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# THE AUDIT COMMITTEE AND DIRECTORS' LIABILITY

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# DIRECTORS' & AUDIT COMMITTEE LEGAL LIABILITY



## GROUPS FOR DIRECTORS' & AUDIT COMMITTEE LIABILITY

### ■ Liability i.t.o. common law:

- Fiduciary duty to exercise powers:
  - Bona fide for the benefit of the company
  - With care, skill and diligence of like person in similar circumstances
  
- Breaches of above:
  - Common law liability: not acting in best interest of company
  - Delict: failure to act with care, skill and diligence
  - Criminal liability

# DIRECTORS' LEGAL LIABILITY (CONTINUED)



## GROUNDINGS FOR DIRECTORS' & AUDIT COMMITTEE LIABILITY

- **Liability i.t.o. Breach of Statute (Statutory Liability):**
  - Companies : Section 77 (Standards for directors' conduct):
    - Act in best interest of company
    - Act with care, skill and diligence
  - Breaches of the above
    - Jointly and severally liable i.t.o. sec.77 for losses suffered by the company

# DIRECTORS' LEGAL LIABILITY (CONTINUED)



## GROUPS FOR DIRECTORS' & AUDIT COMMITTEE LIABILITY

- **Various other legislation, e.g.:**
  - NEMA: Personal liability, fines and imprisonment
  
- **Fines by Stock Exchanges**
  
- **Corporate Governance 'liability':**
  - Represent standards of best practice
  - Could be used as reference/benchmark by Courts

# ROLE OF AC TO LIMIT DIRECTOR LIABILITY



## MOTIVATION FOR FORMING AC

- The law makes provision for boards to delegate responsibilities to subcommittees
- Committees can effectively advance the business of the board and demonstrates that directors' responsibilities are adequately and properly discharged
- Effective ACs are :
  - Small committees with a focused remit
  - Diligent, attentive members, that are
  - Independent, and have the financial experience and expertise to assist the directors in meeting their financial reporting, control and related responsibilities

# ROLE OF AC TO LIMIT DIRECTOR LIABILITY (CONTINUED)



## COULD SERVE AS EVIDENCE

- That directors acted
  - In the best interest of the company
  - With care, skill and diligence
  - by allocating financial reporting, control and related responsibilities to an effective AC (that has the skills, experience, financial expertise)
  
- Effective means: to ensure that the responsibilities of board regarding financial reporting, control and related matters are adhered to

# ROLE OF AC TO LIMIT DIRECTOR LIABILITY (CONTINUED)



## BOARD REQUIREMENTS

- *Board, however, cannot rely blindly on work of AC*
  - Must ensure AC is effective
    - Formation and Charter
    - Authority and resources
    - Membership
    - Monitoring of AC work and findings
  - Must apply critical judgement to AC's work and findings

# LIMITING AUDIT COMMITTEE LIABILITY



## STEPS TO LIMIT LIABILITY

- Constitution/set-up
  - Board resolution
  - Shareholders committee i.t.o. external auditing
  
- Status
  - Committee of the Board for Corporate Governance duties
  - Shareholders committee i.t.o. external audit
  - Ultimate responsibility still reside with the Board

# LIMITING AUDIT COMMITTEE LIABILITY (CONTINUED)



## STEPS TO LIMIT LIABILITY (Continued)

- Terms of Reference (charter)
  - Formal terms of reference
    - roles, duties, responsibilities
  - Formally approved by the Board
  - Regularly reviewed
  
- Chairperson
  - Responsible, respected
  - Non-executive (independent)
  - Elected by board

# LIMITING AUDIT COMMITTEE LIABILITY (CONTINUED)



## STEPS TO LIMIT LIABILITY (Continued)

- Election of members
  - By shareholders for public and SOE
    - Board to provide names of directors for AC
  - By Board for rest of entities
  - Membership requirements: Financial expertise/time/induction
  - Co-opt if board lack expertise ??? (Liability !!!!)
- Proceedings and meetings
  - Normal meeting procedures
  - Documentation in time
  - Agenda
  - Minutes
  - Number: at least 3: difficult for less than 4

# LIMITING AUDIT COMMITTEE LIABILITY (CONTINUED)



## STEPS TO LIMIT LIABILITY (Continued)

- Responsibility : Do not exceed outside remit
- Normal responsibilities, e.g.:
  - Financial Reporting; Internal control; Internal audit
  - External audit; Risk management; Sustainability reporting
  - Other

# CHALLENGES & RISKS FOR AUDIT COMMITTEES



- Skill requirements for AC
  - Financial
  - Other: Sustainability, IT, Ethics
- Increased liability
- Co-opted members : position, liability
- Remuneration: higher risk, higher remuneration
- Availability of experienced AC members
  - Independence \* Skills \* Time \* Co-opt
- Increased time expectations
- Greater expectations of IA function
- Potential conflicts with board
  - Statutory vs. corporate governance responsibilities

# CONCLUSION & RECOMMENDATIONS



- Audit committee can play an important role in assisting directors in meeting their financial reporting and related responsibilities
- Board, however, needs to:
  - Ensure ACs are effective:
    - consist of independent directors with the necessary experience, financial expertise
    - have the resource and support to perform their functions and responsibilities
    - have the full support of the board and its members
  - Apply critical judgement to the Audit Committee work and findings in meeting their financial and related responsibilities
- **AUDIT COMMITTEES: LIMIT THEIR LIABILITY**
  - ***membership, functions, diligence, reporting, etc***

**Thank you**



*Any Questions?*