

# COMPANIES ACT 2006

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## EXPLANATORY NOTES

### COMMENTARY

#### Part 16: Audit

##### *Chapter 2: Appointment of Auditors*

737. This Chapter broadly restates the existing law in sections 384 to 388A of the 1985 Act on the way in which shareholders appoint a company's auditors, with some minor changes (as explained below). The provisions are reorganised to deal with private and public companies separately. The Chapter also restates the rules in sections 390A and 390B of the 1985 Act on auditors' remuneration and the disclosure required of services provided by auditors and introduces a new power for the Secretary of State to require disclosure of the terms of audit appointments.

#### Private companies

738. [Sections 485 to 488](#) restate the law on appointment of auditors of private companies, providing that auditors are generally to be appointed by shareholders by ordinary resolution. For any financial year other than the first, this will generally be done within 28 days of the circulation to a company's shareholders of the accounts for the previous year.

739. There are two changes: firstly, an auditor's term of office will typically run from the end of the 28 day period following circulation of the accounts until the end of the corresponding period the following year. This will apply even if the auditor is appointed at a meeting where the company's accounts are laid. The second change is that an auditor is now deemed to be re-appointed unless the company decides otherwise.

##### *Section 485: Appointment of auditors of private company: general*

740. This section provides for a private company's obligation to appoint an auditor, unless it is taking advantage of an exemption from audit. The appointment is to be made by the shareholders by ordinary resolution, except that the directors can appoint the company's first auditor (or the first after a period of audit exemption), and can fill a casual vacancy.

##### *Section 486: Appointment of auditors of private company: default power of Secretary of State*

741. This section requires a company to inform the Secretary of State if it has failed to appoint an auditor within 28 days of circulation of its accounts. The Secretary of State has power to appoint an auditor in those circumstances.

##### *Section 487: Term of office of auditors of private company*

742. This section provides that the end of the term of office of the auditor of a private company is to be the end of the next period for appointing auditors. At the end of his term an auditor will automatically be deemed to be re-appointed except in five cases:

- if he was appointed by the directors;
- if the company's articles require actual re-appointment;
- if enough members have given notice to the company under section 488;
- if there has been a resolution that the auditor should not be reappointed; or
- if the directors decide that they do not need auditors for the following year.

743. When there is a change of auditor the term of office of the incoming auditor does not begin before the end of the previous auditor's term. This means that a new auditor's term will typically begin immediately after the end of the 28-day period for appointing auditors.

#### ***Section 488: Prevention by members of deemed re-appointment of auditor***

744. This section enables members with at least 5% of the voting rights in a private company to prevent an auditor being automatically re-appointed by giving notice to the company. The company's articles can enable members to do this with less than 5% of the voting rights, but cannot increase the required percentage.

745. *Subsection (3)* provides that the deadline for a notice preventing the deemed reappointment of an auditor is the end of the financial year for the accounts he is auditing.

#### **Public companies**

746. *Sections 489 to 491* restate the law on appointment of auditors of public companies, providing that auditors are generally to be appointed by shareholders by ordinary resolution in the general meeting before which the company's accounts are laid.

#### ***Section 489: Appointment of auditors of public company: general***

747. This section restates a public company's obligation to appoint auditors, unless it is taking advantage of exemption from audit. This is to be done by the shareholders by ordinary resolution, normally at the general meeting at which the accounts are laid. The directors can appoint the company's first auditors (or the first after a period of audit exemption), and can fill a casual vacancy.

#### ***Section 490: Appointment of auditors of public company: default power of Secretary of State***

748. This section restates the obligation of a company to inform the Secretary of State if it has failed to appoint an auditor at the general meeting that considers the previous year's accounts. The Secretary of State has power to appoint an auditor in those circumstances.

#### ***Section 491: Term of office of auditors of public company***

749. This section restates the rule that an auditor of a public company holds office until the end of the meeting at which the accounts are laid, unless re-appointed. Where there is a change of auditor, the term of office of the incoming auditor does not begin before the end of the previous auditor's term. This means that a new auditor's term will typically begin immediately after the end of the accounts meeting.

#### **General provisions**

750. These sections apply to both private and public companies.

***Section 492: Fixing of auditor's remuneration***

751. This section restates the rule that it is the members of a company, by ordinary resolution, who determine the auditor's remuneration, or decide the method by which it should be determined. If the auditor was appointed by someone other than the members, then it will be the directors or the Secretary of State as appropriate who will determine his remuneration.

***Section 493: Disclosure of terms of audit appointment***

752. This section creates a new power for the Secretary of State to require companies to disclose information about the terms on which they engage their auditors. *Subsection (2)* provides some examples of the detailed requirements that the Secretary of State could specify in regulations. *Subsection (3)* provides that regulations can require disclosure of changes in terms as well as the terms at the time of appointment. *Subsection (4)* specifies that the regulations are to be made by affirmative resolution procedure.

***Section 494: Disclosure of services provided by auditor or associates and related remuneration***

753. This section restates the existing power of the Secretary of State, in section 390B of the 1985 Act, to require disclosure of details of all the services supplied to a company by its auditor, and the remuneration involved. *Subsections (2) to (4)* give the detailed requirements that the Secretary of State can specify in regulations: subsection (2) relates to the level of disaggregation of different services and remunerations, and between the auditor and his associates; subsection (3) makes provision for some of the definitional issues that can be covered in regulations; and subsection (4) provides for where the information should be disclosed.
754. Under subsection (4), the regulations might require disclosure in a document compiled by the company rather than the auditor. *Subsection (5)* provides that, if so, the regulations can require the auditor to supply the directors with the information to be disclosed e.g. about the auditor's associates. *Subsection (6)* specifies that the regulations are to be made by negative resolution procedure.