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2007

AUDITORS' DISCLAIMERS

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Are limitation clauses in fund auditors' contracts which limit liability to, for example, a multiple of annual fees necessary and / or desirable?

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Is an auditor's disclaimer lawful?

- “our law does not recognise the right of a court to release a contracting party from the consequences of an agreement duly entered into by him merely because that agreement appears to be unreasonable”

Innes, J in *Burger v Central South African Railways* 1903 TS 571

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Common Law Limitations

- Interpret narrowly [Christie, *The Law of Contract in South Africa*]
- Cannot disclaim against fraud [Wells v SA Aluminite Co 1927 AD 69]
- Cannot disclaim against intentional wrongdoing
- Disclaimer cannot contravene fundamental principle of justice or prejudice the interests of the public [Morrison v Angelo Deep Gold Mines Ltd 190 TS 775]
- Can disclaim gross negligence (even by implication) [Govt of RSA v Fibre Spinners and Weavers (Pty) Ltd 1978(2) SA 794(A)]

Conney v Old Mutual Life Assurance Co **(SA) [2003] BPLR 3544 (PFA)**

- ❑ Regarding disclaimer on benefit statement....
 - ❑ “...couched in wide terms amounts to abdication of responsibility [and] could amount to maladministration of the fund”
 - ❑ “the purpose of [S7D(c) PFA] is to afford protection to members compelled by circumstances to make important life choices”
 - ❑ “*contra bonos mores* and of no force or effect”
 - ❑ “reliance on it to unilaterally exclude liability for negligent misstatement causing prejudice goes beyond the prevailing *boni mores*”
- ❑ Delictual matter between administrator and member: no contract

Auditing Profession Act, 26 of 2005 (“APA”)

- ❑ S46(1)(a) ... limited to an audit performed within the meaning of paragraph (a) of the definition of “audit”
- ❑ (2) “In respect of any opinion expressed or report or statement made”, no liability to client or third party [i.e., incl. members] unless malicious, fraudulent or negligent
- ❑ Not much more protection than common law

Section 1, APA

- “Audit” means the examination of, in accordance with prescribed or applicable reporting standards –
 - a) Financial Statements with the objective of expressing an opinion as to their fairness or compliance with an identified financial reporting framework and any applicable statutory requirements; or
 - b) Financial and other information, prepared in accordance with suitable criteria, with the objective of expressing an opinion on the financial and other information

Example 1

Limitation of Liability

Other than where specific legislation provides for a different level of liability for our services, for instance in the provision of a statutory audit, our liability shall be limited as follows:

The maximum liability of its partners, employees, and agents in respect of any and all claims which may arise in respect of the services shall be limited to twice the fees charged for these services. This maximum liability shall be an aggregate liability for all claims howsoever arising, whether by contract, delict, negligence or otherwise.

Where services are rendered otherwise than in terms of a written agreement, this clause shall apply separately to services relating to each invoice issued.

Partners, employees and agents will not be liable to the fund or any third party for any consequential, punitive or any other loss or damages beyond the maximum liability specified.

Example 2

Exclusions and limitations on our liability

The maximum liability of the auditor or any individual director, or employee, as the case may be, of the auditor or of any body or entity controlled by us or owned by us or associated with us in respect of direct economic loss or damage suffered by you or by other beneficiaries arising out of or in connection with the services, shall be limited to two times the fees charged and paid for these services. The maximum liability shall be an aggregate liability for all claims arising, whether by contract, delict, negligence or otherwise. This limitation of liability will apply to all causes of action other than those in terms of the Act for failure to report in accordance with section 45 of the Act as per paragraph 5.

In the particular circumstances of the service set out in the engagement letter, the liability to you and to other beneficiaries of the auditor in contract or delict or under statute or otherwise, [or any indirect or consequential] economic loss or damage (including loss of profits) suffered by you (or by any such other party), arising from or in connection with the services, however the indirect or consequential economic loss or damage is caused, excluding our willful misconduct, shall be excluded to the extent that such limitation or exclusion is permitted by law.

Our liability to you shall in no circumstances exceed the lower of the amount determined by the application of the monetary limit based upon fees charged to, and recovered from, you and the amount determined by the appointment of responsibility as the case may be.

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Why lawyers talk so much Lillicrap

- ❑ Delictual liability only flows from a contractual breach where a independent duty of care existed outside of the contractual relationship

[Lillicrap, Wassenaar & Partners v Pilkington Bros (SA) (Pty) Ltd 1985(1) SA 475(A)

- ❑ Statutory duty in S46(2) APA only relates to “audit”

- ❑ Unlikely there exists an independent general common law duty i.r.o non-audit functions

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What do Auditors do?

- In relation to pension Funds
 - Audit: S15 PFA (General duty) ✓
 - Audit: Reg12, Schedule D = “Auditors report” ✓
 - Reg 12, Schedule F: “statement of funds and net assets” **X**
 - Reg 12, Schedule I: factual analysis **X?**
 - Control environment testing (necessary to support sample)?
 - Forensic **X**
 - Litigation support **X**
 - Opinion / Advice / Consulting **X**

Financial Institutions (Protection of Funds) Act 28 of 2001 (“FIPFA”)

- Auditor is not a director, member, partner, officer or employee
- To extent auditor maybe an agent, he/she does not invest, hold, keep, control, administer or alienate assets
- N/A

Trustees' Duties

- ❑ S7C protect interests of members
exercise due care, diligence and
good faith
- ❑ S7D proper control systems
- ❑ S9 fund must appoint auditor

What to do?

- Disclaimer is one factor: shop around
- In a totally disclaimed market:
 - Best service provider
 - Two stop shops?
- In a partially disclaimed market: is disclaimer or general reputability the clincher?

In Summary

- Necessary? **No**
- Desirable? **No** (unless you're an auditor)
- Here to stay? **Yes**
- Lesson?
 - Interrogate exact extent
 - Understand what "services" are
 - Assess impact on insurance cover
 - Take expert advice
 - Lobby?

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NOW THAT THAT'S ALL CLEAR....

THANK YOU

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