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# *The Liability of Auditors beyond Their Clients: A Comparative Study*

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Lara Khoury\*

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The constant evolution of the importance of auditors' functions during the twentieth century brought with it considerable scholarship on their responsibility. Indeed, confronted with the insolvency of a company in which they have invested, shareholders, investors, and offerors increasingly seek to recover their economic loss from auditors who, solvent and insured, were negligent in auditing the financial statements of the company in question. Accordingly, the study of the liability of an auditor towards third parties has a growing importance. In this article the author analyzes comparatively auditors' liability under the common law of England and Canada and under the civil law of France and Quebec. Specifically, she attempts to show how courts use the duty of care in the common law and causality in the civil law to limit this liability. Furthermore, she pays particular attention to the influence of Canadian, English, and French law on the law of Quebec. The author not only delineates this influence, but also comments on the extent to which the law of Quebec may legitimately take inspiration from the English and Canadian common law and the civil law of France in the area of auditors' liability to third parties.

L'évolution constante de l'importance des fonctions du vérificateur comptable a entraîné durant le XX<sup>e</sup> siècle une recherche accrue de sa responsabilité. En effet, face à l'insolvabilité de la compagnie dans laquelle ils ont investi, les actionnaires, les investisseurs et les pollicitants cherchent de plus en plus à recouvrer leur dommage économique auprès du vérificateur comptable, solvable et assuré, ayant été négligent dans la vérification des états financiers de la compagnie en question. Cette situation rend l'étude de la responsabilité des vérificateurs comptables envers les tiers d'un intérêt grandissant. Dans le présent texte, l'auteure analyse de façon comparative les règles régissant cette dernière en common law anglaise et canadienne, ainsi qu'en droit civil français et québécois. Plus précisément, elle entreprend de démontrer comment les concepts de *duty of care* en common law, et de causalité en droit civil, ont été utilisés par les tribunaux afin de limiter cette responsabilité. De plus, une attention particulière est portée à l'influence du droit des juridictions canadienne, anglaise et française sur le droit québécois dans ce domaine. L'auteure tente non seulement de décrire cette influence, mais également de se prononcer quant à l'inspiration que le droit québécois peut légitimement tirer de la common law canadienne et anglaise et du droit civil français dans le domaine de la responsabilité des vérificateurs envers les tiers.

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\* LL.B. (Sherbrooke); B.C.L. (Oxon.); candidate to the D.Phil. degree at the University of Oxford; Boulton Junior Research Fellow, Faculty of Law, McGill University; Lecturer, Faculty of Law, University of Sherbrooke. This article is based on the text of a thesis submitted in partial fulfillment of the requirement for the B.C.L. at Oxford. The author wishes to thank Dr. Simon Whittaker, Professor Suzanne Philips-Nootens, and Mr. Colin West for their helpful comments on an earlier version of this text.

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## Introduction

### I. Auditing: A Profession in Context

- A. *The General Role of Auditors*
- B. *Professional Organization of the Auditing Profession*
  - 1. The English and Canadian Professional Organization
  - 2. The French *Commissariat aux Comptes*
- C. *Statutory Context*
  - 1. The Conduct of an Audit in England and Canada
  - 2. The Certification of Accounts by the *Commissaire aux Comptes*

### II. The Common Law

- A. *Duty of Care and Pure Economic Loss in the Law of Negligence*
- B. *Auditors' Liability towards Third Parties in England and Canada*
  - 1. The Search for a Test
    - a. *England*
      - i. The Existence of a Duty of Care
      - ii. The Restriction on the Scope of the Duty of Care
    - b. *Canada*
      - i. *Haig v. Bamford*: The Incorporation of *Hedley Byrne*
      - ii. *Hercules*: The Reign of *Anns*
  - 2. Knowledge of the Plaintiff and the Contemplated Transaction
    - a. *The Scope of the Limited Class*
    - b. *The Scope of the Transaction*
  - 3. The Reliance/Reasonable Reliance Requirement
  - 4. Policy Considerations
- C. *Conclusion*

### III. The Civil Law

- A. *France and Quebec: The Juridical Context*
  - 1. Quebec: Tensions and Influences in a Mixed System
  - 2. *Responsabilité Civile*: General Features
    - a. *General Principle of Liability*
    - b. *The Causation Requirement*
      - i. The Efforts of the Theorists and the Subjectivity of the Courts
      - ii. The Problem of the *Victime par Ricochet*
    - c. *Pure Economic Loss*
- B. *The Liability of the Commissaire aux Comptes towards Third Parties*
  - 1. Assessment of Causation
  - 2. Causation as a Restrictive Tool
  - 3. Similarities with the Common Law

- C. *The Quebec Auditor and Third Parties*
  - 1. The Existence of the Causal Link
  - 2. Causation as a Restrictive Tool
  - 3. The Influence of the Common Law
- D. *Conclusion*

#### **IV. Quebec: At the Border of Civil Law and Common Law**

- A. *The Restrictive Approach*
- B. *The Use of Common Law Concepts*
  - 1. Reasonable Reliance
  - 2. Foreseeability of Reliance and Knowledge of the Plaintiff and the Purpose of the Financial Statements
  - 3. Policy Considerations
- C. *Causation as a Sufficient Limiting Device*

#### **Conclusion**

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## Introduction

Over the last hundred years, the accounting profession has evolved greatly. Modern accountants, once only bookkeepers, have gradually been attributed a large range of responsibilities. They now not only prepare, investigate, and audit accounts, but also perform important advisory, reporting, investigatory, regulatory, and administrative functions.<sup>1</sup> This new diversity in their functions exposes them to a greater risk of liability towards a larger range of people:

The increasing growth and changing role of corporations in modern society has been attended by a new perception of the societal role of the profession of accounting. The day when the accountant served only the owner-manager of a company and was answerable to him alone has passed. The complexities of modern industry combined with the effects of specialization, the impact of taxation, urbanisation, the separation of ownership from management, the rise of professional corporate managers, and a host of other factors, have led to marked changes in the role and responsibilities of the accountant, and in the reliance which the public must place upon his work. The financial statements of the corporations upon which he reports can affect the economic interests of the general public as well as of the shareholders and potential shareholders.<sup>2</sup>

Hence, the question of auditors' liability towards persons other than their clients' has assumed great practical importance. Following the collapse of a company, third parties frequently attempt to recover their losses from a solvent and insured auditor. Faced with such claims, the common and civil law courts had to struggle between two conflicting interests: the public's interest in the independent and competent review of financial statements and the interest of the auditing profession in carrying out its function without the burden of a potentially overwhelming liability. The following comparative analysis examines the nature of the different conceptual devices by which the common law courts of England and Canada and the civil law courts of France have attempted to balance these interests and to keep auditors' third party liability within proper boundaries. Attention is also given to the Canadian province of Quebec, which is of particular interest by reason of the influence of the common law on its civil law system. Ultimately, this comparative analysis will attempt to provide proper guidelines for dealing with the question of auditors' liability towards third parties in the legal system of Quebec.

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<sup>1</sup> R.M. Jackson & J.L. Powell, *Professional Negligence*, 4th ed. (London: Sweet & Maxwell, 1997) at 804.

<sup>2</sup> *Haig v. Bamford* (1976), [1977] 1 S.C.R. 466 at 475-76, 72 D.L.R. (3d) 68 [hereinafter *Haig* cited to S.C.R.].

<sup>3</sup> The word "client" is not meant to have a contractual connotation, but rather refers to an audited person or company.

## I. Auditing: A Profession in Context

At first sight it may appear futile to undertake a comparative analysis of legal systems that evolve in different social, cultural, and economic contexts. Such an exercise can nevertheless be useful, not only in providing a better understanding of one's own legal system, but also as a "theatre of observation" permitting one, through examination of how other legal systems at a comparable stage of social and economic development have dealt with similar problems, to find one's "own paths through 'the forest'."<sup>4</sup> One must, however, avoid engaging in such a comparative venture without a clearer understanding of the context in which each system has evolved. It would, consequently, be ill-advised to undertake the present study without painting a broader picture of the professional and regulatory context in which auditing is carried out in the four jurisdictions studied. The following section therefore considers the organization of the auditing profession, as well as the different aspects of the conduct of audits in these four legal systems.

### A. The General Role of Auditors

The content of auditors' duties varies from one jurisdiction studied to another. There is, however, one substantial role that is central to all auditors: the control<sup>5</sup> of a company's financial statements and reporting to its shareholders, directors, and officers.<sup>6</sup>

Auditors' control over a company's financial statements is traditionally viewed as having a dual aim. First, it enables the company's directors and officers to ensure that they can safely rely on the financial statements in taking managerial decisions. In addition, the financial statements' accuracy and reliability are key to the shareholders' ability to evaluate the strengths and weaknesses of the enterprise, to assess whether the corporation is managed with competence and honesty, and to make informed in-

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<sup>4</sup> J.P. Dawson, cited in M.A. Glendon, M.W. Gordon & C. Osakwe, *Comparative Legal Traditions* (St. Paul, Minn.: West Publishing Company, 1994) at 10.

<sup>5</sup> This broad word is used here since the nature of auditors' control varies in each jurisdiction.

<sup>6</sup> See Jackson & Powell, *supra* note 1 at 809; *Caparo Industries v. Dickman*, [1990] 2 A.C. 605 at 660, [1990] 1 All E.R. 568 (H.L.) [hereinafter *Caparo* cited to A.C.]; F. Iacobucci, M.L. Pilkington & J.R.S. Prichard, *Canadian Business Corporations* (Agincourt: Canada Law Book, 1977) at 403; J.M. Morin, "Aspects de la responsabilité du commissaire aux comptes" (1996) *Affiches Parisiennes* 18 at 18; J. Monéger & T. Granier, *Le commissariat aux comptes* (Paris: Dalloz, 1995) at 17; Y. Guyon, *Droit des affaires*, 8th ed. (Paris: Economica, 1994) at 369; Y. Guyon & G. Coquereau, *Le commissariat aux comptes: aspects juridiques et techniques* (Paris: Litec, 1971) at 277; Compagnie Nationale des Commissaires aux Comptes, *La responsabilité civile du commissaire aux comptes* (Paris: Encyclopédie d'études juridiques, 1995) at 8; *Guardian Insurance Company of Canada v. Sharp*, [1941] S.C.R. 164 at 169, [1941] 2 D.L.R. 417 [hereinafter *Guardian* cited to S.C.R.].

vestment decisions.<sup>7</sup> Second, full and accurate disclosure is essential to third parties who might have access to, and rely on, the company's reports in making financial decisions. Prospective purchasers of shares, potential investors, banks, suppliers, sureties, lenders, and public authorities have a substantial interest in the auditors' work, since it is very often the only objective and independent source of information available to them.

## **B. Professional Organization of the Auditing Profession**

At the outset, it must be observed that the similarities between the English and Canadian professional and statutory contexts justify a joint treatment of these two jurisdictions. Moreover, in Canada, these contexts have been harmonized to such an extent that dissimilarities between the provinces are usually minor.<sup>8</sup> The different background in which French auditors perform their duties, however, necessitates a distinct analysis.

### **1. The English and Canadian Professional Organization<sup>9</sup>**

In England and Canada, the conduct of audits is generally reserved to members of specific professional accounting bodies. These bodies are created by law to ensure the protection of the public and the integrity of the profession and to regulate some aspects of the exercise of the profession. The English *Companies Act 1989*<sup>10</sup> provides that a company's auditor must be a member of a Recognised Supervisory Body<sup>11</sup> and

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<sup>7</sup> On this dual aim, see *Caparo, ibid.* at 630, Lord Oliver.

<sup>8</sup> *Abbyad et al., La vérification. Une approche intégrée* (Gaëtan Morin, 1994) at 98. The *Constitution Act, 1867* (U.K.), 30 & 31 Vict., c. 3, s. 92(13), reprinted in R.S.C. 1985, App. II, No. 5, grants to the provinces the competence for the regulation of professions. See P.W. Hogg, *Constitutional Law of Canada*, looseleaf, vol. 1 (Scarborough: Carswell, 1997) at 21-6. Each province has enacted its own statutes governing the accounting and auditing professions and created its own professional bodies, but the existence of a national professional body, the Canadian Institute of Chartered Accountants [hereinafter CICA], has greatly contributed to the harmonization of the profession across the country.

<sup>9</sup> The statutes of seven Canadian provinces are studied, namely those of Alberta, British Columbia, Manitoba, New Brunswick, Nova Scotia, Ontario, and Quebec.

<sup>10</sup> (U.K.), 1989, c. 40 [hereinafter *CA 1989*]. The *CA 1989* implemented a new system to conform with the EU's Eighth Company Law Directive on the regulation of auditors. See S.W. Mason, D. French & C. Ryan, *French & Ryan on Company Law*, 14th ed. (London: Blackstone Press, 1997-98) at 521; J. Birds *et al.*, *Boyle & Birds' Company Law*, 3d ed. (Bristol: Jordans, 1995) at 402.

<sup>11</sup> This category includes the Institute of Chartered Accountants in England and Wales [hereinafter ICAEW], the Institute of Chartered Accountants of Scotland, the Chartered Association of Certified Accountants, the Institute of Chartered Accountants in Ireland, and the Association of Authorised Public Accountants.

be eligible for appointment under the rules of that body.<sup>12</sup> Auditors must also hold appropriate qualifications,<sup>13</sup> usually granted by Recognised Qualifying Bodies.<sup>14</sup> In Canada, the auditing practice is also reserved to specific professionals, who are usually Chartered Accountants.<sup>15</sup> In some provinces, however, other accountants<sup>16</sup> as well as non-accountants<sup>17</sup> can also perform audits.

Auditors must have professional insurance<sup>18</sup> and can exercise their functions individually or in partnership.<sup>19</sup> Additionally, since the adoption of the *CA 1989*, English

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<sup>12</sup> *CA 1989*, *supra* note 10, ss. 25, 30, Sch. 11, para. 4. On eligibility, see Mason, French & Ryan, *supra* note 10 at 521-22; G. Morse, *Charlesworth & Morse Company Law*, 15th ed. (London: Sweet & Maxwell, 1995) at 555-63; Birds *et al.*, *supra* note 10 at 402.

<sup>13</sup> *CA 1989*, *ibid.*, ss. 31-34, Sch. 11-2.

<sup>14</sup> *Supra* note 11, with the exception of the Association of Authorised Public Accountants.

<sup>15</sup> See *e.g.* *Chartered Accountants Act*, R.S.Q. c. C-48, ss. 2, 19, 24 [hereinafter *QCAA*]; *Professional Code*, R.S.Q. c. C-26, s. 32; *Code of Ethics of Chartered Accountants*, R.R.Q. 1981, c. C-48, r. 2, s. 1.01(d) [hereinafter *QCE*]. In Quebec other accountants are allowed to undertake audits in limited cases (*QCAA*, *ibid.*, ss. 24, 27-28).

<sup>16</sup> See *Company Act*, R.S.B.C. 1996, c. 62, s. 180 [hereinafter *BCCA*]; *Public Accountancy Act*, R.S.O. 1990, c. P37, ss. 7, 14(1), 24(1) [hereinafter *OPAA*].

<sup>17</sup> In Alberta it is not required to be an accountant unless the audit is intended to be relied on by a third party (*Certified Management Accountants Act*, S.A. 1987, c. C-3.8, s. 2(1) [hereinafter *ACMAA*]; *Chartered Accountants Act*, S.A. 1987, c. C-5.1, s. 2(1) [hereinafter *ACAA*]; *Certified General Accountants Act*, S.A. 1987, c. C-3.6, s. 2(1) [hereinafter *ACGAA*]). See also B. Welling, *Corporate Law in Canada: The Governing Principles*, 2d ed. (Toronto: Butterworths, 1991) at 595.

<sup>18</sup> See England: ICAEW's Professional Indemnity Insurance Regulations, *The ICAEW Members Handbook 1995*, vol. 1, 1.309, 341; Canada: *Bylaws*, s. 251, online: Institute of Chartered Accountants <[http://www.ica.bc.ca/pdf/bylaws\\_2000.pdf](http://www.ica.bc.ca/pdf/bylaws_2000.pdf)> (date accessed: 4 February 2001); *ICAO Bylaws*, s. 700, online: Institute of Chartered Accountants of Ontario <<http://www.icao.on.ca/public/handbook/bylaws/bylaws700.html>> (date accessed: 4 February 2001); *Mandatory Professional Liability Insurance Regulation*, online: The Institute of Chartered Accountants of Ontario <<http://www.icao.on.ca/public/handbook/regulations/mpli.html>> (date accessed: 21 February 2001); *ICAO Rules of Professional Conduct*, online: The Institute of Chartered Accountants of Ontario <<http://www.icao.on.ca/public/handbook/RULES95.html>> (date accessed: 21 February 2001), adopted under the authority of *The Chartered Accountants Act, 1956*, S.O. 1956, c. 7, s. 8 [hereinafter *OCAA*]; *Bylaws and Regulations*, s. 701, online: The Institute of Chartered Accountants of Manitoba <<http://www.icam.mb.ca/bylaws/#700>> (date accessed: 21 February 2001); *Ordre des comptables agréés du Québec (Professional Liability Insurance) Regulation*, R.R.Q. c. C-48, r. 1.1.

<sup>19</sup> See England: *CA 1989*, *supra* note 10, s. 26; Canada: *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 2(1) [hereinafter *CBCA*]; *Business Corporations Act*, S.A. 1981, c. B-15, s. 1(1)(c.1) [hereinafter *ABCA*]; *BCCA*, *supra* note 16, ss. 1(1); *Corporations Act*, R.S.M. 1987, c. C-225, s. 1(1) [hereinafter *MCA*]; *Business Corporations Act*, N.B.A. 1981, c. B-9.1, s. 1(1) [hereinafter *NBBCA*]; *Companies Act*, R.S.N.S. 1989, c. 81, s. 2(1)(aa), as am. by *Business Efficiency (1998) Act*, S.N.S. 1998, c. 8, ss. 16-21 [hereinafter *NSCA*]; *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 1(1) [hereinafter *OBCA*]; *QCE*, *supra* note 15, s. 1.01(b).

auditors can also carry out their business by forming a body corporate.<sup>20</sup> The same applies to auditors in Alberta,<sup>21</sup> British Columbia,<sup>22</sup> New Brunswick,<sup>23</sup> and Nova Scotia.<sup>24</sup> Moreover, recent developments now allow accountants of England, Ontario, and Alberta to carry on their practice through a "limited liability partnership".<sup>25</sup>

## 2. The French *Commissariat aux Comptes*

In France, the organization of the auditing profession, as well as the carrying out of the *certification* of financial documents, is strictly regulated by an important legal body constituted by the *Loi n° 66-537 du 24 juillet 1966 sur les sociétés commerciales*<sup>26</sup> and other statutes,<sup>27</sup> *décrets*,<sup>28</sup> and *ordonnances*.<sup>29</sup>

Only one type of independent professional is entitled to carry out *certification*, the *commissaire aux comptes*<sup>30</sup> registered with the Commission of Inscription.<sup>31</sup> Any per-

<sup>20</sup> See CA 1989, *ibid.*, s. 53(1).

<sup>21</sup> See ACMAA, *supra* note 17, s. 2(1); ACAA, *supra* note 17; ACGAA, *supra* note 17.

<sup>22</sup> See BCCA, *supra* note 16, s. 180. Only in British Columbia does this incorporation carry with it limited liability in respect of professional liability claims. In other provinces this is either forbidden directly (*Public Accountants Act*, R.S.N.S. 1989, c. 369, as am. by S.N.S. 1994, c. 30, s. 22A [hereinafter *NSPAA*]), or indirectly by provisions precluding accountants from attempting to elude their personal liability (ACAA, *ibid.*, s. 28(1); ACMAA, *ibid.*, s. 28(1); NBBCA, *supra* note 19, s. 22(1); QCE, *supra* note 15, s. 3.01.06). In Ontario the exercise of public accountancy by a body corporate is explicitly prohibited. See OPAA, *supra* note 16, s. 24(1); ICAO *Rules of Professional Conduct*, *supra* note 18, s. 408.

<sup>23</sup> *Certified General Accountants Act*, N.B.A. 1986, c. 86, s. 2(1); *Chartered Accountants' Act 1986*, N.B.A. 1986, c. 87, ss. 20(1)ff.

<sup>24</sup> NSPAA, *supra* note 22, s. 22.

<sup>25</sup> A partner in a limited liability partnership or LLP is not individually liable for the negligence of another partner. The negligent partner's assets and the partnership's assets are the only ones submitted to a claim in damages. See *Limited Liability Partnerships Act 2000* (U.K.), 2000, c. 12; *Partnership Act*, R.S.A. 1980, c. P-2, ss. 11.1, 79.1-79.996; *Partnerships Act*, R.S.O. 1990, c. P5, ss. 10, 44.1-44.4. See OCAA, *supra* note 18, s. 13.1, added by *Partnerships Statute Law Amendment Act, 1998*, S.O. 1998, c. 2, s. 10. Demands for the introduction of LLPs are currently being made by professionals in other provinces. See also *Partnership Act*, R.S.B.C. 1996, c. 348, Part 3.

<sup>26</sup> J.O., 26 July 1966, as am. by 19 October 1986, 609 [hereinafter *Loi de 1966*].

<sup>27</sup> See *Loi n° 70-1300 du 31 décembre 1970*, J.O., 1 January 1971 [hereinafter *Loi de 1970*]; *Loi n° 84-148 du 1 mars 1984*, J.O., 2 March 1984, 1705 [hereinafter *Loi de 1984*].

<sup>28</sup> See *Décret n° 69-810 du 12 août 1969*, J.O., 29 August 1969, as am. by 12 September 1969, 832 [hereinafter *Décret de 1969*]; *Décret n° 85-295 du 1 mars 1985*, J.O., 5 March 1985, 593 [hereinafter *Décret de 1985*].

<sup>29</sup> *Ordonnance n° 67-821 du 23 septembre 1967*, J.O., 28 September 1967, 589 [hereinafter *Ordonnance de 1967*]; *Ordonnance n° 45-2138 du 19 septembre 1945*, J.O., 21 September 1945 as am. by 30 September 1945 [hereinafter *Ordonnance de 1945*].

<sup>30</sup> See *Décret de 1969*, *supra* note 28, s. 2.

son who satisfies the requirements set out in sections 3 to 7 of the *Décret de 1969* can be inscribed, but in practice the great majority of *commissaires aux comptes* are also *experts-comptables* (accountants). In fact, the same individual can hold simultaneously the status of *expert-comptable* and *commissaire aux comptes*, and exercise both functions, albeit not within the same *société*.<sup>32</sup>

Every *commissaire aux comptes* is a member of a national association called the Compagnie Nationale des Commissaires aux Comptes, as well as of a regional company that comes under the authority of the latter.<sup>33</sup> These are private bodies to which certain public functions are granted, such as the control of the exercise of the profession.<sup>34</sup>

A *commissaire aux comptes*, who has an obligation to hold professional insurance,<sup>35</sup> can be either a physical person or a *société de commissaires aux comptes*.<sup>36</sup> No specific form of *société* is imposed by the *Loi de 1966*.<sup>37</sup> The *société* undertakes legal liability *in solidum* with any *commissaire* held to be at fault.<sup>38</sup>

### C. Statutory Context

#### 1. The Conduct of an Audit in England and Canada<sup>39</sup>

In England the conduct of an audit is regulated by two main statutes, the *Companies Act 1985*<sup>40</sup> and the *CA 1989*. In Canada, it is regulated either by the *CBCA*, a federal statute, or by provincial legislation,<sup>41</sup> which sometimes follows the federal scheme closely.

<sup>31</sup> See *Loi de 1966*, *supra* note 26, ss. 218-29; *Ordonnance de 1945*, *supra* note 29, s. 22; *Décret de 1969*, *ibid.*

<sup>32</sup> There would otherwise be a breach of the requirement of independence. See text accompanying note 72. See Monéger & Granier, *supra* note 6 at 23.

<sup>33</sup> See *Décret de 1969*, *supra* note 28, s. 26.

<sup>34</sup> Monéger & Granier, *supra* note 6 at 23, 24.

<sup>35</sup> See *Décret de 1969*, *supra* note 28, s. 84; *Loi de 1984*, *supra* note 27, s. 234.

<sup>36</sup> See *Loi de 1966*, *supra* note 26, s. 218.

<sup>37</sup> They cannot, however, form a *société en nom collectif*, since all *associés* of this type of *société* are *commerçants*, which is not allowed by the *Loi de 1966*, *ibid.*, s. 219-3.

<sup>38</sup> See *Décret de 1969*, *supra* note 28, s. 69; J.F. Barbiéri, *Commissariat aux comptes* (Paris: Joly, 1996) at 18 [hereinafter *Commissariat aux comptes*]; Monéger & Granier, *supra* note 6 at 161. The *in solidum* obligation compels every debtor to perform the whole obligation. The debtor who does so, however, has a remedy against the other for the part to which that other is obliged.

<sup>39</sup> Only statutory audits are the concern of this section and no mention is made of contractual audits.

<sup>40</sup> (U.K.), 1985, c. 6 [hereinafter *CA 1985*].

<sup>41</sup> The regulation of businesses is, according to the Constitution of Canada, a shared competence. It ordinarily falls under the provincial competence over "Property and Civil Rights in the Province"

Despite the fact that auditors' mission and duties are set out by the law, auditors are generally viewed as having a contract with the audited company.<sup>42</sup> Yet they hold a special status and stand aside from the management of the company.<sup>43</sup> They perform their function on behalf of the shareholders and are accountable to them,<sup>44</sup> without being their agents.<sup>45</sup> Moreover, in order to ensure their objectivity, they have an obligation to act in a state of total independence vis-à-vis the company.<sup>46</sup>

The appointment of auditors is usually made by the shareholders,<sup>47</sup> or by the directors in the case of the first auditors.<sup>48</sup> In principle, every company must appoint an auditor. Exceptions are, however, provided for in the statutes, depending on the nature of the company.<sup>49</sup>

The main obligation of an auditor is to report to the shareholders on the preparation and accuracy of the annual accounts of the company.<sup>50</sup> In England the report must

(*Constitution Act, 1867*, *supra* note 8, s. 92(13)). A few exceptions, though, make some businesses fall within federal jurisdiction (*ibid.*, ss. 91 (introduction), 91(29), 92(10)(c)). See Hogg, *supra* note 8 at 21-8 to 21-10. For provincial legislation, see e.g. *ABCA*, *supra* note 19; *MCA*, *supra* note 19; *NBBCA*, *supra* note 19; *OBCA*, *supra* note 19.

<sup>42</sup> See Iacobucci, Pilkington & Prichard, *supra* note 6 at 414; Abbyad *et al.*, *supra* note 8 at 130.

<sup>43</sup> Iacobucci, Pilkington & Prichard, *ibid.* at 390.

<sup>44</sup> *Ibid.*

<sup>45</sup> See Morse, *supra* note 12 at 571; *Roman Corp. v. Peat Marwick Thorne* (1992), 11 O.R. (3d) 248 at 254, 8 B.L.R. (2d) 43 (Gen. Div.) [hereinafter *Roman I* cited to O.R.].

<sup>46</sup> See England: *CA 1989*, *supra* note 10, s. 27; Canada: *CBCA*, *supra* note 19, ss. 161(1), 161(2); *ABCA*, *supra* note 19, ss. 155(1), 155(2); *BCCA*, *supra* note 16, ss. 183(1)-183(3); *MCA*, *supra* note 19, ss. 155(1), 155(2); *NBBCA*, *supra* note 19, ss. 104(1), 104(2); *NSCA*, *supra* note 19, ss. 119A(1), 119A(2); *OBCA*, *supra* note 19, ss. 152(1), 152(2); *Companies Act*, R.S.Q. c. C-48, s. 113(3) [hereinafter *QCA*]; *QCE*, *supra* note 15, ss. 3.02.01, 3.02.05.

<sup>47</sup> England: *CA 1985*, *supra* note 40, ss. 384-85; Canada: *CBCA*, *ibid.*, s. 162(1); *ABCA*, *ibid.*, s. 156(1); *BCCA*, *ibid.*, s. 178(3); *MCA*, *ibid.*, s. 156(1); *NBBCA*, *ibid.*, s. 105(1); *NSCA*, *ibid.*, s. 117(2); *OBCA*, *ibid.*, s. 149(1); *QCA*, *ibid.*, s. 123.97.

<sup>48</sup> England: *CA 1985*, *ibid.*, s. 385, except in the case of private companies that have elected to dispense with the laying of accounts (*ibid.*, s. 385A) or with the annual appointment of auditors (*ibid.*, s. 386); Canada: *CBCA*, *ibid.*, s. 104(1); *ABCA*, *ibid.*, s. 99(1)(e); *BCCA*, *ibid.*, s. 178(1); *MCA*, *ibid.*, s. 99(1); *NBBCA*, *ibid.*, s. 62(1)(e); *NSCA*, *ibid.*, s. 117(3); *OBCA*, *ibid.*, s. 117(1)(e). No such provision exists in the *QCA*, *ibid.*

<sup>49</sup> England: *CA 1985*, *ibid.*, ss. 249A, 250(3), 384(1), 388A; Canada: *CBCA*, *ibid.*, ss. 160(1), 163(1); *ABCA*, *ibid.*, s. 157; *BCCA*, *ibid.*, s. 179; *MCA*, *ibid.*, ss. 154(1), 157(1); *NSCA*, *ibid.*, s. 118(a); *OBCA*, *ibid.*, s. 148(1)(a); *QCA*, *ibid.*, ss. 123.98-123.100.

<sup>50</sup> England: *CA 1985*, *ibid.*, ss. 235(1), 235(2); Canada: *BCCA*, *ibid.*, s. 188(2); *NSCA*, *ibid.*, s. 119; *QCAA*, *supra* note 15, s. 114(2). In Canada auditors have the duty, even after the termination of their functions or the deposit of their reports, to inform the directors of any material error discovered in the financial statements on which they have reported. See *CBCA*, *ibid.*, ss. 171(7), 171(8); *ABCA*, *ibid.*, ss. 165(8), 165(9); *BCCA*, *ibid.*, s. 195; *MCA*, *ibid.*, ss. 165(7), 165(8); *NSCA*, *ibid.*, s. 119B; *OBCA*,

state whether, in the auditor's opinion, the financial statements have been prepared in accordance with the *CA 1985*, and whether they give a "true and fair view" of the financial situation of the company.<sup>51</sup> In Canada some statutes mention a similar requirement,<sup>52</sup> but usually they do not articulate the specific standards with which the auditor must comply.<sup>53</sup> Unlike their French colleagues, Canadian and English auditors do not "certify" the correctness of the accounts, but merely give an "opinion"<sup>54</sup> that is not meant to provide absolute certainty.<sup>55</sup>

For each financial year, the company's annual accounts, accompanied by the auditor's report, must be presented before the company at a general meeting.<sup>56</sup> Auditors have the right to receive notice of every shareholders' meeting,<sup>57</sup> to attend it, and

*ibid.*, ss. 153(3), 153(4). The *NBBCA*, *supra* note 19, and *QCA*, *ibid.*, contain no similar provision. But see *Abbyad et al.*, *supra* note 8 at 8-9, 14.

<sup>51</sup> *CA 1985*, *ibid.*, s. 235(2). See also Auditing Practices Board, *Auditors' Reports on Financial Statements* (1993), which establishes standards of auditing and provides a framework of practice with which auditors must comply.

<sup>52</sup> See *NSCA*, *supra* note 19, s. 119; *QCAA*, *supra* note 15, s. 114(2) ("true and correct view"); *BCCA*, *supra* note 16, s. 188(2)(a) (whether "the financial statements presents fairly the financial position of the company").

<sup>53</sup> The CICA has, however, issued a document fundamental to the conduct of audits in Canada, *The CICA Members Handbook*, looseleaf (Toronto: CICA), which sets out the auditing standards for all accountants in Canada [hereinafter *CICA Handbook*]. See especially s. 5400.14 (the financial statements must "present fairly" the financial position of the company). The handbook is referred to by many provisions. See e.g. *Canada Business Corporations Regulations*, S.O.R./79-316, ss. 44, 45; *OBCA*, *supra* note 19, s. 153(1); *ICAO Rules of Professional Conduct*, *supra* note 18, s. 206; *NSCA*, *ibid.*, s. 119B(2). In Quebec the courts have stated that the handbook should be complied with when carrying out an audit. See e.g. *Malo v. Michaud*, [1993] R.R.A. 760 (Sup. Ct.) [hereinafter *Malo*]; *Irwin (Management Consultants) v. Thorne, Riddell*, [1991] R.R.A. 187 at 190 (Sup. Ct.) [hereinafter *Irwin* (Sup. Ct.)], *aff'd*, [1995] R.R.A. 589 (C.A.) [hereinafter *Irwin* (C.A.)]; *Caisse populaire de Charlesbourg v. Michaud*, [1990] R.R.A. 531 (C.A.) [hereinafter *Charlesbourg*]. See also *Welling*, *supra* note 17 at 96; *Iacobucci, Pilkington & Prichard*, *supra* note 6 at 390; *J. Ziegel et al., Cases and Materials on Partnerships and Canadian Business Corporations*, 2d ed. (Toronto: Carswell, 1989) at 967; *Abbyad et al.*, *supra* note 8 at 26.

<sup>54</sup> *Birds et al.*, *supra* note 10 at 404.

<sup>55</sup> *CICA Handbook*, *supra* note 53, s. 5025.11; *SSA's Auditors' Report*, *supra* note 51 at para. 6.

<sup>56</sup> England: *CA 1985*, *supra* note 40, s. 241; Canada: *CBCA*, *supra* note 19, s. 155(1); *ABCA*, *supra* note 19, s. 149(1); *BCCA*, *supra* note 16, s. 145(1); *MCA*, *supra* note 19, s. 149(1); *NBBCA*, *supra* note 19, s. 100(1); *NSCA*, *supra* note 19, ss. 121(1), 121(2); *OBCA*, *supra* note 19, s. 154; *QCA*, *supra* note 46, ss. 98(1), 98(2).

<sup>57</sup> England: *CA 1985*, *ibid.*, s. 390(1); Canada: *CBCA*, *ibid.*, s. 135(1)(c); *ABCA*, *ibid.*, ss. 129(1)(c), 162(1); *BCCA*, *ibid.*, ss. 198; *MCA*, *ibid.*, s. 129(1); *NBBCA*, *ibid.*, s. 109; *NSCA*, *ibid.*, s. 119(1); *OBCA*, *ibid.*, s. 96(1)(c). The *QCA*, *ibid.*, contains no similar provision.

to be heard on matters relating to their duties as auditors.<sup>58</sup> Moreover, in Canada auditors have an obligation to attend shareholders' meetings and to answer any questions relating to their duties when a director or shareholder of the corporation gives them prior written notice to this effect.<sup>59</sup>

An auditor's report is prepared in the primary interest of the shareholders.<sup>60</sup> In England, before an annual shareholders' meeting, every member of the company, every holder of the company's debentures, and every person entitled to receive notice of a general meeting has the right to receive a copy of the company's annual accounts, accompanied by a copy of the auditor's report on these accounts.<sup>61</sup> In Canada shareholders have the same right.<sup>62</sup> Moreover, most statutes grant shareholders a general right to examine financial statements and to take extracts from them.<sup>63</sup>

Outsiders can also, in certain cases, have access to the auditor's report. Thus, if the company publishes, or otherwise makes available, its accounts in a manner calculated to invite the general public, or any class of the public, to read them, they must be accompanied by the auditor's report.<sup>64</sup> In addition, the *BCCA* gives a direct right of access to third parties and provides that, in the case of a "reporting company",<sup>65</sup> any person may examine and take extracts from every audited financial statement of the company and its subsidiaries, including the auditor's report.<sup>66</sup> In practice the auditor's report is also often communicated to third parties by the company's directors and officers in the hope of attracting investments, contracts, or financing.

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<sup>58</sup> See England: *CA 1985, ibid.*, s. 390(1); Canada: *CBCA, ibid.*, s. 168(1); *ABCA, ibid.*, s. 162(1); *BCCA, ibid.*, s. 198; *MCA, ibid.*, s. 162(1); *NBBCA, ibid.*, s. 109(1); *NSCA, ibid.*, s. 119B(9); *OBCA, ibid.*, s. 151(1). The *QCA, ibid.*, contains no similar provision.

<sup>59</sup> See *CBCA, ibid.*, s. 168(2); *ABCA, ibid.*, s. 162(2); *BCCA, ibid.*, ss. 193-94; *MCA, ibid.*, s. 162(2); *NBBCA, ibid.*, s. 109(2); *NSCA, ibid.*, s. 119(2); *OBCA, ibid.*, s. 151(2). The *QCA, ibid.*, contains no similar provision.

<sup>60</sup> See *CA 1985, supra* note 40, s. 235: "the company's auditors shall make a report to the company's members." See also *QCA, ibid.*, s. 114(2).

<sup>61</sup> See *CA 1985, ibid.*, ss. 238(1), 238(2), 239(1).

<sup>62</sup> See *CBCA, supra* note 19, s. 159(1); *ABCA, supra* note 19, s. 153(1); *NBBCA, supra* note 19, s. 103(1); *OBCA, supra* note 19, s. 154(3); *QCA, supra* note 46, s. 114(4). In some provinces this is so only in specific circumstances (*BCCA, supra* note 16, s. 172; *MCA, supra* note 19, s. 153(1); *NSCA, supra* note 19, ss. 121(3), 121(6)).

<sup>63</sup> See *CBCA, ibid.*, s. 157(2); *ABCA, ibid.*, ss. 21(1), 21(2); *BCCA, ibid.*, s. 164(2) (right also provided to debenture holders); *MCA, ibid.*, s. 151(2); *NBBCA, ibid.*, s. 101(2); *QCA, ibid.*, ss. 114(3), 122.

<sup>64</sup> See England: *CA 1985, supra* note 40, ss. 240(1), (4); Canada: *CBCA, ibid.*, s. 158(2); *ABCA, ibid.*, s. 152(2); *BCCA, ibid.*, s. 174(1); *MCA, ibid.*, s. 152(2); *NBBCA, ibid.*, s. 102(2)(b); *NSCA, supra* note 19, s. 122(3); *OBCA, supra* note 19, s. 159(2). The *QCA, ibid.*, contains no similar provision.

<sup>65</sup> *BCCA, ibid.*, s. 1(1).

<sup>66</sup> *Ibid.*, s. 164.

## 2. The Certification of Accounts by the *Commissaire aux Comptes*

Traditionally *commissaires aux comptes* were viewed as the agents of the *société* (*mandataires*), as well as the protectors of shareholders' private interests.<sup>67</sup> Since the adoption of the *Loi de 1966*, which institutionalized their functions,<sup>68</sup> however, their status is no longer contractual, but rather statutory.<sup>69</sup> Hence, they do not act in the individual interest of the shareholders, but rather in the general interest of the public,<sup>70</sup> and their duties clearly extend to third parties.<sup>71</sup> In view of this new role, the *Loi de 1966* imposes a strict requirement of independence with severe sanctions for its violation.<sup>72</sup>

Most bodies pursuing economic activities, whatever their form, are subjected to the control of the *commissaire aux comptes*.<sup>73</sup> Depending on the type of *société*,<sup>74</sup> the *commissaire aux comptes* must be appointed by the *associés*,<sup>75</sup> shareholders,<sup>75</sup> mem-

<sup>67</sup> CREDA, *Le commissariat aux comptes* (Paris: 1989) at 414.

<sup>68</sup> Compagnie Nationale des Commissaires aux Comptes, *supra* note 6 at 1.

<sup>69</sup> The *commissaire aux comptes* is now seen as the controller of the legality of the *société*. See Monéger & Granier, *supra* note 6 at 136-37; P. Feuillet, *Pratique du commissariat aux comptes*, 2d ed. (Paris: Sirey, 1978) at 88; D. Kurkdjian, "Responsabilité civile du commissaire aux comptes" (1995) 50 Cahier L.F.E.C. 11-12; CREDA, *supra* note 67 at 418, 420; Sarut, *Dictionnaire permanent de droit des affaires* (Feuillets 143, 1996) at 2299.

<sup>70</sup> Com., 15 June 1993, Bull. C.N.C.C.1994.93; *Commissariat aux comptes*, *supra* note 38 at 3, 14; Monéger & Granier, *ibid.* at 20, 135; Guyon, *supra* note 6 at 372; Compagnie Nationale des Commissaires aux Comptes, *supra* note 6 at 1. This change was introduced to give *commissaires aux comptes* the credibility that they had been lacking compared to their English, American, and German counterparts.

<sup>71</sup> See *Loi de 1966*, *supra* note 26, s. 234. See also Com., 15 June 1993, *ibid.*; Com., 17 October 1984, Bull. C.N.C.C.1985.57.107 Rev Soc.1985.845 (Annot. E. du Pontavice). The third parties can be creditors or investors (Trib. gr. inst. Le Havre, 15 November 1979, aff'd, Rouen, 27 April 1982, Bull. C.N.C.C.47.288), and shareholders or *associés* if they suffer personal harm distinct from the harm caused to the *société*. See Guyon, *ibid.* at 383; CREDA, *supra* note 67 at 433, 438; Kurkdjian, *supra* note 69 at 15; Compagnie Nationale des Commissaires aux Comptes, *ibid.* at 29; E. du Pontavice, *Le commissaire aux comptes. Manuel pratique*, vol. 1 (Ormesson-sur-Marne: 1981) at A.15, 209 [hereinafter *Manuel pratique*].

<sup>72</sup> *Loi de 1966*, *ibid.*, ss. 17-1, 65, 219-3, 220 to 221-1.

<sup>73</sup> Every *société anonyme*, *société en commandite par actions*, and *société par actions simplifiées* must have its accounts reviewed (*ibid.*, ss. 218, 254, 262-1). The same rule applies to the *sociétés civiles faisant publiquement appel à l'épargne* (*Loi de 1970*, *supra* note 27, s. 18).

<sup>74</sup> See *Loi de 1966*, *ibid.*, s. 218.

<sup>75</sup> *Ibid.*, s. 64.

<sup>76</sup> *Ibid.*, s. 79, if the *société par actions* is public. If it is private, they are appointed in the articles of the company (*ibid.*, s. 88). The subsequent auditors, in both cases, will be appointed by the shareholders (*ibid.*, ss. 233, 254).

bers,<sup>77</sup> or *sociétaires*.<sup>78</sup> The law has, however, taken into account the size and importance of some *sociétés* in order to create exceptions to this general rule.<sup>79</sup>

Despite the many responsibilities of the *commissaires aux comptes*,<sup>80</sup> their main task is to certify the lawfulness (*régularité*)<sup>81</sup> and sincerity<sup>82</sup> of the annual statements, and to certify that they give a faithful picture (*image fidèle*)<sup>83</sup> of the financial situation of the *société*.<sup>84</sup> The impact of certification in France is paramount since the *commissaire* gives strong authority to the control and verification undertaken, and attests personally to the likelihood of the regularity and sincerity of the accounts.<sup>85</sup> Yet this certification is not meant to give absolute guarantees.<sup>86</sup> In fact, the *commissaire* must comply only with an obligation of diligence (*obligation de moyens*) towards the *société* and third parties. Consequently, as long as the *commissaires* meet the standard of a prudent, competent, and diligent professional placed in the same circumstances, they are deemed to have discharged their duties.<sup>87</sup>

<sup>77</sup> See *Ordonnance de 1967*, *supra* note 29, s. 10.

<sup>78</sup> See *Décret de 1985*, *supra* note 28, s. 23.

<sup>79</sup> *Décret n° 67-236 du 23 mars 1967*, J.O., 24 March 1967, 2843, ss. 12, 43 [hereinafter *Décret de 1967*]; *Loi de 1966*, *supra* note 26, ss. 17-1, 64; *Loi de 1984*, *supra* note 27, s. 27; *Décret de 1985*, *ibid.*, ss. 19, 22; *Ordonnance de 1967*, *supra* note 29, ss. 5, 10.

<sup>80</sup> See e.g. *Loi de 1966*, *ibid.*, ss. 228, 233(1), 233(2); *Loi de 1984*, *ibid.*, s. 29.

<sup>81</sup> See *Commissariat aux comptes*, *supra* note 38 at 52. This means that the accounts must comply with the relevant substantive rules and procedures.

<sup>82</sup> See Sarrut, *supra* note 69 at 2301. This refers to the quality of the description of the situation of the company. See also *Commissariat aux comptes*, *ibid.* at 52.

<sup>83</sup> See *Commissariat aux comptes*, *ibid.* This concept refers to the common law "true and fair view" concept and means that the accounts must present the situation and results of the company completely and objectively.

<sup>84</sup> See *Loi de 1966*, *supra* note 26, s. 228.

<sup>85</sup> *Commissariat aux comptes*, *supra* note 38 at 52; Com., 9 February 1988, Joly.1988.275, Rev. Soc.1988.555 (Annot. J. Monéger).

<sup>86</sup> *Commissariat aux comptes*, *ibid.*; Guyon, *supra* note 6 at 389; D. Langé, "Commissaire aux comptes" in *Jurisclasseur, Responsabilité civile* (Fasc. 340, 1999) at 3; Com., 9 February 1988, *ibid.*; Com., 27 October 1992, JCP.14.G.22026, Bull. C.N.C.C. II 91.376, Rev. Soc.1993.86 (Annot. M. Jeantin).

<sup>87</sup> Com., 21 January 1997, Bull. C.N.C.C.1997.406 (Annot. P. Merle); Com., 2 July 1973, DS 1973.674; Paris, 23 February 1978, Rev. Soc.79.92; Bordeaux, 4 November 1997, Bull. C.N.C.C. 1998.203; Rennes, 22 February 1999, Bull. C.N.C.C. 1999.463 (Annot. P. Merle); *Commissariat aux comptes*, *ibid.* at 74, 78; *Manuel pratique*, *supra* note 71 at A.15, 192; Morin, *supra* note 6 at 18-19; Guyon, *supra* note 6 at 396; Feuillet, *supra* note 69 at 89; Monéger & Granier, *supra* note 6 at 143, 145; Langé, *ibid.* at 4; Kurkdjian, *supra* note 69 at 11; Compagnie Nationale des Commissaires aux Comptes, *supra* note 6 at 3, 5-6; CREDA, *supra* note 67 at 420-21; annot., Com., 17 October 1984, *supra* note 71; Com., 6 October 1992, RJC.1993.166 (Annot. D. Vidal); annot., Com., 27 October 1992, *ibid.* See also generally G. Viney, *Traité de droit civil. Les obligations. La responsabilité: conditions* (Paris: L.G.D.J., 1982) at 292 [hereinafter *La responsabilité: conditions*]. The same test ap-

The financial documents, as well as the *commissaire's* report on them, are presented to the assembly of *associés* or shareholders, who are their primary recipients and have the right to obtain a copy of these documents.<sup>85</sup> Moreover, any third party can have access to the *commissaire's* report of the *sociétés à responsabilité limitée* and the *sociétés par actions*, since both *sociétés* have the obligation to file a copy with the commercial court.<sup>89</sup> Finally, as in England and Canada, certified accounts are often disclosed voluntarily to third parties by the management of the *société*.

Therefore, the fundamental difference between a French auditor, on the one hand, and an English or Canadian auditor, on the other, lies in the scope of people for whose interest the auditor's report is prepared. It is difficult to exaggerate the importance of the broader statutory and institutional role of the *commissaire aux comptes*, who must act in the public interest, while the Canadian and English auditors' duty is directed primarily towards the shareholders. The practical importance of auditors' work for third parties is not, however, denied in these jurisdictions. In light of these different statutory roles towards non-clients, it is interesting to see how the courts have treated liability of auditors for harm suffered by third parties in the common law and civil law jurisdictions.

## II. The Common Law<sup>90</sup>

Because auditors' liability for negligent misstatements is not, in itself, an autonomous category within the law of negligence, it must first be analyzed in the wider context of liability for pure economic loss.<sup>91</sup>

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plies in the Province of Quebec. See *Roberge v. Bolduc*, [1991] 1 S.C.R. 374 at 395-96, 398, (*sub nom. Dorion v. Roberge et al.*) 78 D.L.R. (4th) 666; *R.M.A. Restaurant Management v. Gallay*, [1996] R.R.A. 485 (Sup. Ct.); *Guardian*, *supra* note 6 at 169, 173; J.C. René, "La responsabilité professionnelle des comptables: développements récents" (1991) 51 Can. Bar Rev. 395 at 398; *Charlesbourg*, *supra* note 53 at 536.

<sup>85</sup> See *Loi de 1966*, *supra* note 26, ss. 56, 157, 168; *Décret de 1967*, *supra* note 79, ss. 36, 139.

<sup>89</sup> *Décret de 1967*, *ibid.*, ss. 44-1, 293.

<sup>90</sup> In the development of the law of auditors' liability towards third parties, the landmark cases in England have had a great impact on the way the Canadian common law has evolved. These two jurisdictions are thus treated together.

<sup>91</sup> Claims brought by third parties against negligent auditors usually seek recovery for pure economic loss. Pure economic loss is harm not associated with any physical damage to the plaintiff's person or property. See e.g. J.G. Fleming, *The Law of Torts*, 9th ed. (North Ryde, N.S.W.: LBC Information Services, 1998) at 195; R.A. Buckley, *The Modern Law of Negligence*, 3d ed. (London: Butterworths, 1999) at 131; R.A. Percy, *Charlesworth & Percy on Negligence*, 9th ed. (London: Sweet & Maxwell, 1997) at 87; J.F. Clerk, *Clerk & Lindsell on Torts*, 17th ed. (London: Sweet & Maxwell, 1995) at 271.

### A. Duty of Care and Pure Economic Loss in the Law of Negligence

To succeed in a claim for negligence, plaintiffs must show that they suffered harm as a consequence of the breach of a duty of care owed to them by the defendant. The absence of a duty of care has the effect of nullifying any possibility of liability, even if the negligence or carelessness of the defendant has caused harm to the plaintiff.<sup>92</sup> It is principally through the use of this requirement that the courts have responded to one of the basic problems of the tort of negligence, namely, keeping recovery for pure economic loss within proper limits.<sup>93</sup>

The recognition of a duty of care in cases of pure economic loss is one of the most controversial issues in the law of negligence, and the courts have traditionally been reluctant to allow recovery for this type of loss. This restrictive approach originates mainly from the belief that, if accepted in principle, liability for negligently caused pure economic loss could be indeterminate.<sup>94</sup> It has incited the English and Canadian courts to interpret the *Donoghue* "neighbour principle" based on foreseeability of harm<sup>95</sup> as applying only to instances of physical damage to persons or property.<sup>96</sup> Thus, to avoid indeterminate recovery in the area of pure economic loss, courts had to formulate safeguards more efficient than the foreseeability of harm. The exact nature of such safeguards, however, is much debated and not yet totally settled.<sup>97</sup>

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<sup>92</sup> See *LeLièvre and Dennis v. Gould*, [1893] 1 Q.B. 491 at 497.

<sup>93</sup> It should be noted that the rule of privity of contract, as it existed in England until recently, did not prevent a person not party to a contract from claiming damages suffered in consequence of the negligent execution of that contract. See *Donoghue v. Stevenson*, [1932] A.C. 562 at 611, [1932] All E.R. Rep. 1 (H.L.) [hereinafter *Donoghue* cited to A.C.]; G.H. Treitel, *The Law of Contract*, 9th ed. (London: Butterworths, 1995) at 551.

<sup>94</sup> See e.g. *Ultramares Corp. v. Touche*, 174 N.E. 441 at 444, 255 N.Y. 170, 74 A.L.R. 1139 (1931). See also *Canadian National Railway v. Norsk Pacific Steamship*, [1992] 1 S.C.R. 1021 at 1137, 1139, 91 D.L.R. (4th) 289, McLachlin J. [hereinafter *Norsk* cited to S.C.R.]; B.S. Markesinis & S.F. Deakin, *Tort Law*, 3d ed. (Oxford: Clarendon Press, 1994) at 79, 85; D. Howarth, *Textbook on Tort* (London: Butterworths, 1995) at 300ff, 319ff; Buckley, *supra* note 91 at 143-44; L.N. Klar *et al.*, *Tort Law*, 2d ed. (Scarborough: Carswell, 1996) at 172; D. Marshall, "Liability for Pure Economic Loss Negligently Caused—French and English Law Compared" (1975) *Int'l & Comp. L.Q.* 748 at 750.

<sup>95</sup> See *Donoghue*, *supra* note 93 at 580. This broad test was said to come close to establishing a general clause in the French style. See Howarth, *ibid.* at 163.

<sup>96</sup> See e.g. Markesinis & Deakin, *supra* note 94 at 77, 79; Klar *et al.*, *supra* note 94 at 139; I.F. Ivankovitch, "Accountants and Third-Party Liability—Back to the Future" (1991) 23 *Ottawa L. Rev.* 505 at 509; P. Cane, ed., *Atiyah's Accidents' Compensation and the Law*, 6th ed. (London: Butterworths, 1999) at 58.

<sup>97</sup> Percy, *supra* note 91 at 77; G.H.L. Fridman, *The Law of Torts in Canada*, vol. 1 (Toronto: Carswell, 1989) at 264; *Norsk*, *supra* note 94 at 1137.

The exact meaning and practical application of the duty of care are difficult to grasp, and no clear test has been articulated for the duty's assessment.<sup>93</sup> It is agreed, though, that it is based upon the existence of a certain kind of relationship between the parties, sometimes called a relationship of "proximity". Yet this last notion, criticized as ambiguous and not susceptible of any precise definition,<sup>99</sup> has failed to render the evaluation of the duty of care easier. In fact, the concept of proximity is mainly a control device that allows the courts to restrict recovery in negligence to limited cases. As for its exact content, it seems to depend on the ease at hand and on the type of harm suffered.<sup>100</sup>

Recovery in tort for pure economic loss was first accepted in *Hedley Byrne & Co. v. Heller & Partners*<sup>101</sup> in the context of negligent misstatements. In this case, the House of Lords attempted to draw boundaries around the possibility of recovery, but did not articulate precise, uniform criteria, and even today the limits of this decision remain uncertain.<sup>102</sup> These boundaries, however, revolved around the following ideas: the concept of a "special relationship";<sup>103</sup> the exercise of special skills by the defen-

<sup>96</sup> B. Feldthusen, *Economic Negligence: The Recovery of Pure Economic Loss*, 2d ed. (Toronto: Carswell, 1989) at 22, 31; Fleming, *supra* note 91 at 150-51; Klar *et al.*, *supra* note 94 at 133.

<sup>99</sup> See N. Rafferty, "Torts—Negligent Misstatement—Recovery for Purely Economic Loss" (1991) 70 Can. Bar Rev. 381 at 383; K.M. Stanton, *The Modern Law of Tort* (London: Sweet & Maxwell, 1994) at 33; Fleming, *ibid.* at 138-39. See also the comments of A.M. Dugdale & K.M. Stanton, *Professional Negligence*, 3d ed. (London: Butterworths, 1998) at 112-13.

<sup>100</sup> See *Caparo*, *supra* note 6 at 633; *Smith v. Eric S Bush (a firm)* (1989), [1990] 1 A.C. 831 at 871, [1989] 2 All E.R. 514 (H.L.) [hereinafter *Smith* cited to A.C.]; *Federal Business Development Bank v. Morris, Burk, Luborsky, David & Kale* (1988), 38 B.L.R. 1 at 4 (Ont. H.C.J.) [hereinafter *Morris*]; *Boyd v. Ackley* (1962), 32 D.L.R. (2d) 77 at 80 (B.C. S.C.); *Hercules Managements v. Ernst & Young*, [1997] 2 S.C.R. 165 at 187, 146 D.L.R. (4th) 577 [hereinafter *Hercules* cited to S.C.R.]. See also *Junior Books v. Veitchi Co.* (1982), [1983] 1 A.C. 520 at 533, 539, [1982] 3 All E.R. 201 (H.L.) [hereinafter *Junior Books* cited to A.C.]; *Norsk*, *supra* note 94 at 1152; *Queen v. Cognos Inc.*, [1993] 1 S.C.R. 87 at 110, 99 D.L.R. (4th) 626 [hereinafter *Cognos* cited to S.C.R.]; *Fletcher v. Manitoba Public Insurance*, [1990] 3 S.C.R. 191 at 206, 74 D.L.R. (4th) 636 [hereinafter *Fletcher* cited to S.C.R.]; *Rivtow Marine v. Washington Iron Works* (1973), [1974] S.C.R. 1189 at 1196, 40 D.L.R. (3d) 530 [hereinafter *Rivtow Marine* cited to S.C.R.]; *B.D.C. v. Hofstrand Farms*, [1986] 1 S.C.R. 228 at 236, 26 D.L.R. (4th) 1 [hereinafter *B.D.C.* cited to S.C.R.]; J.A. Campion & D.W. Dimmer, *Professional Liability in Canada*, looseleaf (Scarborough: Carswell, 1994) at 8-6.

<sup>101</sup> (1963), [1964] A.C. 465, [1963] 2 All E.R. 575 (H.L.) [hereinafter *Hedley Byrne* cited to A.C.].

<sup>102</sup> See *Caparo*, *supra* note 6 at 628, 632; Dugdale & Stanton, *supra* note 99, where the authors note at 106 that it took thirty years for the full implications of the decision to become clear; Percy, *supra* note 91 at 96; Jackson & Powell, *supra* note 1 at 833; Howarth, *supra* note 94 at 328.

<sup>103</sup> See *Hedley Byrne*, *supra* note 101 at 486-87, Lord Reid, at 502, Lord Morris, at 509, Lord Hodson, at 515, 529, Lord Devlin, at 539, Lord Pearce. See the criticism of Feldthusen, *supra* note 98 at 22, 31, 38, 40-43.

dant;<sup>104</sup> the existence of a relationship “equivalent to contract”;<sup>105</sup> and the notion that the maker of the statement has undertaken some responsibility towards the plaintiff.<sup>106</sup> Even though they were interpreted by some as an extension of the *Donoghue* principle<sup>107</sup> and applicable to other areas, the principles established in *Hedley Byrne* were long confined to cases of negligent misstatement.<sup>108</sup>

In 1977 the House of Lords initiated another attempt to create a general test applicable to all types of harm. In *Anns v. Merton London Borough Council*,<sup>109</sup> Lord Wilberforce formulated a two-stage test: first, a prima facie duty of care could arise from a relationship of proximity based on foreseeability of harm; second, once found, this prima facie duty of care could nevertheless be restricted by the application of policy considerations.<sup>110</sup>

This test was subsequently criticized as too broad, and in fact, it provoked an expansion of liability in tort in the late 1970s and early 1980s.<sup>111</sup> It was consequently rejected in England,<sup>112</sup> where the courts returned to the narrower categorization of cases,

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<sup>104</sup> See *Hedley Byrne*, *ibid.* at 502-503, Lord Morris, at 514, Lord Hodson. See also *Mutual Life v. Evatt* (1970), [1971] A.C. 793 at 804, 806-807, [1971] 7 All E.R. 150 (P.C.) [hereinafter *Evatt* cited to A.C.]. *Contra ibid.* at 811, Lord Reid, Lord Morris; *Esso Petroleum Co. v. Mardon*, [1976] 2 All E.R. 5 at 22, [1976] 2 W.L.R. 583 (C.A.); *Spring v. Guardian Assurance* (1994), [1995] 2 A.C. 296 at 318-19, [1994] 3 All E.R. 129 (H.L.) [hereinafter *Spring* cited to A.C.]; Howarth, *supra* note 94 at 277; *Cognos*, *supra* note 100 at 117; *Royal Bank of Canada v. Aleman* (1988), 86 A.R. 64 at 71, [1988] 3 W.W.R. 461 (Q.B.) [hereinafter *Aleman* cited to A.R.]. See also Percy, *supra* note 91 at 95; Klar *et al.*, *supra* note 94 at 183; Fridman, vol. 1, *supra* note 97 at 267; Dugdale & Stanton, *supra* note 99 at 128.

<sup>105</sup> See *Hedley Byrne*, *ibid.* at 529, Lord Devlin. See also *Smith*, *supra* note 100 at 846; *White v. Jones*, [1995] 2 A.C. 207 at 281, [1995] 1 All E.R. 691 (H.L.) [hereinafter cited to A.C.].

<sup>106</sup> See *Hedley Byrne*, *ibid.* at 483, 486, 493, Lord Reid, at 494, Lord Morris, at 529, Lord Devlin. See also Percy, *supra* note 91 at 96, 98; Feldthusen, *supra* note 98 at 46.

<sup>107</sup> See Howarth, *supra* note 94 at 294; Stanton, *supra* note 99 at 333-39; Rafferty, *supra* note 99 at 393; G.H.L. Fridman, *The Law of Torts in Canada*, vol. 2 (Toronto: Carswell, 1989) at 133.

<sup>108</sup> Markesinis & Deakin, *supra* note 94 at 77. But see text accompanying notes 126-31 for an outline of the recent developments concerning “assumption of responsibility”.

<sup>109</sup> (1977), [1978] A.C. 728, [1977] 2 All E.R. 492 (H.L.) [hereinafter *Anns* cited to A.C.].

<sup>110</sup> *Ibid.* at 751-52.

<sup>111</sup> Markesinis & Deakin, *supra* note 94 at 20; Stanton, *supra* note 99 at 33, 68-69; Rafferty, *supra* note 99 at 381; Dugdale & Stanton, *supra* note 99 at 72; Percy, *supra* note 91 at 28; Jackson & Powell, *supra* note 1 at 16. In the area of nervous shock see *e.g. McLoughlin v. O'Brian* (1982), [1983] A.C. 410, [1982] 2 All E.R. 298 (H.L.); for pure economic loss caused by a negligent deed, see *Junior Books*, *supra* note 100.

<sup>112</sup> See *Murphy v. Brentwood District Council* (1990), [1991] 1 A.C. 398, [1990] 2 All E.R. 908 (H.L.) [hereinafter *Murphy* cited to A.C.]. See Dugdale & Stanton, *ibid.* at 72; Percy, *ibid.* at 34-36; Rafferty, *ibid.* at 382.

making analogies with established categories of liability.<sup>113</sup> In Canada, however, the Supreme Court of Canada continued to apply the *Anns* test.<sup>114</sup> This had the impact of rendering the Canadian courts more receptive to claims for pure economic loss. Despite this conceptual divergence, the possibility of recovering pure economic loss in cases other than those of negligent misstatements has been accepted in Canada,<sup>115</sup> as well as in England,<sup>116</sup> though only in a few specific and limited situations.<sup>117</sup>

### B. Auditors' Liability towards Third Parties in England and Canada

In line with this tendency, the English courts have traditionally refused claims alleging negligent misrepresentation causing pure economic loss in the absence of a contract, fraud, or fiduciary relationship.<sup>118</sup> The door was opened, however, by the famous dissenting judgment of Lord Denning in *Candler*,<sup>119</sup> which was later approved by the House of Lords in *Hedley Byrne*.<sup>120</sup>

Despite this new expansion of grounds for liability, pure economic loss caused by words was still viewed with particular suspicion. There was fear of unlimited liability arising from the possibility of such words being transmitted without the consent or foresight of their author.<sup>121</sup> Therefore, one of the preoccupations of the courts dealing

<sup>113</sup> Fleming, *supra* note 91 at 153. See e.g. *Caparo*, *supra* note 6 at 633, 635-36, Lord Oliver, at 618, Lord Bridge, at 628, Lord Roskill; *Murphy*, *ibid.* at 461; *White v. Jones*, *supra* note 105 at 270, 275.

<sup>114</sup> *Kamloops (City of) v. Nielsen*, [1984] 2 S.C.R. 2, 10 D.L.R. (4th) 641 [hereinafter *Kamloops* cited to S.C.R.]; *Norsk*, *supra* note 94; *B.D.C.*, *supra* note 100; *London Drugs v. Kuelme & Nagel International*, [1992] 3 S.C.R. 299, 97 D.L.R. (4th) 261; *Winnipeg Condominium Corporation No. 36 v. Bird Construction*, [1995] 1 S.C.R. 85, 121 D.L.R. (4th) 193; *Hercules*, *supra* note 100; A.M. Linden, *Canadian Tort Law*, 6th ed. (Toronto: Butterworth, 1997) at 274; Klar *et al.*, *supra* note 94 at 143; Dugdale & Stanton, *supra* note 99 at 72.

<sup>115</sup> See e.g. *Norsk*, *ibid.*; *Rivtow Marine*, *supra* note 100.

<sup>116</sup> See e.g. *Ross v. Caunters* (1979), [1980] 1 Ch. 297, [1979] 3 All E.R. 580 [hereinafter *Ross* cited to Ch.]; *Junior Books*, *supra* note 100; *White v. Jones*, *supra* note 105.

<sup>117</sup> Percy, *supra* note 91 at 65; Marshall, *supra* note 94 at 778.

<sup>118</sup> See *Derry v. Peek* (1889), 14 A.C. 337 (H.L.) [hereinafter *Derry*]; *Candler v. Crane, Christmas & Co.*, [1951] 2 K.B. 164, [1951] 1 All E.R. 426 [hereinafter *Candler* cited to K.B.]. See Jackson & Powell, *supra* note 1 at 831; Linden, *supra* note 114 at 423; Fridman, vol. 1, *supra* note 97 at 263-64; Fridman, vol. 2, *supra* note 107 at 132-33. *Contra Nocton v. Ashburton (Lord)*, [1914] A.C. 932 (H.L.).

<sup>119</sup> *Ibid.*

<sup>120</sup> See *supra* notes 101-108 and accompanying text. Even though it did not involve auditors' liability, *Hedley Byrne* became the reference judgment in this field. Its importance was not affected by the fact that the relevant remarks were *obiter*. In *Hedley Byrne* itself the claim was rejected because of the presence of a disclaimer.

<sup>121</sup> *Hedley Byrne*, *supra* note 101 at 482-83. Lord Pearce said at 534 that "[w]ords are more volatile than deeds. They travel fast and far afield." See also *Caparo*, *supra* note 6 at 633; Fleming, *supra* note 91 at 189, 705.

with cases of negligent misstatement in the post-*Hedley Byrne* era was finding an adequate test for the assessment of the duty of care. They attempted to do so by building an intellectual framework capable of keeping the right to recovery within acceptable boundaries.

## 1. The Search for a Test

### a. England

#### i. The Existence of a Duty of Care

In England attempts to identify the existence of a duty of care in cases of auditors' liability towards third parties have been dealt with mainly through three approaches: (1) the adoption of a general test of liability; (2) the development of a threefold test; and (3) the use of the traditional incremental approach. No definitive choice has been made between them, and it was even suggested recently that more than one approach can be adopted.<sup>122</sup>

The first attempt to introduce a general principle of liability in this area was noticed particularly in the 1980s.<sup>123</sup> On the basis of *Donoghue* and *Anns*, a duty of care was found in cases where it was reasonably foreseeable that a person might rely on the statements and could suffer an economic loss if the accounts were inaccurate. It is now clear, however, that foreseeability, while being a necessary requirement, is not sufficient to ground liability in cases of negligent misstatement, since it is too easily met and fails to provide adequate safeguards against the risk of indeterminate liability.<sup>124</sup>

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<sup>122</sup> See *Bank of Credit & Commerce International (Overseas) v. Price Waterhouse (No. 2)*, [1998] B.C.C. 617 at 631-34, [1998] E.C.C. 410, 142 S.J.L.B. 86 (C.A.) [hereinafter *BCCI* cited to B.C.C.]. See also *Electra Private Equity Partners v. KPMG Peat Marwick*, [1999] Lloyd's Rep. P.N. 670 (C.A.) [hereinafter *Electra Private*].

<sup>123</sup> *JEB Fasteners v. Marks Bloom & Co.* (1980), [1981] 3 All E.R. 289 at 296, [1982] Com. L.R. 226 (Q.B.D.) [hereinafter *JEB Fasteners (Q.B.)* cited to All E.R.], aff'd, [1983] 1 All E.R. 583 (C.A.) [hereinafter *JEB Fasteners (C.A.)*]; *Scott Group v. McFarlane*, [1978] 1 N.Z.L.R. 553 (C.A.) [hereinafter *Scott Group*]; *Evatt*, supra note 104 at 807. See also *White v. Jones*, supra note 105 at 273; *Berg Sons & Co. v. Adams* (1992), [1993] B.C.L.C. 1045 at 1054-55, [1992] B.C.C. 661 [hereinafter *Berg Sons* cited to B.C.L.C.].

<sup>124</sup> *Caparo*, supra note 6 at 635, 643, 649-50, Lord Oliver, at 655, 661, Lord Jauncey, at 633, Lord Roskill, at 623, 625, Lord Bridge; *Al Saudi Banque v. Clarke Pixley* (1989), [1990] Ch. 313 at 330, [1989] 3 All E.R. 361 [hereinafter *Al Saudi* cited to Ch.]; *Morgan Crucible & Co. v. Hill Samuel & Co.*, [1991] Ch. 295 at 317, [1991] 1 All E.R. 148 [hereinafter *Morgan Crucible* cited to Ch.]; *Murphy*, supra note 112 at 487; *Berg Sons*, *ibid.* at 1054, 1067, where the claim was rejected even though

In addition, on the basis of *Hedley Byrne*, the House of Lords introduced the notion of "assumption of responsibility" as a theoretical basis for a general right to recovery of pure economic loss in tort. In *Spring*,<sup>125</sup> *Henderson v. Merrett Syndicates*,<sup>125</sup> and *White v. Jones*,<sup>127</sup> the House of Lords stressed that there is a general principle that when defendants have "assumed responsibility" for the plaintiff's economic welfare, they may be liable for economic loss in cases other than those of negligent misstatement. Whether this concept should become the "unifying principle"<sup>123</sup> grounding a general right to recovery is arguable, however, and it has therefore been strongly criticized.<sup>129</sup> Moreover, the use of a broad test of liability is controversial, especially in light of the judgment of the House of Lords in *Caparo*, which continues to be the leading case in the area of auditors' liability towards third parties.<sup>13</sup>

the evidence showed actual foresight of reliance. See also Stanton, *supra* note 99 at 339, 342; Feldhusen, *supra* note 98 at 43, 92; Dugdale & Stanton, *supra* note 99 at 119. See the criticism of Atiyah in Cane, *supra* note 96 at 38-39.

<sup>125</sup> *Supra* note 104 at 316, 318.

<sup>126</sup> (1994), [1995] 2 A.C. 145 at 180-81, [1994] 3 All E.R. 506 (H.L.) [hereinafter *Henderson* cited to A.C.].

<sup>127</sup> *Supra* note 105 at 270, 257, 262. See Canada: *Edgeworth Construction v. N.D. Lea & Associates*, [1993] 3 S.C.R. 206 at 212, 107 D.L.R. (4th) 169 [hereinafter *Edgeworth* cited to S.C.R.]; *Fletcher*, *supra* note 100 at 212. But in *Keith Plumbing & Heating Co. v. Newport City Club (sub nom. Micron Construction v. Hongkong Bank of Canada)* (2000), 184 D.L.R. (4th) 75, [2000] 6 W.W.R. 65 (B.C. C.A.), leave to appeal to S.C.C. refused, [2000] S.C.C.A. No. 192, online: QL (SCCA) [hereinafter *Keith Plumbing*], Esson J.A. said that since *Hercules*, it is the "Anns test" and not the "assumption of responsibility" test which should apply in Canada. This latter concept has received the support of some commentators. See e.g. Rafferty, *supra* note 99 at 396; Fridman, vol. 1, *supra* note 97 at 281; Feldhusen, *supra* note 98 at 22, 39, 46-52. See also Dugdale & Stanton, *supra* note 99 at 113-16.

<sup>128</sup> Jackson & Powell, *supra* note 1 at 830.

<sup>129</sup> *Caparo*, *supra* note 6 at 582-83, 628, 637; *Smith*, *supra* note 100 at 862-64; *Min. of Housing v. Sharp*, [1970] 1 All E.R. 1009 at 1018-19, [1970] 2 Q.B. 223 (C.A.); *Haig*, *supra* note 2 at 479; S.J. Whittaker, "Privity of Contract and the Tort of Negligence: Future Directions" (1996) 16 Oxford J. Legal Stud. 191 at 204; Howarth, *supra* note 94 at 292; Stanton, *supra* note 99 at 341.

<sup>130</sup> Clerk, *supra* note 91, states at 281, however, that there may be little difference in the outcome of these two approaches. Moreover, several recent English cases have applied the "assumption of responsibility" test to misstatement claims, alongside some of the requirements developed in *Caparo*. They have underlined that the relevant question for this test is whether the defendants assumed responsibility for the task that they undertook, not whether they assumed legal responsibility for the statement. See *BCCI*, *supra* note 122; *A.D.T. v. B.D.O. Binder Hanlyn*, [1996] B.C.C. 803 at 824, 828-29 (Q.B.D.) [hereinafter *Binder Hanlyn*]; *Peach Publishing v. Slater & Co.*, [1999] B.C.C. 139 (C.A.); *Yorkshire Enterprise v. Robson Rhodes* (17 June 1998) (U.K. Q.B.); *HIT Finance v. Cohen Arnold & Co.* (14 October 1999) (U.K. C.A.); *Electra Private*, *supra* note 122, where Auld L.J. held that both the *Caparo* "threefold" test and the "assumption of responsibility" test must be applied, but that the latter is the predominant one for the purpose of a case involving auditors' liability. The concept is also mentioned in *Andrew v. Kounnis Freeman*, [1999] 2 B.C.L.C. 641 (C.A.) [hereinafter *Andrew*]. See *ibid.* at 654, Beldam L.J., at 654-55, Buxton L.J. Buxton L.J. stressed that two types of

In *Caparo* a claim was brought by the takeover bidder for a company listed on a stock exchange. The plaintiff argued that the accounts of the company were inaccurate and misleading, and that he purchased 29.9 percent of the shares of the company and made a bid for the remaining shares in reliance on them. He also contended that the defendant ought to have foreseen that the company was vulnerable to a takeover bid, and that the bidders might rely on the accounts and consequently suffer a loss because of their inaccuracy. The question was whether the auditors owed a duty of care to the plaintiff in his capacity as (1) a potential investor and (2) a shareholder. Both claims were rejected.

As a reaction to the extensive liability that followed *Anns*, the House of Lords refused to adopt a general principle on the basis of which tortious liability would be determined in all circumstances.<sup>131</sup> At most, a broad categorization of the decided cases according to the type of situation in which liability has been established could be attempted.<sup>132</sup>

In addition to this return to the traditional case by case approach, *Caparo* also approved the tripartite analysis of *Smith*.<sup>133</sup> This case introduced, as elements demonstrating the existence of a duty of care, foreseeability of damage, proximity, and the fact that the situation is one in which the court considers it fair, just, and reasonable to impose a duty.<sup>134</sup> These three criteria were adopted in other cases.<sup>135</sup> In *Caparo*, however, the House of Lords stressed that these criteria were not to be regarded as elements of a general test, because they could not be defined precisely enough to give them such utility.<sup>136</sup>

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cases exist in which liability might accrue for negligently caused economic loss, the *Hedley Byrne* type and those in which the defendant's conduct can be objectively analyzed as involving an assumption of responsibility for the performance of a task, as in *White v. Jones*, *supra* note 105.

<sup>131</sup> *Caparo*, *supra* note 6 at 633, 635-36, Lord Oliver, adopting the incremental approach advocated by Brennan J. in *Sutherland Shire Council v. Heyman* (1985), 60 A.L.R. 1 at 43-44, 157 C.L.R. 424, 59 A.L.J.R. 564 (H.C.). See also *Caparo*, *ibid.* at 618, Lord Bridge, at 628, Lord Roskill. This approach was approved in *Murphy*, *supra* note 112 at 461, 472; *Evatt*, *supra* note 104 at 809; *Norsk*, *supra* note 94 at 1139, 1149-50; *BCCI*, *ibid.*

<sup>132</sup> *Caparo*, *ibid.* at 635.

<sup>133</sup> *Supra* note 100 at 864-65.

<sup>134</sup> *Caparo*, *supra* note 6 at 617-18. See *e.g. ibid.* at 633, Lord Oliver.

<sup>135</sup> *Morgan Crucible*, *supra* note 124 at 317; *Al Saudi*, *supra* note 124 at 329; *McNaughton Ltd. v. Hicks Anderson & Co.*, [1991] 2 Q.B. 113 at 123, [1991] 7 All E.R. 134 [hereinafter *McNaughton* cited to Q.B.]; *Possfund v. Diamond*, [1996] 2 All E.R. 774 at 782, 787, [1996] 1 W.L.R. 1351 (Ch.D.) [hereinafter *Possfund* cited to All E.R.]; *Al-Nakib Investments v. Longcroft*, [1990] 3 All E.R. 321 at 328, [1990] 1 W.L.R. 1390 (Ch.D.) [hereinafter *Al-Nakib* cited to All E.R.]; *Spring*, *supra* note 104 at 342; *BCCI*, *supra* note 122.

<sup>136</sup> See *Caparo*, *supra* note 6, *e.g.* at 618, Lord Bridge, describing the criteria as "convenient labels", at 628, Lord Roskill. See also Jackson & Powell, *supra* note 1 at 21; *Morgan Crucible*, *ibid.* at 317.

## ii. The Restriction on the Scope of the Duty of Care

In addition to finding an adequate approach to evaluate the existence of a duty of care, the courts also had to ensure that, once this duty was found, its scope would be limited adequately. The first judge to express this concern was Lord Denning in *Candler*. In his dissent, he outlined the necessity of limiting the ambit of the duty of care owed by accountants both in terms of persons to whom they show their accounts, or to whom they know the accounts will be shown, and with respect to the transactions for which the auditors know the accounts will be required.<sup>137</sup>

In *Caparo* the House of Lords followed the path taken by Lord Denning:

What can be deduced from the *Hedley Byrne* case, therefore, is that the necessary relationship between the maker of the statement or giver of advice (the adviser) and the recipient who acts in reliance upon it (the advisee) may typically be held to exist where (1) the advice is required for a purpose, whether particularly specified or generally described, which is made known, either actually or inferentially, to the adviser at the time when the advice is given, (2) the adviser knows, either actually or inferentially, that his advice will be communicated to the advisee, either specifically or as a member of an ascertainable class, in order that it should be used by the advisee for that purpose, (3) it is known, either actually or inferentially, that the advice so communicated is likely to be acted upon by the advisee for that purpose without independent inquiry and (4) it is so acted on by the advisee to his detriment.<sup>138</sup>

These factors were adopted in several cases.<sup>139</sup> In addition, some judges juggled with the idea that the defendant's intent that the plaintiff rely on the financial statement must also be found as an indicator of proximity.<sup>140</sup> This restrictive tendency was recently rejected, however, by the Court of Appeal in *BCCI*.<sup>141</sup>

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<sup>137</sup> *Candler*, *supra* note 118 at 180, 182.

<sup>138</sup> *Caparo*, *supra* note 6 at 638, Lord Oliver. See also *ibid.* at 620-21, Lord Bridge, at 658, Lord Jauncey.

<sup>139</sup> *Al Saudi*, *supra* note 124 at 330; *Morgan Crucible*, *supra* note 124 at 319-20; *Al-Nakib*, *supra* note 135 at 326; *Spring*, *supra* note 104 at 332; *McNaughton*, *supra* note 135 at 125-26. See also *Yianni v. Edwin Evans and Sons*, [1981] 3 W.L.R. 843 at 857, [1981] 3 All E.R. 592 (Q.B.D.); *Smith*, *supra* note 100 at 847-48; *Andrew*, *supra* note 130 at 654.

<sup>140</sup> See *Possfund*, *supra* note 135 at 787; *Anthony v. Wright*, [1995] 1 B.C.L.C. 237 at 239, [1995] B.C.C. 768 (Ch.), relying on *Galoo Ltd. v. Bright Grahame Murray*, [1995] 1 All E.R. 16 at 36-37, 43, [1995] B.C.C. 768 (C.A.); *Al Saudi*, *ibid.* at 330; *Morgan Crucible*, *ibid.* at 319-20; *McNaughton*, *ibid.* at 125; *Clerk*, *supra* note 91 at 281.

<sup>141</sup> *Supra* note 122. However, in *Andrew*, *supra* note 130, Beldam L.J. mentions at 654 that the defendants, in certifying the accounts of their client, were doing so with the intention that the plaintiff should act upon them. See also *Dugdale & Stanton*, *supra* note 99 at 120.

These limiting devices developed by the English courts found their way across the Atlantic, just as did the efforts to establish factors facilitating the search for the duty of care. They have, however, come into play within a different legal framework.

*b. Canada*

*i. Haig v. Bamford: The Incorporation of Hedley Byrne*

In Canada the landmark case in the area of auditors' liability towards third parties was, for many years, the 1976 case of *Haig*,<sup>142</sup> in which the Supreme Court of Canada incorporated *Hedley Byrne* into Canadian law. A firm of accountants had issued an unqualified opinion on the financial statements of a private company. No audit had been carried out, but the report led the reader to believe the contrary. When the company ceased trading, the plaintiff, who had purchased shares of the company and guaranteed a bank loan in its favour, sued the accountants for his loss. The evidence showed that the accountants knew that the financial statements were prepared for the purpose of influencing a limited number of potential investors, but that the plaintiff was completely unknown to them. Dickson J. (as he then was) outlined three possible tests to determine the existence of a duty of care:

- (i) foreseeability of the use of the financial statements and the auditor's report thereon by the plaintiff and reliance thereon; (ii) actual knowledge of the limited class that will use and rely on the statements; (iii) actual knowledge of the specific plaintiff who will use and rely on the statement.<sup>143</sup>

The third test was rejected because it was considered too narrow, and the larger "limited class test" was adopted by the Court.<sup>144</sup> It was not important that the accountants did not know the exact identity of the plaintiff as long as he was within the limited class of persons to whom they knew the company intended to supply the statements for a specific class of transaction. Hence, the applicability of the "foreseeability test" was not evaluated. Subsequent case law did not determine whether or not this broad test could be acceptable on its own,<sup>145</sup> but rather expressed suspicion towards it.<sup>146</sup>

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<sup>142</sup> *Supra* note 2.

<sup>143</sup> *Ibid.* at 476.

<sup>144</sup> See also *Aleman*, *supra* note 104 at 71, 73; *Twiggco Financial v. Peat Marwick Thorne* (1994), 12 B.L.R. (2d) 1 at 6 (Ont. Gen. Div.) [hereinafter *Twiggco*]. For cases of misrepresentation, see *Edgeworth*, *supra* note 127 at 214.

<sup>145</sup> J.E. Sexton & J.W. Stevens, "Accountants' Legal Responsibilities and Liabilities" in *Meredith Memorial Lectures 1983-84: Professional Responsibility in Civil Law and Common Law* (Don Mills: Richard De Boo Publishers, 1985) 88 at 90; G.B. Maughan & M. Paskell-Mede, "Auditors' Liability since *Haig v. Bamford*" in *ibid.*, 57 at 61.

In the following years, under the influence of *Candler*, *Haig*, and *Caparo*, the courts introduced the notion of knowledge of the plaintiff and of the transaction as indicators of proximity, and as a means of restricting the scope of the duty of care.<sup>147</sup> Some courts also adopted the threefold test of *Smith* and *Caparo*.<sup>148</sup> The reception of *Caparo* into Canadian law was, however, only partial, since the Supreme Court did not follow *Caparo*'s rejection of the *Anns* approach to the duty of care.

## ii. *Hercules*: The Reign of *Anns*

While the *Anns* test changed the way Canadian courts deal with the issue of duty of care, it was not clearly applied in negligent misstatement cases until 1997.<sup>149</sup>

Both *Anns* and *Caparo* had an important impact on the path taken by the Supreme Court of Canada in *Hercules*,<sup>150</sup> in which the Court decided that the test used in other

<sup>146</sup> See *Rangen Inc. v. Deloitte & Touche*, [1994] 10 W.W.R. 55, 95 B.C.L.R. (2d) 182 (C.A.) [hereinafter *Rangen*]; *BCCA*, *supra* note 16, s. 100; *Dixon v. Deacon Morgan McEwan Easson* (1989), 64 D.L.R. (4th) 441 at 445, 41 B.C.L.R. (2d) 82 (S.C.) [hereinafter *Dixon* cited to D.L.R.]; *Aleman*, *supra* note 104 at 471; *Kripps v. Touche Ross & Co.*, motion to strike claim (1990), 52 B.C.L.R. (2d) 291 (S.C.) [hereinafter *Kripps* (motion to strike (S.C.))], *aff'd* (1992), 94 D.L.R. (4th) 284, 69 B.C.L.R. (2d) 62 (C.A.), leave to appeal to S.C.C. refused, [1993] 2 S.C.R. viii, 101 D.L.R. (4th) vii, trial of action, [1995] 6 W.W.R. 180, 5 B.C.L.R. (3d) 22 (S.C.) [hereinafter *Kripps* (trial of action (S.C.))], *rev'd*, [1997] 6 W.W.R. 421, 33 B.C.L.R. (3d) 254 (C.A.) [hereinafter *Kripps* (trial of action (C.A.)) cited to W.W.R.], leave to appeal to S.C.C. refused (1997), 225 N.R. 236 (note), 102 B.C.A.C. 238 (note) (S.C.C.), remitted for resolution of contributory negligence and quantum (1998), [1999] 3 W.W.R. 629, 41 B.L.R. (2d) 124 (B.C. S.C.) [hereinafter *Kripps* (contributory negligence and quantum) cited to W.W.R.]; *Toronto-Dominion Bank v. Deloitte Haskins & Sells* (1991), 5 O.R. (3d) 417 at 422, 8 C.C.L.T. (2d) 322 (Gen. Div.) [hereinafter *TD Bank* cited to O.R.]; Fridman, vol. 1, *supra* note 97 at 281; Feldthusen, *supra* note 98 at 22, 33; Dugdale & Stanton, *supra* note 99 at 122. *Contra* Sexton & Stevens, *ibid.* at 99-102, whose views were rejected in *Hercules*, *supra* note 100 at 196-97; see also Linden, *supra* note 114 at 407.

<sup>147</sup> See *Twiggo*, *supra* note 144 at 6, 9; *Hercules*, *ibid.* at 197; *Canadian Commercial Bank v. Crawford, Smith & Swallow* (1993), 9 B.L.R. (2d) 311 at 320, 322, 15 C.C.L.T. (2d) 273 (Ont. Gen. Div.), Rosenberg J. [hereinafter *Crawford* cited to B.L.R.]; *Toromont Industrial Holdings v. Thorne, Gunn, Helliwel & Christenson* (1975), 10 O.R. (2d) 65 at 87, 62 D.L.R. (3d) 225 (H.C.J.) [hereinafter *Toromont Industrial* cited to O.R.], *rev'd* on other grounds (1976), 14 O.R. (2d) 87, 73 D.L.R. (3d) 122 (C.A.), leave to appeal to S.C.C. refused (1976), 13 N.R. 539 (note), 30 C.P.R. (2d) 93 (note) (S.C.C.); *Dixon*, *ibid.* at 445; *TD Bank*, *ibid.* See also *Rivtow Marine*, *supra* note 100 at 1196, 1200; *Campion & Dimmer*, *supra* note 100 at 8-7; *Fleming*, *supra* note 91 at 710-11.

<sup>148</sup> See *Akhtar v. MacGillivray & Co.* (1990), 112 A.R. 242 at 268, 77 Alta. L.R. (2d) 337 (Q.B.) (*obiter*) [hereinafter *Akhtar* cited to A.R.]; *Dixon*, *ibid.*

<sup>149</sup> Its influence was nevertheless sometimes noticed. See e.g. *Edgeworth*, *supra* note 127 at 214ff. See also, in cases of pure economic loss, *Kanloops*, *supra* note 114 at 10; *B.D.C.*, *supra* note 100 at 242; *V.K. Mason Construction v. Bank of Nova Scotia*, [1985] 1 S.C.R. 271 at 284, 16 D.L.R. (4th) 598, Wilson J. [hereinafter *V.K. Mason* cited to S.C.R.]. *Contra Kripps* (trial of action (S.C.)), *supra* note 146.

instances of negligence, namely the *Anns* test, should be applied in negligent misstatement cases. In doing so, the Court moved away from *Caparo*, but only to come back to it by incorporating, within the framework of the *Anns* test, most of the principles developed by *Caparo* to limit the ambit of the duty of care.

In *Hercules* the auditors provided audit reports to the shareholders of two companies. When the companies became insolvent, the shareholders brought an action against the auditors alleging that the audit reports were negligently prepared. They pleaded that, in reliance on these reports, they had suffered financial losses. In a unanimous judgment, the Court refused this argument and applied the two-stage test of *Anns*. Hence, the prima facie duty of care depended on the existence of a sufficiently close relationship of "neighbourhood" or "proximity". Believing, however, that foreseeability of harm was not a sufficient criterion for the assessment of proximity, La Forest J. adopted instead the "foreseeability/reasonable reliance test". This test considers whether the defendant ought reasonably to have foreseen that the plaintiff would rely on his or her misrepresentation, and whether reliance by the plaintiff would be reasonable in the particular circumstances of the case.

The Court recognized the breadth of this test as compared with the English courts' reasoning, which requires that the defendant know the identity of the plaintiff or the class of plaintiffs who will rely on the financial statement, and that the reliance losses stem from the particular transaction in respect of which the statement was made.<sup>151</sup> The Court was thus concerned with establishing limits, since its test was otherwise susceptible of being satisfied in every case.<sup>152</sup> La Forest J. believed, though, that these limiting concepts were nothing other than ways of circumscribing, for reasons of policy, the scope of the potential liability of the author of the statement, and ways to avoid the danger of indeterminate liability.<sup>153</sup> Therefore, the limiting concepts had to be dealt with within the second step of the *Anns* test. It is this requirement that the plaintiffs failed to meet. While there was no apparent concern for indeterminate liability, since the identities of the plaintiffs were known to the auditors, the plaintiffs did not show that the statement was used by them "for precisely the purpose or transaction for which it was prepared."<sup>154</sup>

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<sup>150</sup> *Supra* note 100.

<sup>151</sup> *Ibid.* at 190, referring specifically to *Candler*, *supra* note 118; *Hedley Byrne*, *supra* note 101; *Caparo*, *supra* note 6; *Haig*, *supra* note 2.

<sup>152</sup> *Hercules*, *ibid.* at 193-94.

<sup>153</sup> See also *Crawford*, *supra* note 147 at 322, which seemed to announce this distinction.

<sup>154</sup> *Hercules*, *supra* note 100 at 203.

## 2. Knowledge of the Plaintiff and the Contemplated Transaction

Hence, in Canada and in England, the courts have applied these two requirements in several cases to avoid imposing liability on an indeterminate class of defendants.<sup>154</sup> In most cases, actual knowledge was not essential, and the knowledge attributed to a reasonable person in the same circumstances was sufficient.<sup>155</sup>

These factors are easy to assess where the report has been requested, directly or indirectly, for a specific purpose. The cases are not always so clear, however; indeed, the auditor's report is frequently used by persons, and for purposes, other than those for which it was prepared. To what extent, in such a case, will the courts extend these flexible notions to allow recovery?

### a. *The Scope of the Limited Class*

The specific identification of the plaintiff is not a necessary requirement, and knowledge that the plaintiff is a member of a limited class, which the auditor knows is targeted by the financial information, is sufficient.<sup>157</sup> The "limited group or class" concept has, however, been described as ambiguous,<sup>158</sup> and is susceptible of being fashioned according to the needs of each specific case. The limits of its scope therefore attracted the attention of judges.

This question is particularly relevant in the case of public companies, whose financial statements are included in prospectuses available to the general public. Even in this context, though, the courts are generally reluctant to extend the right of recovery to members of the general public.<sup>159</sup> *Caparo* expressed this reluctance to permit too large a class to claim damages from auditors, even in the case of a public company:

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<sup>154</sup> See text accompanying notes 137-39, 144, 147.

<sup>155</sup> See *McNaughton*, *supra* note 135 at 126; *Caparo*, *supra* note 6 at 638, 641; *Al-Nakib*, *supra* note 135 at 326; *BCCI*, *supra* note 122 ("presumed knowledge"); *Morris*, *supra* note 100 at 13; *Twiggco*, *supra* note 144 at 9; *Toromont Industrial*, *supra* note 147 at 87; *Aleman*, *supra* note 104 at 71; *Andrew*, *supra* note 130 at 653-54, 656, in which the knowledge was in fact actual. *Contra Rangen*, *supra* note 146 at paras. 28-33; *Haig*, *supra* note 2 at 476.

<sup>157</sup> See *Hedley Byrne*, *supra* note 101 at 482, 499; *Haig*, *ibid.* at 483. See also *B.D.C.*, *supra* note 100 at 241; *Stanton*, *supra* note 99 at 344. *Contra Candler*, *supra* note 118 at 183; however, Lord Denning, in *obiter*, mentioned that liability could also arise if the accountant prepared his accounts for the guidance of a specific class of persons; *Smith*, *supra* note 100 at 865; see *Caparo*, *supra* note 6 at 658, Lord Jauncey.

<sup>158</sup> See B.M. Knoppers, *Professional Liability in Canada* (Cowansville, Qc.: Yvon Blais, 1988) at 187; *Ivankovich*, *supra* note 96 at 524-26.

<sup>159</sup> See e.g. *Candler*, *supra* note 118 at 180; *Hedley Byrne*, *supra* note 101 at 483; *Possfund*, *supra* note 135 at 782; *Dixon*, *supra* note 146 at 449-50; *Akhtar*, *supra* note 148 at 268-69. See also *B.D.C.*, *supra* note 100 at 241. *Contra Kripps* (motion to strike (S.C.)), *supra* note 146 at 302.

The situation is entirely different where a statement is put into more or less general circulation and may foreseeably be relied on by strangers to the maker of the statement for any one of a variety of purposes which the maker of the statement has no specific reason to anticipate. To hold the maker of the statement to be under a duty of care in respect of the accuracy of the statement to all and sundry for any purpose for which they may choose to rely on it is not only to subject him in the classic words of Cardozo CJ to "liability in an indeterminate amount for an indeterminate time to an indeterminate class" ... it is also to confer on the world at large a quite unwarranted entitlement to appropriate for their own purposes the benefit of the expert knowledge or professional expertise attributed to the maker of the statement.<sup>160</sup>

### *b. The Scope of the Transaction*

As for the second limiting element, the courts generally require that the specific transaction in sight be known to the defendant.<sup>161</sup> Since most cases have involved either a situation where the transaction was specifically known to the defendant, or not known at all, it is open to discussion whether the courts would agree to enlarge the test so as to include transactions of a "type" known to the auditors.

The courts have faced the interesting question of whether shareholders should be treated differently, since the audited financial statements are legally prepared for the primary purpose of protecting their interest.<sup>162</sup> Auditors should normally foresee that shareholders will have access to the audited statements and might rely on them. Nonetheless, the company's shareholders have not benefited from any special treatment. In *Caparo* the House of Lords rejected the contention that shareholders should be treated specially by stating that the purpose of a statutory audit is not to assist the shareholders in making individual speculations with a view to profit.<sup>163</sup> The interest of the shareholders is, rather, a collective interest in the company's proper management.<sup>164</sup> When this interest is infringed, the claim must be made in the name of the company.<sup>165</sup> This distinction was subsequently approved in England<sup>166</sup> and in Canada.<sup>167</sup>

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<sup>160</sup> *Caparo*, *supra* note 6 at 621.

<sup>161</sup> See *Berg Sons*, *supra* note 123 at 1069; *Al-Nakib*, *supra* note 135 at 329; *Smith*, *supra* note 100 at 847; see also *Caparo*, *ibid.* at 658, Lord Jauncey.

<sup>162</sup> See Part I, above.

<sup>163</sup> *Supra* note 6 at 653, Lord Oliver.

<sup>164</sup> *Ibid.* at 654, Lord Oliver, at 662, Lord Jauncey.

<sup>165</sup> See *ibid.* at 626, Lord Bridge.

<sup>166</sup> *Berg Sons*, *supra* note 123 at 1064. See also *West Wiltshire District Council v. Garland*, [1995] 2 W.L.R. 439 at 445-46, [1995] 2 All E.R. 17 (C.A.).

<sup>167</sup> *Hercules*, *supra* note 100 at 205-207; *Roman I*, *supra* note 45 at 256, 260-61; *Roman Corp. v. Peat Marwick Thorne* (1993), 12 B.L.R. (2d) 10 at 18, 21 (Ont. Gen. Div.).

Nevertheless, this rule does not preclude every action brought by a shareholder. In fact, if a shareholder can show that a duty of care was owed to him or her independently from any duty owed to the company or to the body of shareholders, as where the auditors know that an individual shareholder is likely to rely on the accounts for a particular purpose, the claim will succeed.<sup>165</sup>

### 3. The Reliance/Reasonable Reliance Requirement

To establish the existence of a relationship of proximity, plaintiffs must demonstrate not only that the defendant knew actually or inferentially that his or her advice would be relied on,<sup>169</sup> or in Canada, that the reliance was foreseeable,<sup>170</sup> but also that the plaintiff did in fact rely on the statements.<sup>171</sup> This last criterion is not only relevant when assessing the existence of a duty of care, but also essential to the evaluation of causation.<sup>172</sup>

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<sup>165</sup> *Caparo*, *supra* note 6 at 662. See also *Possfund*, *supra* note 135 at 788; *Twiggco*, *supra* note 144 at 8.

<sup>169</sup> See *Caparo*, *ibid.* at 638, Lord Oliver. The following cases also consider actual and/or deemed knowledge of the reliance necessary to find a duty of care on the part of the defendant: *Hedley Byrne*, *supra* note 101 at 486, 502-503, 514; *Candler*, *supra* note 118 at 185; *McNaughton*, *supra* note 135 at 126; *Smith*, *supra* note 100 at 863; *Yorkshire Enterprise v. Robson Rhodes*, *supra* note 130; *Electra Private*, *supra* note 122; *Grand Restaurants of Canada v. Toronto (City of)* (1981), 32 O.R. (2d) 757 at 772, 123 D.L.R. (3d) 349, Trainor J. (H.C.J.) [hereinafter *Grand Restaurants* cited to O.R.], *aff'd* (1982), 39 O.R. (2d) 752, 140 D.L.R. (3d) 191 (C.A.); *Edgeworth*, *supra* note 127 at 214; *Fletcher*, *supra* note 100 at 212; *Kingu v. Walmar Ventures* (1986), 10 B.C.L.R. (2d) 15 at 23, 38 C.C.L.T. 51 (C.A.) [hereinafter *Kingu* cited to B.C.L.R.]. See Dugdale & Stanton, *supra* note 99 at 116-17, 125-26, 139; *Linden*, *supra* note 114 at 435; *Fridman*, vol. 1, *supra* note 97 at 267. But see the criticism of M.A. Jones, *Textbook on Torts*, 6th ed. (London: Blackstone, 1998) at 104, who believes that a requirement of actual knowledge would be unworkable.

<sup>170</sup> See *Kingu*, *ibid.* at 28.

<sup>171</sup> See generally *Caparo*, *supra* note 6 at 638; *Candler*, *supra* note 118 at 182-83; *Ross*, *supra* note 116 at 313; *Junior Books*, *supra* note 100 at 546; *JEB Fasteners (C.A.)*, *supra* note 123 at 589; *McNaughton*, *supra* note 135 at 126-27; *Edgeworth*, *supra* note 127 at 214; *Fletcher*, *supra* note 100 at 209; *B.D.C.*, *supra* note 100 at 242; *Toromont Industrial*, *supra* note 147 at 87; *Surrey Credit Union v. Willson* (1990), 49 B.C.L.R. (2d) 102 at 105, 107, 73 D.L.R. (4th) 207 (S.C.) [hereinafter *Surrey Credit Union* cited to B.C.L.R.]; *Fridman*, vol. 1, *supra* note 97 at 267; *Fridman*, vol. 2, *supra* note 107 at 138.

<sup>172</sup> *JEB Fasteners (C.A.)*, *ibid.* at 585, 589; *JEB Fasteners (Q.B.)*, *supra* note 123 at 304. See also *Henderson*, *supra* note 126 at 180; *Evatt*, *supra* note 104 at 811; *Ross*, *ibid.* at 313-14; *Akhtar*, *supra* note 148 at 269; *Kripps* (trial of action (C.A.)), *supra* note 146, citing *Cognos*, *supra* note 100, in which the criterion of reasonable reliance is listed separately from the duty of care requirement and thus may be referred to as establishing causation; *Kingu*, *supra* note 169 at 23; *Morris*, *supra* note 100 at 5. J.A. Campion & S.A. Brown, "Professional Liability of Auditors" (1994) *Advocates' Q.* 314 at 331, also list reasonable reliance separately. Finally, actual reliance was similarly part of the assess-

To meet the requirement of actual reliance, it is not sufficient for the plaintiffs to show that they were aware of the statements. They must demonstrate, on a preponderance of evidence, that the financial statements were a real inducement for entering the transaction. In the words of Stephenson L.J. in *JEB Fasteners* (C.A.), the financial statements must have played a "real and substantial part" in inducing the plaintiff to act, without being necessarily a decisive part.<sup>173</sup> Furthermore, the misstatement does not have to be the only or the main element in the plaintiff's decision-making process, nor does it have to have been fundamental to the latter. Hence, plaintiffs are entitled to succeed if they prove that the statements were one of the factors in the decision.<sup>174</sup>

Once reliance on the statements is proven, the defendant may, however, rebut the prima facie causation deduced from them.<sup>175</sup> Liability will not be found if the plaintiff would have acted in the same way even if the statement had disclosed the real situation,<sup>176</sup> or if the plaintiff decided to invest before reviewing the financial statements<sup>177</sup> or in the full knowledge of the true state of affairs.<sup>178</sup> In short, there is no compensation if the same loss would have been suffered in any event.<sup>179</sup>

ment of the causal link in *Hercules*, *supra* note 100 at 184, since La Forest J. believed it was not necessary to inquire into the matter of actual reliance given that the absence of a duty of care made this question inconsequential. See *Sexton & Stevens*, *supra* note 145 at 103; *Campion & Dimmer*, *supra* note 100 at 8-1; *Fleming*, *supra* note 91 at 714; *Jackson & Powell*, *supra* note 1 at 295; *Howarth*, *supra* note 94 at 278; *Dugdale & Stanton*, *supra* note 99 at 117; *Linden*, *supra* note 114 at 445; *H. Rowan*, "Just How Far Does Third-Party Liability Extend?" (1982) 2:115 C.A. Mag. 68 at 69.

<sup>173</sup> *JEB Fasteners* (C.A.), *ibid.* at 588-89, Stephenson L.J., at 588, Donaldson L.J.; *Surrey Credit Union*, *supra* note 171 at 108 (the statements must be a "real inducement into entering upon the transaction"); *Akhtar*, *ibid.* at 252, 269; *Campion & Brown*, *ibid.* at 333; *Feldthusen*, *supra* note 98 at 34. In *Kripps* (trial of action (C.A.)), *ibid.* at 450, Finch J.A. held that reliance may be inferred where the representation is calculated to induce the plaintiff to act.

<sup>174</sup> See *JEB Fasteners* (C.A.), *ibid.* at 588; *Surrey Credit Union*, *ibid.* at 122; *Kripps* (trial of action (C.A.)), *ibid.* at 450. See also *Fleming*, *supra* note 91 at 714; *Jackson & Powell*, *supra* note 1 at 899.

<sup>175</sup> *Kripps* (trial of action (C.A.)), *ibid.*

<sup>176</sup> *JEB Fasteners* (C.A.), *supra* note 123 at 588, Donaldson L.J., at 589, Stephenson L.J.; *JEB Fasteners* (Q.B.), *supra* note 123 at 305; *Surrey Credit Union*, *supra* note 171 at 125.

<sup>177</sup> *Toromont Industrial*, *supra* note 147 at 94.

<sup>178</sup> *Haig*, *supra* note 2 at 484.

<sup>179</sup> But in *Downs v. Chappell* (1996), [1996] 3 All E.R. 344 at 351, [1997] 1 W.L.R. 426 (C.A.), the English Court of Appeal stressed that once it is shown that the plaintiff was in fact induced by a material misrepresentation to act to his detriment, the question of whether he would have gone ahead had the correct information been supplied becomes irrelevant. See also *Bristol and West Building Society v. Mothew* (1996), [1996] 4 All E.R. 698 at 705-706, [1997] 2 W.L.R. 436 (C.A.), where Millett L.J. limited this reasoning to cases in which a negligent misstatement is communicated, by opposition to an omission to give appropriate information or advice. In both cases, which did not involve auditors' liability, *JEB Fasteners* was not referred to. See the criticism of Jones, *supra* note 169 at 109-10; comments in *Swindle v. Harrison*, [1997] 4 All E.R. 705 at 728, [1997] P.N.L.R. 641 (C.A.). In light of *JEB Fasteners*, causation can indeed be inferred without the need for the plaintiff to comply with a

The second aspect of the reliance requirement used in the evaluation of the defendant's duty of care is that the reliance be reasonable.<sup>173</sup> Feldthusen outlines different factors that can be used to distinguish the situations where the reliance is reasonable from those where it is not:

- 1) the defendant had a direct or indirect financial interest in the transaction in respect of which the representation was made;
- 2) the defendant was a professional or someone who possessed special skill, judgement or knowledge;
- 3) the advice or information was provided in the course of the defendant's business;
- 4) the information or advice was given deliberately, and not on a social occasion;
- 5) the information or advice was given in response to a specific enquiry or request.<sup>181</sup>

Reasonableness has been questioned where the plaintiff was an expert, or was knowledgeable in the subject matter of the inquiry and did not verify the accuracy of the statement or representation made by the defendant,<sup>182</sup> where the relative positions of the parties were such that the plaintiff ought to have verified the accuracy of the in-

burden of proof as stringent as the one imposed by the "but for" test of causation. This is true despite the existence of cases in which causation was assessed on the basis of such a reasoning. See *e.g.* *Gran Gelato v. Richcliff Ltd.* (1991), [1992] Ch. 560 at 569, [1992] 1 All E.R. 865 [hereinafter *Gran Gelato* cited to Ch.] (in the context of a claim under the *Misrepresentation Act 1967*, s. 2(1)); *Hongkong Bank of Canada v. Touche Ross & Co.* (1989), 36 B.C.L.R. (2d) 381 at 385 (C.A.) [hereinafter *Hongkong v. Touche*]; *Lloyd Cheyham & Co. v. Littlejohn & Co.* (1986), [1987] B.C.L.C. 303 at 305, 319, [1986] P.C.C. 389 (Q.B.) [hereinafter *Lloyd Cheyham* cited to B.C.L.C.]; *1874000 Nova Scotia v. Adams* (1997), 146 D.L.R. (4th) 466 at 472, 475, 159 N.S.R. (2d) 260 (C.A.) [hereinafter *Adams*]. Nevertheless, this does not prevent defendants from negating causation by showing that even if they had not been negligent, the loss would have been suffered in any event.

<sup>180</sup> See *e.g.* *McNaughton*, *supra* note 135 at 126-27; *Grand Restaurants*, *supra* note 169 at 772; *Fletcher*, *supra* note 100 at 209; *Edgeworth*, *supra* note 127 at 212; *Kripps* (contributory negligence and quantum), *ibid.* at 633; *Keith Plumbing*, *supra* note 127; W.V.H. Rogers, *Winfield & Jolowicz on Torts*, 15th ed. (London: Sweet & Maxwell, 1998) at 384; *Fridman*, vol. 1, *supra* note 97 at 267. Some cases specify that reasonableness has to be warranted by the particular situation of the parties. See *e.g.* *Hedley Byrne*, *supra* note 101 at 486, 503, 514; *Smith*, *supra* note 100 at 847-48; *McNaughton*, *supra* note 135 at 126-27; *JEB Fasteners* (Q.B.), *supra* note 123 at 296-97; *Hercules*, *supra* note 100 at 188; *Clerk*, *supra* note 91 at 294; *McGauley v. British Columbia* (1990), 44 B.C.L.R. (2d) 217 at 232 (S.C.), *rev'd* on other grounds (1991), 56 B.C.L.R. (2d) 1 (C.A.).

<sup>181</sup> Feldthusen, *supra* note 98 at 62-63. These factors were adopted in *Hercules*, *ibid.* at 202, where the Court held, however, that these elements should not be seen as strict tests of reasonableness.

<sup>182</sup> *Fridman*, vol. 1, *supra* note 97 at 267; *Fridman*, vol. 2, *supra* note 107 at 139, citing *Banque Bruxelles Lambert SA v. Eagle Star Insurance*, [1995] 2 All E.R. 769, [1995] 2 W.L.R. 607 (Q.B.D.) [hereinafter *Eagle Star* cited to All E.R.]. See also *McNaughton*, *supra* note 135 at 128.

formation;<sup>183</sup> and where the information was outdated.<sup>184</sup> Conversely, reliance was found to be reasonable where the statements were prepared by two respected auditing firms in accordance with relevant legislative and regulatory schemes.<sup>185</sup>

Reasonableness of the reliance can also be relevant to the assessment of causation.<sup>186</sup> Thus, it is possible for the defendant to defeat a claim on the ground that it was the plaintiff's negligence or recklessness, and not the defendant's representation, that caused the loss.<sup>187</sup> It can also be contended that the plaintiff's negligence evidences that the plaintiff would have acted in the same way even with knowledge of the true situation.<sup>188</sup>

Finally, the reasonableness of the reliance is important to establish the defence of contributory negligence.<sup>189</sup> It is generally accepted that the English *Law Reform (Contributory Negligence) Act 1945* is applicable to instances involving negligent misstatements.<sup>190</sup> This statute allows a court to reduce the amount of damages recoverable by the plaintiff if the latter is also found negligent,<sup>191</sup> and if this negligence has contributed to the loss suffered.<sup>192</sup> In Canada the defence of contributory negligence has been similarly accepted in the context of negligent misstatements.<sup>193</sup>

<sup>183</sup> *McNaughton*, *ibid.* at 127-28. In this case, however, the accounts were only draft accounts.

<sup>184</sup> *Ibid.* at 106. In *JEB Fasteners (Q.B.)*, *supra* note 123 at 297, and *Berg Sons*, *supra* note 123, this element affected the foresight of reliance.

<sup>185</sup> *Surrey Credit Union*, *supra* note 171 at 123.

<sup>186</sup> *Linden*, *supra* note 114 at 445.

<sup>187</sup> *Evatt*, *supra* note 104 at 811, Lord Reid, Lord Morris, dissenting; *Berg Sons*, *supra* note 123 at 1070; *Strover v. Harrington*, [1988] 1 All E.R. 769, 780-81, [1988] 2 W.L.R. 572 (Ch.D.); *Mackenzie Financial Corp. v. McRae* (1998), 81 O.T.C. 321 (Gen. Div.). Clerk, *supra* note 91, notes at 295 that this could be the case if the plaintiff actually knows that the statement is inaccurate.

<sup>188</sup> Howarth, *supra* note 94 at 279.

<sup>189</sup> *Linden*, *supra* note 114 at 448; *Sexton & Stevens*, *supra* note 145 at 104; Howarth, *ibid.* at 279; *Jackson & Powell*, *supra* note 1 at 295; *Fridman*, vol. 2, *supra* note 107 at 138; *Fleming*, *supra* note 91 at 714. *Contra* *Feldthusen*, *supra* note 98 at 22, 128.

<sup>190</sup> (U.K.), 8 & 9 Geo. VI, c. 28. See *Rogers*, *supra* note 180 at 383; *Buckley*, *supra* note 91 at 129-30; *Jackson & Powell*, *ibid.* at 910. See also *JEB Fasteners (Q.B.)*, *supra* note 123 at 297; *Lloyd Cheyham*, *supra* note 179 at 320; *Gran Gelato*, *supra* note 179.

<sup>191</sup> See *Law Reform (Contributory Negligence) Act 1945*, *ibid.*, s. 1(1).

<sup>192</sup> It is not necessary for the plaintiff's negligence to contribute to the accident or other event from which the damage flows. See *Rogers*, *supra* note 180 at 235-37; *Dugdale & Stanton*, *supra* note 99 at 519-24; *Percy*, *supra* note 91 at 202-204; Clerk, *supra* note 91 at 68-72. For Canada, see *Fridman*, vol. 1, *supra* note 97 at 375-80; *Linden*, *supra* note 114 at 438-39.

<sup>193</sup> See *Fridman*, vol. 2, *supra* note 107 at 138-39; *Linden*, *ibid.* at 448; L.N. Klar, "Recent Developments in Canadian Law: Tort Law" (1991) 23 *Ottawa L. Rev.* 177 at 200. The following cases have considered the defence: *Hongkong v. Touche*, *supra* note 179; *Adams*, *supra* note 179. See also the following cases not involving auditor's liability: *Grove Service v. Lenhart Agencies* (1979), 10 C.C.L.T. 101 (B.C. S.C.); *J.D. Irving Ltd. v. Western Plumbing & Heating* (1979), 34 N.S.R. (2d) 285

The fact that reasonable reliance is factored into the recognition of a duty of care and the defence of contributory negligence creates a conceptual difficulty, which continues to be unresolved. It is well explained by Trainor J. in *Grand Restaurants*:

At first blush, there is perhaps some difficulty in finding that a plaintiff ought to recover damages for negligent misrepresentation, which presupposes a *reasonable* reliance on the advice of the defendant, and then to have his damage reduced on account of his reliance ... being to some degree "unreasonable" or excessive.<sup>194</sup>

Similarly, if the plaintiff's reliance on the accounts is so unreasonable as to amount to contributory negligence, it may be argued that he or she cannot be held to have reasonably placed reliance on the statements for the purpose of establishing prima facie liability.<sup>195</sup> Different attempts to resolve this "apparent"<sup>196</sup> contradiction are not all convincing.<sup>197</sup> Despite this difficulty, the courts have nevertheless found contributory negligence along with liability based on reasonable reliance.<sup>198</sup> Some cases, however, have stressed that only in "very special cases" are the courts justified in reducing damages of plaintiffs who have done what the defendant intended them to do by way of reliance on the misrepresentation.<sup>199</sup>

(S.C. (T.D.)); *H.B. Nickerson & Sons v. Wooldridge* (1980), 40 N.S.R. (2d) 388, 115 D.L.R. (3d) 97 (S.C. (A.D.)); *Reardon v. Kings Mutual Insurance Co.* (1981), 44 N.S.R. (2d) 691, 120 D.L.R. (3d) 196 (S.C. (T.D.)); *Dorsch v. Weyburn (City of)* (1985), 43 Sask. R. 46, 23 D.L.R. (4th) 379 (C.A.).

<sup>194</sup> *Grand Restaurants*, *supra* note 169 at 775. See also *JEB Fasteners (Q.B.)*, *supra* note 123 at 297; *Markesinis & Deakin*, *supra* note 94 at 650. This has prompted Lowry J. to say in *Kripps* (contributory negligence and quantum), *supra* note 146 at 633, that it is not very often that a successful plea of contributory negligence in the context of an allegation of negligent misstatement can be made.

<sup>195</sup> *Evatt*, *supra* note 104 at 811, Lord Reid, Lord Morris, dissenting; *Fridman*, vol. 2, *supra* note 107 at 138-39; *Klar*, *supra* note 193 at 200, who believes that apportionment on the basis of contributory negligence is unwise since reasonable reliance is required to establish the duty of care.

<sup>196</sup> *Klar* uses this adjective (*ibid.*).

<sup>197</sup> See e.g. the distinctions made in *Grand Restaurants*, *supra* note 169 at 775-76, analyzed by *Fridman*, vol. 2, *supra* note 107 at 139; *Eagle Star*, *supra* note 182, Phillips J., studied by Clerk, *supra* note 91 at 295, and by Howarth, *supra* note 94 at 279. This interesting question falls beyond the scope of this article.

<sup>198</sup> *Eagle Star*, *ibid.* at 773-76; *Platform House Loans v. Oyston Shipways*, [1998] 4 All E.R. 252, [1998] 3 W.L.R. 94 (Ch.D.); *Edwards v. Lee* (1991), 141 N.L.J. 1517, *The Independent* (1 November 1991) (Q.B.); *Grand Restaurants*, *ibid.* at 773-76; *Hongkong v. Touche*, *supra* note 179; *Lewis v. Coles* (1992), 47 C.C.E.L. 302 (B.C. S.C.); *O.E.X. Electromagnetic v. Coopers & Lybrand* (1992), 75 B.C.L.R. (2d) 384 (S.C.); *Surrey Credit Union*, *supra* note 171 at 121; *Kripps* (contributory negligence and quantum), *supra* note 146.

<sup>199</sup> See *Gran Gelato*, *supra* note 179 at 574; *Eagle Star*, *ibid.* at 824.

#### 4. Policy Considerations

Finally, the importance of policy factors in the analysis of the courts must be discussed. In the words of Lord Pearce, "How wide the sphere of the duty of care in negligence is to be laid depends ultimately upon the courts' assessment of the demands of society for protection from the carelessness of others."<sup>200</sup>

The application of policy considerations is usually done at two levels. First, it can be reserved to cases where proximity is satisfied and a prima facie duty of care is found, but where there is nevertheless an interest in refusing recovery, as was the case in *Anns*. Second, it can come into play within the assessment of the requirement of proximity itself, and therefore is a factor in the decision regarding the existence of a duty of care.<sup>201</sup>

The main policy factor, which has preoccupied the English and Canadian common law courts, is the fear of opening the floodgates of litigation.<sup>202</sup> On the one hand, such factors as the fear that an open-ended liability might seriously injure the profession or burden social and commercial life have also been assessed.<sup>203</sup> On the other, these arguments have been balanced against, *inter alia*, the need to deter negligent conduct and to furnish incentives to caution,<sup>204</sup> as well as the fact that auditors are in a better position to protect themselves by getting insurance and passing on its costs to their clients.<sup>205</sup>

#### C. Conclusion

The most interesting features of this comparative study of the English and Canadian common law are the following. First, a very different approach has guided the courts of these two jurisdictions in the determination of the duty of care, especially in

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<sup>200</sup> *Hedley Byrne*, *supra* note 101 at 536.

<sup>201</sup> *Klar et al.*, *supra* note 94 at 139-45.

<sup>202</sup> See *supra* notes 93-97, 121 and accompanying text. *Contra Binder Hamlyn*, *supra* note 130, where it is noted that the extent of potential liability and commercial problems over insurance can be guarded against by a disclaimer as in *Hedley Byrne*, *supra* note 101.

<sup>203</sup> Linden, *supra* note 114 at 423; Knoppers, *supra* note 158 at 184; B.R. Cheffins, "Auditors' Liability in the House of Lords: A Signal Canadian Courts Should Follow" (1991) 18 Can. Bus. L.J. 118 at 127. See also *B.D.C.*, *supra* note 100 at 243.

<sup>204</sup> Linden, *ibid.* at 276; Sexton & Stevens, *supra* note 145 at 100-101; Dugdale & Stanton, *supra* note 99 at 87-88. But see *Hercules*, *supra* note 100, where this argument was said at 194 to be outweighed by the "socially undesirable consequences to which the imposition of indeterminate liability of auditors might lead." See also Cheffins, *ibid.* at 124.

<sup>205</sup> *Scott Group*, *supra* note 123 at 572; *Norsk*, *supra* note 94 at 1123-1125, 1157. For a more extensive discussion of these policy issues, see Cheffins, *ibid.* at 121-28; Ivankovich, *supra* note 96 at 520-21; Howarth, *supra* note 94 at 320; Sexton & Stevens, *ibid.* at 101; Knoppers, *supra* note 158 at 184-85.

recent years. English law has, with the exception of the tendency to use assumption of responsibility as a general test, adopted an incremental approach and refused to state a broad test that would allow a uniform assessment of the right to recovery. In contrast, Canadian courts have proceeded on a more global theoretical basis and endorsed the *Anns* test as applicable to every case of negligence. As has been observed, however, the difference between the Canadian and the English approaches is probably only a question of semantics.<sup>206</sup> In fact, both jurisdictions are concerned with the possibility of indeterminate liability, and concede that foreseeability alone is not sufficient to prevent it. Both systems believe that policy concerns should play an important role, and express the need to impose limitations on recovery to avoid the dangers of indeterminate liability. In addition, both use knowledge about the plaintiff and the contemplated transaction as limiting devices, albeit at different conceptual levels. Finally, both jurisdictions have stressed the necessity of demonstrating reasonable reliance in order to find liability. Thus, on a practical level, these different theoretical approaches have resulted in little divergence in the courts' conclusions. It is now interesting to examine whether one can make a similar observation in the context of a different legal system, the French and Quebec systems of *responsabilité civile*.

### III. The Civil Law

#### A. France and Quebec: The Juridical Context

In order to draw useful conclusions from the present comparative study, it is important to understand from the outset the specific situation of the legal system of Quebec. Moreover, since the question of auditors' liability towards third parties in France and Quebec is not dealt with through the application of a specific system of liability, this section also gives a broad overview of the relevant rules of *responsabilité civile* in these two jurisdictions.

#### 1. Quebec: Tensions and Influences in a Mixed System

The origin and development of Quebec private law is based on French law, and to some extent, it is still very similar to it. In more than three hundred years of autonomous existence, however, Quebec private law has cultivated its own specificity, influenced by its different societal and cultural context and the considerable influence of its common law neighbours.

The Province of Quebec and the state of Louisiana are the two areas in North America where the French legal tradition has survived, despite the fact that they are

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<sup>206</sup> Klar *et al.*, *supra* note 94 at 145.

members of federal countries ruled entirely by the common law tradition. This is particularly true of Quebec, where the French tradition is kept alive outside the legal system, and dominates its language, culture, and social and economic activities. Moreover, while the French tradition has subsisted in the area of private law, the public law of the Province of Quebec is governed by the English common law tradition.<sup>207</sup> The mixed nature of the Quebec legal system, and the sometimes difficult relationship between its French roots and the direct influence of the common law tradition, makes it a fascinating jurisdiction to study.

In 1866 the distinctiveness of the Quebec private law was settled by the drafting of the *Civil Code of Lower Canada*,<sup>208</sup> which aimed to protect the French legal tradition from foreign influences.<sup>209</sup> The C.C.L.C. was in fact seen as the immune system of the French-Canadian nation,<sup>210</sup> and as a means of protecting not only Quebec's legal roots, but also its religious and linguistic heritage. Since then, the distinctiveness of the private law of Quebec has not disappeared, but the need to protect it against foreign imports has been frequently articulated by courts and commentators alike. One of its greatest advocates was Pierre-Basile Mignault.<sup>211</sup> Through the voices of Mignault J., and subsequently of Beetz J., the Supreme Court of Canada insisted on the necessity of refraining from importing common law concepts into Quebec law, while recognizing that the common law could have an influence over the civil law:

Il me semble respectueusement qu'il est temps de réagir contre l'habitude de recourir, dans les causes de la province de Québec, aux précédents du droit commun anglais, pour le motif que le code civil contiendrait une règle qui serait d'accord avec un principe du droit anglais. Sur bien des points, [...] le code civil et le *common law* contiennent des règles semblables. Cependant le droit civil constitue un système complet par lui-même et doit s'interpréter d'après ses propres règles. Si pour cause d'identité de principes juridiques on peut recourir au droit anglais pour interpréter le droit civil français, on pourrait

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<sup>207</sup> This is the result of historical factors flowing from the conquest of Nouvelle France by England during the eighteenth century. For a detailed historical overview, see F.P. Walton, *Le domaine et l'interprétation du Code Civil du Bas-Canada*, trans. M. Tancelin (Toronto: Butterworths, 1980) at 35ff. See also the following constitutional documents: *Royal Proclamation*, 1763 (U.K.), 3 Geo. III; *Quebec Act*, 1774 (U.K.), 14 Geo. III, c. 83; *Constitutional Act*, 1791 (U.K.), 31 Geo. III, c. 31; *Union Act* 1840 (U.K.), 3-4 Vict., c. 35, all reprinted in R.S.C. 1985, App. II.

<sup>208</sup> The private law was reformed in 1991 by the adoption of the *Civil Code of Québec*, which came into force on 1 January 1994.

<sup>209</sup> See P.-A. Crépeau, "Preface" in Office de Révision du Code civil, *Rapport sur le Code civil du Québec*, vol. 1 (Quebec: Éditeur Officiel, 1978) xxv at xxvi-xxvii, cited in M. Guy, "Le Code Civil du Québec: Un peu d'histoire, beaucoup d'espoir" (1993) 23 R.D.U.S. 453 at 461.

<sup>210</sup> See S. Normand, "Un thème dominant de la pensée juridique traditionnelle au Québec: La sauvegarde de l'intégrité du droit civil" (1987) 32 McGill L.J. 559 at 574.

<sup>211</sup> See e.g. P.-B. Mignault, "L'avenir de notre droit civil" (1923) 1 R. du D. 104.

avec autant de raison citer les monuments de la jurisprudence française pour mettre en lumière les règles du droit anglais.<sup>212</sup>

The Court of Appeal of Quebec also endorsed this protectionist position, preferring in some cases to rely on French law for inspiration.<sup>213</sup> In practice, however, the influence of the common law on the civil law of Quebec can be witnessed in many Supreme Court of Canada decisions,<sup>214</sup> as well as in judgments of the Quebec courts, which have sometimes applied common law principles without scruple.<sup>215</sup> One of the fields where this influence is most remarkable is that of auditors' liability towards third parties for negligent misstatements, despite the fact that, in principle, these cases are governed by the general rules of *responsabilité civile*.

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<sup>212</sup> *Desrosiers v. Canada* (1920), 60 S.C.R. 105 at 126, Mignault J., approved in *Rubis v. Gray Rocks Inn*, [1982] 1 S.C.R. 452 at 469, 41 N.R. 108, Beetz J. See also *National Bank v. Soucisse*, [1981] 2 S.C.R. 339, 43 N.R. 283, Beetz J.; *Driver v. Coca Cola*, [1961] S.C.R. 201, 27 D.L.R. (2d) 20, Cartwright J.; *C.N.R. v. Vincent* (1978), [1979] 1 S.C.R. 364, 93 D.L.R. (3d) 663, Pratte J.; *Augustus v. Gosset*, [1996] 3 S.C.R. 268, 138 D.L.R. (4th) 617, L'Heureux-Dubé J.; *Rawleigh Co. v. Dumoulin*, [1926] S.C.R. 551, Mignault J.

<sup>213</sup> *Dodds v. Schierz*, [1986] R.J.Q. 2623 at 2627, 40 C.C.L.T. 167, Monet J. (C.A.). But see *ibid.*, where Rothman J., echoing Mignault J., added at 2638 that when legal provisions are similar, the common law might be helpful. See also *Chouinard v. Landry*, [1987] R.J.Q. 1954 at 1362-69, [1987] R.R.A. 856 (C.A.); *T.S.C.O. of Canada v. Châteauneuf*, [1995] R.J.Q. 637 at 679, 124 D.L.R. (4th) 308 (C.A.); *Elliott v. Entreprises Côte-Nord*, [1976] C.A. 584 [hereinafter *Elliott*]; *J.E. Construction v. General Motors du Canada*, [1985] C.A. 275 at 280 [hereinafter *J.E. Construction*].

<sup>214</sup> See e.g. *Magann v. Auger* (1901), 31 S.C.R. 186; *Drysdale v. Dugas* (1897), 26 S.C.R. 20; *Canada v. Laperrière*, [1946] S.C.R. 415, [1946] 3 D.L.R. 1; *Taillon v. Donaldson*, [1953] 2 S.C.R. 257; *Ouellet v. Cloutier*, [1947] S.C.R. 521; *Tremblay v. Daigle*, [1989] 2 S.C.R. 530, 62 D.L.R. (4th) 634. It must be noted that three judges of the Supreme Court of Canada are appointed from among the judges or advocates of Quebec. See *Supreme Court Act*, R.S.C. 1985, c. S-26, s. 6.

<sup>215</sup> See e.g. *Imasa Ltd. v. Aritex Knitting Mills*, [1977] C.S. 531, rev'd (12 March 1979), Montreal 500-09-000245-779 (C.A.); *Service alimentaire exclusif v. Trust général du Canada*, [1979] C.S. 838, rev'd, [1984] C.A. 145; *Lange Company of Canada v. Platt*, [1973] C.A. 1068, 18 C.P.R. (2d) 144; *O'Hearn v. Estrada* (17 April 1984), Montreal 500-09-000999-813, J.E. 84-449 (C.A.); *Dunant v. Chong* (13 December 1985), Montreal 500-09-000035-816, J.E. 86-73 (C.A.). The influence of the common law can also be witnessed in the C.C.Q. itself, which incorporates rules of common law origin. Moreover, some areas of private law are of federal competence and thereby ruled by federal statutes. Such is the case for bankruptcy and divorce. See *Constitution Act, 1867*, *supra* note 8, ss. 91(21), 91(26).

## 2. *Responsabilité Civile*: General Features

### a. *General Principle of Liability*

In French and Quebec civil law, a plaintiff to any claim in damages benefits from a general right of action,<sup>216</sup> which comes into play whenever three prerequisites are met: the defendant has committed a fault, the plaintiff has suffered harm, and there is a sufficient causal relation between these two events. These three conditions restrict the extent of the general principle of liability. Thus, not every act of the defendant will constitute a fault, and not every harm claimed will be worth compensating. The main controlling device in cases of auditors' negligence causing a loss to third parties, however, is the causation requirement.

### b. *The Causation Requirement*

In France, this condition is expressed in articles 1382 and 1383 of the *Code civil*:

1382. Any human deed whatsoever which causes harm to another creates an obligation in the person by whose fault it was caused to compensate it.

1383. Everyone is liable for the harm which he has caused not only by his deed, but also by his failure to act or his lack of care.<sup>217</sup>

In Quebec, article 1457 of the C.C.Q. lays down this fundamental principle:

1457. Every person has a duty to abide by the rules of conduct which lie upon him, according to the circumstances, usage or law, so as not to cause injury to another.

Where he is endowed with reason and fails in his duty, he is responsible for any injury caused to another by the act or fault of another person or by the act of things in his custody.<sup>218</sup>

The codes do not indicate how the causal link between the fault and the damage should be evaluated, and stress only that the damage must have been the direct<sup>219</sup> and

<sup>216</sup> See arts. 1382-83 C.N.; art. 1457 C.C.Q.

<sup>217</sup> Articles translated in J. Bell, S. Boyron & S. Whittaker, *Principles of French Law* (Oxford: Oxford University Press, 1998) at 355.

<sup>218</sup> The generality of these provisions can be contrasted with the specificity of the provisions of other civil law countries, such as art. 823 of the German *Bürgerliches Gesetzbuch*, which enumerates an exhaustive list of protected rights.

<sup>219</sup> Directness of the damage amounts to causation. See J.L. Baudouin & P. Deslauriers, *La responsabilité civile*, 5th ed. (Cowansville, Qc.: Yvon Blais, 1998) at 158; M. Tancelin, *Des obligations: L'acte illégitime et les modes d'exécution* (Montreal: Wilson & Lafleur, 1993) at 111 [hereinafter *L'acte illégitime*]; P. Conte & P. Maistre du Chambon, *La responsabilité civile délictuelle* (Grenoble: Presses Universitaires de Grenoble, 1994) at 41.

immediate consequence of the fault.<sup>220</sup> While in many cases straightforward, this determination can become a difficult exercise when dealing with several factors susceptible of having caused the damage.<sup>221</sup> To provide guidance in such circumstances, different theories of causation were developed. They do not always respond properly, however, to the specific problems encountered in the practical application of the causation requirement.<sup>222</sup>

i. The Efforts of the Theorists and the Subjectivity of the Courts<sup>223</sup>

Despite the fact that there is no judicial consensus in France and Quebec as to which theory should be favoured,<sup>224</sup> the theory of *causalité adéquate* (adequate causation) is the one that has received the most support from, and application by, the courts.<sup>225</sup> This theory seeks to eliminate the mere circumstance of the damage to isolate only its immediate cause, namely, the event, which in the normal state of affairs (*dans le cours habituel des choses*), is of a nature to cause the damage. It may be seen, however, as having the disadvantage of isolating only one cause even in cases where the damage flows from many factors.<sup>226</sup> In addition, some Quebec cases tend to adopt the theory of *prévision raisonnable des conséquences* ("reasonable foreseeability").<sup>227</sup> This approach finds the existence of a causal relation when the kind of damage caused could be reasonably foreseen by the author of the fault. It has been criticized as confusing the fault and the causation requirements,<sup>228</sup> and is usually imposed only in cases

<sup>220</sup> See art. 1607 C.C.Q. Compare art. 1151 C.N., extended by the doctrine from contract to cases of *responsabilité civile*.

<sup>221</sup> A. Nadeau & R. Nadeau, *Traité pratique de la responsabilité civile délictuelle* (Montreal: Wilson & Lafleur, 1971) at 607-608.

<sup>222</sup> J. Flour & J.L. Aubert, *Les obligations: 2) Le fait juridique*, 6th ed. (Paris: A. Colin, 1997) at paras. 161, 182.

<sup>223</sup> For analysis and criticism of these theories, see *La responsabilité: conditions*, *supra* note 87 at 410-16; Flour & Aubert, *ibid.* at paras. 155-62; P. Malaurie & L. Aynès, *Cours de droit civil. Les obligations*, 3d ed. (Paris: Cujas, 1992) at 50; B. Starck, H. Roland & L. Boyer, *Obligations. 1) La responsabilité délictuelle*, 5th ed. (Paris: Litec, 1996) at 444-49; *L'acte illégitime*, *supra* note 219 at 132-35; Baudouin & Deslauriers, *supra* note 219 at 344-47.

<sup>224</sup> See Nadeau & Nadeau, *supra* note 221 at 608; *La responsabilité: conditions*, *ibid.* at 406; Baudouin & Deslauriers, *ibid.* at 347.

<sup>225</sup> See Baudouin & Deslauriers, *ibid.* at 353; J. Pineau & M. Ouellette, *Théorie de la responsabilité civile*, 2d ed. (Montreal: Thémis, 1980) at 178; *L'acte illégitime*, *supra* note 219 at 123-34; *La responsabilité: conditions*, *ibid.* at 413; Flour & Aubert, *supra* note 222 at para. 150.

<sup>226</sup> But see Baudouin & Deslauriers, *ibid.*, rightly observing at 351 that, in accordance with this theory, more than one event can be identified as the cause of the harm, as long as each event is its true cause.

<sup>227</sup> *Ibid.* at 350, 353.

<sup>228</sup> *Ibid.* at 342.

of contractual liability.<sup>229</sup> Finally, the *équivalence des conditions* (“equivalence theory”), which retains as causal all the facts contributing to the damage, plays a role in the specific area of auditors’ liability.

Ultimately, however, the judges’ intellectual process is usually not based on any theoretical ground, logical explanation, or search for a scientifically exact solution, but is rather empirical and depends on their sovereign and subjective appreciation, as well as the application of their *bon sens* (common sense).<sup>230</sup> While having the advantage of being flexible<sup>231</sup> and susceptible of adaptation depending on the facts of the case and the results that the court thinks just, this subjective evaluation can have the effect of creating uncertainty.<sup>232</sup>

## ii. The Problem of the *Victime par Ricochet*

Linked to the issue of causation is the question of whether the courts should grant recovery for harm sustained by a “ricochet victim”, that is, a victim whose harm arises from someone else’s damage. The courts generally do so, with some exceptions, as long as it can be proven that there was a causal link, and that the damage suffered was distinct from damage to the immediate victim.<sup>233</sup>

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<sup>229</sup> See art. 1613 C.C.Q.; art. 1150 C.N. See *Companie Miron v. Brott* (1978), [1979] C.A. 255, 11 C.C.L.T. 114 [hereinafter *Miron*], where the court held, in a case of a claim for financial loss, that the question is whether the damage is a direct consequence of the fault, not whether the loss was foreseeable.

<sup>230</sup> Starck, Roland & Boyer, *supra* note 223 at 438, 441, 443; Flour & Aubert, *supra* note 222 at paras. 154, 165; J. Pineau, D. Burman & S. Gaudet, *Théorie des obligations*, 3d ed. (Montreal: Thémis, 1996) at 666; Demogue: “[I]l s’agit d’une question de bon sens plus que de science... qui a parfois laissé les patiences les plus éprouvées,” cited in *La responsabilité: conditions*, *supra* note 87 at 407.

<sup>231</sup> See B.S. Markesinis, “La politique jurisprudentielle et la réparation du préjudice économique en Angleterre: une approche comparative” (1983) R.I.D.C. 31 at 45-46.

<sup>232</sup> See Marshall, *supra* note 94 at 766.

<sup>233</sup> See *La responsabilité: conditions*, *supra* note 87 at 425; Pineau & Ouellette, *supra* note 225 at 24; Baudouin & Deslauriers, *supra* note 219 at 158-59; Malaurie & Aynès, *supra* note 223 at 52, 54; *Congrégation des Petits Frères de Marie v. Regent Taxi* (1928), 46 B.R. 96; Trib. gr. inst. Nanterre, 22 October 1975, Gaz. Pal.1976.1<sup>er</sup> sem. Jur.392 (Annot. A. Plancqueel). It must be noted that the principle of the relative effects of contracts (art. 1440 C.C.Q.; art. 1165 C.N.), which precludes third parties from benefiting from a contract to which they are not a party, does not prevent recovery in favour of a person suffering a loss flowing from the defective performance of a contractual obligation. The third party in fact benefits from an extra-contractual action in damages under certain conditions in Quebec, or automatically in France. See France: *La responsabilité: conditions*, *ibid.* at 256, 258; G. Viney, *Traité de droit civil. Introduction à la responsabilité*, 2d ed. (Paris: Librairie générale du droit et jurisprudence, 1995) at 286, 367, 386-403; J. Ghestin, *Traité de droit civil. Les obligations. Les effets du contrat* (Paris: Librairie générale de droit et de jurisprudence, 1992) at 549; C. Larroumet, *Droit civil*.

In this area, however, French law shares a concern of indeterminate liability with the common law.<sup>234</sup> The concept of causation is, therefore, used to eliminate damages that are considered too indirect.<sup>235</sup> Hence, the real question is not whether the plaintiff is the "immediate victim", but rather if a causal link exists.

### c. Pure Economic Loss

The same observation applies to the question of pure economic loss, which has not unduly preoccupied the judiciaries of France and Quebec. This type of harm has never been categorically excluded or treated separately.<sup>236</sup> It is compensated under the general principle of liability,<sup>237</sup> as long as it meets the conditions of directness, legitimacy, and certainty set out in the codes.<sup>238</sup> The central question is usually whether there is a causal link between the act of the defendant and the harm suffered by the plaintiff.<sup>239</sup> Through the use of this concept, recovery is restricted to cases the courts find appropriate.

*Les obligations*, vol. 3, 3d ed. (Paris: Economica, 1996) at 731-36, 742-44. In Quebec see *Bank of Montreal v. Bail Liée*, [1992] 2 S.C.R. 554 at 581, 583, 93 D.L.R. (4th) 490; *National Bank of Canada v. Houle*, [1990] 3 S.C.R. 122 at 165, 167, 181, 182, 74 D.L.R. (4th) 577 [hereinafter *Houle* cited to S.C.R.]; *Boucher v. Drouin*, [1959] B.R. 814 at 822; *Services immobiliers Royal LePage v. Deschambault*, [1993] R.D.I. 291 at 294 (Sup. Ct.); *Immeubles Léger v. Lafleur*, [1993] R.D.I. 220 at 221-22 (C.Q.); M. Tancelin, *Sources des obligations: L'acte juridique légitime* (Montréal: Wilson & Lafleur, 1993) at 195; D. Jutras, "Le tiers trompé" (1993) 72 Can. Bar Rev. 28 at 36, 39 [hereinafter "Le tiers trompé"]; J.L. Baudouin & P.-G. Jobin, *Les obligations*, 5th ed. (Cowansville, Qc.: Yvon Blais, 1998) at 383.

<sup>234</sup> See Ripert, D.1921.2.17: "Tout acte dommageable peut avoir des répercussions lointaines, et ce serait exagérer la responsabilité que de suivre indéfiniment dans le labyrinthe des actions humaines le fil ténu de causalité qui relie les actes les uns aux autres". The courts have been particularly reluctant to allow recovery for claims of creditors, employers, or partners of a deceased victim. See *La responsabilité: conditions*, *supra* note 87; *Norsk*, *supra* note 94 at 1080; *Markesinis*, *supra* note 231 at 44. Moreover, the courts are more willing to accept a third party claim when the defective performance of the contractual obligation results in physical damage to a person or property than when the damage is purely financial. See D. Jutras, "Civil Law and Pure Economic Loss: What Are We Missing?" (1986-87) 12 Can. Bus. L.J. 295 at 304 [hereinafter "Pure Economic Loss"]; "Le tiers trompé", *ibid.* at 42.

<sup>235</sup> See Baudouin & Deslauriers, *supra* note 219 at 159.

<sup>236</sup> See Linden, *supra* note 114 at 380; "Pure economic loss", *supra* note 234 at 295; *L'acte illégitime*, *supra* note 219 at 126-27. Art. 1607 C.C.Q. states only that the damage may either be "bodily, moral or material."

<sup>237</sup> See *L'acte illégitime*, *ibid.* at 108. See also *Markesinis*, *supra* note 231, who wonders at 32 if the English law is now coming closer on this issue to the liberal attitude of the C.N. because of the exceptions it has recognized in the last decades.

<sup>238</sup> See art. 1607 C.C.Q.; art. 1151 C.N.

<sup>239</sup> See *Francee*: Trib. gr. inst. Nanterre, 22 October 1975, *supra* note 233; Cass. Civ., 11 July 1963, *Gaz. Pal.* 1963.2° sem. Jur.389; Cass. civ. 2°, 19 March 1980, J.C.P. 1980.IV.216, D. 1980.IR.414; Cass. civ. 2°, 19 March 1980, D. 1980.IR.414 (Annot. Laroumet); Colmar, 20 April 1955, D. 1956.

It is mainly with the help of this requirement that the courts have limited, to a great extent, third party recovery of financial losses from auditors. McLachlin J. (as she then was) of the Supreme Court of Canada has stressed that causation and the common law notion of proximity play similar roles:

[P]roximity may be seen as paralleling the requirement in civil law that damages be direct and certain. Proximity, like the requirement of directness, poses the requirement of a close link between the negligent act and the resultant loss. Distant losses which arise from collateral relationships do not qualify for recovery.<sup>240</sup>

The next section is concerned with the use of causation as a controlling device in the area of auditors' liability towards third parties in the legal systems of France and Quebec.

### ***B. The Liability of the Commissaire aux Comptes towards Third Parties***

The distinctness of the French system rests on the fact that the *commissaire aux comptes* has an unequivocal mission of general interest and an institutional role. In addition, it is the only legal system in which the law provides explicitly for auditors' liability towards third parties, through article 234, paragraph 1 of the *Loi de 1966*:<sup>241</sup>

Les commissaires aux comptes sont responsables, tant à l'égard de la société que des tiers, des conséquences dommageables des fautes et négligences par eux commises dans l'exercice de leurs fonctions.

This provision does not replace or derogate from the general principle of liability provided for by articles 1382 and 1383 of the *Code civil*, but rather serves as a specific application of it.<sup>242</sup> Fault, harm, and causation must therefore always be proven before such a claim is accepted.<sup>243</sup> Hence, article 234 of the *Loi de 1966* appears to be de-

Jur.723 (Annot. Savatier); Quebec: *Trans-Quebec Helicopters v. Lee*, [1980] C.A. 596; *Elliott*, *supra* note 213. See also the following cable cases: *J.E. Construction*, *supra* note 213; *Joly v. Ferme Ré-mi*, [1974] C.A. 523; *Syndicat des Employés de Métier d'Hydro-Quebec, section locale 1500 v. Eastern Coated Papers*, [1986] R.J.Q. 1895, 2 Q.A.C. 209 (C.A.); *Miron*, *supra* note 229.

<sup>240</sup> *Norsk*, *supra* note 94 at 1154.

<sup>241</sup> *Supra* note 26. See generally Part 1, above.

<sup>242</sup> Com., 27 October 1992, *supra* note 86; Langé, *supra* note 86 at 3.

<sup>243</sup> Lyon, 27 January 1994, Bull. C.N.C.C. 1994.271 (Annot. P. Merle); Paris, 23 February 1978, *supra* note 87; Com., 27 October 1992, *ibid.*; R. Castell & F. Pasqualini, *Le commissaire aux comptes* (Paris: Economica, 1995) at 87; Guyon, *supra* note 6 at 274; Compagnie Nationale des Commissaires aux Comptes, *supra* note 6 at 2; annot., Rennes, 22 February 1999, *supra* note 87. On the requirement of causation, see Com., 12 November 1992, Bull. C.N.C.C. 1993.89.110 (Annot. M. Jeantin, E. du Pontavice); Com., 15 June 1993, *supra* note 70; Amiens, 20 June 1988, Bull. C.N.C.C. 71.316 (Annot. E. du Pontavice); Trib. gr. inst. Cherbourg, 6 April 1976, B.C.C. 1976.23.318.

claratory of the principles already existing in the *Code civil*. It is interesting to note, however, that the French legislator did not find it sufficient to rely on the general principle provided for in the code. By reaffirming this general principle in the area of auditors' liability towards third parties, the legislator made it clear that the third party is not an "indirect victim" whose *prima facie* right to recovery is uncertain.

The existence of this provision does not necessarily make the third party's right of action easier, since once the fault of the *commissaire aux comptes* and the loss are established, the difficult burden of proving the direct link between the two must be overcome.

### 1. Assessment of Causation

In addition to the particular difficulties related to the application of the notion of causation,<sup>244</sup> the specific context of auditors' liability towards third parties makes this problematic requirement even more difficult to meet. First, the fault of the *commissaire aux comptes* is usually one of omission rather than of positive action, and this creates evidentiary difficulties.<sup>245</sup> Second, *commissaires* do not prepare the accounts themselves and have the obligation not to participate in the management of the *société*.<sup>246</sup> Consequently, their fault is never the only cause of the damage suffered by the *société* or the third party, which usually flows primarily from the lack of care or the fraud of the administrators.<sup>247</sup> Finally, since the work of the *commissaire aux comptes* is not meant to provide any certainty, it should normally be only one of the factors involved in the appreciation of the financial situation of a business. These elements may explain why the courts have shown a reluctance to allow recovery in favour of third parties on grounds of causation even when the *commissaire aux comptes* was at fault.<sup>248</sup>

When assessing the existence of the causal link, courts generally ask whether the normal diligence of a competent *commissaire aux comptes* would have permitted the

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<sup>244</sup> See *supra* notes 223-35 and accompanying text.

<sup>245</sup> See Guyon, *supra* note 6 at 281; Morin, *supra* note 6 at 19; Langé, *supra* note 86 at 8.

<sup>246</sup> See *Loi de 1966*, *supra* note 26, s. 228.

<sup>247</sup> Another alternative is the fault of the *expert-comptable* in the establishment of the accounts.

<sup>248</sup> The commentators recognize unanimously that this requirement is difficult to meet. See *Manuel pratique*, *supra* note 71 at A.15, 208; annot., Lyon, 27 January 1994, *supra* note 243 at 275; Guyon, *supra* note 6 at 399; Com., 27 October 1992, *supra* note 86; Compagnie Nationale des Commissaires aux Comptes, *supra* note 6 at 24. See also Com., 2 July 1973, *supra* note 87; *Commissariat aux comptes*, *supra* note 38 at 82; CREDA, *supra* note 67 at 430; Monéger & Granier, *supra* note 6 at 153. The importance of carefully assessing the existence of a causal link was reiterated in Com., 17 October 1984, *supra* note 71.

plaintiff to avoid the loss.<sup>249</sup> If the loss would have occurred even in the absence of a fault, the claim will be rejected. According to Vidal, the requirement is twofold: first, granted that diligence on the part of the *commissaire aux comptes* would have allowed the real situation to be discovered, the fault must have provoked an error in the mind of the plaintiff in relation to the evaluation of the financial wealth of the company; second, this error must have brought about the prejudicial action of the plaintiff.<sup>250</sup> Moreover, in some cases, that the error has prevented the plaintiff, or the administrators, from taking an action to remedy the situation and to avoid the collapse of the business also demonstrated causation.<sup>251</sup>

It is noticeable that the courts do not require the fault of the *commissaire aux comptes* to be the only or even the main cause of the plaintiff's loss.<sup>252</sup> Such an approach would have the consequence of making almost every case inadmissible, since the cause of the loss is usually multiple and lies, at the outset, in the fault or fraud of the administrators.<sup>253</sup>

According to the rule found in section 234, paragraph 2 of the *Loi de 1966*, *commissaires aux comptes* are only liable for their personal faults, and their fault cannot be substituted for the fault of the administrators.<sup>254</sup> This principle has prompted some commentators to affirm that, when harm has been caused by the fault of both the administrators and the *commissaire aux comptes*, the latter should not be condemned *in solidum* with the former. Thus, it is argued that *commissaires* should be held liable for only the part of the loss directly linked to their fault since they are not the co-author of the faults committed by the administrators or their accomplice and do not participate in the creation of the same loss.<sup>255</sup> Refusing *in solidum* condemnation, some judges have therefore attempted to apportion the damage according to the exact part played

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<sup>249</sup> Com., 27 October 1992, *ibid.*; Aix-en-Provence, 29 May 1981, D. 1982.I.R.66; Rouen, 27 April 1982, *supra* note 71; Rennes, 22 February 1999, *supra* note 87; Bordeaux, 4 November 1997, *supra* note 87; *Manuel pratique*, *ibid.* at A.15, 208; Feuillet, *supra* note 69 at 90; Morin, *supra* note 6 at 19; Monéger & Granier, *ibid.* at 153.

<sup>250</sup> See e.g. Com., 27 October 1992, *ibid.* See also Com., 6 October 1992, *supra* note 87 at 229; Com., 9 February 1988, *supra* note 85; Paris, 20 June 1990, *aff'd*, Com., 12 November 1992, *supra* note 243.

<sup>251</sup> See Com., 9 February 1988, *ibid.*; Rouen, 27 April 1982, *supra* note 71; *Commissariat aux comptes*, *supra* note 38 at 83.

<sup>252</sup> See Com., 18 October 1994, Joly. 1994.1302 (Annot. J.F. Barbiéri).

<sup>253</sup> See Trib. gr. inst. Paris, 22 January 1997, Joly 1997.432 (Annot. J.F. Barbiéri); Langé, *supra* note 86 at 8.

<sup>254</sup> Com., 14 October 1959, J.C.P. 59.11308 (Annot. J. Nectoux); CREDA, *supra* note 67 at 428; Morin, *supra* note 6 at 20. See also annot., Com., 9 February 1988, *supra* note 85.

<sup>255</sup> See *Commissariat aux comptes*, *supra* note 38 at 79. See also Monéger & Granier, *supra* note 6 at 156; Morin, *ibid.* at 20. But see the exceptional cases provided for in *Loi de 1966*, *supra* note 26, ss. 7, 228, 234.

by the fault of the *commissaire aux comptes* in the realization of the harm.<sup>255</sup> Nevertheless, in other cases, there is a discernable tendency to apply the theory of *équivalence des conditions*, and to condemn *commissaires in solidum* with the administrators.<sup>257</sup>

Finally, the courts have sometimes linked the plaintiff's damage solely to the fault of the administrators<sup>258</sup> or to the collapse of the *société*, which was said not to be primarily caused by the *commissaire aux comptes*.<sup>259</sup> This fact, however, present in every case, does not usually in itself prevent the courts from finding a causal link; rather, such a fact demonstrates the *prima facie* indirectness of the actions of the *commissaire aux comptes* as a cause of the failure of the business and the necessity of applying strictly the requirement of causation.

## 2. Causation as a Restrictive Tool

The French courts have frequently rejected claims where the damage would have been suffered even in the absence of a fault on the part of the *commissaire aux comptes*.<sup>260</sup> Thus, third party claims have failed where the evidence showed that the irregularities would not have been discovered even if the *commissaires aux comptes* had ex-

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<sup>256</sup> See Bordeaux, 17 October 1990, Bull. C.N.C.C. 1990.499; Poitiers, 20 October 1998, Bull. C.N.C.C. 1999.125 (Annot. P. Merle); Paris, 23 February 1978, *supra* note 87, where the C.A. refused to condemn the *commissaires aux comptes in solidum* with the administrators. See also Guyon, *supra* note 6 at 400. The concept of loss of a chance is also used to allow partial recovery by linking the fault of the *commissaire aux comptes* to the loss of a chance to reduce or avoid the damages suffered, rather than the total harm. See Paris, 7 February 1997, Bull. C.N.C.C. 1997.257 (Annot. P. Merle); Paris, 26 January 1996, J.C.P. 1996.268; Aix-en-Provence, 29 May 1981, *supra* note 249; Trib. gr. inst. Nanterre, 12 May 1999, Bull. C.N.C.C. 1999.489; Trib. gr. inst. Le Havre, 15 November 1979, *supra* note 71, *aff'd*, Rouen, 27 April 1982, *supra* note 71, where the court took into account the importance of the fault of the *commissaire aux comptes* and held him liable for only 5 percent of the total damage.

<sup>257</sup> See Paris, 24 January 1986, Bull. C.N.C.C. 1986.62.187 (Annot. E. du Pontavice), *aff'd*, Com., 9 February 1988, *supra* note 85; Trib. gr. inst. Marseilles, 10 September 1986, Bull. C.N.C.C. 1986.419; Com., 17 October 1984, *supra* note 71, where the *commissaire aux comptes* and the *expert-comptable* were condemned *in solidum*. See also M.-J. Coffy de Boisdeffre, "La responsabilité du commissaire aux comptes: trois ans de décisions judiciaires" (1988) *Eco. et Compt.* 13 at 19; Guyon, *supra* note 6 at 400; CREDA, *supra* note 67 at 428.

<sup>258</sup> See generally Guyon, *ibid.* at 400; Com., 14 October 1959, *supra* note 254.

<sup>259</sup> See however Com., 17 October 1984, *supra* note 71, where the *commissaire aux comptes* had recently been appointed and consequently had not been able to carry out all the investigations necessary to control the accounts and did not certify the accounts in question.

<sup>260</sup> See Monéger & Granier, *supra* note 6 at 153; Compagnie Nationale des Commissaires aux Comptes, *supra* note 6 at 24; Guyon, *supra* note 6 at 281; Langé, *supra* note 86 at 8.

exercised their control with diligence and prudence;<sup>261</sup> when the errors did not modify substantially the results of the statements;<sup>262</sup> when the court considered that the plaintiff would have acted the same way even with knowledge of the errors,<sup>263</sup> or that the sequence of events would have been the same in the absence of the fault;<sup>264</sup> where the detrimental act of the plaintiff occurred before the fault of the *commissaire aux comptes* was committed;<sup>265</sup> and finally, where the cause of the loss laid solely in an event independent of the defendant, such as the unavoidable failure of the *société*.<sup>266</sup>

In most cases, however, the plaintiff fails because the evidence shows that he or she knew, or should have known, about the real situation.<sup>267</sup> The plaintiff's knowledge need not be linked to the actual deficiencies of the report. It is sufficient that he or she knew, or should have known, about the difficulties experienced by the *société*,<sup>268</sup> if, for example, despite the irregularities, the mere reading of the statements or of the report would have revealed them.<sup>269</sup>

A judgment rendered by the Cour de cassation on 21 November 1989 exemplifies this situation. The plaintiff had invested in a *société*. According to a provision in the agreement, a second investment occurred after the accounts of the *société* were approved on the basis of the report of the *commissaire aux comptes*. This was followed

<sup>261</sup> See Aix-en-Provence, 7 June 1985, Bull. C.N.C.C. 1985.487; Coffy de Boisdeffre, *supra* note 257 at 19; CREDA, *supra* note 67 at 431; Com., 27 October 1992, *supra* note 86.

<sup>262</sup> See e.g. Paris, 20 June 1990, *aff'd*, Com., 12 November 1992, *supra* note 243; Rennes, 24 June 1987, Bull. C.N.C.C. 1987.67.336. In this case, however, the court also judged that the plaintiff knew or should have known the exact nature of the financial situation of the *société*. See also Coffy de Boisdeffre, *ibid.* at 19.

<sup>263</sup> See Paris, 3 November 1987, *aff'd*, Com., 21 November 1989, Bull. C.N.C.C. 1990.78.240 (Annot. E. du Pontavice); CREDA, *supra* note 67 at 432; Rennes, 22 February 1999, *supra* note 87; Paris, 14 November 1997, Bull. C.N.C.C. 1998.209 (Annot. P. Merle); Paris, 8 September 1999, Joly, 1999.1162 (Annot. J.F. Barbiéri).

<sup>264</sup> See e.g. Lyon, 27 January 1994, *supra* note 243.

<sup>265</sup> See Trib. gr. inst. Paris, 14 April 1986, B.C.C. 1986.299; Com., 15 June 1993, *supra* note 70; Com., 21 November 1989, *supra* note 263; Lyon, 27 January 1994, *ibid.*; Trib. gr. inst. Montauban, 21 March 1985, B.C.C. 1985.234; Paris, 14 November 1997, *supra* note 263; Coffy de Boisdeffre, *supra* note 257 at 19.

<sup>266</sup> See e.g. Trib. gr. inst. Cherbourg, 6 April 1976, *supra* note 243; Morin, *supra* note 6 at 19.

<sup>267</sup> See Trib. gr. inst. Paris, 26 May 1981, unreported (transcripts used); Coffy de Boisdeffre, *supra* note 257 at 19; annot. (du Pontavice), Com., 12 November 1992, *supra* note 243. *Contra* Com., 9 February 1988, *supra* note 85, which exemplifies the tendency of the courts to find a causal link more readily in presence of gross fault.

<sup>268</sup> See e.g. Com., 15 June 1993, *supra* note 70; Com., 12 November 1992, *ibid.*; Rennes, 24 June 1987, *supra* note 262; Morin, *supra* note 6 at 19; Trib. com. Marseilles, 27 October 1986, Bull. C.N.C.C. 1986.66.211.

<sup>269</sup> See Com., 17 October 1984, *supra* note 71; Amiens, 20 June 1988, *supra* note 243, hearing a case referred by Com., 17 October 1984, *ibid.*; Coffy de Boisdeffre, *supra* note 257 at 19.

by other investments. Subsequently, a verification requested by the board of directors showed an important loss, which did not appear in the certified statements. On the facts, the claim was refused. The plaintiff had been present at the meeting of the board of directors where the accounts had been approved. At this meeting it had been decided that accounting investigations were necessary and that some order had to be brought into the management of the *société*. The plaintiff, therefore, had been sufficiently alerted by the apparent irregularity of the accounts, and could have decided to postpone subsequent investments until after the investigations requested by the board had been conducted.<sup>270</sup>

The expertise of the plaintiffs is an element that can convince the court that they could, or should, have discovered the irregularities themselves.<sup>271</sup> Moreover, both the plaintiffs' knowledge, or presumed knowledge, of the actual situation, and their expertise can prompt the court to find fault of their own.<sup>272</sup> The courts can also come to this conclusion if it is shown that the plaintiffs failed to exercise reasonable care in relying on the accounts<sup>273</sup> or in their decision to get involved with the controlled *société*, independent of any reliance on the accounts. The fault of the plaintiffs either leads the court to reject the claim,<sup>274</sup> or if it considers that the plaintiffs' and defendant's faults have contributed to the damage, to apportion the damages between them.<sup>275</sup>

On the basis of the plaintiffs' fault, the Tribunal de Grande Instance de Paris refused compensation on 6 April 1990 for their lost investment after the collapse of a *société*.<sup>276</sup> Since the plaintiffs were experts in risk investment, and the fragility of the financial situation of the business was apparent on the face of the statements, the court

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<sup>270</sup> See also Amiens, 20 June 1988, *ibid.*; Paris, 1 February 1984, Rev. Soc. 1984.779 (Annot. D. Schmidt).

<sup>271</sup> See Trib. gr. inst. Lorient, 22 February 1983, Bull. C.N.C.C. 1983.92, *aff'd*, Rennes, 24 June 1987, *supra* note 262; Coffy de Boisdeffre, *supra* note 257 at 19; Trib. gr. inst. Paris, 25 February 1992, cited in Kurkdjian, *supra* note 69 at 25; Trib. gr. inst. Nanterre, 12 May 1999, *supra* note 256 (the plaintiff was both an *expert-comptable* and *commissaire aux comptes*). *Contra* Trib. gr. inst. Paris, 22 January 1997, *supra* note 253.

<sup>272</sup> See Amiens, 20 June 1988, *supra* note 243; Trib. gr. inst. Lorient, 22 February 1983, *ibid.*

<sup>273</sup> See Paris, 1 February 1984, *supra* note 270; Trib. gr. inst. Paris, 6 April 1990, unreported; Trib. gr. inst. Nanterre, 12 May 1999, *supra* note 256; Guyon, *supra* note 6 at 281; annot., Com., 9 February 1988, *supra* note 85. *Contra* Com., 21 January 1997, *supra* note 87, where it was said that an investor commits no fault if he does not undertake an accounting audit before a takeover bid. See the strong criticism of Merle in annot., *ibid.*; annot., Paris, 14 November 1997, *supra* note 263. See also to the same effect Paris, 8 September 1999, *supra* note 263, in a case of emergency; Trib. gr. inst. Paris, 22 January 1997, *supra* note 253.

<sup>274</sup> See Com., 2 July 1973, *supra* note 87, for the case of the preparation of a special report; Rennes, 24 June 1987, *supra* note 262; annot., Com., 18 October 1994, *supra* note 252.

<sup>275</sup> See Paris, 1 February 1984, *supra* note 270.

<sup>276</sup> *Supra* note 273.

judged that it was for the plaintiffs to calculate the risk that they were about to take. It was significant for the court that the plaintiffs never met with the *expert-comptable* and the *commissaire aux comptes*, and that they made their decision on the sole basis of the accounting documents without obtaining further verifications.<sup>277</sup>

On 1 February 1984 the Court of Appeal of Paris<sup>278</sup> had gone even further. A *société* seeking financing to overcome its difficulties signed an agreement with the plaintiff rescuer. After the general assembly approved the certified accounts, the plaintiff invested in the company. Three months later, the plaintiff, by then the principal shareholder and officer of the company, discovered grave irregularities in the accounts of the *société*. The court held the *expert-comptable* and the *commissaire aux comptes* liable for only half the damage suffered by the plaintiff. After stating that he had the right to rely on the certified accounts, the court criticized the plaintiff's attitude as being careless and imprudent, since he did not, before getting involved, verify the values indicated on the accounts, carry out a thorough accounting verification, or seek information from the *expert-comptable* and the *commissaire aux comptes*.<sup>279</sup> Moreover, the court believed that he should have requested a more recent statement, since the financial statements were already six months old at the moment of his investment.

These judgments imply that it is generally imprudent for the plaintiff not to undertake a verification of the financial information contained in the statements.<sup>280</sup> While these decisions are striking, considering the weight given by the law to the certification of the French *commissaires aux comptes*, this type of argument is widely found in the cases and has been approved by some commentators, who emphasize that certification is not insurance.<sup>281</sup>

### 3. Similarities with the Common Law

At first sight, the French courts do not take into account the considerations that have preoccupied the English and Canadian common law courts. Thus, the French courts do not ask openly for actual reliance on the financial statements, and in some cases, the mere disclosure of the documents was held to be sufficient to find causation.<sup>282</sup> Moreover, the examination of the certified accounts does not even appear to be a necessary requirement for establishing causation. In fact, the Tribunal de Grande In-

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<sup>277</sup> See also Trib. gr. inst. Toulouse, 5 January 1987, Bull. C.N.C.C.66.224 (Annot. E. du Pontavice).

<sup>278</sup> *Supra* note 270.

<sup>279</sup> But see Com., 27 October 1992, *supra* note 86, where this "widely spread idea" [translation] was not raised despite the fact that the plaintiff was a regular contractual partner of the *société* and that the irregularity was easily identifiable. See annot., *ibid.*

<sup>280</sup> See annot., Paris, 1 February 1984, *supra* note 270.

<sup>281</sup> See annot., Com., 27 October 1992, *supra* note 86.

<sup>282</sup> See Com., 21 January 1997, *supra* note 87.

stance de Le Havre stated on 15 November 1979 that specific reliance on the statements or on the certification, as well as mere knowledge of them, was not necessary to allow the claim of the creditors of a *société*.<sup>253</sup> In this case, the liability of the *commissaire aux comptes* resulted from the fact that his faulty omission had allowed the *société* to continue its existence and to benefit from a clean reputation, thereby creating a false sense of security in the minds of the creditors.<sup>254</sup>

There are, however, other cases where the court placed some importance on the absence of knowledge or reliance on the statements.<sup>255</sup> Moreover, some judgments have incorporated considerations similar to the notion of "reasonable reliance", in the sense that they have refused to allow total, or even partial, recovery when the third party did not exercise reasonable care in relying on the certification, or in a decision to get involved with the controlled *société*.<sup>255</sup>

Knowledge of the specific plaintiff or class of plaintiffs to whom the accounts will be communicated, and of the transaction in contemplation, are never mentioned as influential considerations.<sup>257</sup> Finally, the study of the case law reveals no real concern for limiting recovery because of the fear of indeterminate liability, and more significantly, this concern is never mentioned by the doctrine.<sup>258</sup>

### C. The Quebec Auditor and Third Parties

The Quebec law of auditors' liability towards third parties is distinguished by the lack of guidance provided by the statutes, courts, and commentators. It does not benefit

<sup>253</sup> BCC.1980.44, aff'd, Rouen, 27 April 1982, *supra* note 71.

<sup>254</sup> The court held that the creditors, contrary to the shareholders, do not get involved on the basis of the statements of the *société*, but by reason of the simple existence and reputation of the *société*. *Contra* Com., 5 March 1980, Gaz. Pal. 1981.4 (Annot. APS), Bull. C.N.C.C. 1980.40.435 (Annot. E. du Pontavice) in a case of liability of a *commissaire aux apports*.

<sup>255</sup> See Trib. gr. inst. Bordeaux, 31 December 1974, Bull. C.N.C.C. 1975.180, aff'd, Bordeaux, 9 February 1976, Bull. C.N.C.C. 1976.169; Trib. gr. inst. Montauban, 21 March 1985, *supra* note 265; Trib. gr. inst. Rouen, 9 March 1998, Bull. C.N.C.C. 1998.401 (Annot. P. Merle); Paris, 14 November 1997, *supra* note 263; Com., 21 January 1997, *supra* note 87; Paris, 8 September 1999, *supra* note 263.

<sup>256</sup> See *supra* notes 271-81 and accompanying text.

<sup>257</sup> Except perhaps in Trib. gr. inst. Rouen, 9 March 1998, *supra* note 285, where it is held that the reports were meant to inform existing shareholders of the suppression of one of their rights (*droit préférentiel de souscription*). It was held that most of the plaintiffs were not part of this group. In this case, however, the court found no fault on the part of the *commissaire aux comptes* and no causal link, which may show that the above element was not of tremendous importance. It seems instead to have been taken into account in the context of the evaluation of the fault.

<sup>258</sup> This does not necessarily mean that this is not a preoccupation in French law. See Markesinis, *supra* note 231 at 44. See also *supra* note 234 and accompanying text.

from any provision similar to section 234 of the *Loi de 1966*,<sup>289</sup> and the few cases that have examined this issue have created confusion as to the applicable legal principles.

Given the absence of any specific rule governing this area of the law, reliance must be placed on the general principle of *responsabilité civile* provided in article 1457 of the C.C.Q. As in France, the requirements of fault, harm, and more particularly, causation, serve as controlling devices restricting the scope of this principle. In addition to the particular difficulties inherent in the application of the causation requirement,<sup>290</sup> Quebec law has to deal with a further problematic factor, the overwhelming influence of the common law.

### 1. The Existence of the Causal Link

In Quebec, as in France, the application of the causation requirement as a restrictive tool has resulted in few successful claims against auditors by third parties. One such case is *Irwin (C.A.)*,<sup>291</sup> in which the plaintiffs became involved with the audited company as shareholders, officers, and guarantors. After the company became insolvent, it was discovered that other shareholders had illegally appropriated large sums of money. The plaintiffs pleaded that the auditors were at fault for not discovering the irregularities, and that had the irregularities been disclosed, the plaintiffs would have closed the business and not suffered any loss. In response, the defendants contended that there was no direct damage, and that if there were any, it was caused to the company and not to the shareholders.

Michaud J. rejected this argument and found a direct causal link between the defendants' fault and the plaintiffs' loss, since the latter were lulled into a false sense of security by the erroneous financial statements.<sup>292</sup> As is the case in France, the error created in the plaintiffs' minds as to the nature of the risk involved, as well as the fact that this error prompted the plaintiffs to act to their detriment, were both fundamental to the existence of a causal link.

Finally, the courts' position with respect to the test of causation is not clear. One case found it sufficient that the audited statements be only one of the factors which

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<sup>289</sup> The only similar provision is *QCE*, *supra* note 15, s. 3.02.12. This statute provides for professional rules that do not bind the civil courts, although they are usually strongly influenced by them. See *Charlesbourg*, *supra* note 53 at 536.

<sup>290</sup> See *supra* notes 223-35 and accompanying text.

<sup>291</sup> *Supra* note 53.

<sup>292</sup> *Irwin* (Sup. Ct.), *supra* note 53 at 195. This reasoning is mentioned by Carrière J. in a judgment rejecting a motion for dismissal. It is applied, however, to the claim made by the auditor's client. See *Richter & Associates v. Wightman*, [1998] R.R.A. 538 at 542 (Sup. Ct.).

prompted the plaintiff's decision.<sup>293</sup> In another case, however, it was required that the statements be the principal factor.<sup>294</sup>

## 2. Causation as a Restrictive Tool

In most cases, courts have refused recovery on grounds of absence of causation. This was so where the loss would have occurred even in the absence of fault,<sup>295</sup> or where the decision to become involved in the company materialized before the auditors performed their duties.<sup>296</sup> In addition, the fact that the plaintiff invested in the company with the knowledge of the actual situation also showed that the auditors' fault did not have any impact on the plaintiff's decision-making process.<sup>297</sup> The expertise of the plaintiff is a factor taken into account to demonstrate actual or deemed knowledge.<sup>298</sup> Finally, both the plaintiff's knowledge and expertise can amount to evidence of the plaintiff's fault, thereby exonerating the defendant or leading to an apportionment of liability.<sup>299</sup>

In *Chevrier v. Guimond* the court refused the claim of purchasers of shares in a company which subsequently became insolvent. The plaintiffs argued that the audited financial statements, which had been prepared by the auditors with the knowledge that they were being relied on by the purchasers of the shares, were erroneous and misleading, since they did not mention the existence of two chattel mortgages. The trial judge believed that the auditors' fault did not cause the loss, since the plaintiffs knew of the existence of the mortgages from the start. Consequently, they were responsible for the events that resulted from their own carelessness. On appeal Tyndale J. added that, in any event, the error did not modify substantially the situation exposed in the statements, since they mentioned two non-existent mortgages, the value of which exceeded that of the undisclosed mortgages. Moreover, even if the plaintiffs were not

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<sup>293</sup> *Garnet Retailack & Sons v. Hall & Henshaw*, [1985] C.S. 409 at 413-14 [hereinafter *Garnet* (Sup. Ct.)], rev'd, [1990] R.R.A. 303 at 306-307 (C.A.) [hereinafter *Garnet* (C.A.)].

<sup>294</sup> *Irwin* (C.A.), *supra* note 53 at 306. See also *Caisse populaire des fonctionnaires v. Plante*, [1990] R.R.A. 250 (C.A.), a case of valuers' liability. The valuer's report was held to be only an opinion, however, and it specifically stated that it should not be used without consent by persons other than the client.

<sup>295</sup> See *Irwin* (Sup. Ct.), *supra* note 53 at 195. But see *Verrier v. Malka*, [1998] R.R.A. 715 (C.A.), in which the claim was allowed and the argument to the effect that the plaintiff investor would have invested in the company even if its true position had been disclosed was rejected (*ibid.* at 719).

<sup>296</sup> See *Sarraaf v. Awad*, J.E. 95-1881 (Sup. Ct.); *Fenêtres St-Jean v. Banque Nationale du Canada*, [1990] R.J.Q. 632, 69 D.L.R. (4th) 384 (C.A.) [hereinafter *Fenêtres St-Jean* cited to R.J.Q.]; *Irwin* (Sup. Ct.), *ibid.* at 195.

<sup>297</sup> See also *Irwin* (C.A.), *supra* note 53 at 306.

<sup>298</sup> See *Charlesbourg*, *supra* note 53 at 538.

<sup>299</sup> See arts. 1470, 1478 C.C.Q.

actually aware of the existence of the mortgages, they could have discovered them by checking the registry had they exercised due care.<sup>300</sup>

### 3. The Influence of the Common Law

Over the years, in the absence of clear guidelines, it has been tempting for the parties to litigation involving auditors' liability to plead the landmark common law cases of Canada and England.<sup>301</sup> While the Quebec cases on this issue make no reference to the French law, except insofar as the general principles of liability are concerned, some have not hesitated, in view of the lack of precedent, to incorporate common law principles.<sup>302</sup> Today, the direct importation of the common law would be more difficult in light of the scepticism shown recently by the Quebec Court of Appeal.<sup>303</sup> This court has nevertheless been persuaded, at least in some cases, to examine the common law approach to this problem and to take inspiration from it.

The most rigid attitude was expressed by Baudouin J. in *Charlesbourg*.<sup>304</sup> In this case, the parties had pleaded English and Canadian decisions such as *Hedley Byrne* and *Haig*. Baudouin J. stated that these cases, despite their comparative interest, were not useful, because the relevant principles of law are only those of *responsabilité civile*.<sup>305</sup> Nonetheless, in *Fenêtres St-Jean*,<sup>306</sup> Baudouin J. recognized the unarguable moral authority of the common law principles developed by the Supreme Court of Canada in *V.K. Mason*,<sup>307</sup> a case involving negligent misrepresentations by a bank. Yet this admission was based on the fact that *V.K. Mason* drew upon rules similar, though not identical, to those applying in Quebec. Baudouin J. refused, however, to substitute

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<sup>300</sup> [1990] R.R.A. 603 (C.A.), aff'g (6 June 1985), Montreal 500-05-012838-817 (Sup. Ct.), leave to appeal to S.C.C. refused (1991), 39 Q.A.C. 80 (note), 129 N.R. 237 (note) (S.C.C.) [hereinafter *Chevrier*]. See also *Garnet* (Sup. Ct), *supra* note 293, where the principal cause of the damage was not the financial statements, but the plaintiff's actions in the knowledge of the situation. But in *Garnet* (C.A.), *supra* note 293, the Court of Appeal agreed to order the plaintiff indemnified for the difference between the real value of the assets and the value indicated on the statements, since the latter had been one of the factors relied on by the plaintiffs in assessing the value of the company.

<sup>301</sup> The influence of the common law in this field has been so great that some commentators have even maintained that the common law jurisprudence has been accepted in the Quebec civil law. See e.g. Maughan & Paskell-Mede, *supra* note 145 at 57.

<sup>302</sup> See *Guardian*, *supra* note 6. The court's position may be explained, however, by the fact that the audit had been conducted under the federal *CBCA*, *supra* note 19, and that the Court was concerned with the standard of care to be applied in evaluating the contractual fault of the auditor.

<sup>303</sup> M. Paskell-Mede, "Made in Quebec" (1990) 8:123 C.A. Mag. 48 at 48.

<sup>304</sup> *Supra* note 53.

<sup>305</sup> *Haig*, *supra* note 2 at 535.

<sup>306</sup> *Supra* note 296.

<sup>307</sup> *Supra* note 149.

the common law conceptual framework used to establish negligence in misrepresentation cases for the traditional civilian analysis.<sup>303</sup>

One of the most important attempts to incorporate a common law type of reasoning is found in *Garnet* (Sup. Ct.).<sup>309</sup> In this case, the plaintiff had requested that the defendants prepare audited financial statements for the express purpose of merger discussions. The statements showed some problems, but did not mention their extent. The plaintiff later discovered serious errors, but proceeded nevertheless with the merger, believing he could turn things around. Martin J. stated that the common law decisions establish a series of "yard-sticks" by which the accountant's error is to be measured. He applied the principle of "substantial reliance" and stressed that, in the context of the civil law, "substantial reliance relates ... strictly to causality and, depending on the circumstances, upon mitigation of damages."<sup>310</sup> In his opinion, the plaintiff had to demonstrate that he relied substantially upon the flawed statements, and that this reliance was reasonable in the circumstances.<sup>311</sup> On appeal Jacques J. stressed that the main issue in this case was one of causation, and that the criterion of "substantial reliance" was not part of the law of the Province of Quebec, unless it referred merely to the need to prove a causal link between the fault and the loss.<sup>312</sup> Moreover, he expressed the same reservation about reasonableness of reliance unless it is used to show the absence of a causal link. Nonetheless, he accepted the conclusion of the Superior Court that the causal link was absent because the plaintiff did not take the "elementary precautions required of the reasonably informed business man in parallel circumstances" and that his reliance on the statements was, therefore, not reasonable.<sup>313</sup>

The notion of reasonable reliance is not the only common law concept which was used by the courts of Quebec. On the basis of *Haig*, foreseeability and knowledge of the object and purpose of the statement were taken into account in *Placements Miracle v. Larose*,<sup>314</sup> a case involving a surveyor's certificate,<sup>315</sup> and in *Malo*,<sup>315</sup> involving a

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<sup>303</sup> *Fenêtres St-Jean*, *supra* note 296 at 635.

<sup>309</sup> *Supra* note 293.

<sup>310</sup> *Ibid.* at 413.

<sup>311</sup> *Ibid.* at 413-14.

<sup>312</sup> *Garnet* (C.A.), *supra* note 293 at 305.

<sup>313</sup> *Ibid.* at 306.

<sup>314</sup> [1980] C.A. 287.

<sup>315</sup> *Ibid.* at 289. The court took into account that the certificate is not an official or authentic document. See also *158661 Canada v. Manolagos*, [1993] R.J.Q. 1543 at 1555 (Sup. Ct.); Maughan & Paskell-Mede, *supra* note 145 at 61.

<sup>316</sup> *Supra* note 53. In this case, however, the court took into account these factors in the assessment of the defendant's "duty of advice". See also *Dupuis v. Pan American Mines*, [1979] C.S. 421; *Valver Real Estates v. Young*, [1977] C.A. 237 at 239, concerning a representation made in a valuation re-

review engagement<sup>317</sup> prepared for the purpose of a share purchase transaction.<sup>318</sup> Conversely, in *Charlesbourg*,<sup>319</sup> Baudouin J. held that the fact that the statements are prepared for a specific purpose does not prevent a finding of liability despite their use by the client for another purpose. In Baudouin J.'s opinion, auditors must accept the consequences of their representations irrespective of the initial destination of the document because of the public trust in the quality of the professional's acts.<sup>320</sup> This tends to attribute to the Quebec auditor a public interest role similar to that of the French *commissaire aux comptes*. An assimilation of these two professionals is not, however, justified, because of their different status. Nevertheless, Baudouin's statement is more in harmony with the general principles of liability, which in the assessment of the causal link do not usually consider as relevant the plaintiffs' knowledge or foresight of the consequences of their actions.

#### D. Conclusion

This analysis shows that the civil law systems of France and of the Province of Quebec have used the flexible concept of causation to limit recovery, while the common law has done so through the concept of duty of care. Yet one qualification to this affirmation must be made with respect to Quebec, where attempts to use common law notions are noticeable in some cases. This leads to the discussion of the hybrid situation in the Province of Quebec.

### IV. Quebec: At the Border of Civil Law and Common Law

Despite the general reluctance of Quebec courts to use common law principles in private law matters, they have drawn upon common law precedents frequently in the area of auditors' liability towards third parties. Meanwhile, surprisingly, the French law on this subject takes no part in the reasoning of the Quebec courts. While this is probably due to the fact that the French law was not pleaded, it can also be explained by the differences existing between the professional role and status of French and

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port. The court used these concepts in assessing the question of whether the plaintiff was "another" within the meaning of art. 1053 C.C.L.C. (ancestor of art. 1457 C.C.Q.).

<sup>317</sup> A review engagement provides a level of assurance lower than that of the audit engagement.

<sup>318</sup> See also *Houle*, *supra* note 233 at 185, a case of abuse of rights. The close relationship existing between a company's bank and the company's shareholders, as well as the knowledge of the transaction in which the latter were involved, prompted the Supreme Court of Canada to conclude that the bank had a legal obligation not to prejudice the plaintiff in the conduct of this transaction, and that the damage caused was foreseeable by the defendant.

<sup>319</sup> *Charlesbourg*, *supra* note 53. See also *Chevrier*, *supra* note 300, where the court refused to grant recovery because of the absence of causation, despite the fact that the auditors were aware of the specific purpose of the statements.

<sup>320</sup> *Charlesbourg*, *ibid.* at 536.

Quebec auditors. These differences render problematic attempts to transpose French solutions into Quebec law. Moreover, the similarity of the status and role of the Quebec, common law Canadian, and English auditors probably encourage courts to look more willingly at the common law treatment of this question.

These observations pose an important question: can, and if so, should, Quebec courts draw inspiration from the common law when dealing with this issue? This question cannot be answered categorically, because it involves two conflicting ideas. First is the conviction that Quebec law should adopt a protectionist attitude towards its civil law tradition, as well as the opinion that the civil law system is complete and does not need to import principles from foreign jurisdictions. Second, and opposed to this point of view, is the belief that use of comparative law should be welcomed, at least as a source of inspiration, in areas where the domestic law is underdeveloped or in need of guidance.

To reconcile these two opposing positions, one can argue that some notions, which are useful and relevant in the context of the civil law analysis, and are in harmony with its conceptual framework, can be taken into account, even though they are also elements of the common law analysis. While it must be recognized that the Quebec system of *responsabilité civile* is complete, and that courts are justified in protecting its integrity, the Quebec courts should not adopt an overly purist attitude, closing their eyes to helpful elements which respect the particular civilian methods.

As for the principles developed by French law, no such debate arises, and they can be studied without having to face any reluctance on the part of courts. In the present context, and despite the basic differences outlined above, these principles are valuable, since they provide examples of how the requirement of causation has been applied in this area. In addition, French cases show how restrictive French courts have been with this question, and how ultimately they arrive at a solution similar to that of the common law courts with regard to the scope of auditors' liability towards third parties.

### **A. The Restrictive Approach**

One of the most striking features of this comparative study is that the French and Quebec courts, without expressing the need to develop conceptual devices specifically meant to circumscribe third party recovery from auditors, have nevertheless adopted a strict attitude towards it. Both the civil and common law systems have shown a desire to restrict the boundaries of liability in this context, but have achieved this goal through a different theoretical framework.

On the one hand, the common law courts have been overwhelmingly preoccupied with the risk of opening the floodgates of litigation if a general right to recover pure economic loss were granted. They have dealt with this issue through a "restricted extension" of the concept of duty of care. Accordingly, they have accepted that a duty to avoid causing pure economic loss could be owed to third parties in circumstances limited by the use of concepts such as proximity, foreseeability, and the application of policy considerations.

The civil law jurisdictions, on the other hand, never had to deal with problems such as the traditional reluctance of the judiciary to compensate for negligently inflicted pure economic loss and the strict approach to the extension of the duty of care in this area. Indeed, the law of France and of Quebec has proceeded on the basis of a broad principle of liability, limited through the requirements of fault, harm, and principally, causation.

The application of this last concept has brought about practical results similar to those arising from the application of the common law duty of care analysis. It is astonishing that, even in France, where the *commissaires aux comptes* act in the public interest, and where their liability towards third parties has been specifically provided for by statute, the requirement of causation has been applied strictly by the courts, and compensation is rarely granted.

Yet because the notion of causation is flexible and can be assessed subjectively, the actual outcome of a specific case is more difficult to predict in the civil law system. This assertion can be contradicted by saying that “proximity”, which serves a similar controlling function in the common law, is no more explicit than the notion of causation. Nevertheless, on the whole, concepts such as reasonable reliance, knowledge of the transaction in contemplation, and knowledge of the specific plaintiff or class of plaintiffs, despite the ambiguity of this last notion, yield more precise guidelines.

### ***B. The Use of Common Law Concepts***

This discussion leads to the question whether some of the conceptual tools developed by the common law should take a place in the reasoning of the Quebec courts.

#### **1. Reasonable Reliance**

The application of the concept of reasonable reliance in the common law can, and should, inspire the Quebec courts, since it is directly relevant to the issue of causation, and has even been accepted as such by the Court of Appeal. When present, reasonable reliance is a strong indication of the existence of a causal link; when lacking, it gives evidence of missing causation, since it shows that the financial documents were not, and could not have been, a factor in the decision that led to the loss. In fact, without actual reliance on the audited financial statements, one cannot say that the statements played a causal role in the plaintiff's detrimental decision.

Moreover, some elements taken into account by the common law courts in order to find reasonable reliance are already at the root of the causal analysis of the French and Quebec courts, even though they do not necessarily frame them in terms of “reasonable reliance”. Factors such as the plaintiffs' knowledge, deemed or actual, of the financial situation of the company, their expertise, the fact that they would have acted in the same way even with knowledge of the errors, or that they had taken the detrimental decision before reviewing the financial statements are used, in both systems, to assess the existence of reasonable reliance or causation.

This argument can be contradicted by accepting, as was done in some of the French decisions, that actual reliance on the financial statements is not necessary. This

argument holds that reliance on the apparent soundness of the financial situation of the company, or on its mere existence, is sufficient. It is possible to see the merits of this argument in the French system where the *commissaire aux comptes* assumes an institutional role towards the public. It is more difficult, though, to accept this argument in Quebec, where the auditor's status is similar to that of the English and common law Canadian counterparts. One can wonder, therefore, why the Quebec auditor should be treated more severely, unless such treatment is justified by some element flowing from the particular nature of the Quebec system of *responsabilité civile*. But this is not the case. Accepting causation as proven when the reliance has not been placed specifically on the company's financial statements, but rather on the company's positive image, is problematic. Depending on the facts of each case, the existence of such an image can flow from several factors independent from the fault of the auditor. Moreover, it is difficult enough to argue that a negligent misstatement played a causal role in cases where the third party actually relied on the financial statements. It should be even more complex a fortiori where the reliance has been placed on the overall image projected by the company or on its mere existence. Consequently, such reliance cannot adequately, by itself, prove causation.

The reasonableness of the reliance should also be taken into account in the analysis of the Quebec courts. It is, in fact, material to the assessment of the causal link, as it may demonstrate the existence of the plaintiff's fault, and depending on the gravity of the latter, may lead to an apportionment of responsibility or a total exoneration of the defendant. The courts should apply this factor rigorously in light of the fact that the auditor's work is not meant to provide any certainty, so it is *prima facie* unreasonable to rely unconditionally on it.

## 2. Foreseeability of Reliance and Knowledge of the Plaintiff and the Purpose of the Financial Statements

The study of the case law on auditors' liability towards third parties shows that, in France as in Quebec, these notions are rarely part of the courts' reasoning. In fact, in most cases, the defendant knew about the plaintiff's reliance and the purpose for which the financial statements were used, so this issue was not discussed.

The fact that the French cases show no use of these concepts is not necessarily significant, and can again be explained by the unequivocal role of general interest of the *commissaire aux comptes*. Hence, it could be contended that the French *commissaire aux comptes* should, in every case, expect a third party to rely for any purpose on the certification. A similar type of analysis cannot, however, apply in Quebec, given the auditor's different status in this province.

Unless the *prévision raisonnable des conséquences* test of causation is explicitly adopted, these factors are difficult to include within the particular framework of the Quebec law of *responsabilité civile*. The general endorsement of this test, however, is doubtful. In fact, it is used, in principle, only to assess the extent of the loss in claims for contractual damages. Moreover, it tends to confuse the requirements of fault and causation. The notions of foresight of reliance/harm and of knowledge of the plaintiff and of the contemplated transaction appear to be more significant at the level of the

determination of the fault than at the level of the evaluation of the adequacy of the causal link. Hence, to be used in harmony with the civil law framework, they should only be accepted as subjective factors in the assessment of what a reasonable auditor would have done in similar circumstances.

### 3. Policy Considerations

Finally, the French and Quebec systems have not demonstrated any overt concern for policy decision making. The differences in the respective frameworks of the civil and common law systems can partly explain this situation.

In the common law, the justification for limiting liability in the area of pure economic loss caused by misstatements is policy-based and lies in the desire to prevent indeterminate liability. In contrast, the French and Quebec systems of *responsabilité civile* are governed by a general principle of liability that imposes limits through the requirements of fault, harm, and causation. Their justification for limiting liability is, therefore, conceptual, and has not rendered necessary any policy-oriented discussion.

This does not mean, however, that the judiciaries of Quebec and France have not been preoccupied with policy concerns when assessing the liability of auditors towards third parties. Policy considerations may explain, first, the courts' rigid application of the causation requirement, and second, their reluctance to allow recovery, even in the presence of fault on the part of the auditor. These concerns do not need to be expressed openly, since the notion of causation can serve limitative purposes without the use of this rationale. The flexibility of this requirement, and the fact that it is applied by the courts to arrive at the result they think just, allows the judges to take policy decisions under the cover of their formal analysis.

#### **C. Causation as a Sufficient Limiting Device**

More generally, one can argue that the civil law does not, ultimately, need to rely on the common law framework to restrict recovery in this area. As the French experience demonstrates, causation is a flexible enough concept to serve as a restrictive device, and in practice it has led to a marked limitation of the acceptance of such claims. This situation has arisen from the fact that causation is difficult to prove, especially in the presence of a multiplicity of faults. Moreover, the particular difficulties that the field of auditors' liability entails have rendered its demonstration more complex. Finally, the ease with which the civil law courts find an absence of causation in this area has allowed them, where a fault on the part of the auditor was found, to refuse compensation in cases where it was thought just to do so.

To reduce the subjective element involved in the courts' evaluation of the causal link, while ensuring the adoption of a restrictive approach, the concept of reasonable reliance should play a role in the assessment of causality. In accordance with the "adequate causation" theory, taking this element into account can permit the courts sufficiently to isolate the cases where the fault of the auditor has played a real role in the detrimental decision of the plaintiff, and thus in the realization of the loss.

## Conclusion

La Forest J. once said that the legal system of every society faces essentially the same problems and solves them by quite different means, though often with similar results.<sup>321</sup> This observation describes remarkably well the conclusion flowing from the present study. In the area of auditors' liability towards third parties, the courts of the common law and civil law jurisdictions have been faced with the same struggle: the need to balance two fundamentally important, but conflicting, interests, the public's interest in relying on sound and fair financial reporting and the interest of the auditing profession not to be burdened with potentially overwhelming liability. Despite the fact that this balancing exercise has been carried out in the context of very different legal systems, the application of the legal principles developed in each jurisdiction studied has led to the same results: recovery against a negligent or faulty auditor in favour of a third party is allowed only in limited circumstances.

In this picture, the civil law of the Province of Quebec, at the crossroads of the civil and common law systems, stands aside. The boundaries Quebec has set to protect its system of *responsabilité civile* from the constant courtship of the Canadian and English common law have become blurred in the area of auditors' liability towards third parties. This has prompted a move towards a reaffirmation of the self-sufficiency of the Quebec civil law system. Nevertheless, Quebec law can and should draw from both the French civil law and the English and Canadian common law in this area. From the former it can adopt the restrictive approach to the application of the causation requirement; from the latter, it can borrow clear limiting devices, such as the concept of reasonable reliance, which could reduce the amount of subjectivity and ambiguity in the assessment of causation by the courts. By taking inspiration from the examples provided by these two different systems, the Quebec law can achieve, with its own tools and within its specific legal system, an adequate balance of these two conflicting interests.

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<sup>321</sup> *Norsk*, *supra* note 94 at 1079.