Financial Reporting Council

IN THE MATTER OF

THE EXECUTIVE COUNSEL OF THE FINANCIAL REPORTING COUNCIL

-and-

(1) SAFFERY LLP

(2) MR MICHAEL DI LETO

EXECUTIVE COUNSEL'S FINAL SETTLEMENT DECISION NOTICE

Pursuant to Rule 133 of the Audit Enforcement Procedure

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.

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I INTRODUCTION

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**"), revised in July 2026.

2. The AEP sets out the rules and procedure for the investigation, prosecution and sanctioning of breaches of *Relevant Requirements*, as defined in Rule 1 of the AEP and Regulation 5(11) of the Statutory Auditors and Third Country Auditors Regulations 2016 ("**SATCAR**").

3. The AEP contains a number of defined terms, and, for convenience, those defined terms are also used within this document (appearing in *italics*). Additional terms have been specifically defined in this *Final Settlement Decision Notice.*

4. Within this *Final Settlement Decision Notice,* "**Respondents**" means:

   4.1 Saffery LLP[1] ("**Saffery**") which was the *Statutory Audit Firm* for the *Statutory Audit* of the financial statements of Greensill Capital (UK) Limited ("**GCUK**") for the year ended 31 December 2019 (the "**FY2019 Financial Statements**"), (the "**FY2019 Audit**" or the "**Audit**", as the context requires); and

   4.2 Mr Michael Di Leto ("**Mr Di Leto**"), a partner of Saffery and a member of the ICAEW, who was the *Statutory Auditor* responsible for the FY2019 Audit and signed off the Audit report on behalf of Saffery.

5. In accordance with Rule 127 of the AEP, Executive Counsel entered into settlement discussions with the Respondents.

6. A *Proposed Settlement Decision Notice* was issued by Executive Counsel on 30 July 2026 pursuant to Rule 128 of the AEP in relation to the conduct of the Respondents in respect of the FY2019 Audit. The Respondents provided written agreement to the *Proposed Settlement Decision Notice*, pursuant to Rule 130 of the AEP, on 30 July 2026. The *Convener* subsequently appointed an *Independent Reviewer*, pursuant to Rule 131 of the AEP, to consider the *Proposed Settlement Decision Notice*. On 13 August 2026, the *Independent Reviewer* approved the issuance of this *Final Settlement Decision Notice* pursuant to Rule 132(a) of the AEP.

7. In accordance with Rule 131 of the AEP, this *Final Settlement Decision Notice* sets out:

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

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

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

[1] The firm changed its name from Saffery Champness LLP on 4 September 2023.

II EXECUTIVE SUMMARY

A. Overview of the breaches of *Relevant Requirements*

8. The audit work carried out by the Respondents in connection with the FY2019 Audit was inadequate in numerous respects and repeatedly failed to comply with the *Relevant Requirements* under the International Standards on Auditing (UK) ("**ISAs**").

9. The breaches of the *Relevant Requirements* set out in this *Final Settlement Decision Notice* were serious and pervasive across multiple areas of the FY2019 Audit.

10. The purpose of an audit is to enhance the degree of confidence of intended users of the financial statements. An audit that is not conducted in compliance with ISAs cannot achieve that purpose. The requirements built into the ISAs acted as safeguards, which were essential to enabling the purpose of the FY2019 Audit to be achieved. These were fundamentally undermined by the Respondents in the conduct of the FY2019 Audit and consequently the reasonable assurance that the Audit should have provided was not delivered. As a result, the FY2019 Audit could not provide an investor or a user with sufficient confidence in the FY2019 Financial Statements.

11. The business operations of GCUK as a provider of various forms of working capital financing ("**WCF**") to customers were complex, as explained in Part V, section 3 below, and the audit work conducted by the Respondents needed to provide them with a proper understanding of that complexity and be responsive to the specific risks of material misstatement associated with GCUK's business.

12. However, inadequate consideration was given to where the particular risks of material misstatement arose in relation to GCUK's business operations and the audit work that was carried out by the Respondents was often superficial, with recurring failures to obtain sufficient appropriate audit evidence in relation to key aspects of the audit and to treat the information obtained from GCUK with the required levels of professional scepticism.

13. The result was an audit that failed to respond properly to both the identified audit risks and other risks that should have been, but were not, identified. The FY2019 Audit was accordingly not fit for purpose in terms of adequately reducing the risk of material misstatement in the FY2019 Financial Statements to an acceptably low level.

14. The five audit areas, and the failings identified within each, that are addressed in the remainder of this *Final Settlement Decision Notice* are summarised below.

B. Planning and Risk Assessment

15. Adequate audit planning is essential to ensure that an audit is performed in an effective manner. In addition, adequate risk assessment is essential to ensure that risks of material misstatement are properly identified and assessed. This in turn ensures that appropriate audit procedures are designed and implemented to address those risks of material misstatement. Failures to plan, or to adequately plan, an audit and/or to perform adequate risk assessment procedures increase the risk of there being an ineffective audit process.

16. There were numerous failures to plan the FY2019 Audit and carry out the required risk assessment procedures properly, including:

16.1 A failure to ensure audit quality control was maintained, notwithstanding that the audit was inherently high risk, by the appointment of an Engagement Quality Control Reviewer ("**EQCR**") (Adverse Finding 1).

16.2 A failure to understand properly GCUK and its business environment (Adverse Finding 2). The information obtained on GCUK's business was insufficient to obtain a proper understanding of such a complex business, including as to the nature and variety of its transactions, the accounting treatment required, the accounting estimates being made and the risks involved in the business.

16.3 A failure to identify and assess the risks of material misstatement properly, both generally and specifically in relation to fraud (Adverse Finding 3 and Adverse Finding 4). The work carried out by the Respondents was wholly deficient in that there was inadequate, if any, design and formulation of the risk assessment procedures during the audit planning process and consequently the work performed to try to identify and assess risks was piecemeal and ineffective without sufficient explanations being provided as to how conclusions were arrived at. There were six risks identified by the Respondents, which were typically described in the audit workpapers as significant risks, albeit two were instead described as key risks in the Audit report (the six "**Significant Risks**").

16.4 A failure to identify and evaluate properly GCUK's internal controls (Adverse Finding 5). This included failing to consider whether substantive procedures alone could provide sufficient audit evidence and, if there was no expectation that controls were operating effectively and therefore no reliance was to be placed on controls such that no controls testing took place, the extent to which the design of substantive audit testing needed to take this into account. The work performed to try and understand GCUK and its environment only identified controls at a high level in an incomplete and piecemeal way and omitted to identify fundamental controls. There was no attempt to evaluate the design and implementation of controls, including those relevant to the Significant Risks identified (including significant fraud risks).

16.5 A failure to develop an audit plan that included a description of the nature, timing and extent of planned risk assessment procedures and planned further audit procedures at the assertion level (Adverse Finding 6)

C. Accounting Policies

17. An assessment of whether there has been correct application of appropriate accounting treatments by the preparers of financial statements is critical to any audit. Specifically, it ensures that financial events are accurately represented in the financial statements and that users of those financial statements are presented with a true and fair view of an entity's financial position and performance.

18. GCUK's selection and application of accounting policies was fundamental to how its assets and liabilities were presented in the FY2019 Financial Statements and how its revenue should be recognised. Which accounting treatment should apply required complicated assessments to be made as to how to apply the detailed requirements of two of the International Financial Recording Standards ("**IFRS**") (IFRS 9 and 15).

19. GCUK's approach to selecting and applying accounting policies had the effect of maximising revenue recognition and minimising liabilities appearing on GCUK's balance sheet and so was particularly susceptible to management bias. Whilst no conclusion has been reached on the question of whether the accounting treatments applied by GCUK were correct, the importance of those treatments to the presentation of the FY2019 Financial Statements is clear when it is considered that, had an alternative approach been adopted then users of financial statements may have been presented with a different picture as to GCUK's exposure to liabilities and profitability in FY2019.

20. The Respondents identified revenue recognition and completeness as a significant audit risk and the appropriateness of the selection and application of accounting policies was a significant part of that risk.

21. However, the Respondents failed to evaluate GCUK's assessment of how the requirements of IFRS 9 and IFRS 15 applied to the specific transactions it entered into, considering how its business was structured and operated in practice. They failed to properly reassess the appropriateness of the accounting policies adopted by GCUK after the Respondents were informed that the wider corporate group (excluding GCUK) would be changing accounting policies in the next financial year (Adverse Finding 7).

D. Revenue

22. Revenue is a critical metric within the financial statements and feeds into numerous key calculations, which enable users of those financial statements to assess the entity's performance and viability and thereby make informed investment decisions.

23. Ensuring that an entity's financial statements recognise revenue both accurately and completely is accordingly an essential part of an audit.

24. As noted above, the Respondents identified revenue recognition and completeness as giving rise to a "*significant*" risk of material misstatement. As GCUK operated through the generation of revenue via a high volume of complex and time sensitive transactions, it was particularly important for the Respondents to have an adequate understanding of GCUK's business model, to assess properly whether revenue generated from different transactions was recognised appropriately.

25. The Respondents, however, failed to design and perform adequate audit procedures to address that risk and to obtain sufficient appropriate audit evidence in relation to the accuracy and completeness of GCUK's revenue. The Respondents failed to: evaluate whether the population of revenue items tested was complete; assess whether certain revenue items had been properly recognised at all, or in the correct financial period; and consider whether the variability of revenue generated by the transactions entered into impacted on GCUK's assessment of revenue recognition. Where the Respondents relied on information provided to them by GCUK, they failed to assess its reliability (Adverse Finding 8).

26. As part of the failure to obtain sufficient appropriate audit evidence, the Respondents failed to sample properly the revenue items tested. They failed to both: consider or explain the appropriateness of the reasoning behind the sample sizes selected or how the sample size selected reduced the sampling risk to an acceptably low level; and consider whether the sample selected properly reflected the characteristics of the populations being sampled (Adverse Finding 9).

27. The Respondents also failed to respond appropriately to the risk of fraud in connection with the reporting of revenue (Adverse Finding 10). The approach taken by the Respondents was wholly inadequate, in part because no evaluation was carried out of any of the internal controls associated with revenue recognition and because no consideration was given as to whether there were any characteristics within revenue streams or transactions tested which gave rise to a risk of fraud.

E. Expected Credit Losses

28. Under IFRS 9, entities are required to assess potential losses or impairments across all financial instruments and recognise a provision in their financial statements to reflect the associated risk, referred to as "*Expected Credit Losses*" ("**ECLs**"). Disclosure of ECL provisions is important as it provides users of financial statements with transparency on the amount of future credit losses that the entity is at risk of incurring, which could impact its cash flow and financial stability.

29. The provision for ECL is a complex accounting estimate, which requires a number of critical judgements to be applied in relation to numerous inputs to the overall calculation. Unsurprisingly, the valuation and recoverability of assets (that included the ECL provision) was identified by the Respondents as a significant risk and, as a significant accounting estimate, could be subject to the risk of management bias.

30. The audit work carried out by the Respondents in relation to GCUK's estimation of the ECL provision was wholly inadequate, from the audit planning and risk assessment through to the disclosures in the FY2019 Financial Statements.

31. The inadequacies included the following failings:

    31.1 Failure to identify and assess properly the risks of material misstatement relating to the estimation uncertainty associated with the ECL provisions (Adverse Finding 11). The work undertaken to assess the risk arising from the ECL provision was extremely limited and insufficient in the circumstances.

    31.2 Failure to respond to the Significant Risk arising and to obtain sufficient appropriate audit evidence in relation to the reasonableness of the ECL provision, in the following contexts:

        a. Evaluating GCUK's overall methodology and approach to the ECL calculation (Adverse Finding 12);

        b. Testing of individual balances included in and excluded from the ECL calculation (Adverse Finding 13);

        c. Testing GCUK's assessment of "*distressed debtors*" (Adverse Finding 14); and

        d. The significant adjustments made to the ECL provision by GCUK referred to as the "*Credit Structure Reduction Factor*" and the "*Haircut*" - introduced for the first time in FY2019 and which resulted in a $29.8 million reduction to the final ECL provision. (Adverse Finding 15).

32. Given the subjective nature of:

    32.1 the assessment of distressed debts;

    32.2 the application of the Credit Structure Reduction Factor; and

32.3 the application of the Haircut:

The judgements reached by GCUK on these matters were particularly susceptible to management bias. However, the Respondents failed to review these judgements properly for bias or to evaluate whether the circumstances producing the bias, if any, represented a risk of material misstatement due to fraud (as set out in Adverse Finding 14 and Adverse Finding 15).

33. The Respondents also failed to evaluate the adequacy of the disclosures in the FY2019 Financial Statements relating to the ECL provision (Adverse Finding 16). GCUK was required to disclose any changes in the estimation techniques made during the reporting period and the reasons for those changes. However, there was no mention made in the FY2019 Financial Statements of either the Credit Structure Reduction Factor or the Haircut.

34. Overall, the Respondents failed to evaluate adequately the reasonableness of the ECL provision and determine misstatement (Adverse Finding 17).

F. Going Concern

35. The going concern assumption is a fundamental accounting principle that assumes that an entity will continue its operations for the foreseeable future, typically at least for 12 months from the date of the financial statements. It is an important piece of information relied upon by users of financial statements, as it underpins investments and other key decisions. It is therefore essential that the assumption, where made, is based on accurate information and takes into account all relevant circumstances that could affect the entity's viability.

36. Where there are uncertainties about events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern in the future, but it is nonetheless considered appropriate for the entity to prepare its accounts on a going concern basis, those uncertainties are required to be disclosed in the financial statements when they are material.

37. The FY2019 Financial Statements were prepared by GCUK on a going concern basis. Although going concern was not identified by the Respondents as a significant risk area for the Audit, the Respondents' evaluation of GCUK's assessment of going concern was critical to the Audit for the reasons above.

38. However, the Respondents failed to perform appropriate risk assessment procedures and to obtain sufficient appropriate audit evidence in relation to the going concern assessment made by GCUK.

39. This included failing to:

39.1 consider whether: ongoing trade credit insurance (which was critical to GCUK's business operations) would continue to be available to GCUK, specifically in light of events and conditions known at the time; and the ongoing appetite or capacity of investors to which GCUK sold its receivables would continue, either at all or at the levels presupposed by GCUK's assumptions about future revenue (Adverse Finding 18);

39.2 assess adequately whether the assumptions made by GCUK in its cashflow forecasts as to the future availability of third-party financing (which were critical to the conclusion that GCUK would have sufficient cashflow) were appropriate or justified (Adverse Finding 19); and

39.3 consider adequately whether other underlying assumptions in GCUK's cashflow forecasts were reasonable (Adverse Finding 20).

G. Review of Audit Evidence and Quality Control

40. Adequate direction, supervision and review of an audit by an engagement partner and a proper assessment of whether sufficient appropriate audit evidence has been obtained before the audit report is completed, is essential to any audit in order to ensure that the audit report issued is appropriate in the circumstances. Inadequate review and/or insufficient direction and supervision of the audit significantly increases the risk that the audit report will fail to meet appropriate standards.

41. However, the Respondents failed to review and evaluate properly whether sufficient appropriate audit evidence had in fact been obtained (Adverse Finding 21).

42. This was evident from the fact that:

42.1 There was no explanation in the relevant working papers as to how certain judgements and conclusions, as referred to in this *Final Settlement Decision Notice*, were reached during the audit process. This in turn meant that no proper review could be carried out simply by reviewing the working papers themselves.

42.2 In light of the extensive failings in the audit work in relation to Planning and Risk Assessment, Accounting Policies, Revenue, ECL and Going Concern, it ought to have been obvious on any proper review that the audit work that had been carried out was deficient in numerous important respects.

43. In addition, the Respondents failed to ensure that appropriate consultations took place on difficult or contentious audit matters (Adverse Finding 22). This included a failure to: ensure proper consultation took place in relation to matters relevant to GCUK's selection and application of accounting policies and its going concern assessment; and consider properly whether specialised skills or knowledge were required in relation to one or more aspects of the ECL provision in order to obtain sufficient appropriate audit evidence.

H. Professional Scepticism

44. It was fundamental to the audit process that the Respondents approached the Audit with appropriate levels of professional scepticism throughout.

45. This involves an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence in light of the circumstances.

46. The Respondents, however, repeatedly failed to exercise adequate levels of professional scepticism and predominantly relied instead on information provided by GCUK without adequate critical assessment of the reliability of that information (Adverse Finding 23). The absence of adequately designed audit procedures and adequate evaluation of the results of such procedures, as would have been expected had appropriate levels of professional scepticism been applied, was a recurring theme across the Audit, resulting in a generally superficial and inadequate approach that underpinned many of the other Adverse Findings.

47. This was particularly evident from the Respondents failure to adequately question or critically assess for themselves:

47.1 key matters and information provided by GCUK as part of their planning and risk assessment;

47.2 how the requirements of IFRS 9 and IFRS 15 applied to GCUK's business, including in light of potentially conflicting information;

47.3 the information provided by GCUK in relation to revenue, including in terms of the completeness of the revenue population, whether revenue had been recorded in the correct financial period and the high variability of net returns;

47.4 the information provided and estimates made by GCUK as part of its ECL assessment, specifically the approach taken by GCUK in respect of each of the matters referred to in paragraph 32 and particularly in the context of the fact that the overall effect of the judgements made by management was to reduce significantly the amount of the ECL provision and a significant increase in GCUK's debtor book in FY2019; and

47.5 the information that should have been sought, the information provided and assumptions made as part of the GCUK going concern assessment and cashflow forecasts.

I. *SANCTIONS*

48. This *Final Settlement Decision Notice* sets out the following *Sanctions* imposed on the Respondents:

Saffery

48.1 A financial sanction of £750,000, discounted for admissions and early disposal by 22.5%, so that the final sanction payable is £581,250.

48.2 A published statement in the form of a severe reprimand.

48.3 A declaration that the FY2019 Audit report signed on behalf of Saffery did not satisfy the *Relevant Requirements*.

48.4 An order to take action to reduce the likelihood of recurrence of the breaches, as outlined in Part VI of this *Final Settlement Decision Notice.*

Mr Di Leto

48.5 A financial sanction of £160,000, discounted for admissions and early disposal by 22.5%, so that the final sanction payable is £124,000.

48.6 A published statement in the form of a severe reprimand.

48.7 An order to take action to reduce the likelihood of recurrence of the breaches, as outlined in Part VI of this *Final Settlement Decision Notice.*

III BACKGROUND

A. The structure and business operations of GCUK

The corporate structure of GCUK

49. GCUK was incorporated in England and Wales on 2 July 2012, it being a wholly owned subsidiary within a financial services group (the "**Greensill Group**"). It had substantial operations in the UK, Germany and Australia. GCUK acted as the primary trading entity for the group.

The business operations of GCUK

50. The business model of GCUK involved the supply of various forms of WCF to customers.

51. A large proportion of GCUK's revenue (c. 90%) was generated from one type of WCF known as supply chain finance ("**SCF**"), which involved the provision of short-term financing to bridge the gap between a supplier providing goods or services (the "**Supplier**") to a customer (the "**Obligor**") and payment for those goods or services being made by the Obligor. The remainder of GCUK's WCF business was made up of accounts receivable funding ("**ARF**"), and, to a lesser degree, other types of financing such as Supplier Irrevocable Payment Undertakings ("**SIPUs**") and Instalment Payment Agreements ("**IPAs**") (see Part V, section 3 below).

52. The duration of WCF arrangements provided by GCUK was variable. GCUK described the arrangements as typically being 'short-dated' so that payment would be payable within 90 days. However, the maturity periods could be much longer than this. In particular, some types of financing could be 'rolled over' at the end of the initial term into a new arrangement, for an additional fee.

53. The basic structure of an SCF arrangement was that GCUK would provide financing by settling the Supplier invoice directly, at a discount for early payment, and in exchange, the right to be paid by the Obligor under the Supplier invoice at full value (the "**receivable**") would transfer to GCUK. The receivables generated by GCUK's business were individual financial assets.

54. In addition, GCUK provided SCF under special terms to companies owned or part owned by an unconnected venture capital fund (the "**Venture Capital Fund**" (managed by an investment holding company (the "**Investment Holding Company**")) which had a significant equity investment in the Greensill Group.

55. As of 31 December 2019, GCUK was owed about $18 billion, in respect of finance provided (predominantly under SCF arrangements).

56. GCUK was not sufficiently capitalised to be able to fund the volume and value of financing it offered on a daily basis. Therefore, in order to finance the transactions GCUK would mostly transfer rights to cash flows generated from the receivables to one of three investors (the "**primary investors**").

    56.1 Funds managed by an unconnected investment bank (the "**Investment Bank**"), typically through one of two funds (the **"V Fund**" or the "**H Fund**");

    56.2 Greensill Bank AG ("**Greensill Bank**"), a private bank incorporated in Bremen, Germany and part of the Greensill Group; or

56.3 Funds raised by an asset manager (the "**Asset Management Company"**) from investors and held in a specific Greensill fund (the "**Asset Management Greensill fund**").

57. As of 31 December 2019, the Investment Bank appeared to be financing 44.5% of the receivables transferred to investors, and Greensill Bank a further 17.2%.

58. The fact that GCUK relied on such a limited number of primary investors meant that its operations and its ongoing ability to place new business was highly dependent on the continuing appetite and ability of those specific investors to continue to acquire the receivables generated by GCUK's WCF transactions.

59. The transfer of the rights to the receivables by GCUK to investors was effected either directly from GCUK to the investors or indirectly, through one of three Special Purpose Vehicles ("**SPVs**") which would then issue loan notes to the investors backed by the receivables.

60. GCUK was not, however, able to (and in some cases chose not to) transfer every receivable it acquired to investors within a short period (ideally one day). In some cases, particular receivables were held by GCUK for a prolonged period of time (although their on balance sheet positions were small (less than 1%) compared to the total receivables as de-recognised from the balance sheet) and in others, until the underlying balance owed under the Supplier invoice had been settled in full.

61. Where transfers were made, this provided GCUK with liquidity (in an amount almost equal to the sum due under the underlying Supplier's invoice) until the debt was repaid. GCUK's profit was the revenue generated by the SCF transaction minus the discount it gave investors on the receivables (referred to as the "*Skim*"). Whether or not the rights to payment of the receivables were transferred to investors, GCUK also charged Obligors various fees connected with the facilities it provided. As it typically retained responsibility for collecting the repayment of the WCF from the Obligors, it would charge the investors a fee for that collection process.

62. Whilst GCUK's financial statements historically showed an increase in revenue year on year, GCUK's business and the revenue it generated was unpredictable. The returns were shared between investors and GCUK, and therefore the revenue recognised by GCUK from individual transactions was highly variable. GCUK received low profit margins and even negative returns on some transactions.

B. The reliance on trade credit insurance

63. A high proportion of the Obligors to whom SCF was provided by GCUK were high credit risk and the receivables generated were accordingly typically considered to be "*sub-investment*" grade.

64. The majority of the SCF receivables generated by GCUK, as well as some other types of receivables, would only be accepted by investors where the risk of repayment default was covered by a trade credit insurance policy taken out by GCUK to improve the risk-rating of the investment. Under a typical policy the insurance company would be liable for a proportion of the outstanding debt in the event of default, leaving GCUK liable under the insurance policy for the remainder known as a "*first loss*" deductible.

65. This would be either a percentage or fixed amount of the value of the receivable, which either would not be paid by the insurance company, leaving GCUK primarily liable for that sum, or would be paid by the insurance company and reclaimed from GCUK.

66. In some cases, a different loss sharing arrangement was put in place with investors and no insurance was arranged (see Part V, section 5 below). Non-insured receivables typically achieved smaller margins than insured receivables.

67. Revenue from insured receivables was the more profitable part of GCUK's business, accounting for around 90% of its revenue each year.

68. The business model was accordingly dependent on the ongoing provision of trade credit insurance which facilitated a significant proportion of the transfers to investors, without which GCUK would not have the liquidity to continue its business operations.

69. The most important trade credit insurance policies for GCUK in FY2019 and for its future operations were:

    69.1 the insurance arrangements issued by an insurance agency ("**Insurer A**"), which arranged a very high level of insurance cover for GCUK and its investors over 11 separate policies, including the "**Standalone Policy**" and the "**CS Policy**" (together, the "**Insurer A Policies**"); and

    69.2 a policy issued by another insurance agency ("**Insurer B**"), the "**Insurer B Policy**".

C. GCUK's entrance into administration in March 2021

70. The Insurer A Policies and the Insurer B Policy together provided cover for the vast majority of GCUK's insured receivables, but these expired at different times between 2019 and 2021 without renewal, with the final policy expiring in March 2021. GCUK was unable to obtain alternative insurance without substantial cash collateral, which it was unable to provide. Following this, press reports indicated that the Investment Bank had suspended subscriptions and redemptions on its funds containing GCUK assets, and both the Investment Bank and the Asset Management Company indicated to GCUK that they would no longer be investing in receivables generated by GCUK's WCF business.

71. As a result, GCUK ceased the origination of new WCF business on 2 March 2021 and, on 8 March 2021, GCUK entered into administration. The failure to renew, or obtain alternative, trade credit insurance was therefore a key factor in GCUK entering administration.

D. The role of the Respondents as Statutory Auditors

72. The Respondents were appointed as the *Statutory Audit Firm* for GCUK from August 2015 and continued in that role until GCUK entered administration, with Mr Di Leto being the *Statutory Auditor* and engagement partner for all GCUK audits.

73. The financial statements for each UK entity were prepared (in US Dollars) on an individual basis.

74. Saffery was, at all material times, a member of a global network of firms.

75. The parent company of the Greensill Group was audited by an accounting and consultancy firm based in Sydney, which was part of the same global network as Saffery (the "**Group Auditor**"). The Greensill Group prepared both: company financial statements, which included amounts for the parent company only; and group financial statements, which included amounts for the parent company and its subsidiaries, including GCUK, presenting them as a single economic entity. In its audit of the Greensill Group financial statements, the Group Auditor therefore placed some reliance on work carried out by the Respondents in respect of GCUK.

E. The background to the FY2019 Audit

76. Several members of the audit team, including Mr Di Leto and the Audit Director, had worked on GCUK audits in previous years. Mr Di Leto and the Audit Director both carried out each of the audits of GCUK since the initial engagement of the Respondent firm in 2015 (for FY2014). Other than this, none of the audit team members had any other prior experience of auditing a WCF business, although a number had other financial services experience.

77. On 17 April 2020, the Respondents produced its "Audit Closing Report to the Audit Committee for the year ended 31 December 2019" (the "**Audit Closing Report**") which recorded that:

    77.1 The Audit was substantially complete, subject to a number of outstanding matters identified in the report and it was anticipated that an unmodified audit opinion would be issued;

    77.2 Final materiality for GCUK had been determined to be $4.2 million, performance materiality had been determined as $3.15 million and the clearly trivial threshold had been determined to be $0.21 million; and

    77.3 No material misstatement had been identified.

78. The FY2019 Financial Statements were signed on 22 May 2020 and the FY2019 Audit concluded on 26 May 2020 with an unmodified audit opinion on the FY2019 Financial Statements issued, signed by Mr Di Leto on behalf of Saffery.

F. The accounting treatment of the financial assets derived from the WCF business

79. The receivables generated through the WCF business model were financial assets, the accounting treatment for which is provided for in IFRS 9 ("Financial Instruments")[2]. IFRS 9, paragraph 3.2.3, required the financial assets, and corresponding liabilities, to be recognised on GCUK's balance sheet until criteria for derecognition had been met.

80. Separately, GCUK was required to assess and determine when its WCF revenue (i.e. the Skim and the fees paid by the Obligor to GCUK for the WCF services provided) should be recognised[3] i.e. at the time of transaction or later. This assessment was required whether GCUK recognised or derecognised a receivable under IFRS 9.

81. GCUK determined that it could and should apply IFRS 15 ("Revenue from contracts with customers") to determine the revenue recognition point for its WCF revenue.

[2] International Accounting Standard 32 para. 11 provides the relevant definitions for financial assets.
[3] IFRS 15 para. 5 sets out when that standard applies, as opposed to another standard such as IFRS 9.

82. When applying the requirements of IFRS 9 and IFRS 15 (each of which came into force on 1 January 2018), GCUK characterised itself as a provider of a financial "*brokerage*" service, rather than a provider of financing. On that basis GCUK generally derecognised receivables generated by WCF transactions from the balance sheet and recognised all WCF revenue at the point of transaction.

83. Both where financial assets were recognised and where financial assets were derecognised, GCUK needed to make provision, under IFRS 9 chapter 5.5, within its financial statements for ECL. This was required to allow for GCUK's potential losses arising from an Obligor's, or Supplier's, default.

IV RELEVANT REQUIREMENTS

84. The *Relevant Requirements* include the ISAs, issued by the Financial Reporting Council and which are based on the standards issued by the International Auditing and Assurance Standards Board.

85. The *Relevant Requirements* referred to in this *Final Settlement Decision Notice* are the following:

ISA 200:	Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing - contains requirements for the auditor to have reasonable assurance about whether the financial statements are free from material misstatement, to report in accordance with financial findings and to act with professional scepticism and professional judgement as well as in compliance with ethical requirements.
ISA 220:	Quality Control for an Audit of Financial Statements - contains requirements concerning how an audit should be resourced and how quality control should be maintained throughout the entire audit.
ISA 240:	The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements - contains requirements for the auditor to identify and assess the risk of material misstatement due to fraud, including risk of revenue recognition and management override of controls, and to design audit procedures that respond appropriately to those risks.
ISA 265:	Communicating Deficiencies in Internal Control to Those Charged With Governance and Management – contains requirements concerning the communication, to those charged with governance and management, of deficiencies in internal control.
ISA 300:	Planning an Audit of Financial Statements - contains requirements for the auditor to establish an audit strategy and develop an audit plan.

ISA 315:	Identifying and Assessing the Risks of Material Misstatement Through Understanding of the Entity and Its Environment – contains requirements for the auditor to understand the entity and the environment, including internal control, in order to identify and assess the risk of material misstatement. The standard also requires the auditor to determine which risks are significant to design appropriate audit procedures.
ISA 330:	The Auditor's Responses to Assessed Risks - contains requirements for the auditor to design and implement audit procedures that are responsive to the assessed risk of material misstatement, including tailoring audit work for significant risk.
ISA 500:	Audit Evidence - contains requirements for the auditor to design and perform audit procedures to obtain sufficient appropriate audit evidence on which to base the audit opinion, considering the relevance and reliability of information used as evidence.
ISA 530:	Audit Sampling – contains requirements concerning how auditors should design and select samples when testing a population to ensure the results provide a reasonable basis for conclusions
ISA 540:	Auditing Accounting Estimates and Related Disclosures - contains requirements for the auditor to assess risks of material misstatement in accounting estimates, including estimation uncertainty and potential management bias, and to design audit procedures to evaluate whether the estimates and related disclosures are reasonable.
ISA 570:	Going Concern – contains requirements concerning how auditors should evaluate management's use of the going concern basis and assess whether material uncertainties exist that may cast significant doubt on the entity's ability to continue as a going concern.
ISA 700:	Forming an Opinion and Reporting on Financial Statements - contains requirements concerning how auditors should form an opinion on whether the financial statements are prepared in accordance with the appropriate financial reporting framework and how that opinion should be expressed in writing in the auditor's report.

86. The ISAs relevant to this *Final Settlement Decision Notice* are those effective for audits of financial statements for periods ending on 31 December 2019.

87. As the *Statutory Audit Firm* responsible for the Audit, Saffery is responsible for any established breaches of *Relevant Requirements* on the part of its partners or employees. As such, references to "Saffery" throughout this *Final Settlement Decision Notice* refer to the Saffery audit team members who conducted the audit and, as applicable, the firm.

88. As the *Statutory Auditor* responsible for the FY2019 Audit, Mr Di Leto was responsible for the overall quality of the Audit and the direction, supervision, and performance of the FY2019 Audit in compliance with the professional standards and applicable legal and regulatory requirements.

V ADVERSE FINDINGS

89. The failings identified have been grouped under the different areas of the Audit covered within this *Final Settlement Decision Notice*.

90. There is inevitably some overlap and repetition between those failings which pervade more than one area of the Audit. Specifically, those concerning the Respondents' failure to respond appropriately to risk, obtain sufficient audit evidence and conduct the Audit with professional scepticism. Each section sets out the particulars of those common failings, and the breaches of the *Relevant Requirements* that follow, to the extent they apply to the particular area of the Audit considered in that section.

SECTION 1: PLANNING AND RISK ASSESSMENT

A. Introduction

91. The planning of an audit and performance of effective risk assessment procedures is a critical part of any audit.

92. The results of audit risk assessments inform the design and implementation of all audit procedures to be performed, as well as the auditor's assessment of the sufficiency of the audit evidence obtained. Where there are deficiencies in carrying out proper risk assessment procedures, this can significantly impact on the quality of the audit work carried out and the audit conclusions reached. Poor quality audit work can in turn demonstrate that the required risk assessment procedures were not planned and performed properly.

B. Relevant Background

<u>The nature of GCUK's business operations</u>

93. Several features of GCUK's business operations were unusual and posed both complexity and significant risks from an accounting and auditing perspective.

94. This included (by way of example) issues such as:

    94.1 The complex nature of GCUK's business model. For example, the significant differences in the way different types of transaction were structured (e.g. the legal arrangements underpinning those transactions, relevant loss-sharing arrangements and insurance provision), there being differences between both each type and subcategories within each type, and the risks associated with understanding that complexity.

    94.2 The complex nature of the accounting judgements to be made. For example:

        a. how GCUK recognised revenue and derecognised financial assets on its balance sheet under the relevant IFRS requirements;

        b. the involvement of special purpose entities and the use of off-balance sheet finance necessitating judgements as to whether such finance should have been on balance sheet;

        c. estimating the relevant ECL provisions and the risks around ensuring that appropriate judgements were made; and

        d. The risks around business viability and dependencies. For example:

i how GCUK financed its ongoing business operations;

ii GCUK's reliance on trade credit insurance to facilitate the onward transfer of sub-investment grade receivables (which provided 90% of its revenue); and

iii the reliance on a small number of investment funds which invested in GCUK's receivables.

95. Having an adequate understanding of GCUK's business model was crucial in respect of all areas of the Audit. Section 4.1 of IFRS 9 stipulates that an entity's business model is used to determine whether a financial asset should be measured on an amortised cost[4] or fair value[5] basis. Paragraph 5.2.2 sets out how the impairment provisions in that standard (i.e. the ECL provision) should be applied, something which differs depending on the applicable measurement basis.

96. There were also several features of GCUK's business operations that had, or may have, changed in FY2019 that added to that complexity and to the risk of a material misstatement arising. These included: proposed changes in accounting policies within the wider Greensill Group for FY2020 (see section 2 below on Accounting policies); any changes in any of the underlying terms under which GCUK traded (see section 3 below on Revenue); the significant expansion of its debtor book and changes to the way the ECL provision was calculated (see section 4 below on Expected Credit Loss); and changes to how GCUK was financed (see section 5 below on Going Concern).

97. The Respondents were required to carry out the audit planning and risk assessment procedures with this complexity and these changing features in mind.

Overview of audit work performed in relation to planning and risk assessment

98. The Respondents commenced the planning of the Audit in October 2019, with the audit team (without Mr Di Leto) attending an audit planning meeting with representatives of GCUK and the Group Auditor on 21 October 2019 (the "**Audit Planning Meeting**").

99. At the outset of the FY2019 Audit, as the engagement partner, Mr Di Leto was required to determine that an EQCR had been appointed. No EQCR was appointed for the FY2019 Audit.

100. The audit team met separately (without GCUK or the Group Auditor) to discuss audit planning, the undated notes of which:

100.1 Contained brief commentary under the headings: Business Background, Significant Risks, Audit and Responsibilities, Fraud and Error, Related Parties and Other Matters; and

100.2 Listed six "*key risks*" (the Significant Risks):

a. risk of material misstatement arising from revenue recognition and completeness;

[4] The accounting method used to measure the value of financial assets or liability by spreading their cost over time.
[5] Where an asset or liability is measured with reference to the price that would be received if it were to be sold or transferred in an orderly market transaction between market participants at the measurement date.

b. risk of material misstatement arising from management override of controls;

c. risk of material misstatement arising from group acquisitions;

d. risk of material misstatement arising from intergroup transactions and balances;

e. risk of material misstatement arising from valuation and recoverability of assets; and

f. risk of material misstatement arising from share awards.

101. The first two of these Significant Risks (revenue and management override) were specific fraud risks. Specifically, ISA 240: presumed that revenue recognition is at risk of fraud and required the Respondents to give reasons as to why they concluded that presumption to be rebutted, if that was the conclusion reached; and required the Respondents design and perform audit procedures in order to address the risk of fraud arising from management override of controls.

102. The Respondents prepared an "Audit Strategy Report to the Audit Committee for the year ended 31 December 2019" (the "**Audit Strategy Report**") which was presented to GCUK's Audit Committee on 4 November 2019, and which identified the same Significant Risks identified at the Audit Planning Meeting.

103. The Audit Strategy Report indicated that the planning stage of the Audit would continue until December 2019 and would involve a number of steps as listed in that document, including updating the understanding of the business, performing risk assessment, identifying potential changes in financial reporting requirements of the Greensill Group and determining the planned audit approach and audit procedures.

104. The Respondents also indicated that their audit approach would include an evaluation of controls as part of the planning process, followed by substantive testing. In relation to controls, however, the Respondents stated that the audit was "*not designed to provide assurances as to the overall effectiveness of the controls*". Therefore, the Respondents did not plan to rely on GCUK's internal controls working effectively, but on evidence from substantive audit procedures.

105. There was no completed audit plan or equivalent document on the Audit File. The Respondents' audit planning and risk assessment process was instead performed through the completion of several sections of the audit software used by the firm ("**CCH**"). The CCH software contained both the permanent section of the Audit File (the "**Permanent Section**"), which included information relating to GCUK from prior audits, and a number of embedded features and tools designed to assist in effectively planning the Audit and meet the *Relevant Requirements* regarding risk assessments, the latter in a separate "*Planning*" area (the "**Planning Section**"). The standard CCH documentation was supplemented by the preparation of individual working papers, in Microsoft Word and Excel format.

C. Adverse Findings

106. The adverse findings set out below address failings in respect of:

106.1 Determining whether an EQCR had been appointed to the Audit.

106.2 Understanding the entity and its environment.

106.3 Identification and assessment of risks of material misstatement.

106.4 Identification and assessment of the risk of material misstatement specifically as a result of fraud.

106.5 Understanding and evaluating internal controls.

106.6 Planning the audit.

106.7 Performing planning and risk assessments procedures without a sufficient level of professional scepticism.

ADVERSE FINDING 1: The failure to appoint an EQCR

107. The Respondents initially assessed the FY2019 Audit as involving a "*high*" inherent risk when answering a number of "*inherent risk*" questions embedded within the CCH software. This meant that, under Saffery's own policies and procedures, an EQCR should have been appointed to the FY2019 Audit.

108. Meanwhile ISA 220.19 requires that, where the audit firm has determined that an engagement quality control review is required, the engagement partner must:

108.1 determine that an EQCR has been appointed;

108.2 discuss significant matters arising from the audit with the EQCR; and

108.3 not date the auditor's report until the completion of the engagement quality control review.

109. Accordingly, Mr Di Leto's failure to ensure that an EQCR had been appointed resulted in the Respondents breaching ISA 220.19.

ADVERSE FINDING 2: The failure to understand the entity and its environment properly as part of the risk assessment procedures

110. The Respondents were required to obtain a sufficient understanding of GCUK's business and its environment in order to be able to plan and perform risk assessment procedures that would enable the Respondents to assess the risk of material misstatement properly.

111. Under ISA 315.11 the Respondents were specifically required, when performing risk assessment procedures, to obtain an understanding of:

111.1 the relevant industry;

111.2 the nature of the entity (including operations, ownership, governance, types of investments being made and how the entity is financed, in order to understand the classes of transactions, account balances and disclosure to be expected in the financial statements);

111.3 the entity's selection and application of accounting policies;

111.4 the entity's objectives and strategies; and

111.5 the measurements and review of the entity's financial performance.

112. Where the Respondents were relying on information obtained from previous audits, they were required under ISA 315.9 to determine whether changes had occurred since the previous audit that could affect the relevance of that information.

113. In addition, under ISA 540.8, when performing risk assessment procedures and related activities to obtain an understanding of the entity and its environment, including the entity's internal controls, as required by ISA 315, the Respondents were required to obtain an understanding of a number of matters to provide a basis for the identification and assessment of the risks of material misstatement for accounting estimates (e.g. GCUK's ECL provision).

114. The information obtained on GCUK's business by the Respondents was insufficient to enable a proper understanding of the complex business operations of an entity such as GCUK. Specifically, the approach adopted to obtaining audit evidence was not sufficient to obtain a proper understanding of: the nature and variety of the individual transactions GCUK entered into; the accounting treatment required for its FY2019 Financial Statements; the detailed accounting estimates it was required to make; and the risks involved in its operations.

115. Whilst there were a number of working papers on both the Permanent Section and the Planning Section of the Audit File (some of which were obtained not as part of the FY2019 Audit but as part of the tender for the FY2020 audit, which took place in October 2019) that referred to background information relating to GCUK:

    115.1 The majority of the background information obtained contained no more than GCUK's own description of its business operations and selection of accounting policies in high-level terms. Even where working papers were authored by the Respondents, the source of the information in those papers was not stated and the Respondents gave no independent description or analysis of the business or the particular risks that its business model posed for accounting and auditing purposes, that were not simply the high-level business risks applicable to any entity within the industry.

    115.2 Other working papers simply included extracts from textbooks, articles or relevant accounting policies, without any accompanying analysis or commentary from the Respondents as to how their contents were relevant to the preparation of the FY2019 Financial Statements and/or the Audit.

    115.3 So far as other background information contained on the Audit File was concerned, there were 15 system generated "*background information documents"* stored on CCH, which either simply cross-referred to other documents or were completed only in very brief and high-level terms. Much of that information was simply rolled forward from previous audits with inadequate consideration being given to whether anything had changed since the previous audit that could affect the accuracy of those materials.

116. The review of the information obtained by the Respondents was recorded on CCH by way of a "Risk Assessment Checklist" without reference to a substantive evaluation having been performed of that information. The documents available, whilst numerous, contained very limited relevant substance and did not represent a proper or cohesive understanding of GCUK and its environment. They therefore could not amount to sufficient appropriate audit evidence for the purposes of satisfying the ISA 315 obligations in respect of the Audit.

117. In addition, whilst the Respondents may have developed an understanding of GCUK's business in the course of carrying out previous years' audits, the extent of that understanding and how changes in GCUK's business operations year to year had been properly understood, was not recorded by the Respondents and so any such undocumented historical understanding could likewise not amount to sufficient appropriate audit evidence for the purposes of satisfying ISA 315 in respect of the FY2019 Audit.

118. In any event the Respondents:

    118.1 Gave very limited consideration to whether the selection and application of accounting policies was appropriate or needed to be assessed or evaluated in any detail. The consideration that was given omitted certain crucial analysis, specifically whether: GCUK's categorisation of itself as a 'broker' of finance was correct; IFRS 9 permitted or required that receivables should be de-recognised when funded by investors; and IFRS 15 or IFRS 9 was the appropriate standard to apply when determining the revenue recognition point for GCUK's WCF revenue.

    118.2 Gave inadequate consideration to: whether there were any aspects of GCUK's business operations and transactions or accounting policies around which there were uncertainties; or if any continued uncertainty might lead to a risk of material misstatement and, if so, how that should be resolved. For example, there was significant variability in the revenue recognised from individual transactions entered into by GCUK (see section 3 below on Revenue). This variability meant that it would have been inappropriate to test GCUK's revenue by way of analytical procedures. Despite this the Respondents initially stated, in the Audit Strategy Report, that analytical procedures would be carried out. Ultimately those procedures were not performed, but the fact that they were unsuitable given GCUK's business operations should have been apparent to the Respondents at the outset of the Audit.

    118.3 Gave inadequate consideration to GCUK's objectives and strategies and whether they led to any related business or other risks that might result in a risk of material misstatement, including:

        a. GCUK's reliance on a limited number of primary investors and funds; and

        b. The extent to which GCUK relied on a small number of insurance policies, the continuity of which was uncertain (see also section 5 below on Going Concern).

    118.4 Carried out no evaluation to verify the accuracy of the information provided by GCUK, including whether the Respondents' own understanding of GCUK's business operations (from previous audits or otherwise) was consistent with GCUK's presentation of its business operations.

119. The understanding of the entity necessitated a much more focused and detailed consideration than is evident from the documents prepared at the time of the Audit, to ensure that the risk assessment procedures and, thereafter the substantive audit procedures performed, were properly tailored to, and reflected, GCUK's business operations and associated risks.

120. Instead, the Respondents took a superficial approach to understanding the entity throughout the Audit process, accepting at face value information which the auditors were provided by GCUK, without assessing whether it, or other information within the Respondents' possession, highlighted risks or other matters that should have informed the design of audit procedures. They failed to consider properly whether information gathered in previous audits remained relevant.

121. In addition, the Respondents had an insufficient understanding of the risks surrounding the ECL provision and how the audit procedures should be designed so as to provide an appropriate response. In particular, they gave inadequate consideration to any changes that were required or proposed to be made to it in FY2019 (noting, for example, the significant increase in GCUK's debtor book). The only reference made to the ECL provision during the planning and risk assessment process was the high-level description of what an ECL provision entailed, within a working paper titled "Management Override", as well as in the Audit Strategy Report (the purpose of which was to communicate the audit strategy to those charged with governance).

122. In conclusion:

    122.1 The Respondents should have performed their own evaluation of the information obtained in relation to the entity and its environment. The Respondents' failure to obtain a sufficiently detailed understanding of a number of critical features of GCUK and its business operations that were fundamental to the Audit was in breach of ISA 315.11.

    122.2 The Respondents should also have determined whether any information relied on that had been obtained in previous audits had changed. The Respondents' failure to do so properly was in breach of ISA 315.9.

    122.3 The Respondents' failure to sufficiently understand the requirements of the applicable financial reporting framework relevant to accounting estimates, specifically in relation to GCUK's ECL provision, was in breach of ISA 540.8.

ADVERSE FINDING 3: The failure to identify and assess risks of material misstatement properly as part of the risk assessment procedures

123. The Respondents were required to obtain, plan and perform appropriate risk assessment procedures that would enable the Respondents to assess the risk of the FY2019 Financial Statements being materially misstated properly.

124. Under ISA 315.25 and ISA 315.26, the Respondents were required to identify and assess the risks of material misstatement at both the financial statement level and the assertion level, including consideration of whether any of the risks were significant risks. For this purpose, they were required to:

    124.1 identify risks throughout the process of obtaining an understanding of the entity and its environment, including relevant controls that relate to the risks, and by considering the classes of transactions, account balances, and disclosures in the financial statements;

    124.2 assess those risks and evaluate whether they related more pervasively to the financial statements as a whole;

    124.3 relate the identified risks to what can go wrong at the assertion level, taking account of relevant controls that the auditor intends to test; and

124.4 consider the likelihood of misstatement, including the possibility of multiple misstatements, and whether any potential misstatement could result in a material misstatement.

125. The attempts by the Respondents to identify and assess the risks of material misstatement were wholly inadequate in that there was inadequate, if any, design and formulation of the risk assessment procedures during the audit planning process and consequently the work performed to try and identify and assess risks was piecemeal and ineffective without sufficient explanations being provided as to how conclusions were arrived at. The work performed was recorded across both CCH and a number of working papers and left a number of key matters unexplained.

126. Firstly, as noted above, there were a number of "*inherent risk*" factors identified at the outset of the Audit as contributing to an inherently "*high*" risk of misstatement. However, these were not considered further by the Respondents. Subsequently, the Respondents recorded (within CCH) that the overall risk of misstatement was "*medium*", without providing an explanation for this apparent discrepancy e.g. as to what other factors were engaged to reduce the overall inherent risk. The basis on which the overall risk was concluded to be lower than the inherent risk should have been properly considered and any factors relevant to the assessment properly evaluated.

127. In addition, whilst the Audit File referred throughout to six Significant Risks, the Respondents gave no explanation as to how these were identified, save that two of the risks were presumed by ISA 240 i.e. revenue recognition and risk of management override. Neither was any explanation provided as to why, within the CCH software, four of those key risks were described as particularly "*significant*" whilst the remaining two (which were also stated to be a greater risk of occurring than the other four and assessed as having the same potential impact on occurrence) were not.

128. In particular, there was no evaluation as to whether, and/or why, no other risks had been considered – including as to how the business risks that were identified through the inputs made in CCH in answer to the "*inherent risk*" questions had been assessed in terms of whether they created a risk of material misstatement. In addition, no evidential basis was provided as to how, in respect of each Significant Risk, the conclusion "*Testing Satisfactory*" was reached.

129. Further, CCH recorded that the same level of risk had been assessed by the Respondents for "*all assertions*" within each audit area. It is improbable that the audit risk would have been the same for all assertions within the same area of the Audit and no explanation was provided as to why that would be the case for the FY2019 Audit. In taking a blanket approach of treating all assertions within the same area of the Audit in the same way for all transaction cycles (i.e. a series of linked transactions) and balances relevant to the FY2019 Financial Statements, the Respondents were not applying any risk assessment at the individual assertion level. There was no explanation provided as to how the audit approach and procedures were developed to respond to these risks.

130. Finally, frequent references were made to risk settings from previous accounting periods, with only some audit areas having a risk setting selected for FY2019. No justifications were provided as to the level of risk selected in FY2019 for most audit areas, e.g. Income and Debtors, and limited justifications were provided for the risk settings selected in FY2019 for the remaining audit areas, e.g. Related Party Transactions.

131. The Respondents accordingly failed to identify and assess properly the risk of material misstatement for the purposes of ISA 315.25 and ISA 315.26.

ADVERSE FINDING 4: The failure to identify and assess the risk of material misstatement properly relating to fraud as part of the risk assessment procedures

132. As noted above, two of the Significant Risks identified by the Respondents were presumed by particular ISA requirements, i.e. under ISA 240.26, revenue recognition was presumed to be at risk of fraud, and under ISA 240.31, the risk of management override of controls was considered to be significant in all audits.

133. The Respondents were under a number of specific obligations when carrying out risk assessment procedures when considering and assessing the risk of fraud.

134. These included requirements to:

    134.1 Perform the procedures in ISA 240.17 – ISA 240.23 to obtain information for use in identifying the risks of material misstatement due to fraud (ISA 240.16).

    134.2 Evaluate whether unusual or unexpected relationships that have been identified in performing analytical procedures, including those relating to revenue accounts, may indicate risks of material misstatement due to fraud (ISA 240.22).

    134.3 Consider whether other information obtained (in performing analytical procedures or otherwise) indicates a risk of material misstatement due to fraud (ISA 240.23).

    134.4 Evaluate which types of revenue, revenue transaction or assertions give rise to the risk of fraud on the presumption that there are risks of fraud in revenue recognition (ISA 240.26).

135. The Respondents prepared two working papers relevant to the proposed risk assessment procedures that appear to have been directed at the requirements in ISA 240, titled “Management Override” and “Fraud and Error”. The working papers show that only a limited assessment was performed of how these risks could manifest in the context of GCUK’s business operations and what their respective likelihood and impact would be.

136. The Respondents identified three possible methods by which fraud could arise, none of which was specific to GCUK. The conclusion reached was that the fraud risk was “*low*” on the basis that:

    136.1 there were “*very tight controls/systems procedures*” in place;

    136.2 there was a competent/experienced management team in place; and

    136.3 the business was not cash based.

137. The basis for these statements was not provided and there was no supporting evidence to substantiate them.

138. There was no consideration of whether GCUK's business strategy or operations could give rise to other forms of management override of controls or bias other than in respect of journal entries or significant accounting estimates. For example, whether individual supply chain transactions might be authorised by management without proper verification (a matter that could result in a material misstatement in relation to either revenue recognition or the valuation and recoverability of assets). In order to assess these matters effectively, the Respondents would have required a good understanding of any controls in place in relation to the approval/authorisations process and whether there were any ways to prevent management, including senior individuals, circumventing the approval process. However, as explained further below, the Respondents did not properly identify or evaluate any such controls.

139. Consequently, the Respondents failed to comply with the requirements of ISA 240.16 and ISA 240.26 in terms of failing to assess properly the risks of material misstatement due to fraud, including by way of evaluating which types of revenue, revenue transactions or assertions give rise to fraud risks.

140. In addition, whilst no unusual or unexpected relationships had been identified during the performance of analytical procedures required by ISA 315, the procedures performed were unfocussed and of such brevity they were unlikely to identify such relationships. Therefore, the Respondents also breached ISA 240.22.

141. Finally, the "Fraud and Error" working paper ended with the statement "[w]*e shall review our assessment if any new information comes to light during the process of our audit*", but no further review was carried out.

142. The need for reassessment, and to specifically evaluate which types of revenue, revenue transaction or assertions give rise to the risk of fraud, was not considered even after the Respondents had identified two errors when carrying out substantive audit tests on revenue. The explanation for the two errors was that there had been "*manual adjustments*" to the figures reported (see section 3 below on Revenue). This was "*other information*" obtained during the Audit that indicated a risk of material misstatement due to fraud.

143. The Respondents consequently failed to comply with the requirements of ISA 240.23.

ADVERSE FINDING 5: The failure to understand and evaluate internal controls properly

144. As explained above, the Respondents in practice adopted a substantive approach to the Audit. This meant that they did not intend to rely on the effectiveness of controls when designing and performing substantive Audit procedures.

145. In those circumstances:

    145.1 the Respondents should have designed and performed substantive Audit procedures that could address the risk of misstatement absent any such reliance on effective controls; and

    145.2 any comments made during the Audit as to the effectiveness of certain controls and/or the effect they had in reducing the risk of fraud, were irrelevant and could not provide any assurance as to there being a reduced risk of misstatement in the FY2019 Financial Statements.

146. The adoption of a substantive approach did not meanwhile obviate the requirement to understand the controls relevant to the Audit, including those related to the risk of fraud. In order to understand the controls, the Respondents were required to evaluate the design of those controls and determine whether they had been implemented, particularly where they were relevant to a significant risk (including fraud), as required by ISA 315.12, ISA 315.13, ISA 315.29 and ISA 240.27.

147. An understanding of internal controls (and therefore an evaluation of their design and implementation):

    147.1 assists the auditor in identifying types of potential misstatements and factors that affect the risks of material misstatement, and in designing the nature, timing, and extent of further audit procedures;

    147.2 underpins the requirements on the auditor to comply with the requirements of ISA 265 (Communicating deficiencies in internal control to those charged with governance and management); and

    147.3 enables the auditor to understand whether a substantive approach is appropriate or whether any particular controls were so integral to the accuracy and reliability of the financial statements, in the context of the entity's business operations, that the audit cannot be undertaken without reliance being placed on those particular controls.

148. In other words, in order to adopt a substantive approach, the Respondents had to be satisfied that the implementation of substantive audit procedures alone could provide sufficient appropriate audit evidence at the assertion level (ISA 330.8(b)). For risks where substantive procedures alone could not provide sufficient appropriate audit evidence, the Respondents were required to test the operating effectiveness of, as well as understand, relevant controls in order to provide sufficient audit evidence that the risk of material misstatement had been reduced to an acceptable level. The Respondents had to keep the appropriateness of their approach under review throughout the Audit. However, the Respondents gave no consideration as to whether a substantive approach was appropriate, including in terms of whether reliance on some of GCUK's internal controls could not be avoided in practice, in breach of ISA 330(8)(b). Whilst a substantive testing approach is generally adopted where the auditor considers that insufficient reliance can be placed on controls, the Respondents did not record this as a reason why the approach was adopted for the Audit and, in any event, did not have a sufficient understanding of the controls in place to be able to make that assessment properly.

149. In a number of the audit working papers the Respondents:

    149.1 made statements that appeared to contradict their adoption of a substantive approach by referring to (generally unspecified) 'controls' as being considered adequate or 'tight' (e.g. there were "*very tight controls/systems procedures*" in respect of fraud); and

149.2 implicitly placed reliance on the operating effectiveness of particular processes that would typically be expected to amount to controls, that should have been identified as such and therefore evaluated in terms of their design and implementation e.g. GCUK's transaction approval process - the Respondents assumed that appropriate credit rating and other checks, such as confirming the valuation and effectiveness of any security provided over amounts owed by Obligors, had taken place when an Obligor was initially approved and subsequently monitored (including approval of subsequent transactions), without evaluating what that process entailed and whether its implementation was effective.

150. Such broad statements, about controls for which implementation had not also been tested, could not be relied upon in designing substantive audit procedures. The substantive audit procedures ought to have been designed and performed in such a way that they were not predicated in any way on the implementation and effectiveness of those controls. If, however, the view was that reliance on these controls was necessary given that the specific risks involved could not be properly assessed solely by substantive procedures alone, then those controls ought to have been properly identified and tested in accordance with ISA 330.8(a).

151. In practice, where controls were identified within the Audit, they were only identified at a high-level, in a way that was piecemeal and incomplete.

152. There was consequently no attempt to identify comprehensively, evaluate the design of and/or determine the implementation of any such controls, and the substantive audit procedures could not accordingly be designed or implemented in a way that properly addressed the risk that the FY2019 Financial Statements may be misstated.

153. In particular, the work undertaken to identify controls relevant to the Significant Risks of material misstatement was inadequate and the lack of any material evaluation meant that the Respondents were unable to conclude properly whether any identified controls were effective, in either design or implementation, either in isolation or in combination with others.

154. The approach taken in relation to controls was described in the Audit Closing Report in the following terms:

> *"We have documented and tested the internal control systems only to the extent that it is necessary for us to complete our audit work. Our work does not constitute a full test of the controls and is not designed to identify all deficiencies or issues that may exist. … The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control".*

155. The phrase "*to the extent that is necessary*" was not explained but, in any event, the work that was performed by the Respondents in respect of controls was inadequate to meet the requirements of the relevant ISAs as explained above and in the following paragraphs.

156. Thereafter, the Audit Closing Report listed a number of system and process failures that had been observed during the Audit, as a result of substantive audit procedures being performed as opposed to audit procedures designed to understand and test controls as part of the risk assessment process. The matters identified resulted in a recommendation that a "*formal procedures manual be produced*" because "*formal documentation for procedures and controls was not readily available*".

157. The main audit work carried out by the Respondents as to controls was contained within CCH; a “System Notes” working paper; and two walkthrough working papers.

158. Within CCH, five controls were listed. In respect of these:

    158.1 Only three were identified as relating to two of the Significant Risks identified by the Respondents, i.e., management override and employee share awards, and the controls related to the management override risk were exactly the same as those identified in FY2018.

    158.2 The comments made on the design of each of the controls (there were none made as to implementation) were extremely high-level and it was confirmed that none of the controls was tested. In relation to income and debtors, for example, no controls other than the fact that a credit committee reviewed new deals on a weekly basis, that might have related to the origination and approval of WCF transactions and the effectiveness of the credit control process (which could have been relevant to a number of other assertions), were identified by the Respondents.

    158.3 No audit evidence was obtained which would have enabled an evaluation of the effectiveness of the controls identified in mitigating the Significant Risks identified, and the Respondents can be inferred to have assumed that the design of the controls was effective and they had been implemented.

    158.4 There were no relevant controls identified for any other Significant Risk – including as to revenue recognition and completeness and the valuation and recoverability of assets. These risks related to areas of the Audit that involved highly technical and complicated accounting judgements and were therefore risks with a potentially significant impact on the FY2019 Financial Statements.

159. The “System Notes” working paper meanwhile contained a brief description of the processes in place for each type of transaction producing revenue The descriptions (for which no source was cited) were in the form of a list of functional tasks that were undertaken as part of the transaction process. The Respondents sought to identify which processes they considered to constitute “*key*” controls by means of highlighting certain words within each description, which might have been considered to amount to a control.

160. However, the attempt to identify the “*key controls*” by highlighting certain words and phrases did not:

    160.1 identify which risk each control related to (either at the financial statement or at the assertion level);

    160.2 explain how each control could mitigate that risk;

    160.3 evaluate whether the design of the control and thereby the potential mitigation was effective; or

    160.4 determine whether the control was implemented.

161. In addition, one “*weakness in internal controls*” was noted on the "System Notes" working paper i.e. that “*Senior members of staff have the ability to raise and approve there [sic] own journals*”. No further consideration was given as to how this (identified, potentially significant) risk of management override was, or not, mitigated by any controls in place within GCUK.

162. Finally, the walkthrough working papers set out some of the steps in the process that a particular transaction passed through from origination to repayment, and the steps in the expenses payments system.

163. No source was cited for the information in either working paper. The stated purpose of these working papers was to: assess the "*strength*" of the controls relating to revenue (without specifying if it was the strength of the design or the operating effectiveness that was being referred to); and to ensure the systems and processes relating to expenses "*operated correctly*". However, depending on how a "*Walk through test*" is performed, it may confirm only that the entity is using a control that management has communicated to the auditor as being in place. This may not be sufficient to assess the control's design and only sufficient to confirm implementation on the day of the test and not its operating effectiveness.

164. In this case, the steps identified were simply based on what was recorded in the "System Notes" working paper, with the focus being on whether the steps performed during the walkthroughs were consistent with that record. Consequently, the steps described did not seek to identify any controls relevant to the Audit, although some might in fact have included such controls. Nor did the mere description of the steps carried out amount to an evaluation of the effectiveness of any relevant controls or a confirmation that those controls were being implemented. In any event, the conclusion reached, that "*walkthrough satisfactory, system operating as expected"* was without any evidence cited to support that assertion.

165. The working papers referred to above noted in a number of places that, as a result of the nature of its business operations, GCUK placed a significant reliance on different types of digital technology and relied on a variety of IT platforms and systems to provide the data on which its financial reporting was based. However, no consideration was given to the design and implementation of any internal controls existing in relation to these platforms or systems in its descriptions of them, or whether the nature of GCUK's business operations meant that the Audit could not be performed properly without testing the effectiveness of any such internal controls.

166. The Respondents accordingly also failed to comply with ISA 315.12, ISA 315.13, ISA 315.29 and ISA 240.27.

ADVERSE FINDING 6: The failure to plan the audit properly

167. Under ISA 300.9, the Respondents were also required to develop an audit plan that included a description of the nature, timing and extent of planned risk assessment procedures, as determined under ISA 315 and the nature, timing and extent of planned further audit procedures at the assertion level, as determined under ISA 330.

168. For the reasons given in the adverse findings set out above, and as a result of those failures the Respondents failed to prepare an audit plan that met the requirements of ISA 300.9.

SECTION 2: ACCOUNTING POLICIES

A. Introduction

169. The appropriate selection and application of accounting policies to GCUK's business operations and the receivables generated by its business were fundamental to the presentation of the FY2019 Financial Statements and to the risk of material misstatement in the reporting process.

B. Relevant Background

170. The accounting policies of particular significance to GCUK related to whether:

    170.1 the receivables and related liabilities generated by WCF transactions should be included as assets and liabilities on GCUK's balance sheet (applying IFRS 9); and

    170.2 at what point in the WCF transaction process revenue should be recognised in the FY2019 Financial Statements (considering IFRS 9 and IFRS 15).

171. These were two important and highly complex accounting judgements with a very significant impact on the FY2019 Financial Statements. They required a detailed and careful analysis of the way the relevant accounting policies applied to GCUK's business operations. The selection and application of the accounting policies by their very nature impacted important aspects of the FY2019 Financial Statements, specifically revenue recognition and completeness and whether amounts received from investors to fund WCF finance should be disclosed as debt or excluded from the balance sheet (along with the WCF asset financed) as off-balance sheet finance.

172. The net effect of GCUK's approach to selecting and applying its accounting policies was to maximise revenue recognition, whilst minimising assets and corresponding liabilities appearing on the balance sheet.

<u>The accounting policies adopted by GCUK</u>

173. The accounting policies adopted by GCUK were summarised in high-level terms by GCUK in its "Group Accounting Policies Manual" and in a memo prepared by GCUK, titled "IFRS Revenue Recognition Memorandum". As referred to above and in section 3 below GCUK effectively characterised the vast majority of its business operations as a provider of a financial "*brokerage*" service (understood to mean buying and selling financial assets using IFRS 9 terminology), rather than a provider of financing (collecting contractual cashflows (scheduled payments under a financial agreement) using IFRS 9 terminology). On that basis, GCUK generally derecognised receivables generated by the WCF transactions from the balance sheet and recognised all revenue at the point of transaction.

174. GCUK considered that the fact that GCUK's business model focussed on loans which originated with a view to distribution meant that it was, in the case of all types of WCF transactions entered into where the receivables were transferred to investors, "*an entity that arranges a loan and retains no part of the loan package for itself*".

<u>Derecognition of financial assets</u>

175. Under paragraph 3.2.3 of IFRS 9 the financial assets (the receivables generated by the WCF transaction) and any corresponding liabilities had to be recognised on GCUK's balance sheet until the criteria for derecognition were met.

176. The relevant criteria were that:

    176.1 The contractual rights to the cash flows from the financial asset had expired (IFRS 9, paragraph 3.2.3) or the financial asset was transferred in accordance with the requirements of IFRS 9, paragraphs 3.2.4 and 3.2.5; and

176.2 Either:

a. Substantially all the risks and rewards relating to the asset had been transferred to another party (IFRS 9 paragraph 3.2.6), or

b. Where it had not been determined whether the entity had either transferred or retained substantially all the risks and rewards of ownership of the asset, the entity was able to determine that it had not retained control of the financial asset.

177. There is no express statement in IFRS 9 as to what amounts to a transfer of "*substantially*" all the risks and rewards of a financial asset.

178. Under IFRS 9, paragraph 3.2.7, whether substantially all of the risks and rewards had been transferred should have been assessed through a comparison of GCUK's exposure to the variability in the amounts and timings of the net cash flows of the transferred asset. The comparison needed to be made as to the variability if the asset was transferred and if the asset was not transferred, i.e., whether GCUK's exposure to variability in the present value of the future net cash flows from the financial asset changed significantly as a result of the transfer. A decision tree was included in IFRS 9 at Appendix B3.2.1 which set out the considerations to be applied when making an assessment as to whether assets could be derecognised.

179. This meant that whenever the rights to a receivable had been transferred to investors, GCUK needed to assess whether the criteria in IFRS 9 for derecognition had been met. This required careful quantitative and qualitative assessment of whether the risks and rewards relating to different types of receivables, and any sub-categories of each type, remained with GCUK following the transfer. This in turn required a detailed understanding of the precise nature of the relevant assets and the legal agreements underpinning the transactions involved. Subsequently, the Respondents needed to obtain sufficient appropriate audit evidence to enable them to conclude whether GCUK's assessment was appropriate.

180. The FY2019 Financial Statements explained GCUK's approach to derecognition, with reference to the criteria in paragraphs 3.2.3 to 3.2.6 in IFRS 9 as follows:

> "*Financial assets are derecognised only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership to another entity".*
>
> *Financial liabilities are derecognised when, and only when, the Company's obligations are discharged, cancelled, or they expire".*

181. The majority of the receivables which were transferred to investors, either directly or via SPVs, were accounted for on the basis that substantially all the risks and rewards of the receivables did not remain with GCUK. The receivables (and the related liabilities) were – on this basis – derecognised from GCUK's balance sheet, with only a small number of transactions not being derecognised.

182. No conclusion has been reached on the question of whether GCUK's application of the derecognition criteria was correct. However, the importance of the criteria's application to the presentation of the FY2019 Financial Statements was critical. If it had been the case that the financial assets should not have been derecognised then up to an estimated $18 billion of loans owed to GCUK would have continued to be shown as a financial asset on its own balance sheet, (as of 31 December 2019). A corresponding, slightly lower (to reflect revenue sharing) liability would be shown on the balance sheet as owing in respect of the repayment of the advances received from investors. Had this been how GCUK's financial assets and liabilities been presented in its FY2019 Financial Statements then users of financial statements would have been aware that GCUK's business operations meant that it was exposed to liabilities in an amount almost equivalent to the financial assets it held.

Recognition of Revenue

183. In assessing when revenue under a WCF transaction ought to be recognised, GCUK applied IFRS 15 rather than IFRS 9.

184. Chapter 31 of IFRS 15, (the content of which was echoed in the Financial Statements[6]), reads as follows: "*An entity shall recognise revenue when (or as) the entity satisfies a performance obligation by transferring a promised good or service (ie an asset) to a customer. An asset is transferred when (or as) the customer obtains control of that asset.*"

185. Whether performance obligations were in fact satisfied, fell to be assessed under IFRS 15, chapters 32 to 47, considering the terms of the contract concerned.

186. GCUK concluded, based on its interpretation of how the requirements of IFRS 15 as to the "*satisfaction of performance obligations*" applied to its WCF transactions, that revenue should be recognised immediately from the satisfaction of contractual performance obligations resulting from the provision of a "*financial service*" to the Obligor/Supplier, rather than as a return on a financial asset held by GCUK i.e. recognised over the lifetime of the asset under IFRS 9.

187. This was on the basis that GCUK treated the amounts advanced by investors in return for GCUK receivables as amounts received for the sale of GCUK's debtor book, rather than as loans made to GCUK to finance the WCF provided to the Obligor/Supplier.

188. Again, no conclusion has been reached on the question of whether GCUK's recognition of revenue under IFRS 15, as opposed to IFRS 9 was correct. However, if adopting an alternative approach of recognising the revenue over the lifetime of the receivables had been appropriate, for example, this would have had the result of deferring the recognition of significant amounts of revenue to subsequent years and presented a different picture of GCUK's profitability to users of financial statements. Obtaining adequate audit evidence as to the validity of GCUK's approach to revenue recognition was therefore essential.

Overview of audit work performed in relation to GCUK's accounting policies

189. The Respondents recognised revenue recognition and completeness as a Significant Risk at the outset of the Audit.

[6] FY2019 Financial Statements at p24.

190. There were a number of working papers relating to GCUK's accounting policies located on either the Permanent Section or Planning Section of the Audit File that contained information as to the requirements of IFRS 9 and 15. However, as explained further below, the Respondents failed to evaluate properly the appropriateness of the accounting policies adopted by GCUK in the particular context of its business operations.

191. No reference was made in any of the audit working papers to any planned audit procedures to assess either the application of IFRS 9 to derecognise financial assets or the assumption that IFRS 15 was the correct standard to apply in respect of revenue recognition.

192. In addition, no explanation was obtained by the Respondents as to how GCUK arrived at the conclusion that it was, primarily, "*an entity that arranges a loan and retains no part of the loan package for itself*", which underlay GCUK's selection and application of its accounting policies. The conclusion that followed in the Audit Closing Report was that the Respondents "*have not identified any material misstatement arising from errors in revenue recognition*" but no explanation was provided as to how that conclusion was arrived at.

193. Thereafter, the work recorded by the Respondents to have been completed in respect of GCUK's accounting policies, in the Audit Closing Report, included "*Reviewed the revenue recognition policy in detail to ensure it is in line with IFRS 15*". Again, no reference was made to any audit work carried out in respect of GCUK's derecognition of assets under IFRS 9 or as to whether revenue should have been recognised on an alternative basis.

<u>Decision by Greensill Group to change accounting policy at Group level</u>

194. During the course of the Audit, the Greensill Group concluded that the accounting policies should change in FY2020 in respect of the de-recognition of financial assets and revenue recognition at a group level, but not within GCUK.

195. On 19 April 2020 (5 weeks before the audit opinion was signed), the Group Auditor forwarded to the Respondents an email with the subject "SPV accounting paper", attaching a presentation titled "Greensill SPV structures – Consolidation and derecognition analysis – January 2020" (prepared by the Greensill Group). The email requested that the Respondents consider the assessment that there would be "*no impact to GCUK in the future if the accounting policy changed for the Group*" and asked whether it was worth having a call to discuss the matter.

196. The conclusion set out in the presentation was that from FY2020 the Greensill Group's returns from its dealings with the SPVs would become more materially variable "*as it takes first loss on the insurance contracts* [through GCUK's exposure to the same]*, which are an integral part of the asset financing structure*" and these losses were expected to increase in FY2020. Therefore (applying IFRS 10 'Consolidated Financial Statements') the SPVs should be consolidated within the Greensill Group's Financial Statements and "*from FY2020 revenue generated should be recognised by the Greensill Group as spread over the lifespan of receivables acquired*" (applying IFRS 9 rather than IFRS 15).

197. However, so far as the reporting for GCUK specifically was concerned, the assessment reached by the Greensill Group was that the new approach above did not necessitate any change to GCUK's accounting policies, on the basis that GCUK continued to transfer substantially all the risks and rewards on the transfer of the receivables.

198. Given that the question of whether the decision taken in respect of the Group affected GCUK's FY2019 Financial Statements was a fundamental audit judgement, it was crucial that the Respondents' consideration of this matter and any steps they took to understand its impact were recorded on the Audit File. Whilst there is evidence to indicate a call took place with the Group Auditor that day, there is no record of that discussion nor of any contemporaneous consideration given by Mr Di Leto to the matter.

199. Whether a call took place as described, the issue clearly required detailed consideration and analysis. Without this there was insufficient appropriate audit evidence on which the audit opinion could be based.

C. Adverse Findings

200. The adverse findings set out below address failings, in the context of GCUK's selection and application of accounting policies, in respect of designing and performing audit procedures to respond appropriately to the Significant Risk of revenue recognition and completeness and obtaining sufficient audit evidence.

ADVERSE FINDING 7: The failure to respond appropriately to risks arising from GCUK's selection and application of accounting policies and to obtain sufficient audit evidence

201. The Respondents identified revenue recognition and completeness as a Significant Risk and were required to design and perform appropriate audit procedures in order to reduce that risk to an acceptably low level.

202. The appropriateness of the selection and application of accounting policies by GCUK was a significant part of that risk, as the policies were fundamental to how the assets and liabilities of GCUK should be recorded in the FY2019 Financial Statements and how revenue should be recognised.

203. Under ISA 330 and ISA 500 the Respondents were required to:

    203.1 Design and perform audit procedures responsive to the assessed risks of material misstatement at the assertion level (ISA 330.6);

    203.2 Consider as part of that process the reasons for the assessment given to the risk of material misstatement at the assertion level for each significant class of transaction, account balance and disclosure (ISA 330.7(a));

    203.3 Obtain more persuasive audit evidence the higher the assessed risk (ISA 330.7(b));

    203.4 Perform substantive procedures that were specifically responsive to the "*significant*" risk identified, including a test of details (ISA 330.21); and

    203.5 Design and perform audit procedures that were appropriate for the purposes of obtaining sufficient appropriate audit evidence (ISA 500.6).

204. In addition, under ISA 500.9, where the Respondents were using information produced by GCUK, they were required to evaluate whether the information was sufficiently reliable for the Respondents' purposes, including the accuracy and completeness of the information, and whether the information was sufficiently precise and detailed.

The failure to evaluate whether GCUK was acting as "*broker*"

205. In considering the accounting policies, the Respondents started from the premise that GCUK was acting as a "*broker*" in the transaction, buying and selling financial assets, rather than acting as lender, collecting contractual cash flows from financial assets.

206. The working paper titled "System Notes" recorded GCUK's explanation of the accounting treatment for revenue and, specifically, the conclusion that GCUK was acting as a broker which meant that it could recognise revenue upfront.

207. The Respondents adopted that position without performing any evaluation as to whether that premise properly reflected the underlying arrangements for all the relevant transactions that were treated in the same way by GCUK.

208. A working paper titled "Revenue recognition overview" described its aim, on a tab titled "*Impact*", as being *"*[t]*o assess the impact on the financial statements of IFRS 15 and to ensure revenue recognition is line with the standard*". It had two tabs which considered the application of the "*5 step*" methodology in IFRS 15 to each of the major revenue streams, first by transaction and then by fee type (on the basis that, given the volume of transactions undertaken by GCUK, individual transaction testing was not possible). This analysis was flawed because the essential first step should have been to consider whether these transactions should have been accounted for under IFRS 9 rather than IFRS 15.

209. Only through a proper evaluation of the appropriateness of GCUK's categorisation of its business operations could the Respondents have begun to address the question of whether the accounting policies applied by GCUK were appropriate. No proper evaluation was carried out and therefore the risk arising in the eventuality that GCUK's assessment was incorrect was not addressed and insufficient appropriate evidence was obtained in relation to this area of the Audit.

The failure to evaluate whether the conditions for de-recognition of assets had been met

210. In respect of the application of IFRS 9 to the receivables generated by GCUK's business, the Respondents should have properly evaluated:

    210.1 Whether GCUK had adequately considered and appropriately concluded that all of the conditions for de-recognition of a financial asset (in paragraph 3.2.5) had been met; and

    210.2 If so, whether GCUK's assessment that substantially all of the risks and rewards attached to a financial asset had also been transferred before it was recognised.

211. No such evaluations were carried out and therefore the risk arising in the eventuality that not all of the receivables that GCUK had derecognised from its balance sheet should have been derecognised was not addressed.

212. In carrying out an assessment of whether substantially all of the risks and rewards had transferred to an investor, GCUK was required to consider whether the exposure to variability in cash flows from the asset changed as a result of the transfer and the Respondents should have performed a proper evaluation of that assessment.

213. It was likely that the principal variability in cash flows from GCUK's financial assets was that arising from irrecoverable (bad) debts. If it was concluded that the financial asset and any associated insurance policy was a single transferred asset, particular complexities arose in respect of the fact that a significant proportion of the receivables transferred onto investors were backed by insurance. Careful consideration needed to be given as to the impact that those arrangements may have had in terms of whether insurance backed receivables met the de-recognition criteria in IFRS 9.

214. In any event, GCUK's only exposure to irrecoverable debts (arising both before and after the rights to the financial asset (including the attached insurance policy) had been transferred) was:

    214.1 Exposure to the "*first loss*" on the insurance policy (which was sometimes substantial); and

    214.2 The much more unlikely risks of failure of the insurer (noting that GCUK included an ECL provision reflecting a continued exposure to insurer default on de-recognised transferred assets as per (section 4 below on Expected Credit Loss).

    Therefore, exposure to the variability of the cash flows did not materially change after any transfer was executed.

215. Consequently, in that scenario, GCUK could not be taken to have transferred substantially all the risks and rewards to the investor. However, no consideration was given by the Respondents to whether removal of variability in the cash flows which permitted derecognition was achieved through the transfer of the debt to an investor.

216. In addition:

    216.1 No audit work was performed to consider what right of recourse an investor might have against GCUK in the event of any Obligor default where an insurer did not make payment under the relevant policy and to consider whether that was consistent with the assessment that GCUK transferred substantially all the risks and rewards of the receivables to investors.

    216.2 No proper consideration was given as to whether a different approach was required for individual transactions or different categories of transaction. There was no assessment, for example, of whether different accounting policies should be applied for categories of receivables that were not covered by insurance, but in relation to which GCUK's exposure was limited in some other way to a lesser extent, such as in relation to the Credit Default Swap arrangement entered into with the Investment Holding Company managing the Venture Capital Fund, to whom GCUK was exposed to $100 million of any first loss. The ECL provision in relation to these assets suggested that it was likely that GCUK would continue to be exposed to all ECLs anticipated in respect of the Venture Capital Fund Obligors and the Respondents should have considered the implications of this when considering the appropriateness of derecognition.

    216.3 No audit work was performed to consider the circumstances or basis on which GCUK might make a "*top up*" payment on behalf of an Obligor, either to cover late payment or potentially non-payment and how this affected the assessment that GCUK transferred substantially all the risks and rewards of the receivables to investors or whether these would appropriately fall within "*short term advances"* as referred to in paragraph 32.5(a) of IFRS.

217. This was the case even after the Respondents were notified that the Group was proposing a change to the accounting policy in FY2020 at a group level.

218. As explained, the Respondents gave wholly inadequate consideration to how any of the matters that led to the conclusion that the SPVs should be consolidated and revenue recognised differently at group level, could affect GCUK's determination to de-recognise assets from its balance sheet. It was arguably counter-intuitive that GCUK should be treated differently from the rest of the Greensill Group in circumstances where it was GCUK that was the party to the transactions with the SPVs and was directly exposed to the first loss risk (the SPVs bore no credit or cash flow risk).

219. There were a number of specific features of GCUK's business operation that were highlighted in the presentation as part of assessing whether a change in accounting approach should also apply to GCUK, which indicated that the conclusion reached by the Group Auditor required further analysis and raised questions as to whether the assessment that GCUK continued to transfer substantially all the risks and rewards on the transfer of the receivables was correct.

220. In addition, it was unclear why the conclusions meant that the treatment for FY2019 should have been any different from FY2020, given that the only explanation for treating FY2019 differently from FY2020 was that, based on forecasts, actual credit default losses were expected to increase. However, the issue for the purposes of assessing whether assets could be derecognised under IFRS 9 was different i.e., exposure to the variability in the net present value from cash flows (the uninsured element of any losses to which GCUK remained absolutely exposed, with the investors having no exposure to credit losses).

221. Finally, there was also no audit work done to assess whether the results of the revenue testing carried out by the Respondents (see section 3 below on Revenue) cast any doubt on the appropriateness of the accounting policies applied by GCUK. This included evaluating whether it was appropriate to recognise revenue immediately from transactions relating to fees received for providing ongoing financing facilities which did not appear to meet the criteria under either IFRS 9 or IFRS 15 to recognise revenue immediately. No view has, however, been reached on the correct accounting policy adopted in respect of such fees.

<u>The failure to evaluate whether revenue was recognised at the appropriate point in time</u>

222. The Respondents should also have properly evaluated whether GCUK was correct to conclude that its revenue recognition point for all revenue received in respect of the receivables transferred on to investors was the date of the transfer.

223. This was not a straightforward question because even if the revenue derived from the Skim could properly be recognised at the date of the transfer, it was far from clear that all the revenue generated from the structuring and arrangement fees associated with the receivables should be recognised at the date of transfer.

224. There was, however, no evaluation of this issue carried out, and no consideration was given to the fact that the risk arising from this approach being incorrect was that not all of the revenue that GCUK obtained from individual SCF transactions should have been recognised upfront.

225. As noted above, is clear from the relevant working papers that the Respondents were not assessing whether IFRS 15 (rather than IFRS 9) was the appropriate accounting policy to adopt in the first place, only how IFRS 15 applied in practice to GCUK's WCF transactions.

226. There was, in addition, no evaluation carried out in relation to the conclusion reached in the "Revenue recognition overview" working paper, that GCUK "*satisfied its performance obligations*" at the date of the transaction for the recognising of revenue under IFRS 15. Audit work should have been performed to consider whether there were any performance obligations that post-dated the date of the transaction that could affect the conclusion to recognise revenue immediately, including the obligation on GCUK to collect the underlying debt and the possibility that fees could have to be paid over extended periods in particular transactions (such as where there was a revolving facility) rather than all up front.

227. One example of how the issue arose in practice was in respect of the transaction referred to in the working paper titled "Other Fees income" as "*Obligor* [A]". In that case the $24 million fee was included within the revenue figure and recognised immediately as falling within the FY2019. This was despite the fact the agreement for the facility had not been signed by either GCUK or Obligor A prior to 31 December 2019 and payment of the fee was therefore not legally enforceable until the next accounting year.

Summary of breaches

228. The Respondents failed to:

    228.1 Respond appropriately to the significant risk of misstatement identified in respect of revenue recognition and completeness, which included the risk that GCUK selected and applied their accounting policies incorrectly; and

    228.2 Failed to properly reconsider the position on accounting policies adopted by GCUK following a proposal to change the accounting policies for the remainder of the Greensill's Group in FY2020, and to consider whether the audit work performed had been sufficient in light of being informed of that proposal or whether further audit work was required to enable them to respond appropriately to that significant risk of misstatement.

229. Consequently, the Respondents breached ISA 330.6, ISA 330.7 and ISA 330.21. Additionally, the Respondents failed to:

    229.1 Obtain sufficient appropriate audit evidence that GCUK's categorisation of itself as a "*broker*" was correct, an assertion understood to mean that its business model was effectively that of buying and selling financial assets, rather than a provider of financing (whereby the objective is to hold financial assets in order to collect contractual cash flows). This was relevant to the evaluation required under paragraph 4.1 of IFRS 9;

    229.2 Obtain sufficient appropriate audit evidence as to whether the derecognition criteria in IFRS 9 were met for individual transactions that GCUK had derecognised;

    229.3 Obtain sufficient appropriate audit evidence as to whether GCUK could recognise all of the revenue at the transaction point for all transactions where the revenue was recognised at that point; and

    229.4 Evaluate for themselves the reliability of the information provided to them by GCUK in relation to the selection and application of accounting policies, including after the proposed change in accounting policies for the Greensill Group, to be applied for FY2020, was communicated to them.

230. Accordingly, they also breached ISA 500.6 and ISA 500.9.

SECTION 3: REVENUE

A. Introduction

231. The Respondents identified revenue recognition and completeness as a Significant Risk in their Audit Planning Meeting and their Audit Strategy Report.

232. As GCUK generated revenue via a high volume of complex and time sensitive transactions, it was particularly important for the Respondents to have an adequate understanding of GCUK's business model, to assess properly whether the revenue generated from different transactions was being recognised appropriately. That understanding being relevant not just to the question of whether GCUK's revenue was accounted for accurately and completely, but also to the question of whether the correct accounting treatment had been applied and to whether GCUK's ECL provision had been calculated appropriately.

233. In particular, section 4.1 of IFRS 9 stipulates that an entity's business model must be used to determine on what basis a financial asset should be measured (either the "*amortised cost*" basis or on the basis of "*fair value*" through either profit and loss or other comprehensive income). Paragraph 5.2.2 meanwhile sets out how the impairment provisions in that standard (i.e. the ECL provision) should be applied, with that application differing depending on the basis for measurement.

B. Relevant Background

234. The FY2019 Financial Statements showed a significant increase in revenue between FY2018 and FY2019 from $233.62 million to $419.61 million.

235. Six types of revenue were identified in the working paper titled "Revenue Recognition Overview" as follows[7]:

    235.1 SCF, a form of WCF that involved GCUK providing financing at the request of an Obligor;

    235.2 ARF, a more common form of WCF, whereby GCUK would be approached by the Supplier to provide the financing;

    235.3 SIPUs, described as an agreement whereby GCUK bought a portfolio of receivables, each of which had a variable rate of return, from a Supplier of services and the Supplier underwrote the portfolio to ensure GCUK received a minimum payment, whatever the eventual return proved to be e.g. a portfolio of mobile phone credit agreements sold to GCUK by a mobile phone provider. This underwriting generated a receivable, which GCUK could then transfer on to investors;

    235.4 IPAs, each of which had an agreed facility amount which the customer could then draw down within the agreed period. Repayments of the balance were pre-agreed in the terms and conditions. In most instances the facility was subject to extensions, or 'rolls', which increased the facility term (potentially with higher

[7] One further type of revenue, referred to in the GCUK administration proceedings, known as Future Receivables Funding, was not referred to in either GCUK's Financial Statements or any of the audit working papers. This was seemingly a form of financing to a supplier that was based on possible future assets that may be available to them, rather than existing assets e.g. future sales of good or services to customers that would generate revenue.

interest rates) on maturity date. Loan notes were issued for the balance of the debt and could be acquired by investors;

235.5 A form of SCF for a specific group of Obligors; and

235.6 "*Other Fees*", which are discussed further below.

236. The revenue arising from the first five categories of WCF transaction was described in the audit working papers as "*Net SCF income*" and the additional income in the sixth category as "*Other Fees*". The split between these two was $216.9 million and $202.6 million respectively and the remaining $0.1 million of total revenue in FY2019 was described as "*Other revenue items*".

237. It was explained, in the "Revenue Recognition Overview" working paper, that GCUK's earned revenue was either as:

237.1 Skims (and Spreads), the difference between the price at which GCUK acquired a receivable from an Obligor and the price at which GCUK transferred the rights to the receivable to an investor;

237.2 Rolls, additional revenue received when a facility term was extended; or

237.3 Fees, which came in three main types:

c. Arrangement Fees – administrative fees charged for arranging credit;

d. Facility Fees - fees that the Obligor paid in exchange for a credit facility; and

e. Structuring Fees – fees that GCUK included in its lender fee letters.

<u>Overview of the audit work performed in respect of revenue</u>

238. A planned audit response to the risk of material misstatement of revenue, an identified Significant Risk, was set out in the Audit Strategy Report.

239. The Audit Strategy Report referred to:

239.1 Developing an expectation of revenue and gross margin and comparing it to actual results, investigating any significant variances;

239.2 Selecting a sample of SCF/ARF transactions entered into and checking that the recording of revenue was in line with the terms of the trade; and

239.3 Reviewing all large one-off financing deals from signed agreements to revenue recorded, checking all applicable performance obligations were satisfactorily met.

240. The Respondents also recorded within CCH that additional cut-off testing would be performed and that the Respondents would "*Confirm our record and understanding of the sales, debtors and receipts system and related controls, either by: performing walkthrough test; or observation and enquiry*". A number of working papers where the testing on revenue was recorded by the Respondents, including the testing of different types of revenue and their approach to sampling transactions as part of that testing, were also identified within CCH.

241. The work said to have been completed by the Respondents as to revenue recognition and completeness was thereafter summarised in the Audit Closing Report dated 17 April 2020. This largely repeated the first two procedures identified in the Audit Strategy Report and referred to additional work relating to:

241.1 Sampling of SIPU deals;

241.2 Cut-off testing; and

241.3 Reviewing the revenue recognition policy to ensure it was in line with IFRS 15.

242. However, neither the Audit Strategy Report nor the Audit Closing Report provided an accurate summary of the work that was carried out in relation to revenue, as explained in more detail below.

C. Adverse Findings

243. The adverse findings set out below address failings, in the context of revenue and revenue testing, in respect of:

243.1 Designing and performing audit procedures to respond to the Significant Risk of revenue recognition and completeness and obtaining sufficient audit evidence;

243.2 Sampling; and

243.3 Designing and performing audit procedures to respond to the risk of material misstatement due to fraud arising.

ADVERSE FINDING 8: The failure to respond appropriately to risks arising in relation to revenue and to obtain sufficient audit evidence in respect of that risk

244. The Respondents, having identified revenue recognition and completeness as giving rise to a Significant Risk of material misstatement, were required to design and perform appropriate audit procedures in order to reduce that risk to an acceptably low level.

245. They were accordingly subject to the requirements contained within ISA 330.6, ISA 330.7, ISA 330.21, ISA 500.6 and ISA 500.9 when performing audit procedures in respect of Revenue.

<u>Failure to test the accuracy and completeness of populations tested</u>

246. As noted above, the revenue generated by GCUK was broadly split between "*Net SCF income*" and "*Other Fees*".

247. The testing of "*Net SCF income*" was carried out on the population of revenue generating transactions contained in what the "Revenue Summary" working paper described as "[t]*he detailed RAO (Remittance Advice Outbound) report*" which showed "*all trades in the year*". The RAO was generated by GCUK from its digital trading platforms and purported to include all the transactions and trades for FY2019. In addition, the "SIPU Testing" and "IPA Testing" workpapers contained testing on those specific revenue streams.

248. Meanwhile, the testing of "*Other Fees*" was set out in the working paper titled "Other Fee income". The testing was carried out on a population also provided by GCUK and, in addition, the Respondents relied on the CSV files provided by GCUK listing invoices as provided by Obligors. In practice (rather than by design) 91.2% of the population of the "*Other Fees*" was tested by the Respondents.

249. No testing was, however, done to confirm the completeness of any of the populations tested and no evidential or testing source was obtained to verify the completeness or accuracy of those populations. This was despite the fact that, as explained in section 1 above (on Planning and Risk Assessment), no evaluation was carried out by the Respondents of the controls relevant to the way in which the populations were generated, including relevant IT systems, to assess their effectiveness.

Lack of cut-off testing

250. The "Identified Risks" report made specific reference to a working paper "120" with a reference to performing detailed cut-off testing to ensure that revenue was included in the correct accounting period, but no such working paper appears in the Audit File.

251. The only evidence of cut-off testing in the Audit File is contained in the working paper entitled "Prepayments and accrued income" (also identified as H130). This, however, related only to a single obligor, Obligor A (referred to above), who had an IPA facility with GCUK. There was accordingly no wider cut-off testing carried out in relation to GCUK's reporting of revenue.

252. This was despite the fact that there was a notable increase in revenue from "*Other Fees"* in the later part of 2019 compared with revenue in the rest of the year, which was apparent from the working paper and, for example, should have been highlighted by a review of income patterns through the year, and raised questions as to whether it was appropriate to recognise all that revenue in 2019.

No explanation of inadequate response to variability in the testing results

253. The working paper "Revenue Summary" set out calculations of net returns for each transaction sampled (i.e., the amount of money received after all costs had been paid) and stated that the calculations involved assessing the "*reasonableness*" of each.

254. What that assessment involved is unclear from the wording used i.e. whether what was intended was for the net returns for each transaction to be agreed to the underlying documentation or for it to be confirmed that the margin on each deal fell within reasonable commercial parameters. However, the audit work carried out was limited to checking the net returns to the underlying documents.

255. This could not alone provide sufficient audit evidence in respect of the reasonableness of the net returns received by GCUK. The Respondents should in fact have assessed reasonableness in terms of whether the margins were commercially "*reasonable*". This was particularly important given the considerable variability in the net returns, as revealed by the calculations performed.

256. For example:

    256.1 There was a negative return for nine out of the 40 items tested;

    256.2 The high-level explanation recorded for this was: "*Negative sales will be down to fund capacity and ability to sell on that day to different investors*", without any further explanation or analysis; and

256.3 The net return as a percentage of the payment amount varied significantly for each item, ranging from 0.004% to 11.1% (excluding negative returns):

f. In some cases, the net return for GCUK and/or investors was very low in comparison to the size of the balance advanced to an Obligor; and

g. In others the shares of the returns between GCUK and note holders appeared to be highly variable.

257. Without clear parameters of what was considered "*reasonable*" there was no basis for assessing the implications of that variability for the assessment of revenue.

258. There was similar high variability of net returns and losses revealed by the testing carried out on the sample of SIPUs and IPAs tested in the "SIPU testing" and "IPA testing" working papers, without any explanation or evaluation of this variability from the Respondents.

Inadequate testing in relation to SIPUs and IPAs

259. The testing of SIPUs (on the "SIPU testing" work paper) involved testing both a sample of 10 SIPU transactions and testing the accrued income balance of $18 million.

260. The calculation of the $18 million accrued income relied on a model prepared by GCUK to calculate the anticipated returns that they would receive over and above the SIPU minimum payments guaranteed by the Obligors (i.e. if the returns on the portfolio of receivables proved to be greater than that minimum payment). The Respondents stated that they had reviewed the model "*to ensure calculated on a reasonable basis*".

261. The performance of that audit procedure was recorded by way of ticks against each item selected, to signify that accrued income was correctly calculated and to indicate: "*Model assumptions reasonable*", "*Model calculations correct*" and "*Spreadsheet integrity reviewed*". There was no explanation or indication as to how any of those conclusions was reached. The testing carried out was limited to testing the mathematical accuracy of the model and checking the cash received against the previous year's accrued income.

262. The sample was then extended as the results for the initial sample balances were inconclusive, with only a small proportion of the accrued income being collected in FY2019 in respect of a number of those balances (the contracts continued beyond the end of FY2019 so there was still a significant accrued income balance of $3.169 million outstanding on 31 December 2019). Against each of the additional balances tested (totalling $0.63 million) it was recorded against these items that cash received in FY2019 was exactly equal to the (estimated) amount accrued on 31 December 2018. It was in fact highly unlikely that the cash received in FY2019 was exactly equal to the amount accrued on 31 December 2018.

263. The working paper did not explain how the calculation of accrued income (involving a significant accounting estimate) was modelled and gave no proper explanation for the conclusions reached as to it being correctly calculated and the model assumptions and calculations being reasonable and correct.

264. Meanwhile, the testing of IPAs (on the "IPA Testing" working paper) involved testing a sample of three IPA transactions from a population of 13. Of these, the record of the audit procedures was unclear on two and contained the following inadequacies:

264.1 Obligor B – a discrepancy was seemingly found which overstated profit by $1.3 million. The working paper referred to two journals with the annotation "*Fund development fees incurred*" but it was not clear how this explained the apparent discrepancy.

264.2 Obligor C – the working paper suggested that the gross return included in the FY2019 Financial Statements was $10.09 million and the amount passed on to investors was $4.7 million. The working paper did not identify these amounts, nor did it clearly demonstrate how the findings from the Respondent's audit procedures provided sufficient appropriate audit evidence that these amounts were not materially misstated.

265. As with the testing on SCF / ARF and SIPUs, this working paper highlighted some highly variable margins. These were not considered further.

Summary of breaches

266. The Respondents failed to respond appropriately to the significant risk of misstatement identified in respect of revenue recognition and completeness in relation to:

266.1 whether the reported revenue and the populations tested contained all revenue items;

266.2 whether the revenue was recognised in the correct financial period through adequate cut-off testing;

266.3 the variability of the revenue generated by the transactions entered into by GCUK and its impact on GCUK's revenue recognition;

266.4 whether the accrued income received from SIPU transactions was accurately recognised; and

266.5 whether revenue was recognised appropriately in respect of the two IPA transactions.

Consequently, the Respondents breached ISA 330.6, ISA 330.7 and ISA 330.21.

267. In addition, the Respondents failed to:

267.1 Obtain sufficient appropriate audit evidence in respect of each of the matters set out in the preceding paragraph; and

267.2 Evaluate for themselves the reliability of the information provided to them by GCUK in relation to the population of revenue transactions to be tested and the accrued income estimated to be received from SIPU transactions.

268. Accordingly, the Respondents also breached ISA 500.6 and ISA 500.9.

ADVERSE FINDING 9: The failure to design and carry out appropriate sampling procedures within revenue testing

269. The audit testing carried out involved sampling of different categories of transactions (SCF and ARF, SIPUs and IPAs and Other Fees). The Respondents' objective, when using audit sampling, should have been to provide a reasonable basis for drawing conclusions about the population from which the sample is selected, and thereby obtain sufficient audit evidence.

270. Under ISA 530.6 – ISA 530.8, when designing an audit sample, the Respondents were required to:

270.1 consider the purpose of the audit procedure and the characteristics of the population from which the sample is to be drawn;

270.2 determine a sample size sufficient to reduce sampling risk to an acceptably low level; and

270.3 select items for the sample in such a way that each sampling unit in the population has a chance of selection.

271. The approach to sampling taken by the Respondents as explained in the "Revenue Summary" working paper, was as follows:

271.1 SCF/ARF transactions - a sample of 40 transactions was selected, chosen from "*those trades deemed riskier*" and to ensure a split between ARF and SCF fees. The sample also "*focussed on the higher value Obligors*";

271.2 SIPUs - a total sample of 10 transactions were tested (no explanation for this selection was provided);

271.3 IPAs – a sample of three transactions was tested, "*focussed on larger facilities provided by GCUK*"; and

271.4 Other fees – a sample of eight transactions were tested (no explanation for this selection was provided).

272. This approach to sampling:

272.1 Failed to consider or explain the appropriateness of the reasoning behind the sample sizes selected, or how the sample size selected reduced the sampling risk to an acceptably low level; and

272.2 Failed to consider whether the sample selected properly reflected the characteristics of the populations being sampled, given:

a. The high levels of net return variability within those populations; and

b. The Respondents' stated methodology was to specifically target the "*larger*" or "*riskier*" transactions which means that each item within the population did not have an equal chance of selection i.e. the methodology did not ensure that there was also an unbiased sample of the remaining items that did not have a chance of selection as "*larger*" or "*riskier*" to provide evidence of the whole population.

273. Consequently, the Respondents breached the requirements of ISA 530.6, 530.7 and 530.8.

ADVERSE FINDING 10: The failure to design and perform audit procedures responsive to the risks of fraud in connection with revenue

274. Under ISA 240.26, when identifying and assessing the risks of material misstatement due to fraud, the Respondents were required to evaluate which types of revenue, revenue transactions or assertions gave rise to fraud.

275. In addition, the Respondents were required to design and perform audit procedures responsive to that assessed risk of material misstatement due to fraud at both the financial statement level and the assertion level under ISA 240.30.

276. The approach taken by the Respondents to auditing revenue was wholly inadequate in addressing the risk of material misstatement of fraud arising. This was in part because no evaluation was carried out (as explained in section 1 on Planning and Risk Assessment) as to the design and implementation of the internal controls which could impact the incidence of fraud in revenue reporting.

277. Specifically, there was no evaluation as to:

    277.1 GCUK's credit application approval process; or

    277.2 The approval process for the amount investors paid for the rights to receivables; or

    277.3 The IT controls, which could impact on the completeness and accuracy of the populations of trades from which the revenue testing was carried out. The need for an evaluation of controls was not reconsidered even after the Respondents had identified two errors in the reporting of SCF/ARF revenue in the "Revenue Summary" working paper. The explanation for the errors was that there had been "*manual adjustments*" to the figures reported, an indication that any controls that did exist may not have been operating effectively and/or were inadequate.

278. Further, and in addition to the failures to evaluate the effectiveness of controls, no consideration was given to whether there were any characteristics within the different revenue streams or transactions tested which gave rise to a risk of fraud. For example: the fact that the high variability of net revenue and the high incidence of negative returns identified in the sampling undertaken could indicate a risk of fraud; and whether Obligors misrepresented their ability to repay the amounts advanced by GCUK to their Suppliers or the security available in the event of default.

279. Consequently, the Respondents were in breach of both ISA 240.26 and ISA 240.30.

SECTION 4: EXPECTED CREDIT LOSS

A. Introduction

280. Under IFRS 9, entities are required to assess potential losses or impairments relating to all their financial assets and include a provision in their financial statements to reflect the risk of loss, referred to as ECLs.

281. The provision for ECL is an accounting estimate which requires a number of judgements to be applied in relation to numerous inputs to the overall calculation. The valuation and recoverability of assets (which included the ECL provision) was identified by the Respondents as a Significant Risk at the outset of the Audit and the Respondents recognised that significant accounting estimates may be subject to the risk of management bias.

B. Relevant Background

The ECL provision in the FY2019 Financial Statements

282. The FY2019 Financial Statements stated (in Note 3) that the calculation of the ECL provision was one of the "*Critical accounting judgements and key sources of estimation uncertainty*".

283. It was noted that:

> *"The recognition and measurement of ECLs under IFRS 9 is a complex process which involves the use of significant judgement and estimation. The calculation of expected loss requires assimilation of forward-looking information into the Probability of Default (PD) and ECL estimates which are used to meet the IFRS 9 measurement requirements".*

284. The FY2019 Financial Statements explained (in Note 28) that GCUK's exposure to first losses under insurance policies was $1.036 billion. GCUK assessed the expected losses arising from this exposure by considering the probability of default of the Obligor and the expected recovery should a default arise.

285. Based on this assessment, the ECL provision in FY2019 was $59.3 million, the main components of which were as follows:

	FY 2019 (million)	FY 2018 (million)
Main ECL provision before "Credit Structure Reduction Factor" applied	$47.59	$12.67
Less "Credit Structure Reduction Factor"	-$15.90	-
Main ECL provision after "Credit Structure Reduction Factor" applied	$31.69	$12.67
Provision for Obligors with different arrangements		
Assets distributed to the [Investment Bank H Fund]	$23.88	$3.75
[Venture Capital Fund] entities	$13.94	-
Full provision for "non-performing" assets	$3.50	-
Other amounts included in the assets	$0.22	$0.14
	$73.23	$16.56
Less "Haircut" applied in FY2019	- $13.95	-
This was calculated as 25% of the balance excluding [Venture Capital Fund] and "non-performing entities".		
ECL provision	$59.28	$16.56

286. The ECL provision therefore increased significantly between FY2018 and FY2019, alongside the significant increase in GCUK's debtor book.

287. It is also clear that there were two significant adjustments made to the ECL provision that were not made in FY2018, namely:

    287.1 The Credit Structure Reduction Factor (a reduction to the main element of the ECL provision); and

    287.2 A further Haircut reduction to the overall total (excluding the amounts that related to the balances owed by the Venture Capital Fund investees and the amount of the full provision made in respect of the non-performing asset). Together these two adjustments resulted in a total reduction to the ECL provision of $29.8 million – almost ten times materiality.

288. The model adopted by GCUK for calculating the main element of the ECL provision, which covered the majority of Obligors, was set out in the working paper titled "System notes" (prepared by the Respondents) and the working paper titled "GC ECL summary" (prepared by GCUK).

289. The model contained the following components:

    289.1 the "*uninsured loss*" (the first loss to be incurred by GCUK if the Obligor defaulted, multiplied by the "*% Probability of Default (PD)*" for each Obligor); plus

    289.2 (where insurance was in place) the "*insurer default loss*" (the "*insured balance*" (the total balance owed by the Obligor minus the first loss) multiplied by the % PD for both the Obligor and the Insurer).

290. The amount of the first loss varied depending on the existence and terms of any insurance cover for that receivable. The PD for each Obligor was determined using a numerical Obligor Risk Rating ("**ORR**") of between 1.0 to 10.0, representing the risk of default. The ORR was taken from the GCUK initial credit assessment for the particular Obligor, which was said to be updated every 12 months or, in certain circumstances, where a change might be indicated.

291. The calculation of the ORR by GCUK involved both:

    291.1 A "*quantitative*" element using the services of a third party financial information platform; and

    291.2 A "*qualitative*" element described by GCUK as using "*expert judgement based on the nature of the company/industry, quality of management etc*", which would factor in both "*external ratings where applicable*" and "*internal financial analysis".*

Overview of the Audit work carried out in relation to the ECL provision

292. As stated above, the valuation and recoverability of assets was identified by the Respondents as a Significant Risk at the outset of the Audit and it was recognised that significant accounting estimates may be subject to the risk of management bias in the "Management Override" working paper.

293. Subsequently, in the Audit Closing Report the Respondents stated that:

"*We are aware that the obligors of GCUK's supply chain finance assets are largely companies with Single A or B credit ratings.*

The inherent credit risk associated with these assets, as well as the material nature of the balances, results in our assessment of this area as that carrying a significant risk of material misstatement."

294. The main working papers recording the work carried out on ECL were the working papers titled: "ECL Reconciliation and Testing 2019" (J225) – which recorded the main testing carried out on ECL in different labelled tabs; "Final – ECL reconciliation" (J227) – which included GCUK's corrected calculations of the ECL provision; "ECL Completeness Review 2019" – which recorded the testing carried out on whether all distributed assets had been considered in calculating the ECL provision; and "CV21" – which contained a review of GCUK's distressed debtors. The main working papers were supported by others which summarised findings, provided background information and addressed specific aspects such as consideration of distressed debtor balances.

295. The Respondents thereafter reported to GCUK's audit committee in the Audit Closing Report that a number of audit procedures had been performed in respect of the ECL provision.

296. However, the work that was described in the audit closing report did not accurately reflect audit work carried out and, as explained further below, the audit work that was performed was inadequate for the reasons set out.

C. Adverse Findings

297. The adverse findings set out below address failings, related to GCUK's calculation of its ECL provision, in respect of:

297.1 identifying and assessing the risks of material misstatement relating to estimation uncertainty within the ECL provision;

297.2 assessing of GCUK's overall approach to the ECL provision calculation;

297.3 testing of individual balances included within the ECL provision;

297.4 testing of GCUK's assessment of "*distressed*" debtors;

297.5 evaluating GCUK's application of the Credit Structure Reduction Factor and the Haircut; and

297.6 evaluating the adequacy of the disclosures in the FY2019 Financial Statements.

ADVERSE FINDING 11: The failure to identify and assess properly the risks of material misstatement relating to estimation uncertainty in respect of ECL

298. Under ISA 540.10, when identifying and assessing the risks of material misstatement under ISA 315, the Respondents were required to evaluate the degree of estimation uncertainty associated with any accounting estimates, in order to obtain sufficient audit evidence as to whether accounting estimates in the FY2019 Financial Statements were reasonable and that related disclosures were adequate.

299. The provision made for ECL was a significant accounting estimate in the FY2019 Financial Statements which generated material estimation uncertainty.

300. The evaluation of estimation uncertainty was particularly important in informing the audit approach because greater estimation uncertainty meant that the ECL provision may be more susceptible to management bias. This was relevant not only to the levels of estimation uncertainty in GCUK's ECL calculation generally, but specifically in respect of the Haircut and the Credit Structuring Reduction Factor, each of which had a significant impact on the level of ECL provision, and the assessments made by GCUK as to the levels of distressed debt.

301. This risk of management bias was acknowledged in general terms by the Respondents in the "Management Override" note, which referred to the risk of material misstatement arising from significant accounting estimates.

302. However, this was the only mention of accounting estimates in the planning and risk assessment working papers and no consideration was given in this note or elsewhere to any specific evaluation of the degree of estimation uncertainty associated with the ECL provision for the purposes of identifying and assessing the risk of material misstatement, in breach of ISA 540.10.

ADVERSE FINDING 12: The failure to respond appropriately to risks arising and to obtain sufficient audit evidence in respect of GCUK's overall approach to the ECL calculation

303. Having identified the valuation and recoverability of assets as giving rise to a significant risk of material misstatement, the Respondents were required to design and perform appropriate audit procedures in order to reduce that risk to an acceptably low level.

304. They were accordingly subject to the requirements contained in ISA 330.6, ISA 330.7 and ISA 330.21 when performing audit procedures in respect of ECL.

305. Under ISA 540.12 the Respondents were additionally required to:

    305.1 determine whether management had appropriately applied the requirements of the applicable financial reporting framework relevant to accounting estimates (ISA 540.12(a)); and

    305.2 determine whether the methods for making the accounting estimates were appropriate and had been applied consistently and whether any changes in accounting estimates or in the method for making them from the prior period were appropriate in the circumstances (ISA 540.12(b)).

306. Under ISA 540.13, the Respondents were also required to do one or more of the following:

    306.1 determine whether events occurring up to the date of the auditor's report provided audit evidence regarding the accounting estimate (ISA 5430.13(a));

    306.2 test how management made the accounting estimate and the data on which it was based, including by evaluating whether the method of measurement and assumptions used were reasonable and appropriate in the circumstances (ISA 540.13(b) and 540.15(b));

306.3 test the operating effectiveness of controls over how management made the accounting estimate, together with appropriate substantive procedures (ISA 540.13(c)); and

306.4 develop a point estimate or a range to evaluate management's point estimate (ISA 540.13(d)).

307. Finally, under ISA 540.15(a) the Respondents were required to evaluate whether management had considered alternative assumptions or outcomes and why those had been rejected.

308. GCUK's methodology for calculating ECL was summarised in the working paper titled "ECL reconciliation and testing 2019" (J225). Reference was also made within the same working paper to a "*review of formulae used* [by GCUK to calculate the ECL provision]" and a "*review of risk rating applied to obligor and insurers*".

309. The section on "*review of formulae used*" then set out the formulae in high-level terms that were in substantively identical terms to the comparable tab in the FY2018 audit working paper. It stated that the entity's methodology was further "*explained in their* [GCUK's] *detailed documentation*".

310. There was, however, inadequate evaluation in the working papers or elsewhere as to whether the formulae or inputs thereto applied in calculating the ECL provision were appropriate or reasonable and whether GCUK's overall approach to the ECL calculation should have been adjusted. At the least, the reasonableness of that overall approach should have been considered by the Respondents in light of the significant reductions made to the provision as a result of the Credit Structure Reduction Factor and the Haircut (see further below).

311. The audit work carried out was insufficient in that:

311.1 No consideration was given to the fact that there had been a significant increase in the size of GCUK's loan book between FY2018 and FY2019 and whether the same methodology remained appropriate in FY2019.

311.2 Whilst reference was made (in the same terms as in the FY2018 audit work paper) to a call with a member of the GCUK finance team to discuss the risk rating used in the ECL calculation, based on credit ratings assessed during 'onboarding', no evaluation was made as to whether the selection of the ORR for each Obligor and insurer was reasonable. Specifically:

a. No consideration was given as to whether reliance on the same credit rating allocated to a particular Obligor during the onboarding process (however long ago that may have been) was appropriate at the reporting date, or to what processes GCUK had in place to monitor the continued appropriateness of individual Obligors' credit ratings (the typical process being to review the same every twelve months, without reference to whether, for example, there may be a different approach needed if there were indications, within the year, that an Obligor's credit worthiness had changed);

b. No consideration was given as to whether any alternative method of calculation had been considered by GCUK and/or rejected; and

c. There was no consideration of the factors applied as part of the "*qualitative*" element of the ORR assessment for each Obligor or any consideration by the Respondents of the reasonableness and appropriateness of how they are applied.

312. It was explained by the Respondents in the working papers that the source of GCUK's risk rating was based on WCF arrangements being for 12 months although the duration of a "*typical*" WCF arrangement covered under "*the main insurance arrangements*" was shorter (80-90 days) (the assumption being that this lessened the risk further) and that this was "*in line with*" the Respondents understanding of GCUK's business model.

313. No explanation was given as to:

313.1 how it had been determined that the typical length of a WCF arrangement backed by insurance was 80-90 days. (Documents did exist outside of the Audit File which contained information as to the length of different WCF arrangements. However, there is no evidence that these were used to verify what the typical length of an arrangement was);

313.2 how this was "*in line with*" the Respondents understanding of GCUK's business model (as noted in section 2 above, and explained further below, in fact many of GCUK's SCF arrangements extended beyond the periods referred to); and

313.3 what extent the length of the SCF arrangements was in fact relevant to the question of the risk of default.

314. In addition, the Respondents failed adequately to identify and evaluate controls applicable to the ECL provision (see also section 1 above on Planning and Risk Assessment). Specifically, GCUK's processes for approving the purchase of receivables, including credit approval, and therefore whether those processes would have resulted in a reliable credit risk rating to form part of the ECL calculation.

315. The Respondents therefore breached:

315.1 ISA 540.12(b), by failing to determine properly whether the methods adopted for the calculation of the ECL provision were appropriate and had been applied consistently;

315.2 ISA 540.13, by failing to perform properly any of the steps listed in ISA 540.13(a) to (d) as part of evaluating overall GCUK's ECL methodology; and

315.3 ISA 540.15(a), by failing to evaluate whether management had considered alternative assumptions or outcomes for the methodology for calculating the ECL provision and why those had been rejected.

316. Further to the ISA requirements set out above, IFRS 9 paragraphs 5.5.19 and 5.5.20 required an assessment to be made of how the ECL provision might be affected (in terms of the maximum period and maximum amount to be considered for the purpose of measurement) by the fact that for certain types of WCF: the re-payment term could be extended by way of a roll; and the drawn down facilities in place (e.g. for IPAs), which allowed Obligors to draw funds down in stages, could affect the maximum period or amount of the loan facility.

317. Such an assessment would have required an understanding of the precise nature of relevant assets and the legal agreements underpinning the particular transactions, as well as what was known of the borrowing patterns or appetite of the Obligor. No such assessment was performed. Therefore, no determination could properly be reached as to whether management had appropriately applied the requirements of the applicable financial reporting framework relevant to its ECL methodology, leading to a breach of ISA 540.12(a).

318. As a result of the above, the Respondents accordingly failed to design and perform audit procedures responsive to the Significant Risk of material misstatement in respect of the valuation and recovery of assets at the assertion level, in breach of ISA 330.6, ISA 330.7 and ISA 330.21.

ADVERSE FINDING 13: The failure to respond appropriately to risks arising and to obtain sufficient audit evidence in respect of individual balances included in the ECL calculation

319. The requirements of ISA 330.6, ISA 330.7, ISA 330.21, ISA 540.12, ISA 540.13 and ISA 540.15 which applied to the audit work relating to the ECL provision are explained and summarised above.

<u>The failure to test the individual balances for the main element of the ECL provision</u>

320. The Respondents' primary assessment of individual balances for the main element of the ECL provision was contained in the "ECL reconciliation and testing 2019" (J225) working paper. The information contained within that working paper, including an explanation of the approach to testing individual balances (the "*method*"), was in substantively identical terms to the comparable tab in the FY2018 audit working paper on ECL. It made no reference to the fact that there had been a significant increase in the size of GCUK's loan book between FY2018 and FY2019 or how that had been taken into account when assessing whether the same methodology was appropriate in FY2019.

321. The testing of the balances was carried out using what was described (in the "ECL Completeness Review 2019" working paper) as the "*NCS*" data (the source data against which the ECL workings were to be reconciled), to "*ensure all assets had been considered".* The NCS data was generated by an IT system generated by GCUK for its own usage and no work was undertaken to identify or evaluate the controls relevant to that software (see also section 1 above on Planning and Risk Assessment).

322. Although the Respondents sought to compare the amounts included in the ECL calculation spreadsheet prepared by GCUK to the NCS data, no audit evidence was obtained to verify that the NCS data was itself a complete and accurate record of all assets generated by GCUK outstanding at the reporting date and therefore whether the balances on which the ECL provision was based were complete.

323. The J225 working paper recorded that GCUK allocated balances different "*statuses*", including whether the Obligor was to be excluded from the ECL provision as an "*exception*".

324. The work paper also showed that material amounts would be excluded from individual "*Total Outstandings*" amounts to arrive at the amount on which the calculation of the ECL provision was based. The amounts excluded appear to be (USD) amounts in columns headed "[HIF] *Outstandings*" (a reference to the H Fund), "*Distribution Outstandings*" and in the case of at least one Obligor the column headed "[IG] *Outstandings*" (contained within the working paper titled "Final – ECL reconciliation"). The balances funded by the H Fund were excluded for example as these were subject to a separate risk sharing agreement.

325. However, these amounts were not consistently excluded for all Obligors and again no audit evidence was obtained to confirm that these amounts were appropriately included or excluded e.g. that each balance included in the "[HIF] *Outstandings*" column was in fact a balance acquired by the [H Fund]. As set out in section 1 above (on Planning and Risk Assessment) the Respondents could not rely on GCUK's controls to ensure that balances were included in the correct column because they did not identify or evaluate any controls that would ensure that was the case.

326. In respect of the balances selected for testing:

    326.1 the Respondents only selected from the balances that GCUK had already concluded should be included within the ECL calculation and no audit procedure was performed in relation to any of the balances that GCUK had excluded from the ECL provision; and

    326.2 the sample selection process was flawed on the basis that the "*sample was focussed on the higher value obligors (based on funded balance)*", rather than ensuring that each item within the population had an equal chance of selection.

327. In practice, however, the Respondents (by default rather than design) tested 97.7% of all balances included within GCUK's ECL provision, which amounted to 20 balances in total and 38.5% of the Total Outstanding amounts.

328. The testing conducted by the Respondents on the balances sampled, as recorded in working paper J225, amounted to seven steps, as per the described "method". The steps involved:

    328.1 Verification of various points of detail to underlying documents. This verification was recorded through ticks and crosses in six columns; and

    328.2 In addition, the Respondents stated they would reach a judgement on whether "*each ECL balance was appropriately calculated"* after "*reviewing the calculation*". Again, the conclusion as to whether each balance was "*appropriately calculated*" was recorded by way of a tick or cross, in a further column.

329. There was no explanation as to how the Respondents assessed whether the individual estimates and assumptions that formed part of the ECL calculation and required some form of subjective judgement to be exercised, were reasonable. The "*tick box*" approach adopted involved merely cross-checking the individual Obligor balances for data accuracy and the recording of a final conclusion on each without any explanation as to how it had been concluded that the balance had been appropriately calculated.

330. Finally, there was no verification of the amount of £1.036 billion disclosed in the FY2019 Financial Statements for exposure under insurance policies, in respect of all the balances included in the ECL provision. This figure does not appear in any of the Audit working papers.

The failure to test adequately the Venture Capital Fund balances

331. Five Venture Capital Fund balances had a different loss sharing arrangement from the main ECL provision, governed by a credit default swap arrangement.

332. The audit work carried out in relation to these five balances was also recorded in working paper J225. The testing involved checking seven different matters and reaching conclusions as to whether "*ECL calculated correctly*" and "*Test satisfactory*". However, as with the testing of balances included in the main ECL provision, the results were recorded simply as a "*tick*" or as "*n/a*", without any further explanation being provided.

333. Two notes on this testing referred to the results of inquiries as to the existence of security put forward by two of the Obligors and checks carried out to ensure the amount of security relied on by GCUK were the same as stated in the security agreement. No information was provided, however, as to how:

    333.1 the security was confirmed in each case;

    333.2 the appropriateness of the types of security being relied upon was evaluated; or

    333.3 the appropriateness of the valuation of the security used in the calculation was assessed as appropriate.

Summary of Breaches

334. Accordingly, as part of testing the individual balances that made up the ECL provision and the Venture Capital Fund balances, the Respondents failed to:

    334.1 determine properly whether the methods adopted for the calculation of the ECL provision were appropriate and had been applied consistently;

    334.2 perform properly any of the steps listed in ISA 540.13(a) to (d); and

    334.3 evaluate whether management had considered alternative assumptions or outcomes for the methodology for calculating the ECL provision and why those had been rejected.

335. Consequently, the Respondents breached ISA 540.12(b), ISA 540.13 and ISA 540.15(a).

336. As a result of the above, the Respondents accordingly failed to design and perform audit procedures responsive to the Significant Risk of material misstatement in respect of the valuation and recovery of assets at the assertion level, in breach of ISA 330.6, ISA 330.7 and ISA 330.21.

ADVERSE FINDING 14: The failure to respond appropriately to risks arising and to obtain sufficient audit evidence in respect of "*distressed*" debtors

337. Under IFRS 9, the FY2019 Financial Statements had to disclose the amounts falling into three separate categories of financial asset known as:

    337.1 Stage one (Performing);

    337.2 Stage two (Under-performing); and

337.3 Stage three (Non-performing).

338. The requirements of ISA 330.6, ISA 330.7, ISA 330.21, ISA 500.6, ISA 500.9, ISA 540.12, ISA 540.13 and ISA 540.15 applicable to the audit work relating to the ECL provision are explained and summarised in the section above.

339. In addition, under ISA 240.32, the Respondents were required to design and perform audit procedures to review accounting estimates for bias and evaluate whether the circumstances producing the bias, if any, represented a risk of material misstatement due to fraud. This required the Respondents to evaluate properly those judgements and decisions made by management.

340. The approach to assessing stages of debtors was set out by the Respondents in working paper J225. Within that working paper the Respondents explained, at a high-level, the considerations that should be taken into account when assessing whether debtors should move between stages:

"*For transfers between stage 1 and stage 2 there must be a significant change in the probability of default between initial recognition and that at the period end, with an increase in the credit risk shown… For transfers between stage 2 and stage 3 there must be breach of contract or significant financial difficulty of the obligor…*"

341. The Respondents' "*Review of assessment stages*" was recorded as follows:

341.1 "*Assessment of the stage is in line with the IFRS 9 considerations (see tab)*";

341.2 "*Given that the maturity of the credit losses are often within 12 months then we would expect the majority to be recorded as stage 1*"; and

341.3 "*Thought has also been given to the 30 days/90 days past due default criteria and the client is aware that this must also be taken into consideration.*"

342. The approach taken by the Respondents to evaluating GCUK's assessment of the identified "*distressed*" debtors as described, was deficient in the following ways:

342.1 It did not explain why the period of time over which the debt was payable was a relevant consideration when assessing which Stage an Obligor's balance fell within. The fact that a debt was due to be paid within 12 months' time did not mean that it always fell within Stage one. Rather, any length debt could potentially fall within Stage two or Stage three where the relevant criteria as to increased credit risk was met.

342.2 A proper assessment of all Obligors balances, of whatever length, needed to be carried out under IFRS 9, with those balances being reclassified as and when appropriate and the potential impact of the relevant ECLs at year end should have been evaluated. No such assessment was performed by the Respondents.

342.3 As part of that assessment, the Respondents should have considered whether any of the facilities related to the distressed debts could be extended by way of a "*roll*" and/or the fact that some involved a "*draw down*" facility that still had an undrawn element.

342.4 Although the Respondents made reference to the "*30 days/90 days past due default criteria*" (which was relevant as evidence of potential distress) needing to be considered by GCUK, no testing was carried out to establish if in fact, or how, GCUK had taken this into consideration. Whilst the Respondents reviewed overdue balances by reference to maturity dates, overdue balances could be masked by 'rolling' the balance into a new advance, which would give the appearance that the loan had been repaid when this was not in fact the case and no audit work was carried out in respect as to how GCUK assessed 'rolled' balances.

343. The Respondents also reviewed an untitled document that was prepared by GCUK (working paper "CV21"). The paper contained GCUK's explanation as to why no adjustment should be made to the level of ECL provision relating to a number of Obligors becoming "*distressed*" (i.e. moving to Stage three) and comments from the Respondents. The conclusion reached by GCUK was that no adjustment was needed despite a number of Obligors becoming distressed since the year end because there was a potential overprovision on other debtors to justify making no adjustment. The Respondents noted (on the working paper) that even on GCUK's approach a potential net under-provision of $2.42 million would arise but concluded that this would only arise in the not "*probable*" event that all the distressed debt defaulted in full.

344. The Respondents' analysis of the information in working paper "CV21" was inadequate as it gave no explanation as to what process was followed by GCUK in identifying only those balances identified in "CV21" as ones that needed to be considered, it simply relied on the assumption that there were no others. The Respondents did not carry out any procedures themselves to identify whether there were any further distressed debts not reported to them by GCUK.

345. In addition, it did not:

345.1 Consider the appropriateness of a factual assertion by GCUK that there was a general over-provision within the ECL calculation in the sum of c.$13.8 million, calculated by taking into account post-year end recoveries on the outstanding balances and reducing the ECL provision accordingly. This was inconsistent with the provision being considered on an overall basis and as at the reporting date, in accordance with IFRS 9, paragraph 5.5.17. In the ordinary course of events, there would typically have been post-year end recoveries, particularly on debts where the probability of default was considered to be low, but that would not justify reducing the ECL provision each year as at the accounting date.

345.2 Evaluate how management's judgement to rely on a general overprovision for ECL as at the accounting date for the purposes of absorbing additional distressed debt, interacted with its judgement to apply a Haircut to the provision, on the same purported justification, at the level of 25% (see further below).

346. The Respondents also accepted, apparently without question, or further investigation (beyond a review of some limited documentation provided in relation to certain of the debts), the factual assertions made by GCUK as to the recoverability of the distressed debts for three Obligors:

346.1 Distressed Debtor A (ECL $5.5 million on a total exposure at default of $30.5 million):

GCUK asserted that the sums owed by this debtor would be fully recoverable on the clearly inadequate basis that a restructuring was planned for the future. This was despite the (unaudited) accounts of Distressed Debtor A available at the time of the Audit showing that it had little revenue, was loss making and was funded mainly by the GCUK facility.

346.2 Distressed Debtor B (ECL $3.5 million on an exposure at default of $3.5 million):

GCUK asserted that because a repayment plan had been put in place by a US court and GCUK was noted as an unimpaired creditor, the existing provision of $3.5 million was an over provision. There was, however, no assessment of whether Distressed Debtor B had the funds and ability to fulfil its obligations under the payment plan.

346.3 Distressed Debtor C (ECL $5.97 million on a total exposure at default of $23.88 million):

GCUK (as a gesture of goodwill to the Investment Bank that invested in its receivables) had agreed to repurchase the whole debt of $29 million in February 2010 but asserted that it would fall within the H Fund loss absorption limit of 1% of total funds, which amounted to $23.6 million. The Respondents concluded on this basis that the under provision for the Distressed Debtor C balance was £5.97 million, but that the effect of the Haircut (25% * $23.6 million = $5.97 million) should be reversed to reflect that the whole absorption limit would be used and to prevent double counting the reduction of the provision the loss absorption mechanism was not used, then the full $23.6 million loss absorption would remain a potential liability for GCUK (and the ECL provision would be understated by that amount).

347. No further evidence or explanation was obtained to support the statements made by GCUK in "CV21", despite this being an area at obvious risk of management override and bias. The Respondents accepted and relied on the factual assertions and subjective judgements made by GCUK for the conclusion that no adjustment to the ECL for these distressed debtors was required.

348. On 1 May 2020, the Respondents received a further document from GCUK titled "ECL update and distressed debts – 31 March 2020" (working paper "CV24"). Both working paper "CV24" and the email to which it was attached included additional information to that provided in working paper "CV21".

349. The main changes made by working paper "CV24", were as follows:

349.1 The IFRS 9 General Provision adjustment was reduced from -$13.8 million to -$7.4 million, apparently to reflect the fact that individual Obligors had made fewer payments than had previously been stated;

349.2 However, to compensate for this, a further adjustment was made in respect of the Venture Capital Fund balances to reflect additional observations made that the provision made in respect of the Obligors who were subject to the credit default swap arrangement that applied to the Venture Capital Fund was overstated by $6.22 million, on the basis of repayments received since 31 December 2019; and

349.3 A further distressed balance was identified for Distressed Debtor D (with exposure at default of $15.9 million).

350. The overall result was that GCUK's overall calculation in working paper "CV24" led to a very similar sum to that reached in "CV21" (-$11.28 million).

351. The Respondents failed to take into account any of that additional information provided by GCUK and, specifically, they did not consider:

351.1 How GCUK identified the additional distressed debtor. This did not prompt the Respondents to either ask GCUK whether there were any further distressed debts not reported to them or carry out procedures to enable them to identify the completeness of the distressed debtors themselves;

351.2 Why post-year end recoveries on the "*top ten*" Obligors set out on working paper "CV24" were significantly lower than those set out on the earlier version of the working paper ("CV21"), with no explanation provided for these differences and whether this raised a question as to whether monitoring processes within GCUK were adequate to ensure credit risk ratings were kept up to date; and

351.3 Whether it was appropriate to introduce Venture Capital Fund Obligors into the analysis, particularly given that their inclusion balanced the effect of the reductions in post year end recoveries identified in "CV24".

352. Consequently, the Respondents failed, as part of assessing GCUK's analysis of the distressed debtors, to:

352.1 determine properly whether management had appropriately applied the requirements of the applicable financial reporting framework relevant to its ECL methodology;

352.2 determine properly whether the methods adopted for the calculation of the ECL provision were appropriate and had been applied consistently;

352.3 perform properly any of the steps listed in ISA 540.13(a) to (d); and

352.4 evaluate whether management had considered alternative assumptions or outcomes for the methodology for calculating the ECL provision and why those had been rejected.

353. The Respondents therefore breached ISA 540.12(a) and (b), ISA 540.13 and ISA 540.15(a).

354. As a result of the above, the Respondents accordingly failed to design and perform audit procedures responsive to the Significant Risk of material misstatement in respect of the valuation and recovery of asserts, in breach of ISA 330.6, ISA 330.7 and ISA 330.21.

355. Given the subjective nature of the assessment of distressed debts, and in the context of a potentially substantial increase in GCUK's ECL provision in FY2019, it should have been apparent to the Respondents that the judgements reached by GCUK in relation to distressed debtors were particularly susceptible to management bias. However, in breach of ISA 240.32, the Respondents failed to design and perform audit procedures to review the analysis of distressed debtors for bias or to evaluate whether the

circumstances producing the bias, if any, represented a risk of material misstatement due to fraud.

ADVERSE FINDING 15: The failure to respond appropriately to risks arising and to obtain sufficient audit evidence in respect of adjustments to the ECL calculation made through the application of the Credit Structure Reduction Factor and the Haircut

356. The requirements of ISA 330.6, ISA 330.7, ISA 330.21, ISA 500.6, ISA 500.9, ISA 540.12, ISA 540.13, ISA 540.15 and ISA 240.32 to the audit work relating to the ECL provision are explained and summarised in the section above.

The failures in respect of the Credit Structure Reduction Factor

357. The majority of the ECL provision was the product of a detailed calculation relating to the probability of default by Obligors, and GCUK's exposure to individual Obligors, involving a range of factors and data points.

358. In FY2019, GCUK introduced a Credit Structure Reduction Factor to be applied to reduce the ECL provision, on the basis of security in place and product type, for individual Obligor balances within the main element of the ECL provision.

359. This resulted in a total reduction of the main element of the ECL provision of $15.9 million, nearly five times materiality.

360. On 24 December 2019, GCUK informed Saffery that there had been an update to the ECL model. Thereafter, on 31 January 2020, a document titled "GC Credit ratings comparison" was provided to the Respondents by GCUK. The document comprised two pages, one headed "*Credit Ratings Comparison Table"* and the second headed "*Loss Given Default Guidance Tables*". The latter tables allocated different (unexplained) percentages (representing the default reduction factor to be applied) to different categories of WCF and the different products within those categories.

361. At the end of the document, the "*Information Source*" was described as being:

> *"LGD values are approximated based upon observed historical loss/ historical rates relating to defaults observed in relation to Greensill facilities. All values will be periodically reviewed and compared to observed losses to refine the outlined guidance".*

362. It was noted by a member of the audit team in an email to GCUK on 26 February 2020, the impact of the provision at year end was to reduce the provision significantly (at this stage estimated to be by $9 million).

363. Whilst a number of enquiries were subsequently made by the Respondents of GCUK for further information relating to the Credit Structure Reduction Factor, the result of these was that:

    363.1 GCUK reiterated that the new credit structure calculation had been approved by the Board and GCUK's Credit Committee;

    363.2 The Respondents recorded their understanding (in an email to GCUK) that:

"*the new credit structure is based upon your experience of historical losses and using professional judgement you have decreased the ECL provision on a range of outstanding balances. It would appear that this is done on a case by case basis as opposed to using an overriding formula as with the previous credit structure calculation";*

363.3 GCUK stated that:

"In the past and in the absence of a database of LGD data, the credit structure has been excluded in a conservative approach to calculating Expected Loss (PD x EAD x LGD) and Loss Reserves. Now that this has been collated and databased these figures can be added to the calculation to more accurately reflect the security and facility structures present";

363.4 GCUK provided a table illustrating how the calculation had been applied to 10 Obligor balances, noting that two of the percentages arrived at did not "*reconcile with the guidance*" and justifying this by reference to a conservative approach being taken by an "*analyst*" "*noting the deal structure*"; and

363.5 The Respondents reproduced the table of balances in work paper J225 with the comment that:

"The above was discussed with the client in detail whilst on site and was concluded to be reasonable considering the level of additional data and resources available".

364. There was no other record of any conversations stated to have been held with GCUK "*on site*" relating to the Credit Structure Reduction Factor.

365. There was no adequate explanation in any of the work papers of the factors or considerations that informed the Respondents' conclusions as to whether GCUK had adopted an appropriate methodology or reasonable assumptions in applying the Credit Structure Reduction Factor and whether the amount of the reduction applied to individual balances was reasonable.

366. In particular:

366.1 The Respondents did not obtain an adequate understanding of how the methodology used to determine the Credit Structure Reduction Factor would apply to an Obligor balance.

366.2 There was no evidence as to how the Credit Structure Reduction Factor percentage was calculated for individual balances beyond the very high-level information provided in the "*Loss Given Default Guidance Tables*" contained in the document titled "GC credit ratings comparison" i.e. by product categories.

366.3 There was no explanation as to what factors (or loss mitigation strategies), other than security, were taken into account as part of GCUK exercising their "*professional judgement*" based on observations of historical losses.

366.4 There was no evidence that the security documents relating to the relevant balances had been reviewed by the Respondents.

366.5 There was accordingly no evidence that the Respondents had considered:

a. Whether any relevant security was legally enforceable by GCUK and, if so, in what circumstances, by what means and in which jurisdiction(s); or

b. The underlying value of the assets over which security was granted, which would be integral to understanding the value of that security; or

c. The nature and quality of the title to those assets.

366.6 There was no evaluation conducted as to whether GCUK had considered alternative assumptions or outcomes (e.g. different methods of calculating any reduction to be applied) when deciding to apply the Credit Structure Reduction Factor in calculating the ECL provision.

366.7 No explanation or justification was explored as to why the "*analyst*" within GCUK considered that the two balances where the percentages did not reconcile with the guidance referred to in the email dated 11 March 2020 were the result of taking a "*conservative*" approach.

<u>The failure to evaluate the Haircut</u>

367. The ECL provision as calculated, including the reductions made applying the Credit Structure Reduction Factor but excluding Venture Capital Fund balances and those of "*non-performing entities*", was subsequently reduced by GCUK by the 25% Haircut, amounting to a reduction of c.$13.9 million.

368. The purported rationale for this adjustment was explained in a short paper headed "Expected Credit Loss (ECL) Provision assessment" produced by GCUK (dated January 2020). In summary it was asserted that GCUK's ECL provisioning had been very conservative historically, noting that circa 50% of the provision was utilised in FY2018. The reasons given for this conservatism were:

368.1 The probability of default rates used in the model are a 12-month tenor. Greensill's tenor is around 80-90 days on average. The credit agency used did not generate probability of default tables for tenors shorter than 12 months; and

368.2 The enhanced credit assessment function created by Greensill has led to more robust customer acceptance procedures and continuous monitoring, resulting in potential defaults being managed down before they become actual bad debts.

369. The reason provided as to how the amount of 25% was arrived at was said to be that "*management are comfortable that 25% is not aggressive*".

370. The extent to which the Respondents considered the reasonableness of the Haircut was described in working paper J225. The Respondents' conclusion was that the Haircut seemed "*reasonable*" taking account of a confirmed 52% utilisation of the provision in FY2018, the fact that the model for calculating the provision was based on much longer tenor periods that the Respondents understood to be typical for GCUK's business, and verification of increased employee numbers in respect of GCUK's credit assessment function.

371. Fundamentally, the Respondents carried out no adequate evaluation of the reasonableness or appropriateness of the Haircut being applied by GCUK at a level of 25% or otherwise, despite the fact that the size of the reduction being proposed, even after excluding the Venture Capital Fund balances, ($13.9 million) was effectively more than four times the materiality threshold.

372. In particular:

372.1 No consideration was given to the appropriateness of that reduction in light of:

a. The significant increase in GCUK's loan book in FY2019, which increased risk of debtor default; and/or

b. The information provided by the Group Auditor in their email dated 19 April 2020 explaining the change in accounting policy in respect of revenue recognition for FY2020. That email explained that the ECL provision for FY2020 was expected to increase significantly and that the Greensill Group's actual losses would follow a normal distribution that more closely aligned with the ECL provision.

372.2 No consideration was given as to whether GCUK's justifications for the Haircut were appropriate. For example:

a. The fact that the ECL provision had not been fully utilised in the past was not necessarily a reason for reducing it in the future. Whilst it was permissible to take into account past events under IFRS 9, paragraph 5.5.17, this could not be done without reference to current and future events. As far as the Respondents may have considered that GCUK may have had scope to reduce the ECL provision by up to the value not utilised in previous years and thereby 25% could be considered to be "*prudent*", this failed to give consideration to the factors referred to above.

b. There was no evidence to support the "*understanding*" asserted that GCUK's "*typical tenor is 80-90 days*" such that the model for calculating the ECL provision was based on much longer tenor periods than was typical for GCUK's business. Nor was it explained how that understanding was to be reconciled with receivables with longer tenors (see further below), including the fact that many WCF arrangements had the characteristics of revolving credit facilities.

c. There was no explanation of why increased employees had "*enhanced customer acceptance procedure*" and the "*continuous monitoring process*" in place.

372.3 No assessment was made of whether the factors used to justify the Haircut were already accounted for in relation to individual Obligor balances through either:

a. the assessment of the IFRS 9 General Provision Adjustment (considered in the assessment of "*distressed debtors*"); or

b. the introduction of the Credit Structure Reduction Factor.

372.4 No evaluation was made as to the extent to which an arbitrary 25% reduction could be reconciled with the detailed calculation carried out by GCUK for assessing ECL or with the requirement that the ECL provision be a "*probability-weighted*" assessment under IFRS 9, paragraph 5.4.17(a). In the circumstances, the Respondents should have considered whether the purported need for a 25% reduction caused concerns that the overall calculation methodology for the ECL provision was inaccurate. If GCUK believed that their own ECL model was unable to accurately assess the

necessary ECL then the solution was for GCUK to address that by preparing a revised, probability-weighted calculation under IFRS 9, paragraph 5.4.17; and

372.5 There was no evaluation conducted as to whether GCUK had considered alternative assumptions or outcomes (e.g. using an alternate methodology for calculating ECL) when deciding to apply the Haircut when calculating the ECL provision.

Summary of Breaches

373. Consequently, the Respondents failed, in the context of the Credit Structure Reduction Factor and the Haircut, to:

373.1 determine properly whether management had appropriately applied the requirements of the applicable financial reporting framework relevant to its ECL methodology;

373.2 determine properly whether the methods adopted for the calculation of the ECL provision were appropriate and had been applied consistently;

373.3 perform properly any of the steps listed in ISA 540.13(a) to (d); and

373.4 evaluate properly whether management had considered alternative assumptions or outcomes for the methodology for calculating the ECL provision and why those had been rejected.

374. The Respondents therefore breached ISA 540.12(a) and (b), ISA 540.13 and ISA 540.15(a).

375. As a result of the above, the Respondents failed to design and perform audit procedures responsive to the significant risk of material misstatement in respect of the valuation and recovery of assets, in breach of ISA 330.6, ISA 330.7, ISA 330.21.

376. In addition, given the subjective nature of the Credit Structure Reduction Factor and the Haircut, and in the context of a potentially substantial increase in GCUK's ECL provision in FY2019, it should have been apparent to the Respondents that these adjustments were particularly susceptible to management bias. However, in breach of ISA 240.32, the Respondents failed to design and perform audit procedures to review either the Credit Structure Reduction Factor or the Haircut for bias or to evaluate whether the circumstances producing the bias, if any, represented a risk of material misstatement due to fraud.

ADVERSE FINDING 16: The failure to obtain sufficient appropriate audit evidence to evaluate the adequacy of the disclosures in the FY2019 Financial Statements relating to the ECL provision

377. The Respondents were required to obtain sufficient audit evidence about whether the disclosures in the FY2019 Financial Statements related to accounting estimates were in accordance with the requirements of the applicable financial reporting framework under ISA 540.19, ISA 540.20, ISA 700.12 and ISA 700.13.

378. As already set out, in FY2019 GCUK made two significant changes to the calculation of the ECL provision in the form of the Credit Structure Reduction Factor and the Haircut.

379. Under paragraph 35G of IFRS 7, GCUK was required to disclose any: "*changes in the estimation techniques or significant assumptions made during the reporting period and the reasons for those changes*".

380. Similarly:

380.1 Paragraph 39 of International Accounting Standard 8 required an entity to disclose the nature and amount of a change in an accounting estimate that has an effect in the current period or is expected to have an effect in future periods, except for the disclosure of the effect on future periods when it is impracticable to estimate that effect; and

380.2 Paragraphs 35K and 35M of IFRS 7 required extensive disclosures to be made in financial statements in respect of credit risk exposures. In the case of GCUK the disclosures were required to enable users of the FY2019 Financial Statements to assess credit risk exposure and understand its significant credit risk concentrations.

381. The required disclosures were particularly important in FY2019 as it was the first year that the Credit Structure Reduction Factor and the Haircut had been made and, in respect of the disclosure required as to the impact of collateral under IFRS 7, the adjustment for the Credit Structure Reduction Factor directly impacted on the reported profit for the year.

382. The FY2019 Financial Statements did not make any mention of the change made to the estimation technique either by adjusting the provision to take account of the Credit Structure Reduction Factor or the Haircut and did not include any disclosures in accordance with paragraphs 35K and 35M of IFRS 7.

383. No assessment was made by the Respondents during the course of the Audit as to whether such disclosures needed to be made by GCUK, in breach of ISA 540.19, ISA 540.20, ISA 700.12 and ISA 700.13.

ADVERSE FINDING 17: The failure to evaluate the reasonableness of the ECL provision and determine misstatement

384. In respect of the ECL provision, based on the matters set out above, the audit team could also not have properly formed a view as to whether the accounting estimates in the FY2019 Financial Statements were either reasonable in the context of the applicable financial reporting framework or were misstated. Therefore, they were also in breach of ISA 540.18.

SECTION 5: GOING CONCERN

A. Introduction

385. The FY2019 Financial Statements were prepared by GCUK on the going concern basis.

386. Although going concern was not identified by the Respondents as a significant risk area for the Audit, the Respondents' evaluation of GCUK's assessment of going concern was critical to the Audit and to the reaching of an independent audit opinion.

387. Notwithstanding that the Respondents' audit work regarding the assessment of going concern breached *Relevant Requirements* (as set out further below), Executive Counsel does not suggest that such breaches caused the insolvent administration of GCUK.

B. Background

388. A proper understanding of GCUK's business operations, risks and dependencies was essential to the Respondents' ability to conduct a proper evaluation of GCUK's going concern assessment. However, as set out in section 1 (on Planning and Risk Assessment) the Respondents' audit work was deficient in these areas in a number of respects.

389. The following matters required careful consideration during the Respondents' evaluation of GCUK's assessment of its ability to continue as a Going Concern:

    389.1 GCUK's SCF business, which generated around 90% of its revenue, depended upon GCUK obtaining trade credit insurance in order to make the majority of the receivables it acquired marketable to investors. GCUK's inability to maintain insurance coverage, for whatever reason, was therefore a clear business risk for GCUK and needed to be considered as part of any going concern assessment;

    389.2 GCUK's business model was reliant on the capacity of investors, particularly the Investment Bank, as well as the Asset Management Company (albeit that the funds managed by the latter were of decreasing significance by the end of FY2019 and into FY2020) and Greensill Bank (which was related to GCUK) to buy the rights to the receivables generated by the WCF business;

    389.3 The central assumptions made by GCUK in its going concern assessment as to the availability of sufficient third-party financing to enable it to have adequate cash resource throughout the period of the going concern assessment; and

    389.4 A number of key underlying assumptions within GCUK's cashflow forecasts.

<u>Overview of the audit work performed</u>

390. The "Going Concern Review" working paper on the Audit File (dated 21 April 2020) recorded the Respondents' conclusions on GCUK's assessment of going concern:

    "Information above is adequate for directors to make going concern assessment.

    All relevant information has been considered.

    Directors have considered a sufficient period in assessing going concern."

391. This was stated to be based on:

    391.1 the Respondents' view that the group had performed well post-year end;

    391.2 an assessment of the risk that SCF might be subject to greater regulation in the future; and

    391.3 a conclusion that there were no indications that Covid-19 would cause any going concern issues.

392. This led to an overall conclusion that "*There are no indications that the UK group is not a going concern*".

393. The majority of the Respondents' work on going concern was recorded in two audit working papers: "Cashflow Forecast Review", dated 19 May 2020; and "Going Concern Review – main work programme and findings", dated 22 May 2020 (the same date that the FY2019 Financial Statements were signed). The Respondents concluded, on the latter working paper, that there was no material uncertainty in relation to GCUK's ability to continue as a going concern.

394. In addition, on 6 May 2020, Mr Di Leto had requested a senior member of the Technical and Compliance team at Saffery to perform a "*technical review*" of going concern work.

395. The Audit Closing Report, dated 17 April 2020 and therefore prior to the above work being carried out, made no reference to the Respondents' work in respect of going concern.

396. On 26 May 2020, the Respondents provided an unqualified audit opinion for the FY2019 Financial Statements. The Respondents therefore accepted GCUK's assessment that there were no material uncertainties that may cast significant doubt on GCUK's ability to continue as a going concern.

C. The Adverse Findings

397. The adverse findings set out below address failings, in the context of GCUK's going concern assessment, in respect of:

    397.1 evaluating the ongoing availability of trade credit insurance and the ongoing appetite and/or ability of WCF investors to fund GCUK's receivables;

    397.2 assessing the availability of third-party financing and therefore to evaluate GCUK's assessment of its ability to continue as a going concern;

    397.3 assessing the assumptions relied on in the GCUK forecasts; and

    397.4 performing audit procedures with a sufficient level of professional scepticism.

ADVERSE FINDING 18: The failures to consider properly, as part of the audit risk assessment, GCUK's dependency on trade credit insurance and the ongoing appetite and/or ability of WCF investors, as events or conditions existing that may have cast significant doubt on GCUK's ability to continue as a going concern, and accordingly to evaluate properly GCUK's going concern assessment

398. The Respondents were required under ISA 570 to evaluate GCUK's assessment of its ability to continue as a going concern and, in particular, to obtain sufficient appropriate audit evidence to conclude whether a material uncertainty existed in relation to going concern.

399. In the first instance, in the context of performing risk assessment procedures under ISA 315, ISA 570.10 required the Respondents to consider whether events and conditions exist that may cast significant doubt on the entity's ability to continue as a going concern.

400. ISA 570 also required the Respondents:

400.1 to evaluate GCUK's assessment of its ability to continue as a going concern in accordance with ISA 570.12, covering a period of at least 12 months following from the date when the FY2019 financial statements were authorised for issue (as per ISA 570.13);

400.2 to remain alert throughout the Audit for audit evidence of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern (ISA 570.11); and

400.3 to consider whether GCUK's assessment included all relevant information of which the Respondents were aware as a result of the Audit, under ISA 570.14.

Failings in respect of the ongoing availability of trade credit insurance

401. During the course of the Audit, the Respondents had material in their possession that indicated trade credit insurance played an integral role throughout the WCF business and was of critical importance to the continuing operation of that business.

402. There were also a number of important developments that the Respondents were aware of or ought to have been aware of during the FY2019 Audit that had the potential to affect the continuity of GCUK's insurance coverage.

403. In particular:

403.1 The two key insurance policies for GCUK (i.e., the Standalone Policy and the Insurer B Policy) both fell for renewal in March 2020 and therefore (even on the assumption that they were renewed at that time for a further 12 months) would fall for renewal by March 2021 – which was within the next 12-month minimum period for any going concern review;

403.2 The significant change to macroeconomic conditions as a result of the impact of the Covid-19 pandemic and the potential impact on the:

a. insurance market; and

b. the likely terms on which any future renewal of insurance would be possible in that environment i.e. any potential tightening of the market in terms of what risks were capable of being insured and to what extent.

403.3 The terms of the Standalone Policy (which was the most significant policy) were highly advantageous to GCUK because they provided unlimited cover without requiring any cash collateral. There was no guarantee that – even if the Standalone Policy were to be renewed in March 2021 – it would be renewed on the same advantageous terms; and

403.4 This was particularly so because ownership of Insurer A had changed from 1 July 2019 and so from that date Insurer A was no longer authorised to underwrite trade credit insurance policies for its previous owner. There was no indication that the new owner would continue to provide insurance cover when the renewal arose, still less on the advantageous terms that had previously been available to GCUK.

404. It also became apparent during the FY2019 Audit that Insurer A's new owner was less willing to provide insurance cover to GCUK than its previous owner had been or, at the very least, that there was no evidence that the new owner would take a similar approach to the previous owner.

405. This became evident from the fact that:

405.1 The CS Policy, the term for which was October 2018 to 2019, was not renewed for a further period beyond October 2019;

405.2 The Standalone Policy expired in March 2021 in the following circumstances:

a. The Standalone Policy had been issued for a period of approximately one year, to cover the period 22 February 2019 to 1 March 2020 with the previous owner as the underwriter.

b. The Standalone Policy was renewed for an additional year to cover the period 1 March 2020 to 1 March 2021, with the renewal dated 10 June 2019 and concluded in the name of the previous owner on 27 June 2019. This was shortly before Insurer A's authorisation to underwrite policies for the previous owner ceased, on 30 June 2019, and eight months before the actual policy renewal date of 1 March 2020; and

405.3 The renewal date for the Standalone Policy was highly significant because renewal took place prior to Insurer A starting to issue insurance policies on behalf of the new owner (from 1 July 2019). It could not, therefore, provide any comfort on the critical issue of whether the new owner would be willing to renew the insurance cover beyond March 2021, still less on the existing terms.

406. In addition, like the Standalone Policy, the Insurer B Policy fell for renewal in March 2020. Although the Insurer B Policy had been renewed every 12 months since 2017, the subsequent renewal was incremental and short-lived. It was extended, first on 28 February 2020 to 15 April 2020, then on 9 April 2020 to 15 May 2020 and on 14 May 2020 to 15 June 2020 and, finally, on 28 May 2020 to 15 August 2020 when it expired. The final renewal was dated post the Audit report being signed by the Respondents; however, three earlier renewals were executed before that date.

407. The Respondents did not, however, identify, either during the course of performing risk assessment procedures or through any other audit procedures, the risk to GCUK's business associated with insurance provision being withdrawn or granted only on less favourable terms. Neither did they identify any of the events identified above that meant that this risk was heightened.

408. The audit work that touched on aspects of GCUK insurance coverage was carried out in respect of verifying insurance costs and the existence of insurance coverage for particular receivables, as part of the testing of ECL provisioning. Other than two brief references on two working papers relating to audit work carried out on the ECL provision, suggesting that a verbal assurance may have been given that the Insurer B Policy was renewed in March 2020 for a further 12 months, there is no evidence of any consideration being given at the time of the risks associated with insurance renewal and there is no suggestion that the Respondents sought to verify or test any information that they recorded as being provided by GCUK.

409. At the very least, the Respondents should have requested and reviewed copies of the current policies, showing the relevant renewal dates, before the FY2019 Audit was concluded. However, they did not do this and, therefore, did not have even a basic understanding of the renewal position or the resulting risks to which GCUK was exposed.

410. Specifically:

410.1 the Audit File did not include a copy of any renewed Insurer B Policy for 2020 or a copy of any renewed Standalone Policy for the period post March 2020; and

410.2 whilst the policies for the previous periods were sent to the Respondents attached to an internal GCUK email dated 29 January 2020, no renewed policies were attached to this email, and they were neither requested by, nor provided to, the Respondents subsequently.

Failings in respect of the ongoing appetite and/or ability of WCF investors to fund GCUK's receivables

411. As of 31 December 2019, a significant concentration of GCUK's receivables were held by the Investment Bank (44.5%) and Greensill Bank (17.2%). In addition, the Asset Management Company held 2.4% and GCUK self-funded 0.9%. The identity of the investors that funded the remaining 34.8% was unclear (from the ECL working paper J227) and the Respondents obtained no evidence as to who the investors were in respect of these receivables.

412. There were a number of potential reasons why the provision of investment funding to GCUK might have reduced, or ceased, creating a business risk for GCUK, including:

412.1 If continuity of trade-credit insurance was not ensured, it would render sub-investment grade IPUs unmarketable;

412.2 The Investment Bank and the Asset Management Company (and possibly other unidentified investors) were reliant on third parties investing in the funds they managed to create the liquidity required, in turn, to invest in GCUK receivables. In a changing economic climate, particularly in the context of the Covid-19 pandemic, there was increasing uncertainty as to any continuing business appetite on the part of investors and/or the ongoing financial ability of investors to continue investing; and

412.3 Continuing investment by Greensill Bank was likewise dependent on sufficient inflow of funds from depositors and subject to any regulatory restrictions relating to its investments imposed by its regulatory body.

413. The consequences of any significant reduction of appetite, financial ability or capacity on the part of any one of these investors would have a highly significant impact on GCUK's business.

414. This was a particularly significant risk for GCUK given the highly concentrated profile of its investors and this risk should have been identified and assessed as part of GCUK's assessment of going concern.

415. In their "Cash flow forecast review" dated 19 May 2020, the Respondents identified, as the second main assumption of the "*low*" scenario forecast produced by GCUK, that "*funding capacity is limited to existing clients only - $29bn ($19bn GCUK & $10bn* [a wholly owned subsidiary])". The Respondents therefore assumed that there would be no reduction in funding capacity from existing investors. GCUK's justification for this was:

415.1 That additional funding was likely to be made through a UK Government (Covid-19 related) scheme they had applied for totalling c£3 billion; and

415.2 The Investment Bank and the Asset Management Company had German Government guaranteed insurance (again Covid-19 related) for the assets to which it was exposed, which made GCUK an attractive investment.

416. After reviewing that assumption, the Respondents accepted the justifications put forward by GCUK and that:

> *"Considering the strong performance of the company there is no indication that the funding capacity would be deceased [sic]."*

417. The Respondents' review did not, however, give any real consideration to the continuing appetite and ability of the primary investors to continue acquiring receivables from GCUK, either at all or at a rate sufficient to support the volumes of WCF business forecast by GCUK and no audit procedures or investigations were carried out to assess this.

418. Instead, the Respondents accepted the views of GCUK, as said to be expressed in a single phone call with a member of the GCUK management team, recorded on the "Cashflow forecast review", without giving the issue any independent consideration.

419. This was despite the fact that:

419.1 A reduction in funding was self-evidently a highly material risk to the ongoing operations of GCUK.

419.2 As Greensill Bank was part of the Greensill Group, information on its appetite and capacity should have been readily available from GCUK's parent company and/or the Group Auditor.

419.3 The assurances provided by GCUK did not justify the assumptions made or evaluate the likelihood of the alternative position. Specifically:

a. The UK government scheme referred to (the Covid Large Business Interruption Loan Scheme ("**CLBILS**") introduced during the Covid-19 pandemic that GCUK applied to join in April 2020) could not have provided any reassurance that future funding would support the forecast revenue. First, the aspect of the scheme that GCUK applied for did not provide funds, it merely provided a guarantee in the event of default by the borrower (being more akin to potential additional insurance capacity for GCUK's SCF business). Secondly, the application had not yet been successful, which should have led the Respondents to discount it as a factor that could properly be used to support GCUK's assessment that GCUK was a going concern.

b. There was no verification of the availability of any German Government guarantees to GCUK's insurers, nor any analysis as to what extent they would apply to GCUK's WCF trades, including what proportion of GCUK's insured receivables were insured under an insurance policy issued in Germany. This was simply an assertion from GCUK which the Respondents appear to have accepted without independent consideration or review.

c. The Respondents might have interpreted these factors as having given them comfort that there would be an increasing capacity in the market as it would encourage new investors, rather than as giving them comfort that the government schemes would translate directly into additional funding. However, this was unquantified speculation and could not provide any comfort that funding capacity would not decrease.

419.4 A presentation prepared by GCUK titled "Financials" (dated 21 April 2020, just over a month before the completion of the Audit) and provided to the Respondents, made explicit reference to the cash position being worse than predicted in part because of redemptions in the Investment Bank's H Fund – meaning that investors were withdrawing from the fund.

419.5 In March 2020, the Investment Bank had issued a notice titled "Information to shareholders of the [H Fund]" stating that: "[d]*ue to increased supply of Notes and the decreased fund size due to redemptions, the Subfund has capacity to accept new subscriptions*".

419.6 The media review carried out by the Respondents during the audit planning identified that the Asset Management Company had taken disciplinary action in relation to an investment manager who had invested significant amounts in GCUK receivables, which in turn led to investors withdrawing funds from the Asset Management Greensill Fund in June 2019.

420. Overall, the Respondents did not evaluate the likelihood of a reduction in future funding and extent to which any reduction should be considered a realistic outcome. Therefore, they did not assess whether GCUK's going concern assessment dealt adequately with the risk of funding reducing. They did not, for example, review minutes of meetings, relevant agreements and correspondence with existing and prospective funders, nor any contingency plans which may have been in place to deal with a withdrawal of or reduction in WCF funding.

<u>Summary of breaches</u>

421. The Respondents failed:

421.1 When performing risk assessment procedures required by ISA 315, to consider whether:

a. The risk of non-renewal of trade credit insurance; and

b. A potential decrease in investment in GCUK's receivables: could cast significant doubt on GCUK's ability to continue as a going concern;

421.2 To evaluate properly GCUK's assessment of its ability to continue as a going concern, specifically the unsupported assumptions that:

a. GCUK's trade credit insurance arrangements would continue; and

b. Investors would continue to invest in GCUK's receivables at the same rate as (or higher than) previously;

421.3 To remain alert throughout the Audit for evidence of events or conditions that may have cast significant doubt on the entity's ability to continue as a going concern, specifically those that indicated that:

a. GCUK's existing trade credit insurance may not have continued; and

b. Investors' appetite and/or ability or capacity to continue investing may decrease.

422. Consequently, the Respondents breached ISA 570.10, ISA 570.11 and ISA 570.12.

423. In addition, the Respondents failed to consider properly whether GCUK's assessment included all relevant information of which the auditor was aware as a result of the audit, as outlined above, including by way of example:

423.1 the change of ownership for Insurer A;

423.2 the dismissal of an investment manager from within the Asset Management Company that invested in GCUK's receivables; and

423.3 redemptions in funds managed by the Investment Bank that invested in GCUK's receivables, contrary to ISA 570.14.

ADVERSE FINDING 19: The failure to assess properly the availability of financing and therefore to evaluate GCUK's going concern assessment

424. The requirements of ISA 570.12 are summarised in the section above.

425. Sensitivity testing and scenario analysis are mechanisms used to assess the risks facing a business and the potential impacts if those risks were to materialise, analysing the effect of changes to the assumptions incorporated in a financial model.

426. One of the central assumptions made by GCUK in its going concern assessment was the availability of sufficient third-party financing to enable it to have adequate cash resource throughout the period of the going concern assessment.

427. This assumption was built into the cashflow forecasts prepared by GCUK which were reviewed by the Respondents in the "Cashflow Forecast Review" working paper, dated 19 May 2020.

428. In that working paper, the Respondents considered the "*low*" case scenario in GCUK's forecast, which assumed revenue remained unchanged. The Respondents conducted a sensitivity analysis looking at the impact of a 25% and 50% reduction in revenues. The 50% scenario also incorporated a reduction in credit loss figures, on the assumption that if revenue decreased then credit losses would reduce at a similar rate.

429. The Respondents' conclusion was that the "*sensitivity analysis has illustrated that the company will remain liquid even in the event that revenue decreases even further than the low forecast predicts*".

430. The forecast liquidity in the "*low*" case forecasts included $200 million from July 2020, from an anticipated new bank facility of $400 million (the "**Bank Facility**") (yet to be confirmed), and what was described as $150 million of "*GCUK Notes*" on the balance sheet. In addition, a potential $100 million financing facility (the "**Greensill Trust Loan**") to be provided by the Greensill Family Trust (the "**Trust**") was referred to in the "Cashflow Forecasts Review" working paper but was not relied upon by GCUK in the forecasts themselves.

431. The audit work on the "*low*" case scenario, showed that GCUK would only remain liquid if it relied on one of the Bank Facility, the GCUK Notes or the Greensill Trust Loan. Meanwhile the sensitised analysis showed that it would need to rely on a combination of more than one of these three options (but not all three).

432. In its initial forecasts GCUK relied on the Bank Facility and the GCUK Notes in combination. However, the Respondents concluded that as the granting of the Bank Facility depended on a guarantee being provided by a third party, it should not be taken into account in the forecast analysis. Therefore, the Respondents based their analysis on the availability of the GCUK Notes and the Greensill Trust Loan.

433. The Respondents' work on the forecasts indicated therefore that GCUK's liquidity was heavily reliant on generation of cash resources from:

433.1 in the "*low*" case, one of the GCUK Notes and the Greensill Trust Loan; and

433.2 in the sensitised scenarios, both of the GCUK Notes and the Greensill Trust Loan.

434. However, the Respondents failed to evaluate whether it was in fact appropriate to rely on the GCUK Notes or the Greensill Trust Loan.

435. In terms of the GCUK Notes:

435.1 It was explained in a note from a member of the audit team on the "Cashflow Forecast Review" working paper that the $150 million GCUK notes were:

"standard notes issued to investors, but because of minor trading delays may be temporarily held on GCUK's balance sheet (usually for 1 – 2 days max). They are effectively an additional source of liquidity to GCUK as they can be quickly converted into cash.

We hold them at $150m because this is our average usage of the GCUK balance sheet".

436. They were forecast to remain at the same level throughout the working capital forecasts.

437. The GCUK Notes were understood to represent an amount that was tied up as part of the normal working capital cycle of the business. The balance held in GCUK Notes would have fluctuated daily. It is understood that although amounts would be realised daily from the GCUK Notes, resulting in cash paid into GCUK's bank account, similar amounts would also be paid from the bank account creating new Notes. As part of the daily cash flow cycle arising from business activities, GCUK would always have an amount tied up in the GCUK Notes. The GCUK Notes were therefore not an additional source of funds, rather they were amounts that needed to be permanently financed out of GCUK free cash resources. GCUK's forecast model shows that the actual amounts held in loan notes fluctuated between $63 million and $170 million at the end of the months of January to March 2020 and that GCUK forecast thereafter that there would always be $150 million of its available cash resources tied up in the GCUK Notes.

438. However, there is, no evidence that:

438.1 The Respondents asked any questions of GCUK as to the extent to which it was appropriate to rely on the $150 million GCUK notes; or

438.2 Any consideration was given as to whether, as the GCUK Notes were stated to be on the balance sheet for "*1-2 days*", this caused any intra-month cashflow issues during the going concern period i.e. whether GCUK may run out of cash temporarily.

439. So far as the $100 million Greensill Trust Loan was concerned:

439.1 In the working paper titled "Going Concern – main work programme and findings", dated 22 May 2020, it was noted that: "*the Client has $100m notes that it can call upon from the […] Greensill Trust as detailed on CV60-1. We have reviewed the […] Greensill Trust and confirmed it has adequate resources to provide a $100m [sic] as and when required*".

439.2 It would appear from the underlying documents that this is a reference to a revolving facility agreement that was entered into between GCUK and the Trust, approved by the GCUK Board in May 2020.

439.3 No explanation was provided as to why the Respondents considered it appropriate to rely on this loan facility, when GCUK had not factored it into its forecasts.

440. The work undertaken by the Respondents to review this facility was summarised in the Cashflow Forecast Review as being: *"We have obtained signed confirmation from […] Greensill. See CV60-1. In addition, we have had a conference call with the accountants of the trust who have confirmed there are sufficient resources to cover the $100m as and when required*".

441. For context, it is noted here that prior to becoming the *Statutory Audit Firm* for GCUK, Saffery had a pre-existing relationship with the Greensill Family Trust. As a result of this, other individuals within Saffery but outside of the audit team may have had knowledge of the Trust's liquidity as well as, potentially, the discretion available to the Trustees to make investment decisions. However, whether or not the audit team were made aware of these matters (there being no record on the Audit File of this being the case) any assurance that could have been forthcoming from elsewhere within Saffery was insufficient for the purposes of the Audit.

442. In the scenario where the Respondents placed reliance on the availability of the Greensill Family Trust to justify reporting on a going concern basis for GCUK, in circumstances where GCUK ultimately did not place reliance on it, it was incumbent upon the audit team to evaluate properly whether the funds could be relied upon.

443. However[8]:

443.1 The Greensill Family Trust accounts that were reviewed by the Respondents (requested and received only six days before the FY2019 Financial Statements were approved) were for the year ended 30 June 2019[9] and therefore out of date;

443.2 Whilst the Respondents had conversations with accountants connected to the Trust, they did not obtain any updated financial documentation, such as management accounts or recent bank statements which could have shown a more up to date position; and

[8] Executive Counsel has made no finding as to whether the trust had sufficient resources to provide the $100m facility, and no conclusion on this should therefore be drawn from the matters set out below.

[9] These being the trust's most recent annual accounts, its financial year ending on 30 June.

443.3 There was no review of the underlying trust documentation, or direct conversations with the Trustees, to assess whether the Trust was legally able to release funds for the purpose of financing GCUK, i.e. whether doing so would be in line with its obligations to the Trust beneficiaries, particularly if the expectation was for the loan to be only a backup "*last resort*" for GCUK and so, on that assumption, GCUK would have failed to find financing elsewhere and careful thought would be needed as to whether the loan would be in the interests of the beneficiaries.

444. Considering the uncertainty around relying on the GCUK Notes as liquidity, in reality even in the "*low*" case the Respondents were relying on the Greensill Trust Loan to support GCUK's assessment that it was a going concern. The central importance of the Greensill Trust Loan to the appropriate going concern confirmation in the FY2019 Financial Statements and the need for more audit evidence was noted by the Technical and Compliance Director who was asked by Mr Di Leto to carry out a "*technical review*" of the going concern analysis, on 6 May 2020.

445. The Respondents subsequently obtained a signed copy of the Greensill Trust Loan facility agreement but did not then go back to the Technical and Compliance Director to make sure that this was all that they considered necessary in terms of sufficient appropriate audit evidence that GCUK was "*appropriately covered*" under the worst-case scenario (see further below).

446. More generally, the Respondents did not consider whether in the sensitised scenario, a 50% reduction of revenue was in fact a worst-case scenario, or whether a greater potential reduction should have been considered. Particularly in light of the fact that no consideration was given as to the factors that could generate either a 25% and 50% reduction in revenue or the likelihood of those factors arising (see above in respect of investor financing and below in respect of other factors relevant to the revenue forecasts). If there was the potential for a worst-case scenario, proper consideration would need to be given as to whether additional financing, from sources other than those referred to in the forecasts, would be needed for GCUK to continue as a going concern.

447. The Respondents accordingly failed to evaluate properly GCUK's assessment of its ability to continue as a going concern, specifically its ability to secure sufficient financing beyond May 2020, contrary to ISA 570.12.

ADVERSE FINDING 20: The failure to assess properly the assumptions relied on in the cashflow forecasts and therefore to evaluate GCUK's going concern assessment and consider whether it included all relevant information

448. The requirements of ISA 570.12 and ISA 570.14 are summarised in the section above.

449. The most substantial examples of the failure to assess the assumptions on which the forecasts were based were as follows.

<u>Movements in current assets and liabilities</u>

450. GCUK had material levels of current assets (total $408 million excluding cash), including the $150 million GCUK Notes, and liabilities ($454 million, including $219 million of intra group debt) on its balance sheet as of 31 December 2019.

451. Some movement in these assets and liabilities was likely to arise across the forecast period and reasonable assumptions in relation to these movements needed to be factored into the forecasts.

452. The Respondents compared the opening bank balance reflected in GCUK's forecasts with bank statements (on the "Cashflow Forecast Review" working paper). They did not, however, consider how the opening net current asset position at that date and any unwinding of that position and future movements might impact on liquidity over the forecast period. The approach taken by the Respondents was merely to comment on movements reflected in the forecasts, rather than to consider whether the forecast movements were complete.

453. The issue of working capital movements was also raised by the Technical and Compliance Director, with the suggestion that they consider working capital movements again once their questions had been answered by the audit team. However, despite the concern raised, the issue was never sent back to the Technical and Compliance Director for final review and approval.

Capital expenditure and investments

454. The Respondents' comments on this topic were likewise contained in the "Cashflow Forecast Review" working paper. They were limited to explaining what the items of capital expenditure and investment are, including capital expenditure on "*Project Verdi*".

455. There was no assessment of whether the forecast cash outflows on these items were adequate.

Revenue forecasts

456. There were a number of determiners of revenue underpinning the forecasts which needed to be considered, one of which was whether the revenue stream arising from large, apparently "*one-off*", items involving significant loan arrangement and facility fees (which represented $202.6 million of the gross profit in the FY2019 Financial Statements) might change.

457. However, the only work carried out by the Respondents, as recorded in the "Cashflow Forecast Review" and the "Going Concern Review – main work programme & findings" working papers, was to compare revenue assumptions to the revenues budgeted.

458. The Respondents did not perform any detailed audit work to assess the extent to which forecast revenue might be expected to fall in the circumstances then pertaining. There were a number of potential reasons why revenue may fall (other than those set out above in respect of the appetite and ability of investors to invest in GCUK receivables). For example, if GCUK's customer base of Obligors and/or Suppliers, or the need of such customers for WCF, was to reduce (taking into account the effects of the Covid-19 pandemic such as businesses becoming insolvent or business models changing).

459. The Respondents should have carried out a more detailed and challenging evaluation of GCUK's forecasts.

Summary of breaches

460. The Respondents accordingly failed to:

    460.1 evaluate properly GCUK's assessment of its ability to continue as a going concern, through a proper evaluation of the assumptions on which GCUK's cashflow forecasts were based; and

460.2 consider properly whether GCUK's assessment included all relevant information of which the auditor was aware as a result of the audit, as outlined above.

461. Therefore, the Respondents breached ISA 570.12 and ISA 570.14.

SECTION 6: REVIEW OF AUDIT EVIDENCE AND QUALITY CONTROL

A. Introduction

462. The requirements relating to evaluating the sufficiency of audit evidence prior to the conclusion of the Audit serve a purpose of providing a further, important opportunity for an auditor to identify and respond to any failure to obtain sufficient audit evidence during the course of the Audit before an audit opinion is issued.

463. Meanwhile, the purpose of the quality control requirements applicable to engagement partners is to ensure that the Audit both complies with professional standards and applicable legal and regulatory requirements and the auditor's report issued is appropriate in the circumstances. The standards emphasise that quality is essential in performing audit engagements.

B. Relevant Background

464. No review memos were completed for the Audit by either Mr Di Leto or other members of the audit team, either prior to the issuing of the Audit Closing Report (on 17 April 2020) or subsequently, prior to the audit opinion being issued.

465. The Respondents' review of the Audit work undertaken was exclusively recorded through tick marks against audit documents and checklists within the CCH and by way of some brief review notes within CCH.

466. The Respondents recorded conclusions within CCH as to whether their audit procedures had, in the Respondents' view, reduced the risk of material misstatement to an acceptably low level by way of:

466.1 In the case of five of the Significant Risks, the entry '*Testing Satisfactory'*; and

466.2 In the case of the Significant Risk relating to management override, the entry: *"*[b]*ased on the audit testing performed, we can conclude that the risk has been mitigated via our review and testing performed. No management override identified*".

467. No reference was made to any individual audit procedures performed or audit evidence obtained from work carried out that could have led the Respondents to these conclusions.

468. Meanwhile, Mr Di Leto, as the Responsible Individual, elected to only consult on one aspect of the Audit, namely the assessment of GCUK's cashflow forecasts. As set out previously, a request for an internal 'technical' review of the audit team's work on this area was made by Mr Di Leto on 6 May 2020.

C. Adverse Findings

469. The adverse findings set out below address failings to:

469.1 review and evaluate properly whether sufficient appropriate audit evidence had been obtained; and

469.2 ensure that appropriate consultations took place.

ADVERSE FINDING 21: The failure to review and evaluate properly whether sufficient appropriate audit evidence had been obtained

470. The Respondents were required, under ISA 330.26, prior to signing the audit opinion, to conclude whether sufficient appropriate audit evidence had been obtained.

471. Where insufficient audit evidence had been obtained in relation to any areas of the Audit, but in particular those involving significant risks of material misstatement, then further audit procedures were required to obtain additional evidence. If none could be obtained, then the obligation was on the Respondents to either provide a qualified audit opinion or to disclaim an opinion as per ISA 330.27. Under ISA 330.7(b) the Respondents needed to obtain more persuasive evidence, the higher their assessment of risk in relation to a particular audit area.

472. Both revenue recognition and completeness and the valuation and recoverability of assets had been identified as significant risks that could lead to material misstatement. Further, there was an obvious need to carefully consider whether there were any significant doubts as to GCUK's ability to continue as a going concern.

473. The lack of clear explanation in the relevant working papers as to how, in some cases very significant, judgements and conclusions were reached on these areas meant that no proper review could be carried out simply by reviewing the working papers themselves.

474. However, there was very little evidence available on the Audit File, or in any other document prepared at the time or for the purpose of the Audit, as to what (if any) review and/or critical assessment of the audit evidence obtained was carried out by members of the audit team, including Mr Di Leto, or any other individuals within Saffery.

475. The two checklists designed to record the Respondents' review of the audit evidence obtained were titled the "Audit Completion Checklist" and the "Responsible Individual Checklist". This latter checklist was completed by Mr Di Leto on 19 July 2020, two months after the audit opinion had been issued.

476. Each of the checklists were completed with the answers either "*Yes*", "*Done*", "*N/A*" or "*Excl*" (also to apparently represent "not applicable"). Neither of the checklists indicated that there were any concerns remaining at the conclusion of the Audit as to the level of audit evidence obtained. It was not recorded in the "Responsible Individual Checklist", or in any other document prepared at the time or for the purpose of the Audit, how Mr Di Leto had satisfied himself at the time of signing off the Audit that all of the items that he was, on 19 July 2020, reviewing and checking off, had in fact been completed satisfactorily.

477. The entries as recorded provided no explanation as to whether either the audit team or Mr Di Leto considered that the audit response to any of the Significant Risks had been adequate and made no reference to the possibility that the audit team should have consulted with others with appropriate knowledge, seniority or experience on any specific difficult or contentious matters.

478. In addition, there were recorded, within the "notes" function of CCH, six review notes that were raised by members of the audit team during the course of the Audit. Five of these related to planning and risk assessment matters and one to GCUK's payroll operations. Each of these notes were subsequently "*cleared*" by Mr Di Leto, on 20 July 2020, with brief responses and the comment, "[T]*he review note has been answered to my satisfaction*".

479. In any event, in light of the extensive failings identified in respect of the audit work across the sections of the Audit addressed in sections 1 - 6 above, and the consequential lack of audit evidence and documentation that those failings gave rise to, had the Respondents conducted an adequate review of the audit evidence obtained it should have been obvious that the evidence obtained was insufficient to enable them to properly reach conclusions on which an audit opinion could be based.

480. The Respondents accordingly failed to review and evaluate properly whether sufficient appropriate Audit evidence had been obtained and accordingly failed either to obtain additional audit evidence or, if no such audit evidence could be obtained, to express either a qualified or a disclaimed opinion, in breach of ISA 330.26 and ISA 330.27.

ADVERSE FINDING 22: The failure to ensure that appropriate consultations took place on difficult or contentious matters and, in respect of ECL, to consider whether specialised skills and knowledge were required

481. The Respondents, and specifically Mr Di Leto as the engagement partner, were required to ensure that the audit team engaged in appropriate consultation on difficult or contentious matters under ISA 220.18.

482. In addition, the Respondents were required, in the context of the audit work required in relation to GCUK's ECL provision, to consider whether specialised skills or knowledge in relation to one or more aspects of the accounting estimates were required in order to obtain sufficient appropriate audit evidence under ISA 540.14.

483. It should have been apparent to the Respondents that the Audit involved highly technical and complicated accounting judgements. As a result, the audit team needed to consider whether to consult someone else (whether within the firm or externally) with particular knowledge and expertise on the issues arising from GCUK's accounting policies and its dependence on trade credit insurance.

484. The potential need for consultation should have been apparent from the outset of the Audit, on the basis that the Respondents should have understood the complexities involved as a result of previous years' audits.

485. At the least, consideration should have been given to consulting with (either internal or external) experts in respect of:

    485.1 GCUK's selection and application of accounting policies, upon receipt of the email from the Group Auditor regarding the Greensill Group's decision to change its accounting policies in 2020; and

    485.2 the risks associated with GCUK's reliance on trade credit insurance, specifically in light of the information available to the Respondents as to matters that heightened the risk that insurance would not be renewed.

486. In addition, having concluded that consultation was required in respect of the audit work completed on GCUK's cash flow forecasts, Mr Di Leto did not ensure that the Technical and Compliance Director agreed the conclusions reached in response to the concerns they had raised, prior to finalising the Audit.

487. Mr Di Leto's request for a 'technical review' was sent to the Technical and Compliance Director on 6 May 2020 with the comment that there was currently "*no material uncertainty on going concern status based on the forecasts provided*" (albeit that the audit team had only just been provided with the underlying workings for those forecasts and so the audit work was still in progress).

488. The Technical and Compliance Director forwarded the request to a Risk and Compliance Partner within Saffery. The Technical and Compliance Director commented that: "*I suspect that this arises due to the coronavirus guidance that where there is judgemental uncertainty they get a second review. This client is tricky – IFRS 9 (full expected credit loss model) but it is only a GC review* […]."

489. The comments of the Technical and Compliance Director were recorded in the working paper "Technical department queries and answers" as follows:

> *"6. In the low case they need the $150m loan from […] Greensill to cover them until they receive a revolving facility of $400m. There is indication from the bank that negotiations are happening but nothing is formally agreed. If they don't get the $400m loan would the $150m be sufficient to get them through the GC period? Why are they asking for $400m if they only need $150m?*
>
> *7. I think that we need something confirming this working capital facility from […] Greensill to ensure that they are appropriately covered under the worst case scenario even if they never actually need it. Their own documentation highlights this need for the facility. They don't need this under the other scenarios. Depending upon what you get we need to consider the Audit report wording. I think probably nothing if they get confirmation but poss mat uncertainty if they don't".*[10]

490. The Respondents subsequently obtained a signed copy of the Greensill Trust Loan facility agreement but did not then go back to the Technical and Compliance Director to make sure that this was all that they considered necessary in terms of sufficient appropriate audit evidence that GCUK was "*appropriately covered*" under the worst-case scenario. Neither did the audit team discuss the Technical and Compliance Director's questions as to the £400 million bank facility, albeit they ultimately did not include that in their sensitivity analysis.

491. Finally, as noted above, the issue of working capital movements was raised by the Technical and Compliance Director, with the suggestion that they would consider working capital movements again once their questions had been answered by the audit team. However, the issue was never sent back to the Technical and Compliance Director for final review and approval.

492. The Respondents accordingly failed to ensure that appropriate consultations took place on difficult or contentious matters, in breach of ISA 220.18.

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[10] Whilst the senior member of the Technical and Compliance team wrongly referred to the Greensill Trust Loan as being $150 million, it was in fact a facility for $100 million as explained above.

493. Finally, in respect of GCUK's ECL provision, in light of the fact that GCUK operated very much like a credit or financing institution (whether or not it actually was one) and that the accounting policies to be applied were very similar to those applied by financing institutions, including banks, it would have been appropriate to consider consulting others with specific expertise in auditing credit institutions and/or banks. The Respondents, however, failed to consider properly whether specialised skills or knowledge were required in relation to one or more aspects of the ECL provision in order to obtain sufficient appropriate audit evidence, in breach of ISA 540.14.

SECTION 7: PROFESSIONAL SCEPTICISM

A. Introduction

494. It is fundamental that every audit is conducted with appropriate professional scepticism.

495. Under ISA 200.15, the Respondents were required to plan and perform the Audit with appropriate professional scepticism.

496. This involves an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence in light of the circumstances (ISA 200.13(l)). It is integral to the audit process that auditors do not simply accept at face value what they are told by the entities they are auditing but that they question and investigate what they are told in order to obtain sufficient appropriate audit evidence of potential material misstatement.

497. This obligation is repeated at a number of points in the ISAs, including at:

    497.1 ISA 240.12 – which required the Respondents to perform the audit with appropriate professional scepticism in evaluating the risk of fraud;

    497.2 ISA 540.21D-1 – which required the Respondents to act with appropriate professional scepticism when reviewing management estimates relating to impairment of assets and provisions for the purposes of the ECL provision; and

    497.3 ISA 570.12D-1 – which required the Respondents to act with appropriate professional scepticism when reviewing future cash flow relevant to GCUK's ability to continue as a going concern.

498. The obligation to act with appropriate levels of professional scepticism applies notwithstanding the auditor's past experience of the honesty and integrity of the entity's management and of those charged with governance (ISA 200.15 and ISA 240.12).

499. The Respondents, however, repeatedly failed to exercise adequate levels of professional scepticism. It is a recurring theme of the Adverse Findings as set out in this *Final Settlement Decision Notice* that the Respondents adopted a superficial approach across the whole audit process, failing to engage diligently with the complexities of either the business itself or the particular risks raised by its operations, and failing to challenge in any substantial way the information with which they were provided by GCUK, all of which evidenced an overall failure to adopt appropriate levels of professional scepticism.

500. This overarching lack of professional scepticism across the audit areas addressed in this *Final Settlement Decision Notice* accordingly underpinned the specific audit failings identified in section 1 – 5 above.

B. Adverse Finding

ADVERSE FINDING 23: Failure to exercise appropriate professional scepticism

501. This adverse finding addresses failings to exercise appropriate professional scepticism during the Audit in the context of the:

    501.1 failure adequately to perform planning and risk assessment procedures (section 1);

    501.2 failure adequately to perform audit procedures in respect of GCUK's selection and application of accounting policies (section 2);

    501.3 failure adequately to perform audit procedures relating to revenue (section 3);

    501.4 failure adequately to perform audit procedures in respect of the ECL provision (section 4); and

    501.5 failure adequately to perform audit procedures relating to going concern (section 5).

Planning and risk assessment procedures

502. The relevant background to the audit work carried out in relation to planning and risk assessment is set out in section 1.

503. The Respondents repeatedly failed to exercise adequate levels of professional scepticism in relation to planning and risk assessment, relying predominantly on information provided by GCUK without critically assessing the reliability of that information. This resulted in a generally inadequate risk assessment process which was clearly unable to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels.

504. This included the Respondents:

    504.1 Failing to question or critically assess GCUK's own description of its business properly, accepting the information provided by GCUK as to its business operations without adequate independent analysis;

    504.2 Failing to question or critically assess properly whether information obtained in previous audits remained relevant to the FY2019 Audit;

    504.3 Failing to be alert to conditions which may indicate possible misstatement and critically assess the potential risks of material misstatement specific to GCUK's business operation, including the areas of GCUK's business that were susceptible to management override or fraud, including the ECL provision (a significant accounting estimate subject to a risk of bias); and

    504.4 Failing to question or critically assess assertions as to the efficacy of GCUK's internal controls, in the face of gaps in the control environment and weaknesses that were left unaddressed. Specifically, no attempt was made to address:

        a. The fact that (as explained above) the Respondents had identified no effective controls for four of the six Significant Risks identified, including the risks in respect of revenue recognition and completeness and valuation and recoverability of assets (including the related risks of fraud);

b. The specific weakness in internal controls noted on the "System Notes" working paper that senior members of staff had the ability to raise and approve their own journals; and

c. The number of failures in systems and processes identified in the Audit Closing Report and the acknowledgment in the Audit Closing Report that "*formal documentation for procedures and controls was not readily available*", such that it was recommended that a formal procedures manual be produced for new members of staff.

504.5 Rather, the Respondents made a number of inconsistent comments that suggested that GCUK had effective internal controls in a number of respects, which they should not have made in circumstances where they had not properly understood, and had made no attempt to test, any such controls.

505. These were all matters that an auditor operating with sufficient levels of professional scepticism should have addressed as part of their audit work. Consequently, the Respondents failure to appropriately question or critically assess these matters was a breach of ISA 200.15.

Accounting Policies

506. The Respondents failed to exercise adequate levels of professional scepticism in relation to the audit work carried out on GCUK's accounting policies and predominantly relied instead on information provided by GCUK. The Respondents failed critically to assess the selection and application of accounting policies proposed by GCUK and failed to carry out any independent evaluation as to their appropriateness.

507. Specifically, the Respondents failed to:

507.1 assess critically for themselves whether the criteria in IFRS 9 (as to derecognition of assets and liabilities) and within IFRS 15 (as to when revenue was recognised) were met for different categories of WCF;

507.2 assess critically the risk of management bias in the selection of accounting policies which maximised revenue recognition and minimised liabilities appearing on GCUK's balance sheet; and

507.3 question appropriately both the position taken by GCUK and the extent to which their own audit processes had been sufficient in evaluating the accounting policies, in response to the contradictory audit evidence obtained after being informed of the proposed change to accounting policies at the Group level.

508. Consequently, the Respondents breached ISA 200.15.

Revenue

509. The Respondents failed to exercise adequate levels of professional scepticism in relation to the audit work carried out on GCUK's revenue and predominantly relied instead on information provided by GCUK without critically assessing for themselves the reliability of that information.

510. Specifically, the Respondents failed to:

510.1 carry out any independent critical assessment of whether the population of revenue provided by GCUK from which the audit procedures were to be carried out was either complete or accurate;

510.2 carry out any independent critical assessment of whether the revenue was recognised in the correct financial period by simply accepting that the information GCUK provided was accurate without any independent cut-off testing evaluation – even though there was a notable increase in revenue at the end of FY2019; and

510.3 investigate the high variability and negative returns arising from revenue transactions included in the sample of transactions tested, and to consider whether that carried any risk of management override or fraud.

511. Consequently, the Respondents breached ISA 200.15 and ISA 240.12.

ECL

512. The Respondents repeatedly failed to exercise adequate levels of professional scepticism in assessing the ECL provision and predominantly relied instead on information provided by GCUK without properly questioning or evaluating the reliability of that information. This resulted in an inadequate assessment of the risk of material misstatement arising in relation to GCUK's reporting of ECL.

513. This included the Respondents failing to:

513.1 in respect of the Venture Capital Fund Obligors, obtain adequate evidence that exposure at default had been correctly calculated by GCUK on the basis of the existence and value of security that GCUK asserted it held and instead simply accepting the information provided by GCUK to be accurate;

513.2 evaluate independently the subjective assertions and judgements made by GCUK in relation to:

a. The analysis of distressed debtors and the completeness of the identified distressed debts;

b. The Credit Structure Reduction Factor and

c. The Haircut, by simply accepting those subjective assertions as appropriate and accurate, despite the self-evident risk of management bias in making those accounting estimates; and

513.3 evaluate independently the methodology for calculating ECL adopted by GCUK, even where it became apparent from the proposed Credit Structure Reduction Factor and the Haircut that GCUK did not consider that methodology produced an appropriate level of ECL provision.

514. Consequently, the Respondents breached ISA 200.15 and ISA 540.21D-1.

Going Concern

515. The Respondents repeatedly failed to exercise adequate levels of professional scepticism in relation to GCUK's assessment of going concern and predominantly relied instead on information provided by GCUK without properly questioning or evaluating the reliability of that information. This resulted in an inadequate assessment of the risk of material misstatement arising in relation to GCUK's reporting of going concern.

516. The Respondents:

516.1 accepted what they were told by GCUK about the renewal of both the Standalone Policy and the Insurer B Policy without carrying out any independent assessment of the accuracy of that information;

516.2 failed to identify any risks surrounding either trade credit insurance renewal or the ongoing appetite or ability of GCUK's limited range of WCF investors to continue investing;

516.3 failed to challenge adequately the underlying assumptions as to revenue and financing relied on by GCUK in its base case forecasts and to assess the level of uncertainty that should have been built into the sensitivity analysis; and

516.4 failed to evaluate properly why it was appropriate for the purposes of the forecasts to rely on either the $100 million Greensill Trust Loan or the GCUK Notes and, in the former case, why it was appropriate for the Respondents to rely on the Greensill Trust Loan in assessing going concern when GCUK did not rely on that facility within the forecasts it provided to the Respondents.

517. If the Respondents had been acting with appropriate levels of professional scepticism, each of these issues would have given rise to further questions as to whether there were material uncertainties that may have cast significant doubt as to GCUK's ability to remain a going concern, including in relation to cash flow, with further audit work being required to obtain sufficient audit evidence.

518. Consequently, the Respondents breached ISA 200.15 and ISA 570.12-D.

VI Sanctions

519. 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:

519.1 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;

519.2 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 or the accountancy profession;

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

519.4 to deter *Statutory Auditors* and *Statutory Audit Firms* from breaching the *Relevant Requirements* relating to statutory audit.

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

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

<u>Nature, seriousness, gravity and duration of the breaches</u>

522. As a result of the breaches of *Relevant Requirements*, the FY2019 Audit failed in its principal objective, namely to obtain reasonable assurance about whether GCUK's FY19 Financial Statements as a whole were free from material misstatement.

523. The going concern assessment in particular is fundamental to *Statutory Audits*, and it is of the utmost importance that this area is audited in accordance with *Relevant Requirements*. Further, three areas in which there were breaches (accounting policies, revenue and ECL) were related to significant risks identified in respect of the FY2019 Audit, and the failings identified pervaded the audit from the planning stage through to its finalisation.

524. The ISAs engaged in this case are all important *Relevant Requirements*, designed to ensure the quality and effectiveness of an audit. There were a significant number of breaches of *Relevant Requirements* which were critical to the role and duties of an auditor and the conduct of a proper audit. For example, the breaches included failures to:

    524.1 maintain professional scepticism (ISA 200);

    524.2 ensure adequate quality control by the Engagement Partner and the EQCR (ISA 220);

    524.3 identify and respond appropriately to risks of material misstatement (ISA 240, ISA 315 and ISA 330);

    524.4 obtain sufficient appropriate audit evidence, including through sampling where appropriate (ISA 500 and ISA 530);

    524.5 properly evaluate accounting estimates and related disclosures (ISA 540);

    524.6 properly evaluate management's going concern assessment (ISA 570); and

    524.7 properly form an opinion on whether the financial statements were prepared, in all material respects, in accordance with the applicable financial reporting framework (ISA 700).

525. The breaches of *Relevant Requirements*:

    525.1 were serious, and numerous;

    525.2 were pervasive throughout the areas of the FY2019 Audit addressed in this *Final Settlement Decision Notice*;

    525.3 related to only one audit year;

    525.4 were not intentional or deliberate, reckless or dishonest; and

    525.5 did not involve financial gain, as the Respondents did not derive or intend to derive any profit or benefit from the breaches of the *Relevant Requirements* (beyond the audit fee chargeable for the FY2019 Audit).

526. At the point GCUK entered Administration it owed significant sums to investors. The collapse of GCUK left a large number of customers, who relied on its financing model to facilitate their business operations, in potential jeopardy. Notwithstanding the fact that the Respondents' audit work regarding the assessment of going concern breached *Relevant Requirements*, Executive Counsel does not suggest that such breaches caused the Administration of GCUK.

527. Overall, however, the Audit did not adequately reduce the risk of material misstatement in the FY2019 Financial Statements to an acceptably low level. It was deficient as it was unable to assess either the risks of material misstatement in respect of GCUK's assets and liabilities (involving an assessment of the applicable accounting policies and the accuracy of its ECL provision) and its revenue, or material uncertainties in respect of its ability to continue as a going concern.

528. For the reasons set out at paragraphs 526 to 527 above, in aggregate, the breaches:

    528.1 Could have harmed investor, market and public confidence in the truth and fairness of the financial statements published by *Statutory Auditors* or *Statutory Audit Firms*, noting that GCUK entered Administration only ten months after an unmodified audit opinion was issued in respect of the FY2019 Financial Statements.

    528.2 Had the potential to adversely affect a significant number of people in the United Kingdom (such as the public, investors or other market users).

    528.3 Undermine confidence in the standards of conduct in general of *Statutory Auditors* and *Statutory Audit Firms*, and/or in statutory audit.

529. The circumstances of the Respondents are also relevant to the determination of *Sanction*. In particular:

    529.1 Saffery is a 'top twenty' accountancy firm in the UK. Its audit fee income in FY2024 was £44.5 million. Saffery received an audit fee of £230,000 for the Audit. Mr Di Leto was considered to be a high performing audit partner at the time of the FY2019 Audit. As such Mr Di Leto was amongst the highest remunerated partners at the time of the Audit.

    529.2 Neither Saffery nor Mr Di Leto has any disciplinary history, with either the FRC or the ICAEW.

    529.3 Saffery have implemented a number of changes and improvements to their audit processes and procedures generally since the FY2019 Audit which seek to address a number of the failings (and related breaches) identified within this *Final Settlement Decision Notice,* albeit the effectiveness of those steps have not yet been assessed. The Order made as part of the Non-Financial Sanctions in this matter will seek to determine the effectiveness of changes and improvement to audit methodology to date, as well as the remedial steps already taken.

    529.4 Personally, Mr Di Leto has taken some remedial steps to seek to address the failings identified in this *Final Settlement Decision Notice*, albeit the effectiveness of these steps has not yet been assessed. The Order made as part of the Non-Financial Sanctions in this matter will seek to determine the effectiveness of the remedial steps already taken by Mr Di Leto.

    529.5 Mr Di Leto's senior role is also relevant to the gravity of the offence. He had accumulated over 25 years of audit experience, with over 18 years' experience as an audit partner at the time of the Audit. As noted above, at the time of the FY2019 Audit, Mr Di Leto held a number of "*significant management positions*" within both Saffery's UK and Irish businesses.

530. Finally, it is noted that both Respondents have accepted their responsibility for the breaches and therefore have been given credit for early admissions and settlement as set out below.

Identification of *Sanction*

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

532. In accordance with paragraph 47(c) and (d) of the Policy, Executive Counsel has taken into account the size, financial resources and financial strength of the Respondents and the effect of a financial sanction on Saffery's business and Mr Di Leto personally when assessing the amount of the financial sanctions to be imposed.

Saffery

533. A financial sanction of £750,000.

534. A published statement in the form of a Severe Reprimand.

535. A declaration that the FY2019 Audit report signed on behalf of Saffery did not satisfy the *Relevant Requirements*.

536. In addition, Executive Counsel requires Saffery to comply with the following Order designed to prevent recurrence of the breaches:

536.1 Saffery shall conduct a review of a sample of audit engagements signed off within the period 1 November 2025 to 31 May 2026 to seek to determine the effectiveness of changes and improvement to audit methodology to date, as well as remedial steps already taken. The sample, together with the full terms and scope of the review, are to be agreed with Executive Counsel and the Executive Director of Supervision within 12 weeks of the date of this *Final Settlement Decision Notice*. The review shall include, in respect of each selected audit engagement, critical evaluation of:

a. planning and risk assessment (including (i) the process of determining whether an Engagement Quality Reviewer ("**EQR**") should be appointed; (ii) understanding and evaluating internal controls; and (iii) use of Saffery's audit approach summary workpaper);

b. assessing the need to consult and/or engage others with specialised skills or knowledge;

c. audit of going concern;

d. application of professional scepticism; and

e. evidence of the Responsible Individual's review and assessment of the audit evidence obtained, including use of Saffery's audit summary memorandum.

536.2 Within a timeframe to be agreed, following completion of the review referred to at 536.1 above, Saffery shall:

a. provide Executive Counsel and the Executive Director of Supervision with a report summarising the findings of the review (in a format to be agreed) together with copies of the reviewers' reports; and

b. provide Executive Counsel and the Executive Director of Supervision with copies of the firm's prevailing policies and process in respect of:

i planning and risk assessment;

ii assessing the need to consult on difficult and contentious matters and/or whether specialised skills or knowledge are required to assess significant accounting estimates, for review;

iii sampling methodology; and

iv application of professional scepticism/challenge.

536.3 Within a timeframe, to be agreed following receipt of the FRC's comments on the report and those policies, Saffery shall implement any updates recommended by the FRC.

536.4 Saffery shall agree with Executive Counsel and the Executive Director of Supervision and introduce, as a mandatory part of the firm's audit training programme for 2027, a thematic 'lessons learned' training session drawn from the breaches identified in this case.

536.5 Saffery's Senior Audit Leadership Team sub-committee on Technical & Compliance matters (SALT T&R) shall add to its scope of work on-going monitoring and assessment of Responsible Individuals' portfolios (to include assessment and consideration of the balance of audit engagement work with firm-wide management roles and responsibilities).

Mr Di Leto

537. A financial sanction of £160,000.

538. A published statement in the form of a severe reprimand.

539. In addition, Executive Counsel requires Mr Di Leto to comply with the following Order designed to prevent recurrence of the breaches:

539.1 Saffery's SALT T&R sub-committee shall review Mr Di Leto's engagement portfolio to confirm that Mr Di Leto has the required time and expertise to lead the engagements where it is intended that he will undertake the role of Responsible Individual and sign an audit opinion in 2027. The output of this review shall be provided to Executive Counsel and the Executive Director of Supervision within 4 weeks of completion.

539.2 A sample of audit engagements where Mr Di Leto undertakes the role of Responsible Individual and signs an audit opinion in 2027 shall be subject to mandatory EQR review. The sample, together with the full terms and scope of the review, are to be agreed with Executive Counsel and the Executive Director of Supervision within 12 weeks of the date of this *Final Settlement Decision Notice*.

539.3 Details of any initial findings made by the EQR and a summary of how any such findings were resolved prior to the relevant Auditor's Report being signed shall be recorded by Mr Di Leto and be made available on demand during 2027 for inspection by Executive Counsel and the Executive Director of Supervision, should Executive Counsel or the Executive Director of Supervision require. Mr Di Leto shall inform Executive Counsel or the Executive Director of Supervision once the relevant audits have been completed. Any request for inspection of Mr Di Leto's completed record shall be made by Executive Counsel or the Executive Direction of Supervision within 12 weeks of receiving Mr Di Leto's notification.

539.4 A minimum number of audit engagements, to be agreed with Executive Counsel and the Executive Director of Supervision, where Mr Di Leto has undertaken the role of Responsible Individual shall be included in the review required by paragraph 536.1 above.

539.5 Mr Di Leto shall complete additional training and CPD requirements within 12 months of this *Final Settlement Decision Notice* – the details of which shall be agreed with Executive Counsel and the Executive Director of Supervision within 12 weeks of the date of this *Final Settlement Decision Notice*. Mr Di Leto shall provide Executive Counsel and the Executive Director of Supervision with evidence of attendance and completion of the agreed additional training and CPD by 24 October 2027.

Aggravating and mitigating factors

540. Executive Counsel has further considered whether any aggravating and mitigating factors that exist (to the extent that they have not already been taken into account in relation to the nature, seriousness, gravity and duration of the breaches) should result in adjustments to the level of *Sanctions* imposed and concluded as follows:

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

540.2 All relevant mitigating factors have already been considered, except the level of co-operation provided by the Respondents. Paragraph 69 of the Policy explains that, since *Statutory Auditors* and *Statutory Audit Firms* are required to co-operate with any investigation conducted under the AEP, only an exceptional level of cooperation will be regarded as a mitigating factor at the point of determining *Sanctions*. Executive Counsel does not consider the co-operation provided by the Respondents in this matter to have been exceptional and therefore no discount has been made to the financial sanctions to reflect exceptional co-operation.

Deterrence

541. 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

542. Having taken into account the admissions by the Respondents and the stage at which those admissions were made (prior to the conclusion of Stage (1) of the case in accordance with paragraph 84 of the Policy), Executive Counsel determined that a reduction of 22.5% as to the financial sanction is appropriate. The financial sanction against Saffery is therefore reduced to £581,250 and the financial sanction against Mr Di Leto is reduced to £124,000.

VII Costs

543. Executive Counsel requires that the Respondents pay her *Costs* of this matter, in the sum of £1,520,895.48. Such costs shall be paid no later than 28 days after the date of this *Final Settlement Decision Notice*.

Signed:

[Redacted.]

SIMON BROADHURST

DEPUTY EXECUTIVE COUNSEL

Date: 24 August 2026