



II-6.26: According to the AMF, auditors are not liable when a company fails in its duty of providing the market with information, as long as they obeyed professional standards.

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Translated
Article



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MAIN INFORMATION

Corporate officers that had provided financial markets with false information, as well as their auditors, were under investigation by the Autorité des Marchés Financiers (AMF—French financial markets authority) for failure to provide information. On March 31, 2011, the AMF's Enforcement Commission punished the corporate officers, but decided to innocent the auditors, on the grounds that they had obeyed professional standards.

CONTEXT AND SUMMARY

A listed corporation that built and sold ships issued a financial statement that touted its turnover and its outstanding orders. But, when it published its earnings from the year's orders, it did not specify what part was income already earned that year. It did this every year for a number of years, the statutory auditors unreservedly certified the company's consolidated accounts, and the financial regulator did not formulate any observation.

Then, the regulator opened enforcement proceedings to investigate whether there had been provision of false information to the financial markets. The regulator believed that this way of describing the company's situation, without defining for the public what the "outstanding orders" were, created confusion with income already earned that year.

The Enforcement Commission's March 31, 2011 decision concluded that there was an infraction to the rules concerning public information, and that the fact that this practice was old and that the regulator had not reacted up to present, were without bearing on the company's obligation to publish exact, precise, and sincere information.

The auditors' behavior was also examined by the Enforcement Commission. The statutory auditors were accused of not have done enough to detect the insufficiency of this information, and should have questioned the managers and verified their affirmations. But, the Enforcement Commission concluded that all applicable professional rules and standards were followed, and therefore decided that the auditors' were innocent in this affair.

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BRIEF COMMENTARY

The remarkable point of this decision of the French Financial Market Authority's Enforcement Commission is that it goes against the intellectual tide that we observe everywhere else.

Indeed, both in Europe (cf. Green Paper on Audit Policy: Lessons from the Crisis), and in the United States (J.R. Doty, PCAOB, Rethinking the Relevance, Credibility, and Transparency of Audit, June 2, 2011), the “procedural conception” of the audit is being refuted. In this conception, auditors simply have to follow the rules. Now, a “substantial conception” is preferred, expounded upon in detail in the Green Paper, which endows the auditor with the function of directly informing markets, and protecting investors against unscrupulous corporate officers. In short, the auditor is seen as a deputy financial regulator, since the audit is integrated into banking and financial regulation.

This is doubtlessly the reason why the auditors were also notified of the complaint, even though their diligences exactly conformed to professional standards. But, they had not seen—and therefore had not denounced—that method of describing the outstanding orders was misleading, especially in the economically cyclical boat construction industry. Because of this, if they were being judged for providing information on financial reality, and not on whether they had obeyed the rules, they would have been punished. The person within the Autorité who drew up the complaint decided to follow the latter reasoning, whereas the Enforcement Commission decided to follow the former. This resulted in the auditor’s being declared innocent.

What should we think of this decision?

This might seem like indulgence towards the auditor, or like an anachronistic incomprehension of auditors’ new role in assuring the proper functioning of financial markets. The fact that the auditors were examined before being declared innocent illustrates this tension.

The difficulty is doubtlessly elsewhere, and is due to professional standards. The professional standards at hand are seen by many as overly formal and in need of revision. This is because they limit auditors to conversations with managers and consulting clients, rather than allowing them to seek out financial information rather than accounting information.

This is why we should revise accounting standards and professional standards before trying to hold auditors liable for such practices. This is why, in the meantime, the AMF’s Enforcement Commission seems wiser than the ambitious reforms of audit currently being discussed, which anticipate reforms in corporate governance that auditors will also have to obey.