

CORPORATE LAWS & GOVERNANCE

PROFESSIONAL 1 EXAMINATION - AUGUST 2017

NOTES:

Two envelopes must be used to enclose answers:

- Enclose answers to questions in **Section A in one envelope**, and
- Enclose answers to questions in **Section B in a second envelope**.

Mark clearly on each envelope the Section to which the answers relate.

Section A:

You are required to answer **three** questions from this section, (Questions 1, 2 and **either** 3 or 4). However, should you provide answers to **both** Questions 3 and 4, you must draw a clearly distinguishable line through the answer not to be marked. Otherwise, only the first answer to hand for each of these two questions will be marked.

Section B:

You are required to answer **one** question from this section. However, should you provide answers to each question in this section, you must draw a clearly distinguishable line through the answer not to be marked. Otherwise, only the first answer to hand for each of these two questions will be marked.

TIME ALLOWED:

3 hours, plus 10 minutes to read the paper.

INSTRUCTIONS:

During the reading time you may write notes on the examination paper, but you may not commence writing in your answer book.

Marks for each question are shown. The pass mark required is 50% in total over the whole paper.

Start your answer to each question on a new page.

You are reminded to pay particular attention to your communication skills, and care must be taken regarding the format and literacy of your solutions. The marking system will take into account the content of your answers and the extent to which answers are supported with relevant legislation, case law or examples, where appropriate.

List on the cover of each answer booklet, in the space provided, the number of each question attempted.

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Time allowed: 3 hours plus 10 minutes to read the paper.

Section A: You are required to answer **three** questions from this section.

Section B: You are required to answer **one** question from this section.

SECTION A

Answer both Questions 1 and 2 and either Question 3 or 4.

- 1.** Fleming, a qualified electronic engineer has been a non-executive director in Hubble Electronic Manufacturers Ltd for the past five years. The company has been run by his father Edison, who was the majority shareholder in the company. Unfortunately, Edison died last month and since then Fleming has taken a more active role in the management of the business. When Edison's last will and testament was read, Fleming discovered that he is the beneficiary of his father's shares in Hubble Electronic Manufacturers Ltd. This bequest includes both ordinary shares and preference shares in the company. When he saw the share certificate for the preference shares he noticed that the nominal value of these shares is €1, but that they were issued to his father at a discounted price of €0.50 per share.

Fleming also inherited a portfolio of shares in other companies from his father's estate. One of these bequests includes 30,000 €1 ordinary shares in Newton Engineering Plc. This company is having its Annual General Meeting next week and Fleming is keen to attend the meeting.

Although Fleming is familiar with the operational issues involved in running Hubble Electronic Manufacturers Ltd, he has no knowledge of company law, and, in particular, company capital. He has contacted you for advice regarding these issues.

REQUIREMENT:

- (a) Review the main characteristics of preference shares. (4 marks)
- (b) Examine the rules regarding issuing shares at a discount, and advise Fleming as to the consequences of a breach of those rules. (3 marks)
- (c) Arising from his inheritances, advise Fleming as to the information that must be recorded in the Register of Members of Newton Engineering Plc and Hubble Electronic Manufacturers Ltd. (5 marks)
- (d) Discuss the disclosure requirements imposed upon Fleming as company director, following his father's bequest of shares in Hubble Electronic Manufacturers Ltd. (5 marks)
- (e) Although Fleming has not yet received a Share Certificate in respect of his shares in Newton Engineering Plc, advise him as to what action he should take in order to attend and vote at the Annual General Meeting of this company. (3 marks)
- (f) Outline the nature of the ordinary business of a company discussed at an Annual General Meeting. (5 marks)

[Total: 25 marks]

2. Maxwell was the managing director and founding shareholder of Sagan Fine Arts Gallery Ltd. since its incorporation in 1984. Last year, Maxwell decided to retire and he resigned from his position on the board of directors. He was instrumental in having both his son Carter and daughter Cassidy appointed as executive directors to the company. In addition to Carter and Cassidy, there are three other executive directors and two other non-executive directors appointed to sit on the board of directors. Upon appointment, a provision was included in the company's constitution stating that Carter is a director for life.

Carter is involved in numerous other business ventures in addition to Sagan Fine Arts Gallery Ltd. In particular, he is also the owner of a garage that sells a range of vans and trucks. Last month, Sagan Fine Arts Gallery Ltd. decided to purchase new delivery vehicles and after a competitive tendering process the contract was awarded to Rutherford Motors, a business that Carter owns. However, at no stage did either Carter or his sister Cassidy mention that Carter was the owner of this business. The other directors of Sagan Fine Arts Gallery Ltd. subsequently discovered that the price they paid for the vehicles was significantly in excess of the market value. Upon investigation, they then discovered Carter's links to this business. When the board confronted Carter with this information he refused to discuss it, stating that the vehicles were purchased at a very competitive price and that he was not willing to discuss the matter further. When Cassidy was approached regarding this issue she broke down and told them that Carter paid her €5,000 to vote to award the contract to Rutherford Motors. The other directors of Sagan Fine Arts Gallery Ltd. are appalled by these events and have informed both Carter and Cassidy that they intend to seek their removal. Carter is challenging any attempt to remove him and has told the board that he cannot be removed as he is a director for life. Cassidy has met with the board and voluntarily tendered her resignation in the circumstances. She explained that as she is currently subject to a Restriction Order and doesn't want any negative publicity regarding her actions brought to public attention. The directors of Sagan Fine Arts Gallery Ltd. were shocked by this disclosure, as they were unaware that Cassidy has a Restriction Order imposed against her and they are now questioning whether she was eligible to act as a director on the board.

They have now contacted you for advice regarding these issues.

REQUIREMENT:

- (a) Discuss the eligibility requirements to act as a company director and advise Sagan Fine Arts Gallery Ltd. as to the prerequisite conditions that must be complied with under the terms of the Companies Act 2014, when appointing a restricted person as a director to their company. (8 marks)
- (b) Review the rules regarding substantial transactions in respect of a non-cash asset pursuant to Section 238 of the Companies Act 2014, and assess whether the actions of Carter are in breach of these rules. Comment also on the consequent penalties. (6 marks)
- (c) Evaluate whether the actions of Cassidy are in breach of her statutory fiduciary duty to Sagan Fine Arts Gallery Ltd. regarding independent judgment, commenting also on the consequent penalties. (5 marks)
- (d) What is the procedure that should be adopted by the company in order to remove Carson's status as a director for life to facilitate his subsequent removal?
Note: A discussion of the procedure to effect the lawful removal of a director is NOT required. (2 marks)
- (e) As a result of the issues with Carter and Cassidy, Maxwell has decided that he wishes to sell his shares in Sagan Fine Arts Gallery Ltd. One of the directors of the company has agreed to buy these shares, subject to obtaining a director's loan from the company. To legally effect this loan, Sagan Fine Arts Gallery Ltd. will be required to adopt the summary approval procedure. Outline the various steps involved in adopting the summary approval procedure. (4 marks)

[Total: 25 marks]

- 3.** After graduating from University with a degree in software design, Darwin set up an on-line dating business. This business quickly grew as Darwin had developed a programme that produced a high rate of compatible dating matches for his clients. After two years in business, his client base had expanded so significantly that he was approached by a multinational company wishing to invest in his business, with a view to launching his company onto the stock market in the near future. Following negotiations, Darwin agreed to accept the proposed investment from the multinational company and in return it required that he register this business as a public limited company. Darwin has contacted you for advice.

REQUIREMENT:

- (a) Discuss the main characteristics of a Public Limited Company, and comment specifically on the meaning and the impact of the company becoming a separate legal entity. (8 marks)
- (b) Darwin has been informed that following incorporation the company will have to apply for a Trading Certificate, but he is unsure as to the nature of this application. Review the information that must be submitted to the Companies Registration Office (CRO) in order to obtain a Trading Certificate. Comment also upon the impact of a company failing to obtain this Certificate before commencing trading. (5 marks)
- (c) Darwin is aware that the veil of incorporation can be lifted in certain circumstances. Advise him on the grounds upon which the veil can be lifted in accordance with the terms of the Companies Act 2014 and the corresponding effects when this happens.
- Note: A discussion of the grounds upon which the veil of incorporation can be lifted at the absolute discretion of the Court is NOT required.* (4 marks)
- (d) Darwin has been informed that the company will be required to notify the CRO of its registered office within the State. Examine the meaning of the term registered office. (3 marks)

[Total: 20 marks]

OR

4. Boyle is a registered auditor whose accounting and auditing practice operates mainly in the midlands. For the past six years she has been auditing the accounts of a national charity, Help4ewe Ltd. Following the audit, a copy of the financial accounts, directors and auditors reports are sent to the Charities Regulator.

It has recently been reported in the media that the Chief Executive of this charity, Hopper, has been defrauding this charity for years – by diverting funds from it to off-shore bank accounts held in his name. This fraud was discovered following an investigation of the company by the Courts and the Revenue Commissioners. The fraud has been headline news in national newspapers for the last month. As the Court and Revenue investigation progressed, even more fraud was detected which involved multiple company officers.

As a consequence of these reports, the shareholders and directors of Help4ewe Ltd. called Boyle to a meeting, wherein they asked her to explain how she had not uncovered any evidence of fraud when conducting the audit of the company. When Boyle could not provide a logical answer they told her that they had no option but to call a meeting for the purpose of effecting her removal based on her breach of duties. Boyle does not believe that she has done anything wrong, as any queries she had regarding irregularities in the finances of the company were discussed with the Chief Executive, Hopper, who always provided a plausible explanation to the queries raised.

Last week, Boyle received a letter from the accountancy institute of which she is a member and which is her regulatory body, notifying her that it required her to attend at a Disciplinary Tribunal in relation to allegations of professional misconduct. It also alerted her to the fact that a representative of Irish Auditing and Accounting Supervisory Authority (IAASA) would be present at this hearing.

Boyle has now contacted you for advice.

REQUIREMENT:

- (a) Examine the duty of the auditor to investigate the financial affairs of a company, commenting also on the prescribed content of an auditor's report. (8 marks)
- (b) Analyse the duty of care and skill owed by an auditor to a client and to potential third parties. (5 marks)
- (c) Based on your examination and analysis in Parts A and B, assess whether Boyle has breached her duties to Help4ewe Ltd. and whether she can be sued by the Charities Regulator for losses arising from the alleged negligence. (2 marks)
- (d) Evaluate the main function of IAASA, commenting specifically on its role in relation to the disciplinary processes of the prescribed accountancy bodies. (5 marks)

[Total: 20 marks]

SECTION B
Answer either Question 5 or 6.

- 5.** *“Enterprise Risk Management has never been higher on the agenda; organisations need to ensure that risk is taken seriously in the boardroom to ensure organisational success and longevity.”*

REQUIREMENT:

- (a)** Discuss the role and responsibility of a company's board of directors in establishing an appropriate risk management and internal control system. (18 marks)
- (b)** Evaluate the information on risk management which the board of directors are required to disclose in the annual statements. (12 marks)

[Total: 30 marks]

OR

- 6.** The UK Corporate Governance Code 2016 states there should be a formal, rigorous and transparent procedure for the appointment of new directors to the board.

UK Corporate Governance Code 2016. Financial Reporting Council.

REQUIREMENT:

- (a)** Discuss how the board of directors can ensure that the process for new appointments to the board fulfils this corporate governance requirement. (18 marks)
- (b)** Discuss the role and function of the companies registration office in Ireland. (12 marks)

[Total: 30 marks]

END OF PAPER

SUGGESTED SOLUTIONS

THE INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS IN IRELAND

CORPORATE LAWS & GOVERNANCE

PROFESSIONAL 1 EXAMINATION - AUGUST 2017

SOLUTION 1

- (a) **Preference Shares:** these are shares that carry certain preferential rights over ordinary shares. Their main characteristics are as follows: (1) where preferred as to capital, they are repaid this capital in priority to ordinary shareholders upon the liquidation of the company, (2) if there are available assets upon winding-up the preference shareholders have the right to participate in this surplus (unless the company's Constitution states otherwise), (3) where preferred as to dividend, they have the right to this payment in priority to ordinary shares, (4) this dividend is a fixed percentage return on their investment – the fixed return is prescribed by the company when the shares are issued, (5) the right to a dividend is normally cumulative, so if no profit is declared in any particular year, this right accumulates to the next profit period (with a maximum accumulation period of 6 years), and (6) these shares generally do not attract the ability to influence company policy as they have no voting rights (any 4 = 0-4 marks)
- (b) **Shares at a Discount:** (1) the general rule is that companies may not allot shares at a discount on their nominal value (as per *Oregum Gold Mining Co of India v Roper* (1892) and Section 71(2) CA 2014), (2) Section 71(3) provides that where a company issues shares in contravention of this rule then the person receiving these shares will be held liable to repay the company an amount equal to the amount of the discount and interest thereon at the appropriate rate, and (3) company officers who issue shares in breach of this rule may also be sanctioned, as contravention is classed as a Category 3 offence (3 = 0-3 marks).
- (c) **Register of Members:** Section 169 CA 2014 requires every company to keep a register of members which contains the following information: (1) the names and addresses of members, (2) a statement of the number and class of shares held by each member, (3) the amount paid or considered to be paid on the shares of each member, (4) the date on which each person was entered on the register as a member, (5) the date at which any person ceased to be a member, and (6) where the company has converted any of its shares into stock, the register must show the amount of stock held by each member instead of the amount of shares and the particulars relating thereto (any 5 = 0-5 marks).
- (d) **Disclosure Requirements:** (1) Section 261 CA 2014 requires that directors and the company secretary disclose any legal or beneficial interests in the company's securities (shares and debentures), held by either themselves or their families – therefore Fleming has to disclose his inheritance of shares in Hubble Electronic Manufacturers Ltd, (2) this disclosure must be made in writing, (3) it is irrelevant whether these interests and rights are given free of charge or by any other member of the public for a fee, (4) such an interest must be notified within five/eight days of becoming aware of it (depending on the type of interest), and (5) Section 267 requires the company, on receipt of the relevant information, to keep a register of these interests and any charges thereto, which must be entered within three days – this register must ordinarily be available free to members, although a nominal fee may be charged to non-members (0-5 marks)
- (e) **Share Warrant:** in order for Fleming to attend and vote at the AGM of Newton Engineering PLC he may request a share warrant from the company in respect of his 30,000 €1 ordinary shares. This is a bearer instrument/negotiable instrument in relation to shares in a PLC, issued under the common seal of the company. The general rule is that the shares specified in the warrant are fully paid. The share warrant is a document of title as it entitles the bearer to the shares specified therein, and may provide for the payment of the future dividends on the shares included in the warrant (Section 88 CA 63 and Section 620(8) CA 2014) (0-3 marks).
- (f) **Ordinary Business of an AGM:** in accordance with Section 186 CA 2014 the ordinary business to be conducted at an AGM is generally as follows: (1) the consideration of accounts and the Directors and Auditors Reports', (2) a review of the company's affairs, (3) the declaration of a dividend (subject to the provisions of the company's Constitution), (4) the fixing of the salary of the statutory auditors (subject to the provisions of the company's Constitution), (5) the election and re-election of directors (subject to the provisions of the company's Constitution), (6) the appointment or re-appointment of the statutory auditors, and (7) the fixing of the remuneration of directors (subject to the provisions of the company's Constitution) (any 5 = 0-5 marks)

SOLUTION 2

- (a) **Eligibility:** the Companies Act 2014 prohibits the following people from acting as company directors: (1) undischarged bankrupts (Section 871(1) CA 2014 – breach is classed as a category 2 offence), (2) corporate bodies, (3) the auditor of a company or its holding company, (4) a minor (under the age of 18 – Section 131 CA 2014), (5) a disqualified person – or (6) in certain situations a restricted person, and (7) a person who already holds more than 25 directorships (any 4 = 0-4 marks)

Appointment of a Restricted Person: (1) where a person is subject to a Restriction Order they are still entitled to act as a director or secretary of a highly capitalised company. This can be defined as a Public Limited Company with an issued share capital of at least €500,000 (Section 819(3)(a) CA 2014) or any other company with an issued share capital of at least €100,000 (Section 819(3)(b)), (2) in this situation the restricted person must give notice to the company before accepting appointment or acting as a director or secretary of the fact of their restriction (Section 825 CA 2014), and (3) in addition, special rules are applied in relation to the maintenance of capital while a company has appointed a restricted person (such as the Summary Approval Procedure cannot be applied (Section 827), and the company cannot acquire certain non-cash assets from subscribers unless particular conditions are satisfied (Section 828)) (0-4 marks).

- (b) **Substantial Transaction in Respect of a Non-Cash Asset:** in accordance with Section 238 CA 2014, this can be defined as the purchase by a the company of a non-cash asset from a director/connected person or the acquisition by a director of a non-cash asset from the company (or its holding companies) whose value exceeds €65,000 or 10% of the company's assets and whose value is not less than €5,000 (0-2 marks) – in this situation before the acquisition can take effect the company must: (1) obtain approval to proceed with the transaction by an ordinary resolution of its shareholders in a general meeting, or (2) if the director or connected person is a director of its holding company or a person connected with such a director, by a resolution of the holding company in general meeting (0-2 marks)

Conclusion: depending on the value of the contract, Carter has breached these rules as he has failed to obtain approval from the shareholders to effect this transaction – failing to comply with these requirements leaves the contract voidable at the option of the company (0-2 marks)

- (c) **Duty to Maintain Independent Judgment:** this duty requires a director to exercise independent judgment in the performance of their duties, except where otherwise permitted by the Constitution of the company or where it is approved by an ordinary resolution of the members in a general meeting. In *Fulham Football Club Ltd and others v Cabra Estates plc* (1992) a substantial payment to the company in return for undertakings given by the directors not to object or support an application by the Council for the compulsory acquisition of the defendant's property, was not deemed to fetter the directors' independent judgment as the agreement conferred substantial benefits on the company and did not personally benefit the directors per se (0-3 marks).

Conclusion: the actions of Cassidy are in breach of this duty as she accepted a payment from Carter not to disclose his interest in the asset – in doing this she was not acting in good faith and the best interests of the company – but rather she acted in a manner to benefit herself personally – in this situation, Cassidy may be liable to account to the company for the €5,000 gain she made from her breach of duty, and indemnify the company for any loss or damage resulting from that breach (Section 232 CA 2014) (0-2 marks).

- (d) **Director for Life:** as Carson's status as a director for life is stated in the company's Constitution, to alter this status the company will need to amend its Constitution. This will require a special resolution (75% approval) of the shareholders at a general meeting (with a minimum of 21 days' notice to the members) and subsequent notification to the Companies Registration Office (0-2 marks).

- (e) **Summary Approval Procedure:** this involves: (1) the passing of a resolution (special or unanimous written) conferring authority, within 12 months prior to the commencement of the restricted activity, (2) the company must deliver to the Registrar a copy of the declaration as required under Section 202 CA 2014, (3) this declaration must be in writing and made by the directors at a meeting of the directors held not earlier than 30 days before (a) the meeting of the members to approve the resolution or (b) the last member signs a written resolution (as the case may be) to approve the activity, and forwarded to the members with notice of the meeting, (4) the declaration is in reality a declaration of solvency, stating that the directors have made a full inquiry into the affairs of the company and that the company will be able to pay its debts and liabilities as they fall due for a period of 12 months after the restricted activity is carried out, and (5) the company must deliver the declaration to the CRO not later than 21 days after the date on which the activity is commenced (any 4 = 0-4 marks).

SOLUTION 3

- (a) **Public Limited Company:** the main characteristics of a PLC are as follows: (1) this company requires a minimum of 1 shareholder – there is no maximum threshold, (2) a public company must have a minimum issued share capital of €25,000 – 25% of which must be fully paid, (3) a public company must have a minimum of two directors and one company secretary, (4) the Constitution of a public company encompasses both a Memorandum of Association and an Articles of Association and the application for registration must state that it is a public limited company, (5) a public limited company's contractual capacity is limited by the terms of its objects clause, (6) a public company can only trade upon receipt of a trading certificate from the CRO (this document evidences everything about the company that makes it public), (7) a public limited company is required to hold an AGM, where it has two or more members, (8) a public company can sell its shares freely to the public, (9) a public limited company can be listed on the stock market, and (10) the name of a public limited company must end in the word PLC or its Irish equivalents (any 4 = 0-4 marks)

Separate Legal Entity: this concept means that a company has a separate legal status from its members – and in reality has a distinct personality from the natural persons who set up the company. This was first recognised in the case of *Salomon v Salomon & Co Ltd* (1897) wherein a debenture created in favour of the majority shareholder was deemed valid as the company was a separate entity to the majority shareholder (0-2 marks) – this separate personality means that a company can: (1) own their own property, (2) enter in contractual relations with either natural persons or other companies, (3) commit crimes and be held responsible for such crimes, (4) have perpetual existence, (5) be sued or sue other persons – and (6) in addition, this separate personality also gives the shareholders of the company limited liability (any 4 = 0-2 marks)

- (b) **Trading Certificate:** Section 1010 CA 2014 states that in order to receive this certificate a public company must deliver a statutory declaration to the CRO stating: (1) the nominal value of the company's allotted share capital and that it is not less than the authorised minimum (€25,000) (Section 1010(2) CA 2014), (2) the amount paid-up, at the time of the application on the share capital of the company, (3) the preliminary expenses of the company and the persons who have been paid or are payable, and (4) any intended payment or benefit to be paid to the company's promoters (persons establishing the company and doing everything necessary to effect its formation) (any 3 = 0-3 marks) – where a PLC does business or exercises borrowing powers without a valid trading certificate: (1) the PLC and any officer of it who is in default will be guilty of a category 3 offence (Section 1010(7)), and (2) the directors of the PLC will be deemed jointly and severally liable to indemnify the other party to the transaction in respect of any loss or damage suffered by that party by reason of the failure by the PLC to hold a valid trading certificate (Section 1010(9)) (2 = 0-2 marks)

- (c) **Lifting the Veil:** (1) personal Liability for company name irregularities: Section 27 CA 2014 provides that if a company fails to affix its name properly on its place of business, letters, documents, and bills of exchange, the officer of the company will be liable on summary conviction, to a fine not exceeding €5,000 or imprisonment for a term not exceeding six months or both, (2) personal liability for taxation offences: Section 94 of the Finance Act 1983 provides that when a tax offence is committed by a company with the consent of a person within the company, that person may also be subject to legal proceedings, (3) personal liability for fraudulent trading: Section 722 CA 2014 provides that if any person is knowingly a party to the carrying on the business of a company with intent to defraud its creditors or the creditors of any other person, or for any fraudulent purpose, he or she shall be guilty of a category 1 offence, (4) personal liability for reckless trading: Section 610 CA 2014 states that if in the course of liquidation a company officer is a party to carrying out business in a reckless matter, the court may, if it considers it proper to do so, upon application by a liquidator/creditor, hold such person personally responsible for all or any of the debts that the court directs, (5) personal liability re contribution/pooling orders upon winding-up: under Section 600 CA 2014 a company may be required to contribute to the debts of related companies, taking into account the extent of the company's control over the related company, (6) personal liability for the failure to maintain proper books of account: in accordance with the requirements of Section 286 liability will be imposed upon the company and its directors for failure to maintain proper accounting records. This is classed as either a category 1 or 2 offence – depending upon the nature of the actual breach, (7) Restriction Orders: Section 819 CA 2014 provides that on the application of either a liquidator or a receiver the courts shall declare that a person who was a director or shadow director of an insolvent company at the date of, or within 12 months before, the commencement of its winding up shall not for a period of five years be appointed or act in any way, directly or indirectly as a director or secretary of a company, or take part in the formation or promotion of a company, and (8) Disqualification Orders: Section 838 CA 2014 provides that a person may be disqualified from being appointed or acting as a director or other officer, statutory auditor, receiver, liquidator or examiner, or being in any way, whether directly or indirectly, concerned or taking part in the promotion, formation or management of a company for a period of five years or more and may be guilty of a criminal offence or may be personally liable for the debts of the company should it become insolvent within 12 months of the disqualification order being made (any 4 = 0-4 marks)

- (d) **Registered Office:** this is (in effect) the company's legal address – as it is the place where legal documents (such as writs or summonses) can be served on the company and also the place where statutory documents and registers, such as the register of members, are required to be kept available for inspection. Details of the company's registered office must be notified to the Registrar of Companies prior to its incorporation (Section 50 CA 2014), as well as any changes to this address (Section 50(3)) – failure to do so will leave the company liable to a category 4 offence (0-3 marks)

SOLUTION 4

- (a) **Auditor's Duty to Investigate:** an auditor is obliged, as part of his statutory duties, to investigate the financial affairs of the company and report to the members on these affairs at the AGM (Section 391 CA 2014). According to Lord Justice Lopes in *Re Kingston Cotton Mills Co. (1896)*: "[a] auditor is not bound to be a detective, or, as was said to approach his work with suspicion, or with a foregone conclusion that there is something wrong. He is a watchdog, not a bloodhound. He is justified in believing tried servants of the company in whom confidence is placed by the company. He is entitled to assume that they are honest and rely upon their representations, provided he takes reasonable care." This duty requires the auditor to protect the interest of those who appointed him. But he can assume the servants of the company are acting honestly and he can rely on their statements – unless evidence indicates otherwise. In doubtful cases he should investigate matters thoroughly. But he is also not expected to act with a suspicious mind (as per Lord Denning in *Fomento (Sterling Area) Ltd. v Selsdon Fountain Pen Co. Ltd. (1958)*) (0-4 marks)

Auditors Report: in accordance with Section 336 CA 2014 the auditor's report must include statements regarding the following matters: (1) whether the auditor received adequate information and explanations from the company necessary for the purpose of the audit, (2) whether the company's accounting records and returns correspond with the balance sheet and profit and loss account, (3) whether, in their opinion, the accounting records of the company were sufficient to permit the financial statements to be readily and properly audited, (4) whether in their opinion the annual financial statements give a true and fair view of the financial state of affairs of the company, (5) whether the accounts are in compliance with the relevant financial reporting framework and the requirements of legislation, and (6) whether the information given in the directors' report for the financial year is consistent with the statutory financial statements (any 4 = 0-4 marks)

- (b) **Auditor's Duty of Care and Skill:** where an auditor fails to perform his duties with reasonable care and skill (as required by his profession, auditing guidelines, SSAP's and accounting standards), he may be liable to the client company for his acts of negligence. In *Re Thomas Gerrard & Sons Limited (1967)* the auditor was held liable in negligence to the client company where they failed to investigate suspicious transactions relating to the company's stock – but instead accepted the managing directors (fabricated) explanation for these discrepancies. Similarly, in *Kelly v Haughey Boland (1989)* the defendant auditors were liable in negligence arising from their failure to attend and observe a client company's stock taking for over 20 years (0-3 marks).

Third Party Liability: an auditor is only liable to a third party where they know or ought to have known that the third party relied upon their report (as per *Caparo Industries plc v Dickman (1990)*) – this can be seen in the case of *Law Society v KPMG Peat Marwick (2000)* where the auditors were appointed by solicitors to prepare a report, which the solicitors on receipt were required to deliver to the Law Society. The Court held that the auditors owed a duty of care to the Law Society as they knew that they would be relying on the accuracy of this report (0-2 marks).

- (c) **Conclusion:** Boyle has breached his duty to Helping Hand Ltd as he has not properly investigated the affairs of the company and has instead relied on the managing director's explanation in relation to queried transactions. He can be sued by the government for losses arising from his alleged negligence, provided he was aware (or should have realised) that the government was relying on his auditor's report when allocating funding to the charity (0-2 marks).

- (d) **Irish Auditing and Accounting Supervisory Authority (IAASA):** pursuant to Part 15 Chapter 2 of the Companies Act 2014, the principal functions of IAASA are to strengthen the regulation of auditors, and to supervise the regulatory functions of the prescribed accountancy bodies (PABs) (0-1 mark). In effect the role of IAASA revolves around: (1) supervising how the PABs regulate and monitor their members, (2) promoting adherence to high professional standards in the auditing and accountancy profession, (3) monitoring whether the financial statements or accounts of certain classes of companies and other undertakings comply with this Act, and (4) acting as a specialist source of advice to the Minister on auditing and accounting matters (Section 904 CA 2014) (any 3 = 0-3 marks)

Disciplinary Processes: IAASA is empowered to: (1) conduct enquires into whether each PAB has complied with its approved investigation and disciplinary procedures, (2) supervise the investigation and disciplinary procedures of the PABs, including accessing their records, and requesting explanations about the performance of their regulatory and monitoring duties, and (3) and where a PAB has not complied with its own disciplinary procedures vis-à-vis their members, IAASA has the power to impose sanctions (any 2 = 0-2 marks)

SOLUTION 5

- (a) The assessment of risk as part of the normal business planning process should support better decision-making and ensure that management respond promptly to risks and inform shareholders and other stakeholders about the principal risks and prospects of the company.

Directors are responsible for implementing appropriate risk management and internal control systems within a company. The directors of the company must consider the material risks and uncertainties the company faces. The directors should consider business, operational and financial considerations and risks in the broader sense such as cyber security and Brexit. The business should carry out, on an on-going basis, an assessment of the principal risks to the company's business model and address its ability to deliver its strategy including solvency and liquidity risks. The focus of the risk management and control system must be a long-term view of the company's prospects. The normal period to be considered is between three and five years.

The directors should consider how specific principal risks are stress tested and provide information on the range of assumption and consider the further use of financial modelling.

The directors are required to confirm that a robust assessment of the principal risks facing the company has been undertaken and how the management believe these risks will be managed and mitigated. This review needs to take place at least annually.

The director should provide meaningful disclosures on how the underlying analysis was performed and what judgements was necessary in arriving at its statements. The directors are required to specifically state in the financial statements on whether the going concern basis of accounting have been adopted and whether there are any material uncertainties about the company's ability to continue to do so in the future.

The directors should ensure that an appropriate culture and reward system has been embedded throughout the organisation. The board will need to monitor and review the risk management and internal control system and satisfy itself that this is functioning effectively and corrective action should be taken if needed.

(18 marks)

(b) **Annual statement**

The directors of the company in their annual review of effectiveness need to consider the company's willingness to take on risk: "its risk appetite", state how the risk management and internal system has been operating throughout the business and how it is integrated with consideration to the strategic and business model.

The information provided in the annual report and accounts should provide sufficient and appropriate information necessary for shareholders to assess the company's position and performance, its business model and strategy and to appreciate the arrangements the company has put in place to gather information to satisfy their information needs.

Directors are required to explain the background processes analysis which have been undertaken. There should be sufficient information for the users to determine how judgements have been arrived at including any qualifications or assumptions.

Directors should give details on the principal risks that have identified and specifically state them in the statement analysis. The report should include a description of the likelihood of a risk and indication of the circumstances under which the risk maybe relevant and its possible impact. The board should explain what actions have been taken and are being taken to remedy any significant failings and weaknesses. The reader should be given sufficient information on the financial modelling approach and the stress testing that has been carried out

(12 marks)

[Total: 30 marks]

SOLUTION 6

- (a) The Board of Directors should establish a nomination committee which would lead the process for appointments and would make recommendations to the board. The nomination committee should be chaired by the chairman and populated by independent non-executive directors, except on the occasion whereby it is the chairman who is being replaced.

The terms of reference of the nomination committee must be clearly determined to ensure that a formal and rigorous approach to appointment is undertaken. The search for and the appointment of board members should be made on the basis of merit with the consideration for the need for diversity on the board including gender.

The nomination committee should consider skills, experience, independence and knowledge currently on the board and identify the role and capabilities required for the new appointment. The object is to ensure that there is an appropriate balance of skills and experience on the board and to continually refresh the skills and talents on the board. The board should ensure that there are plans in place for orderly succession for appointment to the board and to senior management to ensure continuity and succession planning.

Disclosure is required in the annual accounts in a separate section which should describe the work of the nominations committee and how this process is used to make board appointments. Details on external consultancy that has been used in the appointment process for the chairman or the non-executive director should be disclosed. An explanation should be given if an external search consultancy or open advertising has not been used in the appointment of the chairman or the non-executive directors.

(18 marks)

- (b) The companies registration office in Ireland, under the Companies Act 2014, is the central repository of public statutory information on Irish companies and business names. The companies registration office operates within the Department of jobs, enterprise and innovation

The companies registration office has a number of functions including:

1. The incorporation of companies and the registration of business names
The CRO is the statutory authority for registering new companies and registers business addresses in the Republic of Ireland. It also includes the office of the register of friendly societies which regulates industrial and provincial societies, friendly societies and trade unions.

2. The receipt and registration of corporation documents.

There is an obligation on companies to file certain documents with the companies registration office including details of the registered office and any changes, changes to the company officers and changes which affect the company. Companies are required to file annual returns and in most cases they must also file accounts and the companies registration office will also keep details of mortgages and charges imposed on companies.

3. The enforceability of the companies act in relation to the filing obligations of companies
If accounts are not filed then the companies registry office can take measures against companies who failed to file the annual returns including prosecution of the company or its directors or removing the company from the register.

4. Making information available to the public
Some information such as the company name and registered office address can be accessed by the public free of charge. A small fee may be payable for other information held by the companies registration office. The companies registration office provides publication of information on an online gazette on a weekly basis including new companies, annual returns have been received and registered, liquidations, foreign companies and other information.

(12 marks)

[Total: 30 marks]