the TPA which indicates that contributory negligence is available as a defence. The relevant authority is Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd,190 which states that 'the defence of contributory negligence is not available to a respondent in an action for misleading or deceptive conduct' under the TPA.191 The result is that although a plaintiff may have failed to take reasonable care for their own interests, the defendant cannot argue contributory negligence to negate their liability.192 However, it is important to note the effect of s. 75B which provides that a person who 'has been in any way, directly or indirectly, knowingly concerned in, or a party to, the contravention' of s. 52 will be liable under the TPA.193 Therefore, auditors as well as companies who engage in misleading and deceptive conduct may be in contravention of the TPA.

(h) Enforcement and Remedies
A third party plaintiff may seek damages under the enforcement and remedy provisions of Part VI of the TPA. Section 80 provides for injunctive relief, whereas s. 82 allows persons who have suffered loss or damage 'to recover such loss from persons breaching provisions of Part IV or V, including s. 52'.194 Other orders are provided for under s. 87 including an order requiring refund of monies, variation of the contract or the rendering void of a contract. These remedy provisions

187 Ibid.
188 Ibid. at 235.
189 Ibid.
191 See Anderson, above n. 5 at 353.
193 Trade Practices Act 1974 (Cth), s. 75B(c).
194 See Rajacic et al., above n. 10 at 233.
require the plaintiff to establish that breach of a particular provision in the TPA was the actual cause of the plaintiff’s loss. Further, the plaintiff must also prove that the auditor’s opinion on the financial statements was not reasonably held.\textsuperscript{195} Note that the damages awarded for the contravention of s. 52 are less than the amount of damages under the common law.\textsuperscript{196} Even so, these remedy provisions are still attractive to plaintiffs in establishing liability and thus contribute to a wider scope of auditors’ liability in comparison to the common law.\textsuperscript{197}

(i) Recent Cases against Auditors
The case of \textit{Mackman v Stengold Pty Ltd \& Ors}\textsuperscript{198} illustrates the fact that the TPA does apply to the auditing profession. This case involved an application under s. 52 of the TPA, whereby the plaintiffs alleged that the defendant accountants made certain representations about the nature and profitability of a business, which were misleading or deceptive. The facts indicated that figures regarding the profitability of the business were supplied to the accountants and published in an advertisement under the accountants’ name. There was also evidence of a disclaimer which attempted to exclude the accountants from liability for loss suffered by persons relying on their representations. On the whole, the Federal Court held that the defendants were liable for misleading or deceptive conduct in regard to s. 52, and found the disclaimer to be ineffective in excluding liability. The accountants were also held liable for negligence ‘by allowing figures that they had not checked to be presented to the public as their own’.\textsuperscript{199} Further, both the director of the relevant company and the accountants were ‘knowingly concerned in the conduct within the meaning of section 75B of the Act and were liable in damages’.\textsuperscript{200}

There have not yet been any other definitive cases regarding actions against auditors under s. 52 of the TPA; however, there have been some actions under the state and territory fair trading legislation. On the whole, with the improved knowledge and awareness of the applicability of the TPA, it is expected that there will be an increase in litigation claims against the auditing profession in the near future. As a result, action should be taken by the government to reform the law regarding auditors’ liability in anticipation of a further surge in litigation.

\textsuperscript{195} See Anderson, above n. 5 at 359.
\textsuperscript{196} See Rajacic et al., above n. 10 at 232.
\textsuperscript{197} \textit{Ibid.} at 233.
\textsuperscript{198} (1991) \textit{13} ATPR \$41-105.
\textsuperscript{199} \textit{Ibid.}
\textsuperscript{200} \textit{Ibid.}
VII. Proposed Reform of Auditors’ Liability

i. Introduction

Due to the ‘litigation’ crisis faced by the auditing profession in Australia, several schemes have been proposed in order to limit the liability of auditors. In comparing auditors’ liability in Australia with other countries, it is evident that the current system as it applies to auditors is too severe. The system of joint and several liability under tort law inequitably imposes substantial costs on auditors by allowing plaintiffs to recover damages entirely from ‘any of the tortfeasors who caused the loss independent of their relative culpability’. Therefore, it is argued that the system of joint and several liability should be abolished and replaced by statutory capping and proportionate liability schemes, to ensure a fairer allocation of liability amongst parties responsible for the loss.

ii. Statutory Capping

Legislation which provides for the statutory capping of liability has been introduced in New South Wales under the Professional Standards Act 1994 (NSW). In 1997, similar legislation was introduced in Western Australia. The provisions of these Acts are not mandatory and generally apply to trades and associations. The professional accounting bodies determine whether or not the legislation should apply to their members. Currently, the statutory capping figure imposed by the ICAA and CPA in New South Wales is $20 million. However, it is argued that statutory capping may be ineffective in limiting liability due to the potential for ‘forum shopping’, in which aggrieved parties pursue litigation claims in those jurisdictions where auditors’ liability remains unlimited. As a result, it is proposed that the Federal Government introduce a national system of statutory capping into Australia to overcome these problems.

(a) Policy Arguments against Statutory Capping

Despite benefits to the auditing profession in implementing a system of statutory capping, it is important to consider the associated policy implications. First, innocent third parties may be disadvantaged by not being able to claim the full amount of their damages. Secondly, as the capped amount will be calculated as the multiple of the audit fee, this may act as an incentive for auditors to charge lower audit fees (and premium amounts for other work) in anticipation of their liability

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201 See Free, above n. 1 at 130.
202 Ibid.
204 See Gill et al., above n. 3 at 121.
205 See Latimer, above n. 15 at 234.
206 See Gill et al., above n. 3 at 121.
207 Countries which currently impose fixed statutory caps include Germany, Austria, Greece and Portugal. See Free, above n. 1 at 131.
to third parties. Finally, the imposition of a cap would represent an unwarranted intrusion by the state, and could encourage other professions to seek similar concessions. In this regard, caution must be exercised in reforming the law to balance the interests of the auditing profession as well as third parties.

iii. Proportionate Liability

The system of joint and several liability is unjust as it ‘imposes a liability on a defendant out of all proportion to that defendant’s actual responsibility for the damage suffered’. Therefore, several states in Australia have amended the law of contribution to introduce proportionate liability in relation to claims for economic loss under contract, tort and statute. The courts will determine the liability of each defendant in consideration of what is just and equitable, having regard to the extent of the defendant’s responsibility for the harm. Overall, the new system will provide ‘a regime of full proportionate liability between all the parties responsible for the loss’ which will hopefully deal with the litigation and insurance crisis suffered by the auditing profession.

At present, not all states have implemented schemes of proportionate liability, therefore it is proposed that the Federal Government introduce uniform legislation in response to pressure from the auditing profession. However, there are problems associated with implementing proportionate liability as the full recovery of economic loss from wrongdoers by third parties will become increasingly rare. Thus, based on similar arguments regarding statutory capping, the system of proportionate liability should be reformed to ensure that third parties are not disadvantaged.

iv. Other Schemes Limiting Liability

There are other methods of limiting auditors’ liability which may be implemented to protect auditors from incurring high litigation and insurance costs. Currently, auditors are not permitted to incorporate and may only operate as sole traders or in partnerships. It is suggested that laws be enacted in Australia to allow the incorporation of

209 See Gill et al., above n. 3 at 120.
210 See Free, above n. 1 at 130.
211 Civil Liability Amendment (Personal Responsibility) Act 2002 (NSW); Civil Liability Act 2003 (Qld); Civil Liability Amendment Bill 2003; and Wrongs and Limitation of Actions (Insurance Reform) Act 2003 (Vic). Note Queensland does not apply a system of proportionate liability under the Fair Trading Act 1989 (Qld). See Duffy, above n. 35.
212 Ibid. at 11.
213 See Rajacic et al., above n. 10 at 209.
214 See Duffy, above n. 35 at 9.
215 Ibid. at 11.
216 Ibid. at 8.
217 Corporations Act 2001 (Cth), s. 1279(1).
auditors in order to protect the assets of non-negligent partners.\(^{218}\) Once again, the interests of third parties must be considered, as auditors’ liability will be limited to the amount of assets owned by the company which may be insufficient in compensating losses. Further, incorporation could have the effect of undermining the overall creditability of the audited financial statements.\(^{219}\) Other options available to auditors in limiting the extent of liability include the use of contractual clauses, provided they comply with statutory requirements.\(^{220}\) Also, the law could impose penalties on plaintiffs to discourage them from filing frivolous lawsuits.\(^{221}\) Thus, several options for reform are available to auditors in limiting their liability to third parties.

VIII. Conclusion

The auditing professions in both Australia and around the world have been exposed to many litigation claims in recent years. These incidences of liability have been the result of global collapses of corporate entities, which have been linked to accusations of professional negligence and breach of statutory obligations by auditors. Consequently, auditors have often become targets of litigation by third parties seeking compensation for losses suffered in reliance on audited financial statements. Thus, the liability of auditors is a serious issue which is clearly on the agenda of professional bodies, and the subject of law reform inquiries of both judicial and legislative bodies internationally.\(^{222}\)

\textit{i. Limited Liability under the Common Law}

This paper has argued that auditing laws in Australia place the greatest scope of liability on auditors in comparison with other countries such as the United Kingdom, United States, Canada and New Zealand. These findings serve as an indication that Australian auditors are faced with liability resulting from the operation of a vast regime of statutory obligations, in addition to contractual and common law duties. In terms of the common law, the High Court in \textit{Esanda Finance Corporation Ltd v Peat Marwick Hungerfords (reg)}\(^{223}\) effectively narrowed down the liability of auditors to third parties, endorsing the decisions of the English courts in \textit{Caparo Industries plc v Dickman},\(^{224}\) and supporting the policy arguments for limiting liability in the United

\(^{218}\) See Latimer, above n. 15 at 233. Countries in which auditing firms have incorporated include the United Kingdom, France, Germany, Switzerland and Japan. See Gill \textit{et al.}, above n. 3 at 120.

\(^{219}\) See Free, above n. 1 at 132.

\(^{220}\) See Latimer, above n. 15 at 233.

\(^{221}\) See Gill \textit{et al.}, above n. 3 at 121.

\(^{222}\) See Free, above n. 1 at 135.

\(^{223}\) (1997) 142 ALR 750.

\(^{224}\) (1990) 1 All ER 568.
States judgment *Ultramarines v Touche*. The current position is that auditors will not be liable to third parties unless the tests of reasonable foreseeability, proximity and causation have been satisfied. This inherently limits the scope of liability of auditors under the Australian common law system.

**ii. Widening of Liability under Legislation**

It is argued that auditors in Australia still remain subject to a higher level of liability than other countries due to the operation of the Corporations Act 2001 (Cth) and Trade Practices Act 1974 (Cth) (TPA). More specifically, liability has increased significantly due to the applicability of ss. 52, 74 and 68 of the TPA and relevant state and territory fair trading legislation, in regard to misleading and deceptive conduct. For these reasons, it is proposed that uniform legislation be enacted to implement schemes which limit liability. Such proposals include the introduction of systems of proportionate liability and statutory capping in order to limit the quantum of damages. This will ensure that auditing laws in Australia become more aligned with international trends in protecting auditors from further exposure to liability.

**iii. Significance of Findings**

This research will provide a greater knowledge and awareness about auditors' liability in Australia for the benefit of various parties. Research findings may be incorporated into professional body publications to increase the awareness of the auditors' role and responsibility to clients, and detail ways in which auditors can limit liability. In addition, it is suggested that the auditing profession continue to promote active lobbying for the reform of audit laws. Findings will also be useful to government regulatory bodies, which may be responsible for initiating legal proceedings against auditors, and have a duty to step in to mitigate the effects of corporate collapses. Insurance companies will also be better informed as to why auditors are often targeted by third parties, and in turn lobby for greater protection from costly damages payouts. Finally, companies and third parties will be more informed about their legal rights in seeking compensation against auditors, particularly since it is now easier to establish breach under statute laws.

**iv. The Potential for Reform of Auditors' Liability**

In conclusion, there is a strong need to reform the law to limit the scope of auditors' liability in relation to third parties in Australia. It is hoped that such reforms will protect the interests of the auditing profession in deterring third parties from initiating opportunistic litigation. On the other hand, reforms should also be balanced to protect

225 174 NE 441 (1931).

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the needs of innocent third parties in seeking compensation for loss suffered as the result of negligence. Ultimately, any future developments of audit legislation in Australia should be made with caution, and considered in light of international authorities to ensure that the floodgates for the indeterminate liability of auditors are not opened to unprecedented proportions.

Appendix A: Statement of Auditing Standards


Introduction
.01 The purpose of this Auditing Standard (AUS) is to establish standards and provide guidance on the objective and general principles governing an audit of a financial report.

Objective of an Audit
.02 The objective of an audit of a financial report is to enable the auditor to express an opinion whether the financial report is prepared, in all material respects, in accordance with an identified financial reporting framework.
.03 Although the auditor's opinion enhances the credibility of the financial report, the user cannot assume that the opinion is an assurance as to the future viability of the entity nor the efficiency or effectiveness with which management has conducted the affairs of the entity.

General Principles of Audit
.04 The auditor should comply with the ethical requirements of CPA Australia and the Institute of Chartered Accountants in Australia. Ethical principles governing the auditor's professional responsibilities include:
(a) independence;
(b) integrity;
(c) objectivity;
(d) professional competence and due care;
(e) confidentiality;
(f) professional behaviour; and
(g) technical standards.
.05 The auditor should conduct an audit in accordance with Australian Auditing Standards. These contain basic principles and essential procedures, together with related guidance, to be applied in the audit of a financial report.
.06 The auditor should adopt an attitude of professional scepticism throughout the audit recognising that circumstances may exist which could cause the financial report to be materially misstated.

226 Extracts have been sourced from S. Kemp and J. Knapp (eds.), Auditing and Assurance Handbook 2004 (Prentice Hall: Sydney, 2004).
Scope of an Audit
.07 The term 'scope of an audit' refers to the audit procedures deemed necessary in the circumstances to achieve the objective of the audit. The procedures required to conduct an audit in accordance with AUSs should be determined by the auditor having regard to the requirements of AUSs, legislation, regulations and, when appropriate, the terms of the audit engagement and reporting requirements.

Reasonable Assurance
.08 An audit in accordance with AUSs provides reasonable assurance as to whether the financial report taken as a whole is free from material misstatement. Reasonable assurance is a concept relating to the accumulation of audit evidence necessary for the auditor to conclude whether there are any material misstatements in the financial report taken as a whole. Reasonable assurance relates to the whole audit process.

Appendix B: Corporations Act 2001 (Cth)227

Section 308 Auditor's report on annual financial report
(1) An auditor who audits the financial report for a financial year must report to members on whether the auditor is of the opinion that the financial report is in accordance with this Act, including:
   (a) section 296 (compliance with accounting standards); and
   (b) section 297 (true and fair view).
If not of that opinion, the auditor's report must say why.
(1A) An offence based on subsection (1) is an offence of strict liability. [Note: For strict liability, see section 6.1 of the Criminal Code.]
(2) If the auditor is of the opinion that the financial report does not comply with an accounting standard, the auditor's report must, to the extent it is practicable to do so, quantify the effect that non-compliance has on the financial report. If it is not practicable to quantify the effect fully, the report must say why.
(3) The auditor's report must describe:
   (a) any defect or irregularity in the financial report; and
   (b) any deficiency, failure or shortcoming in respect of the matters referred to in paragraph 307(b), (c) or (d).
(4) The report must specify the date on which it is made.

Section 311 Reporting to ASIC
(1) The auditor conducting an audit or review must, as soon as possible, notify ASIC in writing if the auditor:
   (a) has reasonable grounds to suspect that a contravention of this Act has occurred; and

227 Sections have been sourced from the Scaleplus Legal Resources Internet site, provided by the Attorney-General's Department, at: http://www.scaleplus.law.gov.au/html/pasteact/3/3448/top.htm.
(b) believes that the contravention has not been or will not be adequately dealt with by commenting on it in the auditor’s report or bringing it to the attention of the directors.

[Note: Section 1289 gives an auditor qualified privilege for a notification to ASIC under this section.]

(2) For an offence based on subsection (1), strict liability applies to the conduct, notifying ASIC in writing.

[Note: For strict liability, see section 6.1 of the Criminal Code.]

Appendix C: Trade Practices Act 1974 (Cth)\(^{228}\)

Section 52 Misleading or deceptive conduct
(1) A corporation shall not, in trade or commerce, engage in conduct that is misleading or deceptive or is likely to mislead or deceive.

(2) Nothing in the succeeding provisions of this Division shall be taken as limiting by implication the generality of subsection (1).

Section 74 Warranties in relation to the supply of services
(1) In every contract for the supply by a corporation in the course of a business of services to a consumer there is an implied warranty that the services will be rendered with due care and skill and that any materials supplied in connexion with those services will be reasonably fit for the purpose for which they are supplied.

(2) Where a corporation supplies services (other than services of a professional nature provided by a qualified architect or engineer) to a consumer in the course of a business and the consumer, expressly or by implication, makes known to the corporation any particular purpose for which the services are required or the result that he or she desires the services to achieve, there is an implied warranty that the services supplied under the contract for the supply of the services and any materials supplied in connexion with those services will be reasonably fit for that purpose or are of such a nature and quality that they might reasonably be expected to achieve that result, except where the circumstances show that the consumer does not rely, or that it is unreasonable for him or her to rely, on the corporation’s skill or judgment.

(3) A reference in this section to services does not include a reference to services that are, or are to be, provided, granted or conferred under:
   (a) a contract for or in relation to the transportation or storage of goods for the purposes of a business, trade, profession or occupation carried on or engaged in by the person for whom the goods are transported or stored; or
   (b) a contract of insurance.

\(^{228}\) Sections have been sourced from the Scaleplus Legal Resources Internet site, provided by the Attorney-General’s Department, at: http://www.scaleplus.law.gov.au/html/pasteact/0/115/top.htm.
Section 68 Application of provisions not to be excluded or modified

(1) Any term of a contract (including a term that is not set out in the contract but is incorporated in the contract by another term of the contract) that purports to exclude, restrict or modify or has the effect of excluding, restricting or modifying:
(a) the application of all or any of the provisions of this Division;
(b) the exercise of a right conferred by such a provision;
(c) any liability of the corporation for breach of a condition or warranty implied by such a provision; or
(d) the application of section 75A;

is void.

(2) A term of a contract shall not be taken to exclude, restrict or modify the application of a provision of this Division or the application of section 75A unless the term does so expressly or is inconsistent with that provision or section.