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5th November 1993

Mrs Gina Cole,  
Secretary,  
Committee on the Financial Aspects of Corporate Governance,  
c/o The London Stock Exchange,  
London EC2N 1HP.

Dear Mrs. Cole,

**Directors' Responsibilities Statements**

Thank you for your letter of 3rd November.

I am pleased to have confirmation that the Committee on the Financial Aspects of Corporate Governance did not intend the wording in the Report to be used as a pro forma or to increase directors' legal liabilities. I did not suppose that that was the case, but it is helpful to have it confirmed.

Yours sincerely,



MARTIN G. CHESTER  
Chairman  
The Law Society's Company Law Committee

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Martin Chester  
Chairman  
The Law Society Company Law Committee  
Theodore Goddard  
150 Aldersgate Street  
London EC1A 4EJ

3 November 1993

### **Directors' Responsibilities Statements**

Thank you for your letter of 1 November, with which you enclosed a draft of the forthcoming article in the Law Society Gazette on directors' responsibilities statements.

The Committee on the Financial Aspects of Corporate Governance did not intend that the wording in paragraph 2 of Appendix 3 to the Report, which sets out what the statement of directors' responsibilities should cover, should be used by companies as a pro-forma, although as you point out it has been followed literally by some companies. As you are aware, it was not the Committee's intention to increase directors' legal liability.



Gina Cole  
Secretary to the Committee

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1st November 1993

Mrs Gina Cole,  
Secretary,  
Committee on the Financial Aspects of Corporate Governance,  
c/o The London Stock Exchange,  
London EC2N 1HP.

Dear Mrs. Cole,

Cadbury Committee Code of Best Practice: Directors' Responsibilities Statements

The Law Society's Company Law Committee has been considering the wording which some companies have already included in their reports and accounts regarding Directors' responsibilities, in response to the requirement in the Cadbury Committee's Code of Best Practice. The Committee is concerned at the wide scope of some of the statements which have been published and the fact that, by doing so, companies run the risk of extending the legal liability of directors unnecessarily and beyond what appears to be contemplated by the Code of Best Practice.

An article is to be published shortly in The Law Society's Gazette, setting out suggested wording and commenting upon it. I attach an advance copy for your information.

As you will see, the Committee does not suggest there is a single formulation which is appropriate in all circumstances.

Yours sincerely,



MARTIN G. CHESTER  
Chairman  
The Law Society Company Law Committee

cc Sir Adrian.

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[Article for inclusion in The Law Society's Gazette]

**Directors' responsibilities**  
**in relation to Financial Statements**

The Law Society's Committee on Company Law has had its attention drawn to the way in which a number of companies have responded to the requirement in the Cadbury Report that a statement should appear in Accounts explaining the Directors' responsibilities in relation to the preparation of the Accounts. Paragraph 2 of Appendix 3 to the Cadbury Report sets out four points which should be covered.

Although paragraph 2 of Appendix 3 to the Cadbury Report does not seek to prescribe the text of the explanation but simply to identify the points to be covered, it would seem that some companies have followed the wording in paragraph 2 literally. Other companies have closely followed example wording put forward in May 1992 by the Auditing Practices Board as an Exposure Draft and updated in May 1993 (SAS 600).

The Committee is concerned that it appears that responsibility statements are being published without legal advice being taken on the implications of so doing or upon the accuracy of the legal statements which appear in them. Companies which do so run the risk of extending the legal liability of directors unnecessarily.

A Working Party of the Committee (including leading counsel) has produced a draft form of responsibility statement, together with explanatory notes, the text of which is set out below.

In embarking on this exercise and in publishing the draft statement and notes the Committee does not seek to suggest that there is a single formulation for such statements which is appropriate in

all circumstances for all companies wishing to comply with the Cadbury Report. Whilst the draft statement addresses certain issues which are commented upon in the notes, the statement does not purport to provide an exhaustive explanation of the responsibilities of directors in relation to both group accounts and separate company accounts.

The Committee therefore considers that companies issuing responsibility statements, including those based on the draft set out below, should take legal advice on them.

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Statement of Directors' responsibilities  
in relation to Financial Statements

The following statement, which should be read in conjunction with the Auditors' Statement of Auditors' Responsibilities set out below, is made with a view to distinguishing for shareholders the respective responsibilities of the Directors and of the Auditors in relation to the financial statements.

The Directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the Group as at the end of the financial year and of the profit or loss for the financial year.

Following discussions with the Auditors, the Directors consider that in preparing the financial statements [on pages - to -], the Company has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that all accounting standards which they consider to be applicable have been followed [,subject to any explanations and any material departures disclosed in the notes to the financial statements].

The Directors have responsibility for ensuring that the Company keeps accounting records which disclose with reasonable accuracy the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985.

The Directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

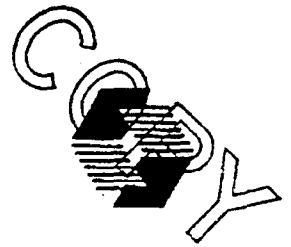
The Directors, having prepared the financial statements, have requested the Auditors to take whatever steps and undertake whatever inspections they consider to be appropriate for the purpose of enabling them to give their audit report.

#### Notes

1. The first paragraph of the above draft has been included to state the purpose of the Responsibility Statement and for whose benefit it is made. It may also limit the use to which the Statement can be put. It also includes a reference to the Auditors' Report, which addresses the same points from the Auditors' point of view, and sets the context in which it is to be read.
2. The second paragraph reflects S.226 and S.227 CA 1985 (but there is a reference to financial statements rather than balance sheets and profit and loss accounts, or individual accounts or group accounts; also S.227(3) refers to group accounts, insofar as they concern the members of the Company).
3. The third paragraph follows Cadbury rather than SAS 600 but describes the accounting policies as "appropriate" rather than "suitable". However, the confirmation required is expressed as an opinion. The opinion as to accounting policies reflects SSAP2 and also Schedule 4 CA 1985; and as to accounting standards Schedule 4 CA 1985.

4. The fourth paragraph reflects Section 221 CA 1985. There is therefore no reference to adequate accounting records, nor to the SAS 600 reference to proper ones.
  5. The fifth paragraph includes a reference to the general responsibility of Directors for safeguarding assets and to prevention and detection of fraud or other irregularities. SAS 600 includes a reference to reasonable steps but only in relation to fraud and other irregularities: this concept has been extended to the safeguarding of assets limb of this statement.
  6. The sixth paragraph has been added to complement the statements relating to the Auditors' responsibilities which will, if example 3 of the APB's May 1992 exposure draft is followed, appear in the Auditors' Statement of Auditors' responsibilities.
-

# EVERSHEDS FACSIMILE



To  
Gina Cole

From  
Andrew Croome

Company

Your Ref

Fax Number  
071 410 6822

Our Ref  
col/apc/mzp  
51515-2/0009.mzp.f

Page one of

Date  
8 September 1993

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Dear Gina,

Many thanks for talking on the phone when I explained that I contribute a chapter to Tolley's Directors Handbook on the subject of the Directors Report.

I wanted to try and make a helpful reference to the responsibility statement required for listed companies by virtue of note 12 to the Cadbury Code of Best Practice and in particular the second limb of 12, namely responsibility for preventing fraud.

I want to point out that note 12 does not purport to set out what the responsibility is but merely requires that the responsibility be covered in the statement. I feel it would be appropriate to point out to my readers that, in consequence, if directors do not wish to accept a greater responsibility to shareholders than actually exists, they should not baldly repeat the relevant section of note 12 (as some companies appear to have done already) but should rather deal with this by including a sentence in the statement along the following lines:

"The directors are also responsible for ensuring that proper and adequate accounting records have been

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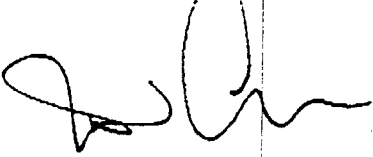


maintained and that reasonable procedures have been followed for safe-guarding the assets of the company and for preventing and detecting fraud and other irregularities."

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I wanted, if possible, to check that this advice does not conflict with your understanding of the recommendation. It has also been suggested to me by a colleague that the Stock Exchange may not insist (for the purposes of a listed company confirming it has complied with the Code) on the responsibility statement containing any reference at all to safe-guarding assets and preventing fraud. Are you able to comment on that as well please.

Many thanks



ANDREW CROOME

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