

# AUDITORS

## **(a) The purposes of auditing company accounts:**

- To add credibility to the financial statements forming part of the annual
- To ensure that the accounts comply with the law.
- To ensure that the financial statements give a true and fair view of the company financial position.
- To ensure that the company maintains limited liability status.
- Failure to keep accounting records as required is an offense for which officers of the company are liable.
- To achieve disclosure of a company's financial affairs for the benefit of those who have invested in the company
- To achieve disclosure of the company's financial position for the benefit of those who do business with the company.

## **(b) Circumstances when the group accounts of the holding company need not include those of the subsidiary:**

### **If the directors are of the opinion that:**

- It is impracticable taking into account the insignificant-amounts involved.
- It would involve many expenses.
- It will result in unreasonable delay.
- The result would be misleading/harmful to the business of company or its subsidiaries
- The business of the holding company and its subsidiary are fundamentally

## **(c)**

### **(I) Rules governing appointment of first auditors of the company**

- The directors of the company must appoint the first auditor.
- The first auditor may hold his office until the end of the first annual general meeting
- The directors may fill a casual vacancy in the office of such auditor.
- Any auditor appointed to fill in any casual vacancy may hold office until the end of the next general meeting.
- If the directors fail to appoint the first auditor, the company can make an application to the cabinet secretary to appoint one.

### **Ways in which an auditor might receive his remuneration**

- The audit fee payable to the auditor
- Reimbursement of the expense, if any, incurred by the auditor in connection with the audit of the company
- Any facility extended to the auditor in connection with the audit of the company.

**November 2017 question one**

### **A retiring auditor can be re-appointed without any resolution unless:**

- He is not qualified for re-appointment.
- A resolution has been passed to re-appoint someone else.
- A resolution has been passed that he should not be re-appointed.
- He has given the company a notice that he is not willing to be re-appointed.
- A director or any other auditor may fill any casual vacancy in the office of an auditor.

**November 2016 question six A**

**Rights of an auditor.**

- Right to examine the company's books, vouchers and other relevant documents.
- Right to access to the company's books, vouchers and accounts.
- Right to demand an explanation from officers of the company
- Right to seek professional advice whenever necessary.
- Right to attend all general meetings of the company.
- Right to be heard in general meetings of the company
- Right to all notices and other- communication to members.
- Right of indemnity for any loss or liability arising in the course of discharging his obligations as an auditor.

**May 2016 question five B ,May 2015 question four A, Dec 2012 Q 3b ,August 2009 Q 6B**

**Matters of an Auditor's report.**

- Whether the company's financial statements were in agreement with the books of accounts and returns.
- Whether in the auditor's opinion proper books of accounts have been kept by the company and whether proper returns were received by them from subsidiaries not visited by them.
- Whether the auditor received all the information and explanation which to the best of their knowledge necessary for the audit.
- In case of a holding company submitting group accounts, it should state whether group accounts have been properly prepared in accordance with the act
- Financial under view

**November 2015 question five A**

**Grounds for removal of an auditor**

- i. If he has been negligent
- ii. Failure to his report
- iii. If he is in of his statutory obligations

**May 2015 question four A**

- Persons who are disqualified for appointment as auditors of a corporate body.
- An officer or servant of a corporate body.
- A person who is a partner of or in the employment of an officer or servant of the corporate body unless the corporate body is a private company:
- A body corporate.
- Any person disqualified for appointment as auditor, For example, a bankrupt person

**December 2014 question seven A**

**ii) For a third party to successfully sue an auditor for professional negligence it must be established that**

- The auditor was engaged on the premise that he professed to have certain skills
- The auditor was at all material times aware that his report would be relied upon
- The third party must prove that he suffered loss of financial nature

**December 2012 question three B**

### **Remuneration of an auditor**

- Where the directors appoint the auditor, they shall fix his remuneration. Where the registrar appoints the auditor, the members shall fix his remuneration.
- Where neither the director nor registrar appoint him, his remuneration shall be fixed by the company at
- the Annual General Meeting
- His remuneration may also be fixed in such a manner as the company may determine.

**June 2012 question one D**

### **Procedure of removal of an auditor from office**

- An extraordinary general meeting (EGM) can be called as allowed by the Articles of Association.
- Where directors are unwilling to call the EGM 10% of shareholders with voting rights may call the meeting
- By ordinary resolution, the company may remove the auditor before the end of his term.
- Special notice of 28 days of this resolution must be given.

### **Rights and duties of auditors**

- Duty to make a report to the members on the accounts examined by them during their tenure in office.
- Report to be read before the company in general meeting and open to inspection by any member.
- Print of access at all times to the books, accounts and vouchers of the company other information and explanation he/she thinks necessary to perform duties as an auditor
- To attend any general and communications relating to any general meeting they attend on matters concerning them as auditors.
- Duty to examine the books of the company' ascertain they are rights prepared a balance sheet showing the time financial position as at the date of the balance sheet, be honest, not certify what he does not believe to be true.

**June 2011 question C**

### **Appointment of auditors.**

- Under Section 722 of the Company Act, every company is required at each annual meeting, to appoint on auditors.
- The auditor so appointed should hold office from that conclusion of that meeting, until the conclusion or the next meeting.
- If the company fails to appoint them, an application may be made to the Registrar to appoint an auditor.
- A retiring auditor can be re-appointed without any resolution unless:
- He is not qualified for re-appointment.
- A resolution has been passed to re-appoint someone else.
- A resolution has been passed that he should not be re-appointed.
- He has given the company a notice that he is not willing to be re-appointed.
- Any casual vacancy in the office of an auditor may be filled by a director or at other auditor.
- Qualified accountant.

**December 2010 question seven A**

**The duties of the auditor sure, laid down by Act and the articles of association of the company**

- The auditors must acquaint themselves with their duties laid down in the Act and articles,
- They must report to the members accounts laid down before 'the company in the general meeting during their tenure of office,
- This report must contain statements as to the matters contained in the seventh schedule
- In preparing the report they must ascertain and state the true financial position of the company by examination of the books, that, they must not just deal with what the books show, but that they show the true financial position,
- They must be honest and exercise reasonable skill and care. However, while they must exercise care, they are not bound to be detectives / investigative.
- And should not approach their work with suspicion or a foregone conclusion that there is something wrong,
- They must not, however confine themselves to the task of arithmetical accuracy of the balance sheet and income and expenditure.
- If the auditors are negligent, the company can sue them for loss incurred and damages and they may be removed from the office or barred from appointment as company auditors in future
- They may equally be deregistered by the supervisor and regulatory of the professional body on the complaint of the company.

**June 2010 question seven A**

**a) Obligations of an auditor**

- To examine the books of accounts and vouchers of the company and to consider information and explanation provided during their tenure of office-
- To make a report to members on the accounts examined by them and on every balance sheet, profit and loss account and all group accounts laid before the company in general meeting.
- To acquaint themselves with their duties under the Companies Act and the articles of the association of the company whose accounts they are appointed to audit.
- To satisfy themselves that the company's securities exist and are in safe custody and if not, demand that urgent action be taken.
- To exercise the care and skill of a reasonably competent, careful and cautious auditor.
- To approach the task with an enquiring mind and not with a foregone conclusion that something is wrong-
- To provide professional advice if called upon to do so.
- To act honestly but not certifying as true what he does not believe to be in and exercising care and skill before certifying something as true.
- Give true and fair view of the books of accounts.

**(a) Fixing the auditors' remuneration**

- By the cabinet secretary if appointed by him.
- By directors if appointed by them.
- By the company in general meeting
- In such a manner as the company in general meeting may determine.

**June 2009 question four**

**Disqualification of a person to be appointed an auditor of a company may be on the following grounds:**

- An officer or servant of the company.
- A person who is a partner of the employment of an officer or servant of the company a body corporate.
- If he is disqualified for appointment as auditor of, any other corporate body which is that company's subsidiary or holding company.

**June 2008 question five B**

**Recent demands by regulatory authorities and shareholders have obviously affected the traditional role of an auditor in various ways for example:**

- **Professional Competence and due care:** An accountant must not only attain professional competence but must maintain the same. General and specific education is necessary. He must be continually aware of developments in the profession. He must exhibit care, competence and diligence.
- **Professional behavior:** Must act in a manner consistent with the good reputation of the profession and refrain from any conduct, which might bring discredit to the profession.
- **Confidentiality:** Must respect confidentiality of information about a client acquired in the course of rendering professional services and should not use or disclose the same without proper and specific authority.
- **Integrity:** Entails fair dealing and truthfulness i.e. must be straightforward and honest in performing professional services.
- **Technical standards:** An accountant should carry out professional services in accordance with the relevant technical and professional standards. Must carry out the clients' instructions with utmost care and skill.
- **Objectivity:** An accountant must be fair, intellectually honest and free from conflict of interest. Objectivity must be demonstrated in all circumstances.
- **Whistle blowing:** Since the accountant has a responsibility to the public, he is bound to blow the whistle whenever necessary to enable relevant bodies take the necessary action to protect the public.
- Indoor/other information about the company e.g. products, markets processes.
- **Investigation:** Though traditionally the auditor is not an investigator unless appointed as such shareholder are demanding more and more information from them and this compels the auditor to "dig deeper" for the information. It is apparent that the traditional statements of auditors no longer appease members who have become more inquisitive.

▪ **June 2006question two**

**a) Compare the position of directors with that of auditors in respect to the standard duty of skill and care expected of them.**

<p>Are elected by members in general meeting Every company must have a board of directors to manage affairs. Directors stand in a fiduciary position in relation to the company. The law does not insist that a director profess any profession. Directors owe their company a duty of care, skill and diligence. The degree of care, skill and diligence expected of them is that of a person of their knowledge and experience. A director is not bound to bring any special qualification to his office, as observed by Neville J. in re: Brazilian Rubber Plantation and Estates Ltd. However if a director possess a particular skill he is bound to exercise the same for the benefit of the company. They are not bound to give continuous attention to the affairs of the company and are entitled to rely on information provided by trusted servants of the company.</p>	<p>Are engaged by the company to discharge certain obligation prescribed by law. There is a contractual relationship between an auditor and the company Are professional registered by the relevant body and licensed to practice accountancy. One of the principal obligation of an auditor is to exhibit a degree of care, skill and caution of a reasonably competent careful and cautious auditor, as observed by Lopes L. J. in re: Kingston cotton mills. An auditor is bound to approach his task with an inquiring mind and not with a foregone conclusion of wrongdoing. He must ensure that errors of commission and omission and downright untruths are ascertained. However it is not his obligation to discover all fraud as he is not an investigator, "He is a watchdog but not a blood hound" His task is not to ensure that the computation is correct. He is not a stock taker. "He is not written off as a professional adder-upper and subtractor" But must satisfy himself that the company's security exists and are in safe custody.</p>
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**b) The rules that govern the appointment and removal of an auditor of company,**

- Under the provisions of the Companies Act, an auditor may be appointed by the board of directors the annual general meeting or the registrar of companies.

**Board of directors:** the provisions of the Companies Act confer upon the board of director power to appoint the first auditor of the company before the first annual general meeting. If no appointment is made before this meeting, directors lose this power.

However, directors are empowered to fill a casual vacancy in the office of the auditor.

**Annual general meeting:** At every annual general meeting, an auditor must be appointed to hold office from the conclusion of the meeting to that of the next annual general meeting.

However, at every annual general meeting a retiring auditor is always deemed to have been re-appointed without any resolution to that effect unless:

He is not qualified for re-appointment.

He has intimated to the company his unwillingness to be re-appointed.

The meeting has expressly resolved that he shall not be re-appointed.

The meeting has resolved to appoint some other person auditor.

Registrar: if at an annual general meeting, no auditor is appointed is deemed to be re-appointed, the company must notify the registrar within 7 days of the meeting. The registrar may appoint an auditor or for the company.

A special notice of the intended resolution to remove an auditor from office must be given to the company by the person proposing to move it.

The company must send a copy thereof to the auditor concerned. The auditor is entitled to make written representations, not exceeding reasonable length as his defense and may request the company to notify its members that he has made representations.

The company must summon a meeting to deliberate the matter among other matters. Notice of the meeting must be sent to all members and must embody the proposed resolution. It must intimate to members that the auditor has made representations if any, and copies must be enclosed unless received too late by the company.

If the auditor's representations are received too late or are not enclosed because of the company's default, the auditor is entitled to have them read out at the meeting.

Copies of the auditors' representations need not be enclosed in the notice or be read out at the meeting if an application by the company or other aggrieved person, the court is satisfied that the auditor is abusing his right to be heard to secure needless publicity for defamatory matter

The removal of an auditor from office take effect when the meeting by ordinary resolution so resolves. '

**(a) Auditor owes a duty of care to**

**In preparing his audit report, the auditor owes a duty of care to:**

- **The company:** Since an auditor is a professional engaged by the company to render certain services, he owes the Company a legal duty of care in preparing his report to the company who appointed him.
- **Third parties:** an auditor owes a legal duty of care to third parties whom he knew or reasonably ought to have known would rely upon his audit report. To that effect such parties are his "neighbors" and the auditor may be
- Held liable for loss or liability arising because of reliance on his audit report.
- The auditor's legal duty of care is founded on the premise that there is a special relationship between him and the company as well as such third parties.

## **COMPANY ACCOUNTS, AUDIT AND INVESTIGATIONS**

### **The purposes of auditing company accounts:**

- To add credibility to the financial statements forming part of the annual
- To ensure that the accounts comply with the law.
- To ensure that the financial statements give a true and fair view of the company financial position.
- To ensure that the company maintains limited liability status.
- Failure to keep accounting records as required is an offense for which officers of the company are liable.
- To achieve disclosure of a company's financial affairs for the benefit of those who have invested in the company
- To achieve disclosure of the company's financial position for the benefit of those who do business with the company.

### **Instances when an auditor may not be held liable to third party for alleged professional negligence.**

- i. If he can show that, he exercised proper duty of care.
- ii. If he relied on the information given by a responsible officer of the company in absence of any suspicion to falsify the information.
- iii. If he can show that, he did not owe him a duty of care.

**May 2017 question four B and C**

### **Legal provisions relating to investigations of company accounts, audit and investigation by the registrar**

- Investigation by the registrar will take place where the registrar has reasonable cause to believe that the provisions of the Companies Act are not being complied with.
- Where on perusal of any document he is of the opinion that the document does not disclose a full and fair statement of the matters to which it relates, he may call on the company concerned to produce all or any of the books of the company as he may
- Such books shall be produced and such information or explanation shall be furnished within such time as may be specified in the order.
- On receipt of an order, it shall be the duty of all persons, who are officers of the company to produce such books or to furnish such information or explanation.
- If any such person refuses or neglects to produce such books or to furnish any such information or explanation he shall be liable to a fine not exceeding 200,000 in respect of each offence.
- If after examination of such books or consideration of such information or explanation the registrar is of the opinion that an unsatisfactory state of affairs is disclosed or that a full and fair statement has not been disclosed, the registrar shall report the circumstances of the case in writing to the court.

**December 2012 question six B**



**Powers of an inspector appointed to investigate the affairs of a company.**

- To interrogate any officers of the company.
- To investigate subsidiary of company and co-subsiaries.
- To apply to the court for attendance and examination on oath of any person he would not otherwise be entitled to examine.
- To make a written report to the court.

**Circumstances under which a court might appoint inspectors**

- Where the company is being conducted with the intention to defraud the company's creditors.
- If the company was formed for fraudulent or unlawful purpose.
- If the company members have not been given all the information all the information with respect to its affairs.
- If it is in public interests.

**November 2016 question seven A, September 2015 question six B**

**Persons responsible for meeting the expenses of an investigation by an inspector appointed by the court**

- The attorney general.
- The person convicted of the offence
- The company.
- The applicants for the investigation.
- The directors.

**November 2015 question two B**

**Group accounts need not to deal with a subsidiary company of the holding company.**

**If the directors are of the opinion that:**

- It is impracticable taking into account the insignificant-amounts involved.
- It would involve many expenses.
- It will result in unreasonable delay.
- The result would be misleading/harmful to the business of company or its subsidiaries
- The business of the holding company and its subsidiary are fundamentally

**May 2015 question four B, December 2011 question seven B**

**Provisions of the Companies Act that govern the content of books of account of a limited company**

- Statement of financial position.
- Income statement.
- Cash flow statement.
- Statement of changes in equity.

**December 2014 question one B**

**Persons to whom the court shall forward any report made by a company inspector;-**

- Any person who is a member of a company
- To the registrar
- Any person who is a member of a company
- Anybody corporate dealt with in the report.
- To the applicants applying for the investigation

**May 2014 question five A**

**Who can apply for inspection/investigation of the company affairs**

In a company having a share capital.

- On the application either of not less than two hundred members
- Members not holding not less than one-tenth of the shares issued

In a company not having a share capital

- On the application of not less than 1/10 of the company's register of members.

**June 2013 question seven B**

**Purpose of profit and loss account.**

- It shows the profit and loss of the company that is difference between the revenue for the period covered by the account and the expenditure chargeable in that period.
- The main purpose is to present the true and fair view of the profit and loss of the company for the financial year.
- It is a basis of corporation tax computation.
- It shows the performance of the company

**Books of accounts the company is obliged to keep**

- All sums of money received and spent by the company and matters in respect of which the receipt of which the receipt and expenditure take place.
- All sales and purchases of goods of a company.
- The assets and liabilities of the company-
- Section 628 of the companies act provides for the books of account required to be kept by a company.
- Cash flow statement.

**December 2010 question seven B and C**

**Provisions of the Companies Act that govern books of account;-**

- Every company ,shall keep in the English language proper books of accounts,
- The books shall contain:
- All sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place.
- All sales and purchases of goods of the company All assets and liabilities
- Books must give a true and fair view of the state of the company's affairs to explain its transactions
- Books of accounts shall be kept at the office of the Registrar of Companies or such other place as the directors think fit.
- The books shall at all times be open for inspection by the directors.
- Books shall only be kept outside Kenya with the concept of the Registrar and subject to the conditions he may impose.