PlanAssure PAC (formerly known as Patrick Lee PAC) v Gaelic Inns Pte Ltd [2007] SGCA 41

Case Number : CA 2/2007

Decision Date : 30 August 2007

Tribunal/Court : Court of Appeal

Coram : Chan Sek Keong CJ; Andrew Phang Boon Leong JA; V K Rajah JA

Counsel Name(s) : Ang Cheng Hock and Kenneth Lim Tao Chung (Allen & Gledhill) for the appellant; Philip Fong, Navin Joseph Lobo and Bernice Tan (Harry Elias Partnership) for the respondent

Parties : PlanAssure PAC (formerly known as Patrick Lee PAC) — Gaelic Inns Pte Ltd

Evidence – Admissibility of evidence – Relevance of admission made in criminal proceedings – Admission by accused not binding on parties not involved earlier

Professions – Accountants and auditors – Professional standards in auditing – Duty to detect fraud

Tort – Negligence – Causation – Absence of reckless or deliberate conduct breaking chain of causation

Tort – Negligence – Contributory negligence – Importance of fact-specific approach – Broad brush assessment – Section 3(1) Contributory Negligence and Personal Injuries Act (Cap 54, 2002 Rev Ed)

Tort – Negligence – Duty of care – Auditors – Whether auditor owing duty to detect fraud – Whether auditor breached duty in performance of audit – Whether loss to company caused by auditor's breach – Appropriate quantum of damages company entitled to

30 August 2007 Judgment reserved.

V K Rajah JA (delivering the judgment of the court):

1 This is an appeal by PlanAssure PAC (previously known as Patrick Lee PAC) ("the appellant") against the decision of the trial judge awarding judgment to Gaelic Inns Pte Ltd ("the respondent") for the sum of $775,266.02 as damages for negligence in respect of audits performed by the appellant (see *Gaelic Inns Pte Ltd v Patrick Lee PAC* [2007] 2 SLR 146 ("GD")).

2 Having heard and carefully considered the submissions of the respective parties, we have decided to allow the appeal in part. We now set out the reasons for our decision.

The facts

3 The appellant is a firm of certified public accountants and was established in 1974 under the name of Patrick Lee & Co. The appellant's partnership was converted to a public accounting corporation incorporated under the Companies Act (Cap 50, 1994 Rev Ed) ("CA") in 2002.

4 The respondent is engaged in the business of owning and operating, *inter alia*, pubs in Singapore.

5 The appellant was engaged by the respondent as its statutory auditors to audit the respondent's accounts for the financial years ("FYs") of 2001, 2002 and 2003. The audit required the appellant to comply with the terms of s 207 of the CA, and express an opinion as to whether the

respondent's financial statements gave a true and fair view of its profit and loss.

6 Pursuant to this, Tow Juan Dean ("Tow"), a director of the appellant and a qualified practising accountant, was assigned to be the statutory auditor in charge of the audit of the respondent's financial statements. Tow was assisted by Phong Wai Lee ("Phong"), who was employed as an audit manager of the appellant but who was not a qualified practising accountant.

7 The yearly audits for FYs 2001 and 2002 were completed without incident. Thereafter, the respondent retained the appellant's services to conduct the yearly audit for FY 2003.

8 Three directors sat on the respondent's board of directors at the material time of the various audits for FYs 2001, 2002 and 2003:

(a) Ian Crowhurst ("Crowhurst"), managing director;

(b) Charles Lew Foon Keong ("Lew"), non-executive director; and

(c) Shaw Hui Jeong ("Shaw"), non-executive director.

9 Between 2001 to 2004, Denise Ang ("Ang"), the respondent's former group finance manager, devised and carried out a scheme whereby she delayed banking in cash on the day of sales into the respondent's bank account, and instead used the cash for her personal benefit. To make up for the resulting shortfall, Ang would bank in an equivalent amount of cash subsequently collected from later sales. For a period of time, Ang managed to avoid detection because she would subsequently bank in the same amount of money that she had taken out. This method of misappropriation is usually described in accounting parlance as "teeming and lading".

10 Ang's misappropriation of funds was eventually detected by the respondent's payroll and administration manager, Maggie Seah ("Seah"), on 24 May 2004. Ang has since been charged with and convicted on three counts of criminal breach of trust under s 408 of the Penal Code (Cap 224, 1985 Rev Ed). Six other similar charges were taken into consideration. The total sum misappropriated was $1,006,115.12. To date, the respondent has recovered from Ang the paltry sum of $8,929 and an additional sum of $100,000 from its insurers.

11 In July 2005, the respondent commenced the present suit against the appellant, in which it seeks damages of close to $1m for negligence in respect of the audits performed by the appellant between 2002 and 2004. The crux of the respondent's case is that the appellant failed to detect Ang's cash misappropriations during the audit of the accounts for FYs 2001, 2002 and 2003, thereby emboldening and enabling Ang to continue with her misappropriation.

12 The respondent avers that the appellant's negligence caused losses at two levels. Where past losses are concerned, the appellant's negligence, it is alleged, caused the respondent to lose the chance of recovering the misappropriated sums from Ang before the sums were dissipated. Additionally, the respondent alleges that the subsequent misappropriations could have been averted had the appellant discharged its duties.

13 In the proceedings below, the appellant strenuously opposed the respondent's allegations of negligence. In disputing its liability, the appellant made the following points:

(a) It had not breached its duty of care to the respondent.

(b) Even if the appellant had been in breach, such breach did not cause any losses in FYs 2001 and 2002.

(c) The appellant had been prevented from discovering Ang's misappropriations in FY 2003 by various factors, such as the respondent's termination of its services before the completion of the audit for FY 2003.

(d) The respondent had been contributorily negligent in failing to put in place internal controls to prevent or detect Ang's cash misappropriations.

14 Both parties adduced expert evidence in support of their case. The respondent's expert, Tay Swee Sze ("Tay"), took the view, *inter alia*, that the appellant had fallen below the standards of reasonably competent auditors and had failed to discover the irregularities, thereby causing the respondent to sustain losses. Tay opined that the appellant's failure to inquire into the whereabouts of the "uncredited lodgments" as well as its failure to perform a cash count and roll-back amounted to a breach of duty. Tay also suggested that the appellant had been negligent in its failure to inquire into the circumstances surrounding the long list of reconciling items and the reasons why cash sales had not been regularly banked into the respondent's bank account in accordance with the respondent's banking policy. Unsurprisingly, the appellant's expert, Seow Teng Peng ("Seow"), took a diametrically opposed view and sought to downplay the appellant's role as an auditor. To this end, Seow averred that the respondent's directors were expected to have included the review of monthly bank reconciliations as part of their responsibilities and should be equipped with the knowledge and expertise to detect any irregularities therein.

The High Court's decision

15 The trial judge first set out and examined the applicable principles in relation to the nature and scope of an auditor's duty, before coming to the view that the appellant had been negligent in the discharge of its duties. She noted (GD at [11]) that where the conduct of an auditor was called into question, the court had to ultimately decide on the legal duty of auditors and what an auditor was required to do in order to discharge his duty of reasonable skill and care. While different auditors could have responded divergently, the trial judge held that the court ultimately had to decide whether an actual breach of duty had been made out on the facts. The duty imposed on the auditor could not exceed the task undertaken, and the actual nature of damage suffered was relevant to the existence and extent of any duty to avoid or prevent it (see GD at [12]–[13]). Taken as a whole, this meant that where breach of a duty of care was alleged, the party making the allegation had to satisfy a two-fold requirement of showing that a duty was owed to him and that it was a duty in respect of the kind of loss which he had sustained.

16 The trial judge went on to observe that whilst an auditor was not expected to be a detective, the duty to audit carried with it an incidental duty to warn the appropriate level of management or the company's directors of fraud or irregularities discovered during the course of the audit. A breach of the duty would have occurred if, in the course of the audit, the auditor uncovered matters which reasonably required him to take further steps that would have uncovered or led to him uncovering the fraud and he omitted to take such further steps (see GD at [27]). The onus was on the plaintiff to show that the defendant's act or omission had caused it loss (see GD at [17]).

17 In relation to the first issue of whether the appellant had been negligent in relation to the audits for FYs 2001 and 2002, the trial judge found in favour of the appellant. Ang's misappropriations had been made good by her practice of teeming and lading in FYs 2001 and 2002, such that the respondent could not be said to have suffered any loss from the cash misappropriations during this

period. In her view, the respondent's inability to show damage (or loss) proved fatal to its claim (see GD at [18]). One further obstacle stood in the way of the respondent's claim – the respondent had not adduced evidence showing a real possibility that it would have recovered the cash misappropriated by Ang in any event (see GD at [21]). She thus dismissed the respondent's claim for losses in FYs 2001 and 2002.

18 However, the trial judge went on to hold the appellant liable for a breach of duty which, in her view, had occurred at the latest by 10 March 2004. She opined that on 9 March 2004, when Phong had seen the bank reconciliation statement ("BRS") for December 2003 ("the December 2003 BRS") indicating substantial unlodged cash deposits of $672,253.94, he should have been put on inquiry (see GD at [28]–[29]). Phong had reacted inadequately by merely waiting for the bank statement and requesting that the respondent's employees provide information relating to the subsequent clearance dates. Instead, Phong ought to have investigated the irregularity immediately (see GD at [29]), and this would in turn have divulged a "pattern of continuing and unabated increase in the amount of 'unlodged cash deposits'" that would have led him to conclude that "something serious was amiss" (see GD at [36]). In failing to review the monthly BRSs throughout 2003, Phong had failed to discharge his duty of care, thereby preventing the respondent from confronting Ang earlier and avoiding the financial detriment which it suffered in 2004.

19 However, the trial judge declined to apportion the 2004 losses from 10 March 2004 onwards. She reasoned in her GD at [37] that:

> … Phong was aware from the previous audits that there would be cash sales which [were] not deposited in the bank as at 31 December and he ought to have informed Tow of the position so that a cash count of the "unlodged cash deposits" could be carried out on 2 January 2004.

Instead, the appellant would be held liable for $775,266.02, being the entire 2004 losses. This figure was arrived at on the basis that the total losses amounted to $884,195.02, this being the amount that the police had charged Ang with having misappropriated from 16 February 2004 to 23 May 2004 and for which she had been convicted, less the sum of $100,000 recovered from the respondent's insurers as well as the $8,929 recovered from Ang.

20 The trial judge also opined that the respondent had been guilty of contributory negligence as far as FY 2003 was concerned. The respondent would thus be precluded from recovery in relation to the 2003 losses (see GD at [38]).

21 However, she held that the respondent's contributorily negligent conduct did not extend to FY 2004, when major management changes had occurred and the evidence was equivocal as to whether Crowhurst had continued to receive the monthly BRSs after he ceased to be involved in the day-to-day operations of the respondent (see GD at [39]).

22 The appellant appealed against the entirety of the trial judge's decision, and challenged her holdings in several material respects. More specifically, the appellant disputed the existence of a duty to detect fraud and a breach thereof. The appellant also took issue with her finding that causation had been made out. In any event, the appellant contended that its liability should be reduced in the light of contributory negligence on the respondent's part.

23 The present appeal thus raises five broad issues, namely:

(a) whether the appellant owed a duty to detect fraud;

(b) whether the appellant had breached its duty in the performance of the audit;

(c) whether this breach, if any, had caused the respondent's loss;

(d) the appropriate quantum of damages which the respondent was entitled to; and

(e) whether the respondent had been contributorily negligent.

Whether the appellant owed a duty to detect fraud

24 In its submissions, the appellant strenuously asserted that the trial judge had erred in finding that the appellant owed a duty of care to the respondent to detect fraud or error. While the appellant conceded that a duty of care existed between itself and the respondent, the appellant submitted that this duty did not extend to the detection of fraud or error in the accounts.

25 The appellant contended that the ambit of its duty should be defined and limited by the terms of its engagement and the disclaimer included therein. The salient portions of the engagement letter dated 22 August 2001 ("engagement letter") read:

> Because of the test nature and other inherent limitations of an audit, together with the inherent limitations of any system of internal control, there is an unavoidable risk that even some material misstatement may remain undiscovered. Accordingly, *our audit should not be relied on to disclose fraud, defalcations or other irregularities*.
>
> *The Companies Act provided [sic] that the responsibility for the preparation of accounts including adequate disclosure is that of the directors*. This includes the maintenance of adequate accounting records and internal controls, the selection and application of accounting policies, and the safeguarding of the assets of the Company. As part of our audit process, we will request from the directors written confirmation concerning representations made to us in connection with the audit.
>
> [emphasis added]

26 More significantly, in the course of oral arguments, counsel for the appellant, Mr Ang Cheng Hock ("Mr Ang"), sought to highlight that the imposition of such a duty would impose unjustifiably onerous obligations on statutory auditors, who were not expected to conduct an audit with the conscientiousness of a forensic accountant and perform a complete audit of each and every transaction. Mr Ang relied heavily on precedents such as *In re Kingston Cotton Mill Company (No 2)* [1896] 2 Ch 279 at 288 for the proposition that an auditor was "not bound to be a detective" or "to approach his work with suspicion or with a foregone conclusion that there [was] something wrong". While an auditor performed a watchdog function, he was not required to be a "bloodhound".

27 Mr Ang also placed considerable emphasis on four factors which allegedly precluded the appellant's duty to detect fraud:

(a) the appellant's engagement as a statutory auditor, rather than as a forensic accountant specially tasked to investigate suspected fraud;

(b) the satisfactory findings of the previous audits for FYs 2001 and 2002, which entitled the appellant to repose a degree of trust in the accuracy of the respondent's accounts;

(c) the low quantum of fees charged by the appellant for the audit; and

(d) the fact that there had essentially been no distinction between the ownership and the management of the respondent.

28 Counsel for the respondent, Mr Philip Fong ("Mr Fong"), on the other hand strenuously contended that the appellant was nevertheless duty-bound to reasonably detect fraud. Mr Fong submitted that the limitation clause was ineffective to preclude the appellant's liability in tort, and disputed the four factors cited by the appellant in support of its case.

29 We reject the appellant's arguments on the duty point. The appellant has mistakenly perceived its role as a statutory auditor to be a perfunctory one, rather than that of a reasonably competent auditor exercising the requisite skill and responsibility coupled with a healthy and reasonable dose of professional scepticism. While a plain reading of the purported disclaimer appeared to exclude the appellant from liability in the event that fraud was not detected during an audit, it was not open to the appellant to seek to exclude or limit its liability in relation to the respondent for negligence or any other breaches of duty in this manner. A similar clause was examined in *Dairy Containers Ltd v NZI Bank Ltd* [1995] 2 NZLR 30 ("*Dairy Containers*") at 53, where the terms of engagement expressly stated that the audit "should not be relied upon to disclose defalcations or other irregularities, but their disclosure, if they exist, may result from the audit tests undertaken". The court held that this provision did no more than confirm the position relating to the detection of such fraud and irregularities as was prescribed by the relevant professional accounting standards, and was thus insufficient to restrict the auditor's liability (at 53). In other words, the limitation clause merely restated the degree of skill and care that was required of an auditor under the accepted professional accounting standards. It bears mention that the Singapore Standard on Auditing ("SSA") 11 and SSA 240 specifically provide that an auditor must "consider the risk of material misstatements in the financial statements resulting from fraud or error" when planning and performing audit procedures. As such, the appellant would not and should not be exempted from its duty to detect the existence of fraud and error.

30 In any case, the insertion of the subject disclaimer did not confer upon the appellant free rein to limit its liability. The dictates of both principle and precedent make it clear that the terms of the appellant's engagement do not constitute the sole determinant of the scope of duties undertaken by the appellant in the performance of its duties. It is beyond peradventure that the appellant remains under an implied duty to exercise reasonable care and skill in the course of the audit even though this is not explicitly stated in the terms of its engagement: *Jackson & Powell on Professional Liability* (Sweet & Maxwell, 6th Ed, 2007) ("*Jackson & Powell*") at para 17-022. Put simply, the appellant would nevertheless remain liable for negligence should it be determined that a reasonable auditor exercising reasonable care and skill would have detected the fraud. We would also underscore that a wholly contractual analysis of the appellant's duties would be overly simplistic and inconsistent with the principles espoused in case law. In *JSI Shipping (S) Pte Ltd v Teofoongwonglcloong* [2007] SGCA 40 ("*JSI Shipping*") at [32] and [35], we observed that a multitude of factors come into play when assessing the nature and extent of an auditor's professional duties:

> As a starting point, it would be apposite to identify the sources from which we can glean the appropriate standard of care expected of an auditor. In this regard, it is helpful to refer to the seminal case of [*Dairy Containers*] at 54 which, in our view, quite correctly assimilated the requisite standard of care from: (a) the standard required as a matter of contract and under the relevant statutes or regulations; (b) expert evidence relating to the conduct of the audit; and (c) the relevant auditing standards set by the governing professional body: see *Jackson & Powell on Professional Liability* (Sweet & Maxwell, 6th Ed, 2007) ("*Jackson & Powell*") at para 17-050. *In*

short, it is an amalgam of considerations that almost invariably permutate and should, therefore, be specifically assessed in accordance with each factual matrix.

…

The nature and extent of an auditor's professional obligations in any given matrix is, therefore, to be assessed by a composite review of the precise contractual obligations undertaken, the duties imposed by statute, the auditing standards reflected in the SSAs and the expert evidence adduced in relation to the conduct of the audit. The multiplicity of criteria is an inevitable function of the dynamic interface between the various interpretative processes which interact in an audit. There is no single all-embracing rule or criterion that consistently or exclusively predominates.

[emphasis added]

31 In the circumstances, we would emphasise that a court will be extremely slow in sanctioning an auditor's attempts to wholly exclude liability for professional negligence.

32 More importantly, we are also not persuaded that the various factors cited by Mr Ang exonerated the appellant from its duty to detect fraud. Mr Ang's submissions, if accepted, would effectively entirely denude the established duties owed by a statutory auditor in the performance of an audit of any meaningful content. We are unable to accept these contentions as they represent an unjustified departure from established precedents and practice.

33 The mere fact that the appellant had been engaged purely as a statutory auditor did not *ipso facto* preclude the existence of a duty to unmask or prevent fraud. The observations of Moffitt J in *Pacific Acceptance Corporation Ltd v Forsyth* [1970] 92 WN (NSW) 29 ("*Pacific Acceptance*") at 63–64 are apposite in this regard:

To date I have considered the duty of an auditor where he discovers matters which in the first instance, or eventually, lead him to suspect fraud. *A somewhat different question arises as to the place, if any, the possibility of fraud plays in a "statutory audit"*. There was a considerable debate on this matter. The defendants' approach was not altogether clear but was inclined to deny its existence in a "statutory audit", then [*sic*] rather to concede it, but approach it as minor or insignificant. *However, it is clear that in planning and carrying out his work an auditor must pay due regard to the possibility of error or fraud. Once it is accepted that the auditor's duty requires him to go behind the books and determine the true financial position of the company and so to examine the accord or otherwise of the financial position of the company, the books and the balance sheet, it follows that the possible causes to the contrary, namely error, fraud or unsound accounting, are the auditor's concern.*

The matter cannot be dismissed by reference to the well-known dicta regarding suspicion and metaphors concerning dogs and detectives, for such are rather directed to the auditor's state of mind and do not suggest that a careful auditor, without suspicion in his mind but doing his duty, will pay no heed to the reality that there is always a material possibility that human frailty may lead to error or fraud in the financial dealings of any organi[s]ation. … [F]or an auditor to plan his programme and perform his audit work so as to take some account of the possibility of fraud, in the sense that if fraud exists there are reasonable prospects of it being revealed, is not to say that an auditor should start his work with suspicion in his mind. …

The duty to pay due regard to the possibility of fraud has been recogni[s]ed by the courts and

by the auditing profession and by the very nature of some of their procedures – for example, the surprise nature in an unannounced cash count. It would be wrong to suppose such recognition to be confined to special audits and to exclude statutory audits which occupy so large a part of audit assignments.

[emphasis added]

34 Admittedly, the scope of a statutory audit is comparatively limited in comparison to a forensic audit. A statutory auditor need only comply with less onerous obligations, and may use samples on a test basis instead of performing a 100% audit of all transactions. This is not to suggest, however, that a statutory auditor is entitled to take a casual view of his functions. The authorities have overwhelmingly affirmed that a statutory auditor remains obliged to remain alive to the possibility of fraud being committed. Thus, in *In re London and General Bank (No 2)* [1895] 2 Ch 673 at 682–683, Lindley LJ opined that an auditor was duty-bound in the following terms:

> His business is to ascertain and state the true financial position of the company at the time of the audit, and his duty is confined to that. But then comes the question, How is he to ascertain that position? The answer is, By examining the books of the company. But he does not discharge this duty by doing this without inquiry and without taking any trouble to see that the books themselves shew the company's true position. He must take reasonable care to ascertain that they do so. Unless he does this his audit would be worse than an idle farce.

35 Further, in *Fomento (Sterling Area) Ltd v Selsdon Fountain Pen Co Ltd* [1958] 1 WLR 45, Lord Denning observed at 61 that:

> An auditor is not to be confined to the mechanics of checking vouchers and making arithmetical computations. He is not to be written off as a professional "adder-upper and subtractor". His vital task is to take care to see that errors are not made, be they errors of computation, or errors of omission or commission, or downright untruths. To perform his task properly he must come to it with an inquiring mind – not suspicious of dishonesty, I agree – but suspecting that someone may have made a mistake somewhere and that a check must be made to ensure that there has been none.

36 Indeed, what perhaps cripples the appellant's case is the fact that the appellant itself had expressly acknowledged its duty to detect irregularities in the respondent's accounts. The terms of its engagement letter (see [25] above) merit reproduction:

> We will conduct our audit in accordance with the Singapore Standards on Auditing (SSAs). *Those SSAs require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements*. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. [emphasis added]

37 The appellant was therefore obliged to apply its mind to how best it could prudently discharge its obligations under the SSAs. In expressing an opinion as to the accuracy of the accounts, the appellant was duty-bound to ensure that no material inaccuracies existed, in so far as such inaccuracies could have been detected on the basis of adequate sampling and the appellant having exercised reasonable care in the audit.

38 Seen in this light, the fact that the previous audits for FYs 2001 and 2002 had proven satisfactory did not, therefore, exculpate the appellant from its breach of its duty of professional scepticism by wholeheartedly reposing its trust in Ang's integrity or in the accuracy of the respondent's books. Similarly, the comparatively low remuneration received by the appellant cannot detract from the scope of its duty to ensure that the respondent's accounts were free of material misstatements. If this were the case, statutory auditors would be given *carte blanche* to discharge their functions in a wholly superficial manner, especially where they have been engaged pursuant to a long-term arrangement and/or for insubstantial remuneration.

39 The appellant had robustly contended that a less extensive duty should be imposed where the terms of the audit had been defined narrowly, and where the costs of the audit that would have been required to detect the fraud under scrutiny would have been significantly higher than the actual remuneration received for the audit that was actually performed. The appellant cited the decision by the Maritoba Court of Appeal in *International Laboratories Ltd v Dewar* [1933] 3 DLR 665 ("*Dewar*") in support of this contention. We have no hesitation in dismissing the appellant's contention on this point. The basis for the decision was succinctly highlighted by Dennistoun JA at 676, where he observed:

> To check and uncover frauds of this type is beyond the scope of auditors whose contract is for part time work in the verification of a balance sheet, with special attention to cash, notes, securities, payrolls, and bank deposits, and not a contract to make a detailed audit of every entry in the book, with a scrutiny of delivery slips, invoices (both out and in), inventories, and all other records of a large business.
>
> Such an audit would have cost many times the sum of $350 which these auditors were receiving, with occasional extra sums for special work.

40 It was on this premise that the court in *Dewar* ([39] *supra*) declined to hold the auditor liable for its failure to discover the fraud, as this would have necessitated a check of all invoices, a task which fell outside the ambit of the auditor's duties in that case. To our minds, the material facts of the present case have been shaped in an entirely different context. In the first place, the appellant's remuneration of some $4,500 to $5,000 annually was no paltry sum to be scoffed at. While the sum might not have been sufficiently large to warrant a full-fledged investigation of the respondent's accounts, it was by no means a token amount given in recognition of casual or routine services. Further, and more importantly, the appellant had been expressly engaged to perform a statutory audit and to ensure that no inaccuracies existed in so far as such inaccuracies could have been detected on the basis of sampling and the appellant exercising reasonable care in the audit. More specifically, the appellant was duty-bound to detect material misstatements arising from fraud, defalcations or other irregularities in the respondent's accounts. In our view, Ang's misappropriations fell squarely within the ambit of the appellant's terms of reference. As the later portion of our judgment will show, the appellant had been conspicuously derelict in the discharge of its duties and could not possibly be said to have exercised reasonable care.

41 Moreover, as the respondent rightly pointed out, if it had been necessary for the appellant to undertake procedures that were not originally anticipated, it was open to the appellant to negotiate for an increase of its fees. The appellant should not be entitled, in the circumstances of this case, to water down its responsibilities by claiming that it had not been paid enough to perform the necessary work. Indeed, it would be wholly untenable from the viewpoint of policy and market discipline if the appellant were to be held to a lower standard simply on the basis that it had not been remunerated sufficiently for its services.

42 Likewise, the appellant's contention that a less extensive duty should be imposed on auditors where the shareholders and the directors of a company are identical must be carefully assessed. Admittedly, a persuasive case may be made for the imposition of a less extensive duty where there is a fortuitous confluence of identity between the shareholders and the directors of the company being audited. This becomes evident when we consider the underlying rationale for the statutory audit. In this respect, reference may usefully be made to the incisive comments articulated by the editors of *Jackson & Powell* ([30] *supra*) at para 17-002:

> … Ownership by the shareholders is separated from management and day-to-day control by the directors. The latter are accountable for the conduct of the company's affairs to the shareholders who may exercise their collective powers to reward, appoint or remove the directors. To that end, shareholders are entitled to an annual report from the directors as to their conduct of the company's affairs. Shareholders are also entitled to a report from independent auditors in order to ensure, so far as possible, that financial information as to the company's affairs prepared by the directors accurately reflects the company's position.

43 Since a statutory audit serves to apprise shareholders of the company's affairs, a pragmatic and more flexible approach may be justified where a congruence of identity exists. Under such circumstances, the shareholders would be fully aware of the company's affairs and the statutory audit may, in certain exceptional circumstances, be a mere formality.

44 The possibility of adopting a more flexible approach in these circumstances has also been adverted to in *Halsbury's Laws of Singapore* vol 6 (Lexis Nexis, 2006 Reissue) at para 70.331:

> **Significance of the auditor's function**
>
> In order to understand the true significance of the auditors' functions, it is necessary to appreciate the practical distinction between the owners of the company on the one hand and the management and directors on the other. In very small companies, the owners of the company (namely, the members) are also usually the directors. They run the company and are responsible for its business. The statutory audit becomes a formality under these circumstances, since the owners are fully aware of what is going on.

45 We would, however, be loath to make a definitive pronouncement in relation to this for the purposes of the present appeal, given that the requisite congruence of identity has not been made out. While Crowhurst, Lew and Shaw held concurrent appointments as directors and shareholders of the respondent, we note that Crowhurst's and Lew's wives also owned shares in the respondent as well.

46 Before us, Mr Ang made much of the allegedly far-reaching consequences that would arise if a duty to detect fraud were imposed on statutory auditors. Among other submissions, he contended that if an overly onerous standard was imposed on statutory auditors, this would lead to an increase in audit fees, insurance premiums and the costs of business. With respect, this concern does not bear scrutiny.

47 In our considered view, we are not holding statutory auditors to an unrealistically extensive scope of duties by finding the existence of a duty to detect and prevent reasonably apparent types of fraud. We would preface our findings by pointing out that we have adopted a measured response in finding liability on the facts before us by only holding the appellant liable for breaches arising in 2004 (and not 2002 and 2003). More significantly, we emphasise that the benchmark against which an auditor is held is that of reasonable care and skill. It is not contemplated that an auditor must detect

each and every material misstatement or instance of fraud in the discharge of his duties. We observed in *JSI Shipping* ([30] *supra*) at [47] that:

> Stripped of all verbiage, it can be said that the demarcation of the boundaries of professional liability remains the judicially determined standard of reasonable care. In other words, the auditor must exercise the reasonable care and skill of an ordinary skilled person embarking on the same engagement. His duty is not to provide a warranty that the company's accounts are substantially accurate, but to take reasonable care to ascertain that they are so. The precise degree of scrutiny and investigative effort which constitutes reasonable care is to be determined on the facts of each individual case.

48 In finding an affirmative duty on the part of a statutory auditor to detect and prevent readily apparent and/or easily detectable types of fraud, we are not suggesting that a statutory auditor must undertake a full-fledged inquiry into the veracity of the accounts in all cases. Rather, the onus is on him to perform his duties with an attitude of professional scepticism (SSA 1 at para 6), and remain alive to the possibility of fraud. The auditor is not simply a professional mathematician computing data. He must approach his task with an inquiring mind and remain constantly alert to the fact that a mistake or oversight could actually be the thin end of a wedge. An auditor would thus be obliged to pursue the matter and make further inquiries where reasonable suspicion would typically have been excited. Indeed, in *Clerk and Lindsell on Torts* (Sweet & Maxwell, 19th Ed, 2006) at para 10-189, it is observed that:

> [I]n general, an auditor must "make a reasonable and proper investigation of accounts and stock sheets, and if a reasonably prudent man would have concluded on that investigation that there was something wrong call his employer's attention to that fact". He is not obliged, however, to "draw the accounts, not to turn every stone and open every cupboard". He is of course not liable for failing to find irregularities that would not have been found by a reasonably competent auditor.

49 The SSAs also recognise the existence of practical limitations and constraints faced in a statutory audit. For instance, SSA 1 expressly acknowledges (at para 9) the existence of inherent limitations in an audit which impinge upon an auditor's ability to detect material misstatements such as: (a) the use of testing; (b) the inherent limitations of any accounting and internal control system; and (c) the fact that most audit evidence is persuasive rather than conclusive. Sufficient leeway is thus given to statutory auditors in the discharge of their duties to verify financial statements.

50 To summarise, we are satisfied that statutory auditors have a duty to be alive to the possible existence of fraud. In our considered view, the appellant's contention that the imposition of a duty would be unsustainable in policy terms and out of step with the realities of the audit process is misconceived. As observed by this court in *JSI Shipping* ([30] *supra*) at [120], the imposition of a duty conduces towards market discipline and serves as a sound exhortation and salutary reminder to the profession of its imperative duty to discharge its obligations with reasonable care:

> It is of singular importance to reiterate that statutory auditors, on whom shareholders are dependent for their skill, judgment and vigilance, should perform their duty with scrupulous care. The potential recourse to a negligence action reassures the public that professionals who hold themselves out as possessing a particular skill will not lightly breach the requisite standard of care expected of them. It is another measure through which discipline is imposed on the profession. Market confidence that errant professionals can be brought to book is an important feature of a mature financial centre.

Whether the appellant had breached its duty to exercise reasonable care

51 Before delving into the facts and assessing whether the appellant had breached its duty of care, two guiding principles ought to be borne in mind.

52 First, the standard which an auditor is held up to is that of reasonable care. An auditor is not expected to be an omniscient capable of detecting every single material misstatement and/or every instance of fraud; neither is an auditor required to take a wholly sceptical view as to the veracity of the account, and make further inquiries in all cases regardless of whether suspicious circumstances exist. Instead, case law has recognised the need to strike a balance between an auditor's duty to detect fraud and the impossibility of doing so in all cases. This is encapsulated in the common law test which holds that an auditor would have discharged his duty by exercising the reasonable skill and care of an ordinary skilled person performing the same engagement: *Jackson & Powell* ([30] *supra*) at para 17-049. The penetrating comments of Lindley LJ in *In re London and General Bank (No 2)* ([34] *supra*) at 683 are apposite in this respect:

> Such I take to be the duty of the auditor: he must be honest – i.e., he must not certify what he does not believe to be true, and *he must take reasonable care and skill before he believes that what he certifies is true. What is reasonable care in any particular case must depend upon the circumstances of that case*. Where there is nothing to excite suspicion very little inquiry will be reasonably sufficient, and in practice I believe business men select a few cases at haphazard, see that they are right, and assume that others like them are correct also. Where suspicion is aroused more care is obviously necessary; but, still, an auditor is not bound to exercise more than reasonable care and skill, even in a case of suspicion, and he is perfectly justified in acting on the opinion of an expert where special knowledge is required. [emphasis added]

53 The SSAs similarly reiterate that an auditor is expected to take a balanced approach when performing an audit. SSA 11 and SSA 240 provide that an auditor should plan and perform the audit with "an attitude of professional scepticism". Put another way, an auditor would not be expected to wholly obliterate audit risk in the discharge of his duties. Rather, what the law mandates is for him to minimise audit risk to an acceptable level by obtaining reasonable assurance of the matters which ought to be verified.

54 Second, in evaluating whether there is an irregularity which would have put the auditor in question on inquiry, the court should guard against using its *ex post facto* knowledge of the existence of fraud to impute on the auditor a level of inquiry that would have been unreasonable in the circumstances. The court should refrain from assessing the situation with the benefit of hindsight, and should instead place itself in the shoes of a reasonably skilled auditor at the time the audit was conducted.

55 The cautionary words of Moffitt J in *Pacific Acceptance* ([33] *supra*) at 62–63 are especially pertinent in this respect:

> Once fraud is revealed and has been investigated it is easy to connect earlier manifestations of it. The natural inclination after the event to do so is apt to mislead. Therefore, if the conduct of the auditor is reviewed after the event and at the same time as the fraud demonstrated, as happens of necessity in a case such as this, *the inclination must be consciously guarded against*. The auditors' conduct must be examined in a practical way upon the matters as they then presented themselves to them, with at least an initially unsuspicious state of mind, or as they ought to have presented themselves to them in such a state of mind. … *[I]t would be unreasonable to expect [the auditor] to connect matters in the fashion that one would expect*

as on a special investigation or by one whose suspicions have already been aroused. [emphasis added]

56 We endorsed this approach in *JSI Shipping* ([30] *supra*) at [69], and noted:

> At this juncture, it is also necessary to reiterate that a court must always guard against the "scapegoat effect" that often magnifies *ex post facto* and makes plausible culpability by employing the spectacles of hindsight. It is almost intuitive for a third party observer, after the occurrence of an unhappy event, to conclude that procedures could or should have been adopted to obviate the subsequently known risks. On the other hand, an auditor looking at the matter as it presented itself at the material time would usually quite naturally conclude that he or she was acting reasonably. It is crucial, in the interests of justice, that the standard of reasonable care be objectively assessed on the basis of knowledge then reasonably available as well as measures that could have been reasonably adopted at the material time. The acid test is certainly not one of retrospective plausibility.

57 Thus viewed, these two guiding principles allow generous leeway to auditors in the discharge of their duties, and avoid the imposition of unrealistically harsh and onerous standards. Despite this, an assessment of the facts discloses that the appellant fell far short of the standard reasonably expected of an auditor in its position.

58 At the outset, we would state that Phong had fallen short of the minimum standards of competence that could legitimately be expected from a reasonably competent auditor through his failure to respond and make further inquiries in relation to the December 2003 BRS ([18] above). On its face, the December 2003 BRS glaringly revealed a sum of $672,253.94 in unlodged cash deposits. It was a red flag, significance of which entirely escaped his attention. However, we do not agree with the trial judge that the breach itself had occurred on 10 March 2004, a day after Phong first had sight of the December 2003 BRS. Instead, we are of the view that the breach occurred only a week after Phong's receipt of the December 2003 BRS (*ie*, on 17 March 2004). Some leeway must be given for Phong to reflect on and evaluate his options for verification, and thereafter respond appropriately to Ang's failure to provide the necessary documentary comfort.

59 We pause at this juncture to observe that there has been some disagreement between the parties about the date on which Phong had received the December 2003 BRS. At the hearing, Mr Fong averred that Phong had been provided with a faxed copy of the document in February 2004 before he visited the appellant's office to perform the audit on 9 March 2004. Given that the respondent was unable to provide any objective evidence (such as a fax transmission) in support of its claim, we are not minded to disturb the trial judge's finding that Phong had only received the December 2003 BRS on 9 March 2004 (GD at [28]).

60 It is our view that the appellant had failed to exercise reasonable care in the performance of its audit duties in at least two material respects.

Failure to understand the respondent's BRS

61 Much of the parties' arguments centred around the meaning of the term "uncredited lodgments" as they appeared in the respondent's accounts. As the trial judge correctly pointed out (see GD at [8]), the term in the present factual matrix is open to two plausible interpretations:

(a) cash sales already deposited into the respondent's bank account but which had not been shown as credited (this first view was taken by Crowhurst and Tow); or

(b) cash sales not yet deposited into the respondent's bank account (this second view was taken by Seah and Phong).

62 In its submissions, the respondent alleged that Tow had misunderstood its BRS or the bank reconciliation exercise, and had thereby failed to show a reasonable degree of competence in the discharge of his duties. Mr Fong urged us to adopt the view that the term "uncredited lodgments" referred to cash sales which had not been deposited into the respondent's bank account.

63 In our view, the meaning to be attributed to the term "uncredited lodgments" is wholly immaterial for the purposes of ascertaining whether a breach had occurred. The appellant had acted in dereliction of its duties, regardless of which meaning is attributed to the term.

64 Tow would be in breach of his duty even on his own understanding of the term "uncredited lodgments" (*ie*, the first view). Tow had opined that the cash sales items ("CFS items") listed under the "uncredited lodgments" in the respondent's BRS referred to cash sales which had been deposited in its bank account at the close of each year. Tow had acknowledged his understanding that cash deposited into the bank would have cleared within a day. However, the facts disclosed a significant time lag of some 11 to 21 days before the CFS items were cleared. This delay in clearance was plainly anomalous or unusual even on Tow's own evidence. Tow had obviously been aware of the lengthy delays in this respect, as he had reviewed the BRS with Phong's handwritten annotations on the dates of clearance of the CFS items and had initialled the bottom of the BRS for FYs 2001 and 2002. However, Tow did not see fit to raise this matter with the respondent. In our view, this omission on Tow's part demonstrated that he had clearly failed to exercise the requisite standard of reasonable care expected of him as an auditor. A competent auditor would have promptly requested the respondent's monthly BRS for January and February 2004 to determine whether the cash had indeed been deposited subsequently and written to the respondent to express its concerns about the large amount of "uncredited lodgments".

65 Phong would likewise be in breach of his duty even if the second view was adopted. As the trial judge rightly pointed out, Phong was put on inquiry by the December 2003 BRS, as this clearly disclosed a substantial increase in unlodged cash deposits in comparison to those in previous years (see [70] below). By failing to inquire further into the reasons for this substantial increase, Phong had failed to exercise the reasonable amount of care and skill expected of someone with his experience and qualification. This is apparent when we consider the context in which Phong had received the December 2003 BRS.

Failure to reasonably suspect existence of fraud

66 The appellant was incontrovertibly in breach of its duty when it failed to detect Ang's misappropriations. While an auditor is not expected to make further inquiries in all cases, the precedents have established that an auditor's duty to inquire is triggered upon a reasonable suspicion of the possible occurrence of an irregularity or fraud. In *Sasea Finance Ltd v KPMG* [2000] 1 All ER 676, the court, citing "*Auditing Guidelines*" (February 1990 Ed) published by the Institute of Chartered Accountants, noted at 681 that:

> If during the course of his work the auditor identifies the *possible existence* of a fraud, other irregularity or error the following action should be taken. The auditor should endeavour to clarify whether a fraud, other irregularity or error has occurred … unless fraud by senior management is suspected, the auditor should inform senior management of his suspicions. [emphasis added]

67 Similarly, in *Pacific Acceptance* ([33] *supra*) at 53–54, Moffitt J held that a breach of duty

would arise if the auditors uncovered matters which "reasonably required them to take further steps, which they did not take and which would have uncovered or led them to the uncovering of … fraudulent and irregular dealings".

68 The terms of the SSAs also confirm this and in effect impose a duty upon auditors to inquire further where there exists a reasonable suspicion as to the possibility of fraud. SSA 11 and SSA 240 specify that an auditor must make additional queries and highlight the matter to the management of the company being audited where he suspects that fraud *may* exist [emphasis added].

69 The duty to inquire is plainly not confined to cases where fraud has been visibly proved. Rather, the touchstone is whether the possibility of fraud can be reasonably suspected on the facts. In our view, Phong had failed to discharge his duty in this respect. We concur with the trial judge's views that Phong had been placed on inquiry by the substantial increase in "uncredited lodgments" in the December 2003 BRS, and that his omission to make further inquiries and ascertain the reasons for such increase constituted a plain dereliction of his duties.

70 It would suffice to highlight three particular features of the present case which, taken together, ought to have given rise to reasonable suspicion on the appellant's part. First, the appellant should have noticed that the "uncredited lodgments" in the December 2003 BRS were $672,253.94, which represented a significant and almost three-fold increase from the figures of $148,111.45 and $160,846.78 in the BRS as at 31 December 2001 and 31 December 2002 respectively. These figures would most certainly have been known to the appellant, given that it had performed an audit for the respondent in 2001 and 2002.

71 This significant aberration in the amount of "uncredited lodgments" for 2003 would have been even more apparent had the trial judge found as a fact that Phong had taken the view that "uncredited lodgments" referred to cash sales that had not been deposited into the respondent's bank account. Based on Phong's understanding of this term (see [61] above), the December 2003 BRS would necessarily have meant that a sum of $672,253.94 remained on the respondent's premises during the material period. However, there were no plausible reasons for the respondent's decision to leave such a substantial amount of cash on its premises; neither could the appellant offer any proper justification for such a course of action. In fact, it would have been nothing short of foolhardy for the respondent to leave substantial amounts of cash on its premises, especially since it would have been far safer for the cash to be deposited at the bank instead. The (supposed) retention of large amounts of cash on the respondent's premises ought to have precipitated, at the very least, a reasonable suspicion on the appellant's part.

72 A second disturbing feature of the established facts is this: Given that the respondent banked in its cash sales twice weekly, there should only have been a maximum of four days' worth of sales which remained undeposited at any point in time. In other words, there should have been a maximum of only four CFS items in the December 2003 BRS. In truth however, the $672,253.94 of "uncredited lodgments" comprised 68 CFS items. This could not have been a mere oversight. Surely, it ought to have warranted a reasonable suspicion that something was amiss. The appellant, however, appeared blissfully oblivious to the prospect of any impropriety.

73 Finally, the unusually large total amount of "uncredited lodgments" and delay in the banking in of cash sales was a basic tell-tale sign of either the breakdown of appropriate financial controls or, indeed, something even more serious, *viz*, fraud. As the trial judge rightly pointed out, it was basic accounting knowledge that these features would reasonably lead to an inference of teeming and lading (see GD at [32]). We would also highlight that the sum of $672,253.94 constituted some 30% of the respondent's costs of sales on an annual basis ($1,740,315 in FY 2001 and $1,679,212 in

FY 2002), and more than 10% of the respondent's annual turnover in previous years ($5,359,693 in FY 2001 and $5,445,374 in FY 2002). The accounts thus revealed that a significant proportion of the respondent's annual turnover and costs of sales were made up of "uncredited lodgments". In our opinion, this was odd, to say the least, and ought to have promptly placed the appellant on notice as to the existence of potential irregularities in the accounts.

74 The presence of all these tell-tale signs mean that it is not open to the appellant to contend that it could not have reasonably suspected the existence of irregularities in the respondent's accounts. We have emphasised these three features for the purpose of showing that the appellant had failed to detect the systematic and persistent nature of the fraud perpetuated by Ang, which could have been uncovered by a reasonably competent auditor endowed with a healthy and reasonable dose of professional scepticism. If we were dealing with a small number of cunningly designed and carefully concealed frauds, the appellant might be given leeway to allege that it was not employed as a bloodhound or detective to discover unusual crimes when there was nothing to arouse its suspicion. But, when we have this catalogue of suspicious features which the appellant was fully aware of, it is an insufficient answer for the appellant to say that it knew and suspected nothing. Connecting the dots together required only a mild application of professional scepticism. While the appellant had been accustomed to accept the existence of smaller amounts of "uncredited lodgments" previously, it was not open to it to take a similarly indolent view subsequently when the December 2003 BRS indicated a startling increase in "uncredited lodgments" for no apparent reason. The appellant was thus well aware of the fact that anomalies existed in the respondent's accounts and that Ang had extensive control over the respondent's monies.

75 We were also unable to accept Mr Ang's attempts to downplay the significance of $672,253.94 in "uncredited lodgments". In his submissions, Mr Ang repeatedly asserted that the mere increase in "uncredited lodgments" was inconclusive, as such an increase could be attributed to several innocuous factors such as delays in banking and unusual sales volumes in the month of December. Mr Ang placed considerable weight on the fact that the respondent was a small set-up, and contended that delays in banking in cash were typical as far as the respondent was concerned, especially when its staff went on leave.

76 We found these arguments unpersuasive. In our considered view, the fact that the respondent was a small outfit was, in the final analysis, a neutral consideration. It could equally be argued that the respondent's small size made the circumstances more conducive for the appellant to raise its concerns directly with the respondent's management and make further inquiries as to a possible irregularity in the accounts. Moreover, the circumstances of the present case were such that it was not open to the appellant to claim that a substantial increase in "uncredited lodgments" would not prove to be a cause for concern. The appellant was fully conversant with the cash-intensive nature of the respondent's business, and had documented this aspect of the respondent's business in its general risk assessment of 2002. In fact, it bears emphasis that the appellant had identified cash as a major risk area at least twice during its tenure with the respondent – once during the general risk assessment of 2002, and again in its detailed general risk assessment of the same year, where the appellant noted the existence of a large number of assets which might be susceptible to loss or misappropriation. Indeed, we ought also to observe that the cash-intensive nature of the respondent's business was the only aspect of the business which the appellant had classified as being highly susceptible to fraud or error, among a multitude of factors which had been considered during the detailed general risk assessment. The appellant was also aware of the respondent's avowed policy of banking in cash deposits twice a week. In the system overview of 2002, which had been conducted to ascertain the respondent's system of recording and processing transactions as well as to assess its adequacy as a basis for the preparation of financial statements, the appellant noted:

6 Cash payment system

Advise staff collecting cash sales receipts and POS payment from previous day, follow cash to POS. … *Cash banked in at least 2 times a week*. [emphasis added]

77 Consequently, the appellant was, by its own express acknowledgement, fully mindful of the respondent's failure to adhere to its policy of banking in cash sales regularly. Despite this, the appellant took no action to promptly advise the respondent of the inherent risks in failing to ensure that the cash sales were deposited twice weekly. In our opinion, the appellant had failed to exercise the standard of care that was to be reasonably expected of it in the circumstances. We would go further to hold that the appellant's breach was made even more egregious by the appellant's actual knowledge of the weaknesses of the respondent's system, as well as the fact that the respondent had fallen prey to precisely the sort of fraud which the appellant had initially considered possible in its working papers.

78 One further observation is in order. The appellant had been plainly oblivious to the possibility of fraud on the facts. The appellant had paid scant attention to the flaws in the respondent's internal control system. While the appellant had made general reference to the respondent's failure to put in place checks of a systemic nature and to conduct spot checks on cash, the appellant had not seen fit to issue any management letters highlighting such weaknesses to the respondent. In fact, it is pertinent to note that the appellant had not even placed on record the existence of loopholes in the respondent's control systems nor expressed any concerns about the increase in "uncredited lodgments".

79 In discharging its functions the appellant appeared to have conducted itself merely as a technician verifying arithmetical accuracy rather than as a professional seeking assurance that the underlying records supported the financial statements. Having determined that the appellant had acted in breach of its duty as a statutory auditor, we now turn to consider what the appellant could reasonably have been expected to do in the circumstances.

The standard of reasonable care

80 Before us, Mr Ang repeatedly underscored that the appellant had requested for information relating to the subsequent clearance and banking in dates of the "uncredited lodgments". He submitted that such a request was part of the profession's standard procedure and that the appellant had complied with the requisite standard of care simply by making such a request.

81 At the outset, we would hold that the mere endorsement of a particular practice by an expert in the field concerned is not to be considered conclusive as to the reasonableness of that practice. We reiterate our view as expressed in *JSI Shipping* ([30] *supra*) at [50]:

> We note that the respondent [the auditor in that case] quite sensibly does not dispute the applicability and relevance of the "logical basis" requirement. It can now be confidently stated that the application of the *Bolam* test [see *Bolam v Friern Hospital Management Committee* [1957] 1 WLR 582] is necessarily subject to and qualified by Lord Browne-Wilkinson's statement in [*Bolitho v City and Hackney Health Authority* [1998] AC 232 at 241–242] ("the *Bolitho* addendum"), which, when adapted to the context of auditors, would read as follows:
>
> > [T]he court is not bound to hold that a defendant [auditor] escapes liability for negligent [auditing] just because he leads evidence from a number of [auditing] experts who are genuinely of opinion that the defendant's [audit] accorded with sound [audit] practice. …

> [T]he court has to be satisfied that the exponents of the body of opinion relied upon can demonstrate that such opinion has a logical basis. In particular in cases involving, as they often do, the weighing of risks against benefits, the judge before accepting a body of opinion as being responsible, reasonable or respectable, will need to be satisfied that, in forming their views, the experts have directed their minds to the question of comparative risks and benefits and have reached a defensible conclusion on the matter.

82 Having perused Seow's report, and applying the "*Bolam/Bolitho*" test as set out above, we are of the view that Seow's opinion as to the sufficiency of a request for subsequent clearance dates should not be accepted. An auditor's duty does not stop at the mere request for information; instead, he is expected to pursue the matter to its logical end by following up to ensure that a satisfactory response is given. It was open to the appellant to utilise alternative and non-direct methods to verify the accounts, where such methods could be justified on a cost-benefit analysis. This approach was also endorsed by Moffitt J in *Pacific Acceptance* ([33] *supra*) at 67–68 in the following terms:

> Prima facie the auditor's job is to check material matters for himself from available documents and he does not ordinarily do his job or "audit" if he merely seeks the assurance of another as to the check that the other has made or as to his views as to the effect of documents.
>
> In principle an auditor is really in no different position from any skilled inquirer. To the inquirer in any field to know by direct examination is surer proof than to believe on the hearsay of others or by inference. *The latter and second-best alternatives may well be acceptable if a direct examination is not possible or the delay, expense or effort that will be occasioned by such examination is out of proportion to the importance of the matter to be proved.*
>
> [emphasis added]

83 On the basis of the facts before us, we were not, however, prepared to go so far as the trial judge to hold that the appellant was obliged to conduct a cash count coupled with a roll-back at the first sign of a possible irregularity on 9 March 2004. In our view, such a course of conduct would have been premature at that point in time, given that there ought to have merely been a suspicion of an irregularity in the accounts and that a cash count and roll-back would have involved significantly more time and expense. This was not to suggest, however, that the appellant was entitled to sit by idly. The substantial sum in "uncredited lodgments" as well as the appellant's awareness that cash was a major audit risk for the respondent meant that further steps were promptly called for. The appellant should have requested for the monthly BRS for January and February 2004 to ascertain whether the cash was subsequently deposited and placed on record its concerns about the large amount of "uncredited lodgments" in a letter to the respondent. Further, the appellant should have gone beyond the standard request for information on subsequent clearance dates by making the necessary inquiries with the respondent's management. For instance, the appellant could have asked whether the respondent had altered its banking procedures recently, thereby explaining the substantial increase in the "uncredited lodgments", or requested that the respondent furnish the monthly BRS for the preceding months in order to discern whether the increase had been a gradual or sudden one. The more severe measure of a cash count and roll-back would only be justified had the respondent refused to provide the information requested for or if the BRSs for January and February 2004 indicated that the cash had not been subsequently deposited. While the making of a request for subsequent clearance dates was a positive first step towards the discharge of its duties, the appellant fell short in the discharge of its duties by failing to take the necessary follow-up action and pursue the matter when no response from the respondent was forthcoming within a reasonable period.

84 At this juncture, we address two arguments made by the appellant in an attempt to dilute its

duty to make further inquiries. Both these arguments are unmeritorious. The appellant first alleged that it did not possess the monthly BRS for January and February 2004 and was thus unable to check the subsequent clearance dates for the cash deposits. Second, the appellant sought to persuade us to have regard to the commercial realities of the auditor-client relationship and the possibility of irreparable damage to such relationship if the appellant attempted to raise a serious allegation of fraud on the facts.

85 With respect, the mere fact that the appellant might not have had the monthly BRS for January and February 2004 did not constitute a good excuse. It was open to the appellant to insist on having sight of these documents from the respondent in its capacity as statutory auditor, and there was no indication that the respondent would have declined to produce the same. The non-availability of the monthly BRS for the months of January and February 2004 could not exonerate the appellant from its failure to adhere to the standard of care expected of it as an auditor.

86 Similarly, the appellant's argument that the making of further inquiries would have jeopardised the parties' relationship misses the point entirely. The appellant had been appointed to perform an audit function – a serious responsibility. Put simply, the appellant was under a duty to verify the accuracy of financial information prepared by the respondent and detect errors or defalcations (if any existed). This required the appellant to exercise a reasonable degree of scrutiny in relation to the respondent's accounts, as opposed to merely rubber-stamping them.

87 While it is true that a certain degree of sensitivity and respect should be shown by auditors to the management of a company under audit, auditors are appointed to act independently of management. Accordingly, they are not entitled or obliged to adopt an overly deferential view of their role for fear of offending management. Auditors must bear in mind that they have been entrusted with the role of ensuring that a company's accounts are accurately reflected. It is thus imperative for them to perform their independent role by garnering sufficient and appropriate audit evidence and alerting management promptly upon a reasonable suspicion that something is amiss, even though this may require them to adopt a seemingly indelicate course of action (such as the making of further inquiries and requests for additional information).

88 On an overall evaluation of the circumstances, the irresistible inference is that the appellant had been woefully deficient in the discharge of its duties as a statutory auditor. The appellant, in failing to recognise from the striking facts before it that something was amiss, had failed to comply with the standard of care which could reasonably be expected of it in the circumstances.

89 The appellant should not have accepted as sufficient a request for subsequent clearance dates. Also, its acceptance of the substantial increase in "uncredited lodgments" without further investigation was, in our view, negligent. The perfunctory manner in which the appellant conducted its audit was remarkable, to say the least, given that the present facts disclosed several disturbing features which were strongly indicative of irregularities in the respondent's accounts.

90 Had the appellant exercised due care and skill in the performance of the audit, it would have initially requested that the respondent furnish subsequent clearance dates and, perhaps, performed the necessary follow-up action of a cash count and roll-back had such information not been forthcoming. We would disagree with the trial judge that the appellant's omission (and breach) occurred one day after Phong received the December 2003 BRS (*ie*, on 10 March 2004). We would hold that a reasonable time ought to be afforded to the appellant in the performance of its audit duties. It would be unrealistic to expect Phong to pursue the matter within a day of receiving the December 2003 BRS, having regard to his typical workload as a statutory auditor. We took the view that seven days would constitute a reasonable time for Seah and Ang to respond on the appellant's

inquiries (see [58]). Therefore, the appellant would have been obliged to act within a week of receiving the December 2003 BRS, and we would accordingly find that the breach occurred on 17 March 2004 when the appellant failed to make further inquiries as to the apparent irregularities in the accounts.

Whether the appellant's breach had caused the loss

91 The respondent's case is a simple one. In relation to the losses sustained in 2004, it contends that if the appellant had performed its audit duties competently, the fraud would have come to light and the respondent would have taken action against Ang for the recovery of the misappropriated monies. The appellant's negligence had deprived the respondent of the chance of such recovery, and the respondent now claims that it is entitled to be compensated for the value of that lost chance.

92 In contrast, the appellant makes a two-pronged attack in its attempt to show that causation had not been made out. First, the appellant's negligence was not the effective cause of the loss because the chain of causation had been broken by the respondent's contributory negligence, which constituted an intervening act. Second, and in any case, the respondent could not claim for the value of its lost chance to recover its losses from Ang. Given that Ang had dissipated most of the misappropriated monies, the chances of the respondent recovering anything were speculative, to say the least. The respondent's claim for loss of a chance was therefore untenable.

93 In holding the appellant liable for the 2004 losses, the trial judge appeared to have taken the view that causation had been made out.

94 The trial judge had analysed the issue of causation in terms of the "scope of duty" doctrine. This was evident from her approval (see GD at [12]–[13]) of the statements made by Lord Bridge of Harwich and Lord Oliver of Aylmerton in *Caparo Industries plc v Dickman* [1990] 2 AC 605 and Lord Hoffmann's judgment in *South Australia Asset Management Corporation v York Montague Ltd* ("*the SAAMCO case*") [1997] AC 191 at 211 that:

> Before one can consider the principle on which one should calculate the damages to which a plaintiff is entitled as compensation for loss, it is necessary to decide for what kind of loss he is entitled to compensation. A correct description of the loss for which the valuer [similarly an auditor] is liable must precede any consideration of the measure of damages. For this purpose it is better to begin at the beginning and consider the lender's cause of action.
>
> …
>
> A duty of care such as the valuer [and similarly an auditor] owes does not however exist in the abstract. A plaintiff who sues for breach of a duty imposed by the law (whether in contract or tort or under statute) must do more than prove that the defendant has failed to comply. *He must show that the duty was owed to him and that it was a duty in respect of the kind of loss which he has suffered*.
>
> [emphasis added].

95 While it was quite appropriate for the trial judge to analyse the issue of causation in terms of the scope of the duty of care, we take the view that this approach in isolation overlooked an anterior question – whether the "but for" test of causation had been made out. Indeed, the editors of *Jackson and Powell* ([30] *supra*) observe at para 17-064 that:

> The perennial problem is to establish whether one or more putative causes provide the required link in law between the duty breached and the loss claimed. *The "but for" test is necessary but not sufficient. It is an exclusionary test serving only to filter out non-causal occasions for the loss.* …
>
> In seeking the elusive ingredient which is *additional* to the "but for" test, the Courts have speaking travelled broadly speaking [*sic*] along two routes. The first is to leave it to judicial "common sense" or to speak of "effective cause" without attempting to analyse what makes a cause effective. …
>
> …
>
> Other judges, notably Lord Hoffmann, have analysed in terms of "scope of duty" the extra ingredient which goes to make up causation.
>
> [emphasis added]

96 In *Sunny Metal & Engineering Pte Ltd v Ng Khim Ming Eric* [2007] SGCA 36, we endorsed the application of the "two-step test" to determine the issue of causation. At [51]–[53], we held:

> 51 … In our view, it would conduce towards clarity to state at the outset that there are, broadly, two rather distinct inquiries, *viz*, causation and remoteness of damage.
>
> (1) Causation
>
> 5 2 ***The first broad inquiry involves causation, which, as alluded to earlier, is in turn made up of causation in fact and causation in law. Causation in fact is concerned with the question of whether the relation between the defendant's breach of duty and the claimant's damage is one of cause and effect in accordance with scientific or objective notions of physical sequence. It is concerned with establishing*** *the physical connection* ***between the defendant's wrong and the claimant's damage. The universally accepted test in this regard is the "but for" test, which we will elaborate on later****.*
>
> ***53 However, satisfying the "but for" test is by no means a sufficient condition because the all important "causation in law" test must be satisfied as well.*** The reason for this is that to adopt the "but for" test without limit would lead to absurd results. … The rationale is to prevent indeterminate liability resulting from causation in fact alone.
>
> [emphasis added in bold italics]

97 Before us, Mr Ang strenuously contended that an application of the 'but for' test would have shown that the chain of causation had been broken by the respondent's negligence, such that the appellant ought not to be held liable at all for the respondent's losses. Mr Ang underscored the trial judge's finding that Crowhurst (and hence, vicariously, the respondent) had been negligent and/or in breach of his duties as director in failing to supervise Ang. She had therefore found the respondent wholly guilty of negligence as far as FY 2003 was concerned, such that it would be precluded from recovery in relation to the 2003 losses. The respondent would have detected the fraud in 2003 had it exercised reasonable supervision over Ang and put in place a system of safeguards where its accounts were concerned. As such, Mr Ang submitted that the appellant should not be held liable for the respondent's losses simply because the appellant's negligence had not been shown to be the operative cause of the respondent's losses.

98 Mr Fong, on the other hand, contended that causation had been made out on two bases. First, Mr Fong argued that the issue of contributory negligence pertained exclusively to the measure of damages, and was irrelevant to an inquiry as to causation and whether the causal chain had been broken. Second, Mr Fong asserted that the respondent nevertheless possessed the right to sue the appellant for its breaches in 2004 as the appellant's duty as an auditor persisted throughout the period of the audit.

99 We agree with Mr Fong's submission that the "but for" test of causation had been established, albeit for somewhat different reasons. In the first place, we are not prepared to confine the role of contributory negligence solely to the quantum of damages. In our view, contributory negligence has a wider role and embrace which may extend to negate causation. It is established law that contributory negligence on the part of a plaintiff can operate to break the causal chain. We can do no better than to adopt the views expressed in *Clerk and Lindsell on Torts* ([48] *supra*) at para 2-96 that:

> When the conduct of the claimant exacerbates, or adds to the injuries, of which he complains, that conduct will generally result in a reduction of his damages on grounds of contributory negligence, or failure in his duty to mitigate damage. However it may be that the conduct of the claimant is so wholly unreasonable and/or of such overwhelming impact that that conduct eclipses the defendant's wrongdoing and constitutes a *novus actus*. His own conduct is found to be the effective cause of his injury.

100 However, the facts of this case do not fall within the four corners of the situation envisaged by the editors of *Clerk and Lindsell on Torts* ([48] *supra*). In taking this view, we are mindful of the editors' caution (at para 2-97) that the courts should not be eager to find that a claimant had acted so unreasonably as to break the chain of causation, and that only "reckless" or "deliberate" conduct would warrant a positive finding in this respect. In our considered view, the respondent's conduct, while negligent, did not amount to such a high degree of culpability so as to warrant a finding that it had acted recklessly or deliberately and thereby broken the chain of causation. We also take into consideration the context in which the editors' comments were made and the fact that such comments resonate more readily with personal injury and physical damage claims, rather than the present claim which relates to economic loss.

101 The respondent has also missed the point entirely in choosing to place emphasis on the continuing duty of the appellant as an auditor. With respect, the respondent has wrongly conflated the existence of a duty of care with the issue of causation when these are two distinct issues in analysing whether causation has been established.

102 A further clarification is in order. Both parties centred much of their submissions on the respondent's right to recover for the loss of a chance. This is misconceived. In our judgment, the loss of chance doctrine is irrelevant on the facts. This becomes evident when one considers the nature of the 2004 losses. The respondent was not claiming for *past* losses, or that the appellant's negligence had caused it to lose the chance of recovering the misappropriated sums from Ang before the sums were dissipated. Instead, the respondent was claiming for *subsequent* losses on the basis that further misappropriations could have been averted had the appellant discharged its duties. Put another way, the respondent's claim was that it would have acted to staunch its losses had the appellant detected Ang's defalcations.

103 A perusal of the facts will readily show that the "but for" test had been established in the respondent's favour. We attached particular significance to the fact that the respondent exhibited considerable resolve in promptly investigating, discovering and preventing further misappropriations

upon discovering Ang's misdeeds in May 2004. We would highlight several aspects of the respondent's conduct in this respect:

(a) At midnight on 24 May 2004, a mere four hours after first being informed by Seah of her suspicion that Ang was misappropriating the respondent's funds, the respondent's directors lodged a police report about the same.

(b) On 25 May 2004, the respondent's directors met with Ang and confronted her about her misappropriation. Ang's employment with the respondent was terminated on the same day, thereby depriving her of the opportunity or ability to carry out further misappropriations.

(c) By 26 May 2004, a detailed police report had been compiled by the respondent and this was submitted to the police to aid in their investigations.

(d) By 28 May 2004, the respondent had instructed its insurance broker, International Testing Co Pte Ltd, to notify its insurers, Liberty Insurance Pte Ltd, of the respondent's claim on its Fidelity Guarantee policies, and, consequently, the respondent managed to recover the sum of $100,000 from its insurance cover under the policies.

(e) As a result of the respondent's assistance in the police investigations, on 5 June 2004, Ang was arrested and the sum of $8,929 was recovered from her.

(f) The respondent engaged forensic consultants, Raffles Corporate Consultants Pte Ltd, in June 2004 to prepare a preliminary report on, *inter alia*, how the misappropriation occurred and a preliminary estimate of the loss arising from Ang's misappropriation.

(g) Once Ang had been found guilty of criminal breach of trust, the respondent instructed solicitors to commence legal proceedings against her in the High Court in an attempt to recover the full amount misappropriated by her. The writ in that suit was issued in November 2004, slightly more than a month after Ang pleaded guilty.

104 These cumulative events strongly indicate that it was more likely than not that if the appellant had exercised due care in its audit and detected the fraud, the respondent would promptly have taken the necessary steps to investigate Ang's misappropriations. In the circumstances, we accept that the element of causation ought to be resolved in the respondent's favour.

The appropriate quantum of damages

105 In the course of oral arguments, Mr Ang sought to undermine the reasoning of the trial judge in quantifying the amount of damages payable. Before delving into the specific merits of his arguments, it would be apposite to set out her holding in relation to the matter. Briefly, the trial judge had quantified the respondent's 2004 losses as comprising $884,195.02 for the period between 16 February 2004 and 23 May 2004, which was the same period as that for which criminal charges had been preferred against Ang (see [19] above). However, the appellant was only held liable for $775,266.02, being the 2004 losses after making a deduction of $100,000 recovered from the respondent's insurers and a further deduction for $8,929 representing the amount recovered from Ang.

106 It is pertinent that the sum of $884,195.02 represented a departure from the sum claimed by the respondent for the 2004 losses in the proceedings below. While the total amount of losses in the civil and criminal proceedings was exactly the same, differences existed in the breakdown of the

losses as between the years. This disparity may be neatly summarised in the form of a table:

	Plaintiff's claim	Criminal proceedings
2001	$148,112.45	0
2002	$12,734.33	0
2003	$511,407.16	$121,920.17
2004	$333,861.25	$884,195.02
TOTAL	$1,006,115.19	$1,006,115.19

107 Mr Ang submitted that the trial judge had erred in assessing the quantum of damages by relying on Ang's confession that was adduced in the criminal proceedings. He alleged that the she was not entitled to adopt the manner in which the losses had been quantified for the purposes of the criminal proceedings, as such figures did not accord with the respondent's claim in the civil proceedings. We do not agree. The mere existence of a disparity in amounts between the civil and criminal proceedings and the adoption of the amounts used in criminal proceedings for a civil suit should not *ipso facto* result in a finding that she had erred in her assessment of damages. Rather, the nub of the issue is whether the judge was entitled, in fact and in law, to have regard to the evidence garnered during the criminal proceedings.

108 The trial judge had taken the view that s 45A of the Evidence Act (Cap 97, 1997 Rev Ed) provided the basis upon which the amount of $884,195.02 was admissible in the proceedings before her (see GD at [83]). We would, however, respectfully depart from her views in relation to this matter.

109 In our considered view, there is considerable fogginess as to the accuracy and reliability of the figures adopted in the criminal proceedings. In *Mohamed Hiraz Hassim v PP* [2005] 1 SLR 622 ("*Mohamad Hiraz Hassim*"), the court cautioned against the blanket acceptance of an admission by an accused where the value of certain goods was in question. The court noted (at [23]) that an accused's assessment of value could be inaccurate for a multitude of reasons, such as where the accused had deliberately under-declared the value of the goods to escape more severe penalties or had simply misstated the value due to a mistaken assumption.

110 Admittedly, the facts of *Mohamed Hiraz Hassim* ([109] s*upra*) may be readily distinguished from the facts before us. The goods in that case were gemstones, and the court had penalised the accused solely on the basis of the accused person's evidence as to the value of the gemstones. This is unlike the present case, where an objective and independent verification of the amounts misappropriated had been undertaken. This verification had been made possible by Ang's paper trail, *viz*, the undeposited bank deposit slips found in the respondent's safe when the fraud was discovered. As such, it can plausibly be contended that the amounts referred to in the criminal proceedings have a reasonable degree of pertinence and can, therefore, be relied upon for the quantification of damages in the civil proceedings.

111 However, an overall assessment of the circumstances points in a different direction. In *Ong*

Bee Nah v Won Siew Wan [2005] 2 SLR 455, Andrew Phang Boon Leong JC (as he then was) correctly observed at [62] that a "holistic approach" should be taken in assessing the precise weight which should be attached to evidence from criminal proceedings:

> In my view, neither approach is, with respect, wholly correct. Each captures a facet of the ***holistic approach*** that ought to be adopted. In the *practical* sphere of application, in addition to shifting the burden of proof, the conviction concerned will almost certainly figure in the court's mind in at least a minimally substantive way. This is consistent with Lord Denning MR's view [In *Stupple v Royal Insurance Co* [1971] 1 QB 50]. However, to the extent that such ***evidence will not be conclusive in and of itself***, Buckley LJ was also correct in pointing out that the court can – ***and must – take into account evidence to the contrary that might prevail at the end of the day***. I am thus of the view, as already alluded to above, that *both* Lord Denning MR's and Buckley LJ's approaches reflect the realism and common sense that are necessary in aiding the court in arriving at a result that must, in the final analysis, be closely linked to the specific facts and circumstances in question. [emphasis added in bold italics]

112 A holistic evaluation of the circumstances required the judge to verify the amounts referred to in the criminal proceedings. As such, it was not appropriate for her to quantify the amount of damages payable by purely relying on the figures proffered in the criminal proceedings. Consideration must also now be given to our finding that the breach had occurred on 17 March 2004 (see [90] above). This necessitates a departure from the figures proffered in the criminal proceedings, which quantified the respondent's losses from 16 February 2004. Finally, there is yet another compelling reason why the judge erred in relying on the amounts adverted to in the criminal proceedings: Any admission by Ang could not bind the appellant, which was neither a party to nor involved in those proceedings.

113 We are, therefore, inclined to vary the assessment of damages made by the trial judge below. The decision in *Flint v Lovell* [1935] 1 KB 354 is oft-cited as the starting point in an inquiry as to whether an appellate court is justified in interfering with a trial judge's assessment of damages. Greer LJ held, at 360, that:

> … [T]his Court will be disinclined to reverse the finding of a trial judge as to the amount of damages merely because they think that if they had tried the case in the first instance they would have given a lesser sum. In order to justify reversing the trial judge on the question of the amount of damages it will generally be necessary that this Court should be convinced either that the judge acted upon some wrong principle of law, or that the amount awarded was so extremely high or so very small as to make it, in the judgment of this Court, an entirely erroneous estimate of the damage to which the plaintiff is entitled.

114 There are thus two distinct grounds of interference: that the trial judge has acted on a wrong principle of law, and/or that he has made an entirely erroneous estimate of the damages. We would set aside the trial judge's assessment of damages on the first ground, as we have found that the breach only occurred a week after Phong received the December 2003 BRS (*ie*, on 17 March 2004). For the sake of completeness, we would highlight that the trial judge had been somewhat handicapped in the assessment of damages as she did not have the benefit of knowing the amounts misappropriated from the date of breach on 17 March 2004 to 23 May 2004, when the fraud was finally detected.

115 A comprehensive breakdown of the amounts misappropriated in 2004 was only tendered in the course of these appellate proceedings. After reserving judgment in this appeal, we invited counsel for both parties to reach an agreement on the amounts misappropriated over three time periods: (a)

10 March 2004 to 23 May 2004; (b) 17 March 2004 to 23 May 2004; and (c) 1 April 2004 to 23 May 2004. By a letter dated 4 June 2007, we were informed that the parties had been able to arrive at an agreement in relation to the figures as reflected in the following table:

	Time period	Amount misappropriated
1	10 March 2004 to 23 May 2004	$697,103.19
2	17 March 2004 to 23 May 2004	$634,216.05
3	1 April 2004 to 23 May 2004	$487,739.97

116 Given that the breach occurred on 17 March 2004, we would set aside the trial judge's assessment of damages and hold that the respondent had suffered a loss of $634,216.05 in 2004 as a result of the appellant's breach (see [115]).

Contributory negligence

General observations

117 A brief overview would be appropriate before we move on to consider whether the appellant is entitled to rely on a plea of contributory negligence. In our view, there exists considerable scope for the application of the defence. PS Marshall and AJ Beltrami in their article, "Contributory negligence: a viable defence for auditors?" (1990) LMCLQ 416 at 421, accurately point out:

> It is undoubtedly correct that the defence of contributory negligence must receive a narrow application. The widespread availability of such a defence would devalue the auditor's responsibilities and duties and would penali[s]e many companies whose only fault was to rely on their auditor to produce an accurate report. However, this need not lead to a conclusion that the defence can never be raised. *Having regard to the nature of the auditor's duty, the fact that an auditor is employed to report whether the accounts show a true and fair view of the company's financial position does not in itself mean that the company should be absolved from the responsibility to look after its own interests. Just because there is a watchdog on the premises, it does not follow that the occupants can safely forget to bolt the doors and omit to switch on the burglar alarm.* [emphasis added]

118 We concur with the learned writers that the issue of contributory negligence can potentially arise under two headings: first, where the company has, by its acts, positively prevented or hindered the auditor from carrying out his duty with due skill and care; and, second, when there has been such negligence that the company may be found to have failed to look after its own interests even though it has appointed an auditor.

119 Additionally, we also gratefully adopt the guidelines propounded by the High Court of Australia in assessing whether a deduction should be made for contributory negligence. The High Court in *Astley v Austrust Ltd* (1999) 197 CLR 1 ("*Astley*") held at [30]:

> The duties and responsibilities of the defendant are a variable factor in determining whether contributory negligence exists and, if so, to what degree. In some cases, the nature of the duty may exculpate the plaintiff from a claim of contributory negligence; in other cases the nature of that duty may reduce the plaintiff's share of responsibility for the damage suffered; and in yet other cases the nature of the duty may not prevent a finding that the plaintiff failed to take reasonable care for the safety of his or her person or property. *Contributory negligence focuses on the conduct of the plaintiff. The duty owed by the defendant, although relevant, is only one of the many factors that must be weighed in determining whether the plaintiff has so conducted itself that it failed to take reasonable care for the safety of its person or property*. [emphasis added]

120 Two observations arise from the decision in *Astley* ([119] *supra*). First, the principal thrust of the inquiry should be directed towards the conduct of the respondent. Second, the principle of contributory negligence would only apply as a basis for reducing the quantum of damages if it can be shown that the respondent's failure to supervise Ang and guard against fraud cannot be excused by its reliance on the audit.

121 With these principles in mind, we now turn to consider whether the principle of contributory negligence ought to apply on the facts presently before us.

The principles as applied to the present case

122 As is evident from the preceding discussion, the question which arose in the present case was whether the respondent's conduct could be brought under the rubric of either of the two headings (see [118] above) such as to warrant a finding of contributory negligence. We determine that this question should be answered in the affirmative.

123 We would preface our findings by first stating that the respondent had not prevented the appellant from performing its audit duties. As it stands, this aspect of contributory negligence has hitherto been confined to situations where the company in question had made a positive representation to the auditors that the embezzler could be trusted (see, *eg*, *Craig v Anyon* 208 NYS 259). The facts of our case are in stark contrast, as the respondent could only be said to have made implicit (or tacit) representations as to Ang's integrity. In fact, we note that it was the appellant itself who viewed Ang favourably on the basis that it had worked with Ang on the audits in previous years.

124 Admittedly, a persuasive case of contributory negligence can also be made out if evidence is adduced to show that the respondent had refused, either wilfully or negligently, to produce the monthly BRS for January and February 2004 despite the appellant's request. However, given that this point was not pursued before us, we hesitate to hold that contributory negligence had been made out under the first heading.

125 We nevertheless hold that the respondent had been contributorily negligent by reason of its own patent failure to safeguard its own interests. To our minds, Crowhurst, Lew and Shaw had been guilty of serious maladministration of the company's affairs, with the result that the respondent failed to detect Ang's defalcations until May 2004.

126 In the proceedings below, the trial judge had declined to find the respondent contributorily negligent in 2004 because of major management changes in the respondent during that period, as well as the fact that Crowhurst no longer received the BRSs on a monthly basis after stepping down from his role as the respondent's managing director. Additionally, she found as a fact that Lew and Shaw

were merely non-executive directors who had not been provided with the monthly BRSs, and that there was thus no evidence to suggest that they had ever become aware of the deficiencies in the internal controls and books of account. Likewise, the trial judge took the view that Crowhurst had become a non-executive director after stepping down from the post of managing director in January 2004, and had thus relinquished his supervisory responsibilities (GD at [39]).

127 Before us, both counsel focused the bulk of their submissions on the judge's findings on the effect of the management changes which the respondent underwent in 2004. Mr Fong sought to defend the judge's holding that no contributory negligence existed, and contended that greater leeway ought to be given to the respondent by virtue of its being a small set-up. Mr Fong urged us to find that there was no reason for Crowhurst, Lew and Shaw, who were non-executive directors, to be provided with the monthly BRS and to review and understand its contents.

128 On the other hand, Mr Ang strenuously contended that the trial judge had erred in exonerating the respondent of contributory negligence. He asserted that Crowhurst, Lew and Shaw were obliged to keep abreast of the respondent's affairs, despite the management changes in 2004. We concur with Mr Ang's submissions. In the first place, the evidence disclosed that Crowhurst continued to act in his capacity as managing director until July 2004 and took on the role of a non-executive director only on 1 July 2004. In the light of this, the mere fact that Crowhurst had vacated the office much earlier and had worked from home during the interim period from January to July 2004 did not absolve him from his duty as managing director to supervise Ang.

129 We were unpersuaded by Mr Fong's arguments that a concession ought to be granted to the respondent solely by virtue of its modest operations. On the contrary, we think that this factor would incline towards a positive finding of contributory negligence. The observations of PS Marshall and AJ Beltrami in "Contributory negligence: a viable defence for auditors?" ([117] *supra*) at 424 are apposite and merit reproduction:

> One area where the courts may be more likely to find contributory negligence is where the company is a small, closely held company. The company's system of control is often dependent on the close involvement of the directors, who are better acquainted with the employees and officers. If there is fraud by an employee of the company, a director may be more likely to have his suspicions aroused than would his counterpart in a large, anonymous, public company.

130 Furthermore, we agree with Mr Ang that it is quite irrelevant whether Crowhurst, Lew and Shaw had in fact received the monthly BRSs. The nub of the issue is whether they remained under a duty to take positive steps to ensure that the accounts were in order (at least on their face), despite their designation as non-executive directors. This question ought to be answered in the affirmative. As pointed out by the court in *Vita Health Laboratories Pte Ltd v Pang Seng Meng* [2004] 4 SLR 162 ("*Vita Health*") at [14], "[e]very director of a company, regardless of whether he has an executive or non-executive designation, has fiduciary duties and legal responsibilities to his company". Thus, the mere fact that Crowhurst, Lew and Shaw were non-executive directors at the material time and took a backseat in the management of the company did not exempt them from the need to exercise a modest level of scrutiny as to the goings-ons in the respondent. The observations of the court in *Vita Health* at [20]–[21] are pertinent:

> 20 The issue of delegation has vexed courts in several jurisdictions. It would be wholly impractical to expect directors to be omniscient or to personally discharge all corporate powers and functions. The larger the business, the greater the commercial need for delegation. The more specialised functions are, the greater the need for independent operations and powers. Legal pragmatism imbued with latitude towards business efficacy is crucial in assessing a director's

delegation of duties. Admittedly, he must reasonably believe that his subordinates will competently discharge their duties in the company's interests. Other than that it is fair to say that there is no acid test that will provide a definitive answer. It can however be safely assumed that the court will be reluctant to take to task a director who has *bona fide* delegated his functions and/or powers to competent subordinates.

21 It has been said that delegation may be improper only if the situation is "of such character, so plain, so manifest and so simple of appreciation" that no one would rely on the subordinates (*cf* Romer J in *In re City Equitable Fire Insurance Company, Limited* [1925] Ch 407 at 428, quoting from *Overend & Gurney Company v Gibb* (1872) LR 5 HL 480 at 486–487). This historical view, set in the context of a wholly different era of commerce, is no longer apposite. ***A director cannot now be viewed as a mere*** *sentinel* ***who may occasionally doze off at his post. Directors are*** *officers* ***who must remain alert and watchful at the helm. Directors ought to have an inquiring, though not necessarily suspicious, mind in discharging their supervisory functions***. The English Court of Appeal in *Re Barings plc (No 5)* [2001] 1 BCLC 523 at [36], approved (*per* Moritt LJ) the instructive summary of principles by Parker J at first instance (see *Re Barings plc* [1999] 1 BCLC 433 at 489):

> (i) Directors have, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them properly to discharge their duties as directors.
>
> (ii) Whilst directors are entitled (subject to the articles of association of the company) to delegate particular functions to those below them in the management chain, and to trust their competence and integrity to a reasonable extent, the exercise of the power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions.
>
> (iii) No rule of universal application can be formulated as to the duty referred to in (ii) above. The extent of the duty, and the question whether it has been discharged, must depend on the facts of each particular case, including the director's role in the management of the company.

[emphasis added in bold italics]

131 In fact, we note that our views in this respect are fortified by certain recent amendments to the SSAs, which are also premised on the existence of meaningful collective obligations on the part of directors in the discharge of their functions. In its amended form, SSA 700 uncompromisingly sets out (at para 60) the duties of directors where audit reports are concerned:

> *Directors' Responsibility for the Financial Statements*
>
> The Company's directors are responsible for the preparation and fair presentation of these financial statements in accordance with the provisions of the Singapore Companies Act, Cap 50 … and [the] Singapore Financial Reporting Standards. ***This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances***. [emphasis added in bold italics]

132 This is a marked departure from the previous standard, which simply declares without more that directors are "responsible for the preparation of the financial statements". Although the revised SSA 700 is confined to auditors' reports dated on or after 31 December 2006 (and thus does not apply on our facts), it is a timely and accurate reminder of the wide obligations owed by directors. When a person aspires to direct a company, he must give serious consideration to the wide obligations imposed on his office by the law. Directors cannot shy away from the fundamentals of putting in place prudent arrangements to oversee the preparation of financial statements. This is, however, far from saying that they invariably bear personal responsibility for the accuracy and integrity of all of a company's financial statements.

133 It is not open to Crowhurst, Lew and Shaw to now distance themselves from allegations of contributory negligence solely because they had not received the monthly bank statements. It was incumbent upon them, as non-executive directors, to at least perform a minimal degree of oversight in relation to the accounts and seek to be regularly apprised of the respondent's financial affairs. While they were not obliged to delve into minute irregularities in the accounts, they were obliged to broadly discern if any irregularities existed on the face of the accounts. Had they done so, the burgeoning amount of "uncredited lodgments" would have been there for them to see without difficulty. In our view, they cannot claim that they were entitled to wholly rely on Ang to ensure that the accounts were in order. The fact that they may have lacked accounting expertise did not completely exonerate them from their duties to reasonably ensure that the respondent's accounts were in order. We also bear in mind that the respondent was a relatively small operation, and that even a cursory monitoring of the bank statements would have immediately revealed that something was seriously amiss in relation to the banking in of collections from customers.

134 To our minds, these cumulative lapses on the part of Crowhurst, Lew and Shaw constitute serious management failure and ought to be treated as fault for the purposes of a defence of contributory negligence. The incisive views of Evans-Lombe J in *Barings plc v Coopers & Lybrand* [2003] Lloyd's Rep IR 566 at [908] are highly pertinent and persuasive on this issue:

> It is the responsibility of a company's board of directors to manage all aspects of the company's business. The board will delegate many aspects of that task to individuals or committees, either within or (more rarely) outside the company. *But if the delegates fail in their tasks, such that the company fails to take proper care of its own interests, their failure is to be attributed to the company and its board of directors. Where the company is a claimant, and its management failures are relevant to an issue of negligence or breach of contract, those failures are to be treated as fault for the purposes of a defence of contributory negligence*. [emphasis added]

135 We also depart from the trial judge's views that the changeover in management exonerated the respondent from a finding of contributory negligence. As Mr Ang rightly points out, notwithstanding the change in management, the respondent remained liable to ensure that the handover process was performed as seamlessly as possible, without compromising the management's oversight of the company's affairs.

136 Our finding of contributory negligence is fortified by two additional factors. First, we determine that Seah had been careless in failing to detect that something was amiss. This was despite the fact that Seah had prepared the monthly BRSs, which disclosed the ever-increasing amount of unlodged cash deposits. By her own admission, Seah regarded the large amounts of unlodged cash deposits as anomalous and harboured "strong suspicions" that Ang was guilty of some wrongdoing. However, she did not see fit to inform the appellant and/or the respondent's management of her suspicions in this respect until much later in May 2004. Secondly, the fact that the respondent was a small corporate entity facilitated the implementation of a simple system of internal checks to

ensure that cash sales were banked in. The respondent was far from being a huge conglomerate, where it might be somewhat difficult to keep track of cash sales and the amounts of cash received and banked in. Unfortunately, the respondent failed to comply with even its basic duties in this respect and neglected to conduct simple checks to ensure that all cash sales were banked in promptly.

137 Having established that the respondent was contributorily negligent, it becomes necessary to consider the extent to which an award of damages ought to be reduced. In *AWA Ltd v Daniels* (1992) 7 ACSR 463, the court made a deduction of 20% for contributory negligence where the plaintiff's chairman and chief executive had become aware of various matters which should have indicated the existence of irregularities, but had failed to take appropriate action in response to such irregularities. The court also ordered the chairman to make a contribution to the auditors of 10% of the 80% for which the auditors were liable. In *Dairy Containers* ([29] *supra*), the court reduced the quantum of damages by 40% where the plaintiff's directors had failed to provide clear direction or supervision in respect of a major part of the company's business.

138 In our judgment, such figures are merely guidelines and do not lay down any rigid rules in determining the extent to which damages ought to be reduced. In a case such as this, which is extremely fact-specific, any assessment of the appropriate reduction in damages on the ground of contributory negligence must necessarily be done with a broad brush. Such an approach would also be consistent with statutory law, as is evident from the terms of s 3(1) of the Contributory Negligence and Personal Injuries Act (Cap 54, 2002 Rev Ed):

> Where any person suffers damage as the result partly of his own fault and partly of the fault of any other person or persons, a claim in respect of that damage shall not be defeated by reason of the fault of the person suffering the damage, but the damages recoverable in respect thereof shall be reduced to such extent as the court thinks *just and equitable* having regard to the claimant's share in the responsibility for the damage. [emphasis added]

139 In the circumstances, we assess that a reduction of the damages recoverable would be appropriate. This is because the omissions by Crowhurst, Lew and Shaw directly contributed to the loss in 2004, in so far as a perusal of the monthly bank statements would undoubtedly have led to discovery of the irregularities and the detection of Ang's fraud. We also took into account Seah's failure to raise a timely alarm despite her growing doubts as to Ang's integrity. Calibrating the respondent's fault against the appellant's negligence, the quantum of damages recoverable by the respondent should be reduced by 50%.

Conclusion

140 Having considered the case in its entirety, we allow the appeal in part and reverse the judge's finding that the breach had occurred on 10 March 2004. In our judgment, the breach only occurred a week after Phong had received the December 2003 BRS (*ie*, on 17 March 2004). As such, the appellant would only be held liable for the losses sustained over the period from 17 March 2004 to 23 May 2004, *ie*, for the sum of $634,216.05.

141 However, we reduced by 50% the amount of damages ultimately recoverable by the respondent in the light of our finding that the respondent had been contributorily negligent in 2004.

142 In the circumstances, we would allow the appeal in part. The appellant is to be awarded the costs of the appeal. The order of costs in favour of the respondent for the proceedings below is to stand. The appellant is to pay the respondent the sum of $317,108.03 by way of damages, with

interest of 3% per annum with effect from 22 July 2005, the date on which the writ was filed.