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Article

Legal evolution in the financial realm: Propelling auditor accountability in England

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Abstract: This article advocates for a fundamental shift in England's legal approach to professional negligence, particularly within the domains of accounting and audit. English law should move away from its intricate and unclear case law surrounding professional negligence towards a clearly defined test for professional misconduct. Drawing upon a comparative analysis with the legal framework in the United States, where auditors are not shielded from liability under the law, the article highlights the need for a more consistent and accountable legal landscape in England. One of the main aspects that necessitates change is the proximity test, as set out in the Caparo case, which currently prevents auditors from being held liable for negligence to investors (as third parties)—despite investors relying on auditors for their professional skill to audit accounts. As investors rely on audited accounts when making financial decisions, a well-defined test for professional negligence should align English law with international standards and empower victims to seek compensation from the auditors themselves and/or the auditors' professional indemnity insurance. Such a change would enhance trust and transparency in the financial domain.

Keywords: negligence; comparative law; England; United States; audit; accounting; professional negligence; reform

1. Introduction

Why does this area of law matter? The audit market in England is a substantial and dynamic sector, with its considerable reflected in its annual financial volume. According to data from 2023, the market size, measured by revenue, of the Accounting & Auditing industry in the UK reached £7.6 billion in that year (IBISWorld). In the contemporary economic environment, emphasizing trust and openness is essential. Thus, financial oversight is paramount and auditors occupy a pivotal position. In a period where nations vie for foreign direct investment (FDI), it is crucial for England and the broader UK to establish a framework that ensures accountability in the realm of financial audits. Ultimately, the fundamental goal of an audit is to validate the accuracy and proper accounting of the financial information presented. Auditor negligence and the ensuing implications for financial transparency and trust cannot be understated. However, the intricate and often ambiguous law in England concerning professional negligence necessitates a transformation. This transformation advocates for an unambiguous test for professional negligence, especially concerning accounting and audit practices, which holds auditors accountable. By drawing upon comparisons with the United States' legal system, which opened the door for accountants doing audits to held liable to third parties in 1931 (Ultramares Corp. v. Touche, 1931), this article underscores the urgency for a more coherent and accountable legal landscape in England. Such reform would not only align English law with global standards but also provides a platform for victims to claim compensation (Thompson and Clark, 2018), ultimately fortifying investor trust and ensuring a transparent financial environment (Baker and Johnson, 2013). A crucial element necessitating change is the proximity test established in the Caparo case (House of Lords, 1990). This test, specifically the proximity element of the test (to be discussed in more detail in a later section) presently acts as a barrier, preventing auditors from being held accountable to investors for negligence as it is deemed that auditors only owe a duty of care directly to the company whose accounts they audit and not investors who rely on the accounts to make an investment. Given that investors rely on audited accounts to make financial decisions, a clearly defined test for professional negligence would not only bring English law in line with international standards but also provide victims with the ability to pursue compensation directly from the audit firm and/or through the accountants' professional indemnity insurance. This, in turn, would boost trust and transparency within the financial domain (Rouas, 2022).

Consider the possible scenario where negligence has come to light. A large hotel group has numerous hotels which it has developed. To repurpose other old buildings, it raises money with debt in the form of loan notes. A shell company in another jurisdiction is set up to market the loan notes. Investors are offered interest on money lent to the parent company. The contract is that the investors' capital and the agreed interest will be returned after one year. The shell company used to market the investments uses information from the strong set of audited accounts, in order to entice investors. However, in this instance, the accounts—which were first produced in-house and then audited by an external accountancy firm were discovered to contain substantial errors. In this example, assets were greatly overvalued and some debts/liabilities were not listed. It results in a multimillion-pound difference in the actual net worth value of the company and the one sent to investors. The company subsequently fails when secured lenders (parties that have 'liens' on the freeholds of the hotel group's estate) move to put a number of the hotel group's companies into administration and then liquidate the companies to retrieve their debts owed. Thus, the investors who leant the company loans in the form of loan notes are left with nothing. Many investors have suffered a substantial financial loss, resulting in a string of lawsuits that reach the courts. The court's judgement is as follows: the business and management team are deemed 35% responsible, given their direct involvement in the negligence; the shell company selling the investment shares 35% responsibility due to marketing the negligent accounts to potential investors without thorough due diligence; and the auditors of the accounts are assigned 10% responsibility for failing to detect the errors after the event (but before investors made their investments). In this scenario, the original business goes into administration and then liquidation, and the marketing company (a shell company established overseas) is no longer operational. Consequently, the auditors are left to foot the entire bill due to English law's joint and several laws regarding professional negligence, as explained and discussed later. At first glance, this might seem like a favorable result for investors as the auditors are held liable not just for their actions but for the actions of everyone else involved. However, while this may seem advantageous, it's essential to note that liability insurance often has a cap, implying that the substantial losses incurred may not be fully recovered. Essentially, investors will probably only recoup a fraction of their invested capital despite the negligence of multiple professional parties. Moreover, from a corporate standpoint, the auditors are held accountable for the consequences of not only their actions but also those of others, resulting in significant payouts for actions beyond their control. This, in turn, raises premiums for audit firms for their future (mandatory) professional indemnity insurance. Under English law, this is what would currently happen in such a scenario. However, despite the auditors being held 'responsible' for the economic loss suffered, it is highly unlikely that they would be held accountable due to auditor not being deemed sufficiently close (proximity) to investors (they merely owe a duty of care to the business whose accounts they audit, as discussed later). The following discussion will detail the mechanisms for why this would happen. It will then compare and contrast the English system for accounting negligence with the US system. Drawing on the contrasts and differences of the two systems, a discussion will detail the benefits and drawbacks of changing the English legal system to align more with the US'. Finally, an explanation of how English law could evolve to better foster trust and increase its reputation will be outlined.

In crafting this article, the methodology employed for the literature review was meticulous and purposeful. The selection process involved a comprehensive survey of scholarly articles, legal commentaries, and industry reports, ensuring a diverse and authoritative representation of perspectives. The criteria for inclusion centered on relevance to the research objectives, emphasizing works that addressed the nuances of auditor liability, professional negligence, and legal reforms within the financial domain. By aligning the literature selection with the research focus, this article aims to present a well-informed analysis, substantiating its arguments with a robust foundation of scholarly discourse. This deliberate approach enhances the transparency and overall rigor of the research, providing readers with a nuanced understanding of the legal landscape surrounding auditor accountability.

2. Auditors' liability: The Caparo case and the threefold test in focus

Hedley Byrne (Hedley Byrne & Co Ltd., 2021) set the foundation for negligence law to cover careless statements causing financial harm, even without a prior contract. However, it didn't involve audits. The 'threefold test' established in the landmark case of Caparo Industries plc v Dickman (1990), which established a precedent regarding auditors' liability to third parties, including investors. This landmark case introduced the "threefold test," requiring proximity, foreseeability, and reasonableness to establish a duty of care owed by auditors to third parties (Baker and Johnson, 2013). However, this test has been criticized for its narrow interpretation, making it difficult for investors to prove a duty of care and establish proximity with auditors (Rouas, 2022). It is the 'proximity' element of the test that prevents investors from being able to hold auditors professionally accountable.

The introduction of the foreseeability element by Caparo represents a crucial aspect of determining auditor liability for negligence. It ensures that before holding auditors accountable, it must be foreseeable that their actions or omissions would lead to harm for the party depending on their audit. While proving foreseeability in intricate financial matters poses a challenge and demands a substantial burden of proof, it ultimately reinforces a fair and rigorous standard for establishing liability.

One of the key components of the legal test, as established by Caparo, revolves around the inherent challenge faced by auditors in being held professionally accountable within the United Kingdom. The House of Lords, in their ruling on the Caparo case, emphasized the crucial role of the proximity of the relationship between the involved parties. The Lords clarified that auditors should be held liable only towards entities with a close and direct connection to them. As a result, this legal principle presents notable challenges for stakeholders or investors who do not possess direct contractual ties with the auditing firm, consequently limiting the scope of potential liability (Thompson and Clark, 2018). Indeed, it is this element of the test that is most criticized. In simple words, under English law, auditors only owe a duty of care to the company that has contracted with them to complete an audit. Investors and shareholders, who use the accounts as part of their due diligence process are not owed a duty of care, unlike in the United States (a comparison to the United States' legal framework will be made in the next section).

The 'test of fairness and reasonableness' in the context of auditors' liability introduces a critical dimension to the legal landscape. While it emphasizes the necessity of a duty of care to be just and reasonable, it also raises pertinent questions regarding the delicate balance between accountability and industry functionality.

The 'threefold test' in the Caparo case, specifically the requirement of proximity, has been a focal point of contention. Proving proximity, which essentially establishes a close and direct relationship between the auditors and the affected parties, has proven to be a significant challenge. In short, investors, who use audited accounts to make their financial decisions cannot bring a tortuous claim against auditors because of the 'lack of proximity.' This, in turn, means investors are not owed 'a duty of care' by auditors as they are classed as third parties. In other words, the auditors only owe a duty of care directly to the company whose accounts they audit. This narrow view of proximity has limited the ability of investors to establish a legal link between their interests and the actions of auditors, highlighting a critical flaw in the current legal framework surrounding auditors' liability.

The concern about the potential impact on the auditing profession is valid and requires careful consideration. Striking a balance between holding auditors accountable for negligence and preserving the integrity and efficiency of the auditing profession is a complex challenge. Overly burdensome liability could stifle auditors, inhibiting their ability to carry out their duties effectively. Conversely, too lenient an approach might undermine the very purpose of ensuring accountability and protecting stakeholders' interests.

The current constraint imposed by the 'proximity test' in the Caparo case regarding auditors' liability warrants a reassessment. It's evident that the existing narrow view, limiting liability to a direct duty of care only toward the audited company, overlooks the significant role investors play in the financial landscape. By affording auditors a broader duty of care encompassing third parties, especially investors relying on audited financial statements for crucial decisions, the legal framework can better reflect the practical reality of modern financial transactions. Such a shift would not only empower investors by holding auditors more accountable but also strengthen the overall trust and credibility in the auditing profession. Striking this balance is essential to ensure a fair and effective legal landscape while upholding the core principles of auditing integrity (Smith, 2009).

3. Comparative legal framework

The disparity in the legal expectations placed on auditors becomes stark when comparing the American legal system to its English counterpart, particularly concerning liability for professional negligence. Put simply, in the United States, "Auditors who are negligent in conducting their audit are liable for losses that result from reliance on misstated financial statements" (Schwartz, 1998). Auditors operate within a legal landscape that is notably more demanding in the US, characterised by rigorous regulations and an environment rich in litigation. Indeed, auditors were also shielded under the United States' law prior to the landmark case of Ultrameres (Ultramares Corp. v. Touche, 1931) where Chief Judge Cardozo opened the door to auditors being liable to third parties (Baker and Prentice, 2008). As summarised in the case of Giles v. General Motors, it was held that economic loss suffered by third parties because of negligence.

"Does not bar recovery in tort where the defendant had a duty imposed by law rather than by contract and where the defendant's intentional breach of that duty caused purely monetary harm to the plaintiff (Giles v. General Motors Accept, 2007)". In other words, the US has, since the 1930s, provided investors with the ability to hold auditors accountable for their negligence—allowing investors to seek compensation from the firm and/or the insurance company that professionally indemnifies the audit firm and the professionals within.

As well as case law in the United States, there is a well-defined legal landscape on negligence and liability, as discussed by Hassan et al. (2023) in the article discussing contract differences between international oil company exploration. In the US, two of the most fundamental pieces of legislation: the Securities Act (1933) and the Securities Exchange Act (1934) act to establish a comprehensive legal basis for auditors to be held accountable for the professional skills that they offer. The combination of government legislation and case law ensures a robust framework that effectively holds auditors accountable for the accuracy and fairness of the financial statements they audit. Under these acts, auditors are expected to meticulously adhere to stringent standards and procedures during the audit process. Furthermore, the legal landscape in the United States allows for investors, who have suffered financial loss because of the negligence made by professional auditors, to reclaim their losses from both the audit firm and the insurance company that insures the firm. This provides investors worldwide with more confidence when investing in the United States and is probably why the United States has far more FDI than the UK (OECD. 2023).

Regarding mitigating liability with contractual disclaimers, the UK and US law is remarkably different. In the UK, 'the Bannerman clause,' a clause first set out in the Scottish case of RBS v Bannerman (Royal Bank of Scotland Plc v Bannerman Johnstone Maclay, 2009) encapsulated the UK's stance. In short, the judge established that despite no direct communication between Bannerman (the auditor) and the third party, Bannerman's acquired knowledge during routine audit procedures was enough, in the absence of any disclaimer, to establish a duty of care toward the third party. In other words, the lack of a disclaimer was a significant factor reinforcing the judge's determination of a duty of care. This was later echoed in the case of Barclays Bank plc v Grant Thornton (2015) where The Commercial Court ruled that sophisticated commercial parties can relinquish liability to third parties with a contractual disclaimer. This led to auditing firms setting out disclaimers as a standard procedure, to absolve themselves from negligent liability (Rouas, 2022). In short, the UK case of Barclays Bank plc v Grant Thornton upheld the 'Bannerman disclaimer' detailed in the Scottish case of Bannerman (Royal Bank of Scotland Plc v. Bannerman Johnstone Maclay, 2005) stating that disclaimers can mitigate the tort of negligence. This provided a crucial precedent for auditors to protect against third-party claims. The important distinction to draw between the 'Bannerman clause' and that of the US' legal system, is that in the US, the Ultrameres case (Ultramares Corp. v. Touche, 1931) as summarised in Giles (United States District Court, Giles v. General Motors Acceptance Corp, 2007) set out that, liability can be established regardless of the contractual disclaimers. Whereas, the UK case of Barclays Bank plc v Grant Thornton (2015) established the legality and effectiveness of a 'Bannerman disclaimer' in audit reports. In other words, the law of tort can be a remedy for third parties in the US regardless of the contractual terms. However, in the UK, audit firms can absolve their responsibility with a disclaimer.

4. The evolving financial landscape and the call for legal reforms

The Audit Market in England: Size, Financial Volume, and Main Auditing Companies:

In addressing the call for legal reforms, it becomes imperative to delve into the specifics of the audit market in England. As of 2023, the market size, measured by revenue, of the Accounting & Auditing industry was £7.6 billion. This significant figure underscores the economic importance of auditing services. Furthermore, the financial volume of businesses subject to auditing and the main auditing companies operating in the English financial market play a crucial role in shaping the landscape. This subsection explores these dimensions, shedding light on the intricacies that demand a nuanced legal framework (IBISWorld, 2023).

Over the years, the global financial landscape has seen a significant evolution. Markets have become more integrated, interconnected, and complex. Foreign investments have surged, blurring national boundaries. In contrast, the Caparo test remains entrenched in a simpler time, struggling to adapt to the contemporary intricacies of international financial transactions and investments (House of Lords, 1990).

Beyond Caparo, the accountancy profession has devoted substantial time and resources to grapple with this concern. Their efforts have been aimed at formulating viable propositions to impose sensible boundaries on the financial implications associated with negligence claims, all while preserving the intrinsic value of the accountants' services. There have been numerous proposals for legal reform of auditor liability (Rouas, 2022).

The evolving global financial landscape necessitates a corresponding evolution in legal frameworks governing auditor negligence. English law, notably the Caparo test (House of Lords, 1990) should be critically reevaluated and adapted to contemporary demands. Failure to do so risks systemic inadequacies and compromises investor confidence, which is fundamental for economic prosperity and growth. A forward-looking, harmonized legal framework is crucial to meet the needs of the modern financial ecosystem and protect the interests of investors worldwide (Smith, 2009).

To remain competitive and uphold investor confidence, England must modernize its legal approach to auditor negligence. Reforms should encompass a broader duty of care owed to investors, aligning with international standards. A more proactive stance would deter negligence, thus nurturing a culture of prudence and accountability within the auditing profession (Thompson and Clark, 2018).

Arguably the following three areas of law are the most crucial to address:

4.1. Reforming joint and several liability

English law's perceived inferiority lies in its inability to adequately protect investors, both domestic and foreign. A reluctance to evolve the legal framework can be seen as a form of systemic failure. The law must adapt to safeguard the interests of investors who place trust in the financial system, thus fostering confidence and promoting economic growth (Smith, 2009).

In the literature concerning professional negligence (Baker and Johnson, 2013), a prevalent suggestion is the reformation of the existing joint and several liability systems. This system allows successful claimants to recover their entire losses from any negligent party involved.

An alternative proposed approach, often seen in the US advocates for a shift towards proportionate liability (Morris, 2009) where each negligent party is held accountable based on their contribution to the incurred loss or damage. Despite the merits of proportionate liability, I argue that overhauling this system is less pressing than reforming the proximity test established in the Caparo case. The joint and several liability systems offers a level of safeguard to investors, enabling them to hold one negligent professional accountable for the entire loss if fault is proven. This aspect provides a protective measure for investors, although it also incentivizes insurers to exercise greater diligence when underwriting new clients.

Arguably, the ramifications of such changes could also protect investors in newer and emerging industries and technologies, such as cryptocurrency. It is imperative to protect these technologies and industries. Indeed, in the article, parallels between the challenges in regulating cryptocurrency, as revealed by Dhali et al. (2023) in their exploration of cryptocurrency in the Darknet, discussed the intricacies of the audit profession. The current joint and several liability systems, while providing a safeguard for investors by allowing them to hold one negligent professional accountable for the entire loss, may not be fully equipped to address the multifaceted risks presented by emerging financial technologies like cryptocurrency. The findings from Dhali et al. underscore the need for a comprehensive reform, such as the one proposed in this article, that extends beyond the traditional bounds of joint and several liability. The proposal can help mitigate against future unknown (at present) threats from negligent accounting which would fortify the financial domain-giving investors and markets further confidence and integrity. Such reforms are crucial not only for protecting investor interests but also for maintaining trust and resilience in the face of a rapidly transforming financial landscape.

4.2. Narrowing proximity and providing more clarity

The need for reform within the auditing landscape is underscored by a crucial factor: the proximity test originating from the Caparo case. This test presently operates as a shield, safeguarding auditors from being held accountable to investors for potential negligence, despite investors heavily relying on their professional expertise in auditing financial accounts. As investors heavily hinge their financial decisions on the accuracy and reliability of these accounts, having a well-defined and robust test for professional negligence becomes paramount.

The proximity test, as it stands, often poses challenges in establishing the necessary closeness of the relationship between auditors and investors. Its current interpretation can potentially limit the scope of accountability and hinder investors' ability to seek redress for errors or negligence that have a direct impact on their investments. In a dynamic and fast-evolving financial landscape, this calls for a reevaluation of the test and a critical examination of how it can be refined to better serve the interests of investors and maintain the integrity of the auditing profession.

One potent avenue for enhancing the effectiveness of the proximity test is through legislative action. Enshrining a more precise and comprehensive proximity test within statutory frameworks would provide clarity and specificity, leaving little room for divergent interpretations. A statutory approach would help define the boundaries of liability more clearly, ensuring auditors are held accountable where their actions or inactions have directly influenced the financial decisions and well-being of investors.

Moreover, a legislative update to the proximity test can act as a catalyst for a more standardised approach, harmonising the interpretation and application of the test across various jurisdictions. This consistency is vital in establishing a robust and dependable framework that fosters trust in the auditing process and promotes confidence among investors, ultimately bolstering the functioning of financial markets.

In summary, the proximity test, given its central role in determining auditors' liability, demands a recalibration to better align with the modern complexities of financial transactions and investor reliance. A legislative intervention to refine and clarify this test would serve as a crucial step toward reinforcing accountability within the auditing profession and ensuring that investors' interests are adequately protected. It's imperative to prioritise this reform to fortify the foundations of trust and integrity upon which financial markets thrive.

4.3. Contractual limitation of liability

When negligence claims arise, insurance companies are often the entities responsible for covering the liabilities of the parties involved, including professionals like auditors. However, nuances within the negligence laws may provide grounds for the insurance company to contest or deny payouts. This could be due to specific clauses, exemptions, or interpretations of the law that enable insurers to limit their liability, delay payments, or altogether avoid compensating the affected parties.

This interaction between the legal system and insurance practices highlights the need for a comprehensive understanding of the legal landscape and its implications on risk management and insurance coverage. Professionals, including auditors, need to be acutely aware of these dynamics to navigate potential gaps or limitations in insurance coverage effectively. Furthermore, as discussed above, the United States' legal system could be used as a model, whereby economic loss suffered by third parties, because of negligence,

"Does not bar recovery in tort where the defendant had a duty imposed by law rather than by contract and where the defendant's intentional breach of that duty caused purely monetary harm to the plaintiff (United States District Court, Giles v. General Motors Accept, 2007)."

5. Implementing reforms

The need to revamp the legal landscape governing professional negligence liability for auditors is urgent and imperative. The sooner England updates its current laws surrounding the professional negligence of accountants auditing accounts, the sooner it will entice more foreign direct investment and improve its standing, truly living up to its reputation as the global financial hub.

Theoretically, the law could evolve organically with case law. However, arguably the best way to revamp the current inadequate law is to pass an Act of Parliament in the United Kingdom to hold accountants professionally negligent to investors for audited accounts. To enhance the efficacy and relevance of the law regarding professional negligence of auditors in England, there are several things that a new statute setting out professional negligence and defining it should consist of. Firstly, the statute should have a clearer definition of the auditor's duty of care. Finally, there have been a number of articles that encourage the collaboration between regulatory bodies, professional associations, and audit firms to establish a centralized database of best practices which would enable the profession as a whole to learn from previous audit failures that could significantly contribute to raising the bar of auditing standards in the UK as a whole (Thompson and Clark, 2018).

As noted in The Modern Law Review (Morris, 2009) various efforts have been undertaken to navigate the intricate landscape of professional negligence, particularly in the context of auditing. Indeed, the Companies Act 2006 changed the law significantly, which further strengthened the 'Bannerman Clause' concept, allowing audit firms to limit their liability towards clients through contractual agreements. It also introduced a criminal offence where a person:

"Knowingly or recklessly causes a report under section 495 (auditor's report on company's annual accounts) to include any matter that is misleading, false or deceptive in a material particular (Companies Act, 2006)."

However, the Companies Act (2006) does nothing to allow third parties who relied on negligent audits to recover their funds.

The Act's inability to effectively address critical issues within the scope of professional negligence and auditing emphasizes the pressing need for streamlined and efficient legal structures to govern these domains. A legal framework that is too cumbersome to serve its purpose ultimately necessitates a reevaluation and reconstruction to ensure clarity, effectiveness, and desired outcomes (Morris, 2009). Embarking on the path of legislative reforms demands a nuanced understanding of audit companies' perspectives on proposed changes. Engaging with these firms is essential to grasp the practical implications, challenges, and potential benefits linked to suggested legal modifications. Further, in considering the challenges associated with implementing reforms in the legal framework, it is also crucial to draw insights from diverse sectors, such as healthcare. Hassan et al. (2021) have extensively explored the regulatory challenges related to big data and predictive analytics in healthcare in Bangladesh. This parallel examination underscores the importance of foreseeing and addressing potential obstacles in the reform process concerning auditors' liability. Regulatory challenges in healthcare, especially those associated with the use of advanced technologies, share commonalities with the complexities faced in the audit profession. Issues related to data security, privacy, and adapting legal frameworks to rapidly evolving technologies are pertinent considerations. By learning from the regulatory challenges in healthcare, the legal reforms for auditors can incorporate measures to mitigate potential risks, enhance adaptability, and ensure the effectiveness of the updated legal landscape.

6. Potential impact of changing the law

Reforming the legal framework governing auditor liability for negligence in the UK can have far-reaching implications. By establishing a clearer and more expansive duty of care owed by auditors to stakeholders, including investors, the law can significantly enhance accountability within the auditing profession (Smith, 2009). This could lead to a higher level of due diligence and scrutiny in financial reporting, ultimately improving financial transparency and bolstering investor confidence (Smith, 2009). Moreover, a reformed legal framework could potentially deter negligent practices among auditors, fostering a culture of prudence and responsibility.

While advocating for crucial legal reforms aimed at enhancing auditor liability, it is essential to approach the issue with a clear understanding of potential drawbacks. One prominent concern centres around the potential escalation of litigation and the associated financial burdens, a consequence of broadening the duty of care imposed on auditors (Thompson and Clark, 2018). The fear is that an expansive duty of care could trigger an upsurge in lawsuits, leading to increased legal costs for auditing firms.

This rise in litigation can indeed impose substantial financial strain on auditing firms, potentially affecting their operational dynamics and resource allocation. The added financial burden may force firms to reevaluate their risk management strategies and potentially shift priorities to navigate this new legal landscape. Striking a delicate balance between enhancing auditors' accountability and ensuring the efficient functioning of the auditing process is of paramount importance.

The challenge lies in finding a middle ground where auditors are held accountable for their actions, yet the legal framework does not suffocate the auditing profession with excessive legal constraints. It requires a thoughtful and judicious calibration of the duty of care, ensuring that it serves its intended purpose of safeguarding stakeholders' interests without unnecessarily hindering the auditing process. Achieving this balance will be instrumental in promoting both trust and efficiency within the financial ecosystem, fostering a symbiotic relationship between legal reforms and the auditing profession's integrity.

7. Conclusion

In conclusion, the imperative for a radical shift in England's legal approach to professional negligence, particularly within the realms of accounting and audit, cannot be overstated. The current proximity test, as established in the Caparo case (House of Lords, 1990), stands as a glaring impediment, shielding auditors from their rightful accountability to investors for negligence. This protection, despite the pivotal aspect of investors entrusting them with auditing accounts, is unacceptable and calls for immediate rectification.

Investors, whose financial decisions hinge crucially upon the accuracy and reliability of audited accounts, deserve a legal framework that leaves no room for ambiguity. A resolute and well-defined test for professional negligence is not just an option but an imperative. Aligning English law with established international standards is non-negotiable. It not only sets the benchmark for professionalism but grants victims the power to seek compensation through professionals' insurance. This single stride can significantly amplify trust and transparency within the financial domain, providing a strong foundation for a robust and reliable financial landscape.

The path to this transformation is clear - it necessitates the swift enactment of new legislation, a comprehensive Act of Parliament that unequivocally defines the duty of care auditors owe to investors and third parties. This legislation should embody the spirit of accountability and justice, leaving no room for ambiguity or evasiveness. The United States' legal system could be used as a benchmark, whereby economic loss suffered by third parties does not bar recovery in tort where the defendant had a duty imposed by law, rather than by contract, and where the defendant intended breach of duty causes financial damage. (United States District Court, Giles v. General Motors Accept, 2007)."

By the UK fostering greater accountability, transparency, and, above all, investor trust, the envisioned legal changes have the power to reshape the auditing landscape fundamentally. The UK has an unparalleled opportunity to lead the global financial arena by embracing a proactive legal approach. It's a moment for British law to stand tall, prioritizing the interests and confidence of investors and welcome a new era of accountability and transparency.

In addition to the practical imperatives outlined, this research makes significant strides in advancing existing theories surrounding auditor accountability. By critically examining the shortcomings of the proximity test and proposing legislative changes, the study contributes theoretically to the discourse on professional negligence. The identification of a clear and defined duty of care owed by auditors to investors challenges conventional legal perspectives, enriching the theoretical understanding of auditors' responsibilities. The comparative analysis with the United States' legal system provides a theoretical framework for reconsidering established norms. Emphasizing the need for a proactive legal approach, this research redefines theoretical expectations within the auditing profession, emphasizing the transformative potential of legal reforms on a broader theoretical landscape. The proposed legislative changes not only address practical concerns but also mark a theoretical paradigm shift, redefining the contours of accountability in auditor negligence within the global legal context.

In unequivocal terms, the UK must urgently and resolutely reevaluate and reform its legal framework governing auditor negligence. This is not just a legal necessity; it is a call to action for the very essence of trust and integrity upon which financial markets thrive. It is time for the UK to legislate to increase investor confidence in the UK and drive up Foreign Direct Investment.

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