Editorial

Caparo Industries

Do auditors owe a duty of care to shareholders in a public company who might be contemplating the purchase of further shares in that company? This interesting and tricky question went to appeal to the House of Lords at the beginning of this year in the case of *Caparo Industries plc v Dickman* (see p 105), the trial judge having answered the question, on a preliminary point, in the negative, and the Court of Appeal reversed him by a majority.

Following a dramatic fall in the share price of Fidelity plc in 1984, another company, Capro, had begun to purchase Fidelity shares; subsequently it made a successful takeover bid for the company. But on closer scrutiny of the books Capro got a nasty shock, which prompted it to launch an action in negligence against Fidelity's auditors, Touche Ross. The basis of the claim was that the purchase of most of the shares, and the bid itself, had been made in reliance on inccurate accounts, which had shown a pre-tax loss as a substantial profit.

However, their Lordships unanimously held that auditors are not liable to third party investors in such circumstances. Lord Bridge drew a sharp distinction between various leading cases in the past where the defendent giving advice had been fully aware of the nature of the transaction that the plantiffs were contemplating and knew that they intended to rely upon his advice, and a case like the present one where a statement had been put into general circulation and might foreseeably be relied upon by strangers to the author of the statement for any one of a variety of different purposes which the author had no specific reason to anticipate. Lord Oliver, in his concurring judgment, felt unable to detect in the relevant statutory provisions any departure from the traditional function of company audit as that of providing shareholders with the necessary information to exercise over a company, "and not for the purposes of individual speculation with a view to profit."

This restrictive interpretation seems unduly protective of the accounting profession, and it may even be said to cast doubt upon the rationale of company audit as presently conceived. And, with the aftershock of the Barlow Clowes affair still ringing in our ears, and with litigation against financial intermediaries in prospect, we are surely entitled to wonder whether the law is sufficiently sensitive to the position of vulnerable creditors and investors in collapsed companies, who will often have precious little independent evidence to guide them through a financial minefield – apart from the auditors' reports.