

IN THE MATTER OF

THE EXECUTIVE COUNSEL OF THE FINANCIAL REPORTING COUNCIL

-and-

(1) BDO LLP

(2) GERAINT JONES

FINAL SETTLEMENT DECISION NOTICE

Pursuant to Rule 108 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 or entities other than the Respondents, and it would not be fair to treat any part of this document as constituting or evidencing findings against any other persons or entities since they are not parties to the proceedings.

1. INTRODUCTION

- 1.1. The Financial Reporting Council (the “**FRC**”) is the competent authority for *Statutory Audit* in the UK and operates the Audit Enforcement Procedure (the “**AEP**”), effective June 2023. The AEP sets out the rules and procedure for the investigation, prosecution and sanctioning of breaches of *Relevant Requirements*. References to the AEP in this *Final Settlement Decision Notice* are to the version dated June 2023 unless otherwise stated.
- 1.2. The AEP contains a number of defined terms and, for convenience, those defined terms are also used within this document. Where defined terms are used, they appear in italics.
- 1.3. This *Final Settlement Decision Notice* also uses the following definitions:

- 1.3.1. “**NMCN**” means NMCN PLC;
- 1.3.2. “**FY19**” means the financial year ended 31 December 2019;
- 1.3.3. the “**2019 Annual Report**” means the Annual Report and Accounts of NMCN for FY19;
- 1.3.4. the “**Financial Statements**” means the consolidated financial statements of NMCN for FY19;
- 1.3.5. the “**Audit**” means the *Statutory Audit* of the Financial Statements of NMCN for FY19;
- 1.3.6. the “**Audit Report**” means the independent auditor’s report on the Financial Statements of NMCN for FY19, signed on 22 April 2020;
- 1.3.7. the “**Audit Team**” means the members of BDO’s staff who performed work on the Audit;
- 1.3.8. the “**Respondents**” means:
 - 1.3.8.1. BDO LLP (“**BDO**”); and
 - 1.3.8.2. Mr Geraint Jones (“**Mr Jones**”), the Audit Engagement Partner. Mr Jones had previously been the Engagement Quality Control Review Partner. He was appointed Audit Engagement Partner on 19 March 2020 when, unexpectedly, the replacement of the original Audit Engagement Partner became necessary.
- 1.4. In accordance with Rule 102 of the AEP, Executive Counsel entered into settlement discussions with the Respondents.
- 1.5. A *Proposed Settlement Decision Notice* was issued by Executive Counsel on 15 December 2025 pursuant to Rule 103 of the AEP in relation to the conduct of the Respondents in respect of the Audit. The Respondents provided written agreement to the *Proposed Settlement Decision Notice*, pursuant to Rule 105 of the AEP, on 16 December 2025. The Convener subsequently appointed an Independent Reviewer, pursuant to Rule 106 of the AEP, to consider the *Proposed Settlement Decision Notice*.
- 1.6. On 2 January 2026, the Independent Reviewer approved the issuance of this *Final Settlement Decision Notice* pursuant to Rule 107(a) of the AEP.
- 1.7. In accordance with Rule 108 of the AEP this *Final Settlement Decision Notice* sets out:
 - 1.7.1. the breaches of *Relevant Requirements*, with reasons;
 - 1.7.2. the *Sanctions* imposed on the Respondents, with reasons;

- 1.7.3. the amount payable by the Respondents in respect of Executive Counsel's *Costs*.
- 1.8. This *Final Settlement Decision Notice* is divided into the following sections:
 - 1.8.1. Section 1: Introduction;
 - 1.8.2. Section 2: Executive Summary of the breaches of *Relevant Requirements*;
 - 1.8.3. Section 3: Background;
 - 1.8.4. Section 4: *Relevant Requirements* to which the breaches relate;
 - 1.8.5. Section 5: Details of the breaches of *Relevant Requirements*;
 - 1.8.6. Sections 6 and 7: *Sanctions*; and
 - 1.8.7. Section 8: *Costs*.

2. EXECUTIVE SUMMARY OF THE BREACHES OF *RELEVANT REQUIREMENTS*

- 2.1. NMCN operated as a construction and consultancy services group delivering major building and national infrastructure projects across the UK. At all material times, its shares were listed on the main market of the London Stock Exchange and accordingly the requirements for a *Statutory Audit* of public interest entities applied to it.
- 2.2. As a listed entity, NMCN was required to prepare its 2019 financial statements in accordance with International Financial Reporting Standards (“**IFRS**”) (also referred to as the “**accounting standards**”).
- 2.3. The *Statutory Audit Firm* for the FY19 Financial Statements of NMCN was BDO. In carrying out the Audit, the Respondents were required to act in accordance with the International Standards on Auditing (UK and Ireland) (“**ISA(s)**”). The provisions of the ISAs were all *Relevant Requirements* within the meaning of the AEP.
- 2.4. The Respondents accept that, in the circumstances set out in this *Final Settlement Decision Notice*, they breached *Relevant Requirements*. As is common in the construction industry, NMCN’s core business operated through long-term contracts. The breaches in large part concern the Respondents’ audit work in respect of NMCN’s long-term construction contracts. They relate to the following areas of the audit:
 - 2.4.1. Controls;
 - 2.4.2. Selection of contracts for testing;
 - 2.4.3. Variable income;
 - 2.4.4. Applications and payments on account;
 - 2.4.5. Costs to complete;
 - 2.4.6. Loss-making contracts;
 - 2.4.7. Contract assets, trade receivables, retentions;
 - 2.4.8. Going concern;
 - 2.4.9. The acquisition of a new subsidiary; and
 - 2.4.10. Non-recurring items.
- 2.5. This *Final Settlement Decision Notice* sets out the following *Sanctions* in respect of the Respondents:

BDO

- 2.5.1. a financial penalty of £2,000,000 adjusted for the mitigating factor of exceptional cooperation by a reduction of 5% and further discounted for admissions and early disposal by 30% so that the financial penalty payable is £1,330,000, to be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;
- 2.5.2. a published statement in the form of a severe reprimand; and
- 2.5.3. a declaration that the Audit Report signed on behalf of BDO did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*.

Mr Jones

- 2.5.4. a financial penalty of £75,000 adjusted for the mitigating factor of exceptional cooperation by a reduction of 5% and further discounted for admissions and early disposal by 30% so that the financial penalty payable is £49,875, to be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;
 - 2.5.5. a published statement in the form of a severe reprimand; and
 - 2.5.6. a declaration that the Audit report signed by Mr Jones did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*.
- 2.6. In determining that no further non-financial *Sanction* was required in respect of either of the Respondents, Executive Counsel took into account the circumstances set out in paragraph 6.13 below.

3. BACKGROUND

NMCN

- 3.1. NMCN was incorporated as North Midland Construction Company Limited in 1946 and was first listed on the London Stock Exchange in 1982. The company rebranded as NMCN in 2018. The group then comprised the parent company, NMCN PLC, its subsidiary NMCN Sustainable Solutions Limited (“**NMCN SS Ltd**”) and three other companies which were dormant. During FY19 (in early October 2019), the group acquired a contracting business operating in the water sector, which was formed of a UK limited company with its single, wholly-owned subsidiary trading company (together, the “**New Subsidiary**”).
- 3.2. The internal organisation of NMCN PLC is described differently across various documents. While the Annual Report for the group referred to two operating segments, Built Environment and Water, internal NMCN documents often treated NMCN PLC’s business as comprising four divisions: Construction, Highways, Telecommunications, and NMCNomenca.¹
- 3.3. The 2019 Annual Report was issued on 22 April 2020. NMCN reported revenue of £405 million and pre-tax profit of £7.5 million.
- 3.4. Following completion of the FY19 Audit, the length of BDO’s tenure as NMCN’s *Statutory Auditor* meant that NMCN was obliged (by the Companies Act 2006) to re-tender for the appointment of auditors for the next financial year ending 31 December 2020 (“**FY20**”). BDO chose not to participate in the re-tender process and new *Statutory Auditors* of NMCN were appointed for FY20.
- 3.5. In October 2020, NCMN announced that a review had been conducted into all major contracts and that it expected to report a loss before tax for FY20, and that an external investigation had been commenced to verify the extent of the prior-year adjustment included within that loss. Over the next 12 months NMCN released several additional profit warnings. Due to continued challenges faced in completing the audit of the FY20 financial statements, ongoing losses and mounting creditor pressure, the group was unable to complete a required refinancing and NMCN entered into administration in October 2021.
- 3.6. It should be noted that this *Final Settlement Decision Notice* does not assert that the going concern basis used in preparing the FY19 financial statements was in fact

¹ The Construction division was also known as the ‘Building’ division. The NMCNomenca division was occasionally referred to as ‘Civil Engineering and MEICA (Mechanical, Electrical, Instrumentation, Control and Automation)’.

inappropriate or subject to material uncertainty. However, the purpose of Executive Counsel's investigation is not to re-perform the Audit but to reach conclusions about the Respondents' performance of the Audit, based on an analysis of the available evidence. That analysis has identified the failings in the Respondents' audit work on going concern that are explained in this *Final Settlement Decision Notice*, in consequence of which the Respondents did not obtain sufficient appropriate audit evidence to be able to conclude on whether a material uncertainty existed.

The Audit

- 3.7. BDO had audited NMCN each year since 2010. Before the FY19 Audit it had done so from its Nottingham office (in the first three years as part of a different firm, before the latter's merger with BDO in 2013).
- 3.8. For the FY19 Audit, the main work of the Audit Team commenced in late October 2019. The audit plan was presented to the audit committee of NMCN's board of directors on 11 December 2019. Materiality for the Audit was set at £519,000; performance materiality was £363,000; and the 'clearly trivial threshold' was £10,000.
- 3.9. The Audit Team identified significant risks of material misstatement of the financial statements in three areas:
 - 3.9.1. Revenue recognition and long-term contract profit recognition, including contracts in joint operations and joint ventures;
 - 3.9.2. Management override of controls; and
 - 3.9.3. Recoverability of trade receivables, retention balances and amounts recoverable under construction contracts.
- 3.10. Three further risks of material misstatement were identified:
 - 3.10.1. Going concern;
 - 3.10.2. Financial statement disclosures; and
 - 3.10.3. Accounting for the acquisition of the New Subsidiary.
- 3.11. The Audit Report was originally planned to be signed on 26 March 2020, although NMCN's management had been forewarned this would be delayed. On 13 March 2020, however, the original Audit Engagement Partner [unexpectedly had to withdraw from the audit], necessitating a change of Audit Engagement Partner, and Mr Jones was appointed to the role. This coincided with the start of the first COVID-19 lockdown.
- 3.12. Following a review of the audit file and consideration of the outstanding audit issues, Mr Jones made the decision to defer the planned sign-off date until 22 April 2020 so

that the outstanding audit work could be completed.

3.13. In the Audit Report signed on 22 April 2020, BDO gave an unmodified audit opinion on the FY19 Financial Statements, and stated that key audit matters included:

3.13.1. “Recognition of revenue and attributable profit (or losses) on contracts and related estimates”; and

3.13.2. “Recoverability of trade receivables and amounts recoverable under construction contracts (contract assets).”

Long-term construction contracts

3.14. The majority of NMCN’s business was carried out under long-term contracts. The accounting of such contracts was complex and involved judgements and estimates by management. For example:

3.14.1. Under the relevant accounting standards and NMCN’s accounting policies, if the outcome of a construction contract was capable of being reliably estimated, revenue from that contract had to be recognised in proportion to the ‘stage of completion’ of the contract, and the ‘stage of completion’ was measured by comparing what costs NMCN had already incurred to its forecasts of the total costs it would have to incur in order to complete the contract. Accurate estimates of costs to complete were therefore crucial for the stage-of-completion method. Estimates of costs to complete can be difficult to make, involve a significant exercise of judgement, and are liable to change for a variety of reasons.

3.14.2. Part of NMCN’s total revenue from construction contracts was derived from variable consideration, including revenue arising from contractual arrangements for ‘pain/gain’-share² and for liquidated and ascertained damages (“**LADs**”). Under IFRS 15, NMCN was required to estimate the amount of variable consideration by using ‘the expected value’ or ‘the most likely amount’. IFRS 15 strictly limits the amount of revenue that can be recognised in such circumstances, by specifying that: “an entity shall include in the transaction price some or all of an amount of variable consideration ... only to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty associated with the variable consideration is subsequently resolved”.

² A pain/gain-share mechanism in a contract allows the parties to share cost overruns or savings. Contractual mechanisms of this type were applicable to four of NMCN’s joint operations for major projects and so had a substantial impact on the group’s revenue.

- 3.14.3. Some of NMCN's contracts experienced modifications as they proceeded. An example of a contract modification would be where NMCN was required to perform additional works beyond those reflected in the original contract specifications, either as a result of work being required to correct defects in the original specifications or as a result of subsequent instructions from the customer. Claims (for example, extensions of time and disputed variations) were also capable of being contract modifications. NMCN was only permitted to recognise any additional amounts in its estimates of total expected revenue from that contract to the extent that the 'highly probable' threshold had been met.
- 3.14.4. All of the above estimates and judgements could also impact the balance sheet. Significant amounts of revenue that management considered recognisable under IFRS 15 were held on the balance sheet as unbilled receivables ("**contract assets**").
- 3.15. When performing an audit, judgements and estimates made by management are a significant area of risk because they involve subjectivity, uncertainty and potential bias. For these reasons, it was important for BDO to consider carefully NMCN's accounting for long-term construction contracts.
- 3.16. The Audit Team acknowledged the importance of long-term contracts to NMCN's business. A key plank of their audit strategy was to try to select certain important contracts for detailed testing.
- 3.17. Most of the breaches set out in this *Final Settlement Decision Notice* relate to the Audit Team's failures to adequately address balances in NMCN's Financial Statements which related directly to NMCN's accounting for long-term contracts.

4. RELEVANT REQUIREMENTS TO WHICH THE BREACHES RELATE

- 4.1. Pursuant to regulation 4(1) of The Statutory Auditors and Third Country Auditors Regulations 2016, a person appointed to conduct a *Statutory Audit* must conduct that audit in accordance with the relevant standards for the conduct of *Statutory Audits*, which include the *Relevant Requirements*. The *Relevant Requirements* include (but are not limited to) the ISAs.
- 4.2. The *Relevant Requirements* referred to in this *Final Settlement Decision Notice* (which were effective for audits of financial statements for periods ending on or after 31 December 2019) are those listed below, which are specified in the following section, by reference to the breaches to which they relate, and are also set out in full in Appendix 1 hereto:
 - 4.2.1. ISA 200: Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (UK);
 - 4.2.2. ISA 230: Audit Documentation;
 - 4.2.3. ISA 315: Identifying and Assessing the Risks of Material Misstatement Through Understanding of the Entity and Its Environment;
 - 4.2.4. ISA 330: The Auditor's Responses to Assessed Risks;
 - 4.2.5. ISA 500: Audit Evidence;
 - 4.2.6. ISA 530: Audit Sampling;
 - 4.2.7. ISA 540: Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures;
 - 4.2.8. ISA 570: Going Concern;
 - 4.2.9. ISA 600: Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors).
- 4.3. As the *Statutory Auditor* responsible for the Audit, Mr Jones was responsible for the overall quality of the Audit and the direction, supervision and performance of the Audit in compliance with professional standards, and applicable legal and regulatory requirements. As the *Statutory Audit Firm* responsible for the Audit, BDO is responsible for any established breaches of *Relevant Requirements* on the part of any of its partners and employees.

5. DETAILS OF THE BREACHES OF *RELEVANT REQUIREMENTS*

Topic 1: Controls

(Audit of internal controls related to long-term contracts)

Overview

- 5.1. The Respondents' audit work over NMCN's internal controls was deficient in two areas, as summarised below: (1) controls over revenue and the contract-reporting process and (2) controls over contract costs.
- 5.2. The Audit Team was not placing reliance on the former set of controls, as it was planning to complete a substantive-based audit, and therefore only assessed the design and implementation of these. However, they did place reliance on the controls over contract costs and so, additionally, tested operating effectiveness of these controls.

Controls over revenue and the contract-reporting process

- 5.3. Controls over revenue and the contract-reporting process were the checks and approvals that NMCN's Finance team used in turning the performance data for long-term contracts into the revenue and profit figures shown in the company's accounts. The basis of the relevant control was that the forecast financial performance and risks for each major contract were assessed by NMCN in the initial tendering process and then reviewed during execution of the contract. Such review involved the assessment, by NMCN's group senior management, in a monthly review meeting, of the results produced by the divisional managers.
- 5.4. Several risks could arise in the course of reporting on long-term contract performance, for example: inaccurate record keeping; inaccurate estimates of costs to complete; inaccurate estimates of variable consideration; inappropriate categorisation of contract modifications; and inappropriate recognition of profit. These were risks which NMCN needed to ensure were appropriately controlled. In the audit of a contracting business such as NMCN, where contract revenue and profit recognition had been identified as significant risks, the controls over contract estimating were particularly relevant. Although the Respondents did not plan to place reliance on controls in this area and test their operating effectiveness, they were required to consider the controls that were (or should have been) in place and the design and implementation of those controls.
- 5.5. The Respondents' audit work was deficient in the following respects:
 - 5.5.1. The Respondents did not consider what controls were operated to prevent the

commercial teams from making errors in record keeping; nor did they consider what controls were in place to guard against inaccurate estimates of, amongst other things, costs to complete and variable income.

- 5.5.2. The Respondents did not consider what controls (if any) NMCN had in place in respect of tendering. The tendering process was the initial step in the estimation process and therefore a key financial reporting function.
- 5.5.3. The Respondents did not consider how NMCN's commercial directors and/or quantity surveyors produced estimates and judgements, and what controls (if any) were in place over their work.
- 5.5.4. The Respondents failed to evaluate the design and implementation of NMCN's controls over contract estimating at the tendering stage and failed to adequately evaluate or failed to evaluate those that applied during the life of the contract.
- 5.5.5. The Respondents overstated the importance of the monthly contract review meeting as a control over NMCN's revenue and long-term contracts. These monthly meetings (also referred to as 'Divisional Business Review meetings') were held between NMCN's central Finance team and its divisional commercial teams. The control represented by these meetings was judged to be relevant to multiple balances, including revenue, contract assets and contract costs, and was therefore central to the audit strategy. Yet the audit working papers gave insufficient explanation of how the monthly contract review meetings addressed the reasonableness of the underlying estimates and judgements.
- 5.5.6. Whilst the Respondents had planned to attend the monthly contract review meetings to ensure that "appropriate scepticism & challenge" was applied, their planned evaluation of the design and implementation of the meetings as a control was inadequately performed. Minutes of the five contract review meetings that the Audit Team attended, included in the Audit file, provide no evidence that the details of cost-to-complete estimates and variable income were addressed in the meetings. The audit working papers provide no explanation of how these meetings gave assurance as to the reasonableness of the estimates and judgements that underpinned management's recognition of revenue and profit, so as to constitute a control in this area of financial reporting. Nevertheless, the Audit Team concluded that the design of the control was "adequate for the purpose of ensuring that financial reporting is based on accurate and reliable data", and that it was being "implemented effectively".

Controls over contract costs

- 5.6. The Respondents sought to place reliance on controls over contract costs, but they failed adequately to assess these controls, specifically in the areas of the purchases system and subcontractor costs. They failed to identify certain key controls in these areas as controls and, consequently, did not adequately test either their design and implementation or their operating effectiveness.
- 5.7. In relation to the purchases system, BDO identified two controls: first, the matching of purchase orders to both invoices and Goods Received Notes and, secondly, the authorisation of payment runs. However, the Audit Team incorrectly labelled other key controls as 'processes' and consequently did not evaluate their design and implementation or include them in their tests for operating effectiveness. These were the operation of an Approved Vendor List and the authorisation requirement for high-value deliveries.
- 5.8. A similar error occurred with subcontractor costs, which constituted the majority of contract costs. The critical control in this area was the review of payment applications by a quantity surveyor, who was to certify the payment amount based on their own assessment of the work delivered. The Audit Team noted this mechanism but treated it at a high level as a 'process' rather than a control. As a result, they did not evaluate its design and implementation or include it in their tests for operating effectiveness.

Breaches of Relevant Requirements

- 5.9. In respect of controls over revenue and the contract-reporting process, the Respondents breached the following auditing standards:
- 5.9.1. ISA 315 paragraph 12, in that (for the reasons set out in paragraphs 5.5.1 to 5.5.3) they failed to obtain an adequate understanding of NMCN's controls.
- 5.9.2. ISA 315 paragraph 13, in that (for the reasons set out in paragraphs 5.5.4 to 5.5.6) they failed adequately to evaluate the design of NMCN's controls and to determine whether those controls had been implemented.
- 5.10. In respect of controls over contract costs, the Respondents breached the following auditing standards (for the reasons set out in paragraphs 5.6 to 5.8):
- 5.10.1. ISA 315 paragraph 12, in that they failed to obtain an adequate understanding of NMCN's controls relevant to the audit.
- 5.10.2. ISA 315 paragraph 13, in that they failed properly to evaluate the design of NMCN's controls and to determine whether those controls had been

implemented.

5.10.3. ISA 330 paragraph 8(a), in that they intended to rely on the operating effectiveness of the controls relating to the purchases system and subcontractor costs but failed to design and perform tests to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant key controls.

5.10.4. ISA 500 paragraph 6, in that they failed to obtain sufficient appropriate audit evidence as to the operating effectiveness of the controls.

Topic 2: Selection of contracts for testing

Overview

5.11. There were deficiencies in the Audit Team's methodology for selecting and testing contracts. While the selective testing of contracts is a permissible audit strategy in principle, the approach taken by the Audit Team was flawed in its design, application and documentation.

Process for selection of contracts for detailed testing

5.12. The Audit Team devised a three-stage process to select a sample of 48 contracts for substantive testing. This process involved:

5.12.1. 'Stage 1': Identifying "risky" contracts.

5.12.2. 'Stage 2': Applying a quantitative filter to select contracts based on four specific financial thresholds. Contracts qualified for selection if they exhibited one or more of the following four criteria: (i) a margin movement in FY19 that changed gross profit by at least 50 per cent of materiality; (ii) a discrepancy between invoiced amounts and recognised revenue of at least 50 per cent of materiality, (iii) turnover exceeding £5 million; (iv) an 'AROC' (amounts recoverable on contracts) balance of more than one month's activity or costs exceeding recognised revenue by at least 50 per cent of materiality.

5.12.3. 'Stage 3': Selecting an additional sample during the audit fieldwork to introduce an element of "randomness".

5.13. Despite this structured plan, the execution was fundamentally deficient:

5.13.1. For Stage 1, the term "risky" was poorly defined, and this criterion was not applied in a coherent or rigorous manner. (In relation to certain contracts, the Audit Team, without making its own assessment, selected them for testing because management had assessed those contracts as risky.)

5.13.2. For Stage 2, not all of the quantitative criteria could have been properly applied by the Audit Team because the available working papers recorded financial data on a cumulative basis, making it impossible to calculate the required period-specific figures for individual contracts. The Audit Team was therefore unable to conclude as to whether all contracts that met the selection criteria had been considered. Many contracts which it appears may have met the criteria were not considered for inclusion in the sample.

5.13.3. Stage 3 was not implemented in a manner capable of introducing an element

of audit sampling within the meaning of the ISAs, to enable information gleaned from the selected contracts to be extrapolated to the entire population.

Treatment of the residual population

- 5.14. A critical failure occurred in the treatment of the residual population of contracts that were not selected for detailed review. No substantive tests of detail were planned or performed on the revenue and profit recognition for this group. This omission meant that 44% of contract revenue, amounting to a material £179.6 million, was not subjected to sampling for any detailed testing. The Audit Team thus failed to obtain sufficient appropriate audit evidence for a significant portion of the financial statements. In effect, they disregarded this untested population and gave little or no consideration to the associated risks. This was a serious failing in the Audit Team's approach to selection of contracts for testing.
- 5.15. The audit documentation was also inadequate. The audit file failed to include a schedule explaining how the selection criteria were applied to each of the 48 chosen contracts. This omission makes it impossible for an experienced auditor to understand the selection rationale or assess the sufficiency of the set of contracts selected for testing. Furthermore, the Audit Team did not adequately document how it verified the completeness of the contract lists from which the sample was drawn. A working paper on the audit file reconciled the revenue recorded for each division to applications in the year. However, the audit file did not document an audit trail between those applications and the contract lists and otherwise lacked evidence of the workings for the reconciliation, leaving only an unsubstantiated narrative assertion.

Breaches of *Relevant Requirements*

- 5.16. In respect of the matters set out in this section above, the Respondents breached;
- 5.16.1. ISA 500 paragraph 6, in that they failed to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence in relation to:
- 5.16.1.1. the process by which contracts were selected for testing of detail;
and
- 5.16.1.2. the reconciliation work to test the completeness of the population from which the selection was made.
- 5.16.2. ISA 500 paragraphs 6 and 10, in that they failed to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence in relation to the residual

population of contracts which were not selected for testing of detail.

5.16.3. ISA 330 paragraphs 5, 6, 7(b) and 21, in that, in relation to that residual population, the Audit Team did not adequately design and perform audit procedures in response to the significant risk of material misstatement that they had identified in respect of revenue and profit recognition on long-term contracts.

5.16.4. ISA 230 paragraph 8, in that they failed to prepare audit documentation sufficient to explain:

5.16.4.1. the process by which they selected contracts for testing of details;
and

5.16.4.2. the reconciliation work to test the completeness of the population from which the selection was made.

Topic 3: Variable income

Overview

- 5.17. There were deficiencies in the procedures applied by the Audit Team to test variable income. Variable income, comprising revenue from variations, claims, and other variable consideration on construction contracts, was correctly identified by the Audit Team within its articulation of the significant risk of material misstatement represented by “revenue recognition and long-term contract profit recognition”. This risk was heightened by the susceptibility of management’s estimates and judgements in this area to potential bias.
- 5.18. Despite identifying the risk, the Audit Team failed to design and execute adequate audit procedures to obtain sufficient appropriate audit evidence that the variable income balances were not materially misstated. The work performed by the Audit Team was deficient in its overall approach, in its specific testing of key components such as LADs, and in its documentation.

Approach to testing variable income

- 5.19. NMCN did not provide a central schedule of variable income for testing, nor were such schedules available at the individual contract level. In response, the Audit Team sought to test unrecovered balances on a selection of 10 contracts.³ This approach was deficient in several material respects:
- 5.19.1. The selection consisted of contracts chosen judgements. The Audit Team obtained no assurance that this selection included all contracts where significant judgements on variable income were made.
- 5.19.2. The team used uncollected contract assets as a proxy for variable income. This was inappropriate, as contract assets also include amounts due under the original contract, not just variable income. This made it difficult to identify and isolate the actual variable income being tested.
- 5.19.3. The assessment was based on contract asset balances at the year-end (31 December 2019), whereas a proper evaluation of variable income should have considered the estimated final contract revenue at the completion of the contract.

³ Additionally, the Audit Team performed post-year-end recoverability work on contract assets in general (as discussed below under the heading ‘Topic 7: Contract assets, trade receivables, retentions’). Despite the limitations explained in paragraphs 5.19.2 and 5.19.3, such work would have provided assurance on variable income included within contract assets at the year end, subject also to the deficiencies in the work on contract assets identified under Topic 7.

5.19.4. There was no clear and consistent audit trail and, in some instances, key working papers could not be reconciled with each other. For example, there were significant differences between the working paper dealing with variable income and that setting out all of the contract results (the figures in the latter were adjusted at a late stage to capture variable amounts). There were also discrepancies between figures in key working papers and those in a summary provided by NMCN's Finance team to the company's audit committee. Furthermore, there is no evidence that the Audit Team verified cash receipts shown in NMCN's reports by reference to the company's bank accounts.

5.19.5. Across the 48 contracts selected for substantive testing, the Audit Team did not apply a consistent or rigorous set of procedures to assess variable income. The Respondents should have made a thorough assessment of original contract sums and provisions for variations, claims and delays, and reconciled these to the final estimated revenue.

LADs

5.20. LADs are predetermined damages due from the contractor to the customer for contractual breaches such as late completion. They represent a key risk in construction auditing as they directly impact final revenue. The Audit Team's working papers indicated that NMCN considered LADs to be a risk as "serious concerns" were raised among NMCN's senior management regarding delays to projects in the Building division. The Audit Team also noted that delays affected nearly every project in that division.

5.21. Despite this, the audit work was inadequate. There was no dedicated audit working paper to address the risks associated with delays and LADs. The Audit Team failed to sufficiently consider the impact of delays on revenue and did not adequately evaluate the risk of customers deducting LADs, even on contracts where delays were noted. In cases where some consideration appears to have been given to LADs, the evaluation was not documented in the audit file.

Breaches of *Relevant Requirements*

5.22. In respect of the matters set out in this section above, the Respondents breached;

5.22.1. ISA 500 paragraph 6, in failing to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence; and

5.22.2. ISA 230 paragraph 8, in that they failed to prepare audit documentation

sufficient to explain (where there was evidence that contracts were behind schedule) their consideration of the risk of LADs or other penalties, reducing revenue and profit.

Topic 4: Applications and payments on account

Overview

- 5.23. There were deficiencies in the Audit Team's work concerning the testing of applications for payment and payments on account.

Applications for payment

- 5.24. In the context of construction contracts, applications are formal requests submitted by contractors to customers to receive payment for work completed during a specific period. Applications are reviewed for accuracy and completeness with a view to resolving discrepancies before approval. The Audit Team's approach in respect of applications was to test them by comparing them to subsequent certificates and cash receipts. The cumulative amount by which applications exceeded subsequent certificates was referred to as uncertified applications and formed part of the contract assets at 31 December 2019.
- 5.25. The Audit Team took two approaches to testing applications, which risked a failure to take an appropriate and consistent approach to the testing of uncertified applications. For three of NMCN's four divisions, each application was compared to subsequent payment certificates, with an attempt to reconcile these certificates with cash receipts. However, for the other division and NMCN SS Ltd, a small, judgementally selected sample of applications was tested. The Respondents failed to prepare audit documentation sufficient to explain the audit work performed in relation to testing applications under either approach.

Payments on account

- 5.26. As regards payments on account, the Audit Team relied on a lead sheet which netted off numerous debit and credit balances. Although the Audit Team identified a £8.7 million offsetting error through reviewing the contract asset balances, the presence of these large, offsetting balances should have prompted further investigation of offsetting amounts, which would have identified that some balances were still incorrectly offset. These large offsetting balances included for the Nomenca division, credit balances totalling £23.6m and debit balances totalling £10.5m. A conspicuous example within this division was a net balance for work in progress ("WIP") of £1.170 million on one contract that was incorrectly offset against payments on account. The presence of those offsetting balances was a patent anomaly, such that it ought to have caused the Audit Team, exercising appropriate professional skepticism, to make further enquiries as to whether the WIP balances were incorrectly

netted off payments on account, contrary to IAS 1. Had they done so, the Audit Team would have detected a material misstatement relating to contract assets and contract liabilities under trade and other payables in the balance sheet.

Breaches of *Relevant Requirements*

5.27. In respect of the audit work performed on payments on account for one of NMCN's divisions, the Respondents breached the requirements of:

5.28.1. ISA 200 paragraph 15, to plan and perform the Audit with professional skepticism; and

5.28.2. ISA 500 paragraph 6, to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.

5.28. In failing to prepare audit documentation sufficient to explain the Audit Team's approaches to the audit work performed on NMCN's applications for payment and on reconciling cash receipts to certificates across the five divisions, the Respondents breached the requirements of ISA 230 paragraph 8.

Topic 5: Costs to complete

Overview

- 5.29. 'Costs to complete' forecasts on contracts are a key aspect of accounting in the construction industry. They are fundamental to the calculation of revenue and profit; an excessively optimistic costs forecast would lead to over-recognition of revenue and profit.
- 5.30. There were deficiencies in the Audit Team's approach to costs to complete. They failed to design and perform audit procedures that were appropriate to obtain sufficient appropriate audit evidence.
- 5.31. NMCN recognised revenue from its contracts in proportion to their stage of completion in accordance with the applicable accounting standards. This metric was determined by comparing the costs already incurred on a contract with the total forecast costs needed for its completion. The accuracy of the forecasts was therefore critical. Costs to complete not only influenced the amount of revenue recognised in a given period but also the overall assessment of a contract's profitability.
- 5.32. The estimation by management of costs to complete was a significant risk area, as it involved the exercise of judgement and there were significant uncertainties due to factors like weather delays, subcontractor performance, and design flaws. There was a risk that management might adopt an overly optimistic outlook in its cost forecasts. Such optimism can inflate reported revenue and profit in the short term by overstating both the stage of completion and the contract's overall expected margin, as well as potentially leading to a loss-making project being incorrectly reported as profitable.

The audit work

- 5.33. The Audit Team correctly identified forecasts of costs to complete as a key estimate, noting the area as a significant risk of material misstatement due to its subjectivity and susceptibility to management bias. The initial audit plan involved assessing the systems that generated the estimates and performing substantive tests of detail on all selected contracts. However, the planned work on controls was not ultimately carried out or relied upon, making the substantive testing the primary source of audit evidence in this critical area.
- 5.34. From an initial sample of 48 judgementally selected contracts, the Audit Team applied a series of exclusion filters which drastically reduced the number of contracts subject to any testing of their costs to complete. The application of these filters resulted in just four contracts being tested. There were deficiencies in respect of each of the filters:

- 5.34.1. Twenty-two contracts were excluded because their reported costs had exceeded 75% (or in one case 71%) of the final forecast cost. No justification was provided for the threshold adopted.
- 5.34.2. Fourteen framework contracts were omitted on the grounds that they had “no final position” – a reason which, again, was not explained in the working papers.
- 5.34.3. Three joint-operation projects were set aside based on an assertion that partner oversight and pain/gain-share clauses reduced the associated risk of material misstatement and because no issues were identified from other audit procedures.
- 5.34.4. Two early-stage contracts were excluded because their year-end margins appeared consistent with tender estimates, although no work was performed which was capable of corroborating the assumptions behind this rationale. The Audit Team had made no evaluation of the design and implementation of NMCN’s controls over cost-to-complete estimates at the tendering stage, and no evidence was obtained for the two contracts to corroborate either their stage of completion or whether they were performing in line with tendering estimates.
- 5.34.5. Three contracts which had been completed in prior periods were also not revisited.
- 5.35. The exclusions were not responsive to the risk of material misstatement, and no adequate justification was provided by the Audit Team for applying them. For example, removing 22 contracts from testing based on an unsubstantiated completion threshold ignored the continuing risk that final costs could be understated. Similarly, the blanket exclusion of framework and joint-operation contracts was based on unevidenced assumptions. The exclusion of framework contracts may potentially have been a reasonable assumption if these contracts were on a cost-plus basis (i.e., where all costs could be recovered from NMCN’s customer), although there was insufficient evidence to support this. The fact that a contract was in a joint operation made little difference to the audit testing that needed to be performed on the financial information relied upon.
- 5.36. Even for the four contracts that were subjected to testing, the work was incomplete and poorly documented. There was no justification recorded for the sample sizes used to test subcontractor costs and, in one instance, a material sum of £539,000 in forecast costs was left entirely untested.
- 5.37. No audit procedures were applied to the residual population of approximately 400 contracts that were not part of the initial judgemental sample. The four tested contracts

could not be considered representative of this wider population, with the consequence that the Audit Team lacked sufficient appropriate audit evidence for a material portion of revenue and cost balances.

Breaches of *Relevant Requirements*

- 5.38. By reason of the matters set out in this section above, the Respondents failed to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence as to costs to complete, in breach of ISA 500 paragraph 6.

Topic 6: Loss-making contracts

Overview

5.39. The Audit Team performed inadequate work in relation to the audit of loss-making contracts.

The audit work

5.40. The Audit Team's stated objective was to ensure that expected losses on contracts were fully recognised and provided for in accordance with IAS 37, which required the immediate and full recognition of any total expected loss. The Audit Team stated that it had identified relevant contracts by reviewing management schedules, comparing January 2020 forecasts against provisions at 31 December 2019, and documenting this analysis in a dedicated working paper. Where differences exceeded a 'clearly trivial threshold', management explanations were sought and recorded. However, the audit work was deficient and the Audit Team failed to obtain sufficient appropriate audit evidence of the completeness of losses recognised in two key respects.

5.41. First, they did not ensure that their working paper contained a complete list of loss-making contracts. Several contracts were omitted from testing without adequate documented justification.

5.42. Secondly, for the contracts that were reviewed, the audit work was insufficient. Even where the Audit Team identified that potential under-provisions exceeded the 'clearly trivial threshold', the subsequent audit procedures performed were limited. These failed to obtain adequate evidence to corroborate key facts or assumptions underpinning management's explanations for the variances.

Breaches of *Relevant Requirements*

5.43. The Respondents failed to design and perform audit procedures that were appropriate in the circumstances for the purpose of verifying both the completeness of the population of loss-making contracts and the adequacy of the related provisions, in breach of ISA 500 paragraph 6.

Topic 7: Contract assets, trade receivables, retentions

Overview

5.44. The balances for contract assets, trade receivables and retentions comprised amounts which NMCN considered it would be paid by its clients for work performed under the construction contracts. The Audit Team identified the recoverability of these balances as a significant risk of material misstatement.

Contract Assets

5.45. NMCN's contract assets increased significantly from £33.35 million in 2018 to £47.01 million by 31 December 2019, representing a rise from 9.8% to 11.6% of revenue, and the Audit Team identified this as a significant risk area. However, the Audit Team performed inadequate testing, focusing only on contract asset balances exceeding £250,000, which left assets totalling £4.7 million untested. Additional significant contracts with assets totalling £3.145 million were addressed separately but were also not tested or not tested adequately.

5.46. For tested items, the Audit Team relied on post-year-end cash receipts totalling £26.6 million and post-year-end certificates amounting to £1.2 million. Where these were unavailable, explanations justifying recoverability were documented, although these were incomplete. The Audit Team's approach therefore failed either to obtain sufficient appropriate audit evidence or to maintain adequate documentation.

5.47. The Audit Team's work on contract assets, which totalled £47.01 million, was flawed in its design and execution. The audit approach was to test only those contracts with asset balances exceeding £250,000. This specific selection process resulted in contract assets with a cumulative value of £4.7 million not being subjected to any audit testing. Furthermore, contract assets relating to three significant items (the New Subsidiary and two major projects), amounting to a further £3.145 million, were also left untested or not tested adequately.

5.48. For the balances selected for testing, the Audit Team sought to confirm recoverability primarily by reconciling them to post-year-end cash receipts (£26.6 million) and, to a lesser extent, post-year-end certificates (£1.2 million). However, this work was deficient in several respects. The audit evidence was inadequate as the cash receipts were not verified by reference to independent bank statements, relying instead on internally-produced reports. There was no clear audit trail to demonstrate that receipts were correctly matched to the specific year-end asset balances. The audit evidence was also inadequate where the Audit Team attempted to reconcile to post-year-end

certificates, and again there was reliance on internally-produced reports, rather than the actual certificates. Finally, the Audit Team examined unrecovered balances for 18 contracts, accounting for almost all the total unrecovered amount (£9.9 million out of £10.1 million). However, the explanations documented by the Audit Team were not supported by sufficient evidence and, in several cases, none was obtained.

- 5.49. Consequently, the Respondents failed to obtain sufficient appropriate audit evidence regarding the recoverability of contract assets. They also failed to prepare documentation sufficient to explain the work performed to ensure certificates relied upon were not duplicative of cash receipts.

Trade Receivables

- 5.50. The Audit Team correctly identified the recoverability of trade receivables (£9.7 million) as a significant risk. However, the procedures designed to address this risk were inadequate. The team selected samples for testing but based the sample size on a "Normal" risk setting rather than the "Significant" risk assessment that had been made. This resulted in smaller sample sizes than required by the firm's own methodology.
- 5.51. The testing involved matching receivables to post-year-end cash receipts. This work was generally defective, in that the working papers lacked reconciliations to show that batch payments cleared the receivables being tested.
- 5.52. Where the receivables were not fully recovered, the audit work was inadequate. The Audit Team failed to perform audit procedures on each item selected in the statistical sample. In certain cases, it was noted that the receivables had been reversed after the year-end and that a corresponding adjustment at year-end was required. These reversals should have prompted the Audit Team to consider whether, extrapolated to the whole population of receivables, the errors indicated a risk of overstatement, necessitating a larger sample for testing. Although the Audit Team proposed an adjustment for these reversals, no consideration of the effect of extrapolation was evidenced on the audit file. These deficiencies left a lack of sufficient appropriate audit evidence.

Retentions

- 5.53. The Audit Team did not test the entire population of overdue retentions; there was no testing of balances that did not correspond to a post-year-end cash receipt. The audit work performed on the retentions that were tested was inadequate. The Audit Team's stated procedures were not properly executed, and the approach lacked a defined selection methodology. The team identified 18 retention balances on completed

contracts that were past their due date. Of these, cash receipts were reconciled for only three balances (£129,000). The remaining 15 balances (totalling £233,000) were not investigated further, on the ground that they were immaterial in aggregate. The audit conclusion reached on this basis was inappropriate, particularly as other documentation on the audit file indicated that the value of overdue retentions was significantly higher than those identified on completed contracts. There was no evidence that the planned work to verify that the counterparties for material retention balances were still trading had been completed.

- 5.54. As the procedures performed failed to verify the validity and existence of retention balances or test the creditworthiness of the customers, there was a lack of sufficient appropriate audit evidence.

Breaches of Relevant Requirements

- 5.55. The Respondents' audit work on recoverability of contract assets, trade receivables and retentions balances breached the requirement of ISA 500 paragraph 6 to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.

- 5.56. In respect of the audit work on trade receivables balances, the Respondents further breached:

5.56.1. ISA 530 paragraph 9, by failing to perform audit procedures on each item selected in the statistical sample; and

5.56.2. ISA 230 paragraph 8, by failing to prepare audit documentation sufficient to explain their approach to:

5.56.2.1. matching the cash receipts relied upon to the receivables; and

5.56.2.2. determining whether reversals of receivables made after 31 December 2019 undermined the assurances that were sought from testing a sample of the balances.

Topic 8: Going concern

Overview

5.57. The Respondents were required to obtain sufficient appropriate audit evidence regarding the appropriateness of management's use of the going concern basis of accounting and to conclude, based on the evidence obtained, whether a material uncertainty existed about NMCN's ability to continue as a going concern. This required extensive audit work on the cash flow forecast that NMCN's management developed for the purpose of their going concern assessment ("**Management's Forecast**"). As set out below, the Respondents' audit work in this area was deficient in respect of the following aspects of Management's Forecast:

5.57.1. the underlying data generated to prepare the forecast;

5.57.2. the underlying assumptions and information supporting the forecast; and

5.57.3. the period covered by the forecast.

5.58. As a result of these deficiencies, the audit procedures were not appropriate in the circumstances to obtain sufficient evidence regarding management's use of the going concern assumption. Moreover, this inadequate audit work is attributable to a lack of professional skepticism on the part of the Respondents.

Background

5.59. NMCN's 2019 Annual Report stated for the purpose of its 'Going Concern and Viability Statement' that management believed the company would continue to meet its liabilities through to at least 31 December 2022. Management's Forecast was provided in support of the going concern assessment to April 2021. Management provided two primary cash flow models covering eight months (to December 2020), alongside supporting documentation from NMCN's bank regarding its overdraft facility. Management also supplied a cash flow model through 2021 that was not included on the audit file. Notably, NMCN faced substantial cash-flow impacts from the transition between the sixth and seventh Asset Management Plans ("**AMP(s)**", i.e., the regulatory framework governing water-sector investment) (the "**AMP Transition**"), which reduced cash receipts significantly. Additionally, assumptions showing significant improvements in WIP/debtor days in three divisions were made despite evidence of deteriorating debtor recovery times.

5.60. The Audit Team's work was conducted in the context of several known risks and critical business factors:

5.60.1. **The AMP Transition:** NMCN's business was significantly impacted by the regulatory cycle of the water sector. The AMP Transition (from 'AMP6' to 'AMP7') on 1 April 2020 was known to involve less favourable payment terms for construction firms, with an expected negative impact on cash receipts of approximately £6 million. This AMP Transition was identified by the Audit Team as critical to NMCN's cash flow and a risk in relation to going concern.

5.60.2. **WIP/debtor days:** Cash flow forecasts prepared by management incorporated assumptions for WIP/debtor days – i.e., the time it would take for recognised revenue to convert to cash – which, for three divisions, represented a significant improvement on NMCN's historical performance. For example, the forecast for the Highways business unit used 49 days, compared to an actual figure of 72 days in 2019. These assumptions, which implied a significantly faster recovery of cash than had previously been the case, required explanation in the face of other evidence, such as NMCN's 41% increase in contract assets compared to only a 19% increase in revenue during 2019, which suggested it was taking longer to convert work into cash.

5.60.3. **The COVID-19 pandemic:** The audit was finalised in April 2020, at a time of significant economic uncertainty following the onset of the COVID-19 pandemic.

5.61. The AMP Transition, the COVID-19 pandemic, financial pressures in the construction sector, the political environment and economic uncertainty were all identified by the Audit Team and were events which may have cast significant doubt on NMCN's ability to continue as a going concern. As a result, in accordance with ISA 570, paragraph 16(c), the Respondents were required to perform additional audit procedures. Among other things, the Audit Team was required (1) to evaluate the reliability of the underlying data generated to prepare NCMN's cash flow forecasts; and (2) to determine whether there was adequate support for the assumptions underlying NMCN's forecasts.

Evaluation of the underlying data

5.62. It was important for the Audit Team to perform a retrospective review of management's forecasting accuracy. To that end, the Audit Team planned to compare management's prior-year forecasts with actual cash positions. However, this test was never done.

5.63. When management produced its initial going concern assessment in early 2020, its cash flow forecasts predicted that NMCN would hold £15.2 million of cash at the end of February 2020. In fact, the group had only £7.4 million – less than half the forecast amount. This was a large variance, especially so early in the forecast period, and it should have prompted the Audit Team to question the reliability of management's

models. However, the variance was not properly investigated or corroborated with evidence. Instead, the audit file simply recorded management's explanation (that it related to a delayed receipt on a single project) without showing any independent testing of that claim, as in the post-Covid cashflow model the Audit Team considered that a delayed receipt would have no overall impact on the going concern conclusion.

- 5.64. The forward order book was also a source of underlying data used by management to support its revenue and cash flow projections. Testing it was therefore necessary to evaluate the reliability of that data. The Audit Team's review of the forward order book was neither properly conducted nor documented.
- 5.65. The audit work on the forward order book was intended to provide evidence that contracts underpinning the forecast revenues had in fact been secured. Although the Audit Team requested supporting documentation for the order book previously received and were provided with access to folders containing evidence of secured contracts, some of this material was uploaded on the date the financial statements were approved, leaving very limited opportunity for audit work to be undertaken. The working paper which purported to evidence the review merely reproduced management's responses at a high level and asserted that documentary evidence had been seen, without properly identifying the contracts tested, describing the procedures performed, or retaining the evidence reviewed. There was no documented evaluation of whether the forward order book reconciled to the forecasts, no assessment of whether the contracts were profitable, and no challenge to management's assertions.

Management's assumptions

- 5.66. The Audit Team accepted without challenge management's assumptions of a significant improvement in WIP/debtor days in three divisions, notwithstanding the existence of evidence contradicting those assumptions. The forecasts assumed a significant improvement in cash collection compared with 2019, with debtor days projected to reduce across key divisions. However, this assumption was inconsistent with the actual trend in NMCN's financial data: during 2019 contract assets (unbilled revenue) rose by 41%, from £33.3 million to £47.0 million, despite revenue increasing by just 19%. This indicated that the group was already experiencing increasing delays in converting work into cash. Rather than subjecting this assumption to critical scrutiny, the Audit Team accepted it at face value.
- 5.67. The Audit Team also accepted management's assertion that NMCN did not expect to need to make any use of its £15 million bank overdraft facility during the period covered by Management's Forecast. In doing so, the Audit Team did not give any consideration

to the sensitivities within the cash flow model used – in particular, how sensitive the utilisation of overdraft was to changes in key assumptions, other than giving high-level consideration to the impact of potential redundancy costs and the impact of a delayed large debtor recovery (as well as to management’s adoption of a 20% reduction in revenue in the second half of 2020, as a COVID-19-related sensitivity). Management had developed their forecast through a number of progressions from the ‘Base’ scenario, culminating in the post-COVID-19 scenario that was then adopted and relied upon (‘S2e’). In the ‘Base’ scenario, NMCN was dependent on the overdraft, whereas in scenario ‘S2e’ the overdraft would not be used at all. However, certain notional points in the progression, without taking into account available mitigation, posit the overdraft being used extensively or even exceeded. The overdraft was conditional and subject to termination on demand by the bank. From early 2020 NMCN was seeking to negotiate a temporary six-month increase of its limit from £15 million to £20 million [redacted]. It was clear that the overdraft was potentially critical to NMCN’s working-capital strategy and central to the going concern assessment. The sensitivity of the cash flow forecast and overdraft utilisation to changes in key assumptions therefore clearly merited the scrutiny by the Audit Team that was lacking.

- 5.68. Furthermore, the updating of Management’s Forecast was carried out by management explicitly as a response to the fact that the COVID-19 pandemic created significant uncertainty for NMCN’s cash flows. The updated scenario, ‘S2e’, purportedly reflected the pandemic’s expected impact. It showed a better liquidity position than the pre-COVID-19 ‘Base’ case, despite the onset of a global pandemic. This significantly improved projection clearly merited further corroboration, yet there is no evidence on the audit file of substantive challenge to management’s assumptions, no stress-testing of the forecasts against external evidence, and no evaluation of whether downside risks were appropriately modelled. The sole COVID-19 memorandum on the file largely repeated management’s assertions without critical analysis.
- 5.69. Finally, limited audit procedures were performed to assess management’s estimate of the amount and timing of the financial impact of the AMP Transition on cash flow. Management’s Forecast posited a reduction in cash flows by £6 million in 2020, yet the Audit Team obtained no evidence either that this was the right amount or that it would impact at a steady rate of £0.5 million per month throughout 2020.
- 5.70. In summary, the Audit Team failed to obtain sufficient appropriate audit evidence to support their conclusion that Management’s Forecast of cash flow was reliable, by failing:

- 5.70.1. to challenge management's assumptions in relation to debtor days;
- 5.70.2. to evaluate management's treatment of the AMP Transition; and
- 5.70.3. to consider the sensitivity of the forecast to changes in key assumptions, especially relating to the impact of the COVID-19 pandemic and NMCN's use of its overdraft facility.

The forecast period

- 5.71. The Audit Team was required to evaluate management's assessment of going concern over at least twelve months from the date of approval of the financial statements. They failed to do so; their documented work focused primarily on the period to December 2020 (i.e., only eight months forward from the expected signing date in April 2020).

Professional skepticism

- 5.72. The Audit Team failed to critically assess evidence and challenge management's assertions. This was evident in its approach to data underlying forecasts, the uncritical acceptance of significant improvements in the WIP/debtor day assumptions, the failure to investigate the material cash forecast variance, and the lack of challenge to the favourable projected impact of COVID-19. These failures constituted a breach of the fundamental requirement to plan and perform an audit with professional skepticism.

Breaches of *Relevant Requirements*

- 5.73. In their overall audit work on going concern, as explained in this section above, the Respondents:
 - 5.73.1. did not approach their assessment of NMCN's ability to continue as a going concern with adequate professional skepticism and so failed to assess critically certain important matters, in breach of ISA 200 paragraph 15 and ISA 570 paragraph 12D-1.
 - 5.73.2. did not design and perform audit procedures which were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence to put themselves into a position to be able to conclude on management's use of the going concern assumption and whether a material uncertainty existed, in breach of ISA 500 paragraph 6 and ISA 570 paragraph 16.
- 5.74. In their audit work on cash flow forecasts in relation to going concern, the Respondents further breached:
 - 5.74.1. ISA 570 paragraph 16(b), in that they failed to evaluate management's plans for future actions in relation to a matter which was acknowledged to have a

material impact on cash flow forecasts, namely the AMP Transition; and

5.74.2. ISA 570 paragraph 16(c), in that they failed adequately to:

5.74.2.1. evaluate the reliability of the underlying data used to prepare the relevant cash flow forecast; and

5.74.2.2. determine whether there was adequate support for the assumptions underlying the forecast.

5.75. Finally in this area of the Audit, the Respondents failed to cover the same period as that used by NMCN's management when evaluating management's assessment of the company's ability to continue as a going concern, in breach of ISA 570 paragraph 13.

Topic 9: Acquisition of the New Subsidiary

Overview

5.76. In October 2019, NMCN acquired the New Subsidiary for £1 in cash plus contingent consideration valued by NMCN at £2.2 million. This contingent payment was linked to the New Subsidiary's cumulative profit before tax over three years. Its valuation, therefore, depended heavily on forecasts of the New Subsidiary's future performance. The acquisition of the New Subsidiary required NMCN to make significant accounting estimates for intangible assets and contingent consideration. The Audit Team's work on the acquisition was deficient in four key areas.

Intangible assets

5.77. The audit of intangible assets – specifically customer relationships and software – was inadequate. NMCN's valuation of customer relationships relied on revenue forecasts, growth and attrition assumptions, and a specific discount rate. The Audit Team failed to obtain sufficient appropriate audit evidence of the value of the intangible asset by using revenue figures from an untested business plan and management accounts. They also did not adequately assess whether management's assumptions on customer attrition and growth were reasonable. This failure to test the underlying data and challenge key assumptions entailed failures to design tests to gather sufficient evidence and to properly evaluate management's accounting estimates.

5.78. Furthermore, the valuation was highly sensitive to the discount rate used, which included a 5% company-specific risk premium that the Audit Team accepted without obtaining evidence to justify it. The Audit Team also failed to carry out any testing of the costs that comprised the valuation of the New Subsidiary's software asset, thus further omitting to design tests to gather sufficient evidence and to evaluate management's accounting estimates.

Contingent consideration

5.79. Failures in respect of the same requirements occurred in the testing of contingent consideration. The Audit Team did not review the reasonableness of management's profit forecasts or an assumption that 50% of a £675,000 debt was recoverable.

Acquisition balance sheet

5.80. The audit work on the acquisition balance sheet was poorly documented and testing was limited, especially concerning debtors and deferred tax balances. The omission of adequate testing caused a lack of audit evidence.

Post-acquisition review

5.81. The Audit Team planned a desktop review of the New Subsidiary's post-acquisition trading figures, but this was never performed. They did not plan or perform a review of the closing balance sheet. These serious omissions left several material balances untested, in breach of multiple auditing standards.

Breaches of *Relevant Requirements*

5.82. In respect of the Audit Team's work in relation to the valuations of both the New Subsidiary's intangible assets and contingent consideration due to the New Subsidiary's previous owners, the Respondents breached:

5.82.1. ISA 500 paragraph 6, in that they did not design and perform tests which were capable of providing sufficient appropriate audit evidence; and

5.82.2. ISA 540 paragraph 13(b), in that, when responding to the assessed risks of material misstatement, they failed to test the data on which accounting estimates were based and to consider whether the assumptions made by management in estimating the values in question were reasonable.

5.83. The Respondents further breached ISA 500 paragraph 6 in their audit work on the acquisition balance sheet in relation to the debtors and deferred tax balances, in that they did not design and perform tests which were capable of providing sufficient appropriate audit evidence concerning those balances.

5.84. In relation to the Audit Team's work on post-acquisition transactions, the Respondents breached:

5.84.1. ISA 500 paragraph 6, in failing to perform any testing over the post-acquisition trading balances and closing balance sheet of the New Subsidiary;

5.84.2. ISA 600 paragraph 18(b), in failing to obtain an understanding of the New Subsidiary which was sufficient to assess the risks of material misstatement of the group financial statements; and

5.84.3. ISA 600 paragraph 28, in that they failed to perform analytical procedures on the post-acquisition financial information of the New Subsidiary.

Topic 10: Non-recurring items

Overview

5.85. In calculating the materiality threshold, the Audit Team properly excluded non-recurring items. However, the Audit Team failed to adequately test those items before excluding them.

The audit work

5.86. Deficiencies in audit testing are apparent in relation to two significant loss-making items relevant to NMCN's overall reported profit for the year: a £1.48 million loss from a particular legacy contract (the "**Legacy Contract**") and £1.86 million in costs following the insolvency of a key subcontractor (the "**Subcontractor Insolvency**"). Although these two items were classified as non-recurring, the Audit Team failed to conduct adequate testing to verify their value before excluding them. The Audit Team's work was superficial, involving minimal substantive testing and an over-reliance on internal management summaries without seeking independent, third-party corroboration to verify the amounts.

5.87. There were two components to the Legacy Contract loss. First, there was a £750,000 income reversal, which the Audit Team explained related to the loss of an adjudication, a copy of which was included in the audit file. Second, there was £748,000 in legal expenses which were not properly tested through substantive procedures, for example by analysing invoices. Instead, the Audit Team relied on a high-level review which was insufficient to provide sufficient appropriate audit evidence in relation to those expenses.

5.88. Similar deficiencies were present in the Audit Team's work on the £1.86 million loss from the Subcontractor Insolvency. The audit work intended to support £1.42 million in direct costs was linked to an incomplete cross-reference in the working papers, and no alternative supporting documentation was placed on the audit file. Furthermore, a £335,000 loss attributed to an associated contract was inadequately explained and lacked any documented reconciliation to detailed records.

5.89. Given that these non-recurring items significantly influenced the company's reported profit and the calculation of materiality, the Audit Team had an obligation to obtain sufficient appropriate evidence.

Breaches of *Relevant Requirements*

5.90. The Respondents' failure adequately to test losses recorded as non-recurring for the Legacy Contract and the Subcontractor Insolvency breached the requirement of

ISA 500 paragraph 6 to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.

6. SANCTIONS – BDO

- 6.1. Paragraph 10 of the FRC’s Sanctions Policy (Audit Enforcement Procedure) (the “**Sanctions Policy**”) provides that *Sanctions* are intended to be effective, proportionate and dissuasive. The reasons for imposing *Sanctions* are identified in paragraph 11 of the Sanctions Policy as the following:
- 6.1.1. to declare and uphold proper standards of conduct amongst *Statutory Auditors* and *Statutory Audit Firms* and to maintain and enhance the quality and reliability of future audits;
 - 6.1.2. to maintain and promote public and market confidence in *Statutory Auditors* and *Statutory Audit Firms* and the quality of their audits and in the regulation of the accountancy profession;
 - 6.1.3. to protect the public from *Statutory Auditors* and *Statutory Audit Firms* whose conduct has fallen short of the *Relevant Requirements*; and
 - 6.1.4. to deter *Statutory Auditors* and *Statutory Audit Firms* from breaching the *Relevant Requirements* relating to *Statutory Audit*.
- 6.2. In considering *Sanctions* to be imposed on BDO, Executive Counsel has, in summary, considered the following matters in accordance with the Sanctions Policy.

Nature, seriousness, gravity and duration of the breaches

- 6.3. As a result of the breaches of *Relevant Requirements*, the Audit failed in its principal objective, that is, to obtain reasonable assurance about whether the Financial Statements as a whole were free from material misstatement.
- 6.4. The audit areas relevant to most of the breaches (revenue and profits from the performance of long-term contracts, and going concern) are fundamental to statutory audits of entities such as NMCN and it is of the utmost importance that audit work of this kind is carried out in accordance with *Relevant Requirements*.
- 6.5. The breaches of *Relevant Requirements* were serious and numerous and were pervasive throughout the Audit (especially in relation to the core substantive testing work on contracts).
- 6.6. The breaches of *Relevant Requirements* relate to only one audit year.
- 6.7. The circumstances in which the Audit was carried out, described at paragraphs 3.11 and 3.12 above, were exceptional and presented significant difficulty in conducting the Audit. In respect of the difficulty attributable to the disruptive effects of the COVID-19 pandemic, the relevant UK regulatory authorities sought to assist *Statutory Auditors* in

responding to the disruption. In March 2020 the FRC issued guidance on dealing with the disruption to audit engagements caused by the pandemic. Separately, on account of COVID-19 disruption the Financial Conduct Authority extended the deadline for publication of companies' audited annual financial reports, from four to six months from the end of the financial year, in effect allowing additional time for the preparation of those reports. For the Audit, the Respondents, faced with the circumstances described at paragraphs 3.11 and 3.12, postponed the completion of their work by four weeks.

6.8. Whilst it is not alleged that the Financial Statements were in fact misstated or that the going concern basis used in preparing the FY19 financial statements was in fact inappropriate or subject to material uncertainty, the Respondents did not obtain sufficient appropriate audit evidence to be able to conclude on whether a material uncertainty existed. In aggregate, the breaches, in leading to a failure to obtain reasonable assurance about whether the Financial Statements as a whole were free from material misstatement:

6.8.1. had the potential adversely to affect a significant number of people in the United Kingdom, such as the public, investors or other market users (NMCN's shares were listed on the main market of the London Stock Exchange); and

6.8.2. could have harmed investor, market and public confidence in:

6.8.2.1. the truth and fairness of the financial statements published with audit reports by *Statutory Auditors* or *Statutory Audit Firms*;

6.8.2.2. the standards of conduct in general of *Statutory Auditors* and *Statutory Audit Firms*, and

6.8.2.3. *Statutory Audit* in general.

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

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

Identification of Sanction

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

6.11.1.a financial penalty of £2,000,000 adjusted for the mitigating factor of exceptional cooperation by a reduction of 5% and further discounted for admissions and early disposal by 30% so that the financial penalty payable is

£1,330,000, to be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;

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

6.11.3. a declaration that the Audit Report signed on behalf of BDO did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*.

6.12. In determining the *Sanctions* to be imposed on BDO, Executive Counsel considered whether any further non-financial *Sanction* was required. The identified failings in the FY19 Audit are ones which would clearly indicate the need for Executive Counsel to impose a requirement to take appropriate remedial measures, by way of non-financial Sanction. However, Executive Counsel has taken the following circumstances into account.

6.13. The FY19 Audit was conducted before BDO undertook and implemented a review of its methodology for the audit of companies, like NMCN, whose business is made up of long-term contracts, most notably in the construction and infrastructure sector. BDO's improvement measures in this regard, which are ongoing, form part of a wider remedial programme for the firm's audit practice, necessitated by adverse regulatory findings. The implementation and effectiveness of BDO's remedial measures, which include ones closely relevant to the identified failings in the FY19 Audit, continue to be under active review by the FRC's Supervision division. (Information on these developments has been published by the FRC in its annual reviews of the quality of the performance of statutory audits of public interest entities, most recently those published in July 2025.) In all these circumstances, Executive Counsel does not consider that any further non-financial *Sanction* needs to be imposed under the present *Final Settlement Decision Notice*.

Aggravating and mitigating factors

6.14. There are no aggravating or mitigating factors that have not already been considered in the context of the seriousness of the breaches, save for the level of cooperation provided by BDO during the investigation.

6.15. Paragraph 69 of the Sanctions Policy explains that, since *Statutory Auditors* and *Statutory Audit Firms* are required to cooperate with any investigation under the AEP, only an exceptional level of cooperation will be regarded as a mitigating factor at the point of determining Sanctions. BDO made certain admissions at an early stage which assisted Executive Counsel in reaching the conclusions set out in this *Final Settlement Decision Notice*. Executive Counsel considers that this amounted to an exceptional

level of cooperation provided by BDO which merits a discount of 5% to the amount of financial penalty imposed.

Deterrence

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

Discount for Admissions and Settlement

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

Other considerations

6.18. In accordance with paragraph 47(c) of the Sanctions Policy, Executive Counsel has taken into account the size / financial resources and financial strength of BDO and the effect of a financial penalty on its business and whether any financial penalty would be covered by insurance.

6.19. BDO is the fifth largest audit firm in the UK. In the financial year to 5 July 2024, BDO's UK fee income was £1.02 billion and its audit fee income was £433 million; it had 335 equity partners in 2024.

7. SANCTIONS – MR JONES

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

Nature, seriousness, gravity and duration of the breaches

7.2. The features of the case set out at paragraphs 6.3 to 6.10 above apply equally to Mr Jones.

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

7.4. Mr Jones' senior role is also relevant to the gravity of the breaches as, at the time of the Audit, he had accumulated 26 years' auditing experience, 15 of them as a partner of BDO.

7.5. Mr Jones has no previous adverse disciplinary record.

Identification of Sanction

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

7.6.1. a financial penalty of £75,000 adjusted for the mitigating factor of exceptional cooperation by a reduction of 5% and further discounted for admissions and early disposal by 30% so that the financial penalty payable is £49,875, to be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;

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

7.6.3. a declaration that the Audit report signed by Mr Jones did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*.

7.7. In determining the *Sanctions* to be imposed on Mr Jones, Executive Counsel considered whether any further non-financial *Sanction* was required in respect of Mr Jones. In view of the circumstances set out in paragraph 6.13 above, Executive Counsel determined that none was required.

Aggravating and mitigating factors

7.8. There are no aggravating or mitigating factors that have not already been considered in the context of the seriousness of the breaches, save for the level of cooperation provided by Mr Jones during the investigation.

7.9. For the same reasons as those stated at paragraph 6.15 above in relation to BDO, Executive Counsel considers that Mr Jones has provided an exceptional level of cooperation to the investigation. Accordingly, Executive Counsel has applied a discount of 5% to the financial penalty against Mr Jones.

Deterrence

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

Discount for Admissions and Settlement

7.11. Having taken into account the full admissions by Mr Jones and the stage at which those admissions were made (within Stage 1 of the case in accordance with paragraph 84 of the Sanctions Policy), Executive Counsel determined that a reduction of 30% as to the financial penalty is appropriate.

Other considerations

7.12. Executive Counsel has considered the applicability of paragraphs 47(d) and 50 of the Sanctions Policy as regards Mr Jones.

8. COSTS

8.1. Executive Counsel requires that the Respondents pay Executive Counsel's Costs in this matter in the amount of £904,064. Such Costs shall be paid no later than 28 days after the date of this *Final Settlement Decision Notice*.

Signed:

[Redacted]

JAMIE SYMINGTON

DEPUTY EXECUTIVE COUNSEL

Date: 6 January 2026

APPENDIX 1 – EXTRACTS OF RELEVANT REQUIREMENTS

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

1. Paragraph 15 states:

“The auditor shall plan and perform an audit with professional skepticism recognizing that circumstances may exist that cause the financial statements to be materially misstated. (Ref: Para. A20–A24).”

ISA 230 (Audit Documentation)

2. Paragraph 8 states:

“The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand: (Ref: Para. A2–A5, A16–A17)

(a) The nature, timing and extent of the audit procedures performed to comply with the ISAs (UK) and applicable legal and regulatory requirements; (Ref: Para. A6– A7)

(b) The results of the audit procedures performed, and the audit evidence obtained; and

(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions. (Ref: Para. A8–A11)”

ISA 315 (Identifying and Assessing the Risks of Material Misstatement Through Understanding of the Entity and Its Environment)

3. Paragraph 12 states:

“The auditor shall obtain an understanding of internal control relevant to the audit. Although most controls relevant to the audit are likely to relate to financial reporting, not all controls that relate to financial reporting are relevant to the audit. It is a matter of the auditor’s professional judgment whether a control, individually or in combination with others, is relevant to the audit. (Ref: Para. A50–A73)”

4. Paragraph 13 states:

“When obtaining an understanding of controls that are relevant to the audit, the auditor shall evaluate the design of those controls and determine whether they have been implemented, by performing procedures in addition to inquiry of the entity’s personnel. (Ref: Para. A74–A76)”

ISA 330 (The Auditor’s Responses to Assessed Risks)

5. Paragraph 5 states:

“The auditor shall design and implement overall responses to address the assessed risks of material misstatement at the financial statement level. (Ref: Para. A1–A3)”

6. Paragraph 6 states:

“The auditor shall design and perform further audit procedures whose nature, timing, and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level. (Ref: Para. A4–A8)”

7. Paragraph 7(b) states:

“In designing the further audit procedures to be performed, the auditor shall:

(a) [...]

(b) Obtain more persuasive audit evidence the higher the auditor’s assessment of risk. (Ref: Para. A19)”

8. Paragraph 8 states:

“The auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls if:

(a) The auditor’s assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively (that is, the auditor intends to rely on the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures); or

(b) [...]”

9. Paragraph 21 states:

“If the auditor has determined that an assessed risk of material misstatement at the assertion level is a significant risk, the auditor shall perform substantive procedures that are specifically responsive to that risk. When the approach to a significant risk consists only of substantive procedures, those procedures shall include tests of details. (Ref: Para. A53)”

ISA 500 (Audit Evidence)

10. Paragraph 6 states:

“The auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence. (Ref: Para. A1–A25)”

11. Paragraph 10 states:

“When designing tests of controls and tests of details, the auditor shall determine means of selecting items for testing that are effective in meeting the purpose of the audit procedure. (Ref: Para. A52–A56)”

ISA 530 (Audit Sampling)

12. Paragraph 9 states:

“The auditor shall perform audit procedures, appropriate to the purpose, on each item selected.”

ISA 540 (Auditing Accounting Estimates, Including Fair Value Accounting Estimates and Related Disclosures)

13. Paragraph 13(b) states:

“In responding to the assessed risks of material misstatement, as required by ISA (UK) 330 (Revised July 2017), the auditor shall undertake one or more of the following, taking account of the nature of the accounting estimate: (Ref: Para. A59–A61)

(a) [...]

(b) Test how management made the accounting estimate and the data on which it is based. In doing so, the auditor shall evaluate whether: (Ref: Para. A68–A70)

(i) The method of measurement used is appropriate in the circumstances; and (Ref: Para. A71–A76)

(ii) The assumptions used by management are reasonable in light of the measurement objectives of the applicable financial reporting framework. (Ref: Para. A77–A83)

(c) [...]

(d) [...]

ISA 570 (Going Concern)

14. Paragraph 12D-1 states:

“In accordance with ISA (UK) 200 (Revised June 2016),3a the auditor shall maintain professional skepticism throughout the audit and in particular when reviewing future cash flow relevant to the entity’s ability to continue as a going concern.”

15. Paragraph 13 states:

“In evaluating management’s assessment of the entity’s ability to continue as a going concern, the auditor shall cover the same period as that used by management to make its assessment as required by the applicable financial reporting framework, or by law or regulation if it specifies a longer period. If management’s assessment of the entity’s ability to continue as a going concern covers less than twelve months from the date of the financial statements as defined in ISA (UK) 560, the auditor shall request management to extend its assessment period to at least twelve months from that date. (Ref: Para. A11–A13)”

16. Paragraph 16 states:

“If events or conditions have been identified that may cast significant doubt on the entity’s ability to continue as a going concern, the auditor shall obtain sufficient appropriate audit evidence to determine whether or not a material uncertainty exists related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern (hereinafter referred to as “material uncertainty”) through performing additional audit procedures, including consideration of mitigating factors. These procedures shall include: (Ref: Para. A16)

(a) Where management has not yet performed an assessment of the entity’s ability to continue as a going concern, requesting management to make its assessment.

(b) Evaluating management’s plans for future actions in relation to its going concern assessment, whether the outcome of these plans is likely to improve the situation and whether management’s plans are feasible in the circumstances. (Ref: Para. A17)

(c) Where the entity has prepared a cash flow forecast, and analysis of the forecast is a significant factor in considering the future outcome of events or conditions in the evaluation of management’s plans for future actions: (Ref: Para. A18–A19)

(i) Evaluating the reliability of the underlying data generated to prepare the forecast; and

(ii) Determining whether there is adequate support for the assumptions underlying the forecast.

(d) Considering whether any additional facts or information have become available since the date on which management made its assessment.

(e) Requesting written representations from management and, where appropriate, those charged with governance, regarding their plans for future actions and the feasibility of these plans. (Ref: Para A20)”

ISA 600 (Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors))

17. Paragraph 18(b) states:

“The group engagement team shall obtain an understanding that is sufficient to:

(a) [...] ; and

(b) Assess the risks of material misstatement of the group financial statements, whether due to fraud or error. (Ref: Para. A30–A31)”

18. Paragraph 28 states:

“For components that are not significant components, the group engagement team shall perform analytical procedures at group level. (Ref: Para. A50)”