



Financial Reporting Council

Annual Enforcement Review 2022



July 2022

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1 Overview by Executive Counsel

It has been another busy year for the Enforcement Division, in which we have concluded a significant number of high-profile cases upholding standards and delivering important messages for the market, whilst continuing our programme of growth in size and skills.

Financial sanctions this year reached a record £46.5m, prior to settlement discounts, reflecting the seriousness and number of cases concluded as well as our improved capability to deliver outcomes in the large complex cases which are an increasing feature of our work.

Non-financial sanctions have also grown in number and scope this year. Such sanctions are targeted at the failures identified and play an important part in our role as an improvement regulator. They are directed at identifying the causes of the failures, imposing measures to prevent recurrence, and monitoring progress and effectiveness of the required steps through ongoing reporting to us.

We continue to encourage and incentivise full and frank cooperation. While progress in this area has been slower than hoped, we are seeing positive changes, including through self-reporting, proactive steps taken to address issues self-identified and comprehensive admissions. These actions, which demonstrate self-awareness and self-improvement, are welcome and important examples of cultural changes essential to secure consistent upholding of high standards of behaviour and delivery of high-quality financial statements and audit.

Timely investigative and enforcement action remains a key priority for the Division with five legacy cases closed this year, and more cases concluded than new investigations opened. FRC teams are now the largest source of case referrals, demonstrating joined-up working across the FRC to improve standards and quality.

In this year's Audit Enforcement Review (AER) we have again reported on the persistent themes emerging from concluded cases, highlighting important Tribunal findings concerning the fundamental requirements of integrity and objectivity. Looking ahead, as part of our holistic regulatory approach, we shall be paying particular attention to deficiencies in areas where other parts of the FRC have issued commentary and guidance. As the risks and uncertainties from climate change and geopolitical events continue to rise, this year's AER takes a closer look at the impact of these risks on the work of preparers, auditors and actuaries.

Thank you to all who have engaged and continue to engage with the Enforcement Division, particularly the members of the Division who have greatly contributed to another successful year.



FRC Executive Counsel
Elizabeth Barrett

2 Year ended 31 March 2022 at a glance



47

current investigations



15

investigations opened into auditors, accountants and/or actuaries¹ in the year



24

cases resolved through Constructive Engagement



13

cases resolved with settlement



1

case resolved through Tribunal proceedings



3

cases closed with no further action



Financial sanctions of
£46.5 million
(before settlement discount)



23%

growth in Enforcement Division



Recurring themes in audit investigations: lack of scepticism, insufficient audit evidence



Tribunal report on Silentnight highlighted failures to act with honesty, integrity and objectivity

¹ No investigations in to actuaries were opened during the year.

3 Themes from completed audit investigations

Introduction

This year, in support of the FRC's purpose to drive high standards of corporate reporting and audit and holding to account those responsible for delivering them we concluded 12 audit investigations with sanctions. All 12 cases concerned audits of FTSE or AIM-listed companies performed by the 'Big 4' audit firms as well as Grant Thornton (GT). In all but two,² the auditors failed to obtain sufficient appropriate audit evidence, performed parts of the audits without sufficient professional scepticism and failed to document their workings properly.⁴ At the time of going to print, the outcome of one concluded audit investigation had not yet been published.

These failings go to the heart of audit, the purpose of which is to give reasonable assurance to users of the financial statements that the amounts and disclosures contained are not materially misstated.

Audit evidence

Audit evidence is necessary to support the auditor's opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the audit.^{5,6} Auditors need to plan and perform the audit so that they obtain sufficient appropriate audit evidence. Sufficiency relates to the quantity of evidence, such that more audit evidence is likely to be required when the assessed risk of misstatement is higher. Appropriateness is the measure of the quality of audit evidence. The amount and type of evidence to be obtained therefore depends upon the auditor's assessment of the risk of misstatement.

Professional scepticism

Auditors must approach an audit with professional scepticism. This means adopting a questioning mind, critically assessing audit evidence, and challenging management's assertions. It includes being alert to contradictory audit evidence, information that brings into question the reliability of documents and responses provided during the course of the audit, and conditions that may indicate possible fraud.⁷

2 These two cases were opened as additional audit years to existing investigations. Breaches in these cases concerned insufficient audit evidence and documentation.

3 In one of the remaining two cases, there were breaches regarding audit evidence and documentation, but not a lack of scepticism. Breaches in the second case related solely to the FRC's Ethical Standard.

4 ISA (UK) 200, A28; ISA (UK) 500 A1.

5 ISA (UK) 500, A4, A5.

6 ISA (UK) 200, A18.



Failings go to the heart of audit

Audit documentation

Auditors are obliged to prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the audit work that was done, including the procedures performed, the results of audit testing, the audit evidence obtained, and – in relation to significant matters – the conclusions reached, and significant professional judgements made in reaching those conclusions.⁷

The requirements to obtain sufficient appropriate audit evidence and to plan and perform an audit with professional scepticism are essential to help address the risk inherent in every audit that, due to error or fraud, financial statements will contain misstatements.

Management estimates and judgements

Obtaining sufficient appropriate audit evidence and applying professional scepticism are particularly important when considering parts of the financial statements that are heavily reliant on management's estimates and judgements, examples of which are below.

Contract accounting

When contracts span more than one accounting period, the amount of revenue to be recognised in the year often involves significant estimates from management, such as how advanced the project is (the stage of completion of a contract) or the costs necessary to complete the contract. Similarly, it is often necessary for management to exercise judgement, for example, in relation to whether variations to the contract terms have been agreed by the parties, or whether claims made against third parties are recoverable. Two investigations concluded this year concerned PwC and its audits of construction companies Kier⁷ and Galliford Try.¹⁰⁹ In both investigations there were failures to obtain sufficient appropriate audit evidence that revenue from unagreed variations would be received and that claims against the contractors or third parties would be successful. In both audits, management's explanations for unagreed variations and adjustments to profit were accepted without applying sufficient professional scepticism to the explanations received. Further, in the audit of Kier the auditors also failed to carry out adequate audit procedures or to challenge explanations provided by management in relation to the accuracy of the forecast costs to complete.



**Areas
reliant on
management
estimates and
judgements
require greater
scrutiny**

⁷ ISA (UK) 230.

⁸ Press notice: [Sanctions against PwC and Audit Partner](#)

⁹ Press notice: [Sanctions against PwC and Audit Partner](#)

Loss-making contracts

When accounting for loss-making contracts, management may be required to make estimates regarding losses. It is vital, therefore, that auditors seek sufficient evidence and ask sufficiently probing questions to test such estimates. In GT's audits of Interserve¹⁰ there were evidence and scepticism failings by the auditors in respect of the key judgements and accounting estimates relating to recovery of claims from subcontractors and PI insurers, and sums payable to the employer on termination of a loss-making contract. In EY's audit of Stagecoach,¹¹ EY failed to apply sufficient professional scepticism or to obtain sufficient appropriate evidence to support management's assertions that a loss-making (joint venture) franchise contract with the Department for Transport would be renegotiated.

Accounting for goodwill

Another area requiring management to make estimates is accounting for goodwill. Goodwill arises from the acquisition of a business and is, in essence, the difference between the amount paid for the acquired business and the net value of its identifiable assets and liabilities. Goodwill needs to be checked for impairment each year. The impairment review requires management to forecast future cash flows attributable to that acquired business and, using an appropriate discount rate (which is also a matter of judgement), estimate the current value of goodwill. Of necessity, this work entails making various judgements and estimates about the future and is therefore an area where the auditors need to be alert to optimistic assumptions of management. Robust and rigorous audit work includes ensuring that sufficient appropriate audit evidence is obtained and management's work and assumptions are sufficiently challenged. In both Deloitte's audit of Mitie¹² and KPMG's audit of Conviviality¹³ the auditors failed to obtain sufficient appropriate audit evidence for assurance regarding the future cash flows used by management.

In its audit of Conviviality, KPMG also failed to obtain sufficient appropriate audit evidence or apply sufficient professional scepticism to a number of other accounting judgements and estimates that had been identified as optimistic or aggressive by the auditors in their risk assessment and that had a material impact on the company's profits.

¹⁰ Press notice: [Sanctions against GT and a Partner](#)

¹¹ Press notice: [Sanctions against EY and a Partner](#)

¹² Press notice: [Sanctions against Deloitte LLP and a Partner](#)

¹³ Press notice: [Sanctions against KPMG and a Partner](#)

Supplier rebates

Auditors need to have a good knowledge of the audited entity and the business environment in which it operates. In many retail industries, supplier rebates are used. These are discounts offered by suppliers as business incentives to retailers, to encourage sales. Accounting for supplier rebates can require significant judgements to be made by management when estimating the period-end amounts receivable.¹⁴ Auditors therefore need to be alert to the risk of material misstatements regarding the rebates. In KPMG's audits of Revolution Bars,¹⁵ the auditors demonstrated a lack of professional scepticism by accepting management's assertions that the terms of supplier rebate agreements had not changed significantly from year to year, rather than corroborating this information by checking the rebate terms to the underlying agreements.

Incomplete information from management

When evaluating evidence, the auditor should critically assess audit evidence and be alert for contradictory evidence and/or incomplete information from management. In GT's audits of Patisserie Holdings,¹⁶ there was a repeated failure to scrutinise documents and challenge management explanations in relation to cash, revenue, journal entries and fixed asset additions. This failure occurred despite several 'red flags' that the auditor was receiving inaccurate and incomplete information from management.

In its audit of Sports Direct¹⁷ International ("SDI"), GT failed to treat with professional scepticism management's assertion that a delivery company was not a related party of SDI, even though management's conclusion was made verbally, without any documentary support or evidence, one day before the 2016 financial statements were due to be issued and the auditors were not aware of any apparent material change of circumstances since the conclusion of the 2016 interim review in December 2015 (when the opposite conclusion had been reached).



Critically assess contradictory evidence and/or incomplete information from management

¹⁴ For this reason in 2014, the FRC published a notice urging clarity in the reporting of complex supplier arrangements.

¹⁵ Press notice: [Sanctions against KPMG LLP and an Audit Engagement Partner](#)

¹⁶ Press notice: [Sanctions against GT and a Partner](#)

¹⁷ Press notice: [Sanctions against GT and a Partner](#)

Compliance with laws and regulations

Auditors also need to be alert throughout the audit for indications that there may have been non-compliance with laws and regulations. In KPMG's audit of Rolls Royce¹⁸ the auditors were made aware of payments which had been made by the company to an agent in India at a time when the use of such agents in connection with Indian Government defence contracts was restricted by the Indian authorities. However, they failed to perform audit procedures that were appropriate in the circumstances for the purposes of obtaining sufficient appropriate audit evidence and failed to apply sufficient scepticism. The auditors failed to make any mention on the audit file of the payments to the agent, including records of discussions, with both management and within KPMG, conclusions about whether there was non-compliance, and the basis for those conclusions.

Documentation breaches

In each of the above cases the documentation was substandard, often containing no details of audit procedures followed, no record of audit work carried out, no rationale for audit judgements, and no record of the conclusions reached or the reasons for such conclusions. This was an issue we saw in concluded cases last year (AER 2021,¹⁹ p.29). Proper documentation is key to ensuring that the auditor both has obtained and can demonstrate that they have obtained the necessary assurance that the financial statements are free from misstatements, and documentation failures are a serious matter. This is not least the case in audits involving estimates and judgements where a clear contemporary record of the factors which have informed the auditors' conclusions in complex areas is likely to be of critical importance.



**Documentation
was
substandard**

¹⁸ Press notice: [Sanctions against KPMG and Audit Engagement Partner](#)

¹⁹ [Audit Enforcement Review 2021](#)

4 The team and processes

Who are the members of the FRC Enforcement Division?

The Division handles case examination and enquiries, investigations and enforcement action.

During the year, our team grew from 52 to 64.

The team comprises:

- | | |
|--|--|
| <p> Executive Counsel:
Elizabeth Barrett</p> <p> Deputy Executive Counsel:
Claudia Mortimore,
Jamie Symington</p> <p> Lawyers (qualified barristers or solicitors and trainee solicitors)</p> | <p> Forensic Accountants</p> <p> Legal Assistants</p> <p> Case Examination and Enquiries team members</p> <p> Operations and Administrative team members</p> |
|--|--|

Who can the FRC investigate?



Accountants and actuaries under the Accountancy Scheme and Actuarial Scheme



Statutory audit firms and auditors under the Audit Enforcement Procedure (AEP)

Case Examination and Enquiries (CEE) - Intelligence-gathering, initial enquiries²⁰

Sources

- Horizon-scanning
- Referrals from other FRC teams, regulators, audit firms and professional bodies
- Complaints
- Whistleblowing disclosures

Outcomes

- Referral to Conduct Committee for decision on opening of investigation
- Constructive Engagement (AEP only)
- Referral to another FRC team
- Referral to a professional accountancy or actuarial body or regulator
- No further action

Investigations and Enforcement - Conduct of investigations referred by Conduct Committee

Outcomes

AEP:

- Investigation Report (IR)
- Decision Notice and proposed sanction
- Accepted or Tribunal convened

Scheme:

- Proposed Formal Complaint/Formal Complaint
- Settlement or Tribunal convened

At any point, Executive Counsel can close a case should the threshold for taking enforcement action not be met

Sanctions

Financial:

- Unlimited fines

Non-financial sanctions e.g.

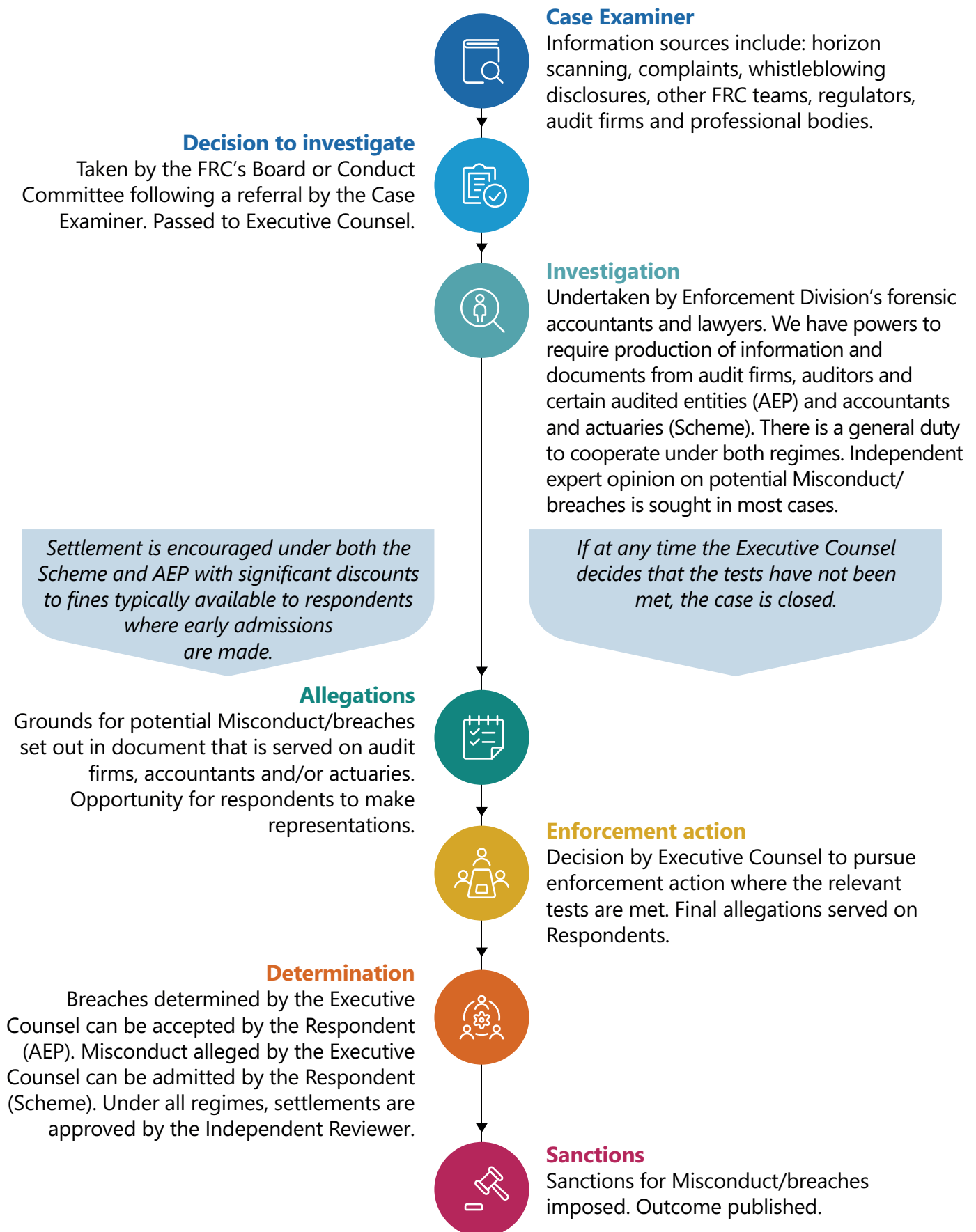
- Reprimand
- Exclusion as a member of a professional body
- Other remedial actions as appropriate

Sanctions are determined by reference to the [Sanctions Policy \(AEP\)](#), [Accountancy Sanctions Guidance \(Scheme\)](#) and [Actuarial Sanctions Guidance \(Scheme\)](#)

²⁰ Since October 2020, Case Examination and Enquiries in audit matters has been handled in the Audit Firm Supervision team within the Supervision Division, though the Case Examiner for such cases remains in the Enforcement Division.

Enforcement process

A high-level overview of our enforcement process is set out in the flow chart below. Further details of the FRC's remit and powers can be found in Appendix A.



5 Review of the year

Case Examination and Enquiries

2021/22 is the fifth year since the AEP came into force and the Case Examination and Enquiry (CEE) process was introduced. The AEP brought a significant shift in audit enforcement, with the expansion of the FRC's remit (to all public interest entities (PIEs), large AIM²¹ companies and Lloyd's Syndicates) and a change to the threshold for examining potential Statutory Audit failures (to potential breaches of Relevant Requirements as opposed to potential Misconduct). The AEP also introduced Constructive Engagement, to deal with cases where the audit quality concerns can be appropriately and satisfactorily addressed, and the risk of repetition mitigated through engagement with the firm without the time and expense of full enforcement action. Further details of the FRC's powers, the AEP and Constructive Engagement process are set out in Appendix A.

The Case Examiner is responsible for decisions taken as to which cases are presented to the Conduct Committee for potential investigation. However, since October 2020, enquiries undertaken to support these decisions in audit matters under the AEP are conducted within the Audit Firm Supervision team. This is to leverage the detailed audit firm knowledge of the Audit Firm Supervisor, who is in general the primary contact for the firm and with whom the firm has regular liaison.

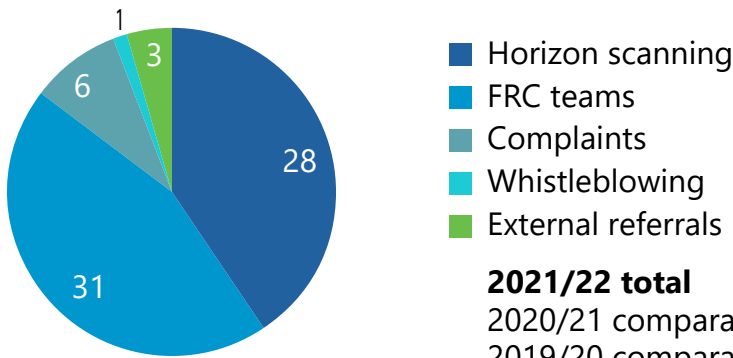
The below table summarises the number of cases opened and closed in the current and preceding two years.

Cases	2021/22	2020/21	2019/20
Open at start of the year	20	28	23
Opened in the year	69	95	88
Closed in the year	(62)	(103)	(83)
Open at end of the year	27	20	28

²¹ UK companies admitted for trading on AIM or Aquis Stock Exchange Growth Market with a market capitalisation of more than €200 million, using the formula in MiFID II.

Cases opened in the year^{22,23}

Cases opened (by source)



2021/22 total	69
2020/21 comparative	95
2019/20 comparative	88

Sixty-nine cases were opened in the year compared with 95 in the previous year, a decrease of 27%. This decrease is due to the number of cases identified through CEE's horizon-scanning activities. This drop is in the main attributable to opening fewer cases on issues in an audit which have already been dealt with by Constructive Engagement or for which Constructive Engagement is already underway with the relevant audit firm, thereby negating the need to open a new case relating to the audit of the same entity on the same issue.²⁴

Referrals from FRC teams are now the largest source of our cases and are fairly consistent with the prior year. These referrals predominantly arose from Audit Quality Review (AQR) inspections of individual audits, with a small number from reviews of financial statements by Corporate Reporting Review (CRR) and from existing Enforcement investigations.²⁵

The number of complaints and whistleblowing disclosures passed to CEE for initial assessment remained consistent with those received in the previous year. However, fewer external referrals were received this year from professional bodies and other regulators, more than halving from seven to three.

Consistent with the prior year, most cases opened were audit-related (94% compared with 93%). This reflects the lower threshold under the AEP, as opposed to the Schemes which cover accountants' and actuaries' conduct.

At 31 March 2022, 27 cases remained open, compared with 20 at 31 March 2021. Eight of the 27 cases open at 31 March 2022 have been open for less than one month.



69
cases opened during the year



94%
of cases opened in the year were audit-related

²² The enquiries and outcomes data comprises all cases passing through the case examination process, including all audit matters dealt with under the AEP, and all Scheme matters progressed to the Conduct Committee.

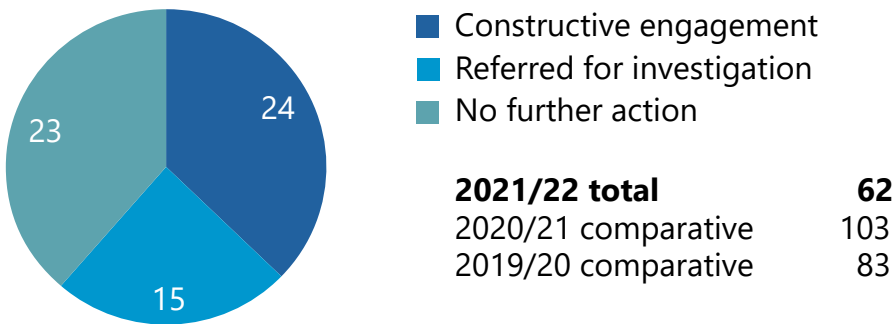
²³ The source category refers to the method by which a matter first came to the FRC's attention. It may be that matters we identify through horizon-scanning activities are also subsequently the subject of complaints or external referrals.

²⁴ Remedial actions agreed in one financial year will not have an impact until the following year's audit.

²⁵ Referrals from the Enforcement team relate to cases where potential breaches have been identified in additional audit years or where potential additional subjects have been identified in relation to an existing investigation under the AEP or the Schemes.

Outcome of CEE cases²⁶

Cases closed by outcome



24
cases were
resolved
through
Constructive
Engagement

During the year, 62 cases were closed, a decrease of 41, or 40%, on the previous year (103 cases closed). This is due to a decrease in the number of cases open at the start of the year (20 compared to 28 in the previous year) and a decrease in cases opened during the year (69 compared to 95 in the previous year). The table on page 12 summarises the number of cases opened and closed in the current and preceding two years. Of the cases closed:

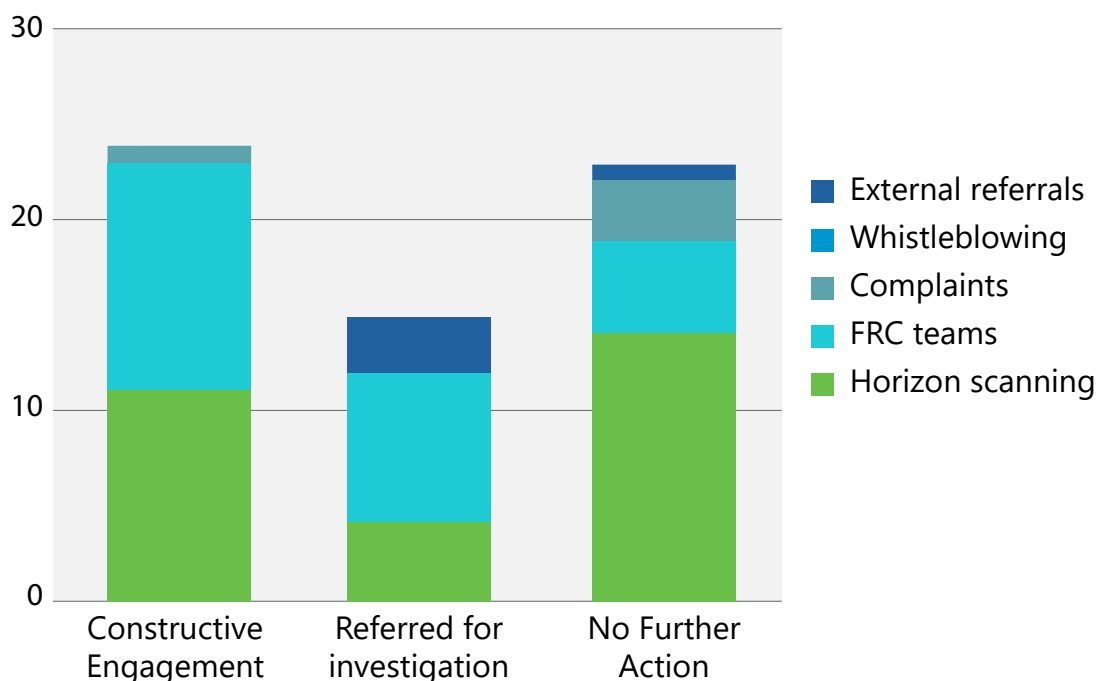
- 15 cases (2020/21: 14) were referred by the Conduct Committee to Executive Counsel for investigation;
- 24 cases (2020/21: 48) were resolved through Constructive Engagement; and
- 23 (2020/21: 41) resulted in no further action by the Case Examiner, of which one was referred to a professional body.

More details of the cases in each closure outcome are set out in the sub-sections below.

²⁶ Cases are regarded as closed at the point of referral for investigation by the Conduct Committee or when the decision is taken that no further enquiry work needs to be undertaken by the Case Examiner. Individual outcomes are not published, except where they lead to the opening of investigations and where, in accordance with the Publication Policies, it is considered appropriate to announce that investigation.

The following chart illustrates how the case outcomes break down by source:

Outcome of cases with source details



Referrals to the Conduct Committee for investigation

The cases referred to the Conduct Committee, and the Conduct Committee's decisions in the year comprised:

	Referred for investigation under the AEP or the Schemes	No further action	Total
Audit	14	1	15
Accountancy	1	0	1
Actuarial	0	0	0
Total	15	1	16

Fifteen of these cases were referred for investigation (under the AEP or the Schemes). Further details of the new investigations opened (to the extent that details may be given) are shown under Investigations and Enforcement later in this section. The remaining case was referred to the relevant professional body after the Conduct Committee decided that there was insufficient public interest for the FRC to open an investigation given the entity was not in the FRC's remit.

While the overall number of cases opened and closed during the year has decreased, the number of cases where an investigation has been opened remains consistent with the previous year (15 versus 14 last year).

The average time taken to refer a case to the Conduct Committee was just over two months, a considerable improvement over last year, which was just under four and a half months. All cases referred to the Conduct Committee were referred within six months from the date the case was opened.²⁷

Constructive Engagement

We continued our focus during the year on further developing the Constructive Engagement process as an effective and efficient alternative to referring qualifying²⁸ cases for investigation.

Twenty four cases (39%), involving a wide range of issues, were resolved through Constructive Engagement during the year, this is a decrease of 50% compared to the previous year (48 cases, or 47%). As noted above, this is mainly attributable to opening fewer cases on audit issues which have already been dealt with by Constructive Engagement or for which Constructive Engagement is already underway with the relevant audit firm, thereby negating the need to open a new case relating to the audit of the same entity on the same issue.

In resolving the 24 cases, we engaged with 10 separate Statutory Audit firms. Eleven (46%) of the cases involved the Big Four accounting firms and 19 cases (79%) involved the seven largest firms.

Half of the cases resolved through Constructive Engagement involved errors in financial statements, which led to subsequent restatements. The suitability of each case for Constructive Engagement is determined on its own merits taking into account a range of factors. In general, we determined cases were suitable for Constructive Engagement where the errors appeared unlikely to have had a real impact on the decisions taken by users of an entity's financial statements. This may have been because the errors were only marginally material in a quantitative sense, were in highly technical areas of the financial statements or were in areas that were not of fundamental importance to the measurement of the underlying financial performance of the entity.

The other cases resolved through Constructive Engagement included potential breaches of auditing standards that had been identified through AQR inspections, CRR reviews or by events in the public domain that warranted further enquiry as to how the auditors had approached the factors underlying those events.

Timely intervention through Constructive Engagement enables remedial actions being taken by the audit firm in time for the following year's audit (as well as improving the firm's overall audit quality control procedures).



Number of cases dealt with through Constructive Engagement down

50%



Average time taken to conclude cases through Constructive Engagement was just over seven months

²⁷ A case is opened on the date of the receipt of complaint, referral from another division, referral from another regulator or date identified through horizon-scanning activities.

²⁸ [Guidance for the Case Examiner \(AEP\)](#), paragraph 13 to 15 outlines where a case may be suitable for Constructive Engagement.

The average time taken to conclude the Constructive Engagement cases was just over seven months.

Across the 24 Constructive Engagement cases, the most common accounting areas were as follows:

- **Revenue (8 cases):** in these cases, either no evidence was available to us that there had been a material error (though deficiencies in the audit work had been identified), or there was an error that we concluded that in the circumstances in question was likely to have had a relatively low impact, for example weaknesses in relation to audit procedures over the completeness of revenue. Two cases concerned revenue recognised on long-term contracts.
- **Acquisition accounting (4 cases):** in these cases, there were technical errors in accounting for acquisitions, typically affecting deferred tax and goodwill balances.
- **Cash flow statements (3 cases):** classification errors relating to investing, financing and operating cash flows were identified as suitable for Constructive Engagement if and when they pre-dated Constructive Engagement already undertaken with the audit firms on this issue.

In these 24 cases, the most common issues underlying the potential breaches of Relevant Requirements under the AEP were as follows:²⁹

- **Lack of professional scepticism (15 cases):** failure to challenge or document the challenge to management's accounting treatment, overreliance on management or its advisers, or failure to consider the need for independent advice and insufficient quality review.
- **Insufficient audit evidence (8 cases):** often in an area not regarded as a significant risk or area of audit focus, for example accounting for reserves, or cash flow statement.
- **Lack of professional judgement (6 cases):** for example, failing to consult technical experts in complex areas or failing to consider the appropriateness of the sampling approach.
- **Lack of technical expertise (3 cases):** for example, by failing to account correctly for acquisitions or to use experts for complex valuations.

The remedial actions undertaken as a result of our Constructive Engagement activity largely involved amendments to a firm's audit procedures and/or training and guidance to introduce the new audit procedures or to reinforce the existing audit methodology and guidance.

²⁹ There may be multiple underlying issues pertaining to a single case.

Examples of remedial actions include:

- undertaking 'root cause analyses' on the issues, including interviewing the audit team;
- the introduction of 'hot reviews' on certain higher-risk audits, allowing for greater technical consultation throughout the audit;
- delivery of mandatory training for audit specialists and experts on both making challenges and being open to challenge;
- updating a firm's audit methodology to increase the level of detail in the procedures.

While each case is considered on its own merits, to illustrate the range of Constructive Engagement activity undertaken, two anonymised case examples are set out below.

Case A

A listed company had materially understated its 2019 provision for dilapidations on a leased building. Our enquiries with the audit team found that they had relied on an estimate from the landlord's agent without assessing the competency and objectivity of that agent. Management had also not recorded a detailed assessment of the works to be carried out and the related costs.

The matter was suitable for Constructive Engagement because there was no apparent financial detriment or adverse investor, market or public comment on the audit resulting in a possible loss of confidence in the auditing profession.

The Constructive Engagement process resulted in the audit firm strengthening its procedures on provisions, with a greater focus on challenge of management and corroboration of estimates. Training was also provided to embed those procedures.



The firm strengthened its procedures on provisions and challenge of management

Case B



A listed company restated its 2019 reserves to correctly account for several long-term incentive plans (LTIPs), including share-based payments. The audit team had identified LTIPs as a significant risk during the 2019 audit based on their complex nature, the magnitude of the amounts involved, and the level of judgement involved.

The restatements arose from accounting errors in recognising a share premium, double-counting adjustments, and inappropriate equity accounting.

The restatements resulted in the reclassification from one non-distributable reserve to another and involved a highly technical accounting area. Additionally, there was no indication of financial harm to any stakeholder – as a result, Constructive Engagement was deemed appropriate.

The audit firm agreed to develop and implement new training modules regarding share-based payments. Furthermore, the audit firm updated existing guidance to audit teams regarding consulting the firm's technical accounting and specialist teams on complex LTIP arrangements.



The firm will develop and implement new training modules regarding share-based payments

Certain actions agreed through our Constructive Engagement activity – designed to improve audit quality – are similar to the types of non-financial sanctions imposed at the conclusion of enforcement action. While Constructive Engagement outcomes do not amount to a sanction, and are not individually published, they can result in potentially significant additional requirements for audit firms. The process requires full and open cooperation by audit firms. During the year, we were generally satisfied with the level of cooperation and timeliness of responses we received.

The value of Constructive Engagement activity is also dependent on the new measures being appropriately followed by audit teams in practice. This is monitored by a firm's dedicated Audit Firm Supervisor within the Audit Firm Supervision team. Where appropriate, the Supervisors will work with the FRC's AQR team in conducting follow-up work. CEE also monitors where similar matters are identified in audits conducted by the same audit firms, and recurring matters may be taken into account when deciding whether to refer a matter to the Conduct Committee to consider opening an investigation.

No further action

There were 23 cases closed in the year with no further action.

In 19 of these 23 cases, the information that came to our attention involved the Statutory Audit of at least one UK PIE or large AIM-listed organisation. We consider all such cases carefully and in detail to identify whether there may be underlying issues of relevance to the work conducted by the Statutory Auditors. However, on examination of the information available in these 19 cases, we found no basis to support further enquiry into the audit. The reasons for this included one or more of the following:

- there was no substantive financial reporting error at the entity;
- there was no indication of a breach of a Relevant Requirement by a Statutory Auditor, for example where the underlying issue was not within the scope of a Statutory Audit; and/or
- the complaints raised related to the conduct of an entity's directors or other personnel not within the FRC's remit

In the remaining 4 cases, the reasons for no further action included:

- the cases involved UK audit matters which the FRC has delegated to the Recognised Supervisory Bodies (RSBs)³⁰ (e.g. the audits of privately owned companies); or
- matters where there was insufficient evidence to demonstrate failings by the auditors, accountants or actuaries.

Where a case raises issues that are not in the FRC's remit, we can direct complainants to other bodies, which may address their complaints. This year, those bodies included the RSBs, the accountancy professional bodies, the Financial Conduct Authority and the Insolvency Service.

Oversight

All decisions by the Case Examiner to resolve cases through Constructive Engagement or to close them with no further action are subject to peer review. In addition, the details of all such cases are reported to the Conduct Committee on a quarterly basis.



23

**cases were
closed with
no further
action**

³⁰ Recognised Supervisory Bodies (RSBs) are the Institute of Chartered Accountants in England and Wales (ICAEW), the Institute of Chartered Accountants of Scotland (ICAS), Chartered Accountants Ireland (CAI) and the Association of Chartered Certified Accountants (ACCA).

Investigations and Enforcement

Investigations opened

	2019/20	2020/21	2021/22
Investigations opened in year	14	16	15
Preliminary enquiries opened in year	3	0	0

The Conduct Committee opened 15 new investigations in the 12 months to 31 March 2022: 14 audit investigations under the AEP and one investigation into accountants under the Accountancy Scheme.

The AEP investigations

The 14 investigations concern a wide range of audit issues, including professional scepticism; audit evidence and documentation; integrity and objectivity; related party transactions; compliance with laws and regulations; control environment; group audits, including oversight of component audit files; going concern; revenue and revenue recognition; fixed asset impairments; inventory and inventory provisions; investments and financial assets; non-audit work; provisions; fraud; and presentation and disclosure. Seven of these investigations opened by the Conduct Committee followed referrals to the Case Examiner from the FRC's AQR team, following audit inspections.

In accordance with the FRC's Publication Policies,³¹ not all investigations are announced at the outset, although if the case leads to enforcement action and the imposition of sanctions, the outcome will be published. The Conduct Committee makes the decision whether or not to announce a new investigation on a case-by-case basis. It will only decide to announce the opening of an investigation if it considers that such publication is necessary in all the circumstances and any potential prejudice to the subject of an investigation is outweighed by the factors in favour of publication.

The 13³² new AEP investigations that have been announced are:

- PwC's audit of the consolidated financial statements of Wyelands Bank plc for the year ended 30 April 2019;
- Saffery Champness's audit of the financial statements of Greensill Capital (UK) Limited for the year ended 31 December 2019;
- Mazars's audit of the consolidated financial statements of French Connection Group plc for the year ended 31 January 2020;
- BDO's audit of the consolidated financial statements of NMCN plc for the year ended 31 December 2019;

³¹ Links to the publication policies are here: [Publication Policy \(Accountancy and Actuarial Schemes\)](#), [Publication Policy \(Audit Enforcement Procedure\)](#)

³² As a comparison, seven investigations were announced in 2020/21. A list of current FRC investigations which have been publicly announced under the AEP can be found [here](#), under the Accountancy Scheme can be found [here](#), and under the Actuarial Scheme can be found [here](#)



15

investigations
opened in the
year

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- Crowe UK's audits of the financial statements of Akazoo Limited for the years ended 31 December 2016, 2017 and 2018;
 - MacIntyre Hudson's (trading as MHA MacIntyre Hudson) audits of the financial statements of MRG Finance UK plc for the years ended 31 December 2018 and 31 December 2019;
 - PwC's audits of the consolidated financial statements of Babcock International Group plc for the years ended 31 March 2019 and 2020;
 - HW Fisher's audit of the financial statements of Liberty Commodities Limited for the year ended 31 March 2020;
 - Four investigations in relation to the Statutory Audits by King & King of:
 - the consolidated financial statements of Liberty Speciality Steels Limited for the year ended 31 March 2019;
 - the financial statements of Alvanco British Aluminium Limited (formerly Liberty Aluminium Lochaber Ltd) for the year ended 31 March 2019;
 - the financial statements of Liberty Steel Newport Limited for the year ended 31 March 2019; and
 - the financial statements of Liberty Performance Steels Limited for the year ended 31 March 2020.
 - Deloitte's audit of the consolidated financial statements of Go-Ahead Group plc for the years ended 2 July 2016, 1 July 2017, 30 June 2018, 29 June 2019, 27 June 2020, and 3 July 2021.

Accountancy Scheme investigations

One new investigation under the Accountancy Scheme was opened. In accordance with the FRC's Publication Policy, this was not announced. Given the higher threshold for investigation, it is to be expected that fewer cases satisfy the criteria for opening an investigation under the Accountancy Scheme than under the AEP. The new investigation under the Accountancy Scheme involves the conduct of the finance director of a listed company in respect of the preparation of financial statements.

Actuarial Scheme investigations

No new investigations were opened by the Conduct Committee under the Actuarial Scheme in 2021/2022.

Preliminary enquiries

No new preliminary enquiries were opened by the Conduct Committee under the Schemes in 2021/22.

Spotlight on Audit Enforcement Procedure

The Audit Enforcement Procedure (AEP) came into force in June 2016. At that time, the FRC committed to a post-implementation review to gauge how the new procedure was working and to see if any amendments were needed. Following that review, a revised version of the AEP, which followed a public consultation on the proposed amendments, came into force on 5 January 2022.

The revisions are intended to ensure a clearer, more effective and streamlined process, and provide more detail where helpful.

The proposed revisions were generally welcomed by those who responded to the consultation, and the greater detail and clarity should be helpful to those using the procedure.

The more significant changes are set out below:

i) Clarification of the Case Examiner's powers

The revised AEP clarifies the powers available to the Case Examiner on receipt of information about a Statutory Auditor or Statutory Audit Firm.³³ The powers largely replicate those of the Executive Counsel, which means that the Case Examiner can serve notices compelling information from audit firms and listed (and other public interest) audited entities. This will enable effective information gathering at the initial enquiry stage, which will help the Case Examiner to determine whether further steps are warranted and, if so, whether the matter should be dealt with by Constructive Engagement or referred to the Conduct Committee to consider opening an investigation.

ii) Clarity about the discretion of the Case Examiner and the Executive Counsel

The revised AEP, through Rules 5 and 19, clarifies that both the Case Examiner (at the initial enquiry stage) and the Executive Counsel (at the investigation stage) have discretion to close enquiries or investigations without taking action.

Rule 5 provides that, even where the Case Examiner determines that information about a Statutory Auditor or Statutory Audit Firm raises a question as to whether either has breached a Relevant Requirement, the options³⁴ available to the Case Examiner include discretion to take no further action.

Rule 19 provides that, after considering representations received from the Respondent following service of an Investigation Report, the Executive Counsel will decide:



A revised version of the AEP came into force on 5 January 2022

³³ The powers were available under SATCAR, but were not expressly referred to in the previous version of the AEP.

³⁴ Other options are to arrange Constructive Engagement, to refer the matter to the Executive Counsel to apply for an Interim Order to be made by a Tribunal, or to refer the matter to the Conduct Committee.

- (a) if the Respondent has breached any Relevant Requirements; and
- (b) if so, whether the Respondent should be liable for Enforcement Action.

This two-limbed test makes clear that the Executive Counsel is not bound to take Enforcement Action for every breach identified, or indeed at all.

Allowing such discretion at both stages is consistent with the Regulators' Code principle that Regulators should take a proportionate approach and allocate resources where they are most effective in addressing risks. We are not bound to commence or to proceed with enquiries or investigations where there is little or no public interest.

iii) Extension of investigations to include another year of audits or additional statutory auditor/s

The 2016 version of the AEP did not contain a mechanism for extending the scope of investigations (unlike the Accountancy and Actuarial Schemes, which allow extensions to scope). As a result, where concerns arose about additional audit years and/or other Statutory Auditors in AEP investigations, a new investigation had to be opened. Whilst, in practice, the investigatory work was usually combined, creating a new investigation was artificial and inefficient. The revised AEP allows for the extension of investigations by adding more audit years or more subjects.

iv) Removal of the Enforcement Committee stage and introduction of an Independent Reviewer

The revised AEP has only two stages: the Executive Counsel investigation stage and the Tribunal stage. The Enforcement Committee has now been removed from the process.

The rationale for creating the Enforcement Committee was to allow for matters which had not been concluded at the Executive Counsel stage to be resolved by the Enforcement Committee at less cost and in a more timely way than a hearing before the Tribunal.

Since its introduction, however, no cases had been heard by the Enforcement Committee under the AEP. All AEP cases concluded to date had done so at the Executive Counsel stage. Further, the FRC considers that, if cases are not resolved early, the most appropriate forum for determining audit issues (which often engage complicated and complex issues) is the Tribunal, where hearings will ordinarily take place in public; the evidence can be presented in full; and parties have the ability to call witnesses, including experts. The FRC was concerned that the Enforcement Committee – which did not allow for live evidence and would not have been held in public – would not have been a suitable forum.

Moreover, to provide a check and balance that the Decision Notices being concluded at the Executive Counsel stage are appropriate, Rules 24–28 and 106–110 of the revised AEP provide for an Independent Reviewer to approve all Decision Notices agreed between the Executive Counsel and Respondents before they are finalised.

This will provide reassurance that sanctions imposed in cases concluded at the Executive Counsel stage reflect the public interest and are proportionate and fair. If the Independent Reviewer does not approve the issue of a Decision Notice, Executive Counsel may either issue a revised Proposed Decision Notice or refer the matter to the Tribunal.

v) Enhanced procedure for obtaining Interim Orders

The revised AEP sets out more clearly the processes for applying for, reviewing, amending and revoking Interim Orders.

It provides clarification that Interim Orders can only be made by the Tribunal when:

- (a) there are reasonable grounds to consider that the Respondent may have breached a Relevant Requirement; and
- (b) it is necessary for the protection of the public or is in the public interest for an Interim Order to be made.

vi) The inclusion of an explicit settlement process

The revised AEP introduces an explicit process for settling cases. That process permits the Executive Counsel, having regard to the public interest, to enter into settlement discussions at any time after the opening of an investigation but prior to the issue of a Final Decision Notice by the Tribunal. Whilst a number of settlements were reached under the 2016 AEP, these have involved the parties agreeing (by side letters and undertakings) to dispense with certain formal stages of the procedure. That is not necessary under the specific settlement process set out within the revised AEP.

vii) Rights of Appeal for all Parties

Rights of appeal under the 2016 AEP were limited to the Respondents, who could appeal Interim Orders (imposed by the Enforcement Committee), or Final Decision Notices imposed by the Enforcement Committee or the Tribunal.

The rights of appeal have been extended to the Executive Counsel. All parties can now appeal to the Appeal Tribunal:

-
- (a) the decision to impose or refuse to impose an Interim Order; and
 - (b) a Final Decision Notice made by the Tribunal.

viii) Confidentiality provisions

The revised AEP makes clear that information disclosed by the FRC as part of its investigations must be treated confidentially, and can only be disclosed to certain people and in defined limited circumstances:

- (a) to that person's legal representatives;
- (b) for the purposes of a Hearing;
- (c) with the prior written consent of Executive Counsel;
- (d) to the extent required by law; or
- (e) to any other person to whom disclosure is necessary for the purposes of obtaining evidence, information or assistance in connection with the investigation or Enforcement Action, subject to that person undertaking to keep the information confidential.

Concluded cases

Outcome of investigations

	Closed with no further action	Closed with findings of Misconduct/breaches and sanctions		Total
		Settlement	Tribunal	
2019/20	4	8	1	13
2020/21	3	6	1	10
2021/22	3	13	1	17

Seventeen cases were concluded in the 12 months to 31 March 2022. Reversing the trend of previous years, this is greater than the number of cases opened in the same period. Following a surge in the number of opened cases between October 2017 and September 2018, in part due to the lower threshold test introduced under SATCAR³⁵ and the AEP, three years on we have seen a significant number of cases reaching settlement.

Cases concluded with sanctions

The FRC published outcomes of 13 investigations that resulted in sanctions being imposed on audit firms and individuals during the year.

Details of the 13 cases are set out below. Additional case summaries are included in Appendix D.



13
published
outcomes of
investigations
that resulted
in sanctions
being imposed
during the
year

³⁵ The Statutory Auditors and Third Country Auditors Regulations 2016/649.

EY/Stagecoach Group plc/AEP³⁶

In June 2021, a Final Decision Notice was issued making findings of breaches of Relevant Requirements by EY and the Audit Partner in relation to the Statutory Audit of the financial statements of Stagecoach Group plc for the 2017 financial year.

The breaches concerned three areas of audit work: defined benefit pension obligations, provisions for insurance liabilities, and an onerous contract provision. Across each of these three areas, similar breaches of Relevant Requirements occurred across the spectrum of the audit process, from planning, through substantive testing, to reporting to those charged with governance, disclosures in the financial statements and documentation. Each of the areas involved material financial balances, and in many cases similar breaches were identified in one or more of those audit areas. In certain cases, the breaches were of a basic and/or fundamental nature, evidencing a serious lack of competence in conducting the audit work. Many of the breaches also reflected a failure to challenge management and to exercise professional scepticism, which is at the heart of auditors' duties in discharging their role. The poor standard of the audit documentation maintained (which is supposed to be a thorough, clear and accurate record of the audit processes and responses taken, and judgements and conclusions reached) was of particular concern in this case.

EY received a financial sanction of £3.5 million (adjusted for mitigating factors by 10% to reflect the root cause analysis EY had conducted and the remedial action the firm had implemented), discounted for admissions and early disposal by 30% to £2.205 million. EY was issued with a Severe Reprimand and a declaration was made that the Audit Report did not satisfy the audit reporting requirements. EY was further required to report to the FRC in respect of audits performed by the firm which involved onerous contract provisions. A financial sanction of £100,000 (discounted by 30% to £70,000 for admissions and early disposal) was imposed on the Partner.

³⁶ Press notice: [Sanctions against Ernst & Young LLP and a Partner](#)

KPMG/Silentnight/Accountancy Scheme^{37,38,39}

In July 2021, the independent Disciplinary Tribunal made findings of Misconduct, under the Accountancy Scheme, and imposed sanctions on a former Partner and Head of KPMG Manchester Restructuring.

The Misconduct related to the Partner's role in providing restructuring services to Silentnight in late 2010 and early 2011.

The Tribunal made findings of Misconduct in respect of breaches of the fundamental principles of integrity and objectivity. It also held that the Partner (and through him KPMG) had acted dishonestly. Specifically:

- the Partner advised and/or assisted both Silentnight and HIG at a time when there was a conflict of interest between the interests of Silentnight and HIG; and
- the Partner dishonestly advanced and associated himself with untrue and misleading and/or materially incomplete statements as to the causes of Silentnight's difficulties, in order to assist HIG.

The Tribunal also made serious findings regarding the manner in which KPMG and the Partner had responded to regulatory action, including finding that the Respondents had in part advanced an untruthful defence. They were also found to have been uncooperative. Further details are set out in the spotlight on page 41.

KPMG received a financial sanction of £13 million (the then highest amount for a non-audit case) and received a Severe Reprimand. As a non-financial sanction, KPMG was ordered to appoint (at their own cost and under the FRC's ongoing supervision) an independent reviewer to conduct a review of certain prior engagements and KPMG policies. KPMG was also ordered to pay Executive Counsel's agreed costs (£2.45 million) and the costs of the Tribunal (£305,814).

The Partner was excluded from membership of the ICAEW, and precluded from holding an insolvency licence, for 13 years. He received a £500,000 sanction and a Severe Reprimand.

37 Press notice: [Sanctions against KPMG and former Partner in relation to Silentnight](#)

38 Press notice: [Publication of the report of the Disciplinary Tribunal](#)

39 [Report of the Disciplinary Tribunal in Silentnight](#)

GT/Patisserie Holdings plc/AEP⁴⁰

In July 2021, a Final Decision Notice was issued, and sanctions imposed against GT and the Audit Partner in relation to the Statutory Audit of the financial statements of Patisserie Holdings plc for the financial years ended 30 September 2015, 2016, and 2017.

The breaches concerned four areas of audit work: revenue, cash, journals and fixed asset additions. In each of the three years, the audit work included serious breaches of Relevant Requirements across the four different audit areas, often repeated year on year, and in relation to several legal entities. The breaches reveal a pattern of serious lapses in professional judgement, failures to exercise professional scepticism, failures to obtain sufficient appropriate audit evidence and/or to prepare sufficient audit documentation.

Consequently, each of the FY2015, FY2016 and FY2017 Audits failed in their principal objectives of providing reasonable assurance that the financial statements were free from material misstatement, whether caused by fraud or error.

GT received a financial sanction of £4.0 million (adjusted for aggravating and mitigating factors, in particular, reflecting an exceptional level of cooperation) by 10% and discounted for admissions and early disposal by 35% to £2.34 million. In addition, a suite of non-financial sanctions was imposed, including reporting to the FRC annually for three years on the impact of GT's remedial actions (including a root cause analysis) on audit quality; a review of the audit practice's culture relating to challenge; additional monitoring in relation to bank and cash audit work; a declaration that the Statutory Audit Report for each of the three years did not satisfy the Relevant Requirements, together with a Severe Reprimand.

The Partner received a financial sanction of £150,000 (adjusted for aggravating and mitigating factors – in particular, reflecting an exceptional level of cooperation – by a reduction of 10%) and discounted for admissions and early disposal by 35%, to £87,750; a three-year prohibition from carrying out Statutory Audits and signing Statutory Audit Reports; and a declaration that the Statutory Audit Report for each of the three years did not satisfy the Relevant Requirements, together with a Severe Reprimand.

⁴⁰ Press notice: [Sanctions against GT and a Partner](#)

GT/Interserve plc/AEP⁴¹

In August 2021, a Final Decision Notice was issued making findings of breaches of Relevant Requirements by GT and the Audit Partner in relation to the Statutory Audits of the financial statements of Interserve for the 2015, 2016 and 2017 financial years.

The Adverse Findings concern the audit work performed on:

- a substantial loss provision in the financial statements for FY2015 and FY2016 against a construction contract. There were evidence and scepticism failings by the auditors in respect of key judgements and accounting estimates relevant to the loss provision, an area identified as a significant risk in the audit; and
- aspects of the auditors' assessments of going concern and goodwill impairment in the financial statements for FY2017, where work on elements of the analysis of management's modelling of the financial data was inadequately performed or, in some respects, inadequately documented.

GT received a financial sanction of £1.3 million (adjusted for mitigating factors, including exceptional cooperation, by a reduction of 15%) and discounted for admissions and early disposal to £718,250; a Severe Reprimand; and a non-financial sanction requiring GT to report to the FRC on its monitoring programme of the quality of audit work on loss-making contracts. The Audit Partner received a financial sanction of £70,000 (adjusted for mitigating factors, including exceptional cooperation, by a reduction of 15%) and discounted by 35% for admissions and early disposal to £38,675, and a Severe Reprimand.

⁴¹ Press notice: [Sanctions against GT and a Partner](#)

GT/Sports Direct International plc⁴²/AEP⁴³

In November 2021, Final Decision Notices were issued making findings of breaches of Relevant Requirements by GT and the Audit Partner in relation to the statutory audits of the financial statements of Sports Direct International plc (SDI) for the financial years ended 24 April 2016 (2016 Audit) and 29 April 2018 (2018 Audit).

In respect of the 2016 Audit, there were failings by the Respondents in the conduct of the audit concerning their assessment as to whether SDI's financial statements contained the necessary disclosures to draw attention to the possibility that its financial position may have been affected by its relationship with a delivery company.

In respect of the 2018 Audit, there were failures in the Respondents' audit work relating to two specific areas of the audit; inventory provisions and website sales revenue.

For the 2016 Audit, GT received a financial sanction of £1.7 million (adjusted for mitigating factors by a reduction of 5%) and discounted for admissions and early disposal to £1.1305 million), a Severe Reprimand, a declaration that the Statutory Audit Report did not satisfy the Relevant Requirements and a requirement that GT report to the FRC on whether changes made to its audit methodology are resulting in a better exercise and documentation of an audit team's judgement. The Partner received a financial sanction of £90,000 (discounted for admissions and early disposal to £63,000) and a Severe Reprimand.

For the 2018 Audit, GT received a financial sanction of £350,000 (adjusted for mitigating factors – in particular reflecting an exceptional level of cooperation) by a reduction of 15% and discounted for admissions and early disposal by 35% to £193,375, a Severe Reprimand, a declaration that the Statutory Audit Report did not satisfy the Relevant Requirements and a requirement that GT undertake thematic reviews and report to the FRC as to the efficacy of enhancements it has introduced. The Partner received a financial sanction of £30,000 (adjusted for mitigating factors in particular reflecting an exceptional level of cooperation) and discounted for admissions and early disposal by 35% to £16,575) and a Severe Reprimand.

This comprises two Investigations.⁴⁴

⁴² Now known as Frasers Group plc

⁴³ Press notice: [Sanctions against GT and a Partner](#)

⁴⁴ In November 2016 an investigation was opened in relation to the Statutory Audit of the financial statements of Sports Direct International plc for the 52 week period ended 24 April 2016 and in June 2019 a second investigation was opened in relation to the Statutory Audit of the consolidated financial statements of Sports Direct International plc for the 52-week period ended 29 April 2018. Under the AEP issued March 2021, a new investigation must be commenced if additional matters are identified outside the scope of the initial investigation. In this instance, matters in a later audit year were identified leading to a second investigation under the AEP.

Deloitte/Mitie Group plc/AEP⁴⁵

In November 2021, a Final Decision Notice was issued, and sanctions were imposed against Deloitte and a Partner in relation to the Statutory Audit of the financial statements of Mitie Group plc (Mitie), for the financial year ended 31 March 2016 (FY2016).

The breaches all concerned the audit of the impairment testing of goodwill in Mitie's Healthcare Division. The Respondents failed to obtain sufficient audit evidence to gain appropriate comfort regarding the future cashflows and the discount rate used in the impairment model, failed to give sufficient consideration to the impact of working capital, failed to exercise sufficient professional scepticism, failed adequately to document their audit work in relation to the discount rate, and allowed inadequate disclosures and incomplete statements to be included in the auditor's report. Due to the Respondents' breaches, the FY2016 financial statements contained a material uncorrected misstatement or misstatements in relation to the headroom and/or carrying amount of the Healthcare Division. If the Respondents had complied with the Relevant Requirements, goodwill in Mitie's Healthcare business might well have been treated as impaired as at the end of FY2016 and deficiencies in the disclosures about Healthcare goodwill would have been detected.

Deloitte received a financial sanction of £2.0 million (discounted for admissions and early disposal by 27.5% to £1.45 million), a Severe Reprimand, a declaration that the Audit Report did not satisfy the Relevant Requirements, and a requirement to report on the impact of remedial actions taken since 2016 to seek to improve the audit of goodwill.

The Partner received a financial sanction of £65,000 (adjusted by 15% for mitigation to reflect his constructive response to the AQR inspection and the investigation) and discounted for admissions and early disposal by 27.5% to £40,056, a Severe Reprimand, and a declaration that the Audit Report did not satisfy the Relevant Requirements.

⁴⁵ Press notice: [Sanctions against Deloitte LLP and a Partner](#)

KPMG/Conviviality plc/AEP⁴⁶

In December 2021, a Final Decision Notice was issued making findings of breaches of Relevant Requirements by KPMG and an Audit Engagement Partner in relation to the Statutory Audits of the financial statements of Conviviality plc for the 2017 and 2018 financial years.

In relation to the FY2017 Audit, the breaches related to multiple audit areas, including risk assessment, revenue recognition, the accounting treatment applied in respect of a contract for the supply of wine, capitalisation of costs and exceptional items, accrued supplier income, and goodwill. The breaches of auditing standards included the failures to revise the assessment of the risk of material misstatement due to management bias in light of information obtained in the audit process, to obtain sufficient appropriate audit evidence, to sufficiently apply professional scepticism, and to adequately document their audit work.

In relation to the FY2018 Audit, the breaches concerned the adequacy of documentation in relation to a decision to provide non-audit services to the audited entity during the period of the FY2018 audit in breach of the FRC's Revised Ethical Standard 2016.

KPMG received a financial sanction of £4.3 million (discounted for admissions and early disposal by 30% to £3.01 million), a Severe Reprimand, a declaration that the Audit report did not satisfy the audit reporting requirements for reasons set out in the Final Decision Notice, and a non-financial sanction requiring KPMG to report to the FRC identifying the causes of the deficiencies in the FY2017 Audit and the steps and remedial action which the firm has taken to prevent reoccurrence of those deficiencies.

The Audit Engagement Partner received a financial sanction of £110,000 (adjusted upwards by 5% for aggravating factors and then discounted for admissions and early disposal by 30% to £80,850) and a Severe Reprimand.

In June 2018, an investigation was opened in relation to the Statutory Audit of the consolidated financial statements of Conviviality plc for the 52 weeks ended 30 April 2017, and in January 2020 a second investigation was opened in relation to KPMG's engagement to conduct the Statutory Audit of the consolidated financial statements of Conviviality plc for the 52 weeks ended 29 April 2018. Under the AEP issued March 2021, a new investigation had to be commenced if additional matters are identified outside the scope of the initial investigation. In this instance, matters in a later audit year were identified, leading to a second investigation under the AEP.

This comprises two investigations.⁴⁷

⁴⁶ Press notice: [Sanctions against KPMG LLP and a Partner](#)

⁴⁷ In June 2018, an investigation was opened in relation to the Statutory Audit of the consolidated financial statements of Conviviality plc for the 52 weeks ended 30 April 2017, and in January 2020 a second investigation was opened in relation to KPMG's engagement to conduct the Statutory Audit of the consolidated financial statements of Conviviality plc for the 52 weeks ended 29 April 2018. Under the AEP issued March 2021, a new investigation had to be commenced if additional matters are identified outside the scope of the initial investigation. In this instance, matters in a later audit year were identified, leading to a second investigation under the AEP.

PwC/Kier/AEP⁴⁸

In December 2021, a Final Decision Notice was issued, and sanctions imposed against PwC and a former Partner in relation to the Statutory Audit of the financial statements of Kier Group plc (Kier), for the financial year ended 30 June 2017 (FY2017).

The Respondents admitted breaches of Relevant Requirements in relation to the audit of long-term contracts within Kier's Construction division. The breaches concerned audit work on recognition of variations and claims receivable, the proposed central profit override and forecast costs to complete. The Respondents also admitted a separate breach concerning their failure to identify errors in Kier's income and cash flow statements.

The breaches of Relevant Requirements reflected the Respondents' failure to obtain sufficient appropriate evidence, adequately determine whether Kier had appropriately applied the requirements of the applicable financial reporting framework, adequately test, or carry out substantive procedures in relation to, Kier's accounting estimates, prepare sufficient audit documentation to support conclusions reached, or exercise professional scepticism.

PwC received a financial sanction of £3.35 million (adjusted for admissions, early disposal and aggravating/mitigating factors, to £1.96 million), a Severe Reprimand; a declaration that the Audit Report did not satisfy the Relevant Requirements, and a requirement to evaluate and report to the FRC on certain audits conducted in 2022-2023 which feature long-term contacts and the impact of remedial actions put in place.

The Partner received a financial sanction of £90,000 (discounted for admissions, early disposal and mitigating factors to £52,650), a Severe Reprimand, and a declaration that the Audit Report did not satisfy the Relevant Requirements.

⁴⁸ Press notice: [Sanctions against PwC and Audit Partner](#)

KPMG/Rolls Royce Group plc/AEP⁴⁹

In December 2021, a Final Decision Notice was issued making findings of breaches of Relevant Requirements by KPMG and the Audit Partner in relation to the Statutory Audit of the consolidated financial statements of Rolls-Royce Group plc (the Company) for the financial year ended 31 December 2010.

The breaches relate to failures to address matters identified in the Audit which indicated risk of non-compliance by the Company with laws and regulations. The relevant compliance area - potential bribery and malpractice through the use of intermediaries and advisers in the defence field - was the subject of allegations which were prominent at the time of the Audit. The matters at issue in the Audit concerned two sets of payments made by the Company to an agent in India. These payments gave rise to allegations of bribery and corruption which later formed two (out of twelve) counts in a Deferred Prosecution Agreement with the Serious Fraud Office in 2017, under which the Company paid large fines. The breaches of the audit standards amounted to serious failures to exercise professional scepticism, to obtain sufficient, appropriate audit evidence and document this on the audit file, and to achieve sufficient Engagement Quality Control.

KPMG received a financial sanction of £4.5 million, discounted for admissions and early disposal by 25% to £3,375,000. The Audit Partner received a financial sanction of £150,000, discounted for admissions and early disposal by 25% to £112,500. Both KPMG and the Audit Partner also received the non-financial sanctions of a Severe Reprimand and a declaration that the Statutory Audit Report for the Audit did not satisfy the Relevant Requirements. Additionally, a non-financial sanction was imposed requiring KPMG to commission a review by an appropriate external independent expert of the effectiveness of the firm's policies, guidance and procedures for audit work in the area of an audited entity's compliance with laws and regulations.

⁴⁹ Press notice: [Sanctions against KPMG and a Partner](#)

KPMG/Revolution Bars Group plc/AEP⁵⁰

In December 2021, a Final Decision Notice was issued against KPMG and the Audit Engagement Partner⁵¹ following their admission of breaches of Relevant Requirements in relation to the Statutory Audits of the financial statements of Revolution Bars Group plc (RBG) for the 2015 and 2016 financial years.

The breaches concerned three specific audit areas: supplier rebates and listing fees, share-based payments, and (for FY2016 only) deferred taxation. The financial statements contained misstatements in respect of all three areas which had to be corrected, and some of these were material to the financial statements as a whole. Some breaches were of a basic or fundamental nature, including failures to exercise adequate professional scepticism, and persisted for two successive audit years.

KPMG and the Audit Engagement Partner received the following sanctions: financial sanctions of £1.25 million and £50,000 respectively (discounted to £875,000 and £35,000 respectively for admissions and early disposal), Severe Reprimands, a declaration that the 2015 and 2016 Statutory Audit Reports did not satisfy the Relevant Requirements, and a bespoke package of non-financial sanctions to mitigate the risk of repetition of the breaches.

KPMG is required to analyse the underlying causes of the breaches of relevant standards, and to identify and implement any remedial measures necessary to prevent a recurrence. The Audit Engagement Partner (who has moved to a new firm since the audits), is required to analyse his own involvement in the breaches, with the oversight of his new firm, and take forward any necessary remedial measures as part of his appraisal and personal development arrangements. KPMG and the Audit Engagement Partner are required to report to the FRC at each stage to demonstrate their compliance with these requirements.

⁵⁰ Press notice: [Sanctions against KPMG LLP and Audit Engagement Partner](#)

⁵¹ The individual performed the role of Audit Engagement Partner in respect of the audits on behalf of KPMG (but he was not a Partner in the firm).

PwC/Galliford Try/AEP⁵²

In March 2022, a Final Settlement Decision Notice was issued making findings of breaches of Relevant Requirements by PwC and the Audit Partner in relation to the statutory audits of the consolidated financial statements of Galliford Try plc (the Company) for the years ended 30 June 2018 (the 2018 Audit) and 30 June 2019 (the 2019 Audit and, together with the 2018 Audit, the Audits).

The breaches concerned the recognition of exposures relating to contract judgements on long term construction contracts for both audit years. When performing audit work on a number of the contracts, the Respondents failed to obtain sufficient appropriate audit evidence; perform adequate testing or carry out substantive procedures on the Company's accounting estimates; prepare sufficient audit documentation to support conclusions reached and carry out the audit with sufficient professional scepticism. Whilst breaches of Relevant Requirements were identified in several areas of the 2018 Audit, the breaches in the 2019 Audit were solely in relation to one construction contract.

PwC received a financial sanction of £5.5 million (discounted for cooperation, admissions and early disposal to £3,038,750); a Severe Reprimand and a declaration that the Statutory Audit Reports for FY2018 and FY2019 did not satisfy the Relevant Requirements. The Audit Partner received a financial sanction of £150,000 (discounted for cooperation, admissions and early disposal to £82,875); a Severe Reprimand and a declaration that the Statutory Audit Reports for FY2018 and FY2019 did not satisfy the Relevant Requirements.

⁵² Press notice: [Sanctions against PwC and Audit Partner](#)

Closed cases

Two investigations under the Accountancy Scheme and one investigation under the AEP were closed without enforcement action. In all three cases, the evidence did not support findings of Misconduct or breaches of Relevant Requirements.

Ongoing cases as at 31 March 2022

As at 31 March 2022, there were 47 open investigations:⁵³ 38 investigations into individuals and firms for audit work, one investigation into individuals and firms for non-audit work, and eight investigations into professional accountants working in business. This is marginally lower than the number of cases open at 31 March 2021 (49 investigations).

Of the 38 audit investigations, one is being investigated under the Accountancy Scheme and the remaining 37 under the AEP. The AEP investigations include three which had been delegated by the Conduct Committee to the ICAEW to conduct the investigation. All three cases have been remitted back to the Enforcement Division for decision by Executive Counsel in light of the findings of the ICAEW's investigations.

Of the 38 audit investigations under the AEP and Accountancy Scheme, 28 have been announced and are included in Appendix B. The 38 audit investigations collectively concern a wide range of areas of the audit, including:

Investigation issues	
Goodwill	Lack of professional scepticism
Going concern	Compliance with ethical requirements
Pensions	Related Party transactions
Inventory valuation and provisions	Compliance with laws and regulations
Presentation and disclosure	Control environment
Costs and liabilities	Reverse factoring
Cash	Investments and financial assets
Other fixed asset impairments	Reserves
Onerous contracts and leases	Setting of materiality levels
Provisions	Recoverability of loans
Audit documentation	Group audits, including oversight of component auditors
Integrity and objectivity	Fraud
Revenue recognition, including long-term contract accounting	Non-audit work

⁵³ An investigation will comprise one of the following: (1) an audit investigation into an audit firm and audit partner(s) (under the Accountancy Scheme or the AEP); (2) an investigation into professional accountant(s) working in business (under the Accountancy Scheme); (3) a non-audit investigation into professional accountant(s) and accountancy firms (under the Accountancy Scheme); or (4) an investigation into actuaries (under the Actuarial Scheme). Each investigation may include multiple subjects, and an investigation is not deemed to be closed until concluded against all subjects.

All open investigations in relation to members who are professional accountants working in business are linked to audit investigations (some current; others concluded) and therefore concern many of the same issues. Of the eight investigations, six have been announced, and can be found in Appendix C.

The investigation into individuals and firms for non-audit work has been announced and relates to the KPMG/AQR Tribunal hearing described below.

Tribunal hearings

Silentnight

On 13 October 2021, the FRC published the Independent Tribunal's report in respect of the Formal Complaint against a former KPMG Partner and Head of KPMG Manchester Restructuring and KPMG, relating to their restructuring work for the Silentnight group of companies. The Tribunal found two allegations of Misconduct proven. First, that in breach of the Fundamental Principle of Objectivity (contained in the ICAEW Code of Ethics), the Partner advised and/or assisted both Silentnight and HIG in relation to a proposed acquisition of Silentnight by HIG at a time when there was a conflict of interest between the interests of Silentnight and HIG, and, as a result, the Respondents' judgement was compromised and objectivity impaired. Secondly, the Partner dishonestly advanced and associated himself with untrue and misleading and/or materially incomplete statements to the Pension Protection Fund (PPF), The Pensions Regulator (tPR), Silentnight and the Trustees of the Silentnight Pension Scheme as to the causes of Silentnight's difficulties in order to assist HIG in its efforts to enable Silentnight to shed its liability under the Pension Scheme as cheaply as possible. The Tribunal ordered sanctions including a 13-year exclusion for the Partner and a £13 million fine for KPMG (being the record non-audit fine). Further detail of the Misconduct and the sanctions imposed can be found on page 86 and in the Tribunal Report.⁵⁴

KPMG/AQR

The hearing of the Formal Complaint under the Accountancy Scheme against KPMG, a former KPMG Partner, and five former KPMG employees, took place over a four-week period in January and February 2022.

The Formal Complaint alleged Misconduct against KPMG and several individual Respondents regarding the provision of allegedly false and misleading information and/or documents to the FRC in connection with the FRC's AQR inspections of two audits carried out by KPMG: the audit of the financial



Breach of objectivity and acting with dishonesty



Provision of false and misleading information

⁵⁴ Report of the Disciplinary Tribunal in Silentnight

statements of Carillion plc for the period ended 31 December 2016 and the audit of the financial statements of Regeneris plc for the period ended 30 June 2014. The FRC agreed terms of settlement with KPMG and another former employee following their admissions of Misconduct in relation to the AQR inspection of the audit of the financial statements of Regeneris plc. The allegations in the Formal Complaint were made against each of the individuals only in respect of their own conduct and did not suggest that any individual was responsible for the Misconduct of any of the other individuals subject to the Formal Complaint.

The Formal Complaint did not allege Misconduct in the performance of the relevant audits, nor did it allege that in either case the financial statements had not been properly prepared. The audit, and preparation, of the 2016 Carillion financial statements are the subject of separate investigations.

Spotlight on responding to regulatory action – the Silentnight case

In deciding what sanctions to impose, the Tribunal made important findings as to the behaviour expected by Members and Member Firms facing regulatory action by Executive Counsel. Regrettably, there were a number of serious failings by KPMG and a former Partner in this regard.

Failure to cooperate

The 2020/21 AER spotlighted the concept of cooperation and its importance in the context of investigations, enforcement action and sanction. The Tribunal made significant findings against KPMG and the former Partner in respect of their failure to cooperate.

Paragraph 14 of the FRC Accountancy Scheme requires that every Member, and Member Firm, shall at all times cooperate fully with the Executive Counsel and with any Tribunal appointed pursuant to the Scheme. Furthermore, such cooperation includes, but is not limited to complying with any notice served by Executive Counsel under paragraph 14(2) of the Accountancy Scheme. Paragraph 14(2) notices are used by Executive Counsel during investigations to obtain information and documentation.

A Respondent having 'failed to cooperate with, or hindered, the investigation' is listed as an example of behaviour that may aggravate the Misconduct, and so should be taken into account when deciding the sanction or combination of sanctions to be imposed. Non-exhaustive examples provided in the Sanctions Guidance include:



The Tribunal made significant findings in respect of failure to cooperate

-
- (a) incomplete provision of documents and information in response to Notices and requests;
 - (b) failure to provide adequate explanation of information provided; and
 - (c) failure to conduct an adequate search for documents and information.

Whether or not a specific failure is sufficiently significant to aggravate sanctions will be fact-specific and require a consideration of the circumstances surrounding the reasons for non-compliance.

At the hearing to determine sanctions to be imposed on the Respondents, Executive Counsel argued that the Respondents had not provided the level of cooperation required, and relied on various failures by the Respondents:

- The failure to provide information to Executive Counsel during a presentation at the outset of the investigation. Specifically: (i) the informal retainer of KPMG by Silentnight during which some £45,000 of time costs were incurred prior to KPMG being formally engaged; and (ii) the nature of the advice given to HIG in this period, which involved the giving of substantive advice to both HIG and Silentnight.
- The failure to reveal to Executive Counsel that a crucial note of a meeting on 16 August 2010 was created some 13 months after the event, specifically in response to the Pensions Regulator's investigation into the facts. The full picture as to how the note was created emerged in cross-examination of the Partner, and his witness statements did not refer to the fact that the note was not produced contemporaneously.
- The failure to conduct an electronic search for emails sent by the Partner using his personal email address, despite two specific requests from Executive Counsel pursuant to paragraph 14(2) Notices. KPMG had merely relied on the Partner's recollection of whether he had used personal email over nine years earlier. This failure meant Executive Counsel may have lost the opportunity to follow up lines of enquiry because, in the intervening period, the Partner's personal emails, which had not been copied to the KPMG email server, would have been deleted. The Tribunal held that, *"The failure to carry out comprehensive searches in response to the specific requests by the Executive Counsel is a serious matter"*.

Full cooperation with Executive Counsel's requests is a minimum requirement under the AEP and Schemes. As this case shows, Executive Counsel takes a robust approach to parties who do not provide the level of cooperation required, and will call out and pursue such behaviour where it occurs.



Untruthful defence

Untruthful defence

For the first time, the Tribunal held that a Respondent advanced a defence that was in part untruthful. Respondents are entitled to defend proceedings honestly and robustly if they wish, and the fact that a Tribunal ultimately disagrees with that defence is not of itself a matter of criticism. However, advancing a defence which a Respondent knows is untruthful seriously risks undermining the regulatory system, compounds the original failings and should be treated as an aggravating factor to sanctions.

The Tribunal held that the contemporary documentation created in the period before HIG's purchase of Silentnight's bank debt (the 'Debt Sale') contained no indication that there was, or that Silentnight, the Partner or HIG considered that there was, a burning platform (a term of art used to describe a situation where a company faces the risk of imminent insolvency). To the contrary, the Partner had stated to his colleagues in a May 2011 email that the Debt Sale would be of interest to the Pensions Regulator as it created the burning platform.

Notwithstanding, a central plank of the Respondents' defence was the claim that Silentnight faced a 'burning platform' prior to the Debt Sale.

Not only did the Tribunal find that the Respondents' defence was wrong on this issue, it held that the Partner did not believe it was true.

The Tribunal stated:

As to the nature of the defence advanced by [the Partner] it was untruthful in that he did not believe that there was a burning platform throughout the material period and was aware that the burning platform was created by the withdrawal of the overdraft facility in the context of the Debt Sale Agreement. Had he admitted that the only burning platform was that created as a result of HIG acquiring the Silentnight debt the course of the hearing might have been very different.

And

[T]he defence put forward by [the Partner] in relation to the burning platform was a construct invented by him to assist in his defence.

Failure of Senior Management to respond to criticism

Before the opening of Executive Counsel's investigation, KPMG and the Partner received the Pension Regulator's First Warning Notice dated 11 December 2014, which contained serious criticism of the Partner's conduct in providing advice to HIG:

[The Partner] provided advice to HIG in relation to its acquisition of the Silentnight Business. ... Despite the obvious conflict of interest ... so far as the Regulator is aware none of [the Partner], anyone else at KPMG ... or anyone else at HIG, ever decided that KPMG could not and/or should not provide advice to HIG and the Silentnight Group at the same time. HIG used this situation to its advantage.

The FRC Tribunal held that, "Such strong criticism from a public regulator should have prompted a thorough investigation of [the Partner]'s conduct and of KPMG's systems, process and controls. There is no suggestion that KPMG took such steps."

Executive Counsel expects that in such cases, criticism by a regulator should prompt a significant evaluation by senior management of the firm's (and its employees') conduct, and if appropriate, self-reporting of any misconduct or breaches of relevant requirements.



Strong regulatory criticism by a regulator should prompt a significant evaluation of conduct

6 Sanctions

Introduction

The imposition of effective, proportionate and dissuasive sanctions where breaches or Misconduct are found to have occurred remains a central element of our process. In this section we consider the overall level of sanctions imposed during the year, before looking in more detail at sanctions in individual cases and drawing out features we consider may be of particular interest or of broader application. Sanctions continue to be imposed in accordance with our published Sanctions Policy and Guidance.⁵⁵

Sanctions

It will be seen from the table below that the number of both financial⁵⁶ and non-financial sanctions increased significantly from the previous two years. This reflects both the increased number of cases which arose for sanctioning purposes and the level of seriousness of some of those cases. In terms of quantity, during 2021/22, sanctions were imposed in fourteen concluded cases: twelve relating to audit matters, one relating to the preparation and review of financial information by a Member and one relating to work undertaken by an accountancy firm's restructuring division. In one case ongoing against others at 31 March 2022, sanctions were imposed on an Audit Engagement Partner⁵⁷ in respect of their engagement with the FRC's AQR team.

As for gravity, there were a number of serious matters which fell to be sanctioned this year, including the audits of Patisserie Holdings, Stagecoach, Conviviality, Rolls Royce, Galliford Try and the non-audit case of Silentnight. The £13 million fine imposed by the Tribunal in the latter case represented a sizeable proportion of the total financial sanction figure for the year, both before and after the application of settlement discounts (£46.5 million and £34.6 million, respectively). It represents the largest financial sanction imposed in a non-audit matter to date.

The overall level of financial sanctions both pre- and post-discount (£46.5 and £34.6 million, respectively) is close to 2018/19 (£42.9 and £32.0 million), a year in which there was a similar number of cases (12 matters closed, with findings of Misconduct/breaches and sanctions). Interestingly, however, there were significantly more non-financial sanctions imposed in the year compared to 2018/19 (62 as against 38), reflecting our continued focus on such sanctions since the Clarke Review⁵⁸ and our ongoing commitment to formulating sanctions designed to secure the quality of future audits.

⁵⁵ Links to the sanctions policies are here: [Sanctions Policy \(Audit Enforcement Procedure\) \(effective from January 2022\)](#); [Accountancy Scheme Sanctions Guidance \(March 2021\)](#); [Actuarial Scheme Sanctions Guidance \(March 2021\)](#)

⁵⁶ The proceeds of financial sanctions imposed in AEP matters are remitted to the government, while in cases under the Schemes the proceeds of such sanctions are remitted to the professional body of the firm or individual which has been sanctioned, in accordance with the contractual arrangements by which the Schemes operate.

⁵⁷ The individual performed the role of Audit Engagement Partner in respect of the audit (but he was not a Partner in the firm).

⁵⁸ [The report of an independent review into the FRC's enforcement sanctions chaired by former Court of Appeal Judge Sir Christopher Clarke](#)



Financial and non-financial sanctions have increased significantly from the previous two years

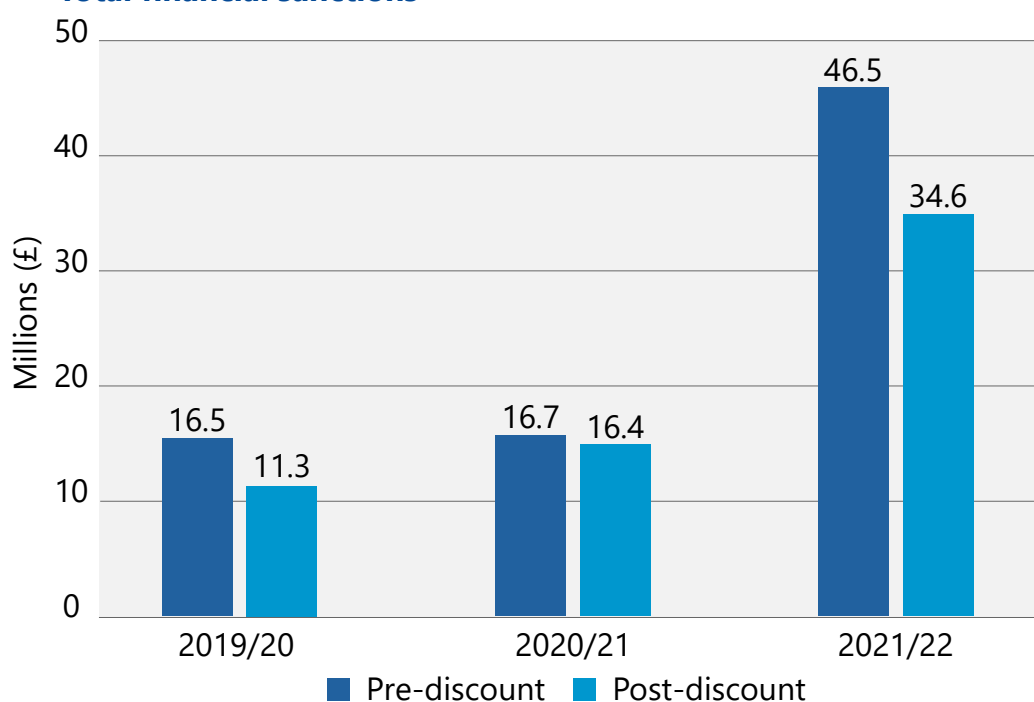
The level of discounts awarded in accordance with the Sanctions Policy and Guidance, ranged from 25% to 45%,⁵⁹ reflecting the varying degrees of cooperation exhibited, and timing of admissions made, by firms in cases which were settled.

	2019/20	2020/21	2021/22
Total financial sanctions imposed:			
Pre-discount	£16.5m	£16.7m	£46.5m
Post-discount	£11.3m	£16.4m	£34.6m
Number of financial sanctions imposed	11	8	25
Number of non-financial sanctions imposed	27	28	62
<i>Of which:</i>			
Exclusions	-	1	5
Requirements and undertakings	10	11	15



Sanctions imposed of **£46.5m** (£34.6m after settlement discounts)

Total financial sanctions



Financial sanctions against audit firms

Eleven financial sanctions were imposed on audit firms during the year in respect of 12 cases, totalling £31.8 million prior to the application of any settlement discount.⁶⁰ All financial sanctions imposed on audit firms in respect of audit matters in the year were under the AEP. While this year's review reveals the increasing emphasis we place on non-financial sanctions, they should not be seen as a replacement for financial sanctions, which continue to play an important role, both to mark the seriousness of the failures in question and in acting as a potentially powerful deterrent.

⁵⁹ The maximum adjustment awarded for mitigation was 15%, and the maximum discount for admissions and early disposal was 35%. As the discount is applied to the adjusted figure, the total discount in these cases amounts to 45%.

⁶⁰ Extensions to existing cases in the AEP in effect in 2021 were counted as new cases, as the AEP did not make provision for amendments to scope. In 2021/22, one set of sanctions was imposed in relation to two AEP cases, where the two cases were in respect of the Statutory Audit of the financial statements for different financial years of the same entity.



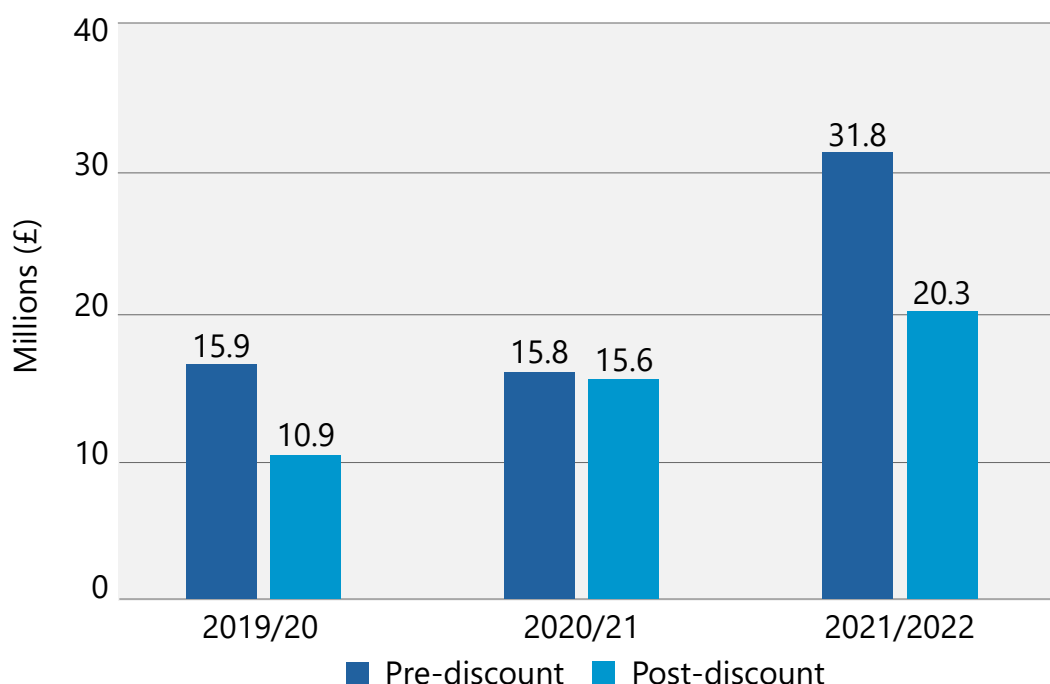
Financial sanctions mark the seriousness of the failures

At £4.0 million, reduced to £2.34 million after settlement discount, one of the highest financial sanctions imposed in the year was on GT in relation to its audit of Patisserie Holdings. As outlined elsewhere in the report, the audit failings identified were significant as they revealed, among other things, a pattern of serious lapses of professional judgement and failures to exercise professional scepticism across four audit areas over three consecutive years. This case is worthy of note in this context as it draws out a number of key themes in our approach to sanctioning, namely, that we:

- (i) are proportionate and take into account the size and financial strength of a firm;
- (ii) accord due weight to cooperation and recognition of failures (in this case an overall 42% discount was awarded to take into account of such factors); and
- (iii) formulate bespoke non-financial sanctions carefully tailored to the facts of the case, which in this instance included reporting to the FRC annually for three years on the impact of the firm’s remedial actions (including a root cause analysis) on audit quality, a review of the audit practice’s culture relating to challenge, and additional monitoring in relation to bank and cash audit work.

Other serious cases resolved with substantial financial sanctions during the year include PwC’s audits of Galliford Try (£5.5 million reduced to £3.04 million after settlement discount and mitigating factors), KPMG’s audits of Rolls Royce (£4.5 million reduced to £3.375 million after settlement discount) and Conviviality (£4.3 million, reduced to £3.01 million after settlement discount) and EY’s audit of Stagecoach (£3.5 million, reduced to £2.205 million after settlement discount and mitigating factors).

Financial sanctions - audit firms



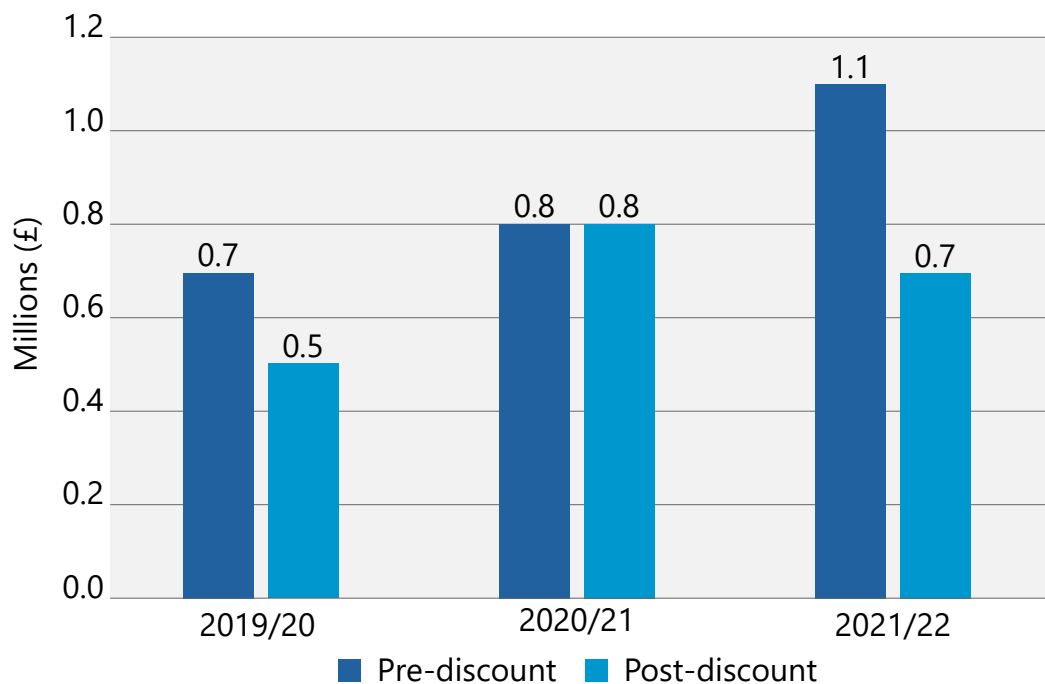
£31.8m
financial
sanctions
imposed on
audit firms

	2019/20	2020/21	2021/22
Number of financial sanctions against audit firms	5	4	11

Financial sanctions against audit partners

The total amount of financial sanctions on audit partners was £1.1 million prior to the application of any settlement discount.

Financial sanctions - audit partners



The financial sanctions imposed take into account a number of factors, including the seriousness of the breaches as well as the financial resources of the Partner.

	2019/20	2020/21	2021/22
Number of financial sanctions against audit partners	6	3	11

Sanctions against firms and accountants in respect of non-audit matters

As noted above, the largest financial sanction of the year by some margin was imposed in the matter of Silentnight, in which KPMG acted as a restructuring advisor and which, as a non-audit matter, was dealt with under the Accountancy Scheme.

The details of this case are set out extensively in other parts of this review but for present purposes it is sufficient to note that the Tribunal considered that the gravity of the Misconduct was at the highest end of seriousness and included both a lack of integrity and a loss of objectivity. In considering the 'starting point' level of financial sanction, the Tribunal referred to the passage of the Clarke Review which indicated that a starting figure of £10 million would be appropriate where one of the Big 4 firms was guilty of seriously bad incompetence in respect of a major public company, the errors were measured in nine figures or more with resultant widespread loss, and that these figures could increase if there was conscious wrongdoing or dishonesty. In deciding on a starting figure of £13 million, the Tribunal noted the facts of the case merited an increase from £10 million and observed: "*[W]e take on board that Silentnight was not a major public company, it was a substantial company nonetheless, and the actions risked causing serious harm to a substantial group of people and risked damaging the accountancy profession.*" The Tribunal went on to find that there were a number of aggravating factors, including a lack of cooperation, the advancing of a defence that was in part untruthful, and a failure of senior management to respond to regulatory criticism. The Tribunal concluded that no uplift was required to reflect these matters given the level of the starting figure.

The case is also notable for its comprehensive and bespoke suite of non-financial sanctions, with KPMG required to appoint an independent reviewer to conduct a root cause review and to conduct a review of relevant policies, procedures and training programmes relating to various of KPMG's advisory services practices in the light of the results of the root cause review.

Two individuals were also subject to sanctions imposed in relation to non-audit matters. This included the Partner in the Silentnight matter, who received a financial sanction of £500,000, with the Tribunal noting that he was the person primarily and directly responsible for the matters giving rise to what they had found to be very serious Misconduct. In addition, the Partner was excluded from the ICAEW for 13 years and precluded from holding an insolvency licence for the same period.

The other matter related to the conduct of an Audit Engagement Partner⁶¹ who made, or was responsible for, representations to the FRC's AQR inspectors which were misleading, and was reckless as to whether those representations were misleading and whether the inspectors would be misled by them. The individual admitted Misconduct and that his actions breached the ICAEW's Code of Ethics Fundamental Principle of Integrity. A financial sanction of £150,000 was imposed, as well as exclusion from the ICAEW for a recommended period of three years.

No financial sanctions were imposed on members who are actuaries in the year to 31 March 2022.

⁶¹ The individual performed the role of Audit Engagement Partner in respect of the audits on behalf of KPMG (but he was not a Partner in the firm).

Non-financial sanctions

As mentioned above, non-financial sanctions have played an increasingly central role in our sanctioning regime as we continue to focus on improving the quality of financial reporting and audits. As well as the imposition of Severe Reprimands and declarations that audit reports did not satisfy certain Relevant Requirements, non-financial sanctions published in the year include:

- a requirement for EY to report to the FRC for the period of one year in respect of audit work performed in relation to onerous contract provisions;
- an order to appoint an independent reviewer to conduct a root cause review to establish why threats to compliance with the fundamental principle of objectivity were not appropriately identified and safeguarded in the period prior to the appointment of office holders in the Silentnight matter; and, in a sample of past cases, whether threats to compliance with the fundamental principle of objectivity were appropriately identified and safeguarded in the period prior to the appointment of office holders and, if not, the reasons for such failures; and conduct a review of various policies, procedures and training programmes relating to various of KPMG's advisory services practices in the light of the results of the root cause review;
- exclusion from membership of the ICAEW for 13 years;
- preclusion from holding an insolvency licence for 13 years;
- reporting to the FRC annually for three years on the impact of GT's remedial actions (including a root cause analysis) on audit quality;
- a review of GT's audit practice's culture relating to challenge;
- monitoring in relation to GT's bank and cash audit work;
- a requirement for GT to report to the FRC on its monitoring programme of the quality of audit work on loss-making contracts;
- a requirement for GT to report to the FRC on whether changes made to its audit methodology are resulting in a better exercise and documentation of an audit team's judgement regarding key audit matters;
- a requirement for GT to undertake thematic reviews and report to the FRC as to the efficacy of enhancements it has introduced regarding the audit of inventory provisions of retail entities and the use of audit data analytics to audit revenue;
- a requirement that Deloitte review the root cause analysis (RCA) previously prepared for the FY2016 Audit, extend that RCA to address any further issues that arise out of the breaches set out in this Final Decision Notice (Extended RCA) and provide the RCA and Extended RCA to Executive Counsel and the FRC Deloitte Supervisor within 120 days of the date of the Final Decision Notice;

- a requirement to report to the FRC on the impact of remedial actions taken by Deloitte since 2016 on audits of goodwill;
- a requirement for KPMG to report to the FRC identifying the causes of the deficiencies in the 2017 Audit and the steps and remedial action which the firm has taken to prevent to reoccurrence of those deficiencies;
- a requirement for PwC to evaluate and report to the FRC on certain audits conducted in 2022-2023 which feature long-term contacts and the impact of remedial actions put in place;
- a requirement that KPMG shall commission a review by an appropriate external independent expert of the effectiveness of the firm's policies, guidance and procedures for audit work in the area of an audited entity's compliance with laws and regulations;
- a requirement for KPMG to analyse the underlying causes of the breaches of relevant standards, to identify and implement any remedial measures necessary to prevent a recurrence, and to report to the FRC at each stage of the process;
- a requirement for an Audit Engagement Partner, who moved to another firm in 2017, to analyse the underlying causes of his role in the breaches of relevant standards, to identify and implement any necessary remedial measures as part of his appraisal and personal development arrangements, and to report to the FRC at each stage of the process.

It will be apparent from the broad range of sanctions set out above that they are carefully tailored to the facts giving rise to the failures identified in any given case. However, it is possible to draw out some overriding themes which demonstrate matters we consider to be of key importance:

- (i) detailed work to understand the underlying causes of the deficiencies which gave rise to the Misconduct/breaches. This may be in relation to a particular audit or in appropriate cases may require a broader review where there is a concern that deficiencies may be more widespread or relate to systemic and/or ISQC1 issues;
- (ii) concrete and specific remedial measures to prevent recurrence;
- (iii) an effective mechanism or framework for measuring the impact of the required remedial work; and
- (iv) detailed reporting to the FRC on the remedial measures and their impact by reference to clear performance indicators.



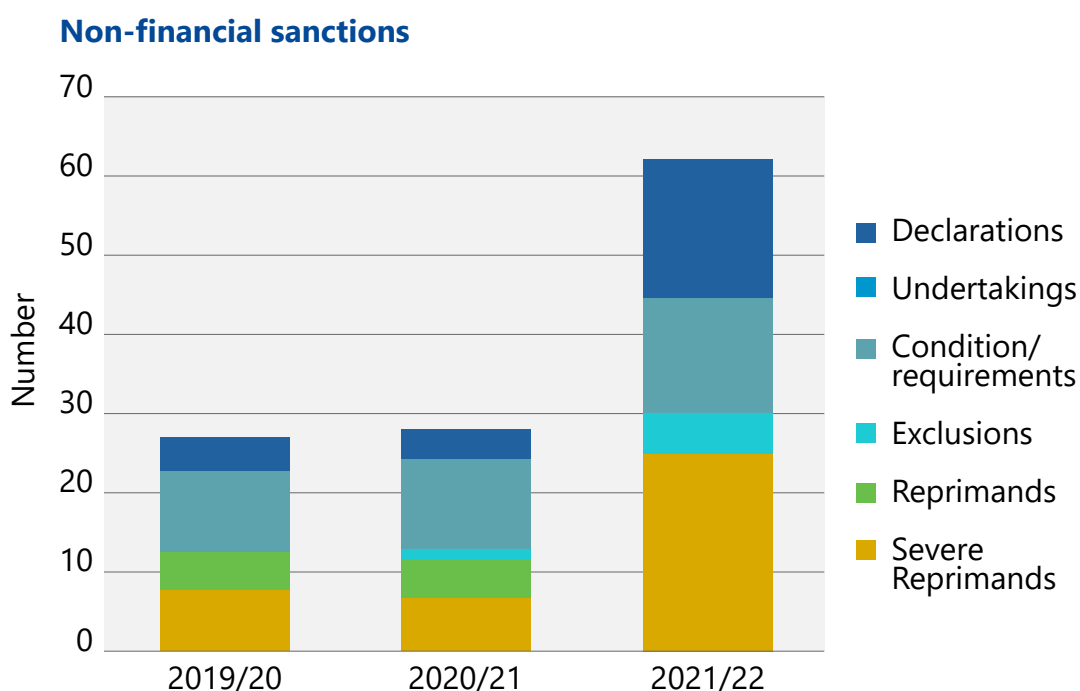
Non financial sanctions are tailored to the facts giving rise to the failures

In relation to the latter, in many cases there are no quick-fix overnight solutions, and it may be necessary for firms to report to us over a number of years. We consider these reports carefully in conjunction with the dedicated Audit Firm Supervisor within the Audit Firm Supervision team. By way of example, in March 2022, GT provided their second of three annual reports in relation to the measures they have taken to address a 2020 case outcome which identified failures in their policies, procedures and systems governing ethical matters.⁶² The report reveals the tangible progress which has been made, including a substantial increase in the size and capability of the firm's ethics function.

The table below illustrates the increasing use of non-financial sanctions as discussed in this section, and the chart below provides an at-a-glance analysis of the composition of such sanctions in this and the preceding two years.

Number of non-financial sanctions

	2019/20	2020/21	2021/22
Severe reprimands	8	7	25
Reprimands	4	4	–
Exclusions	–	1	5
Conditions/requirements	10	12	15
Undertakings	–	–	–
Declarations	5	4	17
Total	27	28	62



62 It should be noted that the failures related to the period 1 April 2014 to 31 March 2017.

7 Timeliness

We continue to recognise the importance of timely investigative and enforcement action and it remains a key priority for the Division. While the pandemic has posed ongoing operating difficulties for us as well as for many others, we were nevertheless able to increase the size of the team by 23% during the year, underscoring our longer-term commitment to securing improvements in this area. In this section, as in previous years, we report on our performance by reference to both our established KPI – a period of two years between commencement of an investigation and service of either the Proposed Formal Complaint (PFC) or Investigation Report (IR)⁶³ (or closure or settlement if sooner) – and other relevant case length data.

Time to service of PFC, IR or settlement or closure (if earlier)

As explained in previous years, the KPI relates to the investigation stage of our process, as in later phases the timetable will largely be set by others (e.g. Tribunal Chair) and is therefore not within the control of Executive Counsel.⁶⁴

KPI Measurement

Our reporting to date on the two-year KPI target has captured those cases where the KPI was achieved in the reporting year, together with those cases where the KPI fell due in the reporting year and has not yet been met (the historical KPI measure). Cases which met the KPI in an earlier reporting year than it was due have been reported in the year the KPI was met.

We continue to reflect on the appropriate KPI measurement and this year we also report on the KPI based on all cases where the two-year KPI date fell due in the reporting year, whether the KPI was achieved in year or earlier, or not yet met (the comparative KPI measure).

Historical KPI measure

Six cases in which the two-year KPI fell due in the year to March 2022 met their KPI early and have been excluded from the KPI reporting for cases meeting a KPI in 2021/22.

Ten enforcement cases fell to be measured against the historical KPI⁶⁵ and the table below sets out our performance against this measure.

⁶³ Since the revised AEP came into force on 5 January 2022, the Initial Investigation Report (IIR) is now known as the Investigation report (IR).

⁶⁴ It should be noted that guidance has been issued to Tribunals that matters should progress as expeditiously as possible.

⁶⁵ i.e. those that either met the KPI, or exceeded 24 months without meeting the KPI, within the year.

	Number of cases
PFC/IR served (or case concluded without PFC/IR) within two years	4
PFC/IR not served/case not otherwise concluded within two years due to:	
Size/complexity	3
Priority given to settlement discussions	1
Lack of internal resource	1
Satellite FRC legal proceedings	1
Total	10

The target has therefore been met in 40% of cases, which, despite the cumulative impact of the pandemic, is the same percentage as last year.

Where we did not meet the KPI, the reasons were as follows:

- In three cases, the exceptional size and complexity of the matters investigated, which spanned multiple audit years, meant that it was not possible to achieve the KPI. Two of these investigations were into audits of the same entity but in relation to different audit years, with the subsequent opening of the investigation into the second audit year inevitably impacting on the time required to conclude the first.
- As noted in previous years, where we are in settlement discussions at the date of the KPI, we assess whether the public interest appears more likely to be served by continuing those discussions or by serving an IR or sometimes both. Settlement discussions in one case this year were given priority over service of an IR.
- In one case, the impact of the pandemic delayed the recruitment of additional forensic accounting resource at the early stages of the investigation. This resulted in an early delay which could not be recovered in terms of the KPI.
- It was necessary to pause our substantive process in one matter pending resolution of satellite litigation proceedings relating to an audited entity's compliance with a statutory notice requiring production of documents issued pursuant to the terms of the AEP and SATCAR.

Comparative KPI measure

Using the comparative KPI measure, the KPI was met in 8 of the 14 cases where the KPI fell due in the year to March 2022. On this measure, the KPI was met in 57% of cases, which is a 10-percentage point improvement over the previous year and a 36-percentage point improvement over the year before.



The historical KPI target was met in **40%** of cases



The comparative KPI target was met in **57%** of cases

The table below sets out our performance over the last three years, assessed against both the historical and comparative measurements.

	2019/20	2020/21	2021/22
Historical KPI			
Number of cases meeting KPI based on completion date ⁶⁶	44%	40%	40%
Comparative KPI			
Number of cases meeting KPI based on KPI due date ⁶⁷	21%	47%	57%

Over the longer term the comparative KPI may provide a clearer indication of progress, as it focuses on the set of cases within the relevant two-year period at the given reporting date. It is therefore encouraging that a broad trend of improvement is emerging on this basis.

It should be noted that the achievability of the KPI can be impacted by external factors outside our control, including aspects of our procedural framework. For example, prior to changes made to the AEP in January 2022, where an investigation was extended to add further audit years, the extension was treated as a 'new' investigation with the clock accordingly restarting for the purposes of measuring performance against the KPI for the investigation into the further audit year. If that new case benefited from investigation work already conducted, the prospects of achieving the KPI were improved. Following recent changes to the AEP, however, which provide for the extension of investigations, the clock will continue to run from the outset of the initial investigation. This will impact on our ability to continue to report on a like-for-like basis and make it more difficult for the extended investigation to meet the original KPI. In light of this, and other such factors outside our control, in the coming year we will review our target KPI with a view to identifying a metric which provides more meaningful and richer insight into our performance while maintaining our emphasis on securing improvements to the timeliness of our investigations and enforcement action.

Average time to service of PFC, IR or settlement (if earlier)

The average length of time to service of PFC/IR (or settlement, if earlier) in cases reaching this milestone during the year is set out below. It will be noted that there has been an increase in average time to issuance of PFC, IR or settlement in this reporting year, and this is largely attributable to three legacy⁶⁸ investigations, two of which were settled prior to issuance of the PFC/IR. Of these two, one investigation was the Sports Direct investigation opened in November 2016 (delayed by parallel litigation) and one unannounced case was opened in 2017. In the third legacy case a PFC was served after a delay caused by related proceedings. Without these three legacy cases the average would have been 27 months.

⁶⁶ Those that either met the KPI, or exceeded 24 months without meeting the KPI, within the year.

⁶⁷ Those where KPI fell due within the year.

⁶⁸ Legacy cases are cases opened prior to 31 March 2018.

	2019/20	2020/21	2021/22
Number of cases where PFC/IR issued (or settled/closed, if earlier)	16	13	14
Average length of time to issuance of PFC/IR (or settlement/closure, if earlier) (in months)	23	26	33

Time to complete a case

The table below sets out average case lengths of those matters that concluded this year and in the previous two years.

	2019/20	2020/21	2021/22
Average length of cases referred to Tribunal (months)	48	91	68
(No. of cases)	(1)	(1)	(1)
Average length of cases concluded as a result of settlement or service of undisputed Decision Notice (months)	23	31	39
(No. of cases)	(8)	(6)	(13)
Average length of cases closed with no further action (months)	20	31	26
(No. of cases)	(4)	(3)	(3)

As in previous years, the relatively small number of cases from which the figures are derived means it is necessary to be cautious when attempting to identify meaningful patterns or trends. The single case referred to the Tribunal that concluded this year was Silentnight. The second row of the table includes the settlement of four cases with a date of opening prior to 31 March 2018, which, while pushing up the average length of matters in this category, represents encouraging progress in dealing with such legacy cases during the reporting year. It is also positive to note that 7 of the 13 cases reaching settlement during the reporting year did so within three years of opening.



13
cases reaching settlement during the reporting year did so within three years of opening

Average age of cases open at year end

The table below sets out the average age and volume of cases that remain open at the year end, over the last three years. It can be seen that the average age of cases open at year end has remained broadly stable.

	2019/20	2020/21	2021/22
No. of cases open at year end	41	42	49
No. of cases opened in year	15	14	16
Average age of cases open at year end (in months)	20.9	25.4	25.4

The table below sets out data relating to the age profile of our cases at year end compared with year end last year.

We closed five legacy cases during the year, with a case open date prior to 31 March 2018. Seven legacy cases remain open; in four we were required to pause our process pending resolution of parallel criminal or other proceedings, two cases are connected to the large and complex Carillion investigations, and the remaining matter is also a sizeable investigation.

Year investigation opened (to 31 March)	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Total
Cases open at 1 April 2021 ⁶⁹	1	–	–	2	3	6	12	9	16	–	49
Cases closed in year	–	–	–	1	1	3	7	3	2	–	17
Cases open at 31 March 2022	1	–	–	1	2	3	5	6	14	15	47



We closed five legacy cases during the year

⁶⁹ Cases open at 31 March 2021 have been restated since the Annual Enforcement Review 2021. One case concluded prior to 31 March 2021 had been reported as a case that had opened in the year to 31 March 2019 whereas it had opened in the year to 31 March 2018.

8 Looking to the Future

Introduction

Last year this section of the review considered how Covid-19, Brexit and climate change would affect audit and our stakeholders.

Over the last year, many organisations have moved to various forms of hybrid-working, with people working both from home and in the office. This has created new challenges for firms and companies adapting to this altered landscape, and whilst the situation continues to evolve it is likely that some change from full-time office working will be permanent.

Government support provided during the pandemic, including furlough payments, grants and business loans, has largely ceased and the future for certain businesses that relied on this support is uncertain. The impact of inflation driven by increasing prices, particularly in the energy sector, and likely to be exacerbated by the geopolitical situation, will affect every business to a greater or lesser degree.

In this economic environment, preparation of financial statements and clarity of disclosure, particularly in relation to the assessment of the going concern assumption, and judgements and estimates will continue to be challenging. In addition, the pressures on management will mean that auditors need to be alert to greater risks to management's integrity and objectivity.

As mentioned by Executive Counsel in her introduction, as part of our holistic regulatory approach, we shall be paying particular attention to deficiencies in areas where other parts of the FRC have issued commentary and guidance, examples of which include:

- AQR's [What Makes a Good Audit](#) sets out good practice and examples of both good and poor practice seen in their reviews.
- AQR's [Key Findings Reported in the 2020/21 Inspection Cycle](#) identified multiple findings in these areas of audits: Credit risk and expected credit losses, going concern, goodwill and intangible asset impairment, group oversight, quality control and revenue.
- CRR's [Reviews of Corporate Reporting](#) also noted findings in these areas of the financial statements, including impairment of goodwill in 888 Holdings plc and Drax Group plc, and revenue recognition in Helios Towers plc, National Express Group plc and WPP plc.
- Regulatory Standards' [Professional Judgement Guidance](#) is non-prescriptive guidance on the effective exercise of professional judgment by auditors. It comprises a framework for making professional judgements and a series of illustrative examples showing the exercise of professional judgement in practice.

Going concern

In periods of uncertainty, the auditor's assessment of going concern is a particularly key area of consideration. The ongoing uncertainties identified in last year's report, i.e. Covid-19, Brexit and climate change, are still features of today's economic landscape, and these are joined and aggravated by other factors, including inflation, the reduction of Government support made available during the pandemic and the geopolitical situation. In current circumstances and the reasonably foreseeable future, uncertainty will affect financial reporting in multiple ways, making the necessary judgements more complex and the clear disclosure of how those judgements are reached even more crucial.

Auditors will need to think widely about the events and uncertainties that may affect companies, beyond the obvious. For example, discussions with management and audit committees will need to encompass the risks faced by companies arising from a rapidly changing social and legal environment, such as the risks and costs of litigation in the environmental, social and governance arena. They may have to consider the losses arising from sudden cessations of access to supplies and costs of replacing those supplies. Similarly, companies may face unexpected market or legislative changes, preventing them from operating in a particular location, or limiting the labour supply. Forecasts of post-pandemic recession and boom differ significantly between providers and change frequently, increasing the difficulties of forecasting and, therefore, auditor's evaluation of management's going concern assessments.

Management will be sensitive to the wider messages being conveyed by the disclosure required of the judgements, assumptions and possible outcomes in relation to going concern. Auditors will need to continue to provide appropriate, focused challenge to ensure both the assessment of going concern, and the related disclosure, provide complete, useful and reliable information to the users of accounts.

Judgements and accounting estimates

Financial reporting relies upon preparers making judgements and estimates that must be evaluated by auditors. Uncertainty makes it more difficult to make estimates, and to provide compelling and reliable support.

Companies' accounts must include details of estimates that have a significant risk of causing a material adjustment to assets and liabilities within the next financial year. Examples of useful information are the basis of the judgement, sensitivity to changes in assumptions, and ranges of possible outcomes. Auditors will need to remain alert to the indicators and risk of management bias. Operating with increased levels of uncertainty will increase the challenge of making disclosures that illuminate rather than obfuscate. The requirement introduced by the FRC in 2012 for the annual report and accounts to present a fair, balanced and understandable assessment of the company's position and prospects has possibly never been so challenging as it is likely to be over the next twelve months.



Assessment of going concern is key during periods of uncertainty



Uncertainty and providing compelling and reliable support for estimates

Challenge of management (or the lack of it) remained a feature in Enforcement cases this year. Whilst the profession may be aware of and better understand the risks, it will remain a priority for auditors to focus on offering appropriate challenge to management and ensuring this is properly recorded in audit files so that it supports the disclosures required in the face of complex and interacting uncertainties.

Integrity and objectivity

In last year's Annual Enforcement Review the Themes section looked at past cases involving accountants working in business found to have breached the fundamental principles in the Codes of Ethics in relation to integrity and objectivity. These issues were also highlighted in the analysis of the issues arising in audit investigations in the Review of the year section. Integrity and objectivity issues have continued to feature in Enforcement investigations this year, both for accountants working in business and auditors in practice. Adverse findings in these areas seriously damage the reputation of individuals and the profession as a whole.

Public confidence in audit is regularly reported on in the press, especially in the wake of each corporate collapse or financial scandal. The public and informed stakeholders question the value of financial statements that turn out to be fundamentally flawed. Where ethical as well as competence issues arise, this calls into question not only the credibility of the preparers of those statements but also the usefulness of audits that fail to provide reasonable assurance, and the integrity and objectivity of the auditors who performed them.

Auditors have to preserve a balance between maintaining their objectivity and building functioning working relationships with the management of the companies they audit, and there is always the risk that one will impinge on or compromise the other. What matters most is the auditor's mindset, and here labels can be illustrative of thinking, hence the recent debate over whether firms should refer to companies they audit as 'audited entities' or 'clients'.

The FRC will continue to pay close attention to ethical issues in its monitoring of published financial statements and the conduct of audits through the work of the Corporate Reporting Review team, the Audit Quality Review team and the Audit Firm Supervision team. In turn, Enforcement will continue to horizon scan and respond to information in the public domain and brought to our attention to identify financial statements and the conduct of members in business and auditors that merit closer attention.



Adverse findings in objectivity and integrity seriously damage the reputation of individuals and the audit profession

ESG reporting, in particular climate

Background

There is a growing interest in how companies report the impact of their activities on the environment and on the wider environmental and social challenges to which they have to respond. Reporting on social issues has so far taken the form of initiatives such as gender pay gap reporting and proposed ethnicity pay gap reporting, commentary on the gender and ethnic diversity of boards and the wider workforce, obligations to ensure the integrity and legality of operation of supply chains, and modern slavery declaration requirements.

Reporting on governance issues has been driven by the 2018 UK Corporate Governance Code and the requirement for a 'section 172(1) statement' to be published on company websites and included in the strategic report.

Section 172(1) Companies Act 2006 says:

A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to:

- a) the likely consequences of any decision in the long term,
- b) the interests of the company's employees,
- c) the need to foster the company's business relationships with suppliers, customers and others,
- d) the impact of the company's operations on the community and the environment,
- e) the desirability of the company maintaining a reputation for high standards of business conduct, and
- f) the need to act fairly as between members of the company.

While the duties set out in section 172 have been in place since the Companies Act came into force, the profile of these duties has risen significantly with the requirement for a statement that 'describes how the directors have had regard to the matters set out in section 172(1)(a) to (f) when performing their duty under section 172.' This additional reporting duty was established in the Companies (Miscellaneous Reporting) Regulations 2018.

The Streamlined Energy and Carbon Reporting Rules were published in March 2019. These rules require obligated companies to report on their energy consumption and associated greenhouse gas emissions within their financial reporting for Companies House.



There is a lack of comparability between company ESG reports

Reporting on environmental impact and mitigations is complex and it has been difficult to create the same sort of clearly defined and comparable benchmarks as the gender pay gap. These difficulties mean that there is a lack of comparability between reports by companies operating in the same or similar sectors, and even less between reports by companies in vastly differing sectors. Stakeholders are keen to understand the environmental impact of companies operating in sectors such as oil and gas, aviation, mining and chemical production; however, the multiplicity of methods of reporting environmental impact and the effectiveness of mitigations make comparisons unhelpful and the audit of such data extremely challenging.

In July 2021, the FRC published its Statement of Intent on Environmental, Social and Governance challenges. It noted the planned regulatory change in this area including:

- companies, asset managers and asset owners, to report using the disclosures developed by the Taskforce on Climate-related Financial Disclosures (TCFD);
- the implementation of integrated Sustainability Disclosures Requirements;
- the creation of the International Sustainability Standards Board in November 2021.

Since then, the TCFD rules for Premium Listed companies came into force for year ends of December 2021 and onwards. These changes throw into sharp focus the need for environmental reporting to be developed using a common conceptual framework. The absence of this common conceptual framework to date has meant that reported environmental information has lacked credibility and therefore failed to provide the level of assurance stakeholders require.

Impact on audit

Auditors must read the information presented in the annual report that is not part of the audited financial statements, for example the strategic report and further 'statutory other information'. They must consider whether there are any material inconsistencies between the financial statements and the other information or the auditor's knowledge obtained in the audit. Descriptions of how directors have complied with section 172 within the strategic report are often narrative and without detailed assertions, and based on judgements that may not be disclosed in the report. Here, again, auditors need to use their professional judgement in relation to the extent and nature of the work required to reach their conclusions.

The strategic report is not the only place in company reporting where environmental considerations may be material, either quantitatively or qualitatively. It is important to understand the impact on financial statements of the judgements made by management in relation to environmental issues. Cash flow forecasts used to make the going concern assessment and judgements about the impairment of the carrying value of goodwill may rely on assumptions, for example, about forecasts of market responses to climate change, availability of raw materials and energy, shipping costs, and product development by the company and its competitors, that will require appropriate challenge and sensitivity testing by auditors to properly interrogate and assess the presentation and disclosure in the financial statements.



Auditors must make judgements on the information presented in the annual report that is not part of the audited financial statements

It is worth also bearing in mind the penalties available to regulators in the event of a breach of environmental legislation. These can be substantial, and auditors must ensure the risk and quantum of such penalties are appropriately disclosed in the financial statements. The costs of clean-up and defending legal action by regulators can be significant, and when combined with the potential for unlimited fines, auditors must carefully assess risks of the business activities under review, the risk appetite of management, and the risk assessment and control environment operated by the business. The auditing standards relevant in this context are:

- ISA (UK) 250 Section A – Consideration of laws and regulations in an audit of financial statements, which includes an objective for auditors ‘To respond appropriately to identified or suspected non-compliance with laws and regulations identified during the audit.’ The auditor must gain a general understanding of the applicable legal and regulatory framework within which the audited entity operates. They then need to obtain sufficient appropriate audit evidence in the areas where the laws and regulations have a direct effect on the financial statements.
- ISA (UK) 250 Section B – The auditor’s statutory right and duty to report to regulators of public interest entities and regulators of other entities in the financial sector, which says:

The objective of the auditor of a regulated entity is to bring information of which the auditor has become aware in the ordinary course of performing work undertaken to fulfil the auditor’s audit responsibilities to the attention of the appropriate regulator as soon as practicable when:

- a) ...
- b) In the auditor’s opinion there is reasonable cause to believe it is or may be of material significance to the regulator.

Auditors need only report to the FRC where the breach was material and was required by law to be reported. This area is complicated as there are many factors determining whether breaches need to be reported and to which regulator.

Climate change and related environmental issues have become significantly more high-profile and important to society on a global scale over the last ten years, and it looks likely that this will continue. In consequence, auditors’ focus on this area will continue to be challenged and challenging.

The principles underpinning the audit of environmental reporting are the same as for all audit work, the difference is the lack of standardised data and the absence of a mature and benchmarked reporting framework.

Regulatory reform

The FRC continues its strategy for taking the organisation through a period of significant change to create the Audit, Reporting and Governance Authority (ARGA).

On 11 May 2022, the Government confirmed its commitment to prepare and publish a draft Bill to revamp the UK's audit and corporate reporting regime. In May 2022, the Government Response to its white paper Restoring trust in audit and corporate governance⁷⁰ was published (the Government Response), which includes far-reaching proposals affecting the FRC's purpose and objectives, and the roles and responsibilities of those we regulate. The new legislative proposals contained in the Government Response have the potential to significantly alter and enhance the FRC's enforcement powers.

A number of extraordinary factors, including Covid-19 and the war in Ukraine, have heavily affected the available parliamentary time, and we are awaiting the Government's update on the timetable for tabling legislation.

Proposals for enhanced enforcement powers for ARGA

Directors' enforcement regime

The Government Response includes proposals for a new directors' enforcement regime that would provide ARGA with powers to investigate and sanction directors of PIEs in relation to corporate reporting and audit-related responsibilities. The Government is also considering whether in exceptional circumstances ARGA's powers could also be applied to non-PIE directors, if doing so was justified by the public interest (for example, if it appears that a large group is structured in such a way as to frustrate proper scrutiny). It proposes that the directors' duties within the scope of the new regime would include the existing statutory duties and the new corporate reporting duties proposed elsewhere in the Government Response. The Government Response also recognises that for civil regulatory enforcement to work effectively, ARGA will need to set out what it reasonably expects of PIE directors by way of compliance with their legal duties. We are working with the Government in considering how best to elaborate on directors' statutory duties, so as to enable regulatory enforcement to apply effectively to all directors in scope of the new regime.



... a period of significant change to create ARGA



Powers to investigate and sanction directors of PIEs

⁷⁰ Restoring trust in audit and corporate governance

Statutory enforcement powers against accountants and actuaries

The Government Response also proposes to introduce legislation giving ARGA statutory powers to take enforcement action in relation to accountants who are members of professional bodies which require them to hold professional-level accountancy qualifications. These powers will be exercisable in cases that give rise to public interest concerns, principally those arising out of corporate reporting by PIEs. The Government envisages that those powers will be similar to the investigatory and sanctioning powers that are exercisable in relation to Statutory Auditors. The Government also proposes that ARGA will use the International Ethics Standards Board for Accountants (IESBA) International Code of Ethics as the basis for enforcement action.⁷¹

Similarly, the Government Response proposes to introduce a strengthened, statutory basis for the regulation of the actuarial profession, with clear and defined roles and responsibilities. The Government proposes that ARGA should have statutory powers to take action against individuals (and, in exceptional cases, the entities) responsible for breaches of technical actuarial standards when public interest actuarial work is carried out by or for PIEs, large pension schemes or large funeral trusts. Consistent with ARGA's ability to require individuals carrying out public interest actuarial work to comply with the Institute and Faculty of Actuaries (IFoA's) ethical standards, ARGA may also take action against the individuals responsible for breaches of ethical standards.

We are giving careful consideration to what the implications would be for Enforcement in giving effect to the legislative proposals arising from the Government Response and continue to work with Government during the consultation and implementation process.

Continuous improvement

The Enforcement Division continues with a programme of transformation steps to implement change that is not dependent on legislation and has been in train since before the FRC Review. Enforcement's drive for improvement in timeliness and efficiency continues. This year saw the continued expansion of the headcount in Enforcement by 23% from 52 on 1 April 2021 to 64 on 31 March 2022. Further headcount growth by March 2023 is planned.

Throughout the Covid-19 pandemic and during the last year as we returned to office and hybrid working, we have ensured that the work of holding professional accountants, auditors and actuaries to account, as far as possible, has remained on track. We have continued to investigate, bring enforcement action, and conduct proceedings, largely now returning to in-person interaction where possible and preferable (e.g. for interviews), but adapting as necessary to remote and hybrid working where appropriate, while ensuring fairness to all parties. In January and February 2022, we conducted a five-week trial in person before the independent Tribunal (with some hybrid adaptations to accommodate Covid restrictions) involving six parties. We have also continued successfully to recruit and onboard a significant number of new staff.

⁷¹ International Code of Ethics for Professional Accountant

Strengthened statutory basis for the regulation of the Actuarial Profession

9 Glossary

Term	Meaning
ACCA	The Association of Chartered Certified Accountants.
Accountancy Scheme	A contractual arrangement between the FRC and the accountancy professional bodies that provides for the FRC to investigate (and take enforcement action against) their members in cases that raise important issues affecting the public interest in the UK.
Actuarial Scheme	A contractual arrangement between the FRC and the actuarial professional body that provides for the FRC to investigate (and take enforcement action against) actuaries in cases that raise important issues affecting the public interest in the UK.
AEP	The Audit Enforcement Procedure, which is the process under which the FRC can investigate Statutory Auditors and audit firms in relation to audits of PIEs, large AIM-listed companies and Lloyd’s Syndicates for breach of a Relevant Requirement.
AER	The FRC’s Annual Enforcement Review.
AIM	Alternative Investment Market.
AQR	The FRC’s Audit Quality Review team. This team is responsible for monitoring the quality of the audit work of Statutory Auditors and audit firms in the UK that audit PIEs and certain other entities within the scope retained by the FRC.
ARGA	Audit, Reporting and Governance Authority.
Audit firm	The sole practitioner, partnership, limited liability partnership or other corporate entity engaged in the provision of audit services.
Audited entity	Entity whose financial statements are subject to audit by the audit firm.
Auditor	Auditor refers to the person or persons conducting the audit, usually the Audit Engagement Partner or other members of the engagement team, or, as applicable, the firm.
BEIS	Department for Business, Energy and Industrial Strategy.
Big Four	The four largest accounting firms – Deloitte, EY, KPMG and PwC.
Big Seven	The Big Four accounting firms, plus GT, BDO and Mazars.
Brydon Review	The independent review led by Sir Donald Brydon into how the audit process and product could be developed to better serve the needs of users and the wider public interest.

CAI	Chartered Accountants Ireland.
CEE	The FRC's Case Examination and Enquiries team. This team is responsible for gathering intelligence and conducting initial enquiries on cases arising under the AEP, the Accountancy Scheme or the Actuarial Scheme.
CIMA	The Chartered Institute of Management Accountants.
Client Asset Reports	Annual reports on client assets required by the FCA.
CMA	Competition and Markets Authority.
CMA Review	<i>The Statutory audit services market study</i> published by the CMA in April 2019.
Conduct Committee	The Conduct Committee is a subcommittee of the FRC that decides whether to open investigations under the enforcement schemes and AEP, and performs an oversight role in relation to the FRC's enforcement work. It is also the body responsible for making decisions about publication of certain case-related matters and issuing guidance.
Constructive Engagement	A process introduced by the AEP for resolving cases with an audit firm where the audit quality concerns do not necessarily warrant a full enforcement investigation.
CRR	The FRC's Corporate Reporting Review team reviews directors' reports and accounts of public and large private companies for compliance with the law. It also keeps under review interim reports of all listed issuers and annual reports of certain other non-corporate listed entities.
Decision Notice	A document served in an AEP investigation by Executive Counsel, the Tribunal or Appeal Tribunal (as relevant) that sets out the breaches of Relevant Requirements by the Respondent, sanctions and an amount payable in respect of Executive Counsel's costs. The Decision Notice may take the form of a Proposed or Final and/or Settlement Decision Notice, depending on the stage of the case.
Engagement partner	The Partner or other person in the firm who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.
Engagement quality control review partner or EQCR	A Partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgements the engagement team made and the conclusions it reached in formulating the report.
Formal Complaint	A document issued at the end of an Accountancy Scheme investigation that sets out the alleged Misconduct.
FRC	Financial Reporting Council.

FRC Review	The independent review of the FRC led by Sir John Kingman, which was published in December 2018.
IAASB	The International Auditing and Assurance Standards Board.
IASB	The International Accounting Standards Board.
ICAEW	The Institute of Chartered Accountants in England and Wales.
ICAS	The Institute of Chartered Accountants of Scotland.
IFoA	The Institute and Faculty of Actuaries.
IFRS	The International Financial Reporting Standards issued by the International Accounting Standards Board.
Independent Reviewer	An independent lawyer (a current or former member of the judiciary, a barrister, an advocate or a solicitor) who is appointed by the Convener in an AEP investigation to consider and approve a Proposed Decision Notice or Proposed Settlement Decision Notice, following agreement of the Respondent. A similar role is performed by an appointed individual in an Accountancy or Actuarial Scheme case.
IR	Investigation Report. Under the AEP, this report is served on the respondent at the end of an investigation and sets out the Allegations against the respondent, the Relevant Requirements that appear to have been breached, and summarises the evidence and documents obtained over the course of the investigation.
ISAs	International Standards on Auditing (UK), which are based on standards issued by the International Auditing and Assurance Standards Board. These form part of the Relevant Requirements that apply to Statutory Audit work.
KPI	Key performance indicator.
Member	A member of any of the bodies that participate in the contractual arrangement of the Accountancy or Actuarial Schemes, or a person who is subject to the systems of discipline, professional conduct and regulation of any such body.
Member Firm	A firm that is subject to the systems of discipline, professional conduct, and regulation of any of the bodies that participates in the contractual arrangement of the Accountancy or Actuarial Schemes.

Misconduct	An act or omission, or series of acts or omissions, by a Member or Member Firm in the course of their or its professional activities (including as a partner, member, director, consultant, agent, or employee in or of any organisation, or as an individual) or otherwise, which falls significantly short of the standards reasonably to be expected of a member or Member Firm or has brought, or is likely to bring, discredit to the member or the Member Firm or to the accountancy profession.
Misstatement	A difference between the reported amount, classification, presentation, or disclosure of a financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework.
Non-audit work	Any engagement in which an audit firm provides professional services to an audited entity, its affiliates or another entity where the subject matter of the engagement includes the audited entity and/or its significant affiliates other than the audit of financial statements of the audited entity.
Objectivity	Acting and making decisions and judgements impartially, fairly and on merit (having regard to all considerations relevant to the task in hand but no other), without discrimination, bias, or compromise because of commercial or personal self-interest, conflicts of interest or the undue influence of others, and having given due consideration to the best available evidence.
Participants in the Accountancy Scheme	Participants in the Accountancy Scheme that are not also RSBs are: the Chartered Institute of Management Accountants (CIMA) and the Chartered Institute of Public Finance & Accountancy (CIPFA).
Partner	Any individual with authority to bind the firm with respect to the performance of a professional services engagement.
PFC	A Proposed Formal Complaint, which is a draft of a Formal Complaint setting out the alleged Misconduct following an Accountancy or Actuarial Scheme investigation. Under the Accountancy Scheme, a Respondent has eight weeks to make representations in response to the PFC. After considering these representations, the FRC may finalise the Formal Complaint.

PIEs	<p>Public Interest Entities. These are:</p> <p>(a) an issuer whose transferable securities are admitted to trading on a regulated market; or</p> <p>(b) a credit institution within the meaning of Article 4(1)(1) of Regulation (EU) No 575/2013 of the European Parliament and of the Council, other than those listed in Article 2 of Directive 2013/36/EU of the European Parliament and of the Council on access to the activity of credit institutions and investment firms; or</p> <p>(c) an insurance undertaking within the meaning given by Article 2(1) of Council Directive 1991/674/EEC of the European Parliament and of the Council on the annual accounts and consolidated accounts of insurance undertakings.</p> <p>No other entities have been specifically designated in law in the UK as PIEs.</p>
Professional accountant	For the purpose of the ISAs (UK) and the FRC's Ethical Standard, professional accountants are those persons who are members of a professional accountancy body, whether in public practice (including a sole practitioner, partnership or corporate body), industry, commerce, the public sector or education.
Professional scepticism	An attitude that includes a questioning mind, being alert to conditions that may indicate possible misstatement due to error or fraud, and a critical assessment of evidence.
Relevant ethical standards	In the UK the firm and its personnel are subject to ethical requirements from two sources: the FRC's Ethical Standard concerning the integrity, objectivity and independence of the firm and its personnel, and the ethical standards established by the auditor or assurance practitioner's relevant professional body.
Relevant Requirement	<p>A requirement with which a Statutory Auditor must comply. The Relevant Requirements include those set out in:</p> <p>(a) SATCAR;</p> <p>(b) the Audit Regulation (537/2014/EU);</p> <p>(c) the ISAs; and</p> <p>(d) the FRC's Ethical Standard.</p>
RNS	Regulatory News Service: a regulatory and financial communications channel managed by the London Stock Exchange for companies to communicate with the professional investor.

RSB	Recognised Supervisory Bodies (RSBs) are: the Institute of Chartered Accountants in England and Wales (ICAEW), the Institute of Chartered Accountants of Scotland (ICAS), Chartered Accountants Ireland (CAI) and the Association of Chartered Certified Accountants (ACCA).
SATCAR	The Statutory Auditors and Third Country Auditors Regulations 2016/649.
Schemes	The Accountancy Scheme and Actuarial Scheme.
Statutory Audit	An audit performed pursuant to the EU Audit Directive and Regulation or otherwise designated by national law as a Statutory Audit, which in the UK is an audit of financial statements or consolidated financial statements required by the Companies Act 2006 (as amended).
Statutory Auditor	A person appointed as an auditor under the Companies Act 2006 who is approved by or on behalf of the FRC to carry out Statutory Audits.
Sufficiency (of audit evidence)	The measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement and also by the quality of such audit evidence.
Tribunal	The panel appointed in order to conduct hearings where Executive Counsel has decided to take enforcement action against the subject of an investigation. Tribunals are formed of former auditors, lawyers and lay persons. An Appeal Tribunal may also be appointed to hear the appeal of an interim or final decision made by a Tribunal.

Appendix A – Summary of remit and powers

Who can the FRC investigate and act against?

The FRC's overarching mission is to serve the public interest by setting high standards of corporate governance, reporting and audit and by holding to account those responsible for delivering them.

As the Competent Authority for Statutory Audit and the independent disciplinary body for accountants and actuaries in public interest cases, the FRC is committed to delivering robust, fair and transparent regulatory outcomes on a timely basis.

Those within the FRC's jurisdiction include Statutory Auditors and audit firms, accountants, firms of accountants, and actuaries.

Auditors

The FRC has responsibility for enforcement action in relation to Statutory Audit firms and individual Statutory Auditors.

Accountants

The FRC can also take enforcement action in respect of suspected Misconduct by individual accountants and firms of accountants who are members of the professional accountancy bodies⁷² in relation to non-audit work in public interest cases. These individuals are often working within businesses preparing financial statements and other financial information.⁷³

Actuaries

The FRC can take enforcement action in respect of suspected Misconduct by individual actuaries who are members of the Institute and Faculty of Actuaries (IFoA) in public interest cases. The FRC has no jurisdiction over firms employing actuaries.

The FRC currently has no powers to investigate, take enforcement action or impose sanctions on individuals, including directors, who are not members of the professional accountancy bodies or the IFoA (members). The scope of our enforcement powers is the subject of consultation for legislative change as discussed above in Chapter 8.

⁷² The professional accountancy bodies referred to in this report, approved as Recognised Supervisory Bodies (RSBs), are the Institute of Chartered Accountants in England and Wales (ICAEW), the Institute of Chartered Accountants of Scotland (ICAS), Chartered Accountants Ireland (CAI), the Association of Chartered Certified Accountants (ACCA) and the Chartered Institute of Management Accountants (CIMA).

⁷³ Members who undertake audit work but are not a Statutory Auditor also fall within the jurisdiction of the Accountancy Scheme.

The Enforcement regimes

The FRC operates three Enforcement regimes.⁷⁴

- The **Audit Enforcement Procedure**⁷⁵ in respect of Statutory Auditors and Statutory Audit firms⁷⁶ in relation to audits of PIEs,⁷⁷ large AIM-listed companies⁷⁸ and Lloyd's Syndicates;⁷⁹
- The **Accountancy Scheme**⁸⁰ in respect of accountants and firms of accountants who are members of the Participants in that scheme, in relation to non-audit work in public interest cases.⁸¹ These individuals are often working within businesses preparing financial statements and other financial information;⁸²
- The **Actuarial Scheme**⁸³ in respect of individual actuaries who are members of the IFoA.

The Audit Enforcement Procedure (AEP)

The AEP confers powers on the FRC Board to open investigations. In the majority of cases, the decision to open investigations is delegated to the Conduct Committee. An investigation is opened by the Board or Conduct Committee where there is information that *'raises a question as to whether a Statutory Auditor or Statutory Audit Firm has breached a Relevant Requirement'* and it considers that there is a good reason to investigate. Enforcement action can be taken if the Executive Counsel concludes that the investigation establishes that there has been a breach of a Relevant Requirement under auditing or ethical standards.

As noted in the Spotlight on Audit Enforcement Procedure on page 23, the AEP was reissued in January 2022 following a public consultation.

74 The three procedures described in this section cover the vast majority of the FRC's Enforcement investigations. The FRC also operates the Auditor Regulatory Sanctions Procedure to determine sanctions against Audit Firms where they have failed to comply with local audit rules, and the Crown Dependencies Recognised Auditor Regulatory Sanctions Procedure 2021 in respect of Recognised Auditors registered in Guernsey, the Isle of Man and Jersey.

75 [The Audit Enforcement Procedure](#)

76 Before June 2016, all audit and accountant investigations were conducted under the Accountancy Scheme. Following implementation of EU legislation, the FRC became the UK Competent Authority for audit, and the AEP replaced the Accountancy Scheme for audit matters. The Accountancy Scheme remains in place for audit investigations that began before June 2016 and all non-audit matters.

77 As defined in Regulation 2, SATCAR.

78 With a market capitalisation of more than €200m.

79 Other audit-related matters are delegated by law to the professional accountancy bodies, although the FRC can investigate such matters where it considers it is in the public interest to do so.

80 [The Accountancy Scheme](#)

81 The Accountancy Scheme does not apply to insolvency work, accountants' statutory obligations in relation to money laundering and terrorist financing, or 'reserved legal activities' under the Legal Services Act 2007.

82 Members who undertake audit work, but are not a Statutory Auditor, also fall within the jurisdiction of the Scheme.

83 [The Actuarial Scheme](#)

The Accountancy Scheme and Actuarial Scheme (the Schemes)

The Schemes are contractual arrangements between the FRC and the accountancy/actuarial professional bodies, and provide for the FRC to investigate and take enforcement action against members in cases that raise important issues affecting the public interest in the UK.⁸⁴

The Schemes confer power on the FRC Board to open investigations. In the majority of cases the decision to open investigations is delegated to the Conduct Committee. Investigations are opened by the Conduct Committee, principally where it determines that a matter raises or appears to raise important issues affecting the public interest in the UK and that there are *'reasonable grounds to suspect that there may have been Misconduct'*.⁸⁵ Misconduct is defined as conduct that falls significantly short of the standards reasonably to be expected of such an accountant, accountancy firm or actuary, or which has brought, or is likely to bring, discredit to the accountant/actuary or to their profession.

Enforcement action can be taken where Executive Counsel determines that there is a realistic prospect that a Tribunal will find that individual professional accountants/actuaries or accountancy firms have engaged in Misconduct.

Information gathering powers

Both the AEP and the Schemes contain provisions allowing the FRC to request information and documentation from a number of individuals and entities. In the case of the AEP, failure to comply with such requests is a criminal offence.

The following table sets out which Enforcement regime applies in respect of the individuals and entities within the FRC's jurisdiction pre- and post-implementation of the relevant EU legislation in June 2016.

Subjects of inquiry and investigation	Auditors (firms and individuals)	Accountants	Actuaries
Powers pre-2016	Accountancy Scheme ⁸⁶	Accountancy Scheme	Actuarial Scheme ⁸⁷
Powers post-2016	Audit Enforcement Procedure ⁸⁸	Accountancy Scheme	Actuarial Scheme

⁸⁴ Matters not affecting the public interest are dealt with by the professional bodies.

⁸⁵ It is also possible for Executive Counsel to commence an investigation into a firm or individual for an apparent failure to comply with the obligations under paragraphs 14(1) or 14(2) of the Schemes.

⁸⁶ [The Accountancy Scheme](#)

⁸⁷ [The Actuarial Scheme](#)

⁸⁸ [The Audit Enforcement Procedure](#)

The FRC has a number of live investigations under each of its Enforcement regimes. Further details are set out below.

Current status of audit investigations

As of 1 April 2021, 1 out of 38 **audit investigations** were under the Accountancy Scheme. There have been no audit investigations under the Accountancy Scheme opened or closed during the year. As of 31 March 2022, 1 audit investigation was being conducted under the Accountancy Scheme and 38 under the AEP.

Current status of non-audit investigations

As at 31 March 2022, there were nine open non-audit investigations into accountants, accountancy firms or actuaries under the Schemes.

Sanctions

The AEP and the Schemes each prescribe a range of sanctions that can be imposed following a finding of Misconduct or a breach of Relevant Requirements. The sanctions may be of a financial nature (e.g. an unlimited fine or waiver of client fees) or non-financial (e.g. a Reprimand or exclusion as a member of a professional body). These include:

- unlimited fines;
- reprimands or severe reprimands;⁸⁹
- orders designed to prevent recurrence, such as placing restrictions on the nature of work undertaken or clients represented, and education and training programmes;
- waiver or repayment of client fees;
- prohibition from conducting Statutory Audits, withdrawal of registration or practising certificate; and
- exclusions from membership of a professional body.

Additional sanctions under the AEP include:

- notice to cease or abstain from conduct giving rise to the breach of a Relevant Requirement (and publication of this);
- a declaration that the Statutory Audit Report does not satisfy the Relevant Requirements; and
- temporary prohibition from being a member of the management body of an audit firm or a director of a PIE.

Details of the sanctions that may be imposed are set out in the relevant published procedural documentation and related guidance.⁹⁰

⁸⁹ The decision as to whether a Reprimand or a Severe Reprimand is appropriate will depend on the facts of individual cases and the seriousness of the Misconduct/breaches.

⁹⁰ [Sanctions Policy \(Audit Enforcement Procedure\) \(January 2022\)](#); [Accountancy Scheme Sanctions Guidance \(March 2021\)](#); [Actuarial Scheme Sanctions Guidance \(March 2021\)](#)

The proceeds of financial sanctions imposed in AEP matters are remitted to the government, while in cases under the Schemes the proceeds of such sanctions are remitted to the professional body of the firm or individual which has been sanctioned, in accordance with the contractual arrangements by which the Schemes operate.

Case Examinations and Enquiries

Case Examination and Enquiry (CEE) in Enforcement is responsible for the initial assessment, and the Enforcement Case Examiner is responsible for decisions taken in respect of all cases reviewed for potential investigation. However, since October 2020, enquiries undertaken to support these decisions on AEP matters are conducted with the assistance of the Audit Firm Supervision team, to leverage the detailed audit firm knowledge of the Supervisors in that division.

Sources of enquiries

Most enquiries are generated from horizon-scanning activities, which include searches of listed company Regulatory News Service (RNS) updates and reviews of reports in the financial press. Other sources of enquiries are complaints, whistleblowing disclosures and referrals from other FRC teams, regulators and professional bodies.

Consideration is given to the nature of the issue before deciding to make further enquiries in order to ensure that our actions are proportionate and risk-based.

Horizon scanning

When performing horizon-scanning activities, the types of issues of interest include:

- material misstatements in a company's financial statements that may not have been detected through the Statutory Audit process (including errors in the audited financial statements themselves and in other parts of the annual report that an auditor has a duty to review);
- indications of fraud that may not have been detected by the Statutory Audit process; and
- indications of Misconduct by professional accountants or actuaries where it may be in the public interest for the FRC to make enquiries, primarily in relation to the preparation and approval of financial statements which may contain material errors.

In relation to errors in a set of financial statements, we focus on those that appear to be material and could reasonably be expected to influence the decisions of users of the financial statements.

Complaints and whistleblowing disclosures

Complaints and whistleblowing disclosures are managed centrally by the FRC, and are referred for further assessment and enquiry if they appear to relate to audit, accounting or actuarial matters within the FRC's Enforcement remit.

Referrals

Other FRC teams may refer matters for further enquiry if they become aware of matters indicative of auditing, accounting or actuarial irregularities. A primary source of such referrals is from audit inspections conducted by the FRC's AQR team.

In addition, the FRC's Corporate Reporting Review (CRR) team may identify a material error in a company's financial statements in terms of an incorrect accounting treatment or a disclosure failure, which may also raise a question as to whether there has been a failure in the audit process.

CEE liaises closely with other relevant regulators and prosecuting authorities to identify cases of public interest and determine which body may be best placed to act. CEE both receives and makes referrals, and information is received from and shared with other agencies as permitted through formal legal gateways.

Outcomes of an enquiry

An enquiry will end in one or more of the following outcomes:

- referral to the Conduct Committee for a decision on whether an investigation should be opened;
- in AEP cases only, resolution through Constructive Engagement (more information on the Constructive Engagement process is set out below);
- referral to another FRC team, such as CRR or AQR;
- referral to a professional accountancy body⁹¹ where that body is better placed to investigate and/or if the matter does not fall within the FRC's remit; or
- no further action by the FRC where the initial enquiry identified no evidence of acts or omissions likely to amount to potential breaches or Misconduct.

CEE may also make a referral to another regulator or agency, regardless of whether the matter is also progressed within the FRC.

⁹¹ Professional accountancy bodies include the Recognised Supervisory Bodies (RSBs), the Participants in the Accountancy Scheme and other accountancy bodies. A list of the RSBs and the Participants is included in the Glossary.

Constructive Engagement

What is Constructive Engagement?

Constructive Engagement is a process introduced by the AEP for resolving cases where the audit quality concerns can be appropriately and satisfactorily addressed without full investigation and enforcement action.

As set out in paragraphs 13, 13A and 14 of the Guidance for Case Examiner, the use of Constructive Engagement is entirely at the discretion of the Case Examiner. Examples given of cases for which it will or may be suitable include:

- cases where there has been a minor technical breach, usually at the very lowest end of the spectrum of possible breaches; and
- cases where there is no real concern about harm to investor, market or public confidence in Statutory Audit process and where there is no evidence of financial detriment to anyone.

Who conducts Constructive Engagement?

Constructive Engagement decisions are made by the Case Examiner. Detailed enquiries, and identification of remedial actions, where appropriate, are conducted by the Audit Firm Supervision team.

How does Constructive Engagement work?

We seek information from the audit firm about the audit work conducted and the issues underlying the potential audit breach, including reviewing relevant audit working papers and obtaining explanations from the audit team. Sometimes, an audit firm will be asked to appoint an independent team to perform an in-depth review of the audit work, to an agreed scope. The Case Examiner will then agree appropriate remedial actions with the firm, for example modifications to firm-wide audit procedures and/or staff training.

Constructive Engagement will only succeed with the full cooperation of an audit firm. If an enquiry is not or cannot be resolved to the Case Examiner's satisfaction, it may be referred to the Conduct Committee for a decision on opening an investigation. As part of its oversight role, the Conduct Committee is provided with information about all cases resolved via Constructive Engagement.

How do we share learnings from Constructive Engagement activities?

Although the FRC does not publish individual outcomes of Constructive Engagement, we communicate themes and learnings to audit firms, and share insights with accountancy bodies (for circulation to their members), other regulators and other teams within the FRC, who feed the results into their work. More information on the cases dealt with via Constructive Engagement is set out on pages 16 to 19.

The Board

The Board is responsible for and oversees the maintenance and operation of Enforcement procedures with the assistance of the Conduct Committee. The Board delegates Enforcement decisions, for example to open and close investigations and take enforcement action, as set out in the FRC's published Enforcement procedures.

Conduct Committee

The Conduct Committee is a committee of the FRC Board, to which its Chair reports on Enforcement matters. It comprises Board members and others, such as lawyers and former auditors,⁹² with a range of skills, experience and relevant technical expertise. It has a majority of lay members and excludes current practising auditors and any officers of the professional bodies it regulates. The Conduct Committee decides whether to open investigations under the AEP and Schemes, and performs an oversight role in relation to the FRC's Enforcement work, including the work of the Case Examiner. If it considers that an AEP case is suitable for Constructive Engagement, it can refer the matter back to the Case Examiner. If it considers that it does not have sufficient information to open an investigation under the Schemes, it can direct Executive Counsel to conduct preliminary enquiries.⁹³ The Conduct Committee is also responsible for making decisions about publication of certain case-related matters and for issuing guidance.⁹⁴

Advisory Panel

Enforcement is able to access expertise from a large pool of subject matter experts on the FRC Advisory Panel. A list of the current members of the Advisory Panel and their biographies can be found on the FRC website.⁹⁵

⁹² Who have not carried out Statutory Audits or worked for an audit firm for the previous three years.

⁹³ Preliminary enquiries will usually be conducted by lawyers and forensic accountants within the Enforcement Division, but assistance from external specialists can also be sought (see paragraphs 6(10) and 7(7) of the Schemes).

⁹⁴ All guidance issued by the Conduct Committee is published on the FRC website.

⁹⁵ [A list of the current members of the Advisory Panel and their biographies](#)

Appendix B – Ongoing audit investigations

As at 31 March 2022, there were 47 open investigations.⁹⁶ 38 investigations into individuals and firms for audit work; 1 investigation into individuals and firms for non-audit work; and 8 investigations into professional accountants working in business.

Of the 38 audit investigations under the AEP and Accountancy Scheme, 28 have been announced:

- PwC's audits of the consolidated financial statements of BT Group plc for the years ended 31 March 2015 to 31 March 2017;
- KPMG's audits of the financial statements of Carillion plc for the years ended 31 December 2014, 2015, and 2016;
- KPMG's audit of certain matters relating to the financial statements of Carillion plc for the year ended 31 December 2013 and additional audit work carried out during 2017;
- Deloitte's audits of the financial statements of SIG plc for the years ended 31 December 2015 and 2016;
- PwC's audit of the consolidated financial statements of Babcock International Group plc for the year ended 31 March 2018.
- EY's audit of the financial statements of Thomas Cook Group plc for the year ended 30 September 2018;
- EY's audit of the financial statements of Thomas Cook Group plc for the year ended 30 September 2017;
- EY's audit of the financial statements of NMC Health plc for the year ended 31 December 2018;
- KPMG's audit of the consolidated financial statements of Eddie Stobart Logistics plc for the year ended 30 November 2017;
- PwC's audit of the consolidated financial statements of Eddie Stobart Logistics plc for the year ended 30 November 2018;
- Oliver Clive & Co's audit of the consolidated financial statements of London Capital & Finance plc for the period ended 30 April 2015;
- PwC's audit of the consolidated financial statements of London Capital & Finance plc for the year ended 30 April 2016;

⁹⁶ An investigation will comprise one of the following: (1) an audit investigation into an audit firm and audit partner(s) (under the Accountancy Scheme or the AEP); (2) an investigation into professional accountant(s) working in business (under the Accountancy Scheme); (3) a non-audit investigation into professional accountant(s) and accountancy firms (under the Accountancy Scheme); (4) an investigation into actuaries (under the Actuarial Scheme). Each investigation may include multiple subjects, and an investigation is not deemed to be closed until concluded against all subjects.

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- EY's audit of the consolidated financial statements of London Capital & Finance plc for the year ended 30 April 2017;
 - Deloitte's audits of the financial statements of Lookers plc for the years ended 31 December 2017 and 2018;
 - PwC's audit of the consolidated financial statements of Babcock International Group plc for the year ended 31 March 2017;
 - PwC's audit of the consolidated financial statements of Wyelands Bank plc for the year ended 30 April 2019;
 - Saffery Champness's audit of the financial statements of Greensill Capital (UK) Limited for the year ended 31 December 2019;
 - Mazars's audit of the consolidated financial statements of French Connection Group plc for the year ended 31 January 2020;
 - BDO's audit of the consolidated financial statements of NMCN plc for the year ended 31 December 2019;
 - Crowe UK's audits of the financial statements of Akazoo Limited for the years ended 31 December 2016, 2017 and 2018;
 - MacIntyre Hudson's (trading as MHA MacIntyre Hudson) audits of the financial statements of MRG Finance UK plc for the years ended 31 December 2018 and 31 December 2019;
 - PwC's audits of the consolidated financial statements of Babcock International Group plc for the years ended 31 March 2019 and 2020;
 - HW Fisher's audit of the financial statements of Liberty Commodities Limited for the year ended 31 March 2020;
 - four investigations in relation to the Statutory Audits by King & King of:
 - the consolidated financial statements of Liberty Speciality Steels Limited for the year ended 31 March 2019;
 - the financial statements of Alvanco British Aluminium Limited (formerly Liberty Aluminium Lochaber Ltd) for the year ended 31 March 2019;
 - the financial statements of Liberty Steel Newport Limited for the year ended 31 March 2019; and
 - the financial statements of Liberty Performance Steels Limited for the year ended 31 March 2020.
 - Deloitte's audits of the consolidated financial statements of Go-Ahead Group plc for the years ended 2 July 2016, 1 July 2017, 30 June 2018, 29 June 2019, 27 June 2020, and 3 July 2021.

Appendix C – Ongoing professional accountants working in business investigations

As at 31 March 2022, there were eight open investigations in relation to members who are professional accountants working in business. Of the eight investigations, six have been announced, and relate to:

- the published financial reporting of Autonomy Corporation plc for the period between 1 January 2009 and 30 June 2011;
- the preparation and approval of the financial statements of Quindell plc for the period ended 31 December 2011 and to the year ended 31 December 2013 and the interim results for the half-year ended 30 June 2014;
- the preparation, approval and audit of the financial statements of Serco Geografix Ltd, Serco Ltd and Serco Group plc for the years ended 31 December 2011 and 31 December 2012;
- the preparation and approval of the financial statements of Sports Direct International plc for the 52-week period ended 24 April 2016;
- the preparation and approval of the financial statements of Carillion plc for the years ended 31 December 2014, 2015 and 2016, and the six months ended 30 June 2017, the preparation and reporting of other financial information during the period 2014–17, and certain matters relating to the financial statements for the year ended 31 December 2013;
- the preparation and approval of Patisserie Holdings plc's financial statements and other financial information for the years ended 30 September 2015, 2016 and 2017.

Appendix D – Summary of cases concluded and published with sanctions in 2021/22

EY/Stagecoach Group plc/AEP

In June 2021, a Final Decision Notice was issued following admissions of breaches of Relevant Requirements by EY and a Partner in relation to the Statutory Audit of the financial statements of Stagecoach Group plc for the 2017 financial year.

Points to note

- This case was an AQR referral made to Executive Counsel.
- The financial sanction imposed represented the highest to date for a case referred by AQR.
- This was a first-year audit for EY and the Audit Partner.
- The investigation concerned the audit of three distinct areas of the financial statements: defined benefit pension contributions, provision for insurance liabilities, and an onerous contract provision.
- Many of the breaches were basic and fundamental to the audit process and the work of an auditor. Similar breaches were identified across two or more of the three areas under investigation.
- The poor standard of the audit documentation maintained (which is supposed to be a thorough, clear and accurate record of the audit processes and responses taken, and judgements and conclusions reached) was of particular concern in this case.

Facts and issues

At all material times, Stagecoach was an international transport group headquartered in Scotland, operating buses, trains, trams and express coaches through subsidiaries in the United Kingdom, United States and Canada. At the time of the Audit, Stagecoach was the second largest transport group in the United Kingdom and listed on the main market of the London Stock Exchange (LSE) and was a constituent of the FTSE 250. Accordingly, Stagecoach was a Public Interest Entity (PIE) for the purposes of the AEP.

This was EY's first year of auditing Stagecoach.

The financial statements were signed on 28 June 2017, as was the audit report, which was unmodified.

Stagecoach made provision for obligations under defined benefit pension schemes, liabilities for insurance claims (e.g. accidents arising from the collision of its vehicles) and an onerous contract in respect of a railway franchise which it held as a 90% partner in a joint venture pursuant to a franchise agreement with the Department for Transport.

Audit materiality was set at £7 million, but the balances involved in each of those three areas was significantly in excess of audit materiality. Each of these three areas was identified at the planning stage as a Significant Risk area of the Audit.

The breaches of Relevant Requirements concerned a number of basic and fundamental audit concepts. These were commonly repeated across each of the three audit areas under investigation.

As to the defined benefits pension obligations, breaches were identified in respect of:

- the planning stage of the audit, where the auditors failed: to perform sufficient work in order to obtain an understanding of the entity and evaluate certain aspects of how management made accounting estimates; to include an assessment of work performed by management's expert; to perform substantive procedures in relation to assumptions input into a pension valuation model built and owned by management's expert; and to obtain a proper understanding of the company's controls in relation to this significant risk (ISA (UK) 315, 300, 500 and 540);
- a failure to design and perform audit procedures regarding the source data which were appropriate in the circumstances for obtaining sufficient and adequate audit evidence in relation to all material populations and all pension schemes (ISA (UK) 200, 220, 330 and 500);
- a lack of adequate evaluation and/or challenge of the work of the auditor's expert (ISA (UK) 200, 220, 230, 540 and 620);
- insufficient attempts to communicate certain significant considerations concerning material assumptions used in relation to this accounting estimate to the Audit Committee (ISA (UK) 260);
- a failure to agree and/or reconcile the disclosures in the financial statements to the accounting records (ISA (UK) 330); and
- a failure to prepare sufficient audit documentation (ISA (UK) 230).

As to the provision for insurance liabilities, breaches were identified in respect of:

- various failures relating to the identification and understanding of the design of controls relevant to certain aspects of certain types of insurance claim (ISA (UK) 315, 330 and 540);

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- a failure to obtain sufficient appropriate audit evidence (including to test a representative sample) when carrying out their testing of insurance claims, and when considering management adjustments to the insurance provision (ISA (UK) 200, 500 and 530);
 - a failure in a number of respects to obtain a sufficient understanding of the work of management's expert (ISA (UK) 500);
 - insufficient evaluation and/or challenge of the work of the auditor's expert (ISA (UK) 200, 500, 540 and 620);
 - inadequate communication of material considerations to the audit committee (ISA (UK) 260); and
 - a failure to prepare sufficient audit documentation (ISA (UK) 230).

As regards the onerous contract provision, breaches were identified in respect of:

- a failure to obtain sufficient appropriate audit evidence and apply sufficient professional scepticism in relation to certain 'bonds' under the franchise agreement which management considered should be disclosed as contingent liabilities (ISA (UK) 500 and 200);
- a failure to perform certain substantive procedures in relation to the onerous contract provision, particularly in relation to certain elements of the profit forecasts and forecast capital expenditure and working capital (ISA (UK) 330 and 540);
- insufficient audit work in relation to the financial statement disclosures and a lack of proper professional scepticism in considering the possibility of management bias in relation to management's approach to those disclosures (ISA (UK) 540 and 200); and
- the very poor documentation retained in this area (ISA (UK) 230).

Outcome

EY accepted that, in aggregate, the breaches potentially adversely affected a significant number of people in the United Kingdom (e.g. the public, investors or other market users), and could have harmed investor, market and public confidence in the truth and fairness of the financial statements published by Statutory Auditors or Statutory Audit firms. Stagecoach's shares were at the material time (and remain) listed on the main market of the LSE. The firm also accepted that the breaches could undermine confidence in the standards of conduct in general of Statutory Auditors and Statutory Audit firms, and/or in Statutory Audit. The breaches were, however, not intentional, deliberate, dishonest or reckless.

Having assessed the nature, seriousness, gravity and duration of the breaches, Executive Counsel identified the following combination of Sanctions as appropriate:

- a financial sanction of £3.5 million;
- a published statement in the form of a Severe Reprimand;
- a declaration that the Audit Report signed on behalf of EY did not satisfy the audit reporting requirements, as set out in the Final Decision Notice; and
- reporting requirements in respect of subsequent audits concerning onerous contract provisions.

The financial sanction was adjusted by 10% for mitigating factors (on account of the fact that EY had performed a root cause analysis and implemented certain remedial measures to prevent reoccurrence of the breaches) and discounted by 30% for admissions and early disposal of the matter.

The following sanctions were imposed against the Audit Partner:

- a financial sanction of £100,000; and
- a published statement in the form of a Severe Reprimand.

The financial sanction was discounted by 30% for admissions and early disposal of the matter.

KPMG/Silentnight/Accountancy Scheme

On 12 July 2021, the independent FRC Tribunal made findings of Misconduct and imposed sanctions on a former Partner and Head of KPMG Manchester Restructuring. This followed a referral from The Pensions Regulator and an investigation undertaken pursuant to the Accountancy Scheme in relation to the Partner's conduct in respect of the Silentnight group of companies in the period August 2010 to April 2011.

The Formal Complaint was heard over a four-week period, commencing in November 2020. The Tribunal reconvened in June 2021 to hear submissions on sanctions.

Points to note

The Tribunal made findings of Misconduct in respect of breaches of the fundamental principles of integrity and objectivity. It also held that the Partner (and through him KPMG) had acted dishonestly.

The Misconduct related to the Partner's conduct in late 2010 and early 2011 in providing restructuring services to Silentnight. Specifically:

- Throughout the period 16 August 2010 to 14 January 2011, the Partner advised and/or assisted both Silentnight and HIG in relation to a proposed acquisition of Silentnight by HIG at a time when there was a conflict of interest between the interests of Silentnight and HIG, and, as a result, the Respondents' judgement was compromised and objectivity impaired.
- The Partner dishonestly advanced and associated himself with untrue and misleading and/or materially incomplete statements to the PPF, tPR, Silentnight and the Trustees of the Silentnight Pension Scheme as to the causes of Silentnight's difficulties in order to assist HIG in its efforts to enable Silentnight to shed its liability under the Pension Scheme as cheaply as possible.

The case is also notable for the additional findings made in relation to the manner in which KPMG and the Partner defended the Formal Complaint; including for the first time a finding that a Respondent advanced an untruthful defence. These issues are discussed in further detail in the spotlight on page 41.

Facts

The Silentnight group of companies was at all material times based in the North West of England. In early 2011, at the time HIG acquired the Silentnight debt from the bank it was the largest bed and mattress manufacturer in the UK. It also had valuable exclusive rights to make and sell, in the UK, licensed mattresses for the world's leading brand. It employed approximately 1,250 employees across sites in Lancashire, Cumbria and West Yorkshire. Silentnight had made a profit in the years 2006 to 2010. Bank borrowings were due to be repaid in November 2011 and absent a restructuring or refinance (which the Tribunal ultimately held was likely) it would have been unable to trade.

Silentnight also had a defined benefit pension scheme with about 1,300 members. By the time of the events material to these proceedings, there was a substantial deficit in the pension scheme's assets as compared with the actuarial assessment of its liabilities. The deficit was a long-term unliquidated liability, which fluctuated in accordance with changes in asset values and actuarial predictions.

A private equity firm identified that if the pension scheme liability could be 'dumped' into the Pension Protection Fund (PPF), the value of the Silentnight business would be significantly increased. This would require the private equity fund to purchase Silentnight's bank debt and engineer a risk of imminent insolvency. In the event of such a risk, the expectation was that an arrangement could be made with the PPF to assume the pension scheme liability.

Ultimately, HIG purchased the bank debt and engineered the risk of imminent insolvency. No agreement could be reached with the PPF and Silentnight appointed administrators in May 2011. This had severe consequences for the members of the pension scheme.

The case against the Partner related to the assistance he provided to HIG, and his involvement in advancing or associating himself with untrue and misleading and/or materially incomplete statements to the PPF, tPR, Silentnight and the Trustees of the Silentnight pension scheme as to the causes of Silentnight's difficulties. The proceedings were robustly defended by the Respondents, who alleged in their defence that Executive Counsel's case was 'a conspiracy theory'.

Issues

The Tribunal found that the Partner had breached the Fundamental Principles of integrity and objectivity in the ICAEW Code of Ethics and, moreover, in relation to the breach of Integrity, he had acted dishonestly.

KPMG was liable, pursuant to the Accountancy Scheme, for the conduct of the Partner, and, accordingly, findings of Misconduct by KPMG were made by the Tribunal in respect of the same matters. A third allegation was not upheld.

In respect of the first allegation (breach of the Objectivity Principle):

- The Tribunal described the history of KPMG's involvement with Silentnight in this case as *'deeply troubling'*, as KPMG failed to act solely in its client's interests, acted in fundamental respects contrary to those interests and in those of a party whose interests were diametrically opposed to those of Silentnight. It concluded that the lack of objectivity in this matter went to the core of the relationship between Silentnight and KPMG.
- Throughout the period 16 August 2010 to 14 January 2011, the Partner advised and/or assisted both Silentnight and HIG in relation to a proposed acquisition of Silentnight by HIG at a time when there was a conflict of interest between the interests of Silentnight and HIG, and, as a result, the Respondents' judgement was compromised and objectivity impaired.
- Further, the Partner assisted with a strategy designed to drive Silentnight into an insolvency process, or to the brink of such a process (the 'Burning Platform'), with a view to passing Silentnight's pension scheme to the PPF at the expense of pension scheme members and PPF levy payers. In this context, the Partner provided advice and assistance to HIG so that it could acquire Silentnight as an otherwise profitable business without the burden of the pension scheme liabilities.

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- The Respondents failed, in addition, to consider the self-interest and familiarity threats which arose from their relationship with HIG and from their desire to nurture that party as a client and keep them 'onside'. The Partner was conscious of the importance of the potential relationship of HIG to KPMG throughout. The Respondents' loss of objectivity underlay or drove much of what they did in relation to Silentnight throughout the relevant period, including assisting and advising HIG in its plan to acquire Silentnight free of the pension scheme liability from the summer of 2010.

In respect of the second allegation (breach of the Integrity Principle):

The Respondents dishonestly advanced or associated themselves with untrue and misleading and/or materially incomplete statements to the PPF, tPR, Silentnight and the Trustees as to the causes of Silentnight's difficulties, in order to assist HIG in its efforts to enable Silentnight to shed its liability under the Pension Scheme as cheaply as possible. There were eight separate and distinct such statements. The Tribunal considered that the Misconduct was especially egregious given that:

- (i) the Partner (and through him KPMG) acted dishonestly, because he knew enough of the facts to know that a misleading picture was being put forward;
- (ii) the Respondents' intended the PPF, tPR and the Trustees of the Silentnight pension scheme to be misled. Their motivation was to assist HIG in its efforts to enable Silentnight to shed its liability to the PPF under the pension scheme as cheaply as possible; and
- (iii) the Respondents knew that they had to be open and transparent with PPF and tPR, and that those parties were dependent on the information supplied to them by Silentnight and HIG.

The Tribunal noted that the standards of integrity and objectivity are of fundamental importance. They express the most basic requirements that society expects of professional accountants.

Outcome

In determining the sanctions, the Tribunal considered the Misconduct was very serious, noting that to a professional accountant the conflicts of interest should have been obvious and that the Misconduct risked the loss of significant sums of money. It put at risk Silentnight's ability to survive and tens of millions of pounds of creditors' claims, potentially exceeding £100 million as the liability to the pension scheme would crystallise. The Misconduct potentially adversely affected a significant number of people. The majority of the membership of the pension scheme comprised factory workers, many of whom had worked for Silentnight and contributed to the pension scheme for much of their working life. This was a foreseeable consequence of the plan to 'dump' the pension scheme into the PPF. In particular regard to allegation 2, the Tribunal considered that there was nothing spontaneous in the representations, but rather that they followed a consistent and deliberate course of conduct intended to assist HIG and were, in effect, the culmination of the loss of objectivity.

KPMG received a fine of £13 million (being the record fine for a non-audit case), were severely reprimanded and ordered to appoint (at their own cost and under the FRC's ongoing supervision) an independent reviewer to conduct a root cause review to establish why threats to objectivity were not identified and safeguarded in the Silentnight engagements, and whether such threats were identified and safeguarded in a sample of past cases. The independent reviewer will also conduct a review of the policies, procedures and training programmes relating to various of KPMG's Advisory practices, in light of the results of the root cause review (involving Silentnight and a selection of past cases) and a review of policies and procedures. The detailed terms of the reviews are set out in Appendix B of the Tribunal's Report.⁹⁷ KPMG were also ordered to pay Executive Counsel's agreed costs (£2.45 million) and the costs of the Tribunal (£305,814).

The Partner was excluded from membership of the ICAEW, and precluded from holding an insolvency licence, for 13 years. He was also fined £500,000 and severely reprimanded.

GT/Patisserie Holdings plc/AEP

In July 2021, a Final Decision Notice was issued following admissions of breaches of Relevant Requirements by GT and the Audit Engagement Partner, in relation to the Statutory Audit of the financial statements of Patisserie Holdings plc (PH) for the financial years ended 30 September 2015, 2016, and 2017.

Points to note

- The breaches of Relevant Requirements related to four different areas of the audits: Revenue, Cash, Journals and Fixed Asset Additions.
- The breaches of Relevant Requirements were often repeated year on year and in relation to several legal entities.
- An exceptional level of cooperation was provided by GT and the Audit Engagement Partner, and this is reflected in the financial sanctions.
- The audits failed in their principal objective of providing reasonable assurance that the financial statements were free from material misstatement, whether caused by fraud or error.

Facts

PH was a holding company for a group of companies engaged in the business of casual dining, predominantly under the brand 'Patisserie Valerie', a well-known high-street chain. GT had acted as Statutory Auditor for PH since 2007 and signed off clean audit opinions for the financial statements in each of the FY2015, FY2016 and FY2017 audits.

⁹⁷ [Report of the Disciplinary Tribunal in Silentnight](#)

In October 2018, PH announced that its board had been notified of potentially fraudulent accounting irregularities and the company subsequently entered into administration, leading to the closure of 70 stores and more than 900 job losses.

Issues

The breaches of Relevant Requirements concern the following audit areas:

Revenue: In the audit of revenue, GT failed in their audit planning by not requiring the testing of large receipts of revenue at year end. They also failed adequately to test disproportionately large receipts, to spot 'red flags' in the FY2017 supporting evidence, and failed to perform the audit with professional scepticism. The size of receipts at year end should have been questioned, and the trading patterns of revenue purportedly received.

Cash: As regards cash and cash equivalents, the cash growth each year, between 2015 and 2017, was significantly larger than growth in revenue or profit before tax. There appeared to be repeated inconsistencies in the information provided to GT by management, which should have led GT to challenge management, increase their professional scepticism and perform a more detailed review of bank account activity. GT received numerous documents as evidence of cash transactions that should have given rise to concerns about their authenticity. For example, third-party invoices with missing company logos, typing errors and documents provided as evidence of cash receipts that in fact looked like purchase invoices. GT did not query the apparently incorrect accounting treatment of lodgements recognised as reconciling items, and failed to investigate adequately individual large entries and the gross quantum of reconciling items received after year end.

Journals: GT did not properly test journals made at year ends and used inappropriate criteria to select which journal entries to test. This resulted in an excessively large number of journals to test, in turn compromising the quality and depth of the testing as entries were left untested and inconsistencies arising from testing were left unexplained.

Fixed Asset Additions: Mis-categorisations of fixed asset additions were not challenged by GT. This allowed £2 million of fixed asset additions to be wrongly categorised by management in the relevant years. Four additions were supported by invoices from prior years but not the relevant year and this should have been investigated further by GT. There was a lack of professional scepticism across the three years in this area of the audit.

The breaches reveal a pattern of serious lapses in professional judgement, failures to exercise professional scepticism and failures to obtain sufficient appropriate audit evidence and/or to prepare sufficient audit documentation.

These failures represent extensive breaches of multiple Relevant Requirements, many of which are core standards. The Relevant Requirements are:

- ISA (UK) 200 (Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing);
- ISA (UK) 220 (Quality Control for an Audit of Financial Statements);
- ISA (UK) 230 (Audit Documentation);
- ISA (UK) 240 (Auditor's Responsibilities Relating to Fraud);
- ISA (UK) 260 (Communication With Those Charged With Governance);
- ISA (UK) 265 (Communicating Deficiencies in Internal Control);
- ISA (UK) 315 (Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment);
- ISA (UK) 330 (Auditor's Responses to Assessed Risks);
- ISA (UK) 500 (Audit Evidence);
- ICAEW Code of Ethics, section 130.

Outcome

The following sanctions were imposed on GT:

- a financial sanction of £4 million (adjusted for aggravating and mitigating factors, in particular reflecting an exceptional level of cooperation, by a reduction of 10% and discounted for admissions and early disposal by 35% to £2.34 million);
- non-financial sanctions requiring GT to report to the FRC annually for three years on: (i) GT's remedial actions and the impact on audit quality, including a root cause analysis; (ii) a review of the audit practice's culture relating to challenge, the actions taken as a result of the review and the impact of those actions on audit quality; and (iii) additional monitoring in relation to bank and cash audit work, and any proposed remedial action;
- a Severe Reprimand; and
- a declaration that the Statutory Audit Report for each of the three years did not satisfy the Relevant Requirements as set out in the Final Decision Notice.

GT was also required to pay Executive Counsel's costs of the investigation.

The following sanctions were imposed on the Audit Partner:

- a financial sanction of £150,000 (adjusted for aggravating and mitigating factors, in particular reflecting an exceptional level of cooperation, by a reduction of 10% and discounted for admissions and early disposal by 35% to £87,750);
- a temporary prohibition of three years from carrying out Statutory Audits and signing Statutory Audit Reports;
- a Severe Reprimand; and
- a declaration that the Statutory Audit Report for each of the three years did not satisfy the Relevant Requirements as set out in the Final Decision Notice.

GT/Interserve plc/AEP

In August 2021, a Final Decision Notice was issued following admissions of breaches of Relevant Requirements by GT and a Partner in relation to the Statutory Audits of the financial statements of Interserve plc (Interserve) for the 2015, 2016 and 2017 financial years.

Points to note

- Certain evidence from GT's audit files relevant to the decision was disclosed to the FRC in confidence and remains subject to the legal professional privilege of Interserve. The administrators of Interserve and Interserve Group Limited (a company which purchased the business of Interserve from its administrators) agreed to the FRC's use of privileged material for the limited purpose of the investigation and any subsequent enforcement proceedings. As such, full details of the failings remain confidential and cannot be published.
- The Respondents provided exceptional cooperation in the investigation, made early admissions, and GT has taken remedial actions to prevent similar breaches in the future. This was reflected in the discount to the financial sanction.

Facts

Interserve was a UK-based global construction and support services group, which entered into administration in March 2019. A company within the Interserve group had won various 'energy from waste' (EfW) contracts, which provided for the construction of waste treatment facilities. The findings in the Final Decision Notice primarily relate to the audit work in respect of the largest of the EfW contracts, against which significant losses had been recognised.

The Final Decision Notice covers audit work carried out in respect of:

- significant sums that Interserve estimated that it would recover in respect of alleged failings by its subcontractors, either by claiming under its professional indemnity insurance or pursuant to a clause in the EfW contract; and
- amounts that Interserve estimated would be payable on termination of the EfW contract.

The Final Decision Notice also covers aspects of the auditors' assessments of going concern and goodwill impairment in the financial statements for FY2017, specifically work on elements of the analysis of management's modelling of the financial data.

Issues

In respect of the audit work on Interserve's estimates of sums that it expected to recover following alleged failings by its subcontractors, it was found that the auditors failed to exercise sufficient professional scepticism. In some cases, there was limited evidence to support the conclusions reached as to amounts estimated as recoverable. Similarly, in respect of the auditors' work on Interserve's accounting estimates relating to sums payable on termination of the EfW contract, it was found that the auditors ought to have challenged Interserve's approach and sought further evidence in relation to aspects of the estimate.

In relation to the work carried out in the area of going concern, there were failures (i) in the audit work on Interserve's IT system used to aggregate divisional budgets; (ii) to complete an adequate evaluation of the source data; and (iii) to adequately record the consideration of the impact of certain differences between Interserve's projected working capital movements and its projected balance sheet movements on the going concern review. As to the work on goodwill impairment, there were failures to (i) challenge adequately the forecast margin used in management's assessment of impairment; and (ii) prepare sufficient audit documentation relating to the nature, timing and extent of the audit procedures performed in relation to goodwill impairment.

The standards found to have been breached across the audit years covered by the Final Decision Notice were:

- ISA (UK) 200 (Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing);
- ISA (UK) 230 (Audit Documentation);
- ISA (UK) 315 (Identifying and Assessing the Risks of Material Misstatement);
- ISA (UK) 500 (Audit Evidence);
- ISA (UK) 540 (Auditing Accounting Estimates and Related Disclosures);
- ISA (UK) 620 (Using the Work of an Auditor's Expert).

Outcome

The following sanctions were imposed on GT:

A financial sanction of £1.3 million, adjusted for mitigating factors and admissions/early disposal to £718,250; and non-financial sanctions, comprising a requirement for GT to report to the FRC on its monitoring programme of the quality of audit work on loss-making contracts; a Severe Reprimand; and a declaration that the Statutory Audit Reports for the Audits did not satisfy the Relevant Requirements.

The following sanctions were imposed on the Audit Partner:

A financial sanction of £70,000, adjusted for mitigating factors and admissions/early disposal to £38,675; and non-financial sanctions comprising a Severe Reprimand and a declaration that the Statutory Audit Reports for the Audits did not satisfy the Relevant Requirements.

GT/Sports Direct International plc/AEP

In November 2021, Final Decision Notices were issued following admissions of breaches of Relevant Requirements by GT and the Audit Partner in relation to the statutory audits of the financial statements of Sports Direct International plc (SDI) for the financial years ended 24 April 2016 (2016 Audit) and 29 April 2018 (2018 Audit).

Points to note

- The breaches concern basic and important requirements which are designed to ensure the quality and effectiveness of an audit; they are fundamental to the work of an auditor.
- The Respondents provided significant cooperation and made early admissions in relation to both the 2016 & 2018 Audits. GT has taken remedial action to prevent similar breaches in the future and will report to the FRC on these as part of the non-financial sanctions imposed.
- The breaches did not result in the financial statements for either 2016 or 2018 being materially misstated. The breaches were limited to discrete areas of each audit.

Facts

SDI is a well-known high street retailer and listed on the main market of the London Stock Exchange. GT had acted as auditor to SDI since SDI's listing in February 2007 and the Audit Partner, who at the time was a partner of GT with 19 years of auditing experience, had been the Statutory Auditor for SDI since 2014.

In February 2015 SDI restructured its arrangements for online retail sales having received external advice. The restructuring was designed to ensure that SDI was registered and accounted for UK VAT on all of its online sales of goods to non-business customers wherever located within the European Union and accordingly, was designed to ensure that SDI did not have to register for VAT and file VAT returns in EU member states outside of the UK. As part of the restructuring, SDI also changed the way in which delivery services were offered to non-UK EU non-business customers. Under the new arrangements non-UK EU non-business customers were required to enter into a delivery contract with Delivery Company A. The consideration of whether Delivery Company A was a related party of SDI and whether the financial statements contained the necessary disclosures was important for the 2016 Audit.

In relation to the 2018 Audit, SDI's inventory provision for FY2018 was £162.2 million. This represented an increase, as compared with the previous year, both in terms of amount (£98.4 million) and percentage (15.6% as compared with 13.5%). The amount of this provision was highly material. SDI's management estimated the inventory provision percentage using their own model. The level of SDI's inventory provision therefore involved considerable judgment. Similarly, SDI's website sales for FY2018 made up £679 million out of total revenue of £3,360 million. It was the second largest area of revenue for SDI, accounting for 20% of total revenue. The audit team also recognised revenue as a significant risk in the audit plan for the 2018 Audit.

Issues

In respect of the 2016 Audit, whilst the Respondents identified related parties as an area of significant risk, they failed to treat with professional scepticism management's assertion that Delivery Company A was not a related party of SDI. There were a number of relevant factors which should have prompted the Respondents to consider and follow up matters further, but they did not. The Respondents should have obtained audit evidence commensurate with the level of risk, but the evidence obtained was insufficient for the Respondents to reach a reasonable conclusion as to the appropriateness of the related parties disclosure. The Respondents failed to evaluate whether the overall presentation of the relationship between SDI and Delivery Company A in the financial statements met reporting requirements. In so far as the Respondents did consider these issues, they failed to document their consideration, conclusions, and audit evidence. Even though related parties had been identified as a significant risk, the Respondents also failed to communicate this to those charged with governance before the 2016 financial statements were finalised.

In respect of the 2018 Audit, the Respondents failed to obtain sufficient appropriate audit evidence, evaluate whether information provided by SDI was sufficiently reliable, or to prepare sufficient audit documentation commensurate with the risk in relation to the two areas of the audit.

The breaches related to:

- ISA (UK) 200 (Overall objectives of the independent auditor and the conduct of an audit in accordance with International Standards on Auditing);
- ISA (UK) 230 (Audit Documentation);
- ISA (UK) 260 (Communication with those charged with governance);
- ISA (UK) 330 (The auditor's response to assessed risks);
- ISA (UK) 500 (Audit Evidence); and
- ISA (UK) 550 (Related Parties).

Outcome

The following sanctions were imposed on GT:

Financial sanctions, comprising:

- In respect of the 2016 Audit a financial sanction of £1.7 million, adjusted for mitigating factors and admissions/early disposal to £1.1305 million; and
- In respect of the 2018 Audit a financial sanction of £350,000, adjusted for aggravating and mitigating factors and admissions/early disposal to £193,375.

Non-financial sanctions, comprising:

- In respect of the 2016 Audit, a requirement for GT to report to the FRC on whether changes made to its audit methodology are resulting in a better exercise and documentation of an audit team's judgement regarding key audit matters;
- In respect of the 2018 Audit, a requirement for GT to undertake thematic reviews and report to the FRC as to the efficacy of enhancements it has introduced regarding the audit of inventory provisions of retail entities and the use of audit data analytics to audit revenue;
- A severe reprimand in respect of both the 2016 & 2018 Audits; and
- A declaration that that the Statutory Audit Report for 2016 & 2018 did not satisfy the Relevant Requirements.

The following sanctions were imposed on the Audit Partner:

Financial sanctions, comprising:

- In respect of the 2016 Audit, a financial sanction of £90,000, adjusted for admissions/early disposal to £63,000; and
- In respect of the 2018 Audit, a financial sanction of £30,000, adjusted for aggravating and mitigating factors and admissions/early disposal to £16,575.

Non-financial sanctions, comprising:

- A severe reprimand in respect of both the 2016 & 2018 Audits.

The Respondents also paid Executive Counsel's costs of the investigations.

Deloitte/Mitie Group plc/AEP

In November 2021, a Final Decision Notice was issued, and sanctions were imposed against Deloitte and a Partner in relation to the Statutory Audit of the financial statements of Mitie Group plc (Mitie), for the financial year ended 31 March 2016 (FY2016).

Facts

Mitie is the parent company of a group of companies which provide facilities management and professional services. Mitie has been listed on the London Stock Exchange since 1988, with Deloitte being appointed to audit its financial statements each year since. The audit of the FY2016 financial statements was the partner's first year as Engagement Partner.

The Respondents admitted breaches of Relevant Requirements relating to their audit of Mitie's impairment testing of goodwill in its Healthcare Division.

Issues

The FY2016 financial statements attributed £465.5 million to the value of goodwill – the single largest asset figure in the balance sheet and 37.5% of the total reported assets. Reported goodwill in the Healthcare Division amounted to £107.2 million (23% of Mitie's total carried goodwill in FY2016).

Recoverability of the goodwill in the Healthcare Division was identified by Deloitte as a significant risk for the audit and was also identified in the audit report as one (of two) assessed risks of material misstatement. It was clearly an area that required robust and rigorous audit work.

Despite being aware of the significant risk, the Respondents failed to obtain sufficient audit evidence to gain appropriate comfort regarding the future cashflows and the discount rate used in the impairment model; failed to give sufficient consideration to the impact of working capital; failed to exercise sufficient professional scepticism; failed adequately to document their audit work in relation to the discount rate; and allowed inadequate disclosures and incomplete statements to be included in the auditor's report.

The breaches concerned the followings Relevant Requirements:

- ISA (UK) 200 (Overall objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing);
- ISA (UK) 220 (Quality Control for an Audit of Financial Statements);
- ISA (UK) 230 (Audit Documentation);
- ISA (UK) 450 (Evaluation of Misstatements Identified During the Audit);
- ISA (UK) 500 (Audit Evidence);
- ISA (UK) 540 (Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures);
- ISA (UK) 700 (The Independent Auditor's Report on Financial Statements);
and
- Section 495 of the Companies Act 2006.

Outcome

The Respondents' accepted that, due to their breaches, the FY2016 financial statements contained a material uncorrected misstatement or misstatements in relation to the headroom and/or carrying amount of the Healthcare Division. If the Respondents had complied with the Relevant Requirements, goodwill in Mitie's Healthcare business might well have been treated as impaired as at the end of FY2016 and deficiencies in the disclosures about Healthcare goodwill would have been detected.

The following sanctions were imposed on Deloitte:

A financial sanction comprising £2 million, adjusted for admissions/early disposal to £1,450,000.

Non-financial sanctions, comprising:

- a requirement to report to the FRC on the impact of remedial actions taken by Deloitte since 2016 on audits of goodwill;
- a Severe Reprimand; and
- a declaration that the Audit Report did not satisfy the Relevant Requirements.

The following sanctions were imposed on the Engagement Partner:

Financial sanctions, comprising £65,000, adjusted for mitigating factors and admissions/early disposal to £40,056.25.

Non-financial sanctions, comprising:

- a Severe Reprimand; and
- a declaration that the Audit Report did not satisfy the Relevant Requirements.

The financial sanctions were discounted by 27.5% to reflect the stage at which admissions were made. Further, Executive Counsel allowed a further 15% reduction for mitigation in relation to the Partner, to reflect his constructive response to the AQR inspection and subsequent Enforcement investigation.

The Respondents also paid Executive Counsel's costs of the investigation.

KPMG/Conviviality plc/AEP

In December 2021, a Final Decision Notice was issued following admissions of breaches of Relevant Requirements by KPMG and the Audit Engagement Partner in relation to the Statutory Audit of the financial statements of Conviviality plc for the 2017 and 2018 financial years.

Points to note

- Conviviality was, at the time of the Audits, the UK's largest independent drinks distribution business and a significant number of customers, suppliers and employees relied on it being audited to a high standard.
- Conviviality went into administration in April 2018.
- The breaches of Relevant Requirements were numerous and occurred across several significant areas of the 2017 financial statements. The principal complaints concerned the fact that there had been a failure to obtain sufficient appropriate audit evidence across five different areas of the audit, a serious lack of professional scepticism in three of those areas, and a poor standard of audit documentation maintained in respect of both audit years under investigation. The breaches were of Relevant Requirements which are central to an auditor's role and function.
- The audit was conducted by KPMG's Manchester office. The Audit Engagement Partner had been appointed to a senior position within the audit function of KPMG at the time of the audit of the 2017 financial statements. In addition, she had been the subject of sanctions in December 2019, and the breaches in that case were of a similar nature to some breaches identified in this case.

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- KPMG and the Audit Engagement Partner both had a poor previous regulatory track record.

Facts

Conviviality listed on the Alternative Investment Market of the London Stock Exchange (AIM) in July 2013 and between 2013 and 2017 grew rapidly through a series of acquisitions. In FY2017, the Company reported significant increases in the key financial reporting areas of revenue, profit and net assets.

In early March 2018, Conviviality issued a series of trading updates which resulted in the company's shares being suspended from trading on AIM. An attempt to raise further equity in March 2018 was unsuccessful and Conviviality entered into Administration on 5 April 2018.

Issues

The breaches of Relevant Requirements by the Respondents in relation to the FY2017 Audit relate to a number of areas:

- A failure to revise, in light of information obtained during the FY2017 Audit, their initial assessment of the risks of material misstatement to the financial statements, to design and perform audit procedures responsive to the risks of material misstatement due to fraud, and adequately to document their audit procedures in respect of the risk assessment and fraud risk assessment.
- A failure to obtain sufficient appropriate audit evidence:
 - (a) in relation to the recognition by Conviviality of £5.9 million as accrued franchise licence revenue in FY2017;
 - (b) in relation to the accounting treatment adopted in respect of a third-party contract for the supply of wine;
 - (c) in relation to the capitalisation of certain costs and the classification of certain items as exceptional, in accordance with the company's accounting policy;
 - (d) in relation to several items of accrued supplier income; and
 - (e) in order to gain reasonable assurance that the carrying value of the goodwill of each cash-generating unit in the Conviviality group had not been impaired.
- A failure to apply sufficient professional scepticism in relation to the recognition of accrued franchise licence revenue, the accounting treatment adopted in relation to the third-party wine supply contract, and in the course of performing their audit procedures in relation to goodwill impairment.
- A failure adequately to document their audit procedures in a number of these areas.

The admitted failings in the FY2018 Audit concern failures to document the decision to prepare a Financial Position and Prospects Procedures report to Conviviality (non-audit services) during the period of the FY2018 Audit, which breached the FRC's Revised Ethical Standard 2016.

The breaches related to:

- ISA (UK) 200 (Overall objectives of the independent auditor and the conduct of an audit in accordance with international standards on auditing);
- ISA (UK) 220 (Quality control for an audit of financial statements);
- ISA (UK) 230 (Audit documentation);
- ISA (UK) 240 (The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements);
- ISA (UK) 300 (Planning an audit of financial statements);
- ISA (UK) 315 (Identifying and assessing the risks of material misstatement through understanding the entity and its environment);
- ISA (UK) 500 (Audit evidence); and
- The FRC's Revised Ethical Standard 2016 (in relation to the FY2018 Audit only).

Outcome

The following sanctions were imposed on KPMG:

- a financial sanction of £4.3 million (discounted for admissions and early disposal by 30% to £3.01 million);
- a Severe Reprimand;
- a declaration that the Audit Report did not satisfy the audit reporting requirements for the reasons set out in the Final Decision Notice; and
- a non-financial sanction requiring KPMG to report to the FRC identifying the causes of the deficiencies in the FY2017 Audit and the steps and remedial action which the firm has taken to prevent reoccurrence of those deficiencies

The following sanctions have been imposed on the Audit Partner:

- a financial sanction of £110,000 (adjusted upwards by 5% for aggravating factors and discounted for admissions and early disposal by 30% to £80,850); and
- a Severe Reprimand.

PwC/Kier plc/AEP

In December 2021, a Final Decision Notice was issued, and sanctions imposed against PwC and a former Partner in relation to the Statutory Audit of the financial statements of Kier Group plc (Kier), for the financial year ended 30 June 2017 (FY2017).

Facts

Kier is a major infrastructure, buildings, developments, and housing group listed on the London Stock Exchange. PwC was appointed as Kier's Statutory Audit Firm in 2014.

In FY2017, Kier generated revenue of £4.282 billion, with 47% of revenue being generated by the Construction division. Long-term contracts accounted for the majority of the Construction division's revenue.

The Respondents admitted breaches of Relevant Requirements in relation to the audit of long-term contracts within Kier's Construction division (and a separate breach concerning failure to identify errors in Kier's income and cash flow statements).

Issues

Contract accounting was identified as a significant risk during the planning of the audit and was a Key Audit Matter in the Auditor's Report. Despite this, when performing audit work on recognition of variations, claims receivable and forecast costs to complete, in respect of four different contracts, and the proposed central profit override, the Respondents failed to (i) obtain sufficient appropriate audit evidence; (ii) adequately determine whether Kier had appropriately applied the requirements of the applicable financial reporting framework; (iii) perform adequate testing or carry out substantive procedures on Kier's accounting estimates; (iv) prepare sufficient audit documentation to support the conclusions they reached; and (v) exercise professional scepticism.

The Respondents also failed to identify and correct errors in Kier's income and cash flow statements relating to the presentation of gains on corporate disposals completed in FY2017.

The breaches concerned the followings Relevant Requirements:

- ISA (UK) 200 (Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing);
- ISA (UK) 230 (Audit documentation);
- ISA (UK) 330 (the Auditor's Responses to Assessed Risks);

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- ISA (UK) 500 (Audit evidence);
 - ISA (UK) 501 (Specific Considerations for Select Items); and
 - ISA (UK) 540 (Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures).

Outcome

The Respondents accepted that, due to their breaches in relation to the four contracts, there was a material risk of misstatement.

The separate breach concerning the failure to identify errors in the income and cash flow statements caused a material misstatement in the FY2017 financial statements (albeit underlying results were unaffected by the subsequent restatement).

The following sanctions were imposed on PwC:

- financial sanction of £3.35 million, adjusted for aggravating/mitigating factors and admissions/early disposal to £1,959,750.
- non-financial sanctions, comprising:
 - a requirement to evaluate and report to the FRC on certain audits conducted in 2022-2023 which feature long-term contacts and the impact of remedial actions put in place;
 - a Severe Reprimand; and
 - a declaration that the Audit Report did not satisfy the Relevant Requirements.

The former Partner received the following sanctions:

- a financial sanction of £90,000 adjusted for mitigating factors and admissions/early disposal to £52,650.
- a non-financial sanctions, comprising:
 - a Severe Reprimand; and
 - a declaration that the Audit Report did not satisfy the Relevant Requirements.

The Respondents also paid Executive Counsel's costs of the investigation.

KPMG/Rolls Royce Group plc/AEP

In December 2021, a Final Decision Notice was issued following admissions of breaches of Relevant Requirements by KPMG and a Partner in relation to the Statutory Audit of the consolidated financial statements of Rolls-Royce Group the 2010 financial year.

Points to note

- The breaches of the audit standards were serious and related to a vital area of compliance for the audited entity's sector: potential bribery and malpractice through the use of intermediaries and 'advisers' in the defence field, which was a prominent public concern at the time of the Audit.
- Executive Counsel does not assert that the breaches resulted in the financial statements being materially misstated.

Facts

At the time of the 2010 audit, the Rolls-Royce Group, specializing in the manufacture and supply of gas turbine engine products and services in the civil aerospace, defence aerospace, marine and energy sectors, was one of the 30 largest companies listed on the London Stock Exchange, with underlying revenue of £10.9 billion.

Allegations of bribery and malpractice through the use of intermediaries and 'advisers' by large multi-national companies in the defence field in particular were achieving a particular prominence in the years leading up to 2010.

Certain matters were identified in the Audit which indicated risk of non-compliance by Rolls-Royce with laws and regulations relating to such bribery and malpractice. Those matters concerned two sets of payments made by Rolls-Royce to an agent in India, which gave rise to allegations which later formed two (out of twelve) counts in a Deferred Prosecution Agreement with the Serious Fraud Office in 2017, under which Rolls-Royce paid large fines.

Issues

The breaches of Relevant Requirements in this case amounted to serious failures:

- to exercise professional scepticism;
- to obtain sufficient, appropriate audit evidence and document this on the audit file; and
- to achieve sufficient Engagement Quality Control.

The breaches related to:

- ISA (UK) 200 (Overall objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing);
- ISA (UK) 220 (Quality Control for an Audit of Financial Statements);
- ISA (UK) 230 (Audit Documentation);
- ISA (UK) 250 Section A (Consideration of Laws and Regulations in an Audit of Financial Statements);
- ISA (UK) 330 (The Auditor's Responses to Assessed Risks); and
- ISA (UK) 500 (Audit Evidence).

The breaches of Relevant Requirements were not intentional, dishonest, deliberate or reckless.

Outcome

The following financial sanctions were imposed:

- on KPMG, £4.5 million adjusted for admissions and early disposal to £3,375,000; and
- on the Audit Partner, £150,000 adjusted for admissions and early disposal to £112,500.

The following non-financial sanctions were imposed on each of KPMG and the Audit Partner:

- a Severe Reprimand; and
- a declaration that the Statutory Audit Report for the Audit did not satisfy the Relevant Requirements.

A further non-financial sanction was imposed on KPMG, requiring the firm to commission a review by an appropriate external independent expert of the effectiveness of the firm's policies, guidance and procedures for audit work in the area of an audited entity's compliance with laws and regulations.

KPMG will also pay Executive Counsel's costs of the investigation.

KPMG/Revolution Bars Group plc/AEP

In December 2021, a Final Decision Notice was issued following admissions of breaches of Relevant Requirements by KPMG and the Audit Engagement Partner⁹⁸ in relation to the audits of Revolution Bars Group plc's (RBG's) financial statements for the year ended 30 June 2015 (FY2015) and the 53 weeks ended 2 July 2016 (FY2016).

Points to note

- The failings persisted for two years and across three separate areas of the audits. However, they were not intentional, dishonest, deliberate or reckless.
- The audit failed in its principal objective: that of providing reasonable assurance that the FY2015 and FY2016 financial statements were free from material misstatement.
- The audit client was a newly listed and relatively small company, but the breaches were nevertheless serious, including lack of professional scepticism.
- The importance of exercising professional scepticism, particularly in relation to areas such as complex supplier arrangements, where the FRC has indicated to the industry that extra care is required (although in this instance the arrangements were not a particularly significant aspect of RBG's business and its financial statements).
- The package of financial and non-financial sanctions, including a requirement for KPMG and the Audit Engagement Partner, who has now joined another firm, to take action to mitigate or prevent breaches recurring.

Facts

RBG is a leading UK operator of premium bars and at the time of the Audits was newly listed on the main market of the London Stock Exchange, meaning that it was a Public Interest Entity (PIE).

KPMG had been the auditor of RBG and its predecessor companies since 2006, and the Audit Engagement Partner performed the role from 2014 until he left KPMG in 2016, after the FY2016 audit. The Audit Engagement Partner was not a Partner in KPMG, but was an employee of the firm with the grade of Director. He was, however, eligible to act as Audit Engagement Partner and sign the relevant audit reports on behalf of KPMG.

In August 2016, a new Chief Financial Officer joined RBG and initiated a review of accounting policies and procedures. RBG's financial statements for FY2015 and FY2016 were found to contain various misstatements which had to be corrected, some of which arose from the three audit areas where there were failings. Some of these were material to the financial statements as a whole.

⁹⁸ The individual performed the role of Audit Engagement Partner in respect of the audits on behalf of KPMG (but he was not a Partner in the firm).

Issues

The breaches of Relevant Requirements related to the following audit areas: (i) supplier rebates and listing fees; (ii) share-based payments; and (for FY2016 only) (iii) deferred taxation.

In their audit work in respect of supplier rebates and listing fees, the Respondents failed to exercise sufficient professional scepticism and they failed to obtain and document sufficient appropriate audit evidence. These breaches related specifically to various failures in the performance of the analytical review of rebates receivable, and the failure to consider the correct period in which to account for listing fees accrued under agreements straddling the year end.

In respect of share-based payments, the Respondents failed to conduct the audit so as to obtain sufficient appropriate audit evidence and, for FY2016, they failed to communicate uncorrected misstatements to Those Charged with Governance. These breaches concerned failures to document the audit team's acceptance of management's conclusion that the share-based payment charge for FY2015 would not be significant, and the basis for their conclusion that the position in respect of share-based payments had been satisfactorily resolved by the time the FY2016 audit report was signed; the failure to perform audit procedures in such a way as to identify errors in RBG's calculation of the share-based payment charge for FY2016; and the failure to report uncorrected misstatements in FY2016, which were not material but were above the threshold for reporting to RBG's Audit Committee.

In respect of deferred taxation, the Respondents failed to prepare documentation which provided a sufficient and appropriate record of the basis for the auditor's report for FY2016. This breach related to a failure by the audit team to identify an error by RBG in a key figure used in the calculation of the deferred tax liability.

There were therefore breaches of the following standards:

- ISA (UK) 200 (Overall Objectives of the Independent Auditor and the Conduct of an Audit)
- ISA (UK) 230 (Audit Documentation)
- ISA (UK) 450 (Evaluation of Misstatements Identified During the Audit); and
- ISA (UK) 500 (Audit Evidence).

The breaches were not intentional, dishonest, deliberate or reckless.

Outcome

The following sanctions were imposed on KPMG:

- a financial sanction of £1.25 million (adjusted for aggravating and mitigating factors, and discounted for admissions and early disposal to £875,000);
- a published statement in the form of a Severe Reprimand;
- a declaration that the reports signed on behalf of KPMG in respect of the Audits did not satisfy the Relevant Requirements, as set out in the Final Decision Notice; and
- a non-financial sanction in the form of an order pursuant to rule 96(c) of the AEP, requiring KPMG to take the following remedial action to prevent a recurrence of the breaches:
 - provide the FRC's Executive Counsel with a report which identifies the reasons why it considers that the breaches occurred, and identifies measures taken since the Audits which may have reduced the risk of any repetition of the breaches;
 - provide a further report to the FRC's Executive Counsel which evaluates the effectiveness of the measures recorded in the first report (as approved by the FRC's Executive Counsel) in reducing the risk of repetition, by the examination of relevant evidence, such as the outcome of reviews of Audits in the intervening period; and identifies any additional measures that could reasonably be taken in order to mitigate any residual risk of repetition; and
 - if required, implement any additional measures agreed with the FRC's Executive Counsel to ensure the risk of repetition was adequately addressed.

The following sanctions were imposed on the Audit Engagement Partner:

- a financial sanction of £50,000 (discounted to £35,000 for mitigating factors, admissions and early disposal);
- a published statement in the form of a Severe Reprimand; and
- a non-financial sanction in the form of an order pursuant to rule 96(c) of the AEP requiring him to take the following remedial action to prevent a recurrence of the breaches:
 - provide FRC's Executive Counsel with a report, prepared by his new employer, which analyses the underlying causes of his role in the breaches and identifies any necessary remedial measures; and
 - implement any necessary remedial measures agreed with the FRC's Executive Counsel, as part of his appraisal and personal development arrangements.

The sanctions determined by Executive Counsel reflect, among other things, the fact that the FRC is prepared to impose a bespoke package of non-financial sanctions to avoid a recurrence even where the Audit Engagement Partner has left the firm.

KPMG also paid Executive Counsel's costs of the investigation.

PwC/Galliford Try plc/AEP

In March 2022, a Final Settlement Decision Notice was issued making findings of breaches of Relevant Requirements by PricewaterhouseCoopers LLP (PwC) and the Audit Partner in relation to the Statutory Audits of the consolidated financial statements of Galliford Try plc (the Company) for the years ended 30 June 2018 (the 2018 Audit) and 30 June 2019 (the 2019 Audit and, together with the 2018 Audit, the Audits).

Points to note

- The breaches concern basic and important requirements which are designed to ensure the quality and effectiveness of an audit; they are fundamental to the work of an auditor.
- In its FY2020 financial statements, the Company made a number of restatements in relation to claims that had been recognised on construction contracts. The combined impact of the restatements, net of associated tax liabilities, was a £94.3 million reduction in net assets and retained earnings as at 30 June 2018, and £72.4 million as at 30 June 2019.
- Executive Counsel does not assert that the breaches were intentional, dishonest or reckless and has taken into account that, since the Audits, PwC has introduced a number of measures designed to improve the quality of audit work on long-term contracts.
- The Respondents provided an exceptional level of cooperation with the investigation. The early stage at which admissions were made has also been reflected in the discount applied to the financial sanctions.

Facts

At the time of the FY2018 and FY2019 Audits, Galliford Try was one of the UK's leading housebuilding, regeneration and construction groups. The Company's Construction & Investments business segment delivered large-scale infrastructure projects and construction work for both private and public sector clients. These projects typically spanned several years, requiring total revenue to be estimated and apportioned across financial reporting periods. The relevant accounting standards for the recognition of such revenue were IAS 11 (in FY2018) and IFRS 15 (in FY2019). These contained specific requirements for uncertain or variable elements of revenue, such as claims or variations. IAS 11 also required that for any contracts forecast to make a loss, the full loss should be recognised in the accounts immediately.

For both the FY2018 and FY2019 Audits, the valuation of Construction contracts was identified as a significant risk by PwC. An additional risk that the recognition of material variations and claims on contracts may not be appropriate was added in FY2019.

Issues

Despite the recognition that the valuation of construction contracts was a significant risk when performing audit work on a number of the contracts, the Respondents failed to obtain sufficient appropriate audit evidence; perform adequate testing or carry out substantive procedures on the Company's accounting estimates; prepare sufficient audit documentation to support conclusions reached and carry out the audit with sufficient professional scepticism. Whilst breaches of Relevant Requirements were identified in several areas of the 2018 Audit, the breaches in the 2019 Audit were solely in relation to Contract A.

The breaches of Relevant Requirements were as follows:

Breach 1 – Contract A

The Respondents failed adequately to determine whether the Company had appropriately applied the requirements of the applicable financial reporting framework, failed to obtain sufficient evidence in response to the assessed risks in respect of Contract A judgements, failed to obtain sufficient appropriate audit evidence or corroboration in relation to the audit of contract judgements or information produced by the Company and failed to carry out the audit of Contract A with sufficient professional scepticism.

Breach 2 – the B Contracts

The Respondents failed adequately to determine whether the Company had appropriately applied the requirements of the applicable financial reporting framework, failed to obtain sufficient evidence in response to the assessed risks in respect of the B Contracts, failed to obtain sufficient appropriate audit evidence or corroboration in relation to the audit of contract judgements or information produced by the Company and failed to carry out the FY2018 Audit of the B Contracts with sufficient professional scepticism.

Breach 3 – Statement of Cash Flows

The Respondents failed to prepare sufficient audit documentation in respect of their conclusion that it was appropriate for the Company to include transactions with Joint Ventures in operating cash flows in FY2018.

Breach 4 – Contract selection and testing

The Respondents did not design and perform audit procedures which were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence on contracts (revenues, costs, assets and liabilities) in the FY2018 Audit.

Breach 5 – Controls over Construction Contracts

The Respondents did not document the design and test the implementation of controls operating over estimating, tendering and monitoring of contracts, and failed adequately or at all, to document and walk through the controls over measurement of contract revenue, costs, receivables and payables (with the exception of controls over subcontractor/supplier payments) in the FY2018 Audit.

The breaches related to:

- ISA (UK) 200 (Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (UK));
- ISA (UK) 230 (Audit documentation);
- ISA (UK) 315 (Identifying and Assessing the Risks of Material Misstatement);
- ISA (UK) 330 (the Auditor's Responses to Assessed Risks);
- ISA (UK) 500 (Audit evidence); and
- ISA (UK) 540 (Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures).

Outcome

The following sanctions were imposed on PwC:

- a financial sanction of £5,500,000 adjusted for aggravating and mitigating factors (in particular reflecting an exceptional level of cooperation) by a reduction of 15% and further discounted for admissions and early disposal by 35% so that the financial sanction payable is £3,038,750;
- a published statement, in the form of a Severe Reprimand; and
- a declaration that the Statutory Audit Reports for FY2018 and FY2019 did not satisfy the Relevant Requirements.

The following sanctions were imposed on the Audit Partner:

- a financial sanction of £150,000 adjusted for aggravating and mitigating factors (in particular reflecting an exceptional level of cooperation) by a reduction of 15% and further discounted for admissions and early disposal by 35% so that the financial sanction payable is £82,875;
- a published statement, in the form of a Severe Reprimand; and
- a declaration that the Statutory Audit Reports for FY2018 and FY2019 did not satisfy the Relevant Requirements.

The Respondents also paid Executive Counsel's costs of the investigation.



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