

IN THE MATTER OF

THE EXECUTIVE COUNSEL TO THE FINANCIAL REPORTING COUNCIL

-and-

(1) DELOITTE LLP

(2) [REDACTED]

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**EXECUTIVE COUNSEL'S FINAL DECISION NOTICE**

**Pursuant to Rule 18 of the Audit Enforcement Procedure**

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*This Final Decision Notice is a document prepared by Executive Counsel following an investigation relating to, and admissions made by, the Respondents. It does not make findings against any persons other than the Respondents and it would not be fair to treat any part of this document as constituting or evidencing findings against any other persons or entities since they are not parties to the proceedings.*

**1. INTRODUCTION**

- 1.1. The Financial Reporting Council (the “**FRC**”) is the competent authority for statutory audit in the UK and operates the Audit Enforcement Procedure (the “**AEP**”), effective 17 June 2016. The AEP sets out the rules and procedure for the investigation, prosecution and sanctioning of breaches of Relevant Requirements.
- 1.2. The AEP is a separate procedure to the disciplinary process set out in the FRC’s Accountancy Scheme (effective 8 December 2014) (the “**Scheme**”) which relates to the accountancy profession more generally. The Scheme sanctions, inter alia, acts or omissions that fall significantly short of the relevant standards and behaviour that constitutes Misconduct. The threshold for a breach of a Relevant Requirement under the AEP (an Adverse Finding) is therefore lower than the test for Misconduct under the Scheme in that it is not necessary for breaches of Relevant Requirements to fall significantly short of the standards in order to be sanctionable.

- 1.3. The AEP contains a number of defined terms and, for convenience, those defined terms are also used within this document. This Final Decision Notice also uses the following definitions:
  - 1.3.1. “**FY2015**” means the 52 weeks ended 2 January 2016;
  - 1.3.2. “**2015 financial statements**” means the financial statements of [REDACTED] (“the **Company**”) for FY2015; and
  - 1.3.3. “**2015 Audit**” means the statutory audit of the 2015 financial statements.
- 1.4. Pursuant to Rule 16(b) of the AEP, Executive Counsel has decided that the Respondents (as defined below) are liable for Enforcement Action, having made Adverse Findings against them. This Final Decision Notice is issued pursuant to Rule 18 of the AEP in respect of the conduct of:
  - 1.4.1. Deloitte LLP (“**Deloitte**”) in relation to the 2015 Audit. Deloitte was the Statutory Audit Firm for the 2015 Audit.
  - 1.4.2. [REDACTED], a former partner of Deloitte, in relation to the 2015 Audit. [REDACTED] was the Statutory Auditor of the Company for FY2015 and he signed the Audit report on behalf of Deloitte.
- 1.5. In this Final Decision Notice, Deloitte and [REDACTED] are referred to collectively as the “**Respondents**”.
- 1.6. On 9 September 2020 Executive Counsel issued her Decision Notice pursuant to Rule 17 of the AEP. On 16 September 2020 Deloitte and [REDACTED] provided written agreement to the Executive Counsel’s Decision Notice.
- 1.7. Consequently, in accordance with Rule 18 of the AEP this Final Decision Notice:
  - 1.7.1. outlines the Adverse Findings with reasons;
  - 1.7.2. outlines Sanctions with reasons; and
  - 1.7.3. outlines an amount payable in respect of Executive Counsel’s costs of the matter.
- 1.8. This Final Decision Notice is divided into the following sections:
  - 1.8.1. Section 2: Executive Summary of the Adverse Findings;
  - 1.8.2. Section 3: Background;
  - 1.8.3. Section 4: Relevant Requirements to which the Adverse Findings relate;
  - 1.8.4. Section 5: Detail of the Adverse Findings;

1.8.5. Section 6: Sanctions; and

1.8.6. Section 7: Costs.

## **2. EXECUTIVE SUMMARY OF THE ADVERSE FINDINGS**

- 2.1. At the time of the 2015 Audit, the Company was one of the largest local and regional multimedia organisations in the UK responsible for operating 236 publications and 203 websites. The Company was listed on the main market of the London Stock Exchange and was therefore a Public Interest Entity for the purposes of the AEP. The audit opinion to which this Final Decision Notice relates was signed on 22 March 2016 at which point the Company had a market capitalisation of approximately £43m.
- 2.2. The Company entered into administration on 17 November 2018.
- 2.3. This Final Decision Notice explains the failings in the Respondents' work for FY2015 in respect of its audit of (i) the Company's defined benefit pension scheme ("**DB Scheme**") and (ii) the carrying value of the Company's publishing titles. This Final Decision Notice makes findings regarding the Respondents' audit work, however it does not question the truth or fairness of the 2015 financial statements.

### **Breaches relating to the audit of the DB Scheme**

- 2.4. **Adverse Finding 1:** The Respondents failed to ensure that the review work carried out by the Engagement Quality Control Reviewer ("**EQCR**") was adequately documented. It was not apparent from the audit file how the EQCR reached his conclusions on the judgments made by the audit team in this significant area of audit risk. The Respondents were consequently in breach of paragraphs 8(c) and 9(c) of International Standard on Auditing (UK and Ireland) ("**ISA**") 230. The documentation of the review work carried out by the EQCR more generally (i.e. outside the review of the DB Scheme) was also inadequate.
- 2.5. **Adverse Finding 2:** The Respondents failed to obtain sufficient appropriate audit evidence to substantiate the cash holding of the DB Scheme. The Respondents were consequently in breach of paragraph 6 of ISA 500.

### **Breaches relating to the audit of the carrying value of the publishing titles**

- 2.6. **Adverse Finding 3:** The Respondents failed to perform stress testing of the impairment model used to calculate the impairment charge on a sufficiently disaggregated basis (i.e. by not applying different sensitivities and assumptions for the Company’s different Cash Generating Units (“**CGU**”). The Respondents consequently breached paragraph 6 of ISA 500.
- 2.7. **Adverse Finding 4:** The Respondents failed to adequately consider the extent to which apparent shortfalls in revenue and EBITDA in the first two months following the balance sheet date (as against budget and prior year results) indicated facts and matters that warranted adjustment of the impairment model. The Respondents consequently breached paragraph 6 of ISA 560.
- 2.8. Section 5 of this Final Decision Notice sets out the detailed Adverse Findings relating to the audit work on the matters set out at paragraphs 2.4 – 2.7 above.

### **Sanctions**

- 2.9. This Final Decision Notice also sets out the sanctions in respect of the Respondents:

#### *Deloitte*

- 2.9.1. A financial penalty of £500,000 discounted for admissions and early disposal to £362,500;
- 2.9.2. a published statement in the form of a reprimand; and
- 2.9.3. a non-financial sanction requiring Deloitte to prepare a progress report for the consideration of the FRC’s Audit Quality Review team (“**AQRt**”) setting out its current EQCR work programmes and how such work is documented during the course of the audit of Public Interest Entities.



- 2.9.4. A published statement in the form of a reprimand.

### 3. BACKGROUND

- 3.1. In 2019, Deloitte was the second largest audit firm in the United Kingdom with total fee income of c.£3,427 million of which c.£469 million was derived from audit work.<sup>1</sup> There are 219 responsible individuals within Deloitte entitled to sign audit opinions.<sup>2</sup>
- 3.2. Deloitte was appointed as the auditor to the Company in 2002 and retained that appointment throughout the intervening period. ██████ was the Statutory Auditor for the 2015 Audit and had been the Statutory Auditor for the Company since 2013. ██████ retired from Deloitte in May 2018.
- 3.3. ██████ signed the FY2015 Audit report, on behalf of Deloitte, in respect of the FY2015 financial statements. ██████ was the audit engagement partner for the FY2015 Audit and was responsible for overall audit quality and the direction, supervision and performance of the audit engagement (ISA 220, paragraphs 8 and 15).
- 3.4. The 2015 financial statements were signed on 22 March 2016. Deloitte's audit opinion on the 2015 financial statements was signed by ██████ and was unmodified. As noted above at paragraph 2.3, Executive Counsel does not question the truth or fairness of the 2015 financial statements.
- 3.5. The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. The Respondents' statutory responsibility was to form an opinion as to whether the FY2015 financial statements gave a true and fair view and had been properly prepared in accordance with IFRS and the Companies Act 2006. An audit conducted in accordance with the ISAs and relevant ethical requirements enables the auditor to form that opinion.
- 3.6. On 10 October 2017 the Executive Counsel was directed by the FRC's Conduct Committee to investigate the FY2015 Audit of the Company following a referral from the AQRt. Following the conclusion of the investigation, Executive Counsel served an Initial Investigation Report on the Respondents in accordance with Rule 11 of the AEP which, inter alia, outlined potential breaches of Relevant Requirements. The Respondents

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<sup>1</sup> <https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/about-deloitte/deloitte-uk-2019-audit-transparency-report.pdf>

<sup>2</sup> Page 44: <https://www.frc.org.uk/getattachment/109373d4-abc2-424f-84d0-b80c2cec861a/Key-Facts-and-Trends-2019.pdf>

subsequently provided written representations to the alleged breaches. Executive Counsel has considered those representations, together with all the evidence and documents obtained during the investigation, in making the Adverse Findings in this Final Decision Notice.

#### **4. RELEVANT REQUIREMENTS TO WHICH THE ADVERSE FINDINGS RELATE**

- 4.1. Rule 1 of the AEP states that Relevant Requirements has the meaning set out in regulation 5(11) of the Statutory Auditors and Third Country Auditors Regulations 2016 (“**SATCAR**”). The Relevant Requirements include, but are not limited to, the ISAs, issued by the International Auditing and Assurance Standards Board.
- 4.2. The ISAs relevant to Executive Counsel’s Final Decision Notice are those effective for audits of financial statements for periods ending on or after 15 December 2010.
- 4.3. The Relevant Requirements referred to in this Final Decision Notice are the following:
  - 4.3.1. ISA 230 (Audit Documentation);
  - 4.3.2. ISA 500 (Audit Evidence); and
  - 4.3.3. ISA 560 (Subsequent events).
- 4.4. Extracts from the ISAs setting out those parts which are of particular relevance to the Adverse Findings are set out in Appendix 1 hereto.

#### **5. ADVERSE FINDINGS**

##### **The audit of the DB Scheme**

###### **Background**

- 5.1. The 2015 financial statements reported a deficit in the Company’s pension scheme of £27 million. This represented a substantial reduction compared to the prior year, when the deficit was reported to be £90 million. This reduction in the deficit was largely a result of a change in the underlying mortality assumptions, based on data derived from a health study of members of the pension scheme (“**Health Study**”) prepared by third party actuaries as well as a change in financial assumptions based on a re-evaluation of the discount rate used in measuring the defined benefit liability. Deloitte’s Total Rewards and Benefits Team (“**DTRB Team**”), a specialist pensions team which included qualified actuaries, reviewed the Health Study and discussed its findings with the third

party actuaries. The DTRB Team concluded that the revised mortality assumptions and discounts rate were at the optimistic end of the reasonable range.

**Adverse Finding 1 – Failures in respect of the DB Scheme: Quality control**

**For the reasons set out below, the Respondents failed to adequately document the review work of the EQCR. It was not apparent from the audit file how the EQCR reached his conclusions on the judgments made by the audit team in this significant area of audit risk. The record of the work carried out and the conclusions reached by the EQCR in respect of his review of the wider audit work was also poorly documented. The Respondents thereby breached paragraphs 8(c) and 9(c) of ISA 230.**

5.2. Audit firms are required to put in place quality control systems, policies and procedures for an audit of financial statements. Deloitte’s own review policies and procedures stated that, *“Conducting the Engagement Quality Review in a timely manner at appropriate stages during the engagement allows significant matters to be promptly resolved to the Engagement Quality Control Reviewer’s satisfaction on or before the date of the report”*. Such a process is necessary to enable appropriate revisions to be made or additional procedures to be performed as required.

5.3. The audit of the DB Scheme, and more particularly the assessment of the liabilities under the scheme, was an area of significant audit risk and the EQCR was asked to review the audit work in this area. By way of a report to the audit committee dated 19 February 2016 (**“Report”**), the Respondents confirmed that the substantive work performed on the pension liabilities of the Company was materially complete. The Report stated, inter alia, that:

*“We have considered in detail the mortality and financial assumptions that together decrease the pensions liability by £53 million to £27 million. We believe these assumptions are at the optimistic end of the acceptable scale, but still acceptable”*; and

*“We have concluded on the significant risk area of....pension assumptions”*.

5.4. The EQCR was sent the first draft of the Report, titled *“Status Update to the Audit Committee on the 2015 audit”*, on 18 February 2016, the day before it was due to be distributed to the audit committee and in advance of ██████’s meeting with the audit committee which was scheduled to take place the following week, on 23 February 2016 (**“Audit Committee Meeting”**). This draft included the above comments about the completion of the work on pension liabilities. The EQCR responded stating that he was

not in a position to endorse those comments: *"I have had no background briefing and no sight of documentation and no discussion with our internal expert on this, so it is a tall order being asked to review one slide with 24 hours to dispatch!"*.

- 5.5. The EQCR went on to suggest that the section on Deloitte's assessment of the pension liabilities be removed from the Report. In the event, it was not. ██████ responded to the EQCR's suggestion by stating that *"This is only a status report and while I could remove pensions, it would not go down well given we have been auditing this matter [for] a long time"*. Subsequently, the EQCR reviewed and commented on the Report, and this led to amendments to it being made by the audit team. Some of the amendments related to sections covering the pension issues, with the EQCR stating in an email to ██████ that he was *"happy with the revisions we have agreed to the [Report] as an interim update"*. However, the EQCR was not able to comment substantively on the assessment of liabilities under the DB Scheme as he had not reviewed the underlying material at that time. Notwithstanding this, the wording quoted at paragraph 5.3 above - *"We have concluded on the significant risk area of....pension assumptions"* - was retained in the Report which was then circulated to the audit committee on 19 February 2016. This was in circumstances where, the EQCR had yet to properly consider the Health Study or the memorandum setting out the conclusions of the DTRB Team ("**DTRB Memo**").
- 5.6. Whilst the plain wording in the Report stated that Deloitte had concluded its work on the liabilities of the DB Scheme, ██████ confirmed at an interview with the FRC in relation to the Report and the section on the liabilities of the DB Scheme that, *"We had to make clear [at the Audit Committee Meeting] it was a status report and try to be clear that there was more work to be done"*.
- 5.7. However, there is no record on the audit file of the EQCR's review of the DTRB Memo, nor is there a record of any comments or queries arising out of any such review with the engagement team. There is also no record of any discussions between ██████ and the EQCR on any matters arising out of the Health Study or the DTRB Memo. Although the audit file recorded that the EQCR planned to hold a call with the DTRB Team, and there was a calendar entry for such a call on 22 February 2016 before the Audit Committee Meeting on 23 February 2016, there is no note on the audit file of said discussion or any resulting work. The EQCR himself stated in an internal Deloitte email on 27 February 2016 that he had yet to review the DTRB Memo, but that he intended to do so. The only record of the EQCR's review is his signing off on various work papers on 21 March 2016,



the day before the audit opinion was signed and his confirmation that he was agreeable to the audit opinion being provided.

- 5.8. In light of the matters at paragraphs 5.3 – 5.7 above, it is apparent that the review work of the EQCR was not adequately documented. There is insufficient evidence that the EQCR reviewed any documentation regarding the liabilities of the DB Scheme. At the time the Report was distributed to the audit committee, the EQCR had not considered the underlying material, e.g. the Health Study and the DTRB Memo. In between the date of the Report and the signing of the audit opinion on 21 March 2016, there is no evidence on the audit file of the involvement of the EQCR in discussions with [REDACTED] and the wider engagement team. Nor is there any record of challenges to the conclusions reached and methodologies used throughout the process.
- 5.9. Finally, the record of the work carried out and the conclusions reached by the EQCR in respect of his review of the wider audit work was poorly documented. In this regard, every audit document that was signed off by the EQCR was dated 21 March 2016, the day before the final results of the Company were released. It was therefore not possible to understand from the audit file when the EQCR carried out his review work, the extent of that review or the nature of any challenge to the work done by the audit team.

**Adverse Finding 2 – Failure to obtain sufficient appropriate audit evidence for the cash holding of the DB Scheme**

**For the reasons set out below, the Respondents failed to obtain sufficient appropriate audit evidence to substantiate the cash holding of the DB Scheme in breach of paragraph 6 of ISA 500.**

- 5.10. The balance of the cash holding of the DB Scheme amounted to approximately £4 million. Whilst this represented approximately 1% of the assets of the DB Scheme, nevertheless it was a material balance and well in excess of the audit materiality threshold of £1,350,000. The Respondents were required to obtain sufficient appropriate audit evidence to substantiate this material balance and in order to obtain reasonable assurance that the financial statements were not materially misstated.
- 5.11. The Respondents obtained an email from the scheme actuaries who noted that the cash balance figure was provided to them by the plan administrators of the DB Scheme. Although the scheme actuaries were independent of the Company, they did not have either sight of, or control over, the DB Scheme bank account.

5.12. The email from the scheme actuaries was therefore not adequate third-party corroboration for this material balance. The Respondents failed to design and perform appropriate audit procedures for the purpose of obtaining sufficient appropriate audit evidence. The Respondents should have obtained a direct confirmation from the plan administrators and/or sight of the scheme bank statement.

### **The audit of the carrying value of the publishing titles**

#### **Background**

5.13. The intangible assets of the Company comprised the publications and websites referred to at paragraph 2.1 above. For the purposes of financial reporting, in the 2015 financial statements, these were grouped into six geographical areas, referred to as CGUs. The 2015 financial statements included a £35 million impairment charge against the value of four of those CGUs. This impairment charge was calculated by the Company using an impairment model. This model reduced the carrying value of the applicable CGUs from £511 million at the end of the prior year, to £476 million as at the balance sheet date of 2 January 2016.

### **Adverse Finding 3 – Failure to conduct the stress testing of the impairment model on a disaggregated basis**

**For the reasons set out below, the Respondents failed to conduct the stress testing of the impairment model on a sufficiently disaggregated basis in breach of paragraph 6 of ISA 500.**

5.14. The Respondents were required to obtain sufficient appropriate audit evidence to corroborate the impairment reviews performed by the Company. The Respondents conducted stress testing of the impairment model by adjusting the underlying assumptions consistently across all six CGUs.

5.15. Certain components of the CGUs failed to meet their respective budget targets in 2015 by varying degrees. The extent to which the components of the CGUs missed budget was variable – for example, the revenue shortfall compared to budget was between 4.8% (Isle of Man) and 11.5% (South Yorkshire), while the operating profits shortfall was wider still at between 11.4% (West Yorkshire) and 32.6% (Midlands). Similar variations between the CGUs were shown at the EBITDA level. The Company's different revenue streams also had different growth profiles – for example, traditional advertising and

circulation revenues were subject to markedly different growth profiles to those for digital revenues.

- 5.16. In view of the factors set out at paragraph 5.15 above and also considering that a significant impairment had already been booked by the Company, the stress testing of the impairment model should have been conducted on a disaggregated basis. The audit work carried out was not precise enough since different sensitivities were not used for different revenue streams that were predicted to move in opposite directions in the budgeted numbers (for example, with the digital revenues forecast to increase but print revenues forecast to decrease). Nor were different sensitivities used for CGUs that had shown different variations to budget at revenue and operating profit levels for a number of previous periods.
- 5.17. The Respondents thereby failed to obtain sufficient appropriate audit evidence in respect of its stress testing of the Company's impairment model.

**Adverse Finding 4 – Failure to carry out adequate work on post balance sheet events**

**For the reasons set out below, the Respondents failed to perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements had been identified in breach of paragraph 6 of ISA 560.**

- 5.18. It was necessary for the Respondents to carry out a review of post balance sheet events and to identify their impact on any aspect of the audit. The Respondents did carry out such a review and recorded that there was:
- 5.18.1. a negative variance of 8.8% against budgeted EBITDA for January 2016;
  - 5.18.2. a negative variance of 5.8% against budgeted revenue for January 2016; and
  - 5.18.3. a negative variance in the total revenues for the two months to 28 February 2016 against the corresponding period in the prior financial year of 13% - that compared to a budgeted annual fall in total revenues for the full year of 5.4%.
- 5.19. As a consequence of the post balance sheet events work, an additional contingency of 4% of EBITDA, mainly to factor in further falls in revenue, was built into the impairment model. However, the audit file does not explain why the Respondents considered that additional contingency to be sufficient. The Respondents should have undertaken

further evidential analysis to determine whether the contingency adjusted impairment model did or did not warrant a greater contingency given the actual experience of the business in the first two months of the year, which showed a negative variance in excess of the additional contingency (see paragraph 5.18 above). No such further analysis was undertaken as it should have been. The post balance sheet events review was therefore not appropriately completed.

## **6. SANCTIONS**

6.1. Paragraph 10 of the FRC's Sanctions Policy (Audit Enforcement Procedure) (the "**Policy**") provides that Sanctions are intended to be effective, proportionate and dissuasive. The reasons for imposing Sanctions are identified in paragraph 11 of the Policy as the following:

6.1.1. to declare and uphold proper standards of conduct amongst Statutory Auditors and Statutory Audit Firms and to maintain and enhance the quality and reliability of future audits;

6.1.2. to maintain and promote public and market confidence in Statutory Auditors and Statutory Audit Firms and the quality of their audits and in the regulation of the accountancy profession;

6.1.3. to protect the public from Statutory Auditors and Statutory Audit Firms whose conduct has fallen short of the Relevant Requirements; and

6.1.4. to deter Statutory Auditors and Statutory Audit Firms from breaching the Relevant Requirements relating to Statutory Audit.

6.2. Paragraph 12 of the Policy provides that the primary purpose of imposing Sanctions for breaches of the Relevant Requirements is not to punish, but to protect the public and the wider public interest.

6.3. In reaching her decision on Sanctions, Executive Counsel has, in summary, considered the following matters in accordance with the Policy.

### Nature, seriousness, gravity and duration of the breaches

6.4. The breaches of Relevant Requirements were not pervasive as regards the wider audit work. However, the breaches did relate to the efficacy of the EQCR process (Adverse Finding 1), and failures to obtain sufficient appropriate audit evidence in relation to a

material balance (Adverse Finding 2) and in an area of significant audit risk (Adverse Findings 3 & 4).

- 6.5. Although this Final Decision Notice does not question the truth or fairness of the 2015 financial statements and it is not alleged that any actual loss was suffered by any third parties as a result of the breaches, the breaches of Relevant Requirements undermine confidence in the standards of conduct in general of Statutory Auditors and Statutory Audit Firms, and/or in Statutory Audit.
- 6.6. The internal review and quality procedures applied at Deloitte were ineffective to prevent the breaches of the Relevant Requirements outlined in this Final Decision Notice.
- 6.7. Executive Counsel considers that the same types of breaches could re-occur in the absence of remedial action (to which see further below).
- 6.8. In 2019, Deloitte was the second largest audit firm in the United Kingdom with revenue of c.£3,427 million (of which c.£469 million was for audit). Deloitte's total audit fee for the 2015 Audit was £430,000.
- 6.9. The breaches of Relevant Requirements relate to only one audit year.
- 6.10. The breaches were neither intentional, dishonest, deliberate nor reckless.

#### Identification of Sanction

- 6.11. Having assessed the nature, seriousness, gravity and duration of the breaches, Executive Counsel has identified the following combination of Sanctions as appropriate for Deloitte:
  - 6.11.1. a fine of £500,000;
  - 6.11.2. a published statement, in the form of a reprimand, to the effect that Deloitte contravened Relevant Requirements in the 2015 Audit; and
  - 6.11.3. a non-financial sanction, in the form of an order pursuant to rule 96(c) of the AEP, requiring Deloitte to prepare a progress report for the consideration of the AQRt setting out how under its current EQCR work programmes such work is documented during the course of the audit of Public Interest Entities, such report to be provided within three months of the date of this Final Decision Notice.
- 6.12. Having assessed the nature, seriousness, gravity and duration of the breaches, Executive Counsel has identified the following combination of Sanctions as appropriate for [REDACTED]:

6.12.1. A published statement, in the form of a reprimand, to the effect that [REDACTED] contravened Relevant Requirements in the 2015 Audit.

6.13. In reaching this conclusion, Executive Counsel has taken into account any aggravating and mitigating factors that exist (to the extent that they have not already been taken into account in relation to the nature, seriousness, gravity and duration of the breaches).

#### Deloitte

#### Mitigating factors

6.14. Deloitte has taken the following remedial action in relation to the failures identified in the Adverse Findings:

6.14.1. In accordance with new Deloitte guidance on the testing of pension plan assets, Deloitte independently verified and recalculated the valuation of the sample pension assets, including bank balances during the AQRt review of June 2016.

6.14.2. In May 2017 Deloitte issued an EQCR Practice Aid and process flow, setting out the enhancements made to the EQCR process. Further, in November 2018 Deloitte introduced a new template entitled the "EQCR team Documentation of Challenge and Resolution". The EQCR teams now have to document their key challenges during the planning stage and at year end and how they were resolved. Also, any key discussions have to be documented within the template.

6.14.3. In relation to the audit of the carrying value of the publishing titles, in the following audit year (for the 52 weeks ending 2 January 2017) the stress testing of the impairment model was carried out on a disaggregated basis for each CGU by each revenue and cost lines.

6.14.4. For audits taking place on or after 31 December 2017, Deloitte has introduced a new "*Impairment Smarter Review Template*" for impairment reviews which aims, inter alia, to improve the documentation of the subsequent events work to the work on the impairment model.

6.15. Whilst Deloitte were paid an audit fee for the engagement (see paragraph 6.8 above), they did not stand to gain any profit or benefit from the breaches.

#### Aggravating factors

6.16. Deloitte has been sanctioned twice in the past four years for failings in relation to audits:

6.16.1. In November 2016, Deloitte was fined £4 million and issued with a severe reprimand for Misconduct<sup>3</sup> in relation to its audit of Aero Inventory (UK) Limited for the financial years ending 2006, 2007 and 2008.

6.16.2. In February 2019, Deloitte was fined £6.5 million (reduced to £4,225 million for settlement) and issued with a severe reprimand for Misconduct in relation to its audit of Serco Geografix Limited for the financial years ending 2011 and 2012.

6.17. These prior cases relate to Misconduct under the Scheme, and not breaches of Relevant Requirements under the AEP (see further at paragraph 1.2 above).

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#### Mitigating factors

6.18. ██████████ has over 30 years of auditing experience and during this time has an unblemished disciplinary record.

6.19. Whilst Deloitte were paid an audit fee for the engagement (see paragraph 6.8 above), ██████████ did not stand to gain any profit or benefit from the breaches.

#### Aggravating factors

6.20. There are no aggravating factors in respect of ██████████.

#### Deterrence

6.21. Having considered the matters set out at paragraphs 72 and 73 of the Policy, Executive Counsel considers that no adjustment for deterrence is required in this case.

#### Discount for Admissions and Settlement

6.22. Having taken into account the admissions by Deloitte and the stage at which those admissions were made (at a point within Stage 1 of the case in accordance with paragraph 84 of the Policy), Executive Counsel determines that a discount of 27.5% is appropriate, such that a financial penalty of £362,500 is payable. This sum is to be paid by Deloitte no later than 28 days after the date of this Final Decision Notice

6.23. Executive Counsel notes that the AQRt carried out an inspection of aspects of the 2015 Audit during July 2016. Following that inspection and Deloitte's own causal factual analysis of the findings, ██████████ was subject to a financial penalty amounting to £10,000

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<sup>3</sup> As defined in the FRC's Accountancy Scheme dated 8 December 2014.

by Deloitte's Audit Quality Remuneration Committee. Executive Counsel considers that it would not be fair or proportionate to impose any further financial penalty on [REDACTED].

Other considerations

6.24. In accordance with paragraph 47(c) of the Policy, Executive Counsel has taken into account the size / financial resources and financial strength of Deloitte and the effect of a financial penalty on its business.

**7. COSTS**

7.1. Executive Counsel requires that the Respondents make a contribution to the FRC's costs in this matter, amounting to £150,000. Such costs shall be paid no later than 28 days after the date of this Final Decision Notice.

**Signed:**

[REDACTED]

**CLAUDIA MORTIMORE**

**DEPUTY EXECUTIVE COUNSEL**

**Date: 17 September 2020**



## **APPENDIX 1 – EXTRACTS OF RELEVANT REQUIREMENTS**

1. Paragraph 8 of ISA 220 states that “*The engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned.*”
2. Paragraph 15 of ISA 220 states that “*The engagement partner shall take responsibility for (a) the direction, supervision and performance of the audit engagement in compliance with professional standards and applicable legal and regulatory requirements, and (b) the auditor’s report being appropriate in the circumstances*”.
3. Paragraph 8 of ISA 230 states that, “*The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand....(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions*”.
4. Paragraph 9 of ISA 230 states that, “*In documenting the nature, timing and extent of audit procedures performed, the auditor shall record....(c) who reviewed the audit work performed and the date and extent of such review*”.
5. Paragraph 6 of ISA 500 states that “*The auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence*”.
6. Paragraph 6 of ISA 560 in relation to “*Subsequent Events*” states that “*The auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor’s report that require adjustment of, or disclosure in, the financial statements have been identified*”.