



TO: European Commission, DG Internal Markets & Services, Unit F4

RE: EC Consultation on Auditor Liability

DATE: March 14 2007,

The European-American Business Council (EABC) is an alliance of 67 European and US-based companies (list attached) committed to increasing Trans-Atlantic investment, innovation and integration through competitive policies and regulatory collaboration.

EABC welcomes the opportunity to participate in the European Commission's consultation on auditor liability and its impact on EU capital markets. This is an important issue for EABC member companies because of their need for audit services from competitive, global and financially strong accounting firms.

Financial audits serve as the foundation of all commercial accountability and the confidence that underpins individual and institutional investments. It is for this reason – risk to investors, capital markets and the European economy – that the sustainability of the audit profession is so important.

The London Economics Report of November 2006 was a powerful statement that reflected a growing consensus among stakeholders – insurance companies, the business community, regulators and institutional, as well as individual investors - that liability reform is an essential component of a modern capital market across the European Union.

The report shed new light on the significant and negative impact of litigation in an unlimited liability regime – an economic threat that should be particularly disconcerting to European public officials and capital market participants. **EABC believes that the following points from the report make the case for reform overwhelming, and sensibly summarise our views on this issue:**

1. Given the number of actual or potential claims outstanding, the risk of an award or settlement in excess of the tipping point is significant and one of the major accounting firms could possibly fail as a result.
2. Given the limited availability of insurance and the large number of actual and potential claims faced by a number of the major accounting firms, it cannot be ruled out that a second network would fail as well.

3. In light of points 1 and 2 – investor confidence will fall significantly.
4. The level of auditor liability insurance available for higher limits from the commercial markets has fallen sharply in recent years in terms of both the level and amount of insurance. The current level of available commercial insurance would cover less than 5% of the larger claims that some firms face today in several EU Member States.
5. Negative perceptions about the viability of audit firms may unfairly create doubt about general accounting standards in all of its forms.
6. A reasonable limitation on auditor liability would reduce risk caused by potential catastrophic claims.
7. A substantial majority of companies are of the view that the liability regime has no impact on the quality of the audit.
8. The existence of an auditor liability limitation will limit risk and thus help middle-tier firms break into the market segment that is now largely dominated by the Big-4 Firms in many countries.
9. The diversity of audit firms and companies across the EU is such that it is unlikely that a one-size-fit-all approach to liability reform is the most useful.

Given that over half of all EU member states have some form of liability limitation and that the move towards reform is either already occurring or at least on the agenda around the world, the time is right for a pan-European approach.

The EABC and its member companies believe the EU should recommend that unlimited liability should end across the Member States. However, while some form of limited liability is essential, Member States should be able to adopt a range of options for limiting liability to suit the circumstances of their own domestic economy. A single European-wide cap, for example, would be too inflexible to respond to the differing audit markets and economies across Europe. We also believe that from a pragmatic point of view, those nations that have some form of liability limitation should keep their own regime.

EABC believes that countries without liability limitations should be encouraged to consider adopting proportionate liability coupled with an appropriate capping regime. This would ensure that auditors pay damages in proportion to their degree of culpability, while providing some protection against catastrophic claims. This builds on the policy options outlined in the consultation paper. It would open the audit market to greater competition, while maintaining audit quality and the long term viability of public interest auditing.

For more information, contact:

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