IN THE MATTER OF:

THE EXECUTIVE COUNSEL TO THE ACCOUNTANCY AND ACTUARIAL DISCIPLINE BOARD

- and -

(1) DELOITTE & TOUCHE
(2) MR MAGHSOUD EINOLLAHI

FORMAL COMPLAINT

INTRODUCTION

1. The Accountancy and Actuarial Discipline Board (the "AADB") is the independent, investigative and disciplinary body for the accountancy and actuarial professions in the UK. The AADB's accountancy rules and procedures are set out in the Accountancy Scheme of 8 December 2011 ("the Scheme").

2. This is the Executive Counsel's paragraph 6 (9) Formal Complaint in respect of:

    (a) Deloitte & Touche ("Deloitte"), a former Member Firm of the Institute of Chartered Accountants in England and Wales ("ICAEW"); and

    (b) Mr Maghsoud Einollahi ("Mr Einollahi"), a Member of ICAEW.

    together "the Respondents" in connection with the Respondents' conduct in relation to the four individuals known as "the Phoenix Four" and the MG Rover group, a group of companies containing MG Rover Group Limited[1] ("MGRG"), Techtronic (2000) Ltd ("Techtronic") and, from December 2000, MG Rover Holdings Ltd (later renamed Phoenix Venture Holdings) ("PVH").

3. The events surrounding the takeover of MGRG, the conduct of its business and its subsequent liquidation have been the subject of a detailed inquiry by the Companies Act Inspectors appointed by the DTI (the "Inspectors"). The Inspectors' report was published on 11 September 2009. The AADB investigation into the Respondents' conduct was put on hold pending the outcome of the DTI inquiry. The Respondents took a full part in the DTI inquiry and provided evidence to it. The DTI inquiry led to enforcement action by the Insolvency Service on behalf of the Government which concluded on 26 April 2011 when the Secretary of State accepted disqualification undertakings by the Phoenix Four. Peter Beale was disqualified from acting in the management of limited companies for 6 years; John Towers and Nick Stephenson were each disqualified for 5 years and John Edwards for 3 years. These undertakings came into effect on 17 May 2011.

4. Since the Inspectors reported and in accordance with its procedures, the Executive Counsel has provided a draft Formal Complaint to the Respondents together with a detailed factual narrative on or about 13 December 2010. The Respondents' solicitors replied with submissions to the AADB by a document dated 25 March 2011. The Executive Counsel has considered those submissions and taken them into consideration before laying the Complaint which follows.

[1] The company was Rover Group Limited until 30 October 2000 when the name was changed to MG Rover Group Limited (MGRG)

5. The Complaint arises out of the Respondents' involvement as corporate finance advisers to various companies involved with MGRG, and the Phoenix Four. The Executive Counsel will rely on the facts and matters contained in the Investigation Report of Grant Thornton dated 11 January 2012 ("The Report") a copy of which is served with this Complaint. References in this Complaint to the Report are to the Grant Thornton Report.

6. The Respondents became involved as potential advisers with those seeking to take over MGRG on or about 28 April 2000 and they acted as corporate finance advisers to companies in the MG Rover group and related entities in the years which followed in relation to transactions including the transactions referred to below until MGRG was put into administration in April 2005. The first Respondent was appointed auditor to MGRG in May 2000[2] and remained auditor until April 2005. The first Respondent also acted during this period as tax advisers to MGRG and associated companies[3]. Appendix 2.7 of the Report lists the first Respondent's engagements with companies in the MG Rover group, and related concerns, during the relevant period.

7. The second Respondent became a member of the ICAEW in 1982. At all material times, he was a partner in the first Respondent's corporate finance department. He advised on the acquisition of MGRG by the Phoenix Four and Techtronic and was corporate finance partner and lead client service partner for the first Respondent on MGRG matters until the audit of MGRG (for the year ended 31 December 2003) was completed by the first Respondent in October 2004[4].

[2] The appointment of Deloitte as auditors to Techtronic and MGRG was agreed in a corporate finance advisory engagement letter dated 4 May 2000, addressed to the directors of Techtronic

[3] Report para 2.21 – 2.33

[4] Report para 2.24

8. MGRG was, until 9 May 2000, owned by BMW. MGRG was loss making and by March 2000 MGRG was a company which BMW wished to dispose of or put into liquidation, MGRG having made substantial losses[5]. MGRG depended upon its parent BMW for financial support. It employed approximately 6,000 people in the West Midlands area, and was the last domestic UK volume car manufacturer. MGRG was a "public interest" company in the sense that it was a major manufacturer, it employed large numbers of people in the West Midlands and it sustained many people and much of the local economy. Such was the concern about MGRG and its future that members of Parliament and of the UK Government including the Secretary of State for Trade became involved in discussions about the future of MGRG in early 2000[6].

9. The Phoenix Four (also known as the Phoenix Consortium) comprised Peter Beale, John Edwards, Nick Stephenson, and John Towers. They became interested in acquiring MGRG after it became known that Alchemy Partners wished to acquire the Group, and that MGRG might, if Alchemy Partners gained control, cease to be a volume car manufacturer in the West Midlands. The Phoenix Four stated publicly that they wished to acquire MGRG in order to save MGRG as a volume manufacturer and employer in the West Midlands. Their publicly stated purpose in acquiring the Group was therefore a public interest one, and was not to acquire large sums of money or assets from their involvement with MGRG for their own private benefit[7]. Their stated

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[5] Report para 4.2 – 4.4
[6] Report para 4.14 – 4.15
[7] Report para 4.14 - 4.19; Mr Towers' Paper "Project Phoenix" sent to Mr Burden MP on 21 March 2000 [Exhibit 443]; Letter from John Towers and John Edwards dated 14 April 2000 setting out offer for RGL [Exhibit 525]

purpose was known to the Respondents[8]. The stated purpose of the acquisition by the Phoenix Four led to public support for their proposal to acquire MGRG including support from the Government.

10. The Respondents acted as advisers on the acquisition of MGRG by Techtronic between 28 April 2000 and completion of the acquisition on 9 May 2000.

11. Thereafter the Respondents acted as corporate finance advisers on, amongst others, the following transactions: Corporate Restructuring[9], Completion Accounts[10], Project Platinum[11], Project Slag/Salt[12], Projects Aircraft and Trinity[13] and Project Patto[14].

12. The fees charged by the first Respondent for corporate finance services, which the second Respondent was responsible for agreeing, amounted in total to £26,720,356 (including the acquisition fee). In the same period the audit fees amounted to £1,936,000 and the tax fees amounted to £1,811,175 which, with various other items of £184,912, brought the total fees charged by the first Respondent between 2000 and 2005 for its work relating to MGRG to £30,652,443[15]. Throughout the period 2000 to 2005 MGRG continued to make substantial losses in each year until it was put into administration in April 2005[16]. MGRG was and remained, following the acquisition

[8] Report para 4.19 - 4.21; 7.433 – 7.435; E mail from John Connolly to Maghsoud Einollahi on 9 May 2000 at 10:33 [Exhibit 424b]; E mail from John Connollly to all Deloitte Partners and staff on 9 May 2000 at 11:35 [Exhibits 424a]; Transcript of evidence of Maghsoud Einollahi on 13 November 2006, page 60
[9] Report Chapter 5
[10] Report Chapter 6
[11] Report Chapter 7
[12] Report Chapter 8
[13] Report Chapter 9
[14] Report Chapter 10
[15] Report para 2.36 and Appendix 2.7
[16] Report para 2.13. MGRG's operating losses in 2000 were £500m, 2001 £182m, 2002 £70m & 2003 £119m

by Techtronic, dependent upon the provision of funding from BMW in the form of £427.4 million nominally by way of loans, and a loan note of £75m[17].

13. On 9 May 2000, the Phoenix Four completed the acquisition of the Rover car manufacturing business when Techtronic acquired the share capital of MGRG and other related assets from BMW for a price of £10. To ensure that MGRG would continue in existence for a reasonable period, BMW had provided Techtronic with a 'dowry' in the form of a long-term interest free loan of £427.4 million to be released in tranches over a two year period and which would not be repayable until the year 2049 save in certain specified circumstances[18]. Techtronic, in turn, lent these funds to MGRG[19]. In December 2000 a corporate restructuring took place which is described in Chapter 5 of the Report. The Phoenix Four inserted a new holding company over Techtronic called MG Rover Holdings Ltd, later renamed Phoenix Venture Holdings[20] and PVH thus became the ultimate parent/ holding company of MGRG. In summary:

(1) PVH was created with four classes of shares A to D. Shares A to C were intended to widen share ownership (A: employees; B: dealers; C: executive directors of MGRG) with participation in aggregate of 60% of the profits derived from MGRG only and no voting rights in PVH. The D shares were for the Phoenix Four, with participation in 40% of the profits derived from MGRG plus 100% of any subsequent acquisitions and 100% of the voting rights in PVH[21].

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[17] Report para 4.27 – 4.29
[18] Earlier partial payment was due from 2004 in the event that MGRG reported profits, payable at 25% of the profit reported by MGRG or £25 million per year (whichever was lower)
[19] Report para 4.27 – 4.29
[20] On 30 January 2002
[21] Report para 5.1

(2) The Phoenix Four's shares in Techtronic were valued at £10 million (having cost £240,000 on subscription in May 2000). The Phoenix Four sold these shares to PVH and received in exchange interest bearing loan notes with a total value of £10 million (£2.5 million each) plus the new D shares in PVH at a nominal amount. The loan notes were subsequently redeemed in 2003[22].

(3) The BMW loan monies, which were interest free for Techtronic (i.e. BMW did not charge interest on them), were deemed to be interest bearing in favour of Techtronic when passed down to MGRG. This was done retrospectively[23] and the interest created an income and distributable reserves in Techtronic, even though MGRG was loss-making and had no distributable reserves[24]. A dividend of £9.8 million was declared[25], payable to the new holding company PVH three days after its acquisition of Techtronic. Only the Phoenix Four, as D shareholders, benefitted from dividends issued by PVH.

14. The standards of conduct reasonably to be expected of the Respondents included those set out in the Fundamental Principles and Statements contained in the Guide to Professional Ethics ("The Guide") issued by the ICAEW. The Executive Counsel will refer to and rely upon the applicable Fundamental Principles and Statements as extracted and annexed to this Complaint (Annex A). The Fundamental Principles and Statements contained in the Guide are made in the public interest and they recognise that members of the ICAEW have duties to their clients or their employer and to the

[22] Report para 5.1
[23] Report para 5.1 and 5.55 – 5.56
[24] Report para 5.40
[25] Report para 5.56

public[26]. Members of the ICAEW, including those who are retained as corporate finance advisers as well as those retained as auditors, are therefore bound amongst other things to consider the public interest and its bearing on the work, and threats to objectivity which may arise actually or potentially[27].

15. The five Fundamental Principles apply to all members and member firms of the ICAEW. They are framed in broad and general terms and constitute basic requirements of professional behaviour. The Statements provide guidance on what is expected of members and member firms in relation to particular situations that commonly arise. Each Statement indicates the kind of member to which it relates. The Guide provides that members of the ICAEW should be guided, not merely by the terms, but also by the spirit of the Guide and the fact that particular conduct does not appear among a list of examples does not prevent it from amounting to misconduct.

16. When dealing with the Phoenix Four, their associated companies and with MGRG and its associated companies it was, the Executive Counsel will submit, essential for the Respondents to have considered all relevant facts and matters which might have had an impact on their professional duties, including:

(1) The public interest;

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[26] See para 1 of the Introduction to the 2000 and 2001 Guides (1.200) and paras 1.2, 2.4 and 2.5 of the Introduction to the 2002 Guide, revised with effect from 1st August 2001 (1.200).
[27] See Statement 1.201 (paras 1.1, 1.2 and 1.4) and the Introduction to the 2002 Guide (1.200 paras 2.2, 2.4 & 2.4)

(2) That MGRG was a substantially loss making company operating in the circumstances described in paragraphs 8 and 12 above and dependent upon the loans referred to in paragraphs 12 and 13;

(3) The potential for there to be different commercial interests between the Phoenix Four, MGRG and associated companies and shareholders including the A to C shareholders in PVH;

(4) The potential for conflicts of interest between the Phoenix Four and MGRG, and PVH and MGRG given the particular structure of the shareholdings;

(5) The conflicts of interest inherent in representing and providing services and advice to the Phoenix Four whilst maintaining client relationships with the MG Rover group (including PVH and MGRG, with which Deloitte had an audit and advisory client relationship after the acquisition in May 2000 and during the events described below).

17. In summary, the conduct of the Respondents fell short of the standards reasonably to be expected of them in that they failed to act in accordance with the Fundamental Principles and the guidance in the Statements as set out in the Complaint below. The two principal transactions to which the Executive Counsel refers in the Complaint below (Projects Platinum and Aircraft) benefitted the interests of the Phoenix Four as opposed to MGRG, and benefitted the Respondents because of the substantial fees received by the first Respondent. For the purposes of Project Platinum, the Phoenix Four established a specific business structure, namely the Phoenix Partnership. It

comprised the Phoenix Four and Kevin Howe. For convenience, the expression 'the Phoenix Four' is used throughout the Complaint. In relation to Project Platinum, unless otherwise apparent, references to the Phoenix Four include the Phoenix Partnership.

COMPLAINT

ALLEGATION 1

Between 1 January 2001 and 31 December 2001, in relation to the transaction known as "Project Platinum", the conduct of Deloitte and Mr Einollahi fell short of the standards reasonably to be expected of, respectively, a member firm and a member of the ICAEW in that:

1.1 **Between 1 January 2001 and 31 December 2001 they failed adequately to consider the public interest before accepting or continuing their engagement in relation to Project Platinum (in particular as corporate finance advisers to the Phoenix Four) and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.201 (paras 1.1 and 1.4) and, from 1 August 2001, with the guidance in Statement 1.200 (paras 2.2, 2.4 and 2.5)[28];**

1.2 **Between 1 January 2001 and 20 September 2001 they failed adequately to identify which of MGRG, PVH, or the Phoenix Four was Deloitte's client and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.201 (paras 1.1 and 1.5), Statement 1.203 (para 3.0) and Statement 1.204 (para 4.0)[29];**

[28] The Executive Counsel relies upon all of the facts below and in particular paras 43 – 46 and 59 – 64. The facts relied upon to establish that MGRG was a "public interest" company are at paras 8 – 9 above. The facts relied upon to estabish that Project Platinum was not in the interests of MGRG, or its creditors, are at paras 28, 60 and 61 below.

[29] The Executive Counsel relies upon all of the facts below and in particular paras 29 - 46

1.3 Between 1 January 2001 and 31 December 2001 they failed adequately to identify and consider potential or actual conflicts of interest between MGRG, the A-C shareholders in PVH, and the Phoenix Four and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.201 (paras 1.1 and 1.5), Statement 1.203 (para 3.0) and Statement 1.204 (para 4.0)[30];

1.4 Between 1 January 2001 and 31 December 2001 they failed (i) to make it clear to MGRG that Deloitte did not represent them or act in their interests (ii) to obtain informed consent from MGRG to Deloitte acting as corporate finance advisers to the Phoenix Four and (iii) to consider discontinuing with its engagement, and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.203 (paras 3.2 and 3.4)[31];

1.5 Between 1 January 2001 and 31 December 2001 they failed to consider and put in place any or any adequate safeguards as between the Phoenix Four and MGRG, including advising MGRG to seek independent advice, and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.203 (para 4.0) and Statement 1.204 (paras 4.0 – 4.4)[32];

1.6 Between 1 January 2001 and 31 December 2001 they held themselves out as advising MGRG, or allowed MGRG to believe that they were advising them, when in fact they were advising the Phoenix Four and failed thereby to act in accordance with Fundamental Principle 2 and, with due care, in accordance with Fundamental Principle 4[33];

1.7 They proposed a contingent fee of £7.5 million and a 5% equity stake in the company to be owned by the Phoenix Four and in so doing failed adequately to

[30] The Executive Counsel relies upon all of the facts below and in particular paras 29 – 33, 36 and 43 – 46. The facts relied upon for the PVH shareholder conflict are at para 27. The facts relied upon in relation to the conflict of interest between MGRG and the Phoenix Four in relation to Project Platinum are at para 28

[31] The Executive Counsel relies upon all of the facts below and in particular paras 33, 43 – 46, 49, 58 and 62

[32] The Executive Counsel relies upon all of the facts below and in particular paras 33, 43 – 46, 49, 58 and 62

[33] The Executive Counsel relies upon all of the facts below and in particular paras 34 – 42 and 55 – 58. The Executive Counsel also relies upon the existing relationships between the Respondents and MGRG and other companies in the MG Rover group, as to which see Appendix 2.7 of the Report which lists the first Respondent's engagements with companies in the MG Rover group

identify, consider and safeguard against the self-interest threat namely that Deloitte had an interest in completing the transaction, earning a large contingent fee and acquiring an interest in the venture. They failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.201 (paras. 1.1, 1.4 and 1.5), Statement 1.203 (para. 9.0), Statement 1.204 (paras. 2.0 – 2.3) and Statement 1.210 (4.0)[34].

__Particulars__

18. The Executive Counsel will rely upon the facts and matters set out in Section 7 of the Report and the further facts and matters set out below.

Background to Project Platinum

19. When MGRG (then called Rover Group Limited) was owned by BMW, BMW established Rover Financial Services Limited ("RFS"), a finance company, whose purpose was to provide loans to Rover (and Land Rover) customers. One of the products provided was a "Personal Contract Plan" ("PCP") which was a form of hire purchase agreement under which the customer was allowed to buy the vehicle by making a balloon payment on expiry of the contract. If the customer chose to return

[34] The Executive Counsel relies upon all of the facts below and in particular (a) paras 33, 43 – 46, 49, 58 and 62 (failure to take approprate steps to guard against self-interest threats generally) (b) paras 47 – 48 (the failure to guard against the self-interest threat inherent in acquiring an interest in the venture) and (c) paras 49 – 58 (further evidence of the failure to maintain objectivity and independence). As to the circumstances which led to Deloitte's fee being agreed, and the cost of their work at standard charge-out rates, the Executive Counsel will rely on para 59 below and the corresponding paragraphs of the Report referred to therein.

the vehicle instead (e.g. if the car was not worth the amount of the balloon payment), RFS would sell it at auction[35].

20. Under that agreement the vehicles were to be collected from dealers, sold by RFS at auction, and RFS would then invoice MGRG for the difference between the guaranteed residual value and the re-sale value achieved[36]. For example if MGRG guaranteed a residual value of £5,000 for a vehicle at the end of the PCP contract, and RFS sold the vehicle at auction for £3,000, the shortfall of £2,000 would be invoiced to MGRG and paid by MGRG to RFS.

21. On 9 May 2000 when BMW sold MGRG to Techtronic, BMW retained RFS[37]. The sale of MGRG did not affect the residual value guarantees. MGRG was therefore still liable to RFS in respect of any shortfall between the guaranteed value and the actual residual value of vehicles which had been subject to PCP contracts[38]. It was necessary to reflect this potential liability in the completion accounts between Techtronic and BMW. A clause was inserted in the sale and purchase agreement which provided for £20 million to be included in the completion accounts in respect of the risks arising on the residual value guarantee[39].

22. Immediately prior to the sale of MGRG, RFS conducted a sale of 9,000 Rover vehicles which were subject to PCP contracts. This flooded the market with second hand Rover vehicles and that in turn drove down the residual value of Rover cars which were subject to ongoing PCP contracts. It also affected the sale price of new

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[35] Report para 7.1
[36] Report para 7.2
[37] Report para 7.4
[38] Report para 7.4
[39] Report para 7.5

Rover cars. The ultimate effect of these matters was that the provision in the sale and purchase agreement of £20 million might not be sufficient to cover amounts payable under the residual value guarantee in respect of vehicles expected to be returned to RFS over the subsequent few years[40].

23. In January 2001 BMW announced that it wanted to dispose of RFS (including the Rover loan book, code-named the 'Platinum' portfolio or loan book) and it looked for buyers[41]. The Platinum loan book was considered to be worth considerably less than its book value to potential purchasers in spite of being profitable, because MGRG had been recently acquired in a distressed financial state and there was concern that it may not be able to meet its liabilities for residual values[42]. On 26 January 2001, Mr Ian Whyte, Risk Controller of BMW Financial Services (GB) Limited wrote to Mr Edwards of the Phoenix Four in his capacity as Deputy Chairman of MGRG, indicating that BMW were interested in selling the Platinum loan book and inviting a firm indication of interest from MGRG[43].

24. The Phoenix Four and MGRG each had a commercial interest in acquiring the Platinum loan book. The loan book was potentially profitable. In addition, it was in MGRG's interests to minimise its costs arising from the guaranteed residual values of vehicles disposed of by RFS, and it was perceived that a sale of the Rover portfolio to a third party may increase the costs to MGRG under the residual value guarantee[44].

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[40] Report para 7.5
[41] Report para 7.6
[42] Report para 7.45 – 7.46; 7.168; note of meeting on 7 February 2001 attended by Mr Whyte, Mr Edwards and Deloitte [Exhibit 428]
[43] Letter from BMW Financial Services (GB) Ltd to John Edwards dated 26 January 2001 [Exhibit 29]
[44] Report para 7.27 & 7.30 - 7.33

25. The structure for the transaction which was ultimately undertaken was the acquisition of RFS by PVH with a simultaneous hive out of the Platinum loan book to a new company outside the group called MG Rover Capital Limited ("MGR Capital") that was owned jointly by the Phoenix Partnership (comprising the Phoenix Four and Kevin Howe) and the lender[45]. The lender was Bank of Scotland (which merged with Halifax on 10 September 2001 to create HBOS Plc). Bank of Scotland funded the acquisition of the Platinum portfolio on the basis that MGRG put up cash collateral to fund in advance its liability in the worst-case scenario (namely, that it would run out of funds and/or be insolvent by May 2002)[46]. The collateralisation which MGRG was to provide was key to Bank of Scotland's willingness to finance the Platinum transaction.

Conflict between the Phoenix Four and MGRG

26. For the reasons set out immediately below, there was throughout 2001 an obvious conflict of interest between MGRG and the Phoenix Four as each had a potentially competing interest in the transaction, or at least by no later than late June 2001, when it became part of the structure of the deal that cash collateral was to be obtained from MGRG to protect the profits of the acquiring company.

27. There was an underlying conflict of interest between the beneficial owners of MGRG and the Phoenix Four, as a result of the restructuring in December 2000 when the ownership of the group was split between those whose interests were aligned with profits derived from MGRG (namely the A, B and C shareholders, comprising MGRG

[45] Report para 7.6 -7.8
[46] Report para 7.74; 7.135; Inspectors' Report Chapter VII, para 216

employees, dealers and executive directors respectively) and those whose interests were aligned with profits derived from companies acquired post completion (namely the D shareholders comprising the Phoenix Four) [47].

28. The conflict of interest between MGRG and the Phoenix Four in relation to Project Platinum, which became increasingly apparent as the structure of the acquisition developed during 2001, was broadly as follows. The Phoenix Four had an interest in acquiring the potentially profitable Platinum loan book from RFS[48]. However this was only achievable through MGRG putting up substantial cash to fund in advance its liabilities under the residual value guarantees (as calculated under a worst-case scenario) in order to protect the profits accruing to the acquiring entity[49]. MGRG had an interest in minimising the cash collateral to be provided, as the more cash that was tied up in the deal the less MGRG would be able to use this cash to support its loss-making operations[50]. In addition, MGRG had an interest in acquiring the portfolio both as it was potentially profitable and would generate positive cash flows[51], and in order to facilitate access to information contained in the portfolio, such as customer details for the purposes of re-marketing and re-financing (through First National) to customers[52]. The Phoenix Four conversely had an interest in maximising the cash collateral obtained from MGRG in order to protect their personal profits, (which would be eroded in the event that residual value losses exceeded the cash provided by MGRG). In addition the Phoenix Four had an interest in keeping the acquiring entity

[47] Report para 5.1, 7.430 – 7.431 and 9.81
[48] The Executive Counsel will rely the Inspectors' conclusion in Chapter VII at para 230, that "in reality…the Phoenix Partnership was involved in the joint venture because its members (other than Mr Howe) wanted the profits to accrue to them…..the members of the Phoenix Partnership had undertaken very little risk and expected large returns."
[49] Report para 7.74, 7.135 and 7.163 – 7.168
[50] Report para 7.203
[51] Report para 7.202; Note headed 'Purchase of RFS Book' [Exhibit 105]
[52] Report para 7.27 & 7.30 – 7.32

and its profits (to which only they were entitled as D shareholders) outside of the loss-making MG Rover group, in order to facilitate their extraction of these profits as dividends[53].

Managing conflict

29. The Respondents began to act on this project in January 2001. By this time, the Respondents had an established relationship with MGRG and the MG Rover group. In particular, the first Respondent was MGRG's auditors and had acted, or were acting, for MGRG in connection with tax matters and other acquisitions[54]. Mr Einollahi was the lead engagement partner on the Platinum project. Ian Barton, who was employed by the first Respondent and acted throughout as a corporate finance director in the corporate finance department and who reported to Mr Einollahi, was one of the directors on this engagement[55]. Whilst the Phoenix Four were the source of the Respondents' instructions throughout, the Respondents failed to identify which of MGRG, PVH or the Phoenix Four was Deloitte's client. Further, as set out more particularly below the Respondents held themselves out, or allowed themselves to be held out, as advising, variously: MGRG, "MG Rover", PVH and the Phoenix Four. It was not until 20 September 2001 that an engagement letter was issued and even then the Respondents failed to identify, consider and safeguard against conflict of interest and to make it clear to MGRG that they acted for the Phoenix Four personally and not MGRG or the MG Rover group.

[53] Report para 7.237– 7.238. The Executive Counsel will rely on the Inspectors' conclusions on this issue at Chapter VII at para 93

[54] See para 6 above; Report para 2.21 – 2.33 & Appendix 2.7 of the Report

[55] Report para 7.335

30. On 31 January 2001 Mr Barton registered an interest with Deloitte's compliance department in relation to the acquisition of RFS indicating that there was to be a joint venture "*including MG Rover and [an] MBI candidate (to be confirmed)*"[56]. This followed Mr Ian Whyte's letter of 26 January 2001 to the Deputy Chairman of MGRG inviting MGRG to give BMW a firm indication of interest [57].

31. On 6 February 2001 Deloitte undertook a conflict search (number 5797) with their internal compliance department. In that search, Deloitte stated that their client was "MG Rover". The ultimate holding/parent company is recorded as Techtronic (suggesting that the reference to MG Rover is to MGRG). Deloitte did not, however, specify a particular company in the group and nor did they identify the Phoenix Four as their client[58].

32. The purpose of the conflict search was not to identify and consider the impact of conflicts within the MG Rover group or between MGRG and the Phoenix Four, or between the different shareholders in PVH, but was designed to identify whether there was a conflict between Deloitte and RFS. The Respondents therefore did not conduct a conflict search relating to conflicts of interest between MGRG and the Phoenix Four at this time, in circumstances where both parties were existing clients of Deloitte, and conflicts of interest had arisen as a result of the re-structuring in December 2000, and could potentially arise in the current transaction, in which the vehicle for the acquisition was not yet clear[59].

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[56] Report para 7.401; Email from Ian Barton to Bob Dowsett of the Deloitte compliance team sent 31 January 2001 states "advising joint venture including MG Rover" in connection with acquisition of RFS [Exhibit 434]
[57] Report para 7.36 – Letter from BMW Financial Services (GB) Ltd to John Edwards dated 26 January 2001 [Exhibit 29]
[58] Report para 7.402 – 7.405; Conflicts Search Form Number 5797, dated 6 February 2001 [Exhibit 390]
[59] Report para 7.401 – 7.423

33. Mr Einollahi told the Inspectors that the Deloitte conflict check was inaccurate[60]. However, he took no action himself to consider and impose safeguards to mitigate the self-interest threat to Deloitte arising both from acting for two or more clients whose interests were in conflict and from the contingent corporate finance fee of £7.5 million by: a) alerting his colleagues in the compliance team of the various conflicts of interest arising or b) obtaining informed consent from MGRG or c) advising MGRG to take independent advice to protect their interests.

34. Following a meeting on 7 February 2001 between Deloitte and Mr Edwards "*MGR*" was noted by Deloitte as the client[61]. Mr Edwards wrote to BMW on 8 February 2001 "for and on behalf of MG Rover Holdings Limited" referring to Deloitte as "our financial advisors" (the sender's reference is "JE/IRB", indicating that Mr Barton was involved in producing the letter)[62]. Mr Barton in his evidence to the Inspectors stated that this reflected his thinking at the time[63].

35. On 22 February 2001 Mr Whyte told Mr Barton that "*Rover*" would be the preferred purchaser"[64]. On 13 March 2001 Deloitte met with Mr Whyte at which Mr Whyte told Deloitte (including Mr Einollahi and Mr Barton) that other bidders will discount the value of the portfolio by approximately 60% in relation to the Rover guarantee[65].

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[60] Report para 7.406; Transcript of evidence of Mr Einollahi, 15 November 2006, pages 43 - 44

[61] Report para 7.355; Nigel Birkett's hand-written note of a meeting with John Edwards and Ian Whyte dated 7 February 2001 [Exhibit 428]

[62] Report para 7.363; Letter from John Edwards to Ian Whyte at BMW Financial Services Group dated 8 February 2001 [Exhibit 163]

[63] IRB evidence to the Inspectors 4 April pp. 15 - 17

[64] Report 7.45; Inspectors' Report, Chapter VII, para 47.2

[65] Report para 7.51; Mr Birkett's notes of the meeting of 13 March 2001 [Exhibit 47]

36. On 26 February 2001, Mr Barton emailed Mr Einollahi to ask for comments on a draft letter to be sent by Deloitte to Mr Whyte which indicated that Deloitte acted for "*MG Rover*"[66]: At this stage, no letter of engagement had been sent out to any possible clients, and none was sent out until 20 September 2001[67]. Failure to send out a letter of engagement on the alleged ground that the Respondents had not yet identified which of their potential clients was to be a party to the transaction is no answer to the Complaint. The Respondents continued to take an active role in the Platinum transaction and they remained bound by their professional duties under the Guide throughout. Further, no conflict checks had been performed in relation to whether there was a conflict between the Phoenix Four, PVH, or MGRG, and more importantly no conflict check was undertaken in June 2001 when the acquiring company changed from an MG Rover group company to the Phoenix Four or their vehicle[68].

37. On 6 March 2001 a meeting was held between Deloitte and the Phoenix Four at which Mr Einollahi was present. Deloitte's note of that meeting described matters as follows: "*Client MG Rover – RFS meeting with Phoenix*"[69]. Nigel Birkett (one of the corporate finance managers for Deloitte) who wrote the note stated that he did not draw a distinction between "Rover", "Phoenix" and the four individuals[70].

38. On 18 April 2001, Mr Barton wrote to Mr Eldridge of KPMG (who were acting on behalf of BMW in respect of the disposal of RFS). Mr Barton wrote: "*We are the*

[66] Report para 7.41; Draft letter from Deloitte to BMW Financial Services Group dated 26 February 2001 [Exhibit 32]
[67] Report para. 7.337 – 7.338
[68] Report para 7.401 – 7.407
[69] Report para 7.357; Nigel Birkett notes of meeting with Maghsoud Einollahi, John Towers on 6 March 2001 [Exhibit 429]
[70] Report 7.356 – 7.357; transcript of evidence of Nigel Birkett on 1 December 2006, page 12

financial advisers to MG Rover Holdings Ltd (MG Rover) and are acting on behalf of John Edwards, Deputy Chairman, in advising MG Rover in respect of this opportunity....We anticipate that your client will acknowledge MR Rover's unique competitive position for purchasing the Portfolio [71].

39. If what Mr Barton had said in his letter of 18 April 2001 were true, and the Respondents were advising MG Rover (through John Edwards), it would have been inconsistent with the advice subsequently given by Mr Einollahi that the Phoenix Four should acquire the portfolio through a joint venture outside the group[72], which was in the interests of the Phoenix Four as individuals, but contrary to the interests of MGRG, as indicated by views expressed by non-Phoenix MGRG directors (such as John Millett and Tony Shine) that the portfolio should be acquired by a group company[73]. In referring to MG Rover's "*unique competitive position*" Mr Barton was not referring to the Phoenix Four.

40. Whilst, in the letter of 18 April 2001, the potential acquirer was referred to as MG Rover Holdings Ltd (i.e. PVH) as opposed to MGRG on 1 June 2001 Peter Beale signed a confidentiality agreement on behalf of MGRG. This identified MGRG as the proposed acquirer. The signed agreement was circulated by fax to Deloitte, including Ian Barton, on 4 June 2001[74].

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[71] Report para 7.363; Letter from Ian Barton to Keith Eldridge at KPMG Corporate Finance dated 18 April 2001 [Exhibit 164]
[72] Report paras 7.68, 7.222 – 7.223
[73] Report paras 7.201-7.206
[74] Report para 7.44 ; Fax from Jane Ruston to Ian Whyte sent on 4 June 2001 attaching a "Confidentiality and Data Security Contract" [Exhibit 40]

41. On 6 June 2001, in correspondence between Deloitte and Barclays Capital concerning funding for the acquisition, MGRG was (again) identified as the proposed acquirer[75].

42. On 22 June 2001, Mr Edwards writing as Deputy Chairman of Holdings to BMW again stated that Deloitte were "*MG Rover's advisers*"[76].

43. On or by 25 June 2001 there was a change in the proposed structure being considered by Deloitte up to that date. On 25 June 2001, Mr Einollahi met with Mr Middleton of Bank of Scotland. Mr Middleton's note of that meeting records that Mr Einollahi had acted for "Phoenix" in the acquisition of MG Rover from BMW, that he had continued as corporate finance advisor since then, and that Mr Einollahi was acting for Mr Towers and a number of fellow directors (through the Phoenix Partnership, distinct from MG Rover) in respect of the proposed acquisition of the Platinum portfolio[77]. Thus Mr Einollahi was prepared to inform Mr Middleton that he was acting for the Phoenix Four (as he had in earlier transactions), and not (in relation to the current transaction) for any company in the MG Rover group. Also on 25 June 2001 Mr Einollahi wrote to Mr Griffiths of BMW Financial Services stating that "*our current conclusion is that this portfolio should be fully ring-fenced from MG Rover Holdings Ltd and we intend to achieve this through ownership structure, i.e. the company set up for the acquisition will be owned primarily by the Phoenix team and their financial partners*"[78].

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[75] Report para 7.43 (footnote 314: Email from Ian Barton dated 6 June 2001 at 18:30. Fax from Deloitte to Barclays Capital dated 6 June 2001 enclosing a draft confidentiality letter. Handwritten note of a call to Barclays on 15 June 2001

[76] Report para 7.363 ; Draft letter from John Edwards to BMW Financial Services Group dated 22 June 2001 [Exhibit 49]

[77] Report para 7.363; Note of Stuart Middleton of HBOS dated 25 June 2001 – [Exhibit 462]

[78] Report para 7.69; Letter from Maghsoud Einollahi to Bob Griffiths of BMWFS dated 25 June 2001 [Exhibit 440]

44. Therefore, following Mr Einollahi's suggestion to the Phoenix Four at some point towards the end of June 2001, that they should buy the portfolio through a personal investment vehicle as opposed to through an MG Rover group company[79], Deloitte themselves began to inform third parties that they were acting for the Phoenix Partnership, contrary to previous representations to third parties made either by Deloitte or on their behalf. Deloitte and Einollahi selected who their client was to be. No consideration was given to whether this was appropriate in the circumstances of this particular group of companies, in particular given the Respondents' existing relationship with the MG Rover group and that MGRG was a 'public interest' company, in parlous financial circumstances[80].

45. Caroline Butterfield of Deloitte gave evidence to the Inspectors that in June or July 2001 "*there was not clarity as to who the client was*"[81]. She was correct about this, although it would appear that, at least from 25 June 2001, Mr Einollahi and Mr Barton considered that they were acting for the Phoenix Four. However, they did not register any potential conflict of interest relating to the Phoenix Four with Deloitte's compliance department until 11 October, three weeks after they had issued a signed engagement letter. The client acceptance form in relation to the Phoenix Four, reported that "*Conflict of interest conclusion outstanding*", but was nevertheless signed off and dated 20 September 2001, the same date as the engagement letter[82]. The conflict form (signed off on 30 October 2001, nine days before the transaction completed) did not identify any potential conflict between the interests of the Phoenix

[79] Report para 7.68; 7.222 – 7.223
[80] Report para 7.429 – 7.435
[81] Report para 7.360 – Transcript of evidence of Caroline Butterfield on 1 September 2006, pages 66-67
[82] Report paras 7.384 – 7.393; Client Acceptance Form dated 20 September 2001 [Exhibit 393]

Four and those of PVH, or MGRG (for whom they had previously registered an interest) in relation to the Platinum transaction even though their interests in the transaction were conflicting[83]. The Respondents failed to carry out or complete proper compliance and conflict check procedures and nevertheless continued to act for the Phoenix Four despite not doing so. The Executive Counsel will rely upon the facts set out in paragraphs 7.384 to 7.428 of the Report. Had the Respondents carried out proper compliance and conflict check procedures and acted in accordance with them and with the Principles and the Statements set out in this Complaint they would not have been able to act for the Phoenix Four without at least ensuring that MGRG had consented to their acting for the Phoenix Four, and advising them to obtain independent advice.

46. Deloitte was alive to the conflict between MGRG and the Phoenix Four in connection with this transaction and the need for MGRG to obtain independent advice. A Deloitte meeting note of 21 August 2001 comments in relation to a discussion with Eversheds over residual value capping:

> *"need for independent advice to MGR directors.*
> *<u>Must</u> be independent director on the MGR board*
> *(John Millet!).*
> *Note: MGR shareholders – non-Phoenix shareholders only entitled to profits from car company"*[84]

[83] Report paras 7.407 – 7.417 – Compliance form Check Number 7687 dated 30 October 2001 [Exhibit 175]

[84] Report para 7.95; Notes of meeting with Ian Whyte, KPMG, Eversheds, D&T by Caroline Butterfield dated 21 August 2001 [Exhibit 437]

Abbey National/First National

47. Deloitte and Mr Einollahi preferred to work with Bank of Scotland rather than with Abbey National. In light of the existing relationship between MGRG and Abbey National (since March 2001, First National, then a subsidiary of Abbey National, had provided finance for dealers and retailers) Mr Edwards wanted to give Abbey/First National the opportunity to compete with Bank of Scotland to fund the Platinum acquisition. However, Mr Einollahi expressed a clear preference for Bank of Scotland[85]. At a meeting Mr Einollahi had with Bank of Scotland on 4 July 2001, the possibility of Deloitte having a 5% interest in the joint venture company (as a "*kicker*") was aired[86]. Notes of that meeting also record: "*Abbey National – D&T not discussing the deal with them because MGR and Abbey are clients [so] a potential minefield to advise MGR in JV with another Deloitte's client*"[87]. There was a further meeting between Deloitte and Bank of Scotland on 1 August 2001, Mr Birkett's notes of the meeting include: "ME noted off the record that Abbey….not seen it as clients [therefore] issue on fees." Deloitte and Mr Einollahi acknowledge that the rules on auditor independence would have prevented Deloitte from taking an equity stake in the joint venture if it was owned by an audit client[88]. The Executive Counsel will rely on the Inspectors' analysis of the evidence at Chapter VII, paras. 116 – 142 and their conclusion that, "On balance we think it likely that Mr Einollahi decided not to approach First National about the proposed joint venture because Abbey was a client

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[85] Report para 7.97 – 7.106

[86] Report para 7.77 ; Handwritten note of meeting on 4 July 2001 [Exhibit 59]

[87] Report para 7.107; Handwritten note of meeting on 4 July 2001 [Exhibit 59]

[88] Report para 7.108 - 109

of Deloitte and, more specifically, because of a concern that involving Abbey could prejudice Deloitte's fee arrangements"[89].

48. Whilst First National and Abbey National were interested in pursuing the transaction, on Mr Einollahi's advice, Mr Edwards ultimately rejected their indicative offer and entered exclusivity with Bank of Scotland, even though the indicative offer from Abbey National appeared to be better than that of Bank of Scotland's[90]. During the summer of 2001 Deloitte's fee hovered at approximately £7-7.5 million in cash plus 5% of an equity stake in the joint venture company. As matters progressed Deloitte's fee became a contingent fee for £7.5 million[91]. Mr Einollahi has cited various reasons for not wanting Abbey as funder, e.g. poor systems, focus diverted due to defending takeover from Lloyds TSB. But, as indicated by the meeting note of 4 July 2001, and as the Inspectors concluded, his advice was influenced by Deloitte's existing relationship with Abbey[92]. The Respondents failed thereby to safeguard their objectivity and in particular, to guard against a self-interest threat inherent in acquiring an interest in the venture. When Deloitte contacted Abbey National to advise them of their rejection, they told Abbey National that their outline offer had not been as good as that of Bank of Scotland[93].

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[89] Inspectors' Report, Chapter VII, para 140 - 141

[90] Report para 7.116 – 7.130; Handwritten note of a telephone conversation between Deloitte and John Edwards [Exhibit 84]

[91] Report para 7.448 – 7.450

[92] Report para 7.109

[93] Report para 7.129

Bank of Scotland's preferred JV partner

49. Bank of Scotland preferred their joint venture partner to be PVH or MGRG and not the Phoenix Four. Mr Einollahi and Mr Barton had attended a meeting with Bank of Scotland on 1 August 2001 and a call with Bank of Scotland on 15 August 2001, in each of which Bank of Scotland had expressed their preference for an MG Rover group company to be the joint venture partner rather than the Phoenix Four[94]. It was not until 15 August 2001 (approximately 8 months after discussions had started) that Deloitte's draft engagement letter was prepared[95]. The letter was not sent out on 15 August 2001 because at that stage Mr Einollahi was not certain of the identity of the joint venture partner, having advised the Phoenix Four to make the acquisition through a personal investment and having subsequently been advised of Bank of Scotland's express preference that the joint venture partner should be a group company due to concerns about transparency[96]. Mr Einollahi wrote to Mr Alan Christie of Bank of Scotland the following day on 16 August 2001 responding to Bank of Scotland's expressed preference, stating "*there is absolutely no issue with regard to transparency and full disclosure*", but the Phoenix Four believe it is "*inequitable that they should now be deprived the opportunity to be rewarded for their enterprise.*"[97] He stated that if MGRG were the joint venture partner, the Phoenix Four's potential return would be significantly reduced, and asked whether the choice of joint venture partner was a requirement or merely a preference, as the Phoenix Four "*have now reluctantly come*

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[94] Report para 7.135 – 7.140; Handwritten note of meeting with Bank of Scotland on 1 August 2001 [Exhibit 95]; Note of Conversation on 15 August 2001 prepared by Ian Barton [Exhibit 98]

[95] Report para 7.436 ; Draft letter from Deloitte to John Edwards of The Phoenix Partnership dated 15 August 2001 [Exhibit 176]

[96] Report paras 7.136-7.139 ; Email from Stuart Middleton to Nigel Birkett dated 27 July 2001 and attached document "Project Platinum Assumptions" [Exhibit 94]

[97] Report para 7.142; Fax from Maghsoud Einollahi to Alan Christie of Capital Bank dated 16 August 2001 [Exhibit 100]

to the conclusion that I should be approaching another financier". Despite writing in these terms, which recognised that the Phoenix Four would be gaining an advantage through acquiring the portfolio outside of the group, Mr Einollahi continued to act as adviser without warning that MGRG needed to have its own separate adviser to protect its interests.

Instructions to Robin Potts QC

50. On 21 August 2001 draft instructions to Counsel, Mr Potts QC, were sent by Eversheds to Mr Einollahi for his comments (copied in to Mr Barton). In those draft instructions Eversheds stated that "*the original rationale behind having the joint venture partner as the Consortium members (as distinct from Group or Holdings) is that no Bank would be interested into [sic] entering into a venture in partnership with MG Rover*"[98]. Eversheds posed the following question for Deloitte: "*Has it always been contemplated that the joint venture partner would be the Consortium as distinct from MG Rover?*" Mr Barton responded to the question shortly afterwards, copying in Mr Einollahi[99]: "*This is the case...it was always envisaged that RFS would be managed as an entirely separate company, either with its own managers, separate from the Group, or as is now the case in a JV company with the Consortium as shareholder.*" Mr Einollahi also read the draft instructions, and was copied in to Mr Barton's response.

51. On 29 August 2001 Mr Einollahi drafted an email, alternatively instructed Caroline Butterfield (a Deloitte employee) to draft an email, to Susan Lewis of Eversheds

[98] Report para 7.229; Draft instructions to Counsel dated 20 August 2001 [Exhibit 108]
[99] Report para. 7.229; E mail from Ian Barton to Liz Kitchen dated 21 August 2001 at 11:34 [Exhibit 109]

regarding the draft instructions for Counsel, which stated that: "*At no point has anyone from MG Rover Holdings, Techtronic or MG Rover Group other than the individual consortium members been in discussion with BMW in connection with RFS. To reiterate one of the points you have already made in your draft instructions, the Four members have assumed that, because of Rover's poor credit rating, none of Holdings, Techtronic or Rover would be able to raise the necessary finance to conclude such a transaction and therefore the opportunity would not arise to them.*"[100].

52. On 31 August 2001 Eversheds sent instructions to Mr Potts for his advice[101]. The instructions reflected the comments Deloitte had made on the draft instructions. Those comments were inaccurate, incomplete and misleading and led to an inaccurate, incomplete and misleading statement being provided to Counsel. The Executive Counsel will rely on the Inspectors' conclusions on this topic[102]. The failure by Mr Einollahi and Mr Barton to correct the instructions and to provide complete information evidences the failure by the Respondents to maintain objectivity and independence.

53. On 10 September 2001 Mr Einollahi and Mr Barton attended a consultation by telephone with Mr Potts during which Mr Potts gave his opinion that the minority shareholders of PVH would experience no unfair prejudice under the proposed

[100] Report para 7.233 – 7.234 ; Email from Caroline Butterfield to Susan Lewis dated 29 August 2001 at 15:51 [Exhibit 30]
[101] Report para 7.236; Email from Susan Lewis dated 31 August 2001 at 17:33 attaching Instructions to Counsel [Exhibit 575]
[102] Inspectors' Report, Chapter VII, para 92 - 94

transaction, based on instructions that were inaccurate, incomplete and misleading[103]. Mr Einollahi, as the senior corporate finance advisor, should have corrected the instructions and ensured that Mr Potts understood the true position. In particular, Mr Einollahi failed to inform Mr Potts that PVH and/or MGRG had the opportunity to make the acquisition and that the Bank of Scotland had expressed a preference for having a group company as its joint venture partner[104].

PVH board meeting 21 September 2001

54. On 21 September 2001 a PVH board meeting was held to consider matters relating to the acquisition of the Rover loan book. The minutes of the meeting were prepared in advance of it being held and on the basis of information provided by Mr Peter Beale[105]. The minutes recorded that the acquisition was being effected by a joint venture between a bank and the Phoenix Four because (i) the PVH Group had experienced difficulty in obtaining finance since May 2000, (ii) the covenants, undertakings and warranties that the deal would require, if done by PVH, would severely restrict the operations of the group and (iii) PVH had been structured to be a manufacturer of motor vehicles and the presence of such a significant liability on its books would affect the company's credit rating and pose a risk to its ability to obtain future financing. These reasons were not true[106] and ignore the fact that Bank of Scotland had expressed a preference for having an MG Rover group company as its joint venture partner. The Executive Counsel will rely on the Inspectors' conclusion that the minutes do not accurately state the reasons the acquisition was being effected

[103] Report para 7.240-7.244 ; Handwritten note of the conference by Maghsoud Einollahi dated 10 September 2001 [Exhibit 115]
[104] Report para 7.245 – 7.246
[105] Report para 7.190; Transcript of evidence of Jane Ruston on 14 June 2006, pp. 34 - 36
[106] Report para 7.193

by a joint venture between a bank and the Phoenix Partnership[107]. The real reason why the transaction was being effected personally by the Phoenix Four was because the Phoenix Four wished to benefit from the transaction and believed it to be "inequitable that they should...be deprived the opportunity to be rewarded for their enterprise"[108]. No such reason was, however, mentioned in the minutes.

MGRG Board meeting 12 October 2001

55. On 12 October 2001 Mr Barton made a presentation on behalf of Deloitte, using slides, to the Board of MGRG, which was required to consider and approve the proposed transaction. The presentation was inaccurate and misleading by reason of the following facts and matters:

(1) By making the presentation to the Board, including reasons why the proposed transaction was in the interest of MGRG, Mr Barton on behalf of Deloitte held Deloitte out, or allowed Deloitte to be treated, as advising the group of companies including MGRG;

(2) The presentation stated that the Phoenix Partnership had entered into discussions with BMW about acquiring Rover Financial Services (GB) Limited ("RFS")[109];

(3) The presentation attributed the decision that the Phoenix Partnership should be the joint venture partner to the fact that "*the existing commercial relationship*

[107] Inspectors' Report, Chapter VII, para 152
[108] Report para 7.138; Handwritten note of meeting with Bank of Scotland on 1 August 2001 [Exhibit 95]; Fax from Maghsoud Einollahi to Alan Christie of Capital Bank dated 16 August 2001 [Exhibit 100];
[109] Report para 7.303

between First National and MG Rover" meant that it was *"not possible"* for MG Rover to enter into a joint venture with another funder to buy the loan book[110]. This was a reference to the operating agreement between MGRG and First National, dated 16 March 2001, under which First National provided finance for dealers and retail customers. However, (i) the negotiations between 31 January 2001, when Ian Barton registered an interest with Deloitte's compliance team regarding acquisition of RFS by "MG Rover"[111], up to at least mid- June 2001[112], had all assumed that the joint venture partner would be an MG Rover group company; (ii) there was no evidence available to Deloitte of any such impossibility arising from the First National Finance contract[113], and; (iii) the real reason for the Phoenix Four being the joint venture partner was the desire of its individual members that profits from it should accrue to each of them directly[114].

(4) The presentation made no mention of the preference of Bank of Scotland (later called HBOS plc[115]) that its JV partner should be an MG Rover group company;

(5) The presentation did not explain that the cash collateral of £43 million to be provided by MGRG on account of and in advance of any liability MGRG may have to pay RFS pursuant to the residual value guarantees (by means of MGRG depositing money in a new fellow subsidiary called RV Capco Ltd ("RV

[110] Report para 7.304; Presentation titled "MG Rover Group – Rover Financial Services – Board Paper" dated 12 October 2001 [Exhibit 22]
[111] Report para 7.401; Email from Ian Barton to Bob Dowsett and others dated 31 January 2001 [Exhibit 169]
[112] Report para 7.363; Email from Ian Barton to Ian Whyte of BMW date 11 June 2001; Inspectors' Report Chapter VII paragraph 41
[113] Report para 7.172 – 7.173; Nigel Birkett notes of meeting with John Edwards and Ian Whyte on 7 February 2001 [Exhibit 428]
[114] Report para 7.138; Handwritten note of meeting with Bank of Scotland on 1 August 2001 [Exhibit 95]
[115] The Bank of Scotland merged with Halifax plc on 10 September 2001 to create a new group, HBOS Plc

Capco") under PVH) meant that the current proposal was radically different from, and far more attractive to financiers than, the discounted book value proposal that BMW had marketed earlier in the year;

(6) The presentation stated that Abbey National plc could not join the bid as funding partner because First National[116] was bidding for the portfolio on their own, without mentioning that Abbey National/First National had in fact submitted a draft offer in competition with Bank of Scotland (having been invited to bid by John Edwards) but were subsequently turned down on the advice of Deloitte[117].

56. The Executive Counsel will rely on the facts set out at paragraphs 7.298 to 7.321 of the Report. The Executive Counsel will also rely on paragraphs 160 – 182 of the Inspectors' Report, including the following conclusions: a) the presentation was principally delivered by Mr Barton b) it was reasonable for those present to take Mr Barton to be speaking on behalf of Deloitte and as an advisor to the MG Rover group, and in particular MGRG c) Mr Barton should have appreciated that the slides and the presentation were deficient and misleading and d) the deficiencies meant that the board was not in a position to make a decision on what was proposed on a fully informed basis and that the directors of MGRG were less likely to challenge the transaction[118].

57. A copy of the slide presentation was later initialled by Mr Einollahi (on 30 October 2001), who knew that the structure of the transaction, including the parties to the joint venture, had arisen based on his own advice to the Phoenix Four. Mr Einollahi has

[116] Then a subsidiary of Abbey National
[117] Report para 7.116 – 7.124.
[118] Inspectors' Report Chapter VII, para 160 – 182; Chapter XXV, para 42.

acknowledged that there was no reason why the deal could not have been done by MG Rover group[119]. However, the ultimate structure of the transaction (as he well knew) was driven by the desire of the Phoenix Four to profit personally [120].

58. In the presentation to the Board the amount of the cash collateral to be provided by MGRG was £43 million, representing £29 million that MGRG had provided in its own accounts (i.e. its own calculation of the total liability for outstanding contracts) plus an additional £14 million to cover the "doomsday scenario" in the event that MGRG became insolvent in May 2002[121]. Deloitte, did not advise MGRG that they were advising the Phoenix Four but by making the presentation to the Board, including reasons why the proposed transaction was in the interests of MGRG, held themselves out or allowed themselves to be treated as advising the group of companies including MGRG. Rather than advising the Board of MGRG that they should obtain independent advice in relation to the proposed transaction, in which MGRG, its directors and beneficial shareholders had competing interests to the Phoenix Four, particularly having regard to the amount of the cash to be set aside by MGRG for the benefit of protecting the joint venture (the Phoenix Partnership's) profits, Deloitte met with MGRG directors and management to discuss the figures, and advised on the final amount, which was set at £41 million[122].

[119] Report para 7.196 – 7.197 ; Witness statement of Maghsoud Einollahi dated 30 May 2008, page 18 paragraph 8.8

[120] Report para 7.138, 7.142 & 7.155 156; Witness statement of Maghsoud Einollahi dated 30 May 2008, page 19, paragraph 8.11

[121] Report para 7.323

[122] Report para 7.327

Benefit to Deloitte, MGRG and the Phoenix Four

59. By the time of the acquisition, the requirement for Deloitte to be paid 5% of the equity had been removed. However the contingent fee element of £7.5 million being paid on completion of the transaction remained in place[123]. As to the circumstances which led to Deloitte's fee being agreed, and the total cost of the assignment at standard charge-out rates, the Executive Counsel relies on paragraphs 7.444 – 7.453 of the Report. In due course the Phoenix Four, together with Mr Howe, made a substantial return on the business, approaching a sum in the order of £12 million net, after deducting the cost of their investment. In addition, large sums were also paid into the Guernsey Trust in connection with Project Platinum[124].

60. The Executive Counsel will rely upon the Inspectors' conclusion that, whilst it was beneficial for MGRG that the RFS loan book should be in "*friendly*" hands, and whilst it might also have been beneficial that the residual value guarantees should be capped, the deal resulted in MGRG losing the ability to use the £41 million transferred to RV Capco to support its (loss-making) day-to-day trading and the cap on MGRG's exposure was of little value since its liabilities were in any event most unlikely to reach the £41 million figure[125]. In reality MGRG had set aside £41 million ring-fenced to cover their future obligations as calculated based on a worst-case scenario, i.e. assuming that they would be insolvent within the year, and reflecting the negative impact on residual values that this scenario would have. MGRG's actual liabilities over the remaining guaranteed contracts in the portfolio were in the end considerably

[123] Report para 7.384; Client Acceptance Form dated 20 September 2001 [Exhibit 393]
[124] Report para 7.21; Inspectors' Report, Chapter VII, paras. 217 – 226
[125] Inspectors' Report, Chapter VII, para 215

less than £41 million set aside, as approximately £24 million was eventually returned to MGRG out of the £53 million set aside in total for RFS/MGRG liabilities[126].

61. The Executive Counsel will also rely upon the Inspectors' conclusion that the returns which were anticipated from Project Platinum can fairly be attributable to a substantial extent to MGRG's £41 million deposit in the RV Capco account: "Since (a) the RV Capco arrangements meant that MGR Capital enjoyed protection against "all the major risks associated with the transaction…even in the severest of downsides" (to adopt the words of Bank of Scotland) but (b) comparable protection was not available to any other potential purchaser, it is not surprising that the transaction was expected to prove a profitable one. Yet MGRG, whose deposit facilitated the transaction, did not share in the returns from it." [127]

62. The Executive Counsel will submit that the evidence demonstrates that the Respondents were, in reality, and at all material times, advancing the transaction for the benefit of the Phoenix Four. As the Inspectors observed, the Phoenix Four were involved in the acquisition of the Platinum loan book because they personally wanted the profits to accrue to them and not for reasons relating to the balance sheets of companies in the Group[128]. However, at no stage did Deloitte or Mr Einollahi advise PVH or MGRG that they were not acting for them in this transaction and that they were advising the Phoenix Four, they did not request informed consent from MGRG to act for the Phoenix Four and did not advise MGRG to seek independent advice notwithstanding:

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[126] Report para 7.211
[127] Inspectors' Report, Chapter VII, para 216
[128] Inspectors' Report, Chapter VII, para 230

(1) The opportunity to acquire the loan book came to MGRG in the first place[129];

(2) The interests of MGRG and the Phoenix Four conflicted in the context of this transaction;

(3) The structure of the MG Rover group was itself unusual, in that the beneficial owners' interests were not strictly aligned with that of the consolidated group or its subsidiaries;

(4) MGRG was a public interest company in distress;

(5) Crucial to the transaction was the deposit, by MGRG of £41 million in an account with RV Capco, the newly formed subsidiary of PVH, so as to provide the purchaser of the loan book with protection against residual value risks. MGRG thereby lost the ability to use the £41 million to support its (loss making) day-to-day trading;

(6) Deloitte had held themselves out, or allowed themselves to be held out, as advising MGRG and PVH on Project Platinum;

(7) Deloitte were MGRG's auditors and had acted, or were acting for MGRG in connection with tax matters and other acquisitions.

[129] The Executive Counsel will rely on the paragraphs 9, 64 – 75 and 196 of Chapter VII the Inspectors Report and the Inspectors' conclusion that there is a strong case for saying that the Platinum opportunity presented itself to the Phoenix Four as directors, whether of MGRG or PVH.

63. In their submissions to the Inspectors the Respondents assert that it is not uncommon in corporate finance transactions for the structure of the transaction to evolve over time and for the purchaser/client to be identified at a later stage. It is said, on behalf of the Respondents, that this "exploratory" stage can sometimes last for several months. In response to which the Executive Counsel will submit as follows:

(1) Whilst there may have been some initial uncertainty as to the vehicle for the acquisition, in reality Deloitte were only ever acting for the Phoenix Four and were advancing the transaction for their benefit;

(2) Further, and in any event, given the facts and matters set out in paragraphs 1 to 62 above, such a process was not appropriate in the circumstances of the MG Rover group of companies.

64. The Respondents also state that, whilst there may have been initial uncertainties as to who was to be Deloitte's client, it will have been clear to all that at no stage was Deloitte acting for MGRG. There was therefore no doubt, it is claimed, that Deloitte did not owe any duties to MGRG. For the reasons set out herein, it is not accepted that it was clear to all that Deloitte was not acting for MGRG. In any event, for the reasons summarised at paragraph 62 above, the conflicts were plainly relevant and gave rise to duties to MGRG under the Guide. Finally, the Respondents also argue that, whilst Deloitte may have had duties to PVH, they did not have any direct duties to the A, B, C shareholders. This argument (a) fails to deal with the facts as set out in this Complaint and in particular the fact that Deloitte and Einollahi were choosing their client and how to benefit their client whilst

leaving MGRG and its shareholders exposed and (b) fails to recognise or deal with the true underlying nature of the professional duties owed by Deloitte and Einollahi under the Guide. In particular the argument ignores the duty which Deloitte and Einollahi had to consider the public interest, and to act with independence and objectivity. A member firm and member of the ICAEW cannot circumvent these duties by choosing to construct a transaction and to act for those who will benefit from the transaction so constructed if in so doing they have failed to consider the public interest, and have failed to act with independence and objectivity.

ALLEGATION 2

Between January 2002 and August 2002 Deloitte and Mr Einollahi advised and acted in relation to a transaction known as "Project Aircraft." The conduct of Deloitte and Mr Einollahi fell short of the standards reasonably to be expected of, respectively, a member firm and a member of the ICAEW in that they:

2.1 Failed adequately to consider the public interest before accepting or continuing their engagement in relation to Project Aircraft (in particular in representing and providing services to the Phoenix Four, PVH and Phoenix Venture Leasing Ltd (formerly MCC Leasing (No. 18) Ltd) and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.200 (paras 2.2, 2.4 and 2.5) and Statement 1.201 (paras 1.1 and 1.4)[130] ;

2.2 Failed adequately to identify and consider potential or actual conflicts of interest between the Phoenix Four, PVH and Phoenix Venture Leasing Ltd (formerly MCC Leasing (No. 18) Ltd) and MGRG (an existing audit and advisory client of

[130] The Executive Counsel relies upon all of the facts below and in particular paras 73 - 77. The facts relied upon to establish that MGRG was a "public interest" company are at paras 8 – 9 above. The facts relied upon to establish that Project Aircraft was not in the best interest of MGRG itself, or its creditors, are at para 69 below

Deloitte and a client on Project Salt/Slag) and other Deloitte clients, namely Barclays Bank plc, Itochu Corporation, Sumitomo Corporation and Thompson Travel Group plc and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.201 (paras 1.1 and 1.5), Statement 1.203 (paras 3.0,) and Statement 1.204 (para 4.0)[131];

2.3 **Failed (i) to make it clear to MGRG that Deloitte did not represent them or act in their interests (ii) to obtain informed consent from MGRG to Deloitte acting for Phoenix Venture Leasing Ltd (formerly MCC Leasing (No. 18) Ltd), the Phoenix Four and/or PVH and (iii) to consider discontinuing with its engagement and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.203 (paras 3.2 and 3.4)[132];**

2.4 **Failed to consider and put in place any or any adequate safeguards as between Phoenix Venture Leasing Ltd (formerly MCC Leasing (No. 18) Ltd), the Phoenix Four, PVH and MGRG, including advising MGRG to seek independent advice, and failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.203 (para 4.0) and 1.204 (paras 4.0 - 4.4)[133];**

2.5 **Wrongly asserted that the letter of engagement dated 26 May 2000 issued in respect of Project Slag was the appropriate letter of engagement for Project Aircraft, and failed to acknowledge that the engagement on Project Aircraft was with a different client with underlying interests that now conflicted with other group entities since the re-structuring, the previous engagement having been prior to the re-structuring. They failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.201 (paras 1.1 & 1.5), Statement 1.203 (para. 3.0), Statement 1.204 (para. 4.0) and with due care, in accordance with Fundamental Principle 4[134];**

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131 The Executive Counsel relies upon all of the facts below and in particular paras 70 – 73. The facts relied upon in relation to the conflict between the Phoenix Four, PVH and MGRG are at para 69. The facts relied upon in relation to the PVH shareholder conflict are at para 27 of Allegation 1

132 The Executive Counsel relies upon all of the facts below and in particular paras 76 - 77

133 The Executive Counsel relies upon all of the facts below and in particular paras 76 - 77

134 The Executive Counsel relies upon all of the facts below and in particular paras 71 – 72. The facts relied upon in relation to the conflict between the Phoenix Four, PVH and MGRG are at para 69. The facts relied upon in relation to the PVH shareholder conflict are at para 27 of Allegation 1

2.6 **Proposed a contingent fee of 15% of the net cash to be received by PVH, which would give rise on completion of the transaction to a fee of approximately £2 million, without (i) giving any or any proper consideration as to whether such a fee was appropriate having regard to the nature of the client's business, the complexity of its operation and the work to be performed, (ii) adequately identifying, considering and safeguarding against the self-interest threat arising from charging a contingent fee and (iii) engaging in proper client engagement acceptance procedures. They failed thereby to act in accordance with Fundamental Principle 2 and the guidance in Statement 1.201 (paras 1.1, 1.4 and 1.5), Statement 1.203 (para 9.0), Statement 1.204 (paras 2.0 – 2.3) and Statement 1.210 (paras. 2.2 and 4.0)[135].**

<u>Particulars</u>

65. The Executive Counsel will rely upon the facts and matters contained in Section 9 of the Grant Thornton Report and the further facts and matters set out below.

66. In May 2000, the Barclays Capital structured finance team approached Deloitte regarding a potential transaction with the MG Rover group. The idea was to enable taxable profits from the Barclays Group to be offset against losses within the MG Rover group. The financial benefit of this transaction, known as Project Salt (or Slag) was to be shared by Barclays Capital and the MG Rover group. An engagement letter was issued on 26 May 2000. It was addressed to Techtronic and stated: "*Following our discussions, we will be pleased to give tax advice to Techtronic (2000) Ltd and its subsidiaries on a proposed structured finance arrangement involving Barclays*

[135] The Executive Counsel relies upon all of the facts below and in particular paras 72

Capital with immediate effect.[136]" The beneficiary of this project was intended to be MGRG. For example, in discussions with the Inland Revenue, Deloitte characterised the project as "*(a) a key element of the funding package currently being put together for Rover and (b) provides positive cashflow in the critical turnaround period*"[137].

67. In October 2000, before the transaction completed, tax legislation was changed and as a result Project Salt was not pursued. It appears to have lain dormant. In early 2002 a further possibility arose for value to be obtained from the use of tax losses at MGRG. On 24 January 2002, Mr Barton emailed Mr Einollahi indicating that he had spoken to Mr Abrahams at Barclays Capital[138]. Mr Abrahams considered that the problems which the parties had encountered on Project Salt might be overcome in relation to Project Aircraft. The proposal was that profits that had inured to the benefit of Barclays Bank in its company MCC Leasing (No. 18) Ltd ("MCCL18") could be set off against tax losses of MGRG. The details of the structure of the proposed arrangement are complicated and are summarised below.

68. In essence PVH acquired MCCL 18, a profitable subsidiary of Barclays engaged in aircraft leasing, thereby bringing it into the same tax group as MGRG. This enabled MGRG's tax losses to be set off against the profits of MCCL18 with the consequent tax savings (some £36 million) being shared between PVH, Barclays Capital and the Lessee[139](i.e. not MGRG).

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[136] Report para 8.6 – 8.8; Engagement Letter from Deloitte to Techtronic dated 26 May 2000, fee [Exhibit 201]
[137] Report para 8.14
[138] Report para 9.21 – Email from Ian Barton to Maghsoud Einollahi dated 24 January 2002 at 10:33 [Exhibit 206]
[139] Report para 9.22

Conflict between the Phoenix Four, PVH and MGRG

69. There was a conflict of interests between the Phoenix Four, PVH, its shareholders and MGRG. The Inspectors found that the transfer of the value of tax losses from MGRG "were of significance to MGRG, particularly since MGRG had negative distributable reserves at the time of the transfers"[140]. However, ultimately, MGRG received no consideration for surrendering its tax losses and no benefit from this transaction (this may be contrasted with the stated intention behind Project Salt) and nor were the Respondents informed that MGRG was to receive any benefit from the scheme. The MG Rover group's share of the returns of Project Aircraft accrued to PVH and its D shareholders and a subsidiary in which MGRG had no interest, and not to MGRG. PVH retained approximately £10.6 million (after professional fees, including £1.995 million plus VAT to Deloitte). PVH thereafter distributed a large proportion of these funds (£7.7 million) to the Guernsey Trust in the form of bonus payments mainly for the benefit of the Phoenix Four[141]. The A, B, C shareholders were not paid any dividend despite the fact that the asset acquired by PVH, being the MGRG tax losses of £122m, were a valuable potential asset as the Inspectors found. The Executive Counsel will also rely on the Inspectors' conclusion that: "the £7.7 million payment [i.e the payment to the Guernsey Trust] can fairly be attributed, at least in large part, to the money received from Project Aircraft[142]" and

[140] Chapter XXIII para 92 of the Inspectors' Report

[141] The Guernsey Trust (or 'the MG Rover Holdings Limited Family Benefit Trust") was consituted by a declaration of trust dated 3 January 2002. During the period 9 May 2000 to 8 April 2005, PVH made payments to the Guernsey Trust totaling £17.03. These trust funds were then allocated to the Phoenix Four, Mr Howe and Ms Ruston (Inspectors' report Chapter XXI paras 14 – 51).

[142] Inspectors' Report, Chapter XI, paras. 17 - 21

that the arrangements were not in the best interest of MGRG itself or of its creditors[143].

Managing conflict

70. The partner in charge of the Project Aircraft engagement was Mr Einollahi, assisted by Mr Barton[144].

71. The client acceptance form completed by Mr Barton on 3 April 2002 identified the client as PVH. However, Deloitte relied on the engagement letter from 26 May 2000 relating to tax advice in respect of Project Salt where the client was Techtronic and its subsidiaries which included MGRG. The client acceptance form was signed by Mr Einollahi on 17 April 2002. His hand written note on the front of the form says. "*This relates to an existing engagement. The form is completed for the sake of good order. No new terms of engagement to be issued*". The form goes on to state that "*PVH [Phoenix Venture Holdings] are an existing CF [Corporate Finance] client. Commercial considerations have been undertaken in previous CF assignments (Panther, Platinum, Lisa)*"[145]. When the Corporate Planning and Completion Checklist was compiled on 12 August 2002 Mr Barton stated in relation to the engagement letter: "NB – letter in force from existing arrangement." Although the letter is referred to as being dated May 2002, this appears to be a reference to Project Salt, the engagement letter for which was dated May 2000[146]. A note on Deloitte's file states that the terms of the Project Salt engagement letter were agreed with Peter

[143] Inspectors' Report, Chapter XI, paras. 61 - 63
[144] Report para 9.33
[145] Report para 9.156 – 9.161; Client Acceptance Form for the Project Aircraft advisory assignment, section 1 [Exhibit 256]
[146] Report para 9.169 - 9.171

Beale as being effective for Project Aircraft[147]. Thus Deloitte advised PVH on the acquisition of MCCL18 under the terms of an engagement letter which specified that Deloitte were to provide their services as tax advisors to Techtronic and their subsidiaries (which included MGRG).

72. The failure to issue a specific engagement letter in relation to Project Aircraft demonstrates a failure by the Respondents to give proper consideration to client identification and conflict checks and, specifically, a failure to consider the potential conflict of interests that had arisen within the MG Rover group as a result of the re-structuring (the Project Salt engagement letter having been issued prior to the re-structuring). It also suggests that the 15% contingency fee (and the self-interest threats inherent within it) which was applied in Project Aircraft was simply imported from the Project Salt engagement letter, without any or any proper consideration being given to whether a such a fee was appropriate. As to the circumstances which led to Deloitte's fee being agreed, and the total cost of the assignment at standard charge-out rates, the Executive Counsel relies on paragraphs 9.169 – 9.175 of the Report.

73. On 15 April 2002 Deloitte completed a conflict form identifying that they would be advising PVH on the acquisition of MCCL18, a subsidiary of Barclays and that MCCL18 leased assets to subsidiaries of Itochu Corporation and Sumitomo, which sub-leased those assets to Thompson Travel Group. Deloitte had client relationships with all these companies[148]. The form did not identify MGRG or the Phoenix Four, each of whom had been clients and/or were the subject of potential conflicts of interest

[147] Report para 9.172; File Note entitled "Project Aircraft – summary"

[148] Report para 9.162 – 9.164; Email from Ian Barton to UK Compliance dated 15 April 2002 at 17:46 attaching a Conflict Form [Exhibit 257]; Compliance form dated 22 April 22 April 2002 [Exhibit 258]; Letter to Peter Beale re: Project Aircraft dated 23 April 2002

(MGRG being a party to the arrangements, albeit not receiving any consideration for the tax losses it surrendered, and the Phoenix Four being the instructing clients albeit through their shareholding in PVH). In reality the transaction was structured to be for the benefit of the Phoenix Four, and Deloitte and Mr Einollahi advised and assisted in the transaction so that it did benefit the Phoenix Four. On 22 April 2002 Deloitte decided that informed consent to act would be required from Barclays Bank plc because of other work which Deloitte was performing for Barclays Bank plc and also from PVH because of other work Deloitte performed for Itochu Corporation, Sumitomo Corporation and Thompson Travel[149]. No consideration was given to the existing relationship with MGRG, or to the conflicts existing within the various classes of ownership of PVH, or to the particular conflicts arising from the fact that the transaction involved the surrender of tax losses by MGRG (for which it received no consideration) for the benefit of the Phoenix Four, or to whether the surrender of tax losses for no consideration was appropriate between group companies when the surrendering company was a public interest company in a parlous financial condition[150].

74. When interviewed by the Inspectors, Mr Einollahi said he had no involvement with discussions over whether MGRG should be paid by the leasing company for the transfer of its losses although he has said that he did discuss the matter with Peter Beale[151]. Mr Einollahi was aware that no consideration would be paid. His view was:

> *"That was an internal matter for the group and not particularly relevant to us obviously...."*

[149] Report para 9.163; Compliance Form dated 22 April 2002 [Exhibit 258]
[150] Report para 9.80 - 81; 9.166 – 9.168
[151] Report para 9.73; Transcript of evidence on 8 June 2007, pages 15, 19, 31, 44 & 71

"...it was of no concern to me ultimately where the benefit sat, in which company. It really did not interest me. What was of concern to me here is my client is asking me to help turn some losses into value... Where they end up in the group is not something which will engage me enormously"[152].

75. Mr Einollahi acknowledged that directors of a (hypothetical) company with tax losses should try to get value for them. However, in respect of MGRG he stated:

"they never sought to have advice and what benefit they could have had out of it. It is a matter for them to have advisers and go and do what they need to do. It is not a matter for me to – I didn't have a relationship with these guys."[153]

76. The surrender of tax losses was not addressed at any stage by the MGRG Board. There was no occasion upon which the directors of MGRG considered whether the proposed arrangements were in the best interests of MGRG and the surrender of tax losses was not in fact approved by the MGRG Board[154]. Deloitte failed to inform MGRG directors or beneficial shareholders that in relation to this transaction they were acting not for, or in the interests of, MGRG, but were instead acting for certain shareholders of PVH (namely the Phoenix Four) in a transaction in which MGRG and the Phoenix Four had competing interests. Deloitte did not therefore obtain properly informed consent to act in this transaction, and nor did they advise MGRG to obtain independent advice.

[152] Report para 9.73; Transcript of evidence on 8 June 2007, pages 19 and 56
[153] Report para 9.77; Transcript of evidence on 8 June 2007, page 41
[154] Inspectors' Report, Chapter XI, para. 42

77. These were clear failures on the part of Deloitte. The question of whether (and, if so, on what basis) tax losses should be surrendered was one on which there was a plain conflict of interest or, at the very least, potential conflict of interest. The Respondents were aware that there was no provision in the proposed transaction for MGRG to receive any benefit from the scheme, and moreover, they were aware of the unusual structure of PVH which meant that there was every possibility that the D shareholders would not pass the proceeds down to MGRG and would instead retain the benefit for themselves. In these circumstances, the need for Deloitte to take steps identified above was obvious.

J M Astley

Alternate Executive Counsel

12th January 2012

Date

ANNEX A

FUNDAMENTAL PRINCIPLES AND STATEMENTS

FUNDAMENTAL PRINCIPLES

Note: all extracts are taken from the 2000 edition of the Guide effective from 1 September 1997 save for wording appearing in square brackets which appears in the 2002 edition of the Guide effective from 1 August 2001

2. A member should strive for objectivity in all professional and business judgments. Objectivity is the state of mind which has regard to all considerations relevant to the task in hand but no other.

4. A member should carry his or her professional work with due skill, care, diligence and expedition and with proper regard for the technical and professional standards expected of him as a member.

STATEMENTS

1.200 INTRODUCTION AND FUNDAMENTAL PRINCIPLES

1. In addition to the duties owed to the public and to his or her client or employer a member of the Institute is bound to observe high standards of conduct which may sometimes be contrary to his personal self-interest. This Guide is an aid to members in the identification of occasions upon which they might be at risk if failing to recognise or conform to any of those standards.

Form and Scope of the Guidance

[1.2 A Chartered Accountant has duties to his client or employer and to the public. His personal self-interest must not prevail over those duties. This Guide helps members fulfil that basic role

Safeguarding Objectivity

2.2 In deciding whether to accept (or continue) an engagement or appointment members and member firms should consider whether their objectivity is, or can be, adequately safeguard in relation thereto. The matters to be considered include:

The expectations of those directly affected (and entitled to be affected) by the work.

The public interest and its bearing on the work.

The threats to objectivity, existing and potential.

The safeguards which are in place, or can be put in place, overt or otherwise, to offset any threats.

The Public Interest

2.4 The term "public interest" relates to matters of public concern, not public curiosity. Public concern extends to the concerns of clients, government, financial institutions, employers, employees, investors, the business and financial community and others who rely upon the objectivity and integrity of the accounting profession to support the propriety and orderly functioning of commerce. This reliance imposes a public interest responsibility on the profession. For example, audit serves the interests of society as well as those of clients. Auditors help to ensure the integrity of the financial institutions in support of loans and to shareholders for obtaining capital. The public confidence is rooted in the objectivity auditors bring to their work. Investors, creditors, employers and other sectors of the business community, as well as government and the public at large, rely on the soundness of reporting by the profession and its impact on the economic well being of their community and country.

2.5 *Members* should therefore take into consideration the public interest and reasonable and informed public perception in deciding whether to accept or continue with an engagement or appointment, bearing in mind that the level of the public interest will be greater in larger entities and entities which are in the public eye.]

1.201 INTEGRITY, OBJECTIVITY AND INDEPENDENCE

1.0 Safeguarding Objectivity

1.1 In order to safeguard their objectivity, members should consider certain matters before deciding whether to accept any appointment. The matters to be considered include those under the following headings:

The expectations of those directly affected (and entitled to be affected) by the work.

The public interest and its bearing on the work.

The threats to objectivity which may arise actually or potentially.

The safeguards which are or can be put in place, overt or otherwise, to offset the threats.

These headings are discussed in more detail in the following paragraphs.

1.2 The responsibility for seeing that the above matters are properly considered resides ultimately, in the case of members in practice, with the engagement partner who takes the responsibility for signing the report for the client concerned. Firms should establish reliable procedures to ensure that these matters are properly addressed.

The public interest and any bearing it has on the work

1.4 The public interest should be a factor which all members should bear in mind when accepting any assignment or appointment.

Threats to objectivity

1.5 Threats to objectivity can arise in a number of ways, some general in nature and some related to the specific circumstances of an assignment or role. Members should identify the threats and consider them in the light of the environment in which they are working; they should also take into account the safeguards which assist them to withstand threats and risks to their objectivity.

1.203 CORPORATE FINANCE ADVICE

Conflicts of Interest

Avoiding Conflicts of Interest

3.0 All reasonable steps should be taken to ascertain whether a conflict of interest exists or is likely to arise in the future between a firm and its clients, both in regard to new engagements and to the changing circumstances of existing clients, and including any implications arising from the possession of confidential information. Relationships with clients and former clients could give rise to the familiarity or trust threat. Before accepting a new appointment such relationships should be reviewed and regularly thereafter. A relationship which ended over two years before is unlikely to constitute a conflict. Where it is clear that a material conflict of interest exists a firm should decline to act as corporate finance adviser.

3.2 Where there appears to be a conflict of interests between clients but after careful consideration the firm considers that the conflict is not material and unlikely to seriously prejudice the interests of any of those clients, the firm may accept or continue the engagement, but not without first informing the clients concerned. Unless security considerations dictate otherwise it would be prudent for this to be in writing.

3.4 Where a conflict of interests is likely seriously to prejudice the interests of a client an engagement should not be accepted or continued even at the informed request of the clients concerned.

Safeguards

4.0 Where a firm acts or continues to act for two or more clients following disclosure in accordance with the previous paragraphs, all reasonable steps should be taken to manage the conflict which arises and thereby avoid any adverse consequences. These steps should include the following safeguards:

a. the use of different partners and teams for different engagements, each having separate internal reporting lines;
b. all necessary steps to prevent the leakage of confidential information between different teams and sections within the firm;
c. regular review of the situation by a senior partner or compliance officer not personally involved with either client; and
d. advising the clients to seek additional independent advice, where it is appropriate.

Fees

9.0 Where a member undertakes an engagement for a fee which is contingent upon the successful outcome of a transaction such as a bid, offer, purchase, sale or raising finance, he or she should take particular care to ensure that the arrangements do not prejudice his or her independence and objectivity with regard to any other role which he or she may have, notably as auditor or reporting accountant of either the bidder or the target. (Members are referred to 1.210, 'Fees').

1.204 CONFLICTS OF INTEREST

Section A - Conflict Between a Firm's Interests and those of its Client

2.0 A self-interest threat to a firm's objectivity will arise where there is or is likely to be a conflict of interest between a firm and its client.

2.1 A test is whether the perception of a reasonable observer at the time would be that the objectivity of the firm is likely to be impaired. The firm should be able to satisfy itself and its client that any conflict can be managed with appropriate safeguards.

Safeguards

2.2 Safeguards will include:

a. disclosure of the circumstances of the conflict;
b. advising the client that, in the particular circumstances, he may wish to seek alternative independent advice;
c. obtaining the informed consent of the client to act.

Disengagement

2.3 Where effective safeguards are not available the firm should refuse or discontinue the particular assignment.

Section B – Conflicting Interests of Different Clients

4.0 A self-interest threat will arise or be seen to arise where the interests of two or more clients are in conflict.

4.1 There is, however, nothing improper in a firm having two clients whose interests are in conflict with each other.

4.2 In such a case the activities of the firm should be so managed as to avoid the work of the firm on the behalf of one client adversely affecting that on behalf of another.

4.3 Where a firm believes that the situation may be managed, sufficient disclosure (see paragraph 4.6 below) should be made to the clients or potential clients concerned together with details of any proposed safeguards to preserve confidentiality and manage conflict.

Safeguards

4.4 Safeguards should include:

a. the use of different partners and teams of staff for different engagements, each having separate reporting lines
b. standing instructions and all other steps necessary to prevent the transfer of confidential information between different teams and sections within the firm;
c. regular review of the situation by a senior partner or compliance partner not person ally involved with either client;
d. advising all the relevant clients that, in the particular circumstances, they may wish to seek alternative independent advice; and
e. obtaining informed consent from all the clients concerned.

1.2010 FEES

Fee Quotations and Estimates

Discussion

2.2 Fee proposals should be made only after proper consideration of the nature of the client's business, the complexity of its operation and the work to be performed.

Percentage and Contingent Fees

4.0 Fees should not be charged on a percentage, contingent or similar basis in respect of audit work, reporting assignments, due diligence and similar non-audit roles incorporating professional opinions and expert witness assignments. Even for other work such methods of charging may be perceived as a threat to objectivity and should therefore only be adopted after careful consideration.