

USE OF BANNERMAN PARAGRAPHS (LECTURE A636 – 8.20 MINUTES)

(reproduced from an article published on AccountingWEB by Steve Collings)

The use of disclaimers which limit the duty of care to third parties by auditors in their auditor's report has increased significantly over the years. The use of 'Bannerman' paragraphs are common in both auditors' reports and other reports issued by accountancy firms which aim to limit the professional firm's duty of care to third parties.

The use of disclaimers in an auditor's report was highlighted more recently in the case of *Barclays Bank plc v Grant Thornton*. Grant Thornton prepared non-statutory audit reports on Von Essen Hotels Limited Group (VEH) and expressed unqualified opinions for both 2006 and 2007. Barclays Bank alleged that the financial statements had been manipulated to show that VEH was capable of meeting bank covenants on its loan facility when, in fact, it could not. As a result, Barclays Bank suffered losses of some £45million when VEH went into administration in April 2011. The bank also stated that it relied on the unqualified opinions when making the loans to VEH.

Barclays claimed that Grant Thornton owed a duty of care to them and that this duty of care was breached because the auditors failed to uncover the alleged fraud. Barclays also said that Grant Thornton would have been aware that they would be placing reliance on the auditor's report. Grant Thornton's auditor's report contained the Bannerman wording which set out that they did not accept or assume responsibility in respect of the reports to anyone other than the company and its directors.

The judge accepted Grant Thornton's argument and struck out the claim. The judge stated that Barclays should have been aware of the Bannerman paragraph in the report – particularly as it was included in the first two paragraphs of the report and, therefore, if Barclays Bank had not read it, then they should have. The judge concluded that the Bannerman paragraph was reasonable having regard to the 1977 Unfair Contract Terms Act.

1.1 Placement of the Bannerman paragraph in the auditor's report

The use of Bannerman continues to feature in auditors' reports – although care needs to be taken if you are regulated by ACCA (see later). As auditors will be aware, the structure of the auditor's report has now changed in ISA (UK) 700 (Revised June 2016) *Forming an Opinion and Reporting on Financial Statements* which apply to audits of financial statements for periods commencing on or after 17 June 2016.

The changes brought about by ISA (UK) 700 are in the form of the structure of the auditor's report itself – for example the 'Opinion' paragraph is the first paragraph of the report and there are additional requirements in respect of going concern and other information.

In May 2018, the ICAEW updated their guidance in the form of Technical Release 01/03AAF (Revised) *The Audit Report and Auditors' Duty of Care to Third Parties*. Appendix 1 to the Technical Release positions the Bannerman paragraph at the end of the report, above the signature section of the auditor's report and is worded as follows:

'Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.'

1.2 Firms regulated by ACCA

Firms regulated by ACCA are required to have an understanding of [Technical Factsheet 84](#) *The use of Disclaimers in Audit Reports*. In particular, paragraph 19 of Technical Factsheet 84 which discourages the use of disclaimers in the auditor's report. ACCA's view is that standard disclaimers are not seen as an appropriate or proportionate response to Bannerman and could devalue the auditor's report. Indeed, ACCA state that where the audit is carried in accordance with the ISAs (UK), there would be no need to include a standard disclaimer in the auditor's report.

ACCA's view is that audit firms that conduct their work in accordance with the ISAs (UK), they reduce the risk of a negligence claim being brought against them. Hence, ACCA's view is that they do not encourage the use of disclaimers such as the Bannerman paragraph. Therefore, they should only be included in justifiable situations and should not be used on a regular basis.

1.3 Conclusion

The use of disclaimers is common, both in audit and non-audit reports generated by professional firms. ICAEW do encourage their use so as to manage the risk of liability to third parties, but this view is not shared by ACCA who continue to suggest that work done in accordance with the required standards would not need a blanket disclaimer.