IN THE MATTER OF

THE EXECUTIVE COUNSEL OF THE FINANCIAL REPORTING COUNCIL

-and-

(1) HW FISHER LLP

(2) SIMON MOTT-COWAN

FINAL SETTLEMENT DECISION NOTICE

Pursuant to Rule 108 of the Audit Enforcement Procedure

28 MAY 2026

This Final Settlement 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 in June 2023. The AEP sets out the rules and procedures for the investigation, prosecution and sanctioning of breaches of *Relevant Requirements*.

1.2 The AEP contains a number of defined terms and, for convenience, those defined terms are also used within this document. Where defined terms from the AEP are used, they appear in italics.

1.3 This *Final Settlement Decision Notice* concerns breaches of *Relevant Requirements* arising from the *Statutory Audit* of the financial statements of Liberty Commodities

Limited ("**LCL**")[1] for the year ended 31 March 2020, performed by HW Fisher LLP, and uses the following definitions:

1.3.1 "**FY20**" means the financial year beginning 1 April 2019 and ending 31 March 2020. "**FY20 Audit**" means the *Statutory Audit* of the financial statements of LCL for FY20. "**2020 Financial Statements**" means LCL's financial statements for FY20.

1.3.2 the "**Auditor's Report**" means the independent auditor's report on the 2020 Financial Statements, signed on 24 September 2020.

1.3.3 the "**Respondents**" means:

1.3.3.1 HW Fisher LLP ("**HWF**") which was the *Statutory Audit Firm* for the FY20 Audit. The FY20 Audit was in fact carried out by HW Fisher, a general partnership. By an agreement dated 22 February 2021, the business of the general partnership was transferred to HW Fisher LLP with effect from 1 March 2021, and HW Fisher LLP assumed the liabilities of the partners of HW Fisher. Where appropriate, references to HWF include HW Fisher (the general partnership).

1.3.3.2 HWF is a member firm of the Institute of Chartered Accountants in England and Wales ("**ICAEW**").

1.3.3.3 Simon Mott-Cowan ("**Mr Mott-Cowan**") was the Senior *Statutory Auditor* responsible for the FY20 Audit. He is a partner of HWF and was at all material times a member of the ICAEW.

1.4 Quotes from documents in this *Final Settlement Decision Notice* are verbatim and "*sic*" is not used.

1.5 Unless stated otherwise, references in this document to dollar or $ amounts are to US dollars.

1.6 In accordance with Rule 102 of the AEP, Executive Counsel entered into settlement discussions with the Respondents.

[1] On 10 April 2025, LCL changed its name to 3349135 LTD. For the purposes of this *Final Settlement Decision Notice*, LCL is used.

1.7 A *Proposed Settlement Decision Notice* was issued pursuant to Rule 103 of the AEP in relation to the conduct of the Respondents in respect of the FY20 Audit. The Respondents provided written agreement to the *Proposed Settlement Decision Notice*, pursuant to Rule 105 of the AEP, on 18 May 2026. The *Convener* subsequently appointed an *Independent Reviewer*, pursuant to Rule 106 of the AEP, to consider the *Proposed Settlement Decision Notice*.

1.8 On 22 May 2026, the *Independent Reviewer* approved the issuance of this *Final Settlement Decision Notice* pursuant to Rule 107(a) of the AEP.

1.9 This *Final Settlement Decision Notice* sets out:

1.9.1 the breaches of *Relevant Requirements*, with reasons;

1.9.2 the *Sanctions* imposed on the Respondents, with reasons; and

1.9.3 the amount payable by the Respondents in respect of Executive Counsel's Costs.

1.10 In the interests of proportionality, Executive Counsel did not investigate all aspects of the FY20 Audit. No comment is made as to the adequacy of the audit work undertaken in other areas.

1.11 This *Final Settlement Decision Notice* is divided into the following sections:

1.11.1 Section 1: Introduction

1.11.2 Section 2: Executive Summary;

1.11.3 Section 3: Background;

1.11.4 Section 4: *Relevant Requirements* to which the breaches relate;

1.11.5 Section 5: Detail of the breaches of *Relevant Requirements*;

1.11.6 Sections 6 and 7: *Sanctions*; and

1.11.7 Section 8: Costs.

2. EXECUTIVE SUMMARY

2.1 Insofar as those areas of the FY20 Audit that have been investigated by the FRC are concerned, the Respondents failed to comply with *Relevant Requirements* in that, amongst other things, they failed to comprehend the fundamental and inherent risks in LCL's business model and failed to properly conduct adequate audit procedures. These issues stem from a pervasive and fundamental lack of professional skepticism running throughout all areas of the FY20 Audit investigated by the FRC.

2.2 Section 5 of this *Final Settlement Decision Notice* sets out the detailed breaches of *Relevant Requirements*. In summary, there were breaches of *Relevant Requirements* in seven areas of the audit work:

2.2.1 Understanding of the entity.

2.2.1.1 The Respondents' work to understand the entity and its environment was insufficient and demonstrated a lack of professional skepticism and a failure to respond appropriately to obvious risks, both within the audit file and those being discussed in the media at the time of the FY20 Audit.

2.2.1.2 Further, despite LCL's business model being overwhelmingly reliant on two sources of finance, the audit work done to understand the relevant financial agreements was superficial and inadequate.

2.2.1.3 As a consequence of the Respondents' failure to obtain an adequate understanding of the entity and its environment, they failed to, amongst other things: (a) properly identify and assess the risk of material misstatement in the financial statements; and (b) design audit procedures that were appropriate for the purpose of obtaining sufficient audit evidence about the financial agreements to enable them to draw reasonable conclusions upon which to base their audit opinion.

2.2.2 Derecognition of assets.

2.2.2.1 An important area of accounting judgment was how to account for the receivables that were payable from customers under the terms of the sale contracts entered into by LCL and whether the associated financing would have to be recognised by LCL as a liability. As at the end of FY20, the financing under two Receivables Purchase Agreements ("**RPAs**") amounted to almost $1 billion. It therefore may have been desirable for LCL not to recognise the financing liabilities. In order to achieve that it would be necessary to derecognise the related trade receivables.

2.2.2.2 LCL derecognised the underlying trade receivables purchased from it through the RPAs, and LCL did not recognise any financing liabilities under the RPAs.

2.2.2.3 The Respondents performed an ineffective audit of this arrangement. The Respondents failed, amongst other things, to: (a) perform audit procedures to evaluate whether the overall presentation of the financial statements was in accordance with the requisite standards and (b) obtain sufficient audit evidence to draw reasonable conclusions upon which to base their opinion in relation to the derecognition of assets and related liabilities.

2.2.3 Recoverability of trade debtors.

2.2.3.1 At FY20 year-end, LCL's trade debtor balance was $180,842,691 and recoverability of debtors was evaluated as a significant risk. It was therefore a critical part of the audit process to obtain sufficient appropriate audit evidence as to the risk of trade debtors being materially misstated.

2.2.3.2 Despite the significant risk posed by the recoverability of trade debtors, the Respondents failed to audit this area properly and showed a lack of professional skepticism with regard to documentation provided.

2.2.3.3 Further, the Respondents failed to maintain control over the debtor confirmation process and failed adequately to perform alternative audit procedures where this was required.

2.2.4 Recoverability of intercompany balances.

2.2.4.1 Intercompany debtors totalled $48,738,639 of the $239,792,552 debtors' total at FY20 year-end and were therefore material.

2.2.4.2 The Respondents assessed recoverability of intercompany balances as a significant risk on account of the age of the debtors and historic difficulties in reconciling the balances. However, there were numerous shortcomings in the Respondents' audit work, including a failure to control the confirmation process, a failure to plan or execute procedures relating to balance assignments and a failure to plan or implement any procedures designed to gain an understanding of LCL's controls.

2.2.5 Revenue recognition.

2.2.5.1 Revenue recognition is a high-risk area of the audit, with the ISAs (as defined below) stating that there is a rebuttable presumption of fraud risk in revenue on every audit. The Respondents identified revenue recognition as a significant risk, with both a high likelihood of material misstatement and high financial impact.

2.2.5.2 However, the Respondents failed, amongst other things, to design and perform audit procedures, appropriate in the circumstances, for obtaining sufficient audit evidence for completeness of revenue and failed to evaluate whether the information provided by LCL was sufficiently reliable for their purposes.

2.2.6 Journals testing.

2.2.6.1 Journals are used for recording standard non-recurring transactions, non-routine transactions and adjustments to the accounting records. They can therefore be used to manipulate financial

statements. Accordingly, the ISAs describe journal entries as a high-risk area and include a number of mandatory requirements.

2.2.6.2 Overall, the Respondents' work on journals testing was insufficient lacked professional skepticism, and demonstrated a failure to understand and respond to the risk properly. The Respondents failed, amongst other things to: (a) obtain an understanding of the controls relating to journal entries; (b) evaluate whether the information provided by LCL was sufficiently reliable for their purposes; and (c) failed to carry out planned audit procedures without recording in audit documentation the fact or reason why the procedures were not carried out.

2.2.7 Going concern.

2.2.7.1 The 2020 Financial Statements were prepared by management on a going concern basis. It was a critical part of the FY20 Audit for the Respondents properly to assess the decision of management to prepare the financial statements on this basis.

2.2.7.2 In their Auditor's Report, the Respondents gave an unqualified opinion confirming that use of going concern accounting was appropriate, and that they were satisfied that there were no material uncertainties that required disclosure.

2.2.7.3 However, the inadequate audit work throughout the rest of the audit, combined with a lack of professional skepticism, culminated in an inadequate assessment of management's adoption of the going concern basis in the preparation of the financial statements. Further, the Respondents failed adequately to consider whether there was a material uncertainty as to going concern, and whether that ought to be disclosed in the financial statements.

3. BACKGROUND

The Respondents

3.1 At the time of the FY20 Audit, HWF was a top 30 UK chartered accountancy firm, with no Public Interest Entity[2] audits. It had 27 partners and an annual turnover of £28,559,403. HWF audited LCL from 1998 and resigned in 2021. In October 2024, the trade and assets of HWF were acquired by a group providing professional services. The Responsible Individuals who were registered with HWF at the time of the acquisition (including Mr Mott-Cowan) re-registered with a company within that group which provides audit services and carried on that part of that company's audit business that trades as "HW Fisher Audit". Mr Mott-Cowan ceased his practice as a *Statutory Auditor* in January 2026.

3.2 The FY20 Audit team comprised six people, including Mr Mott-Cowan (the Audit Partner) and an Engagement Quality Control Review Partner (the "**EQCR**"). As noted above, Mr Mott-Cowan was the Senior *Statutory Auditor*. Mr Mott-Cowan was also the Senior *Statutory Auditor* for the financial periods ending 31 December 2017, 31 March 2019 (change of year-end) as well as 31 March 2020.

LCL

LCL's business

3.3 During the FY20 Audit, LCL was a UK incorporated private limited company and therefore not a Public Interest Entity within the meaning of that term in Regulation 2 of The Statutory Auditors and Third Country Auditors Regulations 2016 ("**SATCAR 2016**"). At that time, LCL had a sole director and shareholder (the "**Shareholder**").

3.4 LCL was part of a group structure, in which the ultimate holding company was registered in Singapore and was wholly owned by the Shareholder. This group structure was part of the wider GFG Alliance, which included entities under the control of the Shareholder and another member of his family.

[2] A Public Interest Entity is defined as: (a) an issuer whose transferable securities are admitted to trading on a UK regulated market; (b) a credit institution (c) a person who would be an insurance undertaking – see FRC's Glossary at https://www.frc.org.uk/library/enforcement/glossary/

3.5 LCL's business was described in the 2020 Financial Statements as the physical trading, supply chain, and logistics management of non-ferrous metals, semi-finished steel, and raw materials required for steel making.

3.6 The majority of sales made by LCL were "back-to-back", meaning that LCL would purchase materials from a supplier (the "**Supplier**") only when onward sale of the same goods to a customer (the "**Customer**") had been agreed. In FY20, 25% of transactions (1.2% of the sales by value) were "unmatched" in that LCL's purchase had no corresponding onward sale at the time of the purchase. Whilst the volume and value of unmatched transactions was relatively low, they significantly exceeded audit materiality of $2.5m.

3.7 In the 2020 Financial Statements, LCL reported a turnover of $4,224,006,395. Costs of sales for FY20 were $4,136,739,711, giving a gross profit of $77,229,831 (and gross profit margin of 2.07%). However, once the interest costs relating to financing were included ($68,430,466), the profit reduced to $9,534,040 (or 0.21% of revenue). It was therefore a very low margin business. For example, non-recovery of only 4% of the debtor balance at year-end would make the entity loss-making.

3.8 The majority of the trading revenues were externally financed. The principal variable costs, apart from cost of sales themselves, were the interest costs on that financing, which increased from $52.7m in the financial year ending 31 March 2019 ("**FY19**") to $68.4m in FY20. In FY20, interest costs increased to 89% of operating profit.

3.9 The overwhelming majority of the facility limits (94%) was provided by either Greensill Capital (UK) Limited ("**Greensill**") or Wyelands Bank Plc ("**Wyelands**"). Greensill was a private limited company incorporated in the UK. Wyelands was part of the GFG Alliance and beneficially owned by the Shareholder and his family.

3.10 The Greensill and Wyelands facilities provided LCL with receivables-based supply chain financing. The agreements were intended to allow for LCL receiving early payment from Greensill or Wyelands of an invoice it had issued to a Customer. LCL would pay a fee for this service. The Customer would then settle the payment with Greensill or Wyelands when the invoice became due. The Greensill and Wyelands facilities were each provided under separate agreements referred to as RPAs. A

diagram setting out a worked example of the stages of a Greensill 'back-to-back' transaction according to the terms of the Greensill RPA is set out at Appendix 1.

3.11 LCL's operations were extremely reliant on the external finance from Greensill and Wyelands. Accordingly, an understanding of these facilities (and in particular, the nature of the contractual obligations thereunder) was fundamental to the FY20 Audit.

3.12 However, the Respondents, amongst other things, failed to identify the risks associated with this business model and failed to understand, and to conduct adequate audit procedures on, the obligations imposed on LCL under the RPAs. Consequently, the Respondents conducted the FY20 Audit without a proper understanding of how the financial arrangements with Greensill and Wyelands operated, which, as set out in section 5, had significant ramifications for several aspects of the FY20 Audit, including derecognition of assets and going concern.

3.13 Greensill entered into administration on 8 March 2021. Whilst LCL remains on the Companies register, it has not filed accounts since Greensill entered into administration.

The Auditor's Report

3.14 HWF conducted the FY20 Audit between July and September 2020.

3.15 In the Auditor's Report, signed by Mr Mott-Cowan on24 September 2020, the Respondents expressed an unqualified opinion that the 2020 Financial Statements gave a true and fair view of the state of LCL's affairs as at 31 March 2020 and of its profits for that year. The Respondents also stated on going concern that there were no material uncertainties that the directors had failed to disclose in the financial statements that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date the financial statements were authorised for issue.

4. RELEVANT REQUIREMENTS

4.1 Rule 1 of the AEP states that *Relevant Requirements* has the meaning set out in Regulation 5(11) of SATCAR 2016.

4.2 The *Relevant Requirements* applicable to the FY20 Audit include, but are not limited to, the International Standards on Auditing (UK) issued by the FRC (the "**ISAs**").

4.3 This *Final Settlement Decision Notice* refers to the following *Relevant Requirements* in force at the time of the FY20 Audit.

4.3.1 ISA (UK) 200 (Revised June 2016) Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing;

4.3.2 ISA (UK) 220 (Revised June 2016) (Updated July 2017) Quality Control for an Audit of Financial Statements;

4.3.3 ISA (UK) 230 (Revised June 2016) Audit Documentation;

4.3.4 ISA (UK) 240 (Revised June 2016) (Updated July 2017) The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements;

4.3.5 ISA (UK) 250 Section A (Revised December 2017) – Consideration of Laws and Regulations in an Audit of Financial Statements;

4.3.6 ISA (UK) 300 (Revised June 2016) Planning an Audit of Financial Statements;

4.3.7 ISA (UK) 315 (Revised June 2016) Identifying and Assessing the Risks of Material Misstatement Through Understanding the of Entity and its Environment;

4.3.8 ISA (UK) 330 (Revised July 2017) The Auditor's Response to Assessed Risks;

4.3.9 ISA (UK) 500 (Updated July 2017) Audit Evidence;

4.3.10 ISA (UK) 505 (Updated July 2017) External Confirmations;

4.3.11 ISA (UK) 520 (June 2016) Analytical Procedures;

4.3.12 ISA (UK) 530 (June 2016) Audit Sampling;

4.3.13 ISA (UK) 550 (June 2016) Related Parties; and

4.3.14 ISA (UK) 570 (Revised June 2016) Going Concern.

4.4 Under the AEP, as the *Statutory Audit Firm* responsible for the FY20 Audit, HWF is responsible for any established breaches of *Relevant Requirements* on the part of its partners or employees. Consequently, the conduct of HWF's employees and partners described in the *Final Settlement Decision Notice* is to be treated as the conduct of HWF for the purpose of establishing any breaches of *Relevant Requirements*.

4.5 As the *Statutory Auditor* responsible for the FY20 Audit, Mr Mott-Cowan was responsible for the overall quality of the FY20 Audit and the direction, supervision, and performance of the FY20 Audit in compliance with the professional standards and applicable legal and regulatory requirements.

5. BREACHES OF RELEVANT REQUIREMENTS

Breach Area 1: Understanding of the entity and assessment of risks

Relevant Requirements

5.1 ISA (UK) 200, paragraph 15.

5.2 ISA (UK) 220, paragraph 12.

5.3 ISA (UK) 230, paragraph 8.

5.4 ISA (UK) 240, paragraphs 12, 15, 18, 42 and 44.

5.5 ISA (UK) 250A paragraphs 16, 19 and 20.

5.6 ISA (UK) 315, paragraphs 11, 25 and 29.

5.7 ISA (UK) 500, paragraph 6.

Overview

5.8 It is essential for auditors to understand the entity and its environment (including the entity's internal controls relating to significant risks) in order to identify and assess the risk of material misstatement in the financial statements.

5.9 Whilst the Respondents carried out audit procedures on each of the areas discussed in this chapter, the work was insufficient and demonstrated a lack of professional skepticism and a failure to respond appropriately to obvious risks, both within the audit file and those being discussed in the media at the time of the FY20 Audit.

5.10 Further, despite LCL's business model being overwhelmingly reliant on two sources of finance, being Greensill and Wyelands, the audit work done to understand the relevant financial agreements was superficial and inadequate.

Matters relevant to the FY20 Audit

(i) The Greensill RPA

5.11 As at FY20 year end, Greensill provided facilities pursuant to an RPA that had been in place from November 2019 (the "**Greensill RPA**"). The Greensill RPA represented approximately 82% of the total external financing provided to LCL as at the end of

FY20. Greensill financing of LCL trading was estimated to be in excess of $3 billion for FY20.

5.12 The key features and operational effect (in simplified terms with illustrative figures) of the Greensill RPA are set out in paragraphs 5.13-5.22 below. See Appendix 1 for a graphical representation of this example.

5.13 A sale of materials would be made by LCL to the Customer for a fixed price (for example, $20m) (see step 3 in Appendix 1) and LCL would submit a request to Greensill to purchase a receivable in that amount (see step 5 in Appendix 1).

5.14 Greensill would only purchase "Eligible Receivables" as defined by the Greensill RPA. This included the requirement that the receivable was valid, current and enforceable against the debtor. Acceptance of a request obliged Greensill to purchase the receivable.

5.15 Upon acceptance, Greensill would remit the "Initial Purchase Price" for the receivables to LCL (see step 6 in Appendix 1). This was calculated as the "Net Invoice Amount"[3] deducted by a "Loss Rate"[4] of 10%. This gave an "Expected Amount" recoverable ($18m). This would then be further reduced by a "Discount Rate"[5] (of 5% - $1m in this example), leaving the net total amount advanced to LCL as financing ($17m).

5.16 If the sums collected from the Customer by or on behalf of Greensill exceeded the Expected Amount (see step 9 in Appendix 1), then an "Additional Purchase Price" equal to the additional amount paid up to the loss rate amount ($2m) would be paid by Greensill to LCL (see step 11 in Appendix 1). Accordingly, the maximum amount LCL could receive under the Greensill RPA would be the Initial Purchase Price (see paragraph 5.15 above) plus the Additional Purchase Price. However, in practice, this

[3] The amount of the purchased receivable shown on the invoice for the receivable as payable by the debtor including VAT, less (i) any discounts, credits or other allowances shown on such invoice, and (ii) any withholding tax applicable on payment of the receivable which has been approved by Greensill.

[4] To reflect the risk that the invoice would not be paid by the Customer, producing the "Expected Amount" recoverable.

[5] Representing a further interest deduction for provision of the financing and an allowance for the credit risk of the Customer.

maximum amount would only be recovered if LCL's Customer paid the receivable in full.

5.17 The facility limit (described in the agreement as a "*maximum OPP*") was set at $527,500,000, unless otherwise agreed between the parties in writing. It was a condition precedent of the agreement that LCL could not submit a request to Greensill to purchase a receivable if the "*aggregate OPP*" (the total amounts outstanding for receivables purchased under the Greensill RPA) exceeded the "*maximum OPP*". A breach of the maximum OPP would be a breach of the terms and conditions of the agreement.

5.18 The Greensill RPA stated that Greensill was purchasing "*all of [LCL's] right, title and interest*" but none of LCL's underlying obligations to the relevant Customer. Further, Greensill's purchase was stated as being made "*without recourse*" to LCL should an LCL Customer fail to pay the receivable. The agreement noted that LCL "*shall have no liability*" to Greensill for any such failure and described the arrangement as "*an absolute, unconditional and irrevocable sale*", noting that both Greensill and LCL agreed to treat each receivable purchase as a "'*true sale*' *for all purposes under applicable law and accounting principles*".

5.19 This "*without recourse*" or "*true sale*" was, however, expressly subject to sections 5 and 6 of the Greensill RPA.

5.20 Under section 5, LCL retained responsibility for collecting the amounts due under the purchased receivables and arranging for them to be paid into an LCL account which was secured in favour of Greensill (the "**Greensill Collection Account**"). As "servicer" under the Greensill RPA, LCL was subject to a number of obligations relating to the collection of sums due to Greensill, including the following:

5.20.1 Identifying, matching and reconciling all payments received in respect of the purchased receivable and ensuring that they were paid into the Greensill Collection Account within the time specified in the Greensill RPA.

5.20.2 Conducting a weekly reconciliation of funds credited to the Greensill Collection Account with all outstanding purchased receivables and providing a reconciliation report to Greensill.

5.20.3 Contacting Customers where receivables were overdue and reporting to Greensill the reasons for non-payment of their invoice.

5.21 Section 6 of the agreement set out the events described as being an "*event of repurchase*", which were divided into two categories:

5.21.1 The first related to circumstances where any representation or warranty made by LCL in relation to a purchased receivable was incorrect when it was made. This could include matters such as inadvertent incorrect information about whether the receivable was eligible for purchase under the agreement.

5.21.2 The second related to failures in the operation of the agreement or issues relating to payments in relation to the purchased receivables. LCL would be obliged to repurchase the affected receivables if any of the following circumstances occurred:

5.21.2.1 There was a "*dispute*" or "*dilution*" arising in respect of a purchased receivable. Dispute was defined widely to include a threatened dispute, irrespective of whether or not it was *bona fide*. A dilution meant any reduction in the amount paid or payable by a Customer even where this arose from a billing error.

5.21.2.2 LCL failed to "*perform or observe any other term or covenant under [the Greensill RPA] with respect to any of the purchased receivables*". Thus, a breach of any of the terms of the Greensill RPA by LCL could result in an obligation on LCL to buy the affected receivables back from Greensill.

LCL instructed a Customer not to make a payment with respect to a purchased receivable or to make a payment to an account other than the Greensill Collection Account.

5.22 The effect of the section 6 provisions was that LCL was at risk of being obliged to repurchase any receivable in circumstances where payment was not made in full in accordance with the payment terms. Given that LCL remained responsible for

collections, the effectiveness of the Customer collection process and associated reconciliation process was critical to avoiding an event of repurchase occurring.

5.23 The agreement could be terminated at 90 days' notice by either party on a no-fault basis. This meant that LCL's guaranteed financing period with Greensill was no longer than 90 days.

(ii) *The Wyelands RPA*

5.24 Wyelands provided facilities to LCL in FY20 under an RPA dated 17 June 2019 (the "**Wyelands RPA**"). The key features and operational effect (in simplified terms) of the Wyelands RPA are set out in paragraphs 5.25-5.35 below.

5.25 LCL would submit a request to Wyelands to purchase the receivables described in the request. Each time LCL made a request to Wyelands, it was representing and warranting that certain representations and warranties were true, including that LCL had "*complied in all material aspects with applicable laws, rules and regulations (including anti-money laundering …laws and regulations)*".

5.26 Wyelands' acceptance of a request obliged it to purchase the receivables described. The Wyelands RPA required that each invoice was "*properly and validly issued in accordance with the relevant Contract*".

5.27 Upon acceptance, Wyelands would pay LCL the relevant "Purchase Price". This was, in essence, a percentage of the invoice amount (the "**Covered Portion**"), less a discount rate.[6] The Covered Portion meant Wyelands only purchased a maximum percentage of each invoice (ranging from 40% - 90% for invoices outstanding at the year-end[7]). LCL retained the risks (including the risk of non-payment) and rewards in relation to the remaining part of each invoice (the "**Seller's Portion**").

5.28 The Wyelands RPA set out approved Customers and applied specific discount rates, payment periods and Covered Portions for each Customer. There was a "Buyer Limit" for each approved Customer, which was the maximum value of receivables that

[6] Calculated by reference to LIBOR and the payment period for the invoice as well as an interest margin to factor in credit risk.
[7] See paragraph 5.97 *et seq.*

Wyelands agreed to buy of a particular Customer's invoices (i.e. the maximum aggregate amount Wyelands could purchase in respect of a particular Customer).

5.29 The combined effect of the operation of the Buyer Limits and Covered Portion meant that the proportion of the invoice purchased by Wyelands could vary significantly. Further, each receivable was effectively purchased on bespoke terms depending on who LCL's Customer was. Reconciling payments made to LCL under the Wyelands RPA to individual invoices purchased by Wyelands was inherently complex.

5.30 In order for a receivable to be eligible for purchase, it was a condition that LCL had to direct its Customers to pay the amounts due under the invoice into an account (referred to in this *Final Settlement Decision Notice* as the "**Wyelands Collection Account**").

5.31 The Wyelands RPA provided that LCL may, from time to time, act as "*agent and trustee*" for Wyelands in relation to the collection and receipt of payments for purchased receivables. Where LCL so acted, it was subject to a number of obligations, including:

5.31.1 To ensure payments received by LCL in respect of receivables purchased under the Wyelands RPA were paid into a specified account, and to hold the Covered Portion of those payments on trust for Wyelands, and to pay them over to Wyelands in accordance with the timescales set out in the agreement.

5.31.2 An obligation to promptly notify Wyelands if all or any part of a purchased receivable was not paid in full on its due date.

5.32 LCL undertook to keep and maintain accurate and up-to-date sales records which could indicate which receivables had been purchased under the agreement and the details of those receivables. It also undertook to notify Wyelands of any breach by a Customer of the payment terms of a purchased receivable, and any non-payment of any receivable.

5.33 Wyelands was stated to have "*no recourse*" to LCL in respect of the Covered Portion of a purchased receivable which was unpaid other than if a "*recourse event*" occurred

or if LCL failed to comply with its obligations as the collection agent. The recourse events included:

5.33.1 Any representation or warranty made by LCL in relation to a purchased receivable being untrue when it was made or LCL breaching any of its undertakings or obligations under the agreement.

5.33.2 LCL failing to transfer funds to Wyelands, for example, where LCL was acting as a collection agent.

5.34 The facility limit was $125,643,000. A breach of that limit would be a breach of the terms and conditions of the agreement, as would any breach of the Buyer Limits for each of the Customers.

5.35 The agreement could be terminated at 30 days' notice by either party on a no-fault basis. This meant that LCL's guaranteed financing period with Wyelands was no longer than 30 days.

(iii) *The Newspaper Articles*

5.36 Prior to the commencement of the FY20 Audit, Mr Mott-Cowan read three articles in the press regarding the nature of Wyelands' financing of the GFG Alliance and the GFG Alliance's relationship with Greensill:

5.36.1 A Financial Times article dated 27 September 2019 noted that "*[the Shareholder's] business empire is still heavily reliant on opaque and unconventional financing linked to working capital and supply chains that can be expensive*". It noted that Wyelands had "*attracted scrutiny*" in relation to its financing of the Shareholder's businesses and that much of GFG's Alliance's "*complex funding*" was via Greensill.

5.36.2 A second article dated 24 February 2020, also in the Financial Times, noted that it appeared that Wyelands had worked around restrictions which limited the amount of core capital that could be lent to related parties "*by routing transactions that financed GFG's companies and assets through a series of seemingly independent intermediaries*". Some of these intermediaries were said to be akin to "*shell companies*".

5.36.3 A third article in The Times, dated 15 March 2020, stated that "*Wyelands has been used to pump cash into a string of businesses that appear related to [the Shareholder's] empire under the GFG Alliance*" and that "*some of [the Shareholder's] companies appear to show an aggressive approach to accounting…*". It also asserted that Greensill's exposure to GFG Alliance businesses put it at growing risk but also notes that Greensill itself claimed that its exposure was minimal[8].

5.37 While none of the articles mentioned or made allegations in respect of LCL specifically, they nevertheless raised issues which were relevant to the FY20 Audit, including:

5.37.1 the appropriateness of the practices of companies controlled by the Shareholder of advancing financing through Wyelands, which (as Mr Mott-Cowan was aware) was one of the main lenders to LCL;

5.37.2 concerns about the companies controlled by the Shareholder adopting "*aggressive*" accounting practices; and

5.37.3 a practice of relying (inappropriately) on passing money through shell companies.

Audit Work

(i) *Client Continuance Assessment*

5.38 The Respondents noted in the audit documentation that "*there [were] no reasons to question the client's integrity*". However, there is no record of the discussions, considerations and conclusions underlying the assessment.

5.39 As to the newspaper articles (see paragraph 5.36 above), there is no evidence on the audit file of any assessment or analysis of the first and third article. Whilst the second article dated 24 February 2020 was discussed in an email exchange between Mr Mott-Cowan and the Senior Audit Manager on 25 February 2020, the analysis of the potential implications for the audit was limited.

[8] The article also notes that Greensill itself claimed that its exposure was minimal.

5.40 Further, the audit file contains no record of any discussion with the Shareholder (or other LCL personnel) about matters relating to the allegations made in the media against the GFG Alliance, or whether those matters had the potential to impact the auditor's assessment/impressions/evaluation of the Shareholder's integrity.

5.41 Mr Mott-Cowan's overall conclusion, as recorded in the audit file, was that "*taking into account issues arising during prior audits for this client, I am satisfied that…there is no reason to doubt the integrity of the client's principal owners and managers*." Mr Mott-Cowan further explained in interview with the FRC that he had seen no evidence of "*anything untoward"* when HWF were performing the audits of LCL.

(ii) <u>*Assessment of risks*</u>

5.42 ISA 315 defines "significant risk" as "An identified risk of material misstatement: (i) For which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the degree to which inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur; or (ii) That is to be treated as a significant risk in accordance with the requirements of other ISAs."[9]

5.43 The Respondents identified 16 significant risks in the risk register. However, the Respondents failed to identify controls in relation to five of the risks, namely recoverability of inter-company balances, provisions, banking covenants, recoverability of trade debtors, and taxation.

5.44 Furthermore, two risks, relating to laws and regulations and impairment of fixed assets, which had been identified by the group auditor of LCL's parent company and added to the risk register were removed from the register because the Senior Audit Manager and Mr Mott-Cowan considered that the risks were not "*significant risks."* No explanation was given in the audit file for why these risks were not significant risks for LCL, particularly in the context of the allegations made against companies controlled by the Shareholder in the media.

[9] ISA 315 (Revised July 2020), paragraph 12(l).

(iii) *HWF's understanding of potential fraud and issues of non-compliance with laws and regulations ("NOCLAR") within LCL*

5.45 Whilst the record of the audit team's discussion in relation to fraud noted that Mr Mott-Cowan considered the audit team needed to be "*more mindful and sceptical over the potential for fraud*", there was no further explanation as to why he considered this to be the case. The record of the discussion does not explain how and where LCL's financial statements may be susceptible to material misstatement due to fraud. Further, the record does not indicate that there was any discussion of any allegations of fraud that had come to HWF's attention, including in particular the allegations in the newspaper article of 24 February 2020 (which the Respondents were aware of) that (i) certain GFG Alliance companies appeared to be transacting with shell or dormant companies, (ii) there were allegations of using third-party intermediaries to work around lending criteria and (iii) allegations of the use of aggressive accounting.

5.46 The audit team's initial discussion with LCL regarding the risk of fraud drew attention to the Shareholder's day to day involvement in running the business as the sole director of LCL. Notwithstanding this, the Respondents did not raise the allegations made in the newspaper articles against companies controlled by the Shareholder and the GFG Alliance with LCL. The conclusion on fraud risk was that "*risk of fraud is considered low, but the team will remain alert for the possibility of any fraudulent transactions occurring*".

5.47 As to NOCLAR, it was noted in the audit file that "*the company runs business through its associated group companies but due to the transfer pricing rules have started to run trades through non associated business partners (meaning businesses [which] are not connected by controlling parties or ownership so not related parties but both parties have informal understandings)*."

5.48 This information, on its face, indicated there was a risk that LCL was not complying with transfer pricing rules. Further, the practice of running transactions through third party (non-associated) intermediaries is a well-known technique used in money laundering schemes.

5.49 However, there is no evidence on the audit file that this indication of NOCLAR was identified, nor that the statement above was critically assessed with any professional skepticism, particularly given similar practices had been described as being used by third party intermediaries to provide funding to GFG Alliance businesses by circumventing lending criteria (see paragraph 5.36.2.)

(iv) *HWF's understanding of LCL's business operations*

5.50 The audit file notes Mr Mott-Cowan's description of LCL as a commodity trader that predominantly undertakes back-to-back sales, such that "*the volatile markets under which they sell their commodities do not adversely affect stock which is held by the company for long periods of time*". It further records Mr Mott-Cowan's understanding of the business model that "*[due] to the back to back transactions, this is a low risk business so margins are low to reflect the lower risk… High volume business with low profit margins*".

5.51 This represented a superficial understanding of LCL's business model. As set out above, LCL's gross profit margin in the FY20 Financial Statements was 2.07%, and its overall profit was only $9.5m (representing 0.21% of the revenue of $4.2bn). Accordingly, small events (such as non-payment or part payment by debtors) could have an effect on LCL's profitability more quickly than in a business with a larger profit margin.

(v) *HWF's understanding of LCL's financing*

5.52 As noted above, the majority of LCL's trading (94%) was externally financed via Greensill and Wyelands. There was thus a significant concentration of funding with two institutions.

5.53 The following key implications of LCL's financial arrangements are to be noted.

5.54 Firstly, the use of an RPA, with its associated interest costs is an expensive way to finance a low margin business. To understand the entity, it was necessary not only to understand the commercial reason why LCL was using this form of financing, but also to consider whether it indicated that LCL could not obtain other forms of financing and, if so, to critically assess what that inability might indicate about LCL.

5.55 Further, it was inherently risky for LCL to have such high exposure to these two main finance providers, committed only for 30 and 90 days respectively. This was particularly so in circumstances where:

5.55.1 The Respondents were specifically aware of concerns that had been raised in the media as to whether the financing activities of Wyelands were appropriate. There was therefore a risk that the Wyelands financing would be withdrawn; and

5.55.2 There was no evidence or basis for assuming that if either Greensill or Wyelands ceased to provide finance, alternative arrangements could be found elsewhere in the market, particularly in light of the public concerns raised in the media about the companies controlled by the Shareholder and his "aggressive" accounting practices.

5.56 In addition, it was critical – in order to understand the entity and business operations of LCL – for the Respondents to understand the Greensill and Wyelands RPAs, given that they imposed obligations on LCL and set out consequences that could flow from breach of the agreements.

5.57 Notwithstanding the importance of the Greensill and Wyelands RPAs as set out above, HWF's workpaper on general knowledge of business information made no reference at all to the extent of LCL's dependence on financing from Greensill and Wyelands.

(vi) *HWF's understanding of the Greensill RPA*

5.58 The Greensill RPA was described in the audit file as a "*factoring agreement*" and "*true sale*", with the "*risks and rewards…transferred to Greensill*". It further noted that LCL continued *"to handle collection from the debtors"* on Greensill's behalf and was obliged to remit the collected funds promptly to Greensill. However, LCL "*had no obligation"* to Greensill for "*slow payment or non-payment by the debtors"*. This was the only consideration on the audit file that LCL was acting as a collection agent on behalf of Greensill.

5.59 As to the facility limit, whilst it was noted that the Greensill RPA included a condition precedent that "*the aggregate OPP must not exceed the maximum OPP which is*

stated as $527,500,000", there was no analysis of the impact of that condition precedent and the obligations it imposed on LCL. As set out above, a breach of the *maximum OPP* would be a breach of the terms and conditions of the agreement (with potential implications for LCL's access to future financing from Greensill) and amount to a breach of a finance covenant.

5.60 The audit filed noted that the total amount factored at the FY20 year-end was "*$879*" (million) and that this was "*greater than the maximum OPP per the agreement of $527.5m"*. Further, that no formal extension had been made to the *maximum OPP* under the RPA. The only evidence of a limit increase obtained by HWF was a letter from Greensill dated 2 September 2020 which stated that the *maximum OPP* as at the FY20 year-end was $880,000,00. There was no contemporaneous evidence of the limit change. Furthermore, the audit file contained no analysis as to whether or not the facility had been breached during FY20.

5.61 It was further noted that Greensill's purchases of the receivables were made "*without recourse*". Whilst HWF purported to analyse the circumstances in which the non-recourse clause was disapplied pursuant to sections 5 and 6 of the Greensill RPA, the analysis was superficial and incomplete, with the incorrect conclusion that "*debtors are without recourse*".

5.62 In particular, HWF did not document that the Greensill RPA specified that an event of repurchase could occur if LCL failed to "*perform or observe any other term or covenant"*. This would include a breach of the facility limit of the RPA which the working paper noted had not been formally extended (as was required under the RPA). Nor did the analysis consider any of the obligations that LCL became subject to under the agreement by virtue of the fact that it acted as servicer (including carrying out collection duties) under the agreement. Further, HWF did not consider that the obligation to repurchase could, in certain circumstances, also arise in relation to dilution, not just dispute.

5.63 The consequence of the foregoing was that the Respondents' understanding of the Greensill RPA, which was critical to LCL's business, was superficial and inadequate. This resulted in an inability to perform an adequate audit.

(vii) *HWF's understanding of the Wyelands RPA*

5.64 It was noted in the audit file that the Wyelands RPA was "*non-recourse*". However, the Respondents failed to perform any meaningful analysis over the terms of the RPA, including to understand whether the agreement was, in fact, non-recourse.

5.65 They also failed to consider:

5.65.1 Whether LCL acted as a collection agent in FY20.

5.65.2 The impact of the difference between the Covered Portion and the Seller's Portion, and whether both of these were paid into the Wyelands Collection Account (despite Wyelands only having rights over the Covered Portion), and the mechanism by which LCL would receive its Seller's Portion.

5.66 In respect of both the Greensill and the Wyelands RPAs, the Respondents failed to perform any audit work to ensure that the receivables being purchased were, in fact, eligible to be purchased under the terms of the agreement (see, for example, paragraphs 5.14 and 5.26 above). This audit work was essential because both RPAs contained clauses which meant that if certain untrue representations or warranties were made about receivables, this amounted to a recourse event.

Breaches of *Relevant Requirements*

5.67 In breach of paragraph 12 of ISA (UK) 220, Mr Mott-Cowan failed to ensure that appropriate procedures regarding the acceptance and continuance of the audit engagement had been followed and that the conclusions reached were appropriate in that:

5.67.1 As Mr Mott-Cowan was aware, the Shareholder was the sole director of LCL, and allegations had been made in the public domain regarding the conduct of companies controlled by the Shareholder;

5.67.2 Mr Mott-Cowan failed to obtain adequate information to rebut allegations in the public domain regarding GFG which was relevant to the integrity of the client in order to determine that the conclusions reached were appropriate;

5.67.3 In particular, the Respondents failed to gain any responses from LCL and/or the Shareholder to the (a) allegations contained in three newspaper articles which, on their face, appeared to impact on the business reputation of companies all controlled by LCL's principal owner; (b) the allegation that other companies controlled by the Shareholder appeared to show "*an aggressive approach to accounting*"; and (c) allegations that shell and dormant companies were being inappropriately used as third-party intermediaries to finance GFG Alliance companies.

5.68 In breach of paragraph 42 of ISA (UK) 240, the Respondents failed to communicate to those charged with governance matters related to fraud which were relevant to their responsibilities in that the Respondents failed to discuss the risk that LCL may have been circumventing transfer pricing legislation or matters raised in the three newspaper articles, despite serious allegations being made about the business practices of companies controlled by the Shareholder, which were relevant considerations about management's integrity.

5.69 In breach of paragraph 8 of ISA (UK) 230, the Respondents failed to document the exercise of their judgment to continue the engagement, and their consideration of the integrity of the client. In particular:

5.69.1 The Respondents failed to document all three newspaper articles and their consideration of them on the audit file.

5.69.2 Mr Mott-Cowan's thought process and exercise of judgement as described in his interview with the FRC (see paragraph 5.41 above) was not documented on the audit file.

5.70 In breach of paragraph 15 of ISA (UK) 200, the Respondents failed to exercise professional skepticism when:

5.70.1 Planning the audit and conducting the risk assessment in that the Respondents failed to consider whether, in light of the allegations considered as part of the client continuance assessments above, there was a risk arising from the Shareholder's ownership of LCL.

5.70.2 Reviewing LCL's financing arrangements in that the work undertaken was superficial in that the Respondents failed to gain an adequate understanding of the operation of the Greensill and Wyelands RPAs.

5.71 In breach of paragraph 11(b) of ISA (UK) 315, the Respondents failed to obtain an adequate understanding of LCL and its environment and, in particular, the nature of LCL's financing arrangements. Notwithstanding the significance of the Greensill and Wyelands RPAs to LCL's financing, the Respondents failed adequately to understand how the Greensill and Wyelands RPAs operated in practice, and the obligations those agreements placed on LCL.

5.72 As a consequence of the Respondents' failure to obtain an adequate understanding of the entity and its environment, in breach of paragraph 25 of ISA (UK) 315, they failed to properly identify and assess the risk of material misstatement at the financial statement and assertion level.

5.73 As a consequence of the Respondents' failure to obtain an adequate understanding of the entity and its environment and to properly identify and assess the risk of material misstatement at the financial statement and assertion level, the Respondents, in breach of paragraph 6 of ISA (UK) 500, failed to design audit procedures that were appropriate for the purpose of obtaining sufficient audit evidence as to the operation of the Greensill and Wyelands RPAs to enable the Respondents to draw reasonable conclusions upon which to base their audit opinion. The Respondents failed to design audit procedures to obtain audit evidence about, amongst other things:

5.73.1 Whether the receivables being purchased under the RPAs were being purchased in accordance with the terms of the agreements.

5.73.2 Whether there was a risk of the lender requiring LCL to repurchase certain receivables.

5.73.3 LCL's performance of its obligations in respect of the collection of sums due to Greensill and Wyelands.

5.73.4 The documentation and agreement of facility increases in accordance with the terms of the RPAs.

5.74 In breach of paragraph 29 of ISA (UK) 315, the Respondents failed to understand LCL's controls relevant to five of the 16 significant risks identified in the FY20 Audit.

5.75 In breach of paragraphs 15 and 44 of ISA (UK) 240, the Respondents failed to:

5.75.1 Adequately discuss and record how and where LCL's financial statements may be susceptible to material misstatement due to fraud, including how fraud might occur.

5.75.2 Bring the discussion about the allegations made against companies controlled by the Shareholder in media articles to the audit team's attention.

5.76 In breach of paragraph 18 of ISA (UK) 240, the Respondents failed to make effective inquiries within LCL to determine whether LCL had knowledge of any actual, suspected or alleged fraud affecting the entity in that the Respondents did not ask LCL about the specific allegations made in the newspaper articles against companies controlled by the Shareholder and the GFG Alliance.

5.77 In breach of paragraph 12 of ISA (UK) 240, the Respondents failed to maintain professional skepticism in relation to the possibility that a material misstatement due to fraud could exist. Whilst Mr Mott-Cowan noted the need to be "*more mindful and sceptical over the potential for fraud"*, in fact the Respondents did not exercise skepticism about matters pertaining to fraud risk. In particular, the Respondents failed to:

5.77.1 Consider the allegations that indicated there was a risk of GFG Alliance companies transacting with shell or dormant companies, and a risk that third party intermediaries might be used as a route to finance GFG Alliance companies.

5.77.2 Exercise any professional skepticism about whether there was a read across from these allegations which might indicate a fraud risk for LCL.

5.77.3 Give meaningful consideration to whether there was domination of management by the Shareholder without compensating controls.

5.78 In doing so, the Respondents also breached paragraphs 16, 19 and 20 of ISA (UK) 250A, in that they failed to:

5.78.1 Remain alert to the possibility that other audit procedures applied may bring instances of non-compliance or suspected non-compliance with laws and regulations to their attention.

5.78.2 Having become aware of information concerning an instance of non-compliance or suspected non-compliance with laws and regulations, obtain a sufficient understanding of the nature of the act and its circumstances, and obtain further information to evaluate the possible effect on the financial statements.

5.78.3 Discuss the potential non-compliance or suspected non-compliance with laws and regulations with management or those charged with governance.

Breach Area 2: Derecognition of Assets

Relevant Requirements and Accounting Standards

5.79 FRS 102, paragraph 11.33.

5.80 ISA (UK) 200, paragraphs 15 and 17.

5.81 ISA (UK) 230, paragraph 8.

5.82 ISA (UK) 330, paragraph 24.

Overview

5.83 The management of LCL prepared its financial statements under the financial reporting standard FRS 102.

5.84 An important area of accounting judgment in applying this financial reporting standard was how to account for the receivables that were payable from Customers under the terms of the sale contracts entered into by LCL. These receivables were "financial assets" which had to be reported on LCL's balance sheet unless derecognised under paragraph 11.33 of FRS 102.

5.85 In light of the requirements of FRS 102, the key question for the Respondents was whether or not the RPAs resulted in the transfer of "*substantially all*" of the risks and rewards of ownership. Where an entity has not transferred substantially all of the risks and rewards of an asset to another party, that asset cannot be derecognised.

5.86 Therefore, if LCL had not transferred substantially all of the risks and rewards of the receivables purchased from it under the Greensill and Wyelands RPAs, the receivables could not be derecognised. Furthermore, some or all of the financing from Greensill and Wyelands would have to be recognised by LCL as a liability.

5.87 As at the end of FY20, the financing under the Greensill and Wyelands RPAs amounted to almost $1 billion. It therefore may have been desirable for LCL not to recognise the financing liabilities, but to achieve that it would be necessary to derecognise the related trade receivables. LCL derecognised the underlying trade receivables purchased from it through the RPAs on the basis that substantially all the risks and rewards of the trade receivables had been transferred to Greensill and Wyelands.

5.88 Consequently, LCL did not recognise any financing liabilities under the RPAs on the basis that there would be no recourse to LCL in respect of the Greensill and Wyelands financing. As both Greensill and Wyelands did not forward LCL the entire amount equivalent to the debtor invoices purchased, the portions retained by both financial institutions were recognised as trade debtors (an asset) by LCL.

5.89 The Respondents performed an ineffective audit of those financial arrangements, and failed, amongst other things, to obtain sufficient audit evidence that the RPAs had transferred substantially all of the risks and rewards of ownership to Greensill and Wyelands.

Audit Work

(i) The Greensill RPA

5.90 In their audit documentation, the Respondents considered the accounting treatment of trade debtors, and noted in relation to the Greensill RPA that whilst LCL continued to handle debt collection, it had "*no obligation to [Greensill] for slow payment or non-payment by the debtors.*" The Respondents concluded that LCL had "*therefore… transferred to the bank substantially all of the risks and rewards of ownership of receivables*" and that it "*accordingly derecognises the factored receivables from its balance sheet*". It was further noted that "*this is a true sale and the risks and rewards and transferred to Greensill*".

5.91 The Respondents' conclusion in respect of the Greensill RPA was that the "*Purchased Receivables are made without recourse and the Seller has no liability to the Buyer for amounts not paid*".

5.92 The audit work performed was inadequate to support a conclusion that the receivables sold under the Greensill RPA were capable of being derecognised, and therefore that the financial statements had been prepared in accordance with the relevant financial reporting standards.

5.93 In particular:

5.93.1 The sole consideration given to whether there had been a transfer of "*substantially all*" of the risks and rewards of the receivables transferred

under the RPAs was the assertion that LCL had "*no obligation*" to Greensill for "*slow payment or non-payment by the debtors*".

5.93.2 In fact, the effect of the Greensill RPA was that LCL retained the risk of dilution, deemed dilution or dispute (including slow or non-payment by debtors), as explained in paragraph 5.21.2.1 above (whereby LCL could become obliged to repurchase the RPA where a dispute or dilution existed).

5.93.3 As to whether the RPA was "non-recourse", no adequate consideration was given to the substance of the agreement over its form from an accounting perspective. As set out in paragraphs 5.61 and 5.62 above, the analysis of circumstances in which the non-recourse clause was disapplied was superficial.

5.93.4 Further, the work performed to test LCL's compliance with sections 5 and 6 of the Greensill RPA, including whether or not any receivables were overdue, was insufficient (see paragraphs 5.20 and 5.21 above). This information should have been readily available to LCL, as it had contracted with the Customers, and was also acting as collection agent under the RPA. The Respondents failed to assess the risk of LCL being obliged to repurchase any receivable or of whether it was complying with its obligations as collection agent.

5.94 Accordingly, insufficient audit evidence was obtained to support the decision to derecognise the $879,283,771.84 trade receivables from underlying Customers (as purchased by Greensill), and the corresponding decision not to recognise the $791,355,394.66 representing the finance provided to LCL by Greensill. As set out below, this had implications for the Respondents' audit work on trade debtors.

(ii) *<u>The Wyelands RPA</u>*

5.95 In relation to the Wyelands RPA, it was noted in the audit file that it was a "non-recourse facility" and that "*Buyers are pre-approved with maximum limits, and a portion of the receivable is purchased initially by Wyelands under pre-set percentages between 80%-90%*". The audit file recorded that "*the debtor from the original*

customer has been completely derecognised, with the 10% difference between the initial purchase value and the invoice value remaining due from Wyelands."

5.96 There was no further analysis of whether the Wyelands RPA amounted to a transfer of substantially all of the risks and rewards of ownership of the receivables sold under the RPA nor any documented explanation as to how the Respondents were satisfied that it was appropriate, in their judgment, to derecognise the receivables in the financial statements.

5.97 Indeed, the Respondents failed to appreciate that according to the Wyelands RPA, the Covered Portion needed to be assessed on an individual invoice and debtor basis, as although there were pre-set percentages of 80%-90%, the Covered Portion could be lower still if that debtor was approaching the Buyers' Limit (see paragraphs 5.27-5.29 above).

5.98 The Wyelands year-end trade debtor balance of $20.998 million consisted of 30 invoices part-purchased by Wyelands from nine separate Customers. The Covered Portion (i.e. the portion purchased by Wyelands) ranged from 40% to 90% of the invoice value (the average was 79%).

5.99 The Respondents' assessment that there was a "*10% difference between the initial purchase value and the invoice value remaining due from Wyelands*" was incorrect and failed to identify the significant complexities and potential variations between different invoices purchased by Wyelands.

5.100 When aggregated by Customer, one of the Buyer's Limits had been breached for one of the Customers by approximately $1 million. The Respondents failed to consider the implications under the RPA of this breach of limit.

5.101 There were therefore two issues which the Respondents did not adequately consider regarding the derecognition of the underlying trade debtor balances.

5.102 Firstly, given that the Covered Portion ranged from 40-90% (see paragraph 5.98 above), the Seller's Portion (i.e. the portion over which LCL retained all of the risks and rewards) was up to 60% of the individual invoice value. This should have raised serious questions as to whether substantially all the risks and rewards of the receivables had in fact been transferred to Wyelands.

5.103 Secondly, the Respondents carried out no audit work to determine whether or not LCL was in compliance with its obligations under the Wyelands RPA in FY20 (including ensuring no breach of Buyer Limits). As set out in paragraph 5.33.1 above, the recourse events set out in the Wyelands RPA included breaching any of its undertakings or obligations in the RPA.

5.104 The audit work performed by the Respondents was therefore insufficient to support a conclusion that trade receivables for the underlying Customers totalling $96,043,438 (and purchased in part by Wyelands) were capable of being derecognised. As a direct consequence, there was insufficient audit evidence to support LCL's decision not to recognise a corresponding liability reflecting Wyelands financing of $72,837,298.

5.105 As set out below, this had implications for the Respondents' audit work on trade debtors.

Breach of *Relevant Requirements*

5.106 In breach of paragraph 24 of ISA (UK) 330, the Respondents failed to perform audit procedures to evaluate whether the overall presentation of the financial statements was in accordance with FRS 102, in that they failed to consider whether the financial statements were presented in a manner that reflected the appropriate classification and description of financial information and the underlying transactions, events and conditions. In particular:

5.106.1 The Respondents did not properly consider whether it was appropriate to derecognise the receivables owed by LCL's Customers, and also did not consider the corresponding impact, whereby the financing provided by Greensill was not recognised as a liability. The Respondents therefore failed properly to consider whether those financial assets and related liabilities were presented appropriately in the financial statements.

5.106.2 The review of the operation of the Greensill RPA was inadequate to support the conclusion reached that LCL had "*transferred to [Greensill] substantially all of the risks and rewards of ownership of the receivables*".

5.106.3 The review of the Wyelands RPA was also inadequate to support the conclusion reached that the agreement was "*non-recourse*" and that the debtors could be "*completely derecognised*". The Respondents also did not consider the corresponding impact, whereby the financing provided by Wyelands was not recognised as a liability.

5.107 In breach of paragraph 17 of ISA (UK) 200, the Respondents failed to obtain sufficient appropriate audit evidence to draw reasonable conclusions upon which to base their opinion in relation to the derecognition of assets and related liabilities, and the overall compliance of the financial statements with FRS 102.

5.108 In breach of paragraph 15 of ISA (UK) 200, the Respondents did not consider the evidence which was obtained in relation to the derecognition of assets and compliance of LCL's financial statements with FRS 102 with sufficient professional skepticism.

5.109 In breach of paragraph 8 of ISA (UK) 230, the Respondents failed to prepare audit documentation sufficient to enable an experienced auditor to understand the basis for their conclusion that the receivables sold under the Wyelands RPA were capable of being derecognised.

Breach Area 3: Recoverability of Trade Debtors

Relevant Requirements

5.110 ISA (UK) 200, paragraph 15.

5.111 ISA (UK) 240, paragraphs 12 and 32(c).

5.112 ISA (UK) 315, paragraph 29.

5.113 ISA (UK) 330, paragraph 26.

5.114 ISA (UK) 500, paragraph 6.

5.115 ISA (UK) 505, paragraphs 7, 10 and 12.

Overview

5.116 At FY20 year-end, LCL's trade debtor balance was $180,842,691, comprised as shown in the table below.

Trade debtors	**$**	**%**
Greensill	88,579,842	49%
Wyelands	20,998,457	12%
Debtors payments post year end	21,669,625	12%
Debtors assigned post year end	43,017,910	24%
Other debtors	6,576,857	4%
Trade debtors balance	**180,842,691**	**100%**

5.117 Recoverability of debtors was evaluated as a "significant risk". It was therefore a critical part of the audit process to obtain sufficient appropriate audit evidence as to the risk of trade debtors being materially misstated.

5.118 Given that the Greensill and Wyelands debtors made up 61% of the balance (c.$89m and c.$21m respectively), it was vital that sufficient appropriate evidence was obtained for these balances, as any evidence of impairment may indicate that the financial statements were materially misstated. While debtor payments post year-

end can be the best evidence of their recoverability, procedures should be carried out to ensure that such payments do indeed relate to the debtors.

5.119 Despite the significant risk posed by the recoverability of trade debtors and the importance of obtaining evidence as noted above, the Respondents failed, amongst other things, to take sufficient steps to maintain control over the external confirmation requests and showed a lack of professional skeptcism with regard to documentation relating to trade debtors.

5.120 Furthermore, as regards the c.$21m debtor balance stated to be from Wyelands, the Respondents accepted an assurance from the Shareholder that the debt was recoverable, without querying why Wyelands owed this money to LCL, why it had not been paid despite being long outstanding or questioning the appropriateness or value of this assurance. In fact, as detailed in paragraphs 5.96 to 5.104 above, the debtor balances should have been presented as being due from the underlying LCL customers. As a result, their audit procedures on the recoverability of this balance were wholly inadequate.

Audit Work

5.121 The 2020 Financial Statements noted, in relation to the impairment of debtors that at the end of each reporting period, that LCL assesses whether there is any objective evidence that a debtor is impaired, and if impaired makes appropriate provision. The Respondents failed to carry out any work to consider or assess LCL's debtor impairment review.

5.122 Further, the Respondents failed to identify or assess any of LCL's controls, including control activities, relevant to the recoverability of trade debtors, a significant risk**.**

(i) Audit work in respect of all debtors

Confirmation using debtors circularisation

5.123 One of the planned audit procedures was the verification, "*by direct confirmation using a debtors circularisation*", of a representative sample of balances. However, the "method" noted in the audit documentation was that following selection of sample debtors, "*[t]he samples were sent to the LCL team who then arranged for the customer*

to be contacted, asking for confirmation of the year-end balance and for the confirmation of the balance to be sent directly to HWF."

5.124 LCL prepared a "pro forma" letter to seek the confirmations and sent this letter to the majority of the sampled debtors. The Respondents did not receive a copy of the requests sent to some debtors, including Greensill and Wyelands. Consequently, the Respondents did not know in all cases, what confirmations had been sought from the debtors.

5.125 Further, in seven out of 20 cases (including Wyelands), the confirmations were not sent by the debtors directly to HWF, and were instead received via LCL. Consequently, those seven confirmations were not external confirmations within the meaning of paragraph 6(a) of ISA (UK) 505.

5.126 The Respondents were obliged to maintain control over external confirmation requests, including designing the confirmation requests (which includes determining that requests are properly addressed and contain return information for responses to be sent directly to the auditor) and sending the requests, including follow-up requests when applicable, to the confirming party (ISA (UK) 505, paragraphs 7(c) and (d)). The Respondents failed to comply with these requirements.

Review of after date receipts

5.127 The Respondents reviewed the post year-end receipts for all the trade debtors (including balances for Greensill and Wyelands, which are addressed separately below).

5.128 There were $21.7m other receipts allocated against trade debtors. However, in respect of three of those debtors, the post year-end receipt recorded was significantly different to the year-end debtor listing recorded by the Respondents in the worksheet. There is no record as to how those amounts were checked against bank statements or remittance advice (per the planned audit procedure) to confirm the receipts to the year-end debtors, as opposed to the possibility of those being amounts relating to more recent sales or other transactions.

(ii) Audit work on the Greensill debtor balance

Confirmation using debtor circularisation

5.129 As with other debtors, HWF arranged for confirmations to be requested through LCL. There is no evidence on the audit file showing LCL's correspondence with Greensill, despite HWF's request to be copied in.

5.130 The trade debtor balance for Greensill represented the outstanding Additional Purchase Price due under the Greensill RPA. However, as explained in paragraph 5.16 above, the extent to which LCL would receive this amount depended on whether the underlying Customers paid their invoices in full.

5.131 On 22 July 2020, HWF received an email attaching what was described as a "balance confirmation" for LCL as at 31 March 2020. The attached document was a letter addressed to LCL, which stated that "*[w]e confirm the Receivable Purchase Facility balance as at 31st March 2020 per below table*." The balance confirmation contained a schedule of five pages of invoices, with the headings and totals shown in the table below:

Invoice no.	Invoice Value Post 90% Advance Rate (USD)	Invoice Value (USD)	Excess Receivable (USD)
Total	791,355,395	879,283,772	87,928,377

5.132 None of the terms used in this table were defined or clarified by HWF as part of their audit work. This was particularly problematic because "Excess Receivable" was ambiguous: as Mr Mott-Cowan accepted when interviewed by the FRC, it could refer to "Excess Collections" and thus represent money Greensill was seeking to recover, or to the "Additional Purchase Price" and thus represent money LCL was seeking to recover.

5.133 Notwithstanding this ambiguity, the Respondents assumed that the c.$88million under the heading "Excess Receivable" was confirmation of LCL's Greensill debtor balance. As the Respondents would have realised if they had understood the

Greensill RPA, LCL would only receive any "Additional Purchase Price" to the extent that Greensill received payments from the underlying customers. Since LCL was acting as the collection agent under the Greensill RPA, LCL in fact had information which would enable it to determine the extent to which Customers had paid, and Additional Purchase Price would be received accordingly. However, the Respondents failed entirely to appreciate this.

Review of after date receipts

5.134 As noted above, HWF took the Greensill balance at FY20 year-end to be $87,928,377.18. Rather than carrying out any audit work on the Collection Account to ensure that the underlying Customers paid in accordance with their terms, the Respondents sought to obtain audit evidence of recoverability through evidence of post-balance sheet date receipts from Greensill.

5.135 Six post year-end receipts for Greensill (the "**six Greensill receipts**") totalling $88,579.841.76 were noted on the audit file. HWF was provided with the details of the six Greensill receipts by email from LCL on 16 August 2020, attaching a document titled "Greensill Settlement". The Greensill Settlement was a scanned copy of a paper document with the six Greensill receipts (shown as being paid into LCL's bank accounts) highlighted.

5.136 However, the audit work carried out in relation to the six Greensill receipts was incomplete:

5.136.1 HWF did not obtain any remittance advice documentation for the receipts.

5.136.2 There was no information in the Greensill Settlement document which indicated that these payments were in relation to settlement of debtor payments or "Additional Purchase Price" or "Excess Receivables" or any equivalent term.

5.136.3 In respect of each receipt, the "Transaction description" was "Internal transfer" and the "Payment details" was "O/O Greensill Capital (UK) Ltd". This was the same narrative for the entire amount of $315 million and $114 million Greensill transferred to LCL's account in March 2020 and April 2020 respectively, which transfers were in respect of the Initial Purchase Price.

Accordingly, it was not possible for the Respondents to tell from the bank statements alone whether the six Greensill receipts were payments in respect of the Initial Purchase Price or Additional Purchase Price. No further inquiries were made by the Respondents regarding these transfers.

5.136.4 A difference of $651,000 between the stated Greensill year-end balance and the total value of the six Greensill receipts was never resolved by the Respondents.

Unusual transactions requiring further evaluation

5.137 On the same day, as five of the six Greensill receipts were received from Greensill, five sums of strikingly similar amounts were transferred by LCL to Greensill, or potentially a treasury management company ("**the Treasury Management Company**") – see paragraph 5.139 below. At the time of the FY20 Audit, the Treasury Management Company's sole director was the Shareholder. The Treasury Management Company's principal activity was described in its financial statements for the year ending 31 March 2019 as the "*provision of treasury management services to Liberty group companies*."

5.138 In respect of three of the five payments referred to above, HWF noted in a workpaper that: "*[p]ayments made to Greensill capital on behalf of* [the Treasury Management Company]". This information was said to have been provided by LCL on 20 August 2020.

5.139 When interviewed by the FRC, Mr Mott-Cowan explained that, at the time of the FY20 Audit, he was unaware of the transactions, but that it was now his belief that the payments were to the Treasury Management Company.

5.140 The audit work carried out in relation to these transactions was inadequate:

5.140.1 HWF failed to obtain any explanation as to why five payments of a very similar size to those received from Greensill were transferred to Greensill, or potentially the Treasury Management Company, on the same day.

5.140.2 Consequently, no explanation or assurance was obtained that the assumed post-year-end repayment of trade debts was in fact a repayment.

5.140.3 No supporting evidence was obtained for the information provided by LCL as to three of the payments being made on behalf of the Treasury Management Company.

5.140.4 Even if the payments were to the Treasury Management Company, the Respondents performed no detailed analysis of the Treasury Management Company, or the extent of LCL's financial interaction with the Treasury Management Company. There was no FY20 year-end creditor recognised for the Treasury Management Company that may have required such post year-end payments.

(iii) *Audit work on the Wyelands debtor balance*

Circularisation using debtor confirmation

5.141 HWF asked LCL to arrange for the confirmations to be provided by Wyelands directly to HWF. However, HWF received the balance confirmations from LCL, not Wyelands.

5.142 The document provided by Wyelands showed a total "Excess Amount" of $20,998,456.87.

5.143 As with the Greensill confirmation, there was no definition of "Excess Amount" and no further questions or inquiries were made by HWF in respect of the reliability of assuming that the "Excess Amount" represented an accurate statement of the trade debtor balance in respect of Wyelands. This is notwithstanding that there was evidence (see paragraphs 5.95 -5.103 above), indicating that at least a significant quantity of this amount was the Seller's Portion, and thus remained part of the receivables not sold to Wyelands.

5.144 Further, the confirmation evidence appeared to contradict evidence obtained within a document showing related party balances, where the value against Wyelands was stated to be "nil".

Debtors outstanding as at the date of the Auditor's Report

5.145 At FY20 year-end, the Wyelands debtor balance – stated to be a total of c$21 million – was already aged more than 120 days. The entire balance was still unpaid as at 24

September 2020, when Mr Mott-Cowan signed the Auditor's Report, almost six months after the FY20 year-end.

5.146 HWF sought evidence from LCL management that this debtor balance was recoverable, but no such evidence was ever sought from Wyelands, with assurances only provided by LCL management.

5.147 HWF noted in the audit file that "*[o]verall, despite the balance for Wyelands not being recovered and being material, management and the sole director shareholder have confirmed that their best estimate is that the balances is fully recoverable*."

5.148 HWF relied, in particular, on the assurance provided by the Shareholder by email to Mr Mott-Cowan on 24 September 2020 (the date the Auditor's Report was signed) in which he stated, amongst other things, that "*[w]ith reference to the finalization of LCL Audit for March 2020 - recoverability of the receivable from Wyelands bank, I can confirm all will be recovered in full and if any issues I will make good*."

5.149 The Respondent incorrectly considered that the Shareholder was a director and shareholder of Wyelands, whereas, the Shareholder had never been a director of the bank. Furthermore, whilst Wyelands was part of the informal family of businesses that comprise GFG Alliance, it was operationally independent of the Shareholder.

5.150 In any event, the "best estimate" of management and the email from the Shareholder were a wholly inadequate basis to form any view or comfort on the recovery of the Wyelands trade balance:

5.150.1 In auditing this "best estimate", the Respondents did not (a) understand the controls in place over determining this estimate, including the required consideration of objective evidence of impairment; (b) understand management's assumptions in reaching this estimate; and (c) perform any audit tests over it.

5.150.2 The Respondents failed to question the basis on which the Shareholder was confirming that the amount would be recovered (given that, as noted above, there was evidence that at least some of the outstanding sum was owed by LCL's Customers).

5.150.3 The Respondents failed to consider the appropriateness or the enforceability of the email (which was addressed to HWF and not LCL, and which did not specify the amount purportedly underwritten).

5.150.4 No consideration was given to whether the Shareholder had the personal means to "make good" a trade debtor balance of c.$21 million.

5.150.5 There is no evidence in the audit file of any consideration by HWF of the fact that the Shareholder was also the sole director of LCL and so was purporting to give comfort on behalf of Wyelands to himself, despite him not being a director of Wyelands and in fact it being operationally independent of him.

(iv) *Other debtors*

5.151 The c$6.6m "Other debtors" figure included a debtor of c.$4.8m for Debtor A who did not respond to the confirmation request. The Respondents noted in the audit file that the balance was not recoverable because Debtor A and its parent had entered into liquidation.

5.152 However, it was further noted that 90% of the debt would be claimed under a credit insurance policy. The only evidence of the 90% being recoverable was a copy of an email correspondence between LCL, the insurance brokers and the insurance company about the claim being submitted. No audit work was carried out on the insurance policy and no third-party evidence of the recoverability of this debt was carried out.

Breaches of *Relevant Requirements*

5.153 In breach of paragraph 7 of ISA (UK) 505, the Respondents did not maintain control over the debtor confirmation process in that they : (a) failed to determine the information to be confirmed or requested by not having sight of all of LCL's correspondence with the sampled debtors (b) failed to design the confirmation request, including ensuring that the responses were sent directly to the Respondents; and (c) did not directly send the confirmation requests to the sampled debtors.

5.154 In breach of paragraph 10 of ISA (UK) 505, the Respondents failed to obtain further audit evidence to resolve doubts about the reliability of the response to a confirmation request in that:

5.154.1 They failed to undertake further audit work in order to request additional confirmation and clarification from Greensill as to the precise meaning of *"Excess Receivable"* stated within its confirmation letter.

5.154.2 As regards the Wyelands receivables, as a result of their failure to undertake sufficient audit work to understand the Wyelands RPA, they failed to understand that a significant part of the balances were in all likelihood the Seller's Portion and failed to send confirmation requests to the underlying Customers.

5.155 In breach of paragraph 12 of ISA (UK) 505 the Respondents, following Debtor A's non-response, failed adequately to perform alternative audit procedures to verify the insurance position.

5.156 In respect of: (a) the testing of the recoverability of the Greensill year-end balance; (b) the testing of the recoverability of the Wyelands' year-end balance; and (c) the testing of recoverability of the Debtor A balance; the Respondents failed (for the reasons set out in paragraphs 5.129 - 5.152 above):

5.156.1 In breach of paragraph 6 of ISA (UK) 500, to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence;

5.156.2 In breach of paragraph 26 of ISA (UK) 330, to consider all relevant evidence in concluding that sufficient appropriate audit evidence had been obtained; and

5.156.3 In breach of paragraph 15 of ISA (UK) 200, to plan and perform an audit with professional skepticism.

5.157 In breach of paragraph 29 of ISA (UK) 315, in relation to trade debtors, which had been assessed as a significant risk, the Respondents failed to: (a) identify or assess any of LCL's controls, including control activities; and (b) plan or implement

adequate procedures to gain an understanding of LCL's year-end processes regarding the impairment of debtors.

5.158 In breach of paragraph 32(c) of ISA (UK) 240, the Respondents failed to evaluate the business rationale (or lack thereof) for the transactions described above at paragraphs 5.137 -5.140 ("Unusual transactions requiring further evaluation") and whether they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets.

5.159 In breach of paragraph 12 of ISA (UK) 240, the Respondents failed to exercise professional skepticism, in failing to recognise the possibility that a material misstatement due to fraud could exist, in relation to the transactions described above at paragraphs 5.137-5.140 ("Unusual transactions requiring further evaluation").

Breach Area 4: Recoverability of Intercompany Balances

Relevant Requirements and Accounting Standards

5.160 FRS 102, paragraph 11.21.

5.161 FRS 102, section 33.

5.162 Paragraph 72(1) of Schedule 1 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (the "**2008 Regulations**").

5.163 ISA (UK) 200, paragraph 15.

5.164 ISA (UK) 230, paragraph 8.

5.165 ISA (UK) 330, paragraph 21.

5.166 ISA(UK) 315, paragraph 29.

5.167 ISA (UK) 500, paragraph 6.

5.168 ISA (UK) 505, paragraph 7.

5.169 ISA (UK) 550, paragraphs 12, 13, 14and 25(a).

Overview

5.170 Intercompany debtors totalled $48,738,639 of the $239,792,552 debtors total at FY20 year-end and were therefore material.

5.171 The Respondents assessed recoverability of intercompany balances as a "*significant risk*" on account of the age of the debtors and historic difficulties in reconciling the balances. The Respondents noted that LCL "*has a number of large amounts owing from group companies, in some circumstances the amount can remain as debtors for a reasonable length of time. There is a risk that the amounts may not be recoverable as such the assets of LCL could be overstated*."

5.172 However, there were numerous shortcomings in the Respondents' audit work, including a failure to control the confirmation process, a failure to plan or execute procedures relating to balance assignments and a failure to understand controls.

Audit Work

(i) Confirmations from related parties

5.173 One of the planned audit procedures was to "*obtain confirmations directly from related party entities as to amounts due to/from LCL*". There were 23 related parties with whom LCL had debtor balances as at FY20 year-end.

5.174 The Respondents did not maintain control over the confirmation process. Instead, LCL sent out the confirmation requests. The Respondents only received fewer than a third of the confirmations (7 out of 23 debtors) directly from the confirming parties. For the rest, they were reliant on LCL forwarding the confirmations to them. For the confirmations they so received, the audit team did not take any additional steps to check their veracity.

(ii) Procedures assessing recoverability

5.175 The components of the intercompany debtors (totalling $48,738,639) were identified in the audit documentation as shown in the table below:

Components of Intercompany debtors	**$**
Amounts received post year-end	$13,419,758
Assignments – balance assigned to the Treasury Management Company	$19,067,877
Balance assigned to Assignee A	$1,245,400
Balance offset with creditor at year-end	$5,491,776
Balances which need further support	$9,082,952
Cumulative trivial balances	$430,876
Intercompany debtors total	**$48,307,763**

Amounts received post year-end ($13,419,758)

5.176 The purpose of this test was to check whether the particular debtor identified had paid after the year-end. Therefore, it was necessary to check that the payment received was associated with the specific debtor being tested.

5.177 The post year-end receipts principally consisted of two amounts – $3,851,216 Intercompany Debtor 1 debtor balance and $9,291,341 Intercompany Debtor 2 debtor balance.

5.178 The Intercompany Debtor 1 debtor balance was stated to have been paid through two payments from a related company totalling $4,001,700. The Respondents did not obtain any supporting documentation for this assignment, nor was there an

explanation as to why the amount paid exceeded the debtor balance. Therefore, the Respondents failed to exclude the possibility that these were payments for entirely different transactions, despite the obvious indicators that it might be – namely that it was paid by a different party, that the total paid was for a different amount, and there being two separate payments.

5.179 As to the Intercompany Debtor 2 balance of $9,291,341, the Respondents explained that this was recovered from a receipt of $20.85m from Intercompany Debtor 2. However, there is no evidence on the audit file for the $20.85m receipt from Intercompany Debtor 2, or how it was confirmed that this was in relation to settlement of the Intercompany Debtor 2 debt. Therefore, again, the Respondents failed to exclude the possibility that this payment was for an entirely different transaction, despite the obvious indicator that it might be - namely that the receipt was for a different amount.

5.180 The Respondents recorded that the post year-end receipt "*[a]greed to bank statements*" but this was incorrect, as the exact amounts did not reconcile. The Respondents accepted receipt of cash as evidence of recoverability, rather than examining specific cash receipts against documentation relating to the debtor.

Assignments

5.181 HWF's records show that LCL was owed a total of $19.9m by eight of its related parties. Separately, LCL also owed $8.6m to the Treasury Management Company. Rather than await receipt of the $19.9m from the eight related parties, and pay the $8.6m to the Treasury Management Company separately, the audit documentation records that LCL assigned the $19.9m to the Treasury Management Company. This would involve each of the parties which collectively owed the $19.9m agreeing to make their payments to the Treasury Management Company instead of LCL.

5.182 According to HWF's records, LCL then netted off the $19.9m owed by the Treasury Management Company against the $8.6m it owed to the Treasury Management Company. As a result, LCL was expecting to receive $11.3m from the Treasury Management Company. HWF then sought assurance over the $11.3m by assessing post year-end payments.

5.183 The effectiveness of this test to check the recoverability of $19.9m relied entirely on this amount being genuinely assigned to the Treasury Management Company. However, the Respondents failed to obtain any supporting documentation whatsoever to show that the Treasury Management Company and any of the seven related parties had agreed to the assignments.

5.184 With respect to the Respondents' assessment of the recoverability of the $11.3m owed by the Treasury Management Company to LCL, the Respondents recorded that it had been paid through three payments totalling $12.4m. HWF obtained no explanation as to why the payment was $1.1m in excess of the amount owed, or why it was made in instalments. The obvious risk that these payments were for unrelated transactions was heightened by the fact that the Treasury Management Company made numerous payments to LCL throughout the year, and no supporting documentation was sought to link the payments to the $11.3m owed.

5.185 Further, there is no record that, in accordance with the planned procedure, the Respondents reviewed the financial or management accounts of the Treasury Management Company or otherwise assessed its ability to pay, despite the Respondents correctly identifying the importance of such a procedure.

5.186 The Respondents also did not consider whether the assignment of the debtors to the Treasury Management Company was indicative of transactions having been concluded under normal market conditions, such as considering whether a third party would have accepted the full value of the assignments, particularly given that there was evidence indicating that they might have been significantly aged debtors.

5.187 As to the Assignee A assignment of $1.2m, there is no evidence on the audit file of any assignment documentation or that Assignee A authorised or was notified of the assignment.

Balance offset with creditor

5.188 A $5,491,776 debtor balance was recorded with Wyelands Capital Ltd, which was also recorded as having a creditor balance at year-end. However, the audit file shows that it was Wyelands Bank Plc (a different entity under a different corporate ownership structure) which had a creditor balance of $5,790,382. There is no

explanation on the audit file as to why or how a creditor balance with Wyelands Bank Plc provided assurance over a debtor balance with Wyelands Capital Ltd.

5.189 Further, there were two letters on the audit file which showed that by 31 March 2020, the Wyelands Bank creditors had been assigned to two other entities, and were therefore no longer available to offset against the $5,491,776 in any event. The Respondents failed to identify or query this.

(iii) *Procedures not carried out*

5.190 Despite recoverability of intercompany balances being identified as a significant risk, in part due to the aged balances (see paragraph 5.171 above), there was no procedure planned to allow the Respondents to gain an understanding of LCL's year-end controls regarding the impairment of intercompany debtors.

5.191 The audit file indicates that material intercompany debtors were aged more than one year at the date of signing the Auditor's Report. As well as not understanding whether management had carried out an impairment assessment, the Respondents did not carry out an analysis of the aged intercompany debtors.

Breaches of *Relevant Requirements*

5.192 In breach of paragraph 7 of ISA (UK) 505, the Respondents did not maintain control over the debtor confirmation process in that they: (a) did not determine the information to be confirmed or requested by not having sight of all of LCL's correspondence with the sampled debtors; (b) did not design the confirmation requests, including ensuring that the responses were sent directly to the Respondents; ; and (c) did not directly send the confirmation requests to the sampled debtors.

5.193 In relation to amounts received post year-end, assignments and balance offset with creditor, the Respondents (for the reasons set out in paragraphs 5.176-5.189 above) failed:

5.193.1 in breach of paragraph 6 of ISA (UK) 500, to obtain sufficient appropriate audit evidence of the recoverability of intercompany debtors;

5.193.2 in breach of paragraph 15 of ISA (UK) 200, to apply sufficient professional skepticism to the results of their testing; and

5.193.3 in breach of paragraph 21 of ISA (UK) 330, having identified recoverability of intercompany balances as a significant risk, to perform substantive procedures responsive to that risk that were adequate to address the risk of material misstatement.

5.194 In breach of paragraph 29 of ISA (UK) 315, the Respondents failed to plan or implement any procedures designed to gain an understanding of LCL's controls and control activities, specifically LCL's impairment processes, despite the recoverability of intercompany balances being identified as a significant risk. Further, the Respondents failed to carry out any review over LCL's analysis of intercompany balance aging despite evidence on the audit file that material intercompany debtors were aged more than one year at the date of signing the Auditor's Report.

5.195 The Treasury Management Company is referred to within the audit file as a "treasury entity" and a related party. The Respondents failed, in breach of paragraph 14 of ISA (UK) 550, to obtain an understanding of LCL's controls to: (a) disclose related party relationships, transactions, and post balance sheet events appropriately; (b) authorise and approve significant transactions and arrangements with related parties; and (c) authorise and approve significant transactions and arrangements outside the normal course of business.

5.196 In breach of paragraphs 12 and 13(c) of ISA (UK) 550, the Respondents failed to consider the susceptibility of the financial statements to material misstatement due to fraud or error resulting from LCL's relationship and transactions with the Treasury Management Company in that they failed to conduct any analysis to obtain an understanding of the nature and purpose of transactions with the Treasury Management Company. The Respondents failed to obtain evidence of whether LCL had made any commitments to it, and the impact of any such commitments.

5.197 In relation to the Treasury Management Company $19.1m assignment and the Assignee A $1.2m assignment, for the reasons set out in paragraphs 5.181-5.187 above, the Respondents failed:

5.197.1 In breach of paragraph 15 of ISA (UK) 200 to exercise professional skepticism.

5.197.2 In breach of paragraph 8 of ISA (UK) 230, to prepare audit documentation sufficient to enable an experienced auditor with no previous connection with the audit to understand, amongst other things, the audit evidence obtained, significant matters arising during the audit, the conclusions reached, and significant professional judgments made in reaching those conclusions.

5.198 In breach of paragraph 25 of ISA (UK) 550, the Respondents failed to evaluate whether LCL's accounts complied with sections 32 and 33 of FRS 102, the Companies Act 2006 and Paragraph 72 of Schedule 1 to the 2008 Regulations, including whether the transactions had been concluded under normal market conditions, by failing to disclose (within Note 21 of the Financial Statements or otherwise) any financial interactions with the Treasury Management Company or with any "treasury entity" within GFG Alliance.

Breach Area 5: Revenue Recognition

Relevant Requirements

5.199 ISA (UK) 220, paragraph 17.

5.200 ISA (UK) 240, paragraphs 12 and 32(c).

5.201 ISA (UK) 500, paragraph 6 and 9.

5.202 ISA (UK) 520, paragraph 5.

5.203 ISA (UK) 530, paragraph 6.

Overview

5.204 Revenue recognition is a high-risk area of the audit, with the ISAs stating that there is a rebuttable presumption of fraud risk in revenue on every audit.

5.205 The Respondents identified revenue recognition as a "*significant risk*" in their post-planning risks register, with both a high likelihood of material misstatement and high financial impact.

5.206 However, their audit work contained serious and basic errors. These included a failure to ensure that the transaction listings used for selecting sample items was complete and accurate and a failure to carry out their sample selection process as planned, resulting in a procedure designed to provide evidence of the completeness of revenue being incapable of doing so. The Respondents also failed to explore the reasons for transactions with unusually high or loss-making gross margins.

5.207 Furthermore, the Respondents placed undue reliance on a number of substantive analytical procedures which were not carried out in compliance with the ISA requirements and were, from their inception, unable to provide meaningful audit evidence.

Audit Work

5.208 As noted above, in the 2020 Financial Statements, LCL's revenue was reported as $4.224 billion. This represented the sums due under the commodities sale contracts with Customers.

5.209 As part of the audit work in this area, the Respondents planned to undertake a number of procedures to test assertions. Assertions are a method used by the auditor to consider the different types of potential misstatements that may occur when identifying, assessing and responding to the risks of material misstatement. The assertions the Respondents planned to test included Completeness (verifying that all items expected to be included in the financial statements are in fact included) and Occurrence (verifying that all transactions included in the financial statements took place).

5.210 In order to undertake these tests, the Respondents selected a sample.

(i) *Sample selection*

5.211 The Respondents reviewed LCL's Sales and Purchase Registers, identifying back-to-back (matched) sales transactions and non-back-to-back (unmatched) sales transactions. The Respondent selected a sample size of 40, as shown below:

	Total samples per category
Transactions with margin below -5%	2
Transactions with a 0% (to 2 d.p.) margin	7
Transactions with margins between 5% and -5%	17
Transactions with margin above 5%	10
4 non back-to-back transactions (2 x purchases, 2 x sales)	4
	40

(ii) *Testing for Completeness*

5.212 Testing the completeness assertion for revenue involves gaining audit evidence howing that items that are expected to be included in the financial statement amount are in fact included.

5.213 The Respondents noted two main methods by which they intended to test completeness. First, tracing purchases of goods from Suppliers through to the sale of those goods to Customers (the "**tracing exercise**") and second, gaining assurance over completeness "*through analytical of review of turnover by location, product, customer and date to find variances period on period*" (the "**analytical review**").

5.214 However, as set out below, the audit procedures were not capable of providing the Respondents with audit evidence of the completeness of revenue.

The tracing exercise

5.215 Whilst the Respondents reviewed the Sales and Purchase Registers to produce lists of matched and unmatched transactions, this exercise would not, of itself, have identified any sales transactions that might have taken place but had not been recorded on the Sales Register.

5.216 Thus, the tracing exercise did not address the risk of understatement of sales. There is no record of the Respondents considering alternative audit procedures which could have addressed this risk.

5.217 Further, given the importance of the Sales Register to the tracing exercise, it was important that the information in the register was accurate and complete. As to this:

5.217.1 The Sales Register provided by LCL did not contain sales invoice numbers. There is no evidence that the Respondents noticed or queried this despite sequential numbering potentially providing a degree of assurance over completeness.

5.217.2 The Respondents *did* obtain Sales invoice documents that were numbered. However, there were sequential anomalies in the invoice numbers: (a) invoice number 16912 was dated 12 April 2019, whereas a sequentially earlier invoice with number 16535 was dated 5 December 2019; (b) there were two invoices numbered "17076" dated 30 March 2020 issued in respect of the same Customer for two different values. The Respondents queried the second anomaly with LCL management, but received no explanation.

5.217.3 The Respondents did not provide any evidence of consideration that the Sales Register provided by LCL contained only 1,327 transactions, yet the range between the minimum and maximum Sales invoice numbers sampled ("15331" and "17109" respectively) was 1,778.

The analytical review

5.218 The Respondents carried out the following analytical reviews in respect of turnover: (a) analysis of sales by three geographical areas ("AME", Europe and "Rest of the

World"); (b) analysis of LCL's top 20 customers and compared these to those of the prior year; (c) analysis of LCL's annual turnover by product and compared this to the prior year; and (d) analysis of the monthly sales for both FY20 and the 2019 financial year.

5.219 However, the Respondents did not set any expectations in advance of conducting the respective analytical procedures against which their conclusions were to be assessed.

5.220 Further, the Respondents did not determine, in advance, the magnitude of the difference between recorded amounts from expected values that would be acceptable without further investigation.

5.221 There was no explanation in the audit file as to how the analytical reviews (which related to geographical location, customer reliance, product and seasonality) could provide any evidence to the Respondents on the issue of completeness of sales.

(iii) *Testing for Occurrence: Debtor Assignments*

5.222 Of the total of $378.7 million revenue sampled, $314.8 million was assigned. Given the high proportion of assignments, the Respondents correctly determined that, as part of testing for occurrence, a separate procedure should be carried out to respond to the risks relating to assignments.

5.223 Part of the procedure relating to debtor assignment included testing which was to be carried out in a workpaper referred to as "*C050*". However, there was no working paper C050 on the audit file.

5.224 Further, of the 40 sampled transactions, three related to invoices which had been assigned to Debtor A. The latest dated of the invoices was dated 2 March 2020 for an amount of $3,732,850. However, by the date of the Auditor's Report, through their testing of debtor recoverability (see paragraph 5.151 above) the Respondents were aware that Debtor Awas in liquidation.

(iv) *Unusual Transactions*

5.225 The audit documentation also recorded that the Respondents planned to "*[i]nvestigate sale/ purchases with unexpected margins (i.e. negative, nil or unexpectedly high margins)*."

5.226 As noted above, the Respondents' sampling method involved sampling two transactions with margins below -5% and ten transactions with margins above 5%.

5.227 Of the two transactions identified for testing on the basis of having a margin below -5%, one transaction had a profit margin of -28%. Of the ten transactions identified for testing on the basis of having a margin above 5%, one had a profit margin of 17% and another 22%. However, the Respondents did not seek or obtain an explanation or evidence for these significant outliers, despite Mr Mott-Cowan describing LCL's business as "*a low risk business so the margins are low to reflect the low risk…*".

(v) *Substantive Analytical Procedures*

5.228 The substantive analytical procedures carried out in relation to revenue are addressed at paragraphs 5.218-5.221 above.

5.229 The Respondents also performed an analytical review of sales and purchases by comparing sales against purchases for the year, as well as comparing year-on-year sales and year-on-year purchases.

5.230 A workpaper in the audit file contained tabs described as "*Sales Registers*" and "*Purchase Registers*" for FY20 and the 2019 financial year. In respect of three of the four registers (Sales register 2020, Sales Register 2019 and Purchase Register 2020), the audit team recorded that it had compared the total sales for the financial reporting period to the relevant profit and loss accounts and had identified reconciling items, described as "*DN/CN for Price Difference received*". The relevant amounts in respect of FY20 were stated to be $246,934.87 for Sales Register 2020 and $562,265.27 for Purchases Register 2020.

5.231 However, there is no evidence in the workpaper that the nature of the reconciling items identified in the registers was confirmed or that it was investigated by the audit team.

Breach of *Relevant Requirements*

5.232 In breach of paragraph 6 of ISA (UK) 500 and paragraph 6 of ISA (UK) 530, the Respondents failed to design and perform audit procedures, appropriate in the circumstances, for obtaining sufficient appropriate audit evidence for completeness of revenue and the Respondents failed to consider the purpose of the audit procedure and the characteristics of the population from which the sample was drawn. In particular, the audit procedures carried out were not capable of detecting sales transactions that had been entered into but not recorded.

5.233 In breach of paragraph 9 of ISA (UK) 500, the Respondents did not consider the completeness or accuracy of the Sales Register provided by LCL, before the sample of transactions was selected.

5.234 In breach of paragraph 12 of ISA (UK) 240, the Respondents failed to exercise professional skepticism including remaining alert to the possibility that a material misstatement due to fraud could exist when considering the reliability of the sales invoices listing provided by LCL. In particular, the Respondents failed to follow up a query they raised with LCL with regard to the invoice numbering which did not appear to be sequential by date and failed to query apparent duplicate invoice numbers.

5.235 Mr Mott-Cowan breached paragraph 17 of ISA (UK) 220 in that, on or before the date of the Auditor's Report, he failed to conduct a proper review of the audit documentation or have sufficient discussion with the engagement team, in order to be satisfied that sufficient appropriate audit evidence had been obtained. As a result of this failure, he was unaware that workpaper C050 was not included in the audit file.

5.236 In breach of paragraph 32(c) of ISA (UK) 240, the Respondents failed to evaluate the business rationale for loss making trades and trades with high profit margins, and whether, given the Respondent's characterisation of LCL's business model being

primarily based around back-to-back low margin trades, these transactions may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets.

5.237 In breach of paragraphs 5(c) and 5(d) of ISA (UK) 520, the Respondents failed to set expectations and the magnitude of the acceptable deviation, before carrying out substantive analytical procedures.

5.238 In breach of paragraph 5(a) of ISA (UK) 520, the Respondents failed to determine the suitability of the substantive analytical procedures in providing audit evidence for the completeness of revenue.

5.239 In breach of paragraph 9 of ISA (UK) 500, the Respondents failed to evaluate whether the sales and purchases listings were sufficiently reliable to be used in substantive analytical procedures, sample selection and substantive tests of detail, given that reconciling items had been identified between the Sales and Purchase Registers and the profit and loss accounts, and the Sales invoice numbering anomalies described at paragraph 5.217 above, but these were not further investigated.

Breach Area 6: Journals Testing

Relevant Requirements

5.240 ISA (UK) 230, paragraph 8.

5.241 ISA (UK) 240, paragraph 32.

5.242 ISA (UK) 300, paragraph 12.

5.243 ISA (UK) 315, paragraph 18(f).

5.244 ISA (UK) 330, paragraph 26.

5.245 ISA (UK) 500, paragraphs 6 and 9.

5.246 ISA (UK) 530, paragraphs 6 and 11.

5.247 ISA (UK) 550, paragraph 13.

Overview

5.248 Journals are used for recording standard non-recurring transactions, non-routine transactions and adjustments to the accounting records. They can therefore be used to manipulate financial statements. Accordingly, the ISAs describe journal entries as a high-risk area and include a number of mandatory requirements.

5.249 Overall, the Respondents' work on journals testing was perfunctory, lacked professional skepticism, and demonstrated a failure to understand and respond to the risk properly. For example, they did not carry out certain planned procedures and even failed to notice that a procedure attempted (to detect entries with potentially risky keywords), was not possible to carry out with the information provided to them. Further, they failed to obtain supporting documents or make proper inquiries as to the business rationale of transactions falling outside LCL's normal course of business.

Audit Work

5.250 The Respondents planned a number of procedures in relation to "*ledger maintenance and journal testing*". Some of the planned procedures were designated in the risk register as procedures that addressed the significant risk of management override However, the Respondents did not carry out

all of the planned procedures even though some of them were aimed at addressing a significant risk.

(i) *Understanding the controls*

5.251 The Respondents did not plan any procedures, or carry out any procedures, to gain an understanding of the controls relevant to the risk of management override of controls in relation to LCL's processing of journal entries.

(ii) *Inquiries of Management*

5.252 The Respondents did not plan to, and in the course of the FY20 Audit did not, make inquiries of individuals involved in LCL's financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments.

5.253 Despite reviewing the journal workpapers, Mr Mott-Cowan did not detect the audit team's failure to make these mandatory inquiries.

(iii) *Narrative searches*

5.254 One of the procedures the Respondents planned was to obtain a full listing of LCL's journal postings and review "for any material or unusual entries and vouch these to the relevant backup." Further to this, they received an email from LCL on 27 August 2020, containing the "journal register for the full year" (the "Spreadsheet") to HWF by email.

5.255 The Spreadsheet listed the dates, particulars, debits and credits of the LCL Journal Register. There was no narrative providing information about the particulars, such as whether the entry had been cancelled or had been made to correct either an error or a duplicate transaction.

5.256 There were 5,465 journal entries in the Spreadsheet, which were transferred to a worksheet. The Respondents then conducted keyword searches for "'*Cancel', 'Error', 'Duplicate' as entries with these terms may suggest something untoward*." No such keywords were found.

5.257 However, the plan to carry out a keyword search was flawed from the outset in that, as noted above, the Spreadsheet did not contain any narrative information. The

audit team failed to notice this shortcoming in the data provided. They did not consider any alternative or additional audit procedures to test for significant transactions outside of the normal course of LCL's business, or otherwise unusual transactions.

5.258 Consequently, no proper audit procedures were designed or performed that were capable of testing for unusual transactions, which the audit team had planned to do.

(iv) Audit work carried out on completeness

5.259 There is no evidence that the audit team carried out any completeness checks or considered the completeness of the listing of journals that LCL management had provided. The Respondents did not, for example, inquire as to how the Spreadsheet had been prepared, nor was any consideration given to whether any entries could have been removed from the list, either intentionally or accidentally.

(v) Journals close to year-end and sampling method

5.260 814 of the 5,465 journal entries were within the last month of the financial year, including 161 journal entries dated 31 March 2020 (the last day of the financial year). Notwithstanding this, the Respondents did not tailor their sample selection to select journals close to year-end. Because fraudulent journal entries and other adjustments are often made at the end of a reporting period, an auditor is required to select the journal entries and other adjustments made at that time[10]. Further, the Respondents selected the samples without any consideration of whether the entries on the Spreadsheet were complete and/or accurate.

5.261 The Respondents selected a sample of 15 journals to test. The journals were chosen by "*random number generator based on row count in excel*."

(vi) The testing of the samples identified

5.262 As noted in paragraph 5.254 above, the Respondents planned to "*review for any material or unusual entries and vouch these to the relevant backup*." Further *"for the remainder of the journals*" they planned to *"use a sample basis and vouch to backup*."

[10] Paragraph A44 of ISA 240

5.263 The planned procedure was not followed in that whilst 1,741 of the 5,465 journal entries exceeded the materiality threshold, only the 15 sampled entries were reviewed.

5.264 Further, despite a sample size of 15 entries, the Senior Audit Manager only requested "*back-up documentation*" from LCL in relation to 10 entries. In response to this request, LCL provided, on 31 August 2020, supporting documentation in relation to nine entries. It did not provide documentation in relation to sample 8, one of the sampled journal entries, which had been requested. Notwithstanding that HWF had not obtained supporting documentation in relation to six items (items 4,7,8,9,11 and 15), the Senior Audit Manager affirmed in the workpaper that the entry *"appears reasonable"* and *"test ok"*.

5.265 The Respondents noted that the likely reason as to why the audit team had not requested supporting documents for items 4,7,9,11 and 15 was that the team had already tested the area that each respective journal entry related to elsewhere in the audit. However, this explanation was not recorded in the audit file and there was no explanation as to how the need for supporting documentation was negated.

(vii) <u>*Related parties journal entry*</u>

5.266 Sample 8 related to Wyelands Capital Ltd. The entry showed a debit of $200,847.22 on 15 October 2019 with description "*Wyelands Capital Ltd*" and a credit of the same amount with the description "*business rates expense*".

5.267 As noted above, the Respondents did not receive supporting documentation in relation to this sample, and notwithstanding this, affirmed that the entry "*appears reasonable*".

5.268 There is no record in the audit documentation explaining how the audit team was able to conclude that the amounts were expenses paid on behalf of Wyelands Capital or how they were able to apply the planned audit procedure. Further, the Respondents did not carry out suitable alternative procedures or consider treating sample 8 as a misstatement.

5.269 The Respondents explained to Executive Counsel that the journal entry showed a net debit and credit in relation to business rate expenses and inferred that they had

been comfortable with not receiving the requested information because there was no net expense to LCL, and they had received confirmations of the relevant year-end balance indicating that the related party accepted the adjustment. However, there is no explanation in the audit file as to why a related entity needed to transact via LCL.

5.270 Three of the 15 entries sampled were recorded in the audit documentation as being payments made to third parties on behalf of companies related to LCL. Two of the entries were stated to relate to a hedge fund operated by a Hong Kong investment management firm", acting on behalf of a company related to LCL.

5.271 Despite these journal entries being described as payments, the journal does not include an entry to bank or cash. Mr Mott-Cowan subsequently explained to the FRC that these journal entries were not payments, but a "*movement of a payment that had been made on behalf of another company from an expense account to that other company's intercompany account*." This explanation was not documented in the audit file and is inconsistent with the description of the entries as payments in the audit file.

5.272 In any event, the audit team did not obtain any documentation to verify that the journal entries were in fact related to expenses paid on behalf of other companies. Further, the audit team did not consider the rationale for LCL, an entity engaged in commodities trading, acting as intermediary for multiple other companies, despite these journals being selected in the Respondents' small random sample.

Breaches of *Relevant Requirements*

5.273 The Respondents breached paragraph 18(f) of ISA (UK) 315 in that they failed to obtain an understanding of the controls relating to journal entries.

5.274 The Respondents breached paragraph 32 of ISA (UK) 240 because, in designing and performing audit procedures to test the appropriateness of journal entries recorded in the general ledger, the Respondents failed to make inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and adjustments, contrary to paragraph

32(i) of ISA (UK) 240. The Respondents also breached paragraph 26 of ISA (UK) 330 in that they failed to detect that this requirement of ISA (UK) 240 had not been met.

5.275 In breach of paragraph 9 of ISA (UK) 500, the Respondents did not consider the completeness or accuracy of the journal listing provided by LCL, before the sample of journal entries was selected. Further, in breach of paragraph 6 of ISA (UK) 530, the Respondents did not, when designing the sample, consider the characteristics of the population from which the sample would be drawn.

5.276 The risk that the listing of journals provided to the Respondents was not complete and/or accurate was particularly serious because the testing of journal entries that the audit team had planned to carry out was aimed at addressing the risk of management override of controls which, as stated in ISA (UK) 240, was a risk of material misstatement due to fraud.

5.277 In breach of paragraph 9 of ISA (UK) 500, the Respondents failed to evaluate whether the information provided was sufficiently precise and detailed for their purposes, in that they ran keyword searches across the Spreadsheet without noticing that there were no narrations or journal descriptions which could be responsive to the search terms.

5.278 In breach of paragraph 12 of ISA (UK) 300, the audit documentation did not record the fact or reason why the following procedures of the audit programme were not carried out:

5.278.1 Review of 1,741 journal entries exceeding materiality and vouching to back-up documentation;

5.278.2 Review of unusual entries and vouching to back-up documentation; and

5.278.3 Testing of postings from the journals to the nominal ledger and from the nominal ledger to the journals.

5.279 These deviations from the audit plan were significant, being a failure to carry out audit procedures which Mr Mott-Cowan had deemed necessary, at the planning phase of the FY20 Audit, to address a significant risk and a risk of material misstatement due to fraud.

5.280 In breach of paragraph 32(a)(ii) of ISA (UK) 240 the Respondents failed to design and perform audit procedures that tested journal entries made at the end of the reporting period.

5.281 In relation to samples 1, 5 6 and 8, the Respondents breached paragraph 13(c) of ISA (UK) 550 in that they failed to make inquiries with management about the type and purpose of related party transactions, despite having identified related parties as a significant risk. The Respondents also breached paragraph 32(c) of ISA (UK) 240 in relation to samples 1, 5 and 6 in that the Respondents failed to evaluate the business rationale (or lack thereof) for these transactions and whether they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets.

5.282 In relation to samples 1, 5, 6, and 8, the Respondents also breached paragraph 6 of ISA (UK) 500 in that they failed to obtain sufficient appropriate audit evidence in the circumstances.

5.283 Additionally, in relation to sample 8, the Respondents breached paragraph 11 of ISA (UK) 530 in that they failed to treat the sample as a misstatement, after being unable to apply the designed audit procedure or suitable alternative procedures.

5.284 The Respondents breached paragraphs 8(a) and (b) of ISA (UK) 230 in that they failed to record sufficiently to enable an experienced auditor having no previous connection with the audit, to understand the evidence that had been obtained elsewhere during the FY20 Audit and that was relevant to each of the journals with sample numbers 7, 9, 11 and 15.

Breach Area 7: Going Concern

Relevant Requirements and Accounting Standards

5.285 FRS 102, Section 3

5.286 ISA (UK) 330, paragraphs 7(b) and 24.

5.287 ISA (UK) 500, paragraphs 6 and 9.

5.288 ISA (UK) 570, paragraphs 10, 11, 12, 12D-1, 14, and 16.

Overview

5.289 The 2020 Financial Statements were prepared by management on a going concern basis. It was a critical part of the FY20 Audit for the Respondents properly to assess the decision of management to prepare the financial statements on this basis.

5.290 In their Auditor's Report, the Respondents gave an unqualified opinion confirming that the director's use of going concern accounting was appropriate, and that they were satisfied that there were no material uncertainties that required disclosure.

5.291 However, the inadequate audit work throughout the rest of the audit, combined with a lack of professional skepticism, culminated in an inadequate assessment of management's adoption of the going concern basis in the preparation of the financial statements.

5.292 Given LCL's absolute reliance on external finance, the Respondents' review of access to future financing was inadequate. The Respondents failed properly to respond to the forecast of a serious financing shortfall, and uncritically accepted management's assertions, which were clearly uncertain in the light of other evidence available to the Respondents. The Respondents also failed to identify or deal with obvious and important deficiencies in the management accounts and forecasts.

5.293 The work on guarantees was also insufficient and was compounded by the Respondents' conclusion that the guarantees could be paid, if necessary, by relying on the recoverability of trade debtors, their audit work on which was itself inadequate.

5.294 As a result, the Respondents failed adequately to consider whether there was a material uncertainty as to going concern, and whether that ought to be disclosed in the financial statements.

The Audit Work

(i) The Review of Management Accounts

5.295 The review of post year-end management accounts was identified as a necessary audit procedure in the audit documentation.

5.296 The Respondents held in the audit file a document which contained high-level financial information as at 30 June 2020. These were not provided on a month-by-month basis and there was no underlying data provided with the high-level figures. Further, there were no management accounts provided post 30 June 2020 despite the FY20 Audit being signed off in September 2020.

5.297 There was no evidence on the audit file that the Respondents requested the additional detail from management to substantiate the figures as at June 2020. This was so notwithstanding that there were unexplained discrepancies between the information provided in the management accounts and the detailed transactional data that the Respondents had available to them as part of the FY20 Audit.

5.298 In particular, for the three-month period ending 30 June 2020, the management accounts showed lower turnover (c.$950,000 vs c.$1.1 million) and gross profit margin (2.08% vs 3.59%) than the detailed transactional data.

5.299 The Respondents failed to explore the discrepancy. The unexplored and unexplained discrepancy was significant because:

5.299.1 Based on the transactional data (annualised), a 6% increase in turnover from FY20 was identified. As a result, the Respondents concluded that there had been no downturn in trade and that Covid-19 had not adversely impacted trade.

5.299.2 However, when annualised, the turnover figure in the management accounts reflected a 10.4% decrease in turnover from FY20. The Respondents failed adequately to evaluate the transactional data. They therefore failed properly to evaluate or challenge the assertion from management that COVID had not adversely impacted trade based purely on management accounts.

(ii) *Review of Management Forecasts*

5.300 The audit file contained two working papers provided by management setting out management forecasts for the business as at 31 March 2021 and as at 31 March 2022. One working paper provided balance sheet, profit and loss and cash flow

forecasts as at 31 March 2021 and the second working paper provided that information both as at 31 March 2021 and as at 31 March 2022.

5.301 Some of the metrics identified in the forecasts included the following: (a) an increase of short-term borrowings of $61.3m being required in the year to 31 March 2021 ("**FY21**"); and (b) the cashflow forecasts showed an increase in the cash position of $8.1m in FY21 from $2.0m in FY20. A further $2.6m increase was forecast for the year to 31 March 2022 ("**FY22**"). The assumed additional short-term borrowing of $61.3m in FY21 prevented a negative cash flow in FY21.

5.302 The assumptions identified in the audit file included that short term borrowings would increase to $61.5m due to an expected Coronavirus Large Business Interruption Loan Scheme ("**CLBILS**") backed loan in 2021.

Reliability and integrity of the data

5.303 Despite the fact that the two working papers on management forecasts contained figures as at 31 March 2021, the figures were not the same in both working papers. The Respondents failed to investigate the differences between the forecasts as at 31 March 2021in the two working papers.

5.304 Further, the only data provided was high-level balance sheet, profit and loss and cash flow figures at particular year-end dates, i.e. as at 31 March 2021 and as at 31 March 2022. Without a month-by-month breakdown, it was not possible for the Respondents to gain an understanding of LCL's projected cash flow shortfalls:

5.304.1 There was a projected cash flow shortfall of $51.1m in FY21 and $48.49m in FY22. It was impossible to understand from the forecasts when in the financial year the cashflow shortfall was projected to occur and when additional financing would be required.

5.304.2 In the second working paper, the Respondents noted that cash flow was positive in all scenarios, including the sensitised scenarios adopted. However, without looking at intra-year cash flow, it was not possible for that conclusion to be reached because it was not possible to determine whether – even on management's forecasts – there would be material intra-year cash flow difficulties which could cause concerns about LCL's

ability to continue as a going concern either in the base case scenario or in any of the sensitised scenarios.

5.305 The Respondents therefore drew conclusions from the forecasts relating to management's going concern assessment without any understanding of the intra-year cash flow pressures.

5.306 In circumstances where LCL's 2020 Financial Statements showed: (i) LCL had creditors totalling approximately $145m (ii) only c.$2m in cash; (iii) 90% of LCL's current assets were accounts receivables; (iv) where underlying audit evidence showed that there was uncertainty about recoverability of debtors (and the Respondents had failed to carry out an adequate audit in this regard) and (v) there were guarantees totalling up to $211.1m, the Respondents' understanding of cash flow was critical.

5.307 Further, the Respondents failed to carry out any reconciliation between the forecasts and the management accounts.

Limited sensitisation of forecasts

5.308 The second working paper also contained the Respondents' review, consisting of a sensitised forecast for FY21 and FY22 which assumed that (i) the Gross Profit Margin ("**GPM**") did not increase from FY20 levels in either FY21 or FY22 and (ii) the overheads of the business remained the same as in FY19.

5.309 The sensitivities applied were inadequate for the purposes of properly testing the management forecasts.

5.310 The first sensitivity simply assumed a GPM of 2.05% in line with FY20's GPM of 2.07%. There was accordingly no significant downside analysis at all relative to FY20. In selecting a GPM of 2.05%, the Respondents made no reference to the following factors, which cast doubt on the suitability of this figure:

5.310.1 The financial year to 31 March 2018 ("**FY18**") and FY19 both had materially lower GPMs of 1.23% and 1.47% respectively;

5.310.2 FY20 was a pre-COVID financial year, whereas FY21 was likely to be affected by the COVID-19 pandemic; and

5.310.3 GFG Alliance had publicly expressed the view (in June 2020) that there was expected to be a 20% - 40% drop in the steel market in FY21.

5.311 No historical context was accordingly considered in sensitising the GPM in the forecasts, contrary to the Respondents own stated methodology that "*the forecasts have been sensitised based on historic trends…"*. For example, an average GPM over the period FY18, FY19 and FY20 of 1.59% as a basic sensitivity would have disclosed tens of millions of dollars of projected losses in FY21.

5.312 No other sensitivities to the forecasts were carried out.

(iii) *Review of Financing*

Reliance on obtaining new lending

5.313 It was an assumption in the forecasts that LCL would have access to $61.5m of new lending in FY21 (see paragraphs 5.301 to 5.302 above). This figure assumed that neither Greensill nor Wyelands reduced their lending limits or gave notice to terminate their agreements. Should either of those things have occurred, the new lending required could have been significantly higher.

5.314 It is clear from the forecasts that without the assumption that $61.5m of new lending would be secured, there would be very serious concerns about LCL's ability to continue as a going concern in FY21 because it would result in LCL having a *negative* cash flow of $51.1m in FY 21 and $48.49m in FY22. The forecasts were relying on this additional $61.5m lending being obtained despite the fact that it had not yet been secured and no time frame had been provided by management for it being secured.

5.315 The EQCR noted in the audit file that the cashflow and forecasts "*become negative by around $50m in 2021*" if the CLBILS backed loan did not become available and queried how "*the company [would] finance the working capital should this inflow not be secured."* The response noted in the audit file was that this $50m negative cashflow could be mitigated by its existing factoring arrangements with Greensill and other factoring arrangements.

5.316 However, no detailed workings were provided explaining how Greensill or Wyelands[11] factoring additional debtors would be sufficient to cover a $50m negative cashflow. In particular:

5.316.1 The Respondents did not consider that the Greensill facility, as the major financing provider, and the potential CLBILS loan were not comparable. The Greensill facility allowed the financing of individual trades, each of which had low profit margins. Accordingly, in order to generate the $50m through Greensill, LCL would have to achieve an extremely high level of sales. To illustrate, in FY20 $4.2bn of sales only generated $9.5m of total profit and so even doubling the FY20 turnover would not come close to generating enough profit to cover the $50m negative cashflow.

5.316.2 GFG Alliance had publicly stated that there was expected to be a 20%-40% drop in the steel market in FY21, yet the Respondents failed to consider this against the assertion that negative cashflow could be mitigated by its existing factoring arrangements.

5.316.3 As further explained below, there was no headroom left on the Greensill facility.

5.317 Despite these points, the Respondents accepted the explanation from management that existing cash flow could be mitigated by existing factoring arrangements without further analysis or scrutiny.

5.318 The Respondents also accepted, without scrutiny, management's assertion that obtaining new finance or the extension of existing finance was not a concern because "*LCL have a healthy financial background and a strong business reputation in the market.*" This was despite the fact that:

5.318.1 In 2021 it was reported in the press that four banks had ceased doing business with LCL between 2016 and 2019 (HWF was LCL's auditor during this period).

[11] As already noted, Greensill and Wyelands provided approximately 94% of LCL's financing. There were no other significant factoring arrangements in place.

5.318.2 The audit team recorded in the audit file that European banks from whom LCL has traditionally obtained finance had been less supportive in recent time, causing it to resort to alternative financers.

5.318.3 Reports in the media that the GFG Alliance was under stress.

No consideration of the risk of withdrawal of existing facilities

5.319 The Wyelands and Greensill facilities could be cancelled with 30 days' and 90 days' notice respectively. Given LCL's overwhelming reliance on these facilities, the Respondents should have considered the importance of this point.

5.320 However, there is no mention of this issue as a risk anywhere in the going concern analysis despite the fact that it was widely publicised at the time that part of the wider Greensill group (Greensill Bank AG) had come under public pressure to reduce its exposure to the GFG Alliance, thus increasing the chance of this risk materialising within the going concern period.

5.321 The Respondents also gave no consideration to the consequences of the risk of withdrawal of existing lending facilities.

No proper review of breaches of covenant on existing lending facilities

5.322 The Respondents identified breaches of covenants as a significant risk which could lead to the withdrawal of financing facilities and the company's ability to continue as a going concern.

5.323 The Respondents noted in the audit documentation that "*[w]e have also carried out a review of banking covenants and none have been breached in the period*".

5.324 However, as set out in foregoing sections, a number of critical aspects of the covenants applicable under the RPAs were not investigated either properly or at all by the Respondents and so the Respondents were not in a position to be able to draw that conclusion. It is, in particular, explained in paragraph 5.93.4 above that the Respondents did no material audit work on LCL's role as servicer under the Greensill RPA or collection agent for Wyelands. This is notwithstanding that LCL's non-compliance with its obligations could amount to a breach of covenant and an event of repurchase.

5.325 This was highly significant for the going concern assessment because an event of repurchase would require LCL to buy-back the relevant receivables sold to Greensill which could directly impact its cash position and would bring back on to the balance sheet debtors relating to the underlying Customers, the recoverability of which had not been assessed by management or audited by the Respondents, in addition to the corresponding Greensill creditor simultaneously being recognised.

The Greensill facility limit (Maximum OPP)

5.326 The *maximum OPP* for Greensill was $527.5m on the RPA documentation, yet the year-end balance was $879.3m.

5.327 The Respondents sought confirmation from LCL as to whether the limits had been breached and received indirectly via LCL a confirmation letter from an "Analyst" at Greensill addressed to LCL on 02 September 2020 stating that the "*Maximum OPP as of 31/03/2020 was USD 880,000,000*". The Respondents did not contact Greensill directly for this confirmation and had no oversight over the request that was actually made from LCL to Greensill.

5.328 It was indicated in LCL's management letter to the Respondents that this extension had been agreed orally during the financial year, which is not consistent with the terms of the RPA, which stated that changes needed to be in writing.

5.329 The Respondents failed to consider, amongst other things:

5.329.1 Whether the confirmation letter from the Greensill "Analyst" was sufficient appropriate audit evidence, especially given the importance of the Greensill RPA to LCL's business model;

5.329.2 Whether to seek confirmation of the *maximum OPP* at year-end from a more authoritative source;

5.329.3 Evidence suggesting the Greensill balance was in excess of the original OPP by around February 2020, and the Respondents failed to consider whether LCL was in breach of covenant at that point.

5.330 The Respondents appear simply to have accepted the representations from management and the verbal assurance that that there had been no breaches of covenant without further scrutiny or investigation.

The Wyelands facility limit

5.331 The Wyelands facility limit under the RPA was $125,643,000.

5.332 At FY20 year-end, the outstanding Wyelands balance was $96,043,438.32 and was accordingly within the facility limit. However, there is no evidence on the audit file that the Respondents tested the in-year balances to ensure the limit was not exceeded at any point during the period as represented in their conclusion on going concern.

Overdue interest owed to Wyelands

5.333 The Wyelands balance confirmation indicated that there was overdue interest of $3,124,912.37 at FY20 year-end, which was recognised as a cost by LCL.

5.334 There is no evidence on the audit file that the Respondents considered this overdue interest may have been indicative of a breach of terms of the Wyelands facility agreement.

Other Recourse Events under the Greensill RPA and the Wyelands RPA

5.335 It is explained in paragraphs 5.58 - 5.66 above, that the Respondents did not properly consider the different recourse events under either the Greensill RPA or the Wyelands RPA and did not obtain sufficient appropriate audit evidence as to whether any of the relevant provisions that could result in an event of repurchase had been breached during the relevant period.

5.336 This was highly significant to the going concern assessment because any recourse event would have required LCL to repurchase the debtors from either Greensill or Wyelands, necessitating a significant immediate cash outflow when LCL only had $2m in cash at year-end. It would bring back on to the balance sheet debtors relating to the underlying Customers, the recoverability of which had not been assessed by management or audited by the Respondents, in addition to the corresponding Greensill and/or Wyelands creditor simultaneously being recognised.

No assessment of future breaches of covenant on existing lending facilities

5.337 There was no consideration given in the forecasts to the fact that the Greensill credit was only fractionally below the facility limit at FY20 year-end ($879.3m of the $880m extended limit).

5.338 This caused obvious issues for ongoing trading because it meant that there was no head room on the facility to continue to trade.

5.339 The average daily amount of LCL trades factored by Greensill in FY20 was approximately $9.7m, so LCL was likely to have breached this limit on the first working day of the new financial year. This issue was obfuscated in the forecasts by the analysis providing only year-end data, not month-by-month data.

5.340 Whilst the Wyelands facility continued to have some headroom of c.$20m at year-end, taking into account Buyer Limits (see paragraph 5.28), this was also close to the maximum available and was only accessible in respect of trades with specified Customers and subject to their individual Customer limits, rather than being a generally available working capital facility.

5.341 None of these issues were identified or considered by the Respondents as part of their going concern analysis. Further, the Respondents did not plan any audit procedures for going concern directed at considering the risk of any of the other covenants in either the Greensill or Wyelands RPAs being breached during the next 12-month period.

(i) <u>The review of guarantees</u>

5.342 Commitments and guarantees were considered a significant risk by the Respondents.

5.343 It was recorded in the audit file that in FY21 the "current liability" was $35.8m and a further $175.3m was recorded as "non-current liability" (total guarantee liabilities of $211.1m). These related to guarantees over trading and property commitments of other group entities. The Respondents calculated the size of the guarantee on a pro-rata basis according to the end date of the lease or contract vis-a-vis the audit date.

5.344 However, the Respondents did not obtain or review underlying leases or relevant contractual documents to identify whether LCL would be liable to only pay a proportion of the guarantee, or the full amount, depending upon when in the contract the guarantee was called in. The Respondents did not perform any other audit procedures such as contacting the beneficiary of the guarantee to confirm what portion of the total liability could be payable in FY21.

5.345 For example, it was assessed that the current liability for one guarantee which had been provided was $3,083,500 and the non-current liability was recorded as $30,835,000, based on there being eleven years remaining on the guarantee after the audit date. However, the Respondents failed to obtain any evidence that the entire amount would not be due regardless of what point in time in the duration of the lease the guarantee was called in.

5.346 As a consequence, the Respondents failed to obtain sufficient appropriate audit evidence that the sum of contingent liabilities within 12 months of FY20 year-end was $35,834,778. If the total guarantees were called in, $211,122,300 would be due. For context, LCL's net assets were $121,164,251.

5.347 The Respondents noted, in the conclusion on guarantees, that there was insufficient cash to cover them should they be called within the 12-month going concern period. However, the Respondents considered that because the majority of debtors were deemed recoverable, LCL would be able to continue trading (albeit with some movements required on the working capital) if all potential commitments were called in in the same 12-month period post signing.

5.348 However, this conclusion was reached on the basis that the FY21 current liability was calculated as $35,834,778, rather than $211,122,300, based upon audit work which was superficial and incomplete. Further, as explained above, the audit work carried out in relation to the recoverability of trade debtors was also superficial and incomplete and could not provide any real assurance over LCL's ability to pay the guarantees should they all be called in.

(ii) *The relevant disclosure in the financial statements*

Going concern

5.349 The disclosure wording contained in the 2020 Financial Statements is as follows:

> "*The director has considered the effect of the Covid-19 outbreak. The director considers that the outbreak is unlikely to cause a significant disruption to the company's business and is confident that the company can continue as a going concern. The company's management has produced projected financial forecasts for the financial years ended 2021 and 2022. Management has assessed the working capital requirements and the director is confident in the company's ability to use its existing facilities and availing new financing facilities for continued business operations. Based on the assessments completed the director has a reasonable expectation that the company has adequate resources to continue in operation for the foreseeable future*."

5.350 This wording was provided by LCL on 23 September 2020, a day before the 2020 Financial Statements were signed off. This wording made no reference at all to the reliance that was being placed by management in its forecasts on obtaining new financing and that issue was obfuscated by referring together to existing and new facilities. The Respondents had earlier noted on the audit file, in relation to forecasts, that "*[g]oing concern policy to be updated to state that the going concern position is reliant upon the ability to raised additional borrowings if required*."

5.351 In response to receiving the draft wording on 23 September 2020, the Senior Audit Manager asked whether the new facilities were now available and "*if not, does the company have sufficient existing facilities to meet the working capital requirements*". LCL responded that:

> "*With respect to the working capital requirements of LCL, the existing financing facilities as at 31st March 2020 are also good enough for LCL's business and LCL is not in working capital crunch as at 31st March 2020.*
> *Further in the financial year beginning from 01st April 2020, LCL have already received new financing worth of $ 35 Mln by now (Increase in* [Facility Provider 1] *facility of $ 24M and new facility from* [Facility Provider 2]*$ 11M) which adds up to the funding available to LCL*"

5.352 LCL's response failed to address the issue of whether LCL would have sufficient working capital facilities in the future if new financing was not obtained.

5.353 On 24 September 2020 (the date the 2020 Financial Statements were signed), the Respondents received a Letter of Representation, signed by the Shareholder which stated, amongst other things, that he considered the entity to be a going concern and that financing had been extended by facility providers. However:

5.353.1 The Respondents had been given no proper answer to their main question on the going concern analysis (i.e. whether LCL would have sufficient working capital facilities throughout the going concern period if new financing, as assumed in the forecasts, was not obtained); and

5.353.2 The only stated extension of its existing financing arrangements was the [Facility Provider 1] facility, but which was an uncommitted facility, and which was of a low value compared to the extent of LCL's trading.

5.354 The Respondents accepted the revised wording provided by LCL without considering if they ought to qualify their opinion in the Auditor's Report. They failed to consider or address whether LCL's reliance on a new financing arrangement being obtained reflected a material uncertainty that required disclosure.

Guarantees

5.355 Note 20 to the 2020 Financial Statements states that: "*The total amount of the guarantee obligations was $42,494,986 (2019: $48,837,915) at year end.*"

5.356 It appears that the $42.5m figure was based on an assessment of the proportion of the total guarantees which were deemed at risk of being called in during FY21. As at the audit signing date, this figure reduced to the $35.8m figure quoted in paragraph 5.343 above, due to expiry of some of the guarantees within that intervening period.

5.357 However, the Respondents did not obtain or review underlying leases or relevant contractual documents to identify whether LCL would be liable to only pay a proportion of the guarantee, or the full amount, depending upon when in the contract the guarantee was called in. Neither did they perform any other audit procedures such as contacting the beneficiary of the guarantee to confirm what portion of the total liability could have been payable in FY21.

5.358 As a consequence, the Respondents failed to obtain sufficient appropriate audit evidence that the stated value of the guarantees in the financial statements was accurate.

Breaches of *Relevant Requirements*

(i) Breaches relating to the evaluation of management's going concern assessment

5.359 The Respondents failed, in breach of paragraphs 10 and 12 of ISA (UK) 570, properly to evaluate LCL's assessment of its ability to continue as a going concern, including failing to give adequate consideration to whether a material uncertainty existed, and failed to remain alert throughout the audit, in breach of paragraph 11 of ISA (UK) 570, for evidence of events or conditions that may cast significant doubt on LCL's ability to continue as a going concern.

5.360 This included a general failing as part of that evaluation to consider properly whether LCL's going concern assessment included all relevant information in breach of paragraph 14 of ISA (UK) 570.

5.361 In particular, as regards the management accounts, the Respondents:

5.361.1 failed to evaluate properly or at all the underlying data underpinning management accounts to June 2020; and

5.361.2 failed properly to evaluate or challenge the assertion from management that COVID had not adversely impacted trade based purely on management accounts, whereas the detailed transactional data indicated that there had in fact been a 10.4% decrease in annual turnover.

5.362 The failure to evaluate properly the underlying data underpinning management accounts to June 2020 was also a breach of paragraph 9 of ISA (UK) 500 properly to assess the reliability of information used in an audit procedure. In further breach of paragraph 9 of ISA (UK) 500, the Respondents failed to reconcile the inconsistencies in data between management accounts and the detailed transactional data that the Respondents had available to them as part of the FY20 Audit.

5.363 As regards the review of forecasts and financing, in breach of paragraphs 10, 12 and 14 of ISA (UK) 570:

5.363.1 The Respondents failed to consider the potential inadequacy of the forecasts produced by LCL, including the risks and limitations associated with them not including a month-by-month breakdown.

5.363.2 The Respondents drew conclusions from the forecasts relating to management's going concern assessment without any understanding of intra-year cashflow pressures.

5.363.3 No reconciliation was carried out between the forecasts and the management accounts.

5.363.4 No proper evaluation was carried out as to the significance and risk to LCL in FY21 if the new lending on which the forecasts were premised was not obtained, despite the fact that this was a specific issue raised by the EQCR during the audit process.

5.363.5 Instead of evaluating that issue properly, the Respondents simply accepted the explanation from management that existing factoring arrangements with Greensill and other factoring arrangements could mitigate that shortfall, without any proper consideration as to how that would be possible given that (i) there was no headroom left on the (extended) Greensill facility, and (ii) the Greensill RPA was not a simple loan facility but required additional trading to take place to generate significant additional financing.

5.363.6 The Respondents also accepted management's assertion that obtaining new financing was not a concern because LCL had a healthy financial background and strong business reputation in the market without question, despite the evidence that LCL had experienced difficulties obtaining financing.

5.363.7 The Respondents failed to consider the risk of withdrawal of existing financing facilities despite the fact that both the Wyelands and Greensill facilities could be withdrawn on demand on 30 days and 90 days' notice respectively and despite the growing public pressure, as reported in the

media, on Greensill at the time concerning its existing exposure to the GFG Alliance.

5.363.8 No proper review was carried out as to whether there had been any breaches of covenant under the Wyelands or Greensill RPAs which could result in facilities being withdrawn – including as to (i) whether the *maximum OPP* under those facilities had been breached during the prior financial year, (ii) compliance with the Respondents' Collection Agent activities under those facilities and/or (iii) whether the outstanding interest payments owed to Wyelands was a breach of the Wyelands RPA.

5.363.9 No proper consideration was given to whether there had been any other events of repurchase under either the Greensill or Wyelands RPAs which could require LCL to repurchase receivables and the Respondents simply accepted at face value management's assertion that there had not been.

5.363.10 No consideration was given to how LCL could continue trading in FY21 when it was already at its maximum (extended) OPP under the Greensill RPA and the limited headroom it had under the Wyelands RPA only permitted trades with specified clients up to the allocated limits.

5.363.11 The Respondents failed to evaluate the forecasts by reference to meaningful sensitisations. This included the fact that the Respondents:

5.363.11.1 Only sensitised gross profit margin to the FY20 level – ignoring the much lower gross profit margin levels in FY19 and FY18 despite their own methodology in in their working paper stating that "*the forecasts have been sensitised based on historic trends…*".

5.363.11.2 No sensitivity was accordingly applied to reflect the risk that COVID could adversely impact the business in FY21/FY22 relative to FY20, despite the GFG Alliance being on public record as saying the demand for steel had dropped and was likely to continue to do so.

5.363.11.3 No other sensitivities were conducted except for an assumption that certain cost savings projected for FY21 and FY22 did not materialise.

5.364 The Respondents' failure to design and perform audit procedures to obtain sufficient appropriate audit evidence as to whether the Greensill OPP or Wyelands facility limit had been breached during the financial year was a breach of paragraph 6 of ISA (UK) 500.

5.365 As regards the review of guarantees:

5.365.1 The Respondents acknowledged that the intra-group guarantees could not be met by LCL if they fell due for payment in FY21 or FY22 unless the trade debtors were substantially or fully recoverable. On that basis, the Respondents concluded that LCL could continue trading even if the guarantees became payable.

5.365.2 However, in breach of paragraph 12D-1 of ISA (UK) 570 and paragraph 6 of ISA (UK) 500, that conclusion was premised on the sum of the contingent liability within 12 months after FY20 year-end within the going concern analysis being $35,834,778. However, the Respondents failed to obtain sufficient appropriate audit evidence that this was the relevant figure, rather than the total value of the guarantees ($211,122,300).

5.365.3 Furthermore, the audit work carried out to assess the recoverability of debtors was inadequate and did not provide sufficient appropriate audit evidence on which the Respondents could properly draw that conclusion.

5.365.4 In breach of paragraph 6 of ISA (UK) 500, the Respondents failed to obtain sufficient appropriate audit evidence that the relevant figure for the guarantees disclosed in Note 20 of the financial statements was $42.5m.

5.365.5 Further, in breach of paragraph 24 of ISA (UK) 330, the Respondents failed to evaluate whether the overall presentation of the financial statements was in accordance with FRS 102, in that they failed to consider whether the financial statements were presented in a manner that correctly described

the value of the guarantees, based on the underlying conditions, being the specific terms of those guarantees.

(ii) *Breaches of professional skepticism relating to the evaluation of management's going concern assessment*

5.366 The Respondents demonstrated a lack of professional skepticism in the evaluation of management's going concern assessment in breach of paragraph 12D-1 of ISA (UK) 570 by:

5.366.1 accepting at face value management accounts without seeing underlying data or assessing their reliability;

5.366.2 failing to properly consider the impact of the following on LCL's forecasts including: (i) whether the management accounts had been factored in; (ii) global demand for products traded by LCL; (iii) the impact of the Covid-19 epidemic; (iv) news articles about GFG and the Shareholder; and (v) LCL's reliance on the wider GFG group;

5.366.3 failing to consider the risks and limitations of relying on forecasts without a month-by-month breakdown of forecasts (such as there being no visibility as to any intra-year financing challenges), meaning that the Respondents were not in a position to apply sufficient critical assessment to the forecasts;

5.366.4 failing properly to question whether the fact that management were unable to provide a month-by-month breakdown of the forecasts undermined the reliability of the forecasts as a whole;

5.366.5 not seeking to understand from management when LCL's cashflow was projected to turn negative in FY21 without additional lending being obtained, despite this being an area raised by the EQCR;

5.366.6 not carrying out any meaningful sensitisation to the forecast figures;

5.366.7 not seeking to evaluate the prospects of additional lending being obtained and instead accepting management's assertions at face value that LCL would be able to access either (i) additional financing under the existing

Greensill facility or (ii) new lending, despite the Respondents having evidence that both those assertions were (at best) doubtful;

5.366.8 accepting inadequate answers received on 24 September 2020 to questions about LCL's reliance on obtaining new lending. Despite the importance of the issue and the lack of details provided, there were no follow up questions from the Respondents and the financial statements were simply signed without any clarity on these points being obtained.

(iii) *Breaches in relation to obtaining sufficient appropriate evidence in connection with a potential material uncertainty*

5.367 The Respondents identified LCL's reliance on obtaining new lending to avoid a substantial cashflow shortfall as something that gave rise to the need for an amended disclosure in the financial statements.

5.368 This was clearly an issue that the Respondents considered may cast significant doubt on the ability of LCL to continue as a going concern resulting in the need for adjustment to the disclosure in the financial statements.

5.369 It was accordingly incumbent on the Respondents, under paragraph 16 of ISA (UK) 570, to obtain sufficient appropriate audit evidence as to whether a material uncertainty existed. Since going concern had been identified as a significant risk, the Respondents were required to obtain particularly persuasive audit evidence on that point.

5.370 In breach of paragraph 16 of ISA (UK) 570 and paragraph 7(b) of ISA (UK) 330, the Respondents failed to obtain sufficient appropriate audit evidence in relation to the obtaining of new lending facilities in FY21 and the risks associated with that reliance.

5.371 In particular:

5.371.1 No evidence was obtained as to when any cashflow shortfall might materialise during FY21 in the absence of new financing being obtained or as to how long management would have to find new financing before any cashflow shortfall materialised;

5.371.2 No evidence was obtained to support management's assertion that additional financing from the RPAs could mitigate any cashflow shortfall, including particularly as to (i) whether Greensill would continue to provide financing beyond its (already extended) *maximum OPP* and (ii) what level of additional trading would be required to generate the requisite level of cashflows;

5.371.3 No meaningful sensitivity of the forecasts was carried out to evidence other scenarios that could arise and to assess the extent of the cashflow risks being run by LCL, as well as what level of additional financing would be required to cover those risks;

5.371.4 No evidence was obtained from management in relation to any contingency plans if new financing was not obtained by LCL; and

5.371.5 No evidence was obtained in relation to the answers given by management on 24 September 2020 relating to two "new facilities" that were referred to by management and which related directly to this issue.

6. SANCTIONS – HWF

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. In considering *Sanctions* to be imposed on HWF, Executive Counsel has, in summary, considered the following matters in accordance with the Policy.

Nature, seriousness, gravity and duration of the breaches

6.3. As a result of the breaches of *Relevant Requirements*, the Audit failed in its principal objective namely to obtain reasonable assurance about whether the 2020 Financial Statements as a whole were free from material misstatement.

6.4. The audit areas relevant to the breaches (in particular, Going Concern) are fundamental to statutory audits and it is of the utmost importance that they are audited in accordance with *Relevant Requirements*.

6.5. The breaches of *Relevant Requirements*:

6.5.1. were serious and numerous;

6.5.2. demonstrate a pervasive lack of professional skepticism applied in the seven areas relevant to the breaches referred to in this *Final Settlement Decision Notice*;

6.5.3. relate to one audit year.

6.6. Whilst it is not alleged that the 2020 Financial Statements were in fact misstated, in aggregate the breaches undermined confidence in the standards of conduct in general of *Statutory Auditors* and *Statutory Audit Firms*, and in S*tatutory Audit*.

6.7. The breaches were neither intentional, dishonest, deliberate nor reckless.

6.8. HWF did not stand to gain any profit or benefit, beyond the fee chargeable for the Audit, from the breach of the *Relevant Requirements*.

Identification of *Sanction*

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

6.9.1. a **financial penalty** of £200,000 discounted for admissions and early disposal by 30% so that the financial penalty payable is £140,000, to be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;

6.9.2. a published statement in the form of a **severe reprimand**; and

6.9.3. a **declaration** that the Auditor's Report signed on behalf of HWF did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*.

Aggravating and mitigating factors

6.10. There are no aggravating or mitigating factors that have not already been considered in the context of the seriousness of the breaches.

6.11. HWF dealt timeously, properly and fully with all requests for information and provided the level of co-operation required of them during the investigation as required.

Deterrence

6.12. 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

6.13. Having taken into account the full admissions by HWF and the stage at which those admissions were made (within Stage 1 of the case in accordance with paragraph 84 of the Policy), Executive Counsel determined that a reduction of 30% as to the financial sanction is appropriate, such that a financial penalty of £140,000 is payable.

Other considerations

6.14. In accordance with paragraph 47(c) of the Policy, Executive Counsel has taken into account the size / financial resources and financial strength of HWF and whether any financial penalty would be covered by insurance.

6.15. For the financial year ending 30 April 2024, the total turnover for HWF was £33,109,913 and the estimated turnover for HWF's audit work was £6,169,333.

7. SANCTIONS – Mr Mott-Cowan

7.1. In considering the *Sanctions* to impose on Mr Mott-Cowan, Executive Counsel has, in summary, considered the following factors in accordance with the Policy.

Nature, seriousness, gravity and duration of the breaches

7.2. The features of the case set out at paragraphs 6.3 to 6.7 above apply equally to Mr Mott-Cowan. The breaches of the *Relevant Requirements* were neither intentional, dishonest, deliberate nor reckless.

7.3. Mr Mott-Cowan did not stand to gain any profit or benefit from the breaches of the *Relevant Requirements* (save to the extent that he had an interest in HWF being paid engagement fees for the Audit).

7.4. At the time of the Audit, Mr Mott-Cowan was a partner of HWF with 19 years' auditing experience, and has been an audit partner since 2009. He was the Head of Audit at HWF between 2013 and 2024.

7.5. Mr Mott-Cowan voluntarily ceased his audit practice from the end of 2025. He will no longer be acting as a Responsible Individual or undertaking any audit work, and has been removed from the ICAEW Register of Statutory Auditors.

7.6. Mr Mott-Cowan has no previous adverse compliance or disciplinary record.

Identification of *Sanction*

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

7.7.1. a financial penalty of £25,000 discounted for admissions and early disposal by 30% so that the financial penalty payable is £17,500, to be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;

7.7.2. a published statement in the form of a severe reprimand; and

7.7.3. a declaration that the Auditor's Report signed by Mr Mott-Cowan did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*.

Aggravating and mitigating factors

7.8. There are no aggravating or mitigating factors that have not already been considered in the context of the seriousness of the breaches.

Deterrence

7.9. 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

7.10. Having taken into account the full admissions by Mr Mott-Cowan and the stage at which those admissions were made (within Stage 1 of the case in accordance with paragraph 84 of the Policy), Executive Counsel determined that a reduction of 30% as to the financial penalty is appropriate, such that a financial penalty of £17,500 is payable.

Other considerations

7.11. Executive Counsel has considered the applicability of paragraphs 47(d) and 50 of the Policy as regards Mr Mott-Cowan.

8. COSTS

8.1 Executive Counsel requires that the Respondents pay costs in this matter in the amount of £837,744. Such costs shall be paid no later than 28 days after the date of this *Final Settlement Decision Notice*.

Signed:

[Redacted.]

ANDREW TWOMEY

ACTING DEPUTY EXECUTIVE COUNSEL

Date: 28 May 2026

APPENDIX 1

DIAGRAM IN RELATION TO THE STAGES OF A GREENSILL 'BACK-TO-BACK' TRANSACTION

