Online comparisons volume

Post Publication Comment Wednesday, 20 November 2019

Current 2019 update and issues (for other cases see)**

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All these downloads and others can be found here:
http://www.fin-rep.org/which-book/financial-failures-scandals-from-enron-to-carillion/

* see (downloadable)
http://www.fin-rep.org/which-book/financial-failures-scandals-from-enron-to-carillion/
** see (downloadable)
http://www.fin-rep.org/wp-content/uploads/book1/1-Current-Audit-Market-2019.pdf

Current 2019 update and issues (for other cases see**)/Continued

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More cases to be discussed during from the back end of 2018.

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Overview of some cases - another perspective

An interesting article in the Guardian reviewed some of the recent cases of failure or financial problems[1]. The cases examine are:

Patisserie Valerie (auditor: GT)

With this company there seem to be secret loans and fake invoices. What seemed to be a profitable chain looks as if it actually wasn't. Probably loss making a result from too fast expansion (plus 20 stores a year) and too weak financial controls and governance. Some would say the famous guru Luke Johnson should 'eat his heart out'. That however is not being very charitable. We think it is case of too fast expansion and too little control and governance. See separate file**.

This is discussed separately in a download. Our view is that, ostensibly, it seemed to be a case of fast expansion without financial controls, with too little governance and allegedly flawed auditing. FRC investigation and SFO fraud impossibility. So the worst scenario is that possibly a senior management effort to conduct fraud and falsify the accounts – making them seem gloriously profitable when the reality was probably the reverse.

Carillion (auditor KPMG)

This is discussed in Volume 2 over several chapters. It is a case of management failure as well as weakness in the auditing – too ready to agree with management. See below For KPMG suspending partners. .

Conviviality (auditor KPMG)

This is dealt with in the book. As with Patisserie Valerie a case of expansion without adequate internals controls. There were errors in spreadsheets and a misplaced and forgotten £30m tax bill. The FRC may find other issues during it investigation.

Rolls-Royce (auditor KPMG)

We did not deal with this case. To us it was a simple case of something closer to bribery – a commercial fact which is common and expected in the Middle East. However Jolly makes the point that:

> Rolls-Royce agreed in 2017 to pay £671m in penalties to settle long-running corruption allegations in a deferred prosecution agreement. Months later, the FRC said it had started investigating KPMG's conduct in relation to its audit of Rolls-Royce's financial statements between 2010 and 2013.

Sports Direct (ex-GT and now ?)

Discussed on page 35 at length.

AssetCo

Grant Thornton (GT) was ordered to pay £21m damages to AssetCo, a fire engine supplier, for negligence in 2019. It followed a £2.3m fine by the FRC in 2017. Downloadable file.

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[1] Jolly, J., 2019, Decline in quality': auditors face scrutiny over string of scandals: In recent years, major audit firms have failed to spot key problems. We list the most prominent cases, The Guardian, 1 February 2019. Available at:
https://www.theguardian.com/business/2019/feb/01/decline-in-quality-auditors-face-scrutiny-over-string-of-scandals
Accessed February 2019

The latest cases in 2019

Bank of New York Mellon [BNY Mellon] (KPMG)

We have some sympathy for KPMG as they seem to be the one firm, out of the Big Four, who seem to be most keen to change and reform. That said after the £10m fines awarded earlier in the month of May along comes a proposal to fine KPMG with a record-breaking fine of £12.5m over their work connected with a long-standing case of Bank of New York Mellon. The FRC said the penalty would be justified because of the size of the US bank's operations and truly exceptional seriousness of the abuse.

The FT reported this case, which has yet to be finalised[2]:

> Due to the disagreement over the size of the fine an independent disciplinary tribunal will decide the appropriate sanction after the three-day hearing. The largest sanction imposed by the FRC to date was the £6.5m penalty PwC paid last year for misconduct on its audit of retailer BHS.
>
> The latest case relates to reports produced by KPMG on how BNY Mellon complied with rules on safeguarding client assets, which were submitted to the UK's Financial Conduct Authority in 2011. The work, which referred to about £1tn of client assets held in custody by the US bank, fell short of UK standards designed to protect customers.
>
> ….
>
> BNY Mellon itself was fined a record £126m by the FCA in 2015 for failing to comply with rules that required customer accounts at its London branch and its international unit to be kept properly ringfenced between 2007 and 2013.

So there was the Co-op Bank fine of £5m and then the insurance fine £6 m. There is of course the Carillion failure which is still be adjudicated.

> Last June, the FRC criticised the company for an "unacceptable deterioration" in the quality of its audit work for large listed companies in the UK. KPMG is also under investigation by the FRC for its work at collapsed UK contractor Carillion, which was audited by the firm for 19 years[3].

Then in 2018 KPMG was also fined twice by the FRC last year, receiving a £2m penalty over its work for retailer Ted Baker[4] and a £3m fine relating to its work for insurance software firm Quindell[5].

For more information on the scandal see this article by The Guardian[6].

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[2] Morris, S., KPMG faces record £12.5m fine for bungled bank reports, *Financial Times*, 21 May 2019.
Available at:
https://www.ft.com/content/3a0b4002-7bd5-11e9-81d2-f785092ab560
Accessed May 2019.
[3] Ibid.
[4] See
http://www.fin-rep.org/wp-content/uploads/book2/1-Current-2019-cases-and-issues.pdf
[5] As above.
[6] Press Association, Bank of New York Mellon fined £126m by regulator for 'failings', The Guardian, 15 April 2015.
Available at:
https://www.theguardian.com/business/2015/apr/15/bank-of-new-york-mellon-fined-126m

BHS, Arcadia and Sir Philip Green (auditor: PwC)

This was discussed in the book. BHS and the holding group, Taveta, are private companies. It is a case of audit failure and sharp business practices by a group headed up by Sir Philip Green. His wife who resides in Monaco, are the controlling shareholders and use this base in our view as a tax haven.

Sir Philip Green is in possible trouble again with new claims of sexual harassment, though in a milder form. Though these allegations (misdemeanours) were charged in the US[7]. However, the parent company, Arcadia (and its parent Taveta Investments), is in what may be termed another financial crisis. No tales of wrongdoing however. What is at the root cause of the group's decline is online trading and a switch in fashion tastes. Perhaps no enough investment with too much taken out of the business[8].

The latest is that Topshop lost £300m in 2018 and that Taveta and Arcadia lost around $170m. Interestingly Taveta was split in to as second company Taveta No 2 we think in order to facilitate the sale of part of the Arcadia empire.

Not really a financial scandal except that it raises questions about the TPR once again which was seen to be almost without any real teeth in the case of BHS – despite Sir Phi
lip's claimed generosity.

The Sunday Tines (Oliver Shah again) reported[9]

> The future of Sir Philip Green's Topshop empire is on a knife-edge as the pensions authorities threaten to kill a controversial restructuring to close stores and cut rents.
> A source close to the Pension Protection Fund (PPF), the lifeboat for final salary schemes, said it was prepared to vote against a company voluntary arrangement (CVA) for Arcadia Group.
> Green hopes to win approval for the closure of almost 50 stores and rent cuts on a further 200 on Wednesday, but needs the support of the Pensions Regulator and the PPF, given the £744m "buyout" deficit in Arcadia's funds. He has offered a package worth a total of £360m in return for long-term cuts to Arcadia's contributions. The regulator is reported to be holding out for a further £50m in cash.

Accessed May 2019.
[7] BBC, Sir Philip Green charged with misdemeanour assault in US, BBC, 31 May 2019.
Available at:
https://www.bbc.co.uk/news/uk-48480365
Accessed June 2019.
[8] As suggested by: Eley, J., What went wrong at Philip Green's Arcadia?, *Financial Times*, 24 May 2019.
Available at:
https://www.ft.com/content/7d647930-7d52-11e9-81d2-f785092ab560
Accessed May 2019
[9] Shah, O., Watchdog threatens to topple Sir Philip Green's Arcadia, *The Sunday Times*, 2 June 2019.
Available at:
https://www.thetimes.co.uk/edition/business/watchdog-threatens-to-topple-sir-philip-greens-arcadia-gqv68k7z0
Accessed June 2019.

BHS, Arcadia and Sir Philip Green (auditor: PwC)/Continued

However, Oliver Shah went on to discuss this development in his resturing and pensions deficit reduction plans[10]:

> Approval from the pensions authorities will be crucial, given the deficit of up to £744m in Arcadia's funds. Green has offered £185m in property and loan notes, plus £175m in various payments. The regulator is said to want a further £50m in cash.
>
> Green, an inveterate gambler, is haggling until the eleventh hour. He is betting that despite the embarrassment of BHS, the Pensions Regulator will not dare block the company voluntary arrangement (CVA) and send Arcadia into administration, triggering chaos. The Pension Protection Fund, the lifeboat that exercises the vote, is insisting it will stand tall on what is an important matter of precedent.
>
> As much as it pains me to say it, I suspect Green will sweeten the deal slightly at the last minute, allowing the regulator to wave it through without losing face. The CVA will kick the can down the road and both sides will hope that when Arcadia's inevitable collapse comes in a few years' time, gilt yields will have risen and the deficit shrunk.
>
> It's a cynical game to play with 9,400 pensions, but at least that outcome would keep many of Arcadia's staff in work for longer. Whether its owner keeps his liberty is another matter.

And, being true to form, Oliver Shah was correct. Sir Philip has offered to put in a further £25m (and possibly there is more bargaining room) and wants to close 50 stores as well as reducing rents through a CVA[11]:

> Sir Philip's wife, Lady Tina Green, who is Arcadia's main shareholder, had already offered to put in £100m of funding over the next three years to help plug the pension deficit, which is around £750m.
>
> It was part of a £360m package to make up for planned reductions in contributions resulting from the restructuring deal.
>
> The Pension Regulator said this wasn't sufficient.
>
> Arcadia currently has more than 560 shops across the UK and Ireland, and employs 22,000 staff.
>
> It has already shut 200 of its UK stores over the past three years amid intensifying competition from a crop of more contemporary "fast fashion" retailers ranging from High Street chains such as Zara and H&M to pure online players like Asos.
>
> Arcadia has also faced the same problems as other High Street retailers, including rising business rates and labour costs, too many unprofitable stores and inflexible leases that make it hard to close failing shops.

Continued

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[10] Shah, O., William Hill needs an elegant escape plan, *The Sunday Times*, 2 June 2019.
Available at:
https://www.thetimes.co.uk/article/william-hill-needs-an-elegant-escape-plan-xl87zfb2r
Accessed June 2019.

[11] BBC, Philip Green agrees £25m pension deal ahead of key vote, BBC, 4 May 2019.
Available at:
https://www.bbc.co.uk/news/business-48510300
Accessed June 2019.

BHS, Arcadia and Sir Philip Green (auditor: PwC)/Continued

So with £385 contribution to the pension's deficit, The Pensions Regulator is on side. Bu the meeting to agree the rent reductions on the 5Th of June did not go to plan. It has been postponed which does not look so good for Arcadia Group. Some the landlords believe that Sir Philp could put more money of his own into the restructuring deal.

By 11th June 2019, a deal had been agreed. The group was advised by insolvency experts at Deloitte and property consultants GCW. The Sir Philp's Arcadia group managed to avoid (as reported) collapse after securing backing for its controversial restructuring plan. Arcadia needed and received agreement from 75% of its unsecured creditors (including landlords, suppliers, HMRC and Arcadia's pension scheme) to vote for its CVA. Arcadia received this support and will close 23 of stores immediately and a further 25 to 30 later. Rents will be cut by up to 70 per cent for 194 others[12].

So despite all the delays and criticisms, Sir Philip survives another day. Of closure during this period of negotiation Green family offered to put up about £9.5m a year over three years (say up to £30m in total), so that rent cuts for landlords would be reduced to 25%-50% from the 30%-70% previously planned. That move finally won over sufficient creditors. The multiple CVAs, apart from up to 23 store closures and rent cuts on almost 200 stores, are part of a wider restructure in which about 25 more UK stores will close as the property arms of Miss Selfridge and Evans are put into administration.

We believe he will put renewed effort into revitalising the business including:

- More closures than the original 50 stores
- A greater and vibrant online presence with multiple online tie-ups
- A renewed and more modern and changeable fashion line
- Some new purchases and new business relationships in both online and off-line synergistic partners and/or rivals
- M&S: it remains to be seen whether Sir Phillip will rekindle his lifelong desire tot makeover this traditionally British store which has also run into problems. We give it evens.

[12] Eley, J., and Evans, J., Arcadia avoids collapse as landlords back rescue plan, *Financial Times*, 12 June 2019. Available at:
https://www.ft.com/content/72647010-8d03-11e9-a24d-b42f641eca37
Accessed June 2019.

BHS, Arcadia and Sir Philip Green (auditor: PwC)/Continued

Our views are reinforced by an article in The Guardian:[13]

> But retail industry experts said that rent cuts and store closures would not be enough to guarantee Arcadia's long-term survival.
>
> Richard Lim, the chief executive of consultancy Retail Economics, said: "There's still a huge battle ahead. It's not just fewer stores that are needed to ensure Arcadia's long-term survival. It ultimately needs a leaner business model, including less staff and fewer brands, as well as investment into its identity and customer experience to fend off online and value retailers."
>
> Chloe Collins, a senior retail analyst at research firm GlobalData, said Arcadia would need to invest much more than it had so far promised in updating its stores and online services if it was to compete effectively with the likes of Asos, Boohoo.com and H&M.

BHS October/November 2019

Sir Philip Green untangles Topshop and Topman logistics from Arcadia Group[14] as part of its strategy to reduce cost in its bid for survival.

Sir Philip Green in race to pay back £300m loan on flagship Oxford Street store[15]

Continued

[13] Butler, S., Philip Green's Arcadia avoids administration as rescue deal backed. *The Guardian*, 12 June 2019.
Available at:
https://www.theguardian.com/business/2019/jun/12/philip-green-arcadia-avoids-administration-as-rescue-deal-backed
Accessed June 2019.

[14] Chambers, S., Sir Philip Green untangles Topshop and Topman logistics from Arcadia Group, *The Times*, 27 October 2019.
Available at:
https://www.thetimes.co.uk/article/sir-philip-green-untangles-topshop-and-topman-logistics-from-arcadia-group-ng9msk33g
Accessed October 2019.

[15] Chambers, S., Sir Philip Green in race to pay back £300m loan on flagship Oxford Street store, *The Times*, 27 October 2019.
Available at:
https://www.thetimes.co.uk/article/sir-philip-green-untangles-topshop-and-topman-logistics-from-arcadia-group-ng9msk33g
Accessed October 2019.

BT (auditor PwC)

This involves the Italian subsidiary and for us, the joke about all companies having two sets of books might have an element of truth. So we did not dwell on this case. However, Jolly reports:

> BT announced in 2017 that it had uncovered inappropriate behaviour at its Italian subsidiary, which misstated profits by more than £500m. The FRC is investigating PwC over its audit of the Italian division. In 2017 BT said KPMG would replace PwC as its auditor, ending a relationship that had lasted more than three decades.

That said Matt Oliver goes further in his reporting and critique[16]:

> BT bosses in London embroiled in a £500 million accounting fraud scandal failed to challenge the accounts, an internal probe found. There was a 'serious breakdown of accounting processes and controls' at the company's Italian arm and a 'loss of balance sheet integrity', the review seen by the Mail found. It raises serious questions about how thoroughly bosses in London scrutinised figures from BT Italia before the fraud was uncovered. Last night an accounting expert said the UK authorities needed to launch fresh investigations into the scandal. It comes just days after police in Italy released an explosive report suggesting bosses in London urged staff in Italy to use 'aggressive, anomalous and knowingly wrong accounting practices'.
>
> The company has consistently maintained that the accounting scandal was a local matter – despite the internal report being published in January 2017. The 2017 annual report, published four months later, said the fraud 'was not identified by our monitoring controls' and went 'undetected for a number of years'.Prem Sikka, a professor of accounting who has advised the Labour Party, said: 'BT's Italian subsidiary was submitting numbers to someone in London that whole time. The review raises questions which now need to be investigated by UK authorities.' BT's internal review of the Italian fraud scandal was produced by KPMG in January 2017 but was never published. The findings resulted in a £530 million write-down and a share slump that wiped £8 billion off the company's market value. The report said staff at BT Italia sought to artificially inflate the subsidiary's earnings with a complex web of fraudulent transactions. Italian staff made 'misrepresentations' to BT Group and its auditors at the time, PwC, it added.

Continued

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[16] Oliver, M., 2019, British chiefs in firing line over BT accounting fraud scandal in Italy, This is Money, *Daily Mail*, 28 April 2019. Available at:
https://www.thisismoney.co.uk/money/markets/article-6969797/British-chiefs-firing-line-BT-accounting-fraud-scandal-Italy.html
Accessed April 2019

BT (auditor PwC)/Continued

However, BT seems to have calmed the fear of investors and has launched into a radical reorganization and reduction of its international arm. This has led to a sell-off of its Irish division with a possible auction for its £400 million Irish arm.

Meanwhile an internal investigation leaked to the Daily Mail[17] with the British directors being criticised. The so-called £500 m accounting fraud scandal had insufficient challenges to the accounts, according to the Mail's report on the internal investigation. The Daily Mail found that there was a serious breakdown of accounting processes and controls at the company's Italian arm and a loss of balance sheet integrity.

Carillion

See page 16, 17 and 18.

Cineworld's affair (June 2019)

This may be much ado about nothing. But Louisa Clarence-Smith of the Times thinks different [18]:

> KPMG resigned as auditor of **Cineworld** after 15 years, sending shares in the cinema operator down.
>
> Although Cineworld framed the change in its auditor as good corporate governance, a resignation letter from KPMG hinted at a disagreement over fees. "The reason connected with our ceasing to hold office is the holding of a competitive tender for the audit, in which we declined to participate as we did not consider that it was likely that we would be able to agree acceptable commercial terms," the firm said.
>
> PWC, another Big Four accountant, was appointed as Cineworld's auditor with immediate effect.
>
> KPMG was paid £600,000 to audit Cineworld in 2017 and took a further £1.3 million from the group for "other advisory services", according to its annual report. The year before, KPMG was paid £600,000 for its audit but received just £400,000 in fees for other advice.

Continued

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[17] Oliver, M., British chiefs in firing line over BT accounting fraud scandal in Italy, *This is Money*, 28 April 2019.
Available at:
https://www.thisismoney.co.uk/money/markets/article-6969797/British-chiefs-firing-line-BT-accounting-fraud-scandal-Italy.html
Accessed April 2019

[18] Clarence-Smith, L., Cineworld's break-up with auditor is a real tearjerker, The Times, 21 June 2019.
Available at:
https://www.thetimes.co.uk/article/cineworld-s-break-up-with-auditor-is-a-real-tearjerker-pkvzszvwx?region=global
Accessed June 2019

Co-operative Bank plc (KPMG)

KPMG has been fined £5m (reduced to £4m) and severely reprimanded by the UK accountancy watchdog for its audit of the Co-op Bank in 2009 when the bank merged with Britannia Building Society[19].

The FT reported this succinctly[20]:

> The fines relate to the belated discovery of a £1.5bn capital black hole after the Co-op Bank's 2009 acquisition of Britannia Building Society. The FRC said the audit of Britannia's commercial loan book and a series of securities, known as Leek Notes, which were acquired from Britannia, fell below the standards expected.
> "The misconduct in respect of these two areas included: failures to obtain sufficient appropriate audit evidence; failures to exercise sufficient professional scepticism and a failure to inform Co-op Bank that the disclosure of the expected lives of the Leek Notes in the financial statements was not adequate," the FRC said.

This was a bad week for KPMG, along with the fines for Equity Syndicate Management.

Continued

[19] FRC, Sanctions in relation to the 2009 audit of The Co-operative Bank plc, 8 May 2019.
Available at:
https://www.frc.org.uk/news/may-2019/sanctions-in-relation-to-the-2009-audit-of-the-co
Accessed May 2019.
[20] Gorgiadis, P., and Megaw, N., KPMG reprimanded and fined £5m over Co-op Bank audit, *Financial Times*, 8 May 2019.
Available at:
https://www.ft.com/content/00f93c2c-715a-11e9-bf5c-6eeb837566c5
Accessed May 2019.

Danske Bank

Of course, some of the latest scandals occur in Europe. One of the latest scandals occurred in Denmark involving Dances Bank[21]:

> The Danish government has reported Big Four auditor EY to the domestic fraud squad to investigate whether the firm broke money laundering rules when it audited Danske Bank in 2014.
>
> The Danish Business Authority, a government agency, said it had conducted its own investigation into EY's 2014 audit of Danske and found the firm had discovered information about potential money laundering issues at the bank.
>
> The firm should have made further inquiries and reported the matter to the authorities at the time, according to the business authority. It said on April 12 it had asked the Danish state prosecutor to launch a police investigation into whether EY violated laws against money laundering and terrorist financing.
>
> Danske's money laundering scandal started in 2007 and stretched until 2015, with €200 billion of non-resident money — much of it suspicious and from Russia — passing through its Estonian branch during the period.
>
> The referral to Denmark's fraud investigators is a fresh blow to EY and the wider audit industry, which has come under heavy criticism during the past 18 months following a series of high profile corporate scandals involving the Big Four firms.

This case will continue to release a series of revelations.

Continued

[21] Milne, R., and Marriage, M., Danish police to investigate EY over its Danske Bank audit, Financial Times, 12 April 2019.
Available at:
https://www.ft.com/content/e4acb586-5d17-11e9-939a-341f5ada9d40
Accessed April 2019

Equity Syndicate Management

The FT summarises this:[22]

> KPMG has been fined £6m and issued with a severe reprimand by the UK accounting watchdog over its audit of insurer Equity Syndicate Management over 10 years ago.
> Britain's Financial Reporting Council said on Tuesday that it had also issued sanctions against KPMG partner Mark Taylor, as well as former partner Anthony Hulse and Douglas Morgan, a former director of the insurer.
> Mr Taylor has been fined £100,000, severely reprimanded and agreed to the imposition of a requirement to have a second partner review his audits until the end of 2020.
> Mr Hulse has been fined £100,000 and also received a severe reprimand, while Mr Morgan has been excluded from membership of the Chartered Institute of Management Accountants for two years.

The details of what went wrong are outlined in the FRC website[23]. A copy of the report can be downloaded[24].

Continued

[22] Marriage, M., 2019, KPMG hit with £6m fine over insurance audit, Financial Times, 30 April 2019.
Available at:
https://www.ft.com/content/035651b2-6b1a-11e9-a9a5-351eeaef6d84
Accessed May 2019

[23] FRC, 2019, Sanctions against KPMG and others in relation to Equity Syndicate Management Limited, 30 April 2019.
Available at:
https://www.frc.org.uk/news/april-2019/sanctions-against-kpmg-and-others-in-relation-to-e
Accessed May 2019

[24] FRC, Disciplinary Tribunal Report against KPMG and others over Equity Syndicate Management Limited, 14 May 2019.
https://www.frc.org.uk/getattachment/ad7e2e49-9bdb-4d93-af19-87ca37f946b6/Report-of-the-Disciplinary-Tribunal-re-sanctions-against-KPMG-re-Equity-Syndicate-Management-Limited.pdf

HBOS (auditor KPMG)

Although this was discussed in the book, KPMG was cleared of any wrongdoing over its auditing of HBOS, which was rescued by Lloyds during the height of the 2008 crisis (with some government help and direction), after accounting regulators concluded the accountancy firm could not have foreseen the bank's problems[25]. However, the FT now reported[26] that:

> The British audit regulator has been accused of brushing off a whistleblower who came forward in April 2017 with information that HBOS had significantly understated the loan loss provisions in the bank's 2007 figures.
>
> Rob Kennedy, 57, worked on the audit of the bank's corporate division just before the financial crisis, helping to compute the division's general provision against expected loan losses. He told the Financial Reporting Council that the figure had been slashed after the models it employed threw up a figure that was unacceptably high to his boss.
>
> The contentious 2007 audit has been the study of two FRC reviews. Mr Kennedy's approach came when the FRC was conducting the second one, examining the work done by the bank's external auditor KPMG over concerns that it had underplayed the scale of HBOS's financial problems. The 2007 figures were used to support a £4bn rights issue launched in April 2008. When this failed to halt the bank's slide, HBOS subsided under £40bn of losses, having later to be rescued its bigger rival Lloyds Banking Group.
>
> The watchdog concluded in September 2017 that the audit "did not fall significantly short of the standards reasonably to be expected" and that KPMG's assessment of the bank's health in 2008 "was not unreasonable at the time". It followed a review into the bank's loan loss provisioning that concluded there were no reasonable grounds to suspect misconduct and therefore no need for a full investigation.

Continued

[25] Treanor, J., 2017, KPMG cleared by watchdog in HBOS audit investigation: FRC rules out wrongdoing by accountancy firm in reviewing bank's accounts before financial crisis, The Guardian, 22 September 2017.
Available at:
https://www.theguardian.com/business/2017/sep/19/kpmg-cleared-in-hbos-audit-investigation
Accessed December 2017

[26] Ford, J., and Marriage, M., 2019, UK audit regulator accused of brushing off HBOS whistleblower: Rob Kennedy told the Financial Reporting Council the bank slashed its provisions, *Financial Times*, 5 February 2019.
Available at:
https://www.ft.com/content/ef9c01c8-2963-11e9-88a4-c32129756dd8
Accessed February 2019

Interserve

The background to Interserve, a Carillion type services comply, The FRC commenced an investigation into the audit work by GT of Interserve for the years 2015, 2016 and 2017. The investigation will be conducted under the Audit Enforcement Procedure[27]. Thus investigation into GT's audit of Interserve was initiated after this UK government contractor collapsed into administration in March 2019, wiping out the shareholders and further damaging the reputation of the outsourcing sector.

The BBC summarised the fast track packaged sale under administration[28]:

> It comes after shareholders rejected a rescue deal for the company, which has 45,000 UK staff, and 68,000 globally. Under a pre-arranged agreement, administrators EY were installed and the assets moved immediately to a group controlled by Interserve's lenders.
> EY was appointed under a so-called pre-pack administration, an insolvency procedure in which a company arranges to move its assets to a another owner before administrators are officially appointed.
> The lenders who are now in control of Interserve Group include banks RBS and HSBC, and investors Emerald Asset Management and Davidson Kempner Capital.

The FT summarised the situation as[29]:

> Interserve, which employs 65,000 people globally, is the third major UK outsourcing company in the past two years where audits have been scrutinised by the Financial Reporting Council. Interserve was taken into the hands of its creditors in March after warning that it would run out of cash to pay staff and suppliers by the end of the month.
>
> Although the company suspended dividends in February 2017 it was criticised last year for paying chief executive Debbie White £525,890 for four months' work at the end of 2018, with questions raised over whether her 125 per cent bonus was justified.

[27] FRC News, 2019, Investigation in connection with the audit of the financial statements of Interserve Plc, *FRC,* 11 April 2019.
Available at:
https://www.frc.org.uk/news/april-2019/investigation-in-connection-with-the-audit-of-the
Accessed April 2019
[28] BBC, 2019, Interserve: UK contractor completes fast-track sale, BBC News, 15 March 2019.
Available at:
https://www.bbc.co.uk/news/business-47582406
Accessed April 2019
[29] Marriage, M., 2019, UK regulator opens probe into Grant Thornton's audit of Interserve, Financial Times, 11 April 2019.
Available at:
https://www.ft.com/content/1364e832-5c21-11e9-9dde-7aedca0a081a
Accessed April 2019

Interserve/Continued

> Interserve's advisers, which include Grant Thornton, received £90m in fees over the past 12 months — more than the stock market value of the company before it collapsed. Interserve is already being investigated by the Financial Conduct Authority, the financial services regulator, over the accuracy of statements it made between July 2016 and February 2017.

KPMG slammed with £40m fine for changing audit results in US (June)

This is the largest fine ever for the US and worldwide[30]:

> The Securities and Exchange Commission has charged KPMG LLP in the US with altering past audit work after receiving stolen information about inspections of the firm that were conducted by the Public Company Accounting Oversight Board (PCAOB).
> The SEC's order also found that numerous KPMG audit professionals cheated on internal training exams by improperly sharing answers and manipulating test results.
> KPMG agreed to settle the charges by paying a $50m (£40m) penalty and complying with a detailed set of undertakings, including retaining an independent consultant to review and assess the firm's ethics and integrity controls and its compliance with various undertakings.
> 'High-quality financial statements prepared and reviewed in accordance with applicable accounting principles and professional standards are the bedrock of our capital markets. KPMG's ethical failures are simply unacceptable,' said SEC chairman Jay Clayton. 'The resolution the enforcement division has reached holds KPMG accountable for its past failures and provides for continuing, heightened oversight to protect our markets and our investors.'
> 'The breadth and seriousness of the misconduct at issue here is, frankly, astonishing,' said Steven Peikin, co-director of the SEC's enforcement division. 'This settlement reflects the need to severely punish this sort of wrongdoing while putting in place measures designed to prevent its recurrence

Continued

[30] White, S., KPMG slammed with £40m fine for changing audit results in US, *Accountancy Daily*, 3 June 2019. Available at:
https://www.accountancydaily.co/kpmg-slammed-ps40m-fine-changing-audit-results-us
Accessed June 2019

KPMG suspends Carillion audit partner and three others (Feb 2019)

To some extent this reinforces our conclusions in this volume of the series.

As reported in Accountancy Age31 KPMG has suspended Peter Meehan, the audit partner for Carillion, and three other members of staff after discovering issues with documentation provided to the FRC's audit quality review (AQR) of the company in 2017:

> A KPMG spokesperson said: 'Over the past year, we have been performing a thorough review of the firm's audit of Carillion. Our investigation included the audit team's response to the FRC's AQR undertaken during 2017, which looked at aspects of the 2016 audit.
>
> 'Concerns were identified in connection with a small number of documents provided to the FRC's team during the routine AQR. On discovery of this information, we immediately reported our findings to the FRC.
>
> 'It is important to note that this took place after the signing of the audit opinion and we have not identified any evidence or indication that it had any impact on the audit conclusions of Carillion.
>
> 'We are taking this matter extremely seriously and have engaged outside legal counsel to conduct an independent investigation into the circumstances of the AQR and the conduct of the individuals involved.
>
> 'We acted swiftly and decisively and will continue to take all necessary steps to deal with this, including cooperating fully with the FRC.'

KPMG faces lawsuit threat over Carillion audit (August 2019)

The FT reported that[32]:

> KPMG faces the threat of a legal challenge from the UK agency tasked with unwinding Carillion, the outsourcer that collapsed last year, over allegations that the Big Four accountancy group's audit of the company was negligent.
>
> US law firm Quinn Emanuel has been hired to pursue a legal case by the official receiver, a civil servant employed by the Insolvency Service on behalf of Carillion's creditors, and PwC, the special manager of the company's liquidation, according to two people familiar with the matter.
>
> Quinn Emanuel was first retained late last year, but the legal challenge has gathered momentum in recent weeks after the firm appointed barristers. It is now preparing to notify KPMG that it plans to file claims at the High Court, the people said.

Continued

[31] Sweet, P., KPMG suspends Carillion audit partner, *Accountancy Age*, 21 January 2019. Available at:
https://www.accountancydaily.co/kpmg-suspends-carillion-audit-partner
Accessed January 2019

[32] Kinder, T., KPMG faces lawsuit threat over Carillion audit, *Financial Times*, 4 August 2019. Available at:
https://www.ft.com/content/277dfdce-b6ec-11e9-96bd-8e884d3ea203
Accessed August 2019.

Kingman on the Carillion (Jan 2019)

As we know Kingman, responsible for reviewing the performance of the UK's FRC said that the body should be wound up and replaced with new regulator led by a "credible" leadership team. In an article[33] Kingman claimed that:

> "It will take time… because building credibility does take time, but we have seen other regulators in this country come on that journey, so I see no reason why this one cannot."
> Sir John added that the political appetite to deal with the issues highlighted in his report at the FRC was strong.
> He said: "I have had very positive engagement with the Secretary of State in particular. He took a very close interest in the review as it progressed… The sense I have from him is that he wants to make really serious progress in this area; he wants to see a new and more effective regulator."
> Quizzed about the future regulation of the audit profession following the Carillion collapse, Sir John said any new regulator must have the power to "go in and have a look" where there were concerns about the financial health of a company.
> The call for a more proactive regulator effectively signals the end of the era of self-regulation by the audit and accounting profession in the UK.

Update on FRC investigations in relation to Carillion[34] (Jan 2019)

The bottom line is that this report is going to take some time to complete –even under the FRC's new faster rules. The FRC says it has obtained and is analysing very significant quantities of documents relating to this case. They go on to claim that detailed interviews have been conducted with audit team members and Carillion senior executives and further interviews are planned for 2019.

[33] Bouvier, S., Accounting roundup: Kingman on the FRC; Carillion audit report, *Investment Pensions Europe*, 1 February 2019.
Available at:
https://www.ipe.com/pensions/pensions/pensions-accounting/accounting-roundup-kingman-on-the-frc-carillion-audit-report/10029283.article
Accessed February 2019

[34] FRC, Update on FRC investigations in relation to Carillion, 22 January 2019.
Available at:
https://www.frc.org.uk/news/january-2019-%281%29/update-on-frc-investigations-in-relation-to-carill
Accessed February 2019

Value of new KPMG contracts from UK government rises despite scandals (Aug 2019)
Despite the problematic audits of Carillion, KPMG (Carillion's auditor) has not suffered a loss from this branch of its audit work[35]:

> The value of new UK public sector contracts awarded to KPMG increased more than fourfold last year, despite a series of high-profile scandals at the Big Four accounting firm and scrutiny over its work for government outsourcer Carillion.
>
> KPMG won public sector contracts worth £55m last year, its most in three years, compared with £12m in 2017 and £22m in 2016, according to figures from Tussell, a research firm that compiles data on public procurement.
>
> The bulk of the new fees from government departments came from the Ministry of Defence, which awarded KPMG contracts with a lifetime value of more than £20m last year. It also received £13m worth of contracts from the Department for International Development.
>
> The sharp rise in fees from public sector contracts comes despite several controversies surrounding KPMG, including a corruption scandal involving its South Africa arm and the collapse of Carillion, which it had audited since 1999.

OObvoiusly the government does not seem to be influenced by KPMG's audit of Carillion. Or perhaps some think that maybe they do not wish to have an auditor delve too closely?

Laura Ashley (Moore Stephens)

Moore Stephens (now MSR Partners) was fined £825,000 though subsequently heavily discounted for in relation to the audit of Laura Ashley for the financial year 2016. MSR Partners admitted 11 breaches of relevant requirements in relation to the audit of materiality, revenue and going concern. The breaches were claimed by the FRC to be serious and pervasive throughout the audit and included: setting materiality at three times the appropriate level; failing to gather sufficient appropriate audit evidence when assessing the use of the going concern assumption; and a failure to obtain sufficient appropriate audit evidence in relation to their work on revenue[36].

Continued

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[35] Kinder, T., Value of new KPMG contracts from UK government rises despite scandals, *Financial Times*, 29 July 2019.
Available at:
https://www.ft.com/content/28bfdfd4-afc8-11e9-8030-530adfa879c2
Accessed August 2019

[3636] FRC, Sanctions against MSR Partners LLP and Stephen Corrall, 9 May 2019
Available at:
https://www.frc.org.uk/news/may-2019/sanctions-against-msr-partners-llp-and-stephen-cor
Accessed May 2019.

London Capital & Finance (LCF)

This is a case which is going to continue and continue. The FT heading encompasses this scandal:

> "LCF savings scheme channelled millions to chief before collapse: Millions invested with London Capital & Finance ended up with CEO and connected people, say administrators"[37].

The article goes on to explain[38]:

> Millions of pounds invested by 11,600 British retail investors into a failed savings company ended up enriching its boss and the head of its biggest borrower, according to administrators who tracked its funds.
> The money trail left by the collapse of London Capital & Finance revealed a "number of highly suspicious transactions," administrators at Smith & Williamson concluded in their report into the £236m collapse of the firm.
> Funds traced by administrators at LCF were lent to companies that used the money to buy a helicopter, acquire an undeveloped plot of land in the Dominican Republic and invest in a rundown holiday village in Cornwall. But the administrators said that many of these companies were unlikely to repay their loans.
> The scandal is one of the most far-reaching to hit UK retail investors in recent years. LCF sold unregulated "mini-bonds" to many retirees or first-time investors at promised returns as high as 8 per cent which in some cases it erroneously claimed had

The FCA was the watchdog that was supposed to protect such investors in what appears is the sale of unusually and suspiciously high yielding bonds of 8%. So it is not surprising that the FCA is now facing a government probe into its oversight of LCF, after customers of the firm lost thousands of pounds in investments. The criticism is that the FCA was too slow to protect consumers before LCF went into administration. The 11,605 investors (many small) would only receive 20% of the £236 million invested[39].

The story gets worse for the small investors:

> Victims of collapsed business London Capital & Finance have been told they could face income tax bills on failed investments that were mis-sold to them as tax-free savings accounts.

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[37] Binham, C., 2019, LCF savings scheme channelled millions to chief before collapse, *Financial Times*, 26 March 2019.
Available at:
https://www.ft.com/content/670ab2d8-4fc3-11e9-9c76-bf4a0ce37d49
Accessed March 2019

[38] Ibid.

[39] BBC News, 2019, Watchdog faces probe over LCF collapse, *BBC*, 1 April 2019.
Available at:
https://www.bbc.co.uk/news/business-47773404
Accessed April 2019

London Capital & Finance (LCF)/Continued

Meanwhile two of the Big Four and one smaller audit firm were involved in audits which failed to find or warn of anything untoward[40]:

> The auditors of London Capital & Finance were changed three times in two years, prompting questions about why none of them raised warnings about the investment firm now at the centre of a £237 million criminal investigation.
>
> The company, which is being investigated by the Serious Fraud Office, was audited by EY, the Big Four accountant, when it went into administration in January. EY took over from PWC, its rival, for the 2016-17 financial year. It is understood that London Capital & Finance did not want to pay PWC's fees.
>
> PWC had picked up the contract a year earlier from Oliver Clive & Co, a small, London-based firm that also audited the company for a year, according to accounts filed at Companies House.
>
> EY was weeks from signing off on London Capital & Finance's latest accounts when the business collapsed, The Times understands.
>
> Smith & Williamson, its administrator, is understood to be looking at several years of audits. "The joint administrators will be looking into the role and potential liability of all parties involved with the company. There will be no hiding place," Mike Stubbs, a partner at Mishcon de Reya, the law firm advising Smith & Williamson, said.
>
> Commentators have questioned how EY and PWC, two of Britain's biggest accounting firms, did not notice that London Capital & Finance was marketing a high-risk mini-bond scheme as a fixed-rate Isa.
>
> Smith & Williamson has raised concerns about £70 million of loans made by London Capital & Finance to Prime Resort Development. The administrator said that the property company had provided no evidence of its ability to repay the debt.
>
> The Financial Reporting Council, which regulates auditors, said that it would investigate if it was given evidence of audit failures. EY would not comment on companies it had audited. PWC also declined to comment.
>
> Although LCF was approved by HMRC as an official Isa manager, the minibonds it sold were not Isa-compliant. The tax authority has therefore ruled that income tax must be paid on any interest earned over and above individual tax allowances, despite requests for leniency from the joint administrators[41].

Continued

[40] Kinder, T., 2019, No warning from three auditors over failed firm, *The Times*, 30 March 2019.
Available at:
https://www.thetimes.co.uk/article/no-warning-from-three-auditors-over-failed-firm-s7qnwznmt
Accessed April 2019

[41] Beioley, K., Customers of collapsed LCF face tax bills on mis-sold Isas, *Financial Times*, 3 April 2019.
Available at:
https://www.ft.com/content/ea5002e8-5558-11e9-91f9-b6515a54c5b1
Accessed April 2019

London Capital & Finance (LCF)/Continued

The fallout from the FCA's failure to spot or prevent this scandal will continue:

> The Financial Conduct Authority will appoint an independent individual to examine its role in the growing scandal surrounding London Capital & Finance and whether existing regulations are sufficient to protect people who invest in mini-bonds.
>
> John Glen, economic secretary to the Treasury, said: "The recent stories of those affected by the collapse of LCF are incredibly concerning . . . By ordering this investigation, we will better understand the
>
> Questions have been raised about whether the FCA acted quickly enough to put a stop to London Capital & Finance's activities. It attracted investors by selling mini-bonds that promised interest rates of up to 8 per cent and said that it would lend the money raised to UK businesses. It collapsed after the FCA froze its bank accounts and ordered it to withdraw marketing materials that were ruled to be misleading circumstances around the collapse and make sure we are properly protecting those who invest their money in the future."[42]

Then the final report on this scandal is a LCF broker now in a fraud probe in connection with the LCF scandal[43]:

> Fraud investigators probing a £236m mini-bond scandal have turned their attention to an aborted property deal involving the middle man who brought investors into the fund.
>
> Paul Careless owns Surge Financial, a marketing firm that earned about £60m in fees by drumming up interest in the mini-bonds sold by London Capital & Finance.
>
> LCF is being investigated by the Serious Fraud Office (SFO) after it collapsed into administration last month with £236m of investor cash.

and

> Administrators believe that bondholders' money may have ended up enriching four men: LCF chief executive Andy Thomson, Simon Hume-Kendall, Elten Barker and Spencer Golding.

Then an extension[44].

> Fraud investigators probing a £236m mini-bond scandal have turned their attention to an aborted property deal involving the middle man who brought investors into the fund.

And[45]

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[42] Martin, B., 2019, Inquiry into watchdog's handling of London Capital & Finance failure, The Times, 1 April 2019.
Available at:
https://www.thetimes.co.uk/article/inquiry-into-handling-of-lcf-failure-lcrhspgnq
Accessed April 2019

[43] Millard, R., 2019, LCF broker in fraud probe, Business, *Sunday Times*, 31 March 2019.
Available at:
https://www.thetimes.co.uk/article/lcf-broker-in-fraud-probe-b5nzfbzhb
Accessed April 2019

[44] Millard, R., 2019, LCF broker in fraud probe, *The Sunday Times*, 31 March 2019. Available at:
https://www.thetimes.co.uk/article/lcf-broker-in-fraud-probe-b5nzfbzhb
Accessed April 2019

[45] Beioley, K., 2019, Customers of collapsed LCF face tax bills on mis-sold Isas, *Financial Times,* 3 April 2019.
Available at:
https://www.ft.com/content/ea5002e8-5558-11e9-91f9-b6515a54c5b1
Accessed April 2019

London Capital & Finance (LCF)/Continued

> Victims of collapsed business London Capital & Finance have been told they could face income tax bills on failed investments that were mis-sold to them as tax-free savings accounts.

Also the FCA'[s conduct is being probed[46]:

> The Financial Conduct Authority is facing a government probe into its oversight of London Capital & Finance (LCF), after customers of the firm lost thousands of pounds in investments. It follows concerns the FCA was too slow to protect consumers before LCF went into administration last month. Some 11,605 people invested a total of £236m with LCF, but only about 20% of this money may end up being recovered. The Treasury, which will run the probe, said it was "incredibly concerning".

The latest reports claim that the Financial Services Compensation Scheme made the wrong call: [47]

> Retail bondholders facing the wipeout of their savings in a £236m investment scandal are accusing the UK's financial compensation scheme of giving misleading information over the protection they should expect. People who bought "mini-bonds" from London Capital & Finance have told the Financial Times that they only did so after receiving assurance from the Financial Services Compensation Scheme that their money was safe. More than 11,500 bondholders — many of them retirees and first-time investors — may now be wiped out following LCF's collapse in late January, which sparked a regulatory and criminal probe.

So this scandal will continue to unfold. The latest is an attempt to turn the tables on the FCA[48]:

> The former Court of Appeal judge conducting an independent probe into the UK's financial watchdog's failings around a £236m mini-bond scandal has no powers to force regulators to attend an interview.
>
> The Financial Conduct Authority and any individuals singled out for criticism by Elizabeth Gloster will also be allowed to make comments on her draft findings that she must take into account before her final report is published, according to a protocol that lays out guidelines for her investigation into any mis-steps by the FCA in the run-up to the collapse of London Capital & Finance, which pushed unregulated mini-bonds on 11,600 customers who now face being wiped out.
>
> The FCA has come under fire from politicians for missing red flags about LCF's business model. Dame Elizabeth was named in May — although only officially appointed earlier this month — to lead the investigation into the regulator's actions.

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[46] BBC, Watchdog faces probe over LCF collapse, BBC News, 1 April 2019.
Available at:
https://www.bbc.co.uk/news/business-47773404
Accessed April 2019

[47] Binham, C., Beioley, K., and Ford, J., 2019, UK redress scheme accused of misleading London Capital & Finance investors, *Financial Times,* 30 April 2019. Available at:
https://www.ft.com/content/c1aa46e4-6b62-11e9-80c7-60ee53e6681d
Accessed April 2019

[48] Binham, C., LCF probe will not be able to force regulators to be interviewed, Financial Times, 25 July 2019.
Available at:
https://www.ft.com/content/56083742-aecf-11e9-8030-530adfa879c2
Accessed July 2019.

London Capital & Finance (LCF)/Continued

The protocol published by the FCA on Thursday reveals that she has no powers to compel FCA employees to attend an interview as part of her probe, and that she must email ahead of time to alert interviewees as to the topics she wants to cover.

Mark Taber, a bond expert and campaigner assisting the LCF bondholders' group, said that the FCA's ability to respond to criticism before publication was "dreaded Maxwellisation" that could slow the process down. Maxwellisation is when people identified in a report have a chance to put their sides of the story before publication. The process can be drawn-out and previous reports into other regulatory failings have been slowed down considerably because of it.

Continued

Marc Ltd (Marlon Abela) [July 2019]

We are not sure whether is a relevant case. It has the initial trappings but there is no evidence of any scandal or wrongdoing. Just, perhaps, a business that is not performing well – as many restaurants chains currently do with the growth of recipe boxes and home delivery of ingredients. However, The Times did report this case[49]:

> The restaurant empire of Mayfair mogul Marlon Abela is under fresh scrutiny after auditors revealed they could not reconcile its bank statements with cash.
> According to accounts for Marc Ltd — the parent company of Morton's Club, Umu, The Square and The Greenhouse — auditors at the accountancy firm Haysmacintyre were not handed sufficient evidence to give an opinion on the financial statements.
> The accounts, for the year to December 2017, also reveal that Abela, 44, is owed £47.7m by the company, which made a loss of £5.8m on sales of £12.1m.
> It is the latest in a string of upsets for the restaurant tycoon, the son of Albert Abela, whose Abela Group supplied in-flight meals to airlines and catered for hospitals and schools in the Middle East and France.
> ….
> A restaurant he co-owned in New York, A Voce, filed for bankruptcy in 2016. In January 2018, the Financial Times reported allegations of late payments, tax difficulties and legal disputes at the wine merchant OW Loeb, which was bought by Abela in 2014. He disputes the claims.

Of course the charismatic Marlon Abela denies any issues or problems blaming it on the banks. Sometimes the expression there is no smoke without fire can be wrong. We will see.

[49] Meddings, S., Auditors choke over accounts for Mayfair dining mogul Marlon Abela, *The Times*, 28 July 2019.
Available at:
https://www.thetimes.co.uk/article/auditors-choke-over-accounts-for-mayfair-dining-mogul-marlon-abela-0mvghldlz
Accessed July 2019

Metro bank (March to September 2019)

This is a slightly strange financial crisis. It started with an FT report[50]:

> The body in charge of a major scheme to boost competition in UK banking warned Metro Bank not to provide misleading information about its business plans after it was criticised for giving the under-fire bank a £120m prize.
>
> Banking Competition Remedies [BCR]gave Metro the largest award from the hotly-contested "capability and innovation fund" last month, despite the fact Metro had recently revealed a major miscalculation in part of its loan book.
>
> The company assured BCR the mistake would not affect its bid for a share of the funds, which were being paid for by Royal Bank of Scotland as a condition of its bailout in the financial crisis. However, less than a week after receiving the award, Metro announced it would cut its growth plans, issue £350m in new shares, and was being investigated by regulators over the accounting error.

The trigger for these and other comments was a letter that was published by the Treasury select committee. Nicky Morgan, chair of the committee, had also written to BCR demanding more information about its decision-making process.

Previously the FT reported[51]:

> Regulators are pressing for an overhaul of Metro Bank's board, amid mounting investor criticism of the troubled lender's weak corporate governance.
>
> Metro, rocked by a serious accounting error in January, announced last month that Ben Gunn, previously Metro's senior independent director, would take the newly-created position of deputy chairman in April, despite having already breached the nine-year maximum board tenure recommended under the corporate governance code.

And then of course the inevitable shareholder reaction. The BBC reported:[52]

> Metro Bank shares have fallen sharply for a second day running, after it unveiled plans to raise £350m from investors to plug a funding gap left by an accounting error. The bank revealed last month that it had underestimated the risk level of some of its commercial loans.

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[50] Megaw, N., Head of UK banking competition prize warns Metro Bank after criticism, *Financial Times*, 19 March 2019.
Available at:
https://www.ft.com/content/10abdfd0-4a72-11e9-bbc9-6917dce3dc62
Accessed March 2019

[51] Megaw, M., and Jenkins, P., UK regulators press for overhaul of Metro Bank board, *Financial Times*, 18 March 2019.
Available at:
https://www.ft.com/content/e5bd3b2a-4733-11e9-a965-23d669740bfb
Accessed March 2019

[52] BBC News, Metro bank shares slump on cash call, *BBC*, 27 February 2019.
Available at:
https://www.bbc.co.uk/news/business-47387630
Accessed February 2019

Metro bank/Continued

> Sources said Metro had suspended lending to new commercial real estate customers in recent weeks. Business and commercial property lending represents about a third of its book.

However this is not the end of the story[53]:

> Metro Bank's customers have withdrawn £2bn of deposits from the lender since the start of the year following a misreporting scandal that forced the company to raise fresh capital.
>
> The bank said that total deposits had fallen to £13.7bn compared to £15.7bn at the start of the year, which the lender attributed to "intense speculation at the time of the capital raise".
>
> The deposit flight was "primarily driven by a limited number of commercial customers withdrawing" their cash, the bank said, adding that total deposits had returned to net growth in the past eight weeks.
>
> The disclosure, contained in the company's second-quarter results announcement, came as the bank fell to a statutory quarterly loss of £1.2m after tax versus a profit of £8.8m a year ago. Goodbody, the stockbroker, had forecast a statutory post-tax profit of £3.6m.

And then immediately:[54]:

> Shares in Metro Bank fell to an all-time low on Thursday as investors reacted to a messy plan to replace co-founder Vernon Hill as chairman and the revelation that customers pulled £2bn of deposits from the lender in the first half.
>
> On Wednesday evening, the bank said it would start searching for a new chairman but did not set a timetable for the appointment.
>
> Mr Hill — who will stay on the board as a non-executive — set the stage for a protracted transition by telling the Financial Times he wanted his replacement to spend some time as a director before taking the helm. Mr Hill pledged to remain deeply involved in running the bank he founded, vowing not to take a "back seat".
>
> He said: "I'm not leaving. I would never leave at a low point. Think of me as a founder that plays a different role from a non-executive director. 'Back seat' is not a word they use for me very often, but I'm very happy to have an independent chairperson with skills that complement mine."
>
> The company's shares were down almost 16 per cent at 401p in early trading in London on Thursday, taking the decline for the stock this year to 76 per cent.

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[53] Crow, D., Metro Bank customers withdrew £2bn in wake of loan scandal, *Financial Times*, 24 July 2019.
Available at:
https://www.ft.com/content/5ea5d846-ae34-11e9-8030-530adfa879c2
Accessed July 2019.

[54] Crow, D., Hammond, G., and Jenkins, P., Metro Bank shares tumble to record low on chairman concerns, *Financial Times*, 25 July 2019.
Available at:
https://www.ft.com/content/3176890c-ae3d-11e9-8030-530adfa879c2
Accessed July 2019.

Metro bank/Continued

> Mr Hill's vacation of the chair may be seen as a victory for regulators, who had long been uneasy about Mr Hill's leadership of the bank. But governance experts expressed astonishment at the unusual decision to keep him on the board.
> "I've never seen anything like it," said one investor. "How do you stop him being chair in all but name?"
> …
>
> Metro Bank announced the 73-year-old's exit as it revealed its customers withdrew £2bn of deposits in the first six months of the year following a misreporting scandal that broke in January, which forced the bank to raise £375m of fresh capital in May.

Metro bank is a challenger bank in the UK to the traditional high street banks. The FT commented[55]:

> … Metro Bank, which sought to challenge them all, had seemed genuinely different: investing in branches, welcoming customers' thirsty dogs, selling investors a not-too-capital-heavy growth story . . . until it also proved too good to be true. An accounting error took it from being a £2.7bn company growing its loan book by 66 per cent a year to a £500m company with growth plans on hold until it could raise £375m of capital.
> On Monday, news that Metro was discussing a loan-book sale to further rebuild its capital merely emphasised how difficult it is to be a bank that challenges others. Metro had only been able to appear sufficiently capitalised as it rapidly grew its loan book because it misclassified commercial property and buy-to-let loans. Metro had also avoided criticism of its questionable corporate governance — notably, the tenure and independence of chairman Vernon Hill — thanks to that loan book growth. Now, the nature of that growth — the property and buy-to-let loans were acquired, not granted, by Metro — is worrying the market. Metro shares are down 72 per cent this year and 6 per cent of them have been sold short by speculators. That leaves Metro's other shareholders having to decide how much of a challenger they can afford to have it be.
> Do they want Metro to sell its property and buy-to-let loans so it can resume capital-intensive and low-margin, branch-based retail lending? Its common equity tier one ratio fell close to its own minimum of 12 per cent in March, and Barclays analysts reckon selling its entire £1.7bn loan portfolio at face value could add 3 percentage points to that. But branch expansion and a renewed push into hyper-competitive mortgages could quickly eat into capital and require more, while delivering meagre earnings from a net interest margin as thin as 1.6 per cent.
> Do they want Metro to slow down and challenge less? Its half-year results on Wednesday will show this is happening, after first-quarter pre-tax profit halved to £4.3m. Craig Donaldson, chief executive, already talks of "optimising the balance of growth, profitability and capital efficiency" and Exane analysts suggest Metro's shares can no longer be rated as a growth stock. But that would mean no return for investors who bought them as such.

[55] Vincent, M., How much of a challenger bank can Metro still afford to be? *Financial Times*, 22 July 2019. Available at:
https://www.ft.com/content/7ba7469a-ac7d-11e9-8030-530adfa879c2
Accessed July 2019.

Metro bank/Continued

Or do they need Metro to become more like other banks? Rumoured private equity deals would do nothing to solve Metro's capital or digital challenges. But a takeover by a plc bank, or a merger with another challenger, just might.

Those that tried to profit from the anomalies earlier in the year actually lost money:[56]

> Some of the world's richest businessmen have lost almost £400m in just five months after stepping in to shore up ailing Metro Bank.
> Billionaire hedge fund chief Steven Cohen was among those to bag what analysts dubbed "a bargain" during the bank's cash call in May when it issued stock at 500p a share.
> But Metro's shares plummeted again this week (https://www.telegraph.co.uk/business/2019/09/24/metro-bank-plunges-new-record-low-failure-200m-bond-sale/)
> after the bank was forced to cancel a bond sale due to a lack of investor interest. The stock is now worth just 187p, a record low - meaning backers have suffered a further plunge in the value of their stock.

Continued

[56] Burton, L., Tycoons who grabbed a 'bargain' during Metro Bank cash call sit on £400m losses, *Daily Telegraph*, 25 September 2019.
Available at:
https://www.telegraph.co.uk/business/2019/09/25/tycoons-grabbed-bargain-metro-bank-cash-call-sit-400m-losses/
Accessed Septmber 2019.

Mitie Group (auditor: Deloitte)

Along with Carillion, there are a number of similar companies and these include Capital, Serco, Mitie, Mears, Kier, Interserve, G4S and others. All have varying degrees of financial issues as margins are being squeezed in this contracted-out, service and construction segments. Not surprisingly Mitie comes within this financial squeeze scenario. To some extent the whole of this sector has suffered. Capital and Interserve have had their share of problems. Jolly[57] picked out Mitie:

> Mitie reported a full-year loss in 2017 after an accounting review forced it to take a significant financial hit. The £88.3m charge meant the outsourcing company – a rival of collapsed Carillion – swung to a loss. The FRC announced an investigation into Deloitte's audit shortly after.

Continued

[57] Op. Cit Jolly 2019.

Petrofac

This is another ongoing and developing story. The Times reported[58]:

> The oil services group at the centre of a corruption inquiry has warned investors of increased risks to its future after one of its former employees was convicted of bribery.
> Petrofac said that developments in the investigation by the Serious Fraud Office had increased "the risk of a loss in share price value, prosecution, fines, penalties or other consequences, including reputational damage".
> In its annual report it said that, as a result, risks had increased since last year in five principal areas that could threaten its future prospects, including the threat of "loss of licence to operate" and "loss of financial capacity".
> The warning comes two months after a former senior executive pleaded guilty to bribery over payments of more than $50 million that the group made to secure almost $4.5 billion of work in Saudi Arabia and Iraq.
> The troubled company also disclosed that it had given Ayman Asfari, its chief executive, a 16 per cent pay rise to $2.3 million last year.
> Petrofac designs, builds and operates oil and gas facilities and employs 11,500 people worldwide. It reported revenues of $5.8 billion last year and net profit of $64 million.

At the moment there is little evidence of this case which frist goes back to My 2017 but has recently re-emerged. EY, Petrofac's auditor, said that Lufkin's guilty plea "raises the possibility of financial sanctions which could have a material impact on the financial statements and ongoing concern/viability" of Petrofac[59].

> Petrofac said in its annual report that it remained "unclear when or how the investigation" by the SFO would conclude. It said that while shareholder confidence had been affected, its clients remained supportive[60].

Just a case of bribery or something deeper? We shall see.

Continued

[58] Gosden, E., 2019, Petrofac warns investors of risk to future from fraud office inquiry, The Times, 2 April 2019
Available at:
https://www.thetimes.co.uk/edition/business/petrofac-warns-investors-of-risk-to-future-from-fraud-office-inquiry-lxhqnnmwx
Accessed April 2019
[59] Ibid.
[60] Ibid.

Quindell (auditor: KPMG)

This was briefly discussed in the book. Jolly summarises this:

> Insurance claims handler Quindell, now known as Watchstone, is being investigated by the Serious Fraud Office after delayed accounts in 2015 showed a £238m loss for the previous year, following questions over how it accounted for previous acquisitions. KPMG was fined more than £3.1m for misconduct related to its audit of Quindell after it failed “to obtain reasonable assurance that the financial statements as a whole were free from material misstatement”.

For us another major scandal was Steinhoff the aftermath of which is ongoing. HBOS, MG Rover, SIG in the UK also featured.

We also covered other important cases including (mostly in the appendices [online]) including Satyam in India, GE in the US, Petrobras (Brazil), Juridica, Redcentric and others.

Continued

Redcentric

PwC has been fined £6.5m (reduced to £4.6m) and given a severe reprimand by the FRC for failures of professional scepticism over the audit of AIM-listed IT managed services provider Redcentric, while two of the firm's partners in its Leeds office have also been sanctioned (and fined £140,000 each)[61]. This relates to the statutory audits of Redcentric of the years 2015 and 2016. The FRC commented:

> The sanctions reflect the seriousness and extent of the breaches. Professional scepticism was lacking in this audit. Had it been applied, it is likely that certain material misstatements would have been detected. As this is the second Final Decision Notice involving PwC Leeds' office in recent years, we have mandated that the firm supplements its ongoing monitoring and support for that office, to further improve the quality of audit work in the future."[62]

As the FT reported:[63]

> PwC has been hit with the second multimillion pound fine in a year for audit work by its Leeds office, prompting the regulator to order a strengthening of special monitoring measures at the regional office. In a ruling on Thursday the accounting watchdog said PwC and two of its partners, Jaskamal Sarai and Arif Ahmad, had shown a "serious lack of competence" in their 2015 and 2016 audits of Redcentric, the Harrogate-based IT services group. In late 2016, Redcentric admitted to having overstated its assets by £13m and its profits by £9.5m.
> …
> This comes after the Financial Reporting Council fined PwC £6.5m in June 2018 for its work on the accounts of collapsed British retailer BHS that was handled by its Leeds office.

Continued

[61] Sweet, P., FRC fines PwC £6.5m over Redcentric audit failures, Accountancy Daily, 13 June 2019
Available at:
https://www.accountancydaily.co/frc-fines-pwc-ps65m-over-redcentric-audit-failures
Accessed June 2019.
[62] FRC, Sanctions against PwC and partners in relation to Redcentric plc, 13 June 2019
Available at:
https://www.frc.org.uk/news/june-2019/sanctions-against-pwc-and-partners-in-relation-to
Accessed June 2019.
[63] Rovnick, N., PwC receives second fine in a year for audit work by same office, Financial Times, 13 June 2019.
Available at:
https://www.ft.com/content/8e13a416-8dcb-11e9-a24d-b42f641eca37
Accessed June 2019.

Serco (July/October 2019)

The FRC fined Deloitte £6.5m for misconduct in audits of a subsidiary of Serco, a day after the outsourcer agreed to sanctions over its role in a scandal involving its electronic tagging of offenders[64]:

> The Financial Reporting Council "severely reprimanded" and fined Deloitte and its audit engagement partner, Helen George, in relation to audits of Serco Geografix in 2011 and 2012.
> Serco on Wednesday announced it had reached a deal with the Serious Fraud Office in which it was hit with a £19.2m fine for three offences of fraud and two of false accounting committed by the subsidiary between 2010 and 2013. The deal means Serco will not face criminal charges.
> The scandal involved Serco overstating profits on the contract it had with the UK's Ministry of Justice for the electronic tagging service, including charging for some offenders who were dead.
> The FRC fined Deloitte £6.5m and Ms George £150,000, discounted to £4.2m and £97,500 respectively because the parties settled. Deloitte will also pay £300,000 towards the costs of the investigation and all of its audit staff will have to undergo a specially designed training programme

Interestingly, The FRC said the settlement agreement and particulars of the case would not be published at present. Not sure why. We think errors made should be widely disseminated so other do not make the same mistake.

The FRC announced its sanctions against Ross Howard the Deloitte's audit engagement partner in relation to Serco Geografix. Previously Deloitte had been fined £4,2m and also Helen George, another audit engagement partner[65].

Continued

[64] McCormick M., and Beioley K., Deloitte fined £6.5m over Serco audit misconduct, *Financial Times*, 4 July 2019.
Available at:
https://www.ft.com/content/062eff9c-9e23-11e9-b8ce-8b459ed04726
Accessed July 2019

[65] FRC, Sanctions against Ross Howard in relation to the audit of Serco Geografix Ltd, FRC News, 29 October 2019.
Available at:
https://www.frc.org.uk/news/october-2019/sanctions-against-ross-howard-in-relation-to-the-a
Accessed October 2019

Staffline (March 2019)

Press reports put this issues as:

> PwC has been accused of ignoring conflicts of interest at a listed audit client that was forced to suspend trading in its shares after it admitted to investigating potential accounting irregularities.
> The Big Four accounting firm's relationship with Staffline — one of the UK's largest recruitment firms — has come under scrutiny after it delayed publishing its results in January and admitted to potential accounting irregularities involving "invoicing and payroll practices".
> The AIM-listed company said at the time that these issues could have a material impact on its profitability.
> Staffline's finance director, Mike Watts, and the head of its audit committee, Ed Barker, both previously worked at PwC. One of its previous finance directors, Phil Ledgard, was also an alumnus of PwC.
> Prem Sikka, an accounting professor recently commissioned by the Labour Party to lead a review of Britain's audit market, said PwC's independence at Staffline was "clearly" compromised by these relationships. He added that the firm's role as the company's auditor was "inappropriate".[66]

Some investors have suffered greatly through a drastic fall in their shares as much as a 87% write-down. Though some of the write-down of its shares are due to Brexit[67]:

> Staffline, a recruitment agency that supplies temporary workers to groups including Tesco and Marks and Spencer, lost more than half of its market value after claiming that Brexit was prompting companies to hire UK rather than foreign staff.
> The recruiter, whose customers rely heavily on overseas labour, said on Friday that 2019 earnings before interest, tax and other adjustments would be £23m to £28m. Analysts had expected Staffline to earn £43m on this adjusted basis.
> Uncertainty over the future supply of EU labour meant some Staffline customers were hiring permanent staff for jobs such as driving goods around the UK, instead of using temps, "to mitigate the risk of that labour market tightening", the recruiter said.

Continued

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[66] Barbyshire, M., and Marriage, M., PwC accused of ignoring conflicts over Staffline audit, *Financial Times*, 4 March 2019.
Available at:
https://www.ft.com/content/5a98393c-3c52-11e9-b856-5404d3811663
Accessed March 2019.

[67] Rovnick., N., and Gross, A., Recruiter Staffline issues profit warning on Brexit uncertainty, *Financial Times*, 17 May 2019.
Available at:
https://www.ft.com/content/93a1726a-786c-11e9-be7d-6d846537acab
Accessed May 2019.

Tanfield

This is an old case relating to 2007 to 2009. The FRC has sanctioned and fined the auditors of Tanfield, when the electric vehicle maker's shares collapsed amid allegations of incompetence and malpractice[68]:

> Baker Tilly, which has since become RSM, was fined £750,000 for misconduct and errors in its audit work, including failing to properly review the accounts, which could have identified discrepancies in millions of pounds worth of assets.
>
> The partners in charge of the audit, Steve Railton, RSM's head of the North East, and Richard King, who runs its Nottingham office, were reprimanded and fined £35,000 and £30,000, respectively.
>
> In 2008 Tanfield's shares plunged by 80 per cent in only a week after it issued a profit warnings and after analysts criticised it for weak financial controls and poor standards of disclosure.
>
> Tanfield, based in Newcastle, was worth £700 million at its peak, when it was the biggest company Aim, London's junior stock market. At present it is worth about £7 million. Its shares fell 13 per cent yesterday to 4½p.

Ted Baker (auditor: KPMG)

The FRC fined and reprimanded KPMG (£3m) and one of their partners following their admission of Misconduct in relation to their audits of the financial statements of Ted Baker.

The misconduct arose from KPMG providing expert witness services to Ted Baker in a commercial court claim. This meant that there could have been a breach of the ethics and could have led to the loss of KPMG's independence in respect of the audit. There was a risk that the audit team would review the work of the expert when auditing Ted Baker's treatment of the claim in its accounts and this posed an unacceptable self-review threat. The FRC also claimed that there was a self-interest threat arising from the fact that the fees for the expert engagement significantly exceeded the audit fees in the relevant years[69],

[68] Kinder, T., 2019, RSM auditors fined over Tanfield failings, The Times, 16 April 2019.
Available at:
https://www.thetimes.co.uk/article/rsm-auditors-fined-over-tanfield-failings-0kl2j6m3p
Accessed April 2019

[69] FRC, Sanctions against KPMG and Senior Statutory Auditor in relation to the audits of Ted Baker Plc, 20 August 2018.
Available at:
https://www.frc.org.uk/news/august-2018/sanctions-against-kpmg-and-senior-statutory-audito
Accessed December 2018

Continued

Woodford (June/October 2019) [GT]

We think that Woodford is scandal but it does not directly deal with accounting or auditing rules. It deals with operational policy decisions. Oliver Shah succinctly sum this up as[70]:

> When he launched his own equity income fund in 2014, half the portfolio was invested in FTSE 100 shares. By the time it was gated due to a wave of redemptions in June this year, highly liquid stocks accounted for just 8%. It was closed last week, bringing down Woodford Investment Management.
>
> According to Gilovich and co, Woodford would have missed at some point even had he stuck to blue-chips. Yet in backing esoteric start-ups, he was also moving further and further away from the hoop, taking ever more ambitious and difficult shots.
>
> We may never know why he veered so far from the strategy that had served him well. Did he think he could walk on water? Was he convinced these bets would come good, as many had in the past? Was he angling for a knighthood by supporting Britain's biotech industry?
>
> In a sense, it doesn't matter. The 1985 paper's findings have been disputed in recent years, but good chief executives and star fund managers are often lucky, and those with big egos find it hard to separate that from their own brilliance. The antidote is strong governance — the crucial element that was missing at Woodford Investment Management.

/Continued

[70] Shah, O., Oliver Shah: Unbridled Woodford needed reining in, *The Sunday Times*, 20 October 2019. Available at: https://www.thetimes.co.uk/article/oliver-shah-unbridled-woodford-needed-reining-in-m7ltdl6t3 Accessed October 2019.

Woodford/Continued

Woodford's problems described below were added to by the billionaire behind Hargreaves Lansdown and that company is criticised below for keeping its buy recommendations in the top 50 well beyond an objective view of the fund's performance[71]:

> The billionaire behind Hargreaves Lansdown has launched a blistering attack on Neil Woodford, slamming the beleaguered stockpicker for appearing not to be "truthful" about the performance of his frozen Equity Income Fund.
>
> Peter Hargreaves, who started the funds platform with Stephen Lansdown in 1981 and built it into a FTSE 100 giant, also added to the wave of criticism of his old company for holding too many of Woodford's funds and for failing to spot the crisis until it was too late.
>
> "It's annoyed the hell out of me that it would appear he [Woodford] has not been truthful with Hargreaves Lansdown. But it's also annoyed me that they let it go on so long," Hargreaves said.
>
> Hargreaves Lansdown has come under fire for using its Wealth 50 list of recommended funds to promote Woodford's Equity Income fund, which blocked withdrawals in May after a string of corporate collapses at mostly unquoted companies held by the fund. Woodford's fund has shrunk to £3.1bn during its suspension from a value of £10.2bn at its height just two years ago.
>
> Hargreaves, 72, has kept his counsel since the fund was gated. He still owns 32% of Hargreaves Lansdown, a stake worth £3.1bn at Friday's closing share price of £20.30. He stood down from the board in 2015.

We are not sure whether this company belongs here in financial scandals and failures. Rod thinks definitely not as there is no financial or accounting irregularities. This concerns the behaviour and operations of the investment fund which then ran into problems – but there were no accounting issues (that have come to light).

This is a case of a poor performance investment fund over time (see article below). The fund seemed to have invested in lots of unquoted companies meaning that they are essentially difficult to sell and therefore are illiquid. If investors in Woodford want to withdraw their money, the fund many not have sufficient cash to meet the demand. Because many of the unquoted investments were unprofitable or failed, and then there was a run on the fund. Woodford could not raise sufficient cash so the fund was frozen.

A secondary concern was that is the investment advisers such as Hargreaves Lansdowne kept recommending such companies in their top 50 list despite consistently poor performances – we think such behaviour may have been induced by high commissions paid by Woodford.

[71] Evans, P., Peter Hargreaves: Neil Woodford 'did not tell the truth', The Sunday Times, 22 September 2019, Available at:
https://www.thetimes.co.uk/article/peter-hargreaves-neil-woodford-did-not-tell-the-truth-j0gz8vms7
Accessed September 2019.

Woodford/Continued

The story according to The Times was explained as[72]:

> When Neil Woodford launched his eponymous investment firm five years ago the star fund manager attracted billions of pounds of inflows and soon boasted the top performing UK equity income fund.
>
> However, despite the spectacular start from Mr Woodford, who had built up a big investor following from his two decades at Invesco, all was not as it seemed. After Woodford Investment Management secured approval from the Financial Conduct Authority in May 2014 and launched the Equity Income Fund the following month, problems that would lead to the fund's dramatic suspension this month are alleged to have already been surfacing behind the scenes.
>
> Sources have claimed:
>
> - There was a lack of due diligence at Woodford on investments in private companies that were knocking down the firm's door and a "lot of backfilling of analysis".
> - A bullying workplace culture under Craig Newman, Mr Woodford's chief executive and former head of sales at Invesco, who one source claimed was "near enough to a psychopath".
> - Mr Newman sought to appoint as a non-executive director of Woodford his linguistics coach, but the application was withdrawn after questions from the City regulator. The Financial Conduct Authority declined to comment.
>
> Mr Woodford attracted £8.5 billion of clients' money in 2014 as investors flocked to his new firm, based on the business park at Oxford, which is part of the old William
>
> The fund was gated on June 3 after a prolonged downturn in its performance and a wave of exemption requests from anxious investors. It has triggered recriminations and regulatory investigations. They include concerns over the suitability of the open-ended fund investing in many hard-to-sell private companies and Mr Woodford's contentious listing of stakes in companies in Guernsey to circumvent rules limiting the fund's unquoted investments to 10 per cent.
>
> Despite the fanfare which greeted the launch, Mr Woodford, 59, and Mr Newman, 48, had left Invesco under a cloud. The FCA fined Invesco £18.6 million on the day before Mr Woodford formally left the Henley-on-Thames-based firm for breaching investment limits and introducing leverage into funds, including those run by Mr Woodford, without sufficient disclosure. It was one of the largest fines against a retail fund manager.

Now the FT exposed a role in hedge funds that may be responsible for some of the worst issues. That is the ACD (authorised corporate director). The FT explains[73]:

[72] Ralph, A., Issues beneath the surface that wrecked Woodford, *The Times*, 1 July 2019.
Available at:
https://www.thetimes.co.uk/article/issues-beneath-the-surface-that-sunk-woodford-95plqc9jb?region=global
Accessed July 2019.

[73] Walker, O., Woodford scandal exposes the flawed cog in the machine, *Financial Times*, 27 July 2019.
Available at:
https://www.ft.com/content/bddb9ca5-c2d9-3aba-983b-3bb7c9760634
Accessed August 2019.

Woodford/Continued

> The implosion of Neil Woodford's investment business has revealed the part played by a crucial cog in the fund management machine that is virtually unknown to outsiders: the authorised corporate director.
>
> These administrators, known as ACDs, ensure that funds stay within the rules and are run in the best interests of end investors.
>
> But the Woodford saga has exposed flaws in the system, which has prompted regulatory scrutiny.
>
> "The ACD world is a mystery to everyone apart from those who work closely with the regulatory side of funds — and it is probably a concept that is lost on many professional advisers," says Patric Foley-Brickley, head of institutional business development and client management at Maitland, which provides ACD services.
>
> Of the hundreds of thousands of individuals who piled into Mr Woodford's flagship Equity Income fund, few will have known that the authorised fund manager (in this case the ACD) was not the high-profile stockpicker but a little-known business called Link Asset Services, previously part of outsourcing company Capita.
>
> As Andrew Bailey, head of the Financial Conduct Authority, conceded in a parliamentary hearing last month: "There are many confusing things about the . . . [European fund] world. That is one of them. The fact that Link's role is so important is confusing to the outside world."

This takes Woodford into the firm realm of financial failure. That said the scandal or whatever deepens[74]:

> Neil Woodford's woes deepened on Friday after two companies backed by the embattled UK fund manager revealed troubles that raise new doubts about the valuations of investments held by the one-time star stockpicker.
>
> Investors are currently barred from making withdrawals from Mr Woodford's flagship Equity Income fund and these latest problems threaten to further delay a resumption of normal trading, which is not expected until December at the earliest.
>
> The Woodford Equity Income fund has lost 11.2 per cent, including dividends, since it was suspended in early June, compared with a return of 1.5 per cent for the FTSE All Share index over the same period, according to an update on Friday from Link Asset Services.
>
> Eddie Stobart, the UK logistics and haulage company in which Mr Woodford is the biggest shareholder, suspended share trading as it issued a profit warning and announced that its chief executive was leaving.
>
> Also on Friday, the Woodford Patient Capital Trust said its net asset value would be reduced by about 4 per cent from its close on Thursday, because of lack of progress at cold-fusion technology company Industrial Heat.

No doubt if there is anything more to be declared, however small, this will eventually be publicised.

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[74] Flood,C., Pooler, M., Kinder, T. and Riding, S., Woodford woes deepen as Eddie Stobart chief steps down , Financial Times, 23 August 2019.
Available at:
https://www.ft.com/content/b586c10e-c534-11e9-a8e9-296ca66511c9
Accessed August 2019.

Woodford/Continued

As of late September 2019, the latest event is Woodford's attempt to salvage its equity fund. It will be remembered that Woodford was forced to block investors from withdrawing their money from the equity income fund in June following a string of bad investments in unquoted investments that prompted a surge in redemptions that he could not fulfil. Since then, the value of the suspended fund has fallen by 13%, and has underperformed the benchmark FTSE all-share index[75]:

> Woodford has been using the suspension period to sell off stakes in unquoted stocks and unlisted companies that can be more difficult to get rid of. On Monday, Woodford Investment Management revealed that the bulk of the proceeds – about 84% – had been reinvested in London-listed blue chip stocks including Imperial Tobacco, BT and the British Airways owner, IAG.

[75] Makortoff, K., Neil Woodford buying up FTSE 100 shares after fund suspension, The Guardian, 23 September 2019.
Available at:
https://www.theguardian.com/business/2019/sep/23/neil-woodford-buying-up-ftse-100-shares-after-fund-suspension
Accessed August 2019.

Dewan Housing India/KPMG (July 2019)

This Indian based case might have ramifications far beyond India[76]:

> Deloitte has resigned as auditor of an embattled non-bank lender in India, marking the latest in a series of resignations that come as New Delhi is putting the Big Four auditor firms under scrutiny.
>
> In a statement posted to the Bombay Stock Exchange on Tuesday, Dewan Housing Finance Corporation Limited said Deloitte had stepped down "with immediate effect" after raising concerns about intercorporate deposits and lack of transparency.
>
> Deloitte confirmed that it had resigned the DHFL contract but would not comment further.
>
> The resignation comes as the Big Four firms are under pressure in India following a meltdown in the shadow banking sector that has raised questions about audit quality.
>
> Deloitte and KPMG affiliate BSR are fighting criminal charges and a potential five-year ban following the near-collapse of Infrastructure Leasing & Financial Services, a major infrastructure and finance group whose default last year triggered a credit crisis.
>
> In court documents seen by the Financial Times, Indian prosecutors allege that Deloitte and KPMG were complicit and "connived" with the IL&FS management to perpetrate financial fraud after giving the company a clean bill of health before it defaulted on part of its $13bn debt.
>
> The auditors have denied the allegations. Both have stated they are confident that they have acted in accordance with their duties as an auditor and the relevant legal framework and intend to robustly defend their position.
>
> Against this backdrop, auditors have been resigning from Indian companies. In June, PwC resigned from Reliance Capital, another non-bank lender, citing "observations or transactions" that might be significant or material to the companies' financial results. Reliance Capital said in a letter that PwC's "observations are completely baseless and unjustified".
>
> In response to the flurry of resignations, India's market regulator last month proposed a tightening of the rules governing auditor resignations, saying that surrendering a contract before an audit of annual results had completed "seriously hampers investor confidence and leaves the investors with lack of reliable information for taking their financial decisions."
>
> …
>
> The turbulence in India's shadow banking sector over the past year combined with stiffer regulatory oversight of auditors in the country has created a "perfect storm" for the Big Four, said Saurabh Mukherjea, founder and chief executive of Marcellus Investment Managers."
>
> As skeletons tumble out of the cupboard, it's becoming apparent that auditors were looking the other way as these accounts were being evergreened," alleged Mr Mukherjea. "India is going to go through an extended period of cleansing for our auditors to tighten up and become more diligent."

[76] Findlay, S., Deloitte resigns from Indian non-bank lender, *Financial Times*, 29 July 2019.
Available at:
https://www.ft.com/content/8e2f7026-b858-11e9-8a88-aa6628ac896c
Accessed August 2019.

Burford Capital (August 2019)

Not sure whether this has any element of financial scandal. Muddy Waters, the US short-seller, has not always been correct. Carson Block has a reputation, often admired and respected, but not always. One of the casualties of Muddy waters was Burford Capital[77]:

> Litigation financing specialist Burford Capital lost about half its market value on Wednesday after prominent US short-seller Muddy Waters took aim at a favourite of London's stock market.
> The US hedge fund, which is headed by Carson Block, described Burford as a "poor business masquerading as a great one" in a report that sent shares in the company crashing more than 50 per cent.
> Burford, which counts troubled stockpicker Neil Woodford among its largest shareholders, makes money by funding lawsuits and then taking a share of any proceeds. The litigation finance industry has been turbocharged by the era of low interest rates, as investors plough money into the sector in search of juicier returns.
> The report by Muddy Waters criticises the accounting that Burford uses to value its litigation cases, which it says it is "aggressively marking", while arguing that the company is then "actively misleading investors" further with some of the metrics it reports.
> "We view it as a lottery ticket model in that it relies on huge, but rare, successes, rather than consistently producing solid returns," Mr Block told the Financial Times. "It's rare for us to come across such a dichotomy between what we see and what the market sees."
> In a stock exchange statement on Wednesday, Burford said that it had employed IFRS accounting standards that it said were "used widely across the financial services industry", while citing years of "clean" audit opinions from Ernst & Young. The company also said that it had reported on its investments in "extraordinary detail".
> The steep declines in Burford's shares on Wednesday followed an almost 20 per cent drop on Tuesday, when Muddy Waters tweeted that it would be announcing a new short position. The company has lost £1.7bn of market value over two days. Its shares were down 46 per cent at the close.
> Burford said it was "strongly suspicious" of Tuesday's share price fall and that it would "take appropriate legal action" if misconduct was discovered. "There is a clear line between appropriate commentary and market manipulation," the company said.
> Until this week, Burford's market value was more than £3bn, making it the largest stock listed on Aim, the London Stock Exchange's market for smaller growth companies. It has also been one of Aim's strongest performers, with its share price having previously surged more than 1,000 per cent over the past five years.
> Burford Capital is the second-largest holding in troubled stock picker Mr Woodford's now-suspended Equity Income fund. Mr Woodford has backed the company for a decade, having first invested in its shares in its 2009 initial public offering when at Invesco, the then-star fund manager's longtime home before he set up his own firm.

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[77] Smith, R., and Fortado, L., Burford Capital shares tumble as Muddy Waters takes aim, *Financial Times*, 7 August 2019.
Available at:
https://www.ft.com/content/29f4ac20-b8e9-11e9-96bd-8e884d3ea203
Accessed August 2019.

Burford Capital (August 2019)/Continued

This was not the end of the story however as reported in the Times[78]:

> Burford Capital launched a fightback yesterday after a vicious attack by a US short-seller wiped out almost half its value, insisting the critique included "factual inaccuracies, simple analytical errors and fallacious insinuations".
>
> Shares in Burford, one of the biggest companies on the junior Aim market, rebounded after its robust response to the criticism from Muddy Waters, the US firm. They had tumbled by 46 per cent on Wednesday after Muddy Waters issued its 25-page report.
>
> The shares bounced back by 26 per cent yesterday as Burford, a litigator funder, also said it was considering a share buyback "given the potential investment return the shares represent at their current price".

Hard to believe this swing in the value[79]:

> Down 46 per cent one day, up 26 per cent the next. Who'd have thought litigation finance was such a rollercoaster business? Maybe not even Carson Block, the Muddy Waters chief who picked a fight on Wednesday with his Burford Capital short.
>
> Mr Block has been poking around Burford since September. So, no doubt he'll have spotted from its terrible website that the Aim-listed outfit is chocka with more than 50 lawyers: a breed that gets twitchy when their business is accused of being the "ultimate 'trust me' stock", built on "Enron-esque" accounting and other "egregious" carry-ons.
>
> So Mr Block would have been braced for Burford's "response to short attack". It lifted the shares to 760p, even if he remains well ahead on points: the shares closed on Monday at £13.81 before Tuesday's mischief-making tweet.
>
> Still, Burford's up for a scrap. And there was nothing equivocal about this: "The Muddy Waters report is false and misleading". It met the gibe that it's "arguably insolvent" with lawerly gusto: "Presumably, the reason 'arguably' is inserted is because Muddy Waters knows they would lose a lawsuit if they accused Burford of insolvency". Indeed, it says it's got $400 million cash "on hand" and "has no current intention of raising equity capital".
>
> It also rebutted each of Muddy's seven "techniques" for the alleged manipulation of "performance metrics". Quite a treat, too, for fans of acquisition accounting, "delayed recoveries", trial loss treatment — and all the other delights that come with a business that guesses at how much money it'll make from a court case long before the money arrives.

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[78] Ralph, A., and Clarence-Smith, L., Burford pulls no punches in riposte to short-seller, *The Times*, 9 August 2019.
Available at:
https://www.thetimes.co.uk/article/burford-pulls-no-punches-in-riposte-to-short-seller-snklfrrt7
Accessed August 2019.

[79] Osborne, A., Burford retort makes for a capital scrap, *The Times*, 9 August 2019.
Available at:
https://www.thetimes.co.uk/article/burford-retort-makes-for-a-capital-scrap-35sktmtnn
Accessed August 2019.

Burford Capital (August 2019)/Continued

Muddy Waters was not the only fund that took a position on Burford[80]:

> A notorious short-selling activist has joined the attack on litigation funder Burford Capital, claiming its shares were overpriced before last week's broadside by Muddy Waters.
>
> Gotham City Research, which toppled the insurance technology provider Quindell in 2014, is understood to be preparing to publish its own criticism of Burford, which was hit by a scathing report last week from Muddy Waters, another short-seller.
>
> Gotham will reveal it made a bet against shares in Burford, which funds lawsuits, last year over fears about its debt-fuelled litigation, but did not make its concerns public.

The Times reviewed the history of Gotham City and blamed the result on Mifid II where no one is willing to undertake research and analysis as users and investors are not prepared to pay for this service[81]:

> Muddy Waters, run by Carson Block, is among a feared breed of investors that target companies they believe are overvalued, borrow their shares, then publish critical research they hope will destroy their target's value. These have included Quindell, the insurance tech company, which was hit by short-seller Gotham City Research in 2014. Gotham also has Burford in its sights. Welsh chip-maker IQE was blindsided by separate attacks from Muddy Waters and another short-seller, ShadowFall, early last year.
>
> Such attacks are a natural consequence of the retreat by investment banks and brokerages from researching companies caused by Mifid II rules on analysts' research, said hedge fund tycoon Crispin Odey. "Look how quickly the research side of the City is disappearing because no one's willing to pay for it," he said. "If you do that, how are you going to judge what's a good or bad investment? That's where we come in because we do it ourselves with our own analysts. It's part of a trend."

That said Oliver Shah of the Sunday Times makes a valid point about he perhaps dodgy valuation principles used by Burford. His point is a realistic one[82]:

> Strip out the flamboyant language and Muddy Waters made a good point. Unlike privately owned peers, Burford often writes up the value of its cases before they conclude.

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[80] Collingbridge, J., and Kelly, L., New predator Gotham City Research circles lawsuit funder Burford Capital, *The Sunday Times*, 11 August 2019.
Available at:
https://www.thetimes.co.uk/article/new-predator-gotham-city-research-circles-lawsuit-funder-burford-capital-0kqzrx5mh
Accessed August 2019.

[81] Collingbridge, J., and Shah, O., Burford Capital in the dock over how it judges profits, *The Sunday Times*, 11 August 2019.
Available at:
https://www.thetimes.co.uk/article/burford-capital-in-the-dock-over-how-it-judges-profits-k68cmd037
Accessed August 2019.

[82] Shah, O., Serving two masters makes it hard to deliver, *The Sunday Times*, 11 August 2019.
Available at:
https://www.thetimes.co.uk/article/serving-two-masters-makes-it-hard-to-deliver-dqh76fb25
Accessed August 2019.

Burford Capital (August 2019)/Continued

> It has upped the value of its star asset, “Petersen”, a claim against the Argentine government, by 150% to $1bn based on selling minority stakes. Yet if Burford had to offload the claim tomorrow, it would never get that price — and as Therium’s experience with Brooke proved, winning and getting the money can be two separate things.
>
> Litigation funding is fundamentally unsuited to the public markets. Burford may not be guilty of every amped-up allegation Muddy Waters makes, but I doubt this story will end happily.

That valuation of the Petersen claim is also subject to a currency risk and on the 12 August 2019, the Argentinian peso dropped 25%. That would wipe out up to one quarter of the value of the Petersen valuation.

More recently Burford tried to calm the markets by replacing the CEO’s wife as finance chief. Burford said it had replaced Elizabeth O’Connell, wife of chief executive Christopher Bogart, as finance chief with “immediate effect”. Jim Kilman, a former Morgan Stanley banker, was named as her replacement[83].

Things may have just got worse[84]:

> Burford Capital has been accused of knowing that one of its directors leaked client-sensitive information in return for a sex tape.
>
> The litigation funder has become embroiled in a $91m (£74m) court case involving a Russian tanker company, Novoship, which alleges documents were leaked by Dan Hall, co-head of global corporate intelligence for Burford.
>
> He and the litigation funder have been accused of “deceit” by Novoship, which claims they knew that disclosing the information was a breach of “a duty of confidence”, according to court documents.
>
> The allegations raise questions over how Burford treats client information. They are another blow to the firm — a top holding in Neil Woodford’s frozen Equity Income fund — after an attack from the short-seller Muddy Waters Research earlier this month, which almost halved its market value.
>
> Hall allegedly gave sensitive documents he had obtained while working for Novoship to a contact who supplied him with “video material of a sexual nature” relating to the American billionaire Harry Sargeant III, whose assets Hall was investigating in a separate case. Burford recouped about $12m from Sargeant in 2017, according to reports.

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[83] Beioley, K., and Smith, R., Burford tries to calm storm by replacing CEO’s wife as finance chief, *Financial Times*, 15 August 2019.
Available at:
https://www.ft.com/content/ce24cee4-bf6d-11e9-89e2-41e555e96722
Accesses August 2019.

[84] Dunkley, E., Burford Capital ‘knew of sex-tape swap’, *Sunday Times*, 25 August 2019.
Available at:
https://www.thetimes.co.uk/article/burford-capital-knew-of-sex-tape-swap-2sp0tmt8b
Accesses August 2019.

Japan Post (August 2019)

This is a case of mis-selling rather than accounting errors or misstatements[85]:

> Four years, $23bn worth of share issuance and a ballooning insurance mis-selling scandal later, the country has learnt a much coarser reality about how Japan Post's insurance sales force is prepared to treat the elderly. And while the breach of public trust is seismic, the insight into the world's fastest-ageing economy and the warnings for the rest of corporate Japan are arguably even greater.
>
> An internal investigation into the five years of business to 2018 last week reported 183,000 cases of dubious sales practice — twice the number it declared a few weeks ago when the problem first came to light. The company, which insures 15 per cent of Japan's population and has 20m policyholders, has said it will not actively sell any new policies until the end of August.
>
> The sudden jump in the scale of the scandal came about when the probe was expanded from its original two-year scope. That suggests the malpractice could date back even further and may have been well entrenched before Japan Post began exploiting its "pillar of the community" image to sell its mega-listing. The emergence of the scandal just as Japan Post was preparing to issue the third of three Y1.3tn ($12.2bn) tranches of shares in September has convinced many investors that the sale will be delayed into the next calendar year.
>
> The broad facts of the scandal, in which Japan Post Insurance sales staff managed to fox tens of thousands of customers into paying double premiums or switching into less advantageous new policies, are bad enough. The minutiae reported by Japanese media — including a 90-year-old woman sold 54 policies in 10 years and sales staff slang for the "half-senile" — have disgusted the public.
>
> Corporate scandals erupt all the time but Japan Post holds a particular place in the national psyche and the ripping off of the elderly by their supposed champion delivers a supremely acute sting. Its banking and insurance units, in particular, exist in the public imagination as bastions of trustworthiness. That faith has been doubly shattered by both the scandal itself and the mounting public suspicion that the mis-selling was covered up to smooth the initial public offering in 2015.
>
> Grim though that all is, Japan Post's crisis becomes most troubling in the context of the country's recent roster of big scandals — a list that includes Suruga Bank's mis-selling of loans, Toshiba's accounting debacle, Kobe Steel's data falsification and Subaru's inspection fraud. In all those cases (and others) the core wrong originates in an effort to meet targets that were wholly divorced from reality but could not, for whatever reason, be challenged. Avarice, at the personal level, barely featured as a motive.

[85] Lewis, L., Post scandal lays bare mythology of corporate Japan, *Financial Times*, 6 August 2019.
Available at:
https://www.ft.com/content/50a29b66-b849-11e9-8a88-aa6628ac896c
Accessed August 2019.

Ruihua Certified Public Accountants (August 2019)

Of course China has always had a somewhat dodgy history to governance, controls and audit violations. This more recent one is no exception expect that it has scale and has alarmed the authorities in China[86]:

> An accounting scandal rocking corporate China is drawing comparisons with the collapse of US firm Arthur Andersen as dozens of Chinese companies are forced to halt public listing work.
>
> Ruihua Certified Public Accountants, one of China's largest accounting firms, was investigated by the country's securities regulator early this month after a listed company it audited was found to have inflated profits by about Rmb12bn ($1.74bn) over four years.
>
> The probe has caused an unprecedented disruption in fundraising activities for Chinese companies, with more than 50 Ruihua clients halting initial public offerings and private capital raising, according to state media.
>
> The China Securities Regulatory Commission has suspended IPO approvals for at least 20 Ruihua clients. Several listings on China's new Star Market board have also been delayed.
>
> Ruihua did not respond to emailed queries.
>
> The situation, which Chinese media have dubbed the "Ruihua incident", is evoking the collapse of US accounting firm Arthur Andersen, one of the largest in the world until the 2001 bankruptcy of energy group Enron led to its dissolution.

[86] Weinland, D., China accounting scandal threatens corporate fundraising, *Financial Times*, 31 July 2019. Available at:
https://www.ft.com/content/6ae569ee-b336-11e9-8cb2-799a3a8cf37b
Accessed August 2019.

1MDB

The 1Malaysia Development Berhad scandal is an ongoing financial and political scandal occurring in Malaysia. It is too complex to go into in detail. Sums of up to $1 billion or more have been channelled improperly. This reference is comprehensive:
https://en.wikipedia.org/wiki/1Malaysia_Development_Berhad_scandal

It involves three of the Big Four, Deloitte, EY and KPMG and the bank Goldman Sachs. Recently the FT reported some penalties being levied from this scandal which started in 2015 and continues today[87]:

> Hong Kong's securities regulator has banned former Goldman Sachs partner Tim Leissner for life after he pleaded guilty to charges related to the multibillion-dollar 1MDB scandal in Malaysia.
> The Securities and Futures Commission said on Wednesday it had banned Mr Leissner from re-entering the industry, saying his conduct "demonstrates a serious lack of honesty and integrity and called into question his fitness and properness to be a licensed person".
> The Monetary Authority of Singapore also banned Mr Leissner from the city state's securities industry for life in December. Mr Leissner pleaded guilty to US charges that he participated in the fraud and is awaiting sentencing.
> In May, the judge in the trial of former Goldman banker Roger Ng, a central figure in the 1MDB scandal, extended the time for prosecutors to produce evidence and present it to the defence. Mr Ng, 46, has pleaded not guilty to allegations of bribery and money laundering after his extradition to the US from a Malaysian jail.
> …
> A Goldman spokesperson said: "Tim Leissner deliberately hid certain activities from us and repeatedly violated our policies and procedures. We continue to cooperate with all authorities looking into these matters."

But that was one individual Goldman Sacks as a whole came under further criticism, charges and possible penalties[88]:

> Malaysia has filed criminal charges against 17 current and former Goldman Sachs executives in connection with the 1MDB embezzlement scandal, as it ramps up efforts to recover billions of dollars allegedly missing from the state investment fund.
> Tommy Thomas, attorney-general, said on Friday that the individuals had been charged under the Capital Markets and Services Act, which allows for senior staff to be held responsible for offences committed by their organisations.
> "They occupied the highest executive positions" in three Goldman Sachs subsidiaries, Mr Thomas said in a statement, "and exercised or ought to have exercised decision-making authority over the transactions of those bodies corporate".

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[87] Lockett, H., and Palma, S., Hong Kong securities watchdog deals Tim Leissner lifetime ban, *Financial Times*, 3 July 2019.
Available at:
https://www.ft.com/content/faae7658-9d72-11e9-9c06-a4640c9feebb
Accessed July 2019.

[88] Palma, S., and Shrikanth, S., Malaysia charges Goldman Sachs executives over 1MDB scandal, *Financial Times*, 9 August 2019.
Available at:
https://www.ft.com/content/e0dad026-ba6b-11e9-8a88-aa6628ac896c
Accessed August 2019

1MDB/Continued

> The move marks an escalation in Kuala Lumpur's investigation into 1MDB, from which $4.5bn of public money is alleged to have gone missing. Goldman underwrote a series of bonds in 2012 and 2013 that raised $6.5bn for the fund, much of which is suspected to have been stolen as part of a scheme allegedly masterminded by Jho Low, a Malaysian financier. Mr Low, who has denied any wrongdoing, remains at large.

No doubt this case will continue for some time.

CannTrust (August 2019)

This is a strange case. The company is dealing with the growth and sales of Cannabis – now legal in Canada along authorised parcels of land. KPMG then withdrew its audits[89]:

> Canadian cannabis company CannTrust Holdings Inc. said Friday its auditor KPMG is withdrawing its audits of the company's financial statements for 2018 and the recent March quarter, saying they can no longer be relied on.
>
> KPMG made the decision after a special committee shared newly uncovered information from an investigation that led to senior leadership changes announced on July 25. That was the day that Chief Executive Peter Aceto was fired for cause and President Eric Paul was forced to resign.
>
> The special committee was formed to investigate the actions that led Health Canada to seize five metric tons of the company's cannabis in July after discovering it was being grown in unlicensed rooms. The scandal quickly worsened after a whistleblower told Canadian newspaper the Globe and Mail that employees were instructed to construct false walls to conceal the illegal grow rooms.

Now that is not the end of the story because then the share price suddenly and inexplicably exploded 40% regain all its lost ground and then rising into new highest market values closing to its highest level since a fall in 5 July 2019[90].

[89] Linnane, C., KPMG withdraws audits for CannTrust's 2018 and March quarter after illegal grow scandal, *Market Watch*, 11 August 2019.
Available at:
https://www.marketwatch.com/story/canntrusts-auditor-kpmg-withdraws-audits-for-2018-and-march-quarter-after-illegal-grow-scandal-2019-08-09?siteid=rss&rss=1
Accessed August 2019.
[90] Cherney, M., CannTrust stock explodes 40% during last few minutes of trading,

Goals Soccer Centres (August/September 2019)

The Sunday Times also reported of a partly owned Mike Ashley company[91]:

> The City watchdog has launched an investigation into alleged fraud at five-a-side football group Goals Soccer Centres, as a report claims that directors deleted emails to avoid detection.
>
> The Financial Conduct Authority (FCA) has acted after Goals, backed by Mike Ashley's Sports Direct, said it had uncovered "improper behaviour" stretching back almost a decade.
>
> The inquiry comes as a report, prepared by forensic accountants at BDO, alleges that former finance chief Bill Gow sent email requests to former chief executive Keith Rogers asking him to "work your usual magic" and create false invoices. According to the report, the pair also made adjustments to the financial results with the intention of preventing Goals breaching key banking covenants with lender Bank of Scotland.
>
> Gow, who left Goals last year, allegedly arranged for some emails to be deleted — even asking an external IT provider to help him "purge" historic items.
>
> Other emails suggest the pair panicked when an airline lost Rogers's laptop.

The latest event is that Sports Direct has approached Goals Soccer Centres with a possible offer to buy the ailing football pitch operator at a heavily discounted price of less than £4m ahead of its expected delisting next week. Sports Direct approached Goals Soccer Centres with this offer to buy the ailing football pitch operator at a heavily discounted price of less than £4m ahead of its expected delisting next week[92]:

> Mike Ashley's group — already the biggest shareholder in Goals with a 19 per cent stake — said on Monday that it had proposed a possible cash offer to the Goals board of 5p a share on September 5. This would value the group at around £3.6m — a fraction of its £20.5m market capitalisation when its shares were suspended in March.
>
> Sports Direct has been particularly scathing of Goals' management and led a failed attempt to oust the entire board at its June AGM over what it said had been a "lack of transparency" surrounding the accounting debacle. Shares in Goals are expected to be cancelled at the end of September as the company has been unable to publish its accounts due to the investigation. The group last month put itself up for sale as its crisis deepened.
>
> Sports Direct said on Monday that should the delisting proceed, Goals' shareholders would lose the ability to influence the sales process.

[91] Meddings, S., Watchdog FCA pursues Goals Soccer Centres, backed by Mike Ashley, *The Sunday Times*, 11 August 2019.
Available at:
https://www.thetimes.co.uk/article/watchdog-fca-pursues-goals-soccer-centres-backed-by-mike-ashley-pg2wnc550
Accessed August 2019.

[92] McCormick, M., Sports Direct weighs £4m buyout of Goals Soccer Centres. Financial Times, 23 September 2019.
Available at:
https://www.ft.com/content/77130138-ddc8-11e9-b112-9624ec9edc59
Accessed September 2019.

PwC Mexico (August 2019)

This is a balck mark of this auditor albeit in an often crisi torn Mexican business community. Going Concern reported[93]:

> A friendly reminder to audit firms: an auditor must maintain independence in both fact and appearance. Maybe PwC Mexico forgot this when it took over in fiscal year 2016 as the auditor of one of the largest financial services holding companies in Mexico.
>
> It just so happened that at the time the engagement letter was signed, at least six of PwC Mexico's partners had personal financial relationships with that bank, which Francine McKenna of MarketWatch reported was Banco Santander Mexico. That's a no-no under those pesky auditor independence rules, as the PCAOB found the partners' ties to the bank as "inconsistent with a firm's obligation to maintain independence from its audit client."
>
> So, the PCAOB fined PwC Mexico $100,000 on Aug. 1 for violating rules and standards related to P. Dubs' independence, audit committee communications, and system of quality control.

[93] Bramwell, J., PwC Mexico Partners Must Have Thought Auditor Independence Rules Did Not Apply to them, *Going Concern*, 7 August 2019.
Available at:
https://goingconcern.com/pwc-mexico-partners-must-have-thought-auditor-independence-rules-did-not-apply-to-them/
Accessed August 2019.

General Electric (August 2019)

Two events to update progress on this troubled conglomerate:

1) GE's auditor relationship came under scrutiny last year after startling, multibillion-dollar charges in its finance and power businesses raised questions about KPMG's ability to provide proper oversight. Under then-CEO John Flannery, GE defended its auditor and said dumping KPMG would be costly[94]. Proxy advisory firms Glass Lewis & Co. and Institutional Shareholder Services last year recommended that shareholders reject the auditor at GE's annual meeting, an unusual decision prompted by the "severity and ongoing nature'' of accounting issues. While KPMG was ultimately brought back, support dropped dramatically: About 65 percent voted in favor, down from almost 97 percent the prior year.
2) Enron and WorldCom were two of the largest frauds in history (though in stemming from the US), it is now claimed (but not proven) that GE has conducted an even bigger fraud. It ought to be said that this is not universally accepted and after a sharp fall in share price, GE's shares recovered somewhat. The story is[95]:

> An accounting fraud "bigger than Enron and WorldCom combined" is hidden inside General Electric, according to the financial investigator who sounded the first alarms over Bernard Madoff's Ponzi scheme.
>
> GE, which dismissed the claims as meritless, saw its shares fall as much as 15 per cent after publication of a 170-page report by Harry Markopolos. He alleged that the industrial conglomerate's accounts concealed a $38bn fraud in its insurance and oilfield services businesses. "I think that they're a bankruptcy waiting to happen,"
>
> Mr Markopolos told CNBC. Mr Markopolos is known for his — largely unheeded — warnings on the Madoff Ponzi scheme in the years before it imploded in 2008.
>
> He and his team provided an advance copy of their report on GE to a hedge fund and said they would share profits from any market moves their allegations set off.
>
> Larry Culp, GE's chief executive, called that arrangement "market manipulation — pure and simple". In a statement, he said: "The fact that he wrote a 170-page paper but never talked to company officials goes to show that he is not interested in accurate financial analysis but solely in generating downward volatility in GE stock so that he and his undisclosed hedge fund partner can personally profit."

[94] Clough, R., GE Urged to Drop Auditor KPMG Following Accounting Missteps, *Bloomberg*, 16 April 2019.
Available at:
https://www.bloomberg.com/news/articles/2019-04-16/ge-urged-to-drop-kpmg-as-auditor-following-accounting-missteps
August 2019.
[95] Meyer, G., and Badkar, M., GE shares tumble after Madoff investigator alleges $38bn fraud, *Financial Times*, 15 August 2019.
Available at:
https://www.ft.com/content/20c2e468-bf57-11e9-89e2-41e555e96722
August 2019.

General Electric (August 2019)/Continued

This story will continue. Some say there is no smoke without fire. Others say that this a is leftover from earlier and admitted erroneous valuations of their insurance business. However time will tell.

Continued

Disney (August 2019) [PwC]

The mainstream press did not report this or not in any detail so we are not sure what to make of this accusation. So in the interests of completeness we have included it. This was report by Market Watch[96]:

> A former Walt Disney Co. accountant says she has filed a series of whistleblower tips with the Securities and Exchange Commission alleging the company has materially overstated revenue for years.
>
> Sandra Kuba, formerly a senior financial analyst in Disney's DIS, +0.25% revenue-operations department who worked for the company for 18 years, alleges that employees working in the parks-and-resorts business segment systematically overstated revenue by billions of dollars by exploiting weaknesses in the company's accounting software.
>
> ….
>
> A Disney spokesperson said the company had reviewed the whistleblower's claims and found that they were "utterly without merit."
>
> Kuba's whistleblower filings, which have been reviewed by MarketWatch, outline several ways employees allegedly boosted revenue, including recording fictitious revenue for complimentary golf rounds or for free guest promotions. Another alleged action Kuba described in her SEC filing involved recording revenue for $500 gift cards at their face value even when guests paid a discounted rate of $395.

Continued

96 Disney whistleblower told SEC the company inflated revenue for years, Market Watch, 21 August 2019. Available at: https://www.marketwatch.com/story/disney-whistleblower-told-sec-the-company-inflated-revenue-for-years-2019-08-19
Accessed August 2019.

H2O (August 2019) [Deloitte]

The FT explains this case whereby the auditors are actually being accused of negligence to the FRC[97] and as explained below several of these may result in cases whereby the auditors are sued – which is a rare occurrence in the UK:

> Deloitte has been dragged into a long-running scandal over a collapsed telecoms company that laid cables in the UK's sewer network, after its founder reported the auditor to regulators.
>
> Elfed Thomas, the founder and former chief executive of H2O Networks, commissioned a forensic accountant to evaluate Deloitte's performance as the company's auditor during a period when a £160m financing fraud took place.
>
> This week he submitted the report alleging potential negligence by Deloitte, which became H2O Networks' auditor in 2003, over its historic audits to the Financial Reporting Council. He has also appointed law firm Keystone to start legal proceedings against the auditor.
>
> It is the latest in a growing number of actions against auditors accused of negligence for failing to spot fraudulent activity that led to trading losses.
>
> H2O Networks was one of the first companies to lay fibre cables in sewer networks, which cuts costs by removing the need to dig up roads. It was seen as a potential challenger to BT and Virgin Media but collapsed into administration in 2011 after the Serious Fraud Office launched an investigation into its financing arrangements.
>
> A company called Total Asset Finance had arranged loans, based on the value of H2O Networks' contracts, from KBC and Barclays to finance expansion. However many of the contracts were inflated in value or did not even exist and four men, including H2O Networks' finance director Carl Cumiskey, were convicted of conspiracy to commit fraud in 2017.
>
> The company's broadband assets were sold out of administration for a nominal sum to the then start-up company CityFibre, which floated in 2014, and was sold four years later for £538m to the Goldman Sachs fund West Street Infrastructure and Antin Infrastructure Fund.
>
> Mr Thomas was acquitted as part of the H2O Networks trial. He later commissioned John Frenkel, a forensic accountant, to explore potential negligence by Deloitte. The report submitted to the FRC alleges that Deloitte's audit of H2O Networks' 2009 and 2010 accounts had not been thorough and missed key issues that would have uncovered the fraud and saved the company from collapse.

Continued

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[97] Fildes, N., and Kinder, T., Boss of collapsed UK telecom reports Deloitte to FRC, *Financial Times*, 15 August 2019.
Available at:
https://www.ft.com/content/0f0e5254-bdd4-11e9-b350-db00d509634e
Accessed August 2019.

H2O (August 2019) [Deloitte]/Continued

The report says that it should have been evident that Total Asset Finance was "technically insolvent" and that certain contracts in Bournemouth and Dundee that were sold to TAF to raise new financing did not exist.

Mr Thomas told the Financial Times that the auditor was supposed to be his "sense checker". He has since founded a company that provides broadband internet for new housing developments.

….

A handful of cases have been brought against auditors for negligence in recent years.

In January, Grant Thornton was ordered by the High Court to pay its former audit client Assetco, a fire engine leasing service, damages in excess of £21m for negligence "of the utmost gravity". A judge said Grant Thornton failed to apply appropriate professional scepticism when signing off Assetco's accounts, meaning that dishonesty by some senior executives was not exposed and the company ran up significant trading losses.

Administrators to Patisserie Valerie, the café chain that collapsed this year, are considering a possible negligence claim against Grant Thornton, which audited the business. The official receiver in charge of liquidating the failed government outsourcer Carillion has instructed US law firm Quinn Emanuel to pursue an auditor negligence lawsuit against KPMG.

Continued

QuadrigaCX a cryptocurrency failure (August 2019)

Well cryptocurrencies are supposed to be ultra secure? Right. In practice this is wrong. This case is a salutary lesson on just how cryptocurrencies are as insecure as anything else[98]:

> Former QuadrigaCX users are losing patience with their court-appointed lawyers and looking for answers about how more than 100 bitcoins were "inadvertently" lost.
>
> QuadrigaCX, once Canada's largest crypto exchange, collapsed virtually overnight earlier this year after CEO Gerald Cotten died while traveling in India. An affidavit filed by Cotten's widow said the exchange owed customers as much as $190 million ($250 million CAD).
>
> The Nova Scotia Supreme Court, which is overseeing the company's unwinding, appointed Big Four auditor Ernst & Young (EY) as monitor to try to recover funds for the exchange's customers, and law firms Miller Thomson and Cox & Palmer (Miller Thomson's Nova Scotia-based local partner) as counsel to represent these customers' interests.
>
> However, some of these creditors believe Miller Thomson and EY are failing to keep costs down or recover user funds. Much of this frustration stems from the 103 bitcoins that were accidentally transferred into wallets whose passwords were known only to the late founder, several creditors told CoinDesk. Unless the passwords are recovered, there's no way to get the bitcoin back.
>
> The blunder occurred in February, and at the time, the lost bitcoin was worth some $375,000 ($500,000 CAD). The coins are now worth about $1.03 million ($1.37 million CAD).
>
> Six months on, EY has not provided much in the way of detail explaining how the bitcoin was transferred to what are effectively locked wallets. In a report published in late February, the firm said the transfer occurred due to a "platform setting error."

Continued

[98] De, N., A Big Four Audit Firm Lost $1 Million In Bitcoin. Victims Are Losing Patience, *Coindesk*, 16 August 2019,

Wrightbus failure (September 2019)

The Northern Irish company that built London's distinctive red double-decker "Boris bus" (officially called the New Routemaster) went into administration, with 1,200 workers made redundant.

There is no evidence of any wrongdoing. Brexit uncertainty, the cyclic nature of bus demand, the fall in the pound (a function of Brexit), budgetary pressure on the bus buying authorities, uncertainty as to the switch to electricity, and so on.

See this reference for the best background on this collapse:

Campbell, J., Wrightbus: From driving seat to financial failure, *BBC News*, 25 September 2019. Available at:
https://www.bbc.co.uk/news/uk-northern-ireland-49801334
Accessed September 2019.

Continued

Clarks (late September 2019)

The Sunday Times[99] broke this story and it is uncertain as two whether there is any substance to this accounting irregularity. The background as reported is:

> Shearwood claims he was not given a chance to respond to the allegations before being forced to resign and says a press statement announcing his ousting was issued hours after he was presented with them. In an employment tribunal ….in Bristol…

Clarks is the 36th-biggest private company in Britain by sales (Sunday Times Top Track 100 index). If private equity-backed companies were excluded, it would rank 22nd. Clarks made a £31.3m post-tax loss last year (2917: £24.5m and 2016: £36m). The 2018 annual report tended to blame Brexit as well as the UK. For the US, the company mainly blamed the poor performance on Donald Trump's tax reforms, which it said had reduced the value of its historic tax losses in the US. And that does not sound like a plausible reason. Group revenue was down and sales of shores were down in all geographical markets but the largest fall was in Europe – indicating that Brexit may have had a significant impact as well as the fall in the pound – though one would have expected an impact in 2017 as well. .

Oliver Shah[100] expects the claims to be:

1) Clarks was close to insolvent when he joined in September 2016. It is not clear that this can be substantiated.
2) A crucial refinancing deal was being held up because one of its lenders, Barclays, was troubled by an investigation into whether Clarks had breached sanctions on Iran, and by its practice of paying dividends using debt. . Paying dividends by increasing borrowings sounds a very Carillion like behaviour and something that should cause real criticism.
3) The chairman at the time, former Burberry president Tom O'Neill, was desperate to hide Clarks' parlous financial position from its family shareholders (who own 86.8% of the equity shares) and to keep paying dividends.
4) Board minutes and accounts were manipulated to disguise the problems. We can confirm that the auditors, EY, gave the company a clean bill of health with note issues or notes. That's aid the annual report does not make any reference or real explanation, or strategy to overcome the worsening financial situation.
5) Clarks' international divisions were in disarray, with losses hidden in its American business and fraud uncovered in China and Malaysia. We can't comment as there is insufficient information. For us the real problem was Europe.

No doubt further revelations and information will be forthcoming.

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[99] Shah, O., Clarks faces tribunal with ex-boss Mike Shearwood amid claims of racist and sexist language and allegations of fraud, The Sunday Times, 29 September 2019.
Available at:
https://www.thetimes.co.uk/article/clarks-faces-tribunal-with-ex-boss-mike-shearwood-amid-claims-of-racist-and-sexist-language-and-allegations-of-fraud-dl6kj9b7z
Accessed September 2019.
[100] Ibid.

PwC in bid to dismiss £25m claim over Guernsey ‘Ponzi’ scheme | Financial Times

This is a tricky case. It is disputed as the heading shows. PwC wants to dismiss a £25m lawsuit in which it is accused of negligence for signing off on the accounts of Providence Investment Fund, a Guernsey “Ponzi scheme” that collapsed owing investors millions. The suit

The FT described this case as[101]:

> PwC is trying to quash a £25m lawsuit in which it is accused of negligence for signing off on the accounts of Providence Investment Fund, a Guernsey “Ponzi scheme” that collapsed owing investors millions.
>
> The Big Four accounting firm has filed an application to dismiss the claims against it, which are being brought by administrators to the failed investment company in the Guernsey courts.
>
> The administrators at Deloitte, another large accounting firm, are suing PwC for “negligence, breach of duty and breach of contract” in its role as auditor to the Providence fund. PwC called the lawsuit “misconceived” and said it would vigorously defend it.
>
> Providence was put into administration in 2016 owing investors, who were promised returns of up to 14 per cent, more than £40m. Court documents filed by lawyers for the administrators allege the business was run as a “fraudulent Ponzi scheme”.
>
> Providence claimed to invest in Brazilian factoring, a type of debt financing. Instead, 97 per cent of investors’ money was used to finance the wider Providence group, according to the court papers

/Continued

[101] Kinder, T., PwC in bid to dismiss £25m claim over Guernsey ‘Ponzi’ scheme, Financial Times, 30 September 2019.
Available at:
https://www.ft.com/content/1b0a3768-e2b3-11e9-9743-db5a370481bc
Accessed September 2019.

Credit Suisse, suicide and a spy scandal (Oct 2019)

This is not an accounting issue and this reference[102] is a good explanation of the scandal. Senior management started spying on another executive before and after he left to go to a Swiss rival bank, UBS. The person being spied upon found out and submitted a criminal complaint. The chief operating officer and the head of security of Credit Suisse resigned.

The chairperson became involved in trying to clean-up the issue. The person being spied upon was the head of wealth management. Credit Suisse staff involved ordered the spying because of fears that he was preparing to poach bankers and clients to bolster the fortunes of the rival UBS bank[103]. The bank has been under pressure as details of the spying operation became public, including a chase and subsequent altercation between the person being spied upon and a private investigator. Then the contractor involved in the surveillance of this 'high-flying' executive committed suicide.

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[102] Jones, S., Crow, D., and Shane, D., Credit Suisse rocked by suicide as spy scandal deepens, Financial Times, 1 October 2019.
Available at:
https://www.ft.com/content/53da861a-e407-11e9-9743-db5a370481bc
Accessed October 2019.
[103] Ibid.

M&C Saatchi (October 2019)

Shares in M&C Saatchi lost nearly half their value after the company disclosed a "misapplication of accounting policies" in August 2019. It emerged the company had at times counted outstanding fees as revenues and included assets no longer used, such as old software, on its balance sheet[104].

PWC is poised to take over the audit from KPMG, which resigned amid an accounting controversy that plunged M&C Saatchi into its worst crisis since it was founded in 1995. This is despite being hit with fresh accusations of a conflict of interest after it was lined up as auditor to M&C Saatchi despite also doing advisory work for the listed advertising agency[105].

Ted Baker (KPMG)

Admitted breaching ethical standards and losing independence in the audits. As reported by Accountancy Age[106]:

> The Financial Reporting Council (FRC) has imposed sanctions against KPMG and a senior statutory auditor over the audits of retailer Ted Baker.
>
> The Big Four firm together with Michael Francis Barradell, senior statutory auditor and audit engagement partner, has been fined and reprimanded by the watchdog following admission of misconduct in the audits of Ted Baker's financial statements.
>
> The misconduct occurred during the financial years ending 26 January 2013 and 25 January 2014, and apply to Ted Baker plc and No Ordinary Designer Label Limited, which combined make up Ted Baker.
>
> Settlement terms have been agreed by the FRC's Executive Counsel. KPMG will receive a Severe Reprimand plus a fine of £3,000,000, which has actually been discounted due to the firm's agreement to settle to £2,100,000.

[104] Kinder, T., PwC poised to take over as auditor for M&C Saatchi, *Financial Times*, 28 October 2019. Available at:
https://www.ft.com/content/fd564de6-f749-11e9-9ef3-eca8fc8f2d65
Accessed October 2019.
[105] Ibid.
[106] Skoulding, L., KPMG fined and reprimanded over Ted Baker audits, *Accountancy Age*,

Nichols Plc

Reuters reported[107]:

> LONDON (Reuters) - The Financial Reporting Council (FRC) said on Wednesday it had fined Grant Thornton 4 million pounds ($5.1 million) after four of its senior staffers admitted misconduct in handling the financial audits of Nichols Plc and the University of Salford.
>
> The latest in a series of reprimands for several of Britain's biggest auditing firms, the FRC said it had also issued a 200,000 pound fine to the company's former senior partner Eric Healey and excluded him from the Institute of Chartered Accountants in England and Wales for five years.
>
> The FRC found Healey, who settled a discounted fine of 150,000 pounds, was providing consultancy services while at the same time performing duties on the audit committees of Nichols Plc and the University of Salford.
>
> The FRC said this created "serious familiarity and self-interest" and resulted in the loss of independence in respect of eight audits over the course of four years.

[107] Reuters, Grant Thornton hit with $5.1 million fine over audit misconduct, *Reuters*, 29 August 2019. Available at:
https://uk.reuters.com/article/uk-grantthornton-fine/grant-thornton-hit-with-5-1-million-fine-over-audit-misconduct-idUKKCN1LE0KHAccessed August 2019.

Late 2018

KPMG have probably had worst set of challenges and comments, plus special measures from the FRC, has the largest audit growth, and soars past FTSE 100 as leader taken from the PwC. 8 November 2018.
https://www.accountancydaily.co/kpmg-grabs-largest-number-ftse-100-audits
KPMG will stop providing non-audit services to listed companies whose finances they are inspecting after coming under intense pressure over perceived conflicts of interest.
Bill Michael, KPMG's UK chair, said the firm would stop providing non-audit services for FTSE 350 companies "to remove even the perception of a possible conflict", in a memo to partners sent on Thursday. The firm declined to give an end date for the changes.
https://www.theguardian.com/business/2018/nov/08/kpmg-to-drop-non-audit-services-for-its-ftse-350-clients
KPMG and Deloitte have backed a suggested ban on UK auditors selling extra services to audit clients. KPMG has made the decision to stop providing any non-audit services for FTSE 350 clients, unless it is essential; Deloitte has followed suit.
https://www.accountancyage.com/kpmg-deloitte-and-the-audit-dilemma/
See quotes from the Guardian article at the end.

PwC starts roundtable discussions on future of audit
The company has set up a web page and will produce a white paper with suggestions on how the audit sector can move forward. 27 November 2018.
https://www.accountancyage.com/2018/11/27/pwc-starts-roundtable-discussions-on-future-of-audit/
https://www.accountancydaily.co/pwc-opens-discussions-future-audit
And for the website hosted by Gilly Lord, PwC's Head of Audit Strategy and Transformation
https://www.pwc.co.uk/services/audit-assurance/statutory-audit/insights/confidence-in-the-future-audit-innovation/confidence-in-the-future-gilly-lord-video.html

BDO to merge with Moore Stephens
But this won't make a rival for the Big Four. As noted in the audit market book such mergers fail to get anywhere near the size of the Big Four. This may change but it would require many more mergers and acquisitions plus some organic growth. We cannot see this happening but we would not rule it out as a possibility.
https://www.accountancyage.com/2018/11/26/bdo-to-merge-with-moore-stephens/
In a similar vain Baker Tilly come together with RGL Forensics.
https://www.accountancyage.com/2018/12/05/baker-tilly-come-together-with-rgl-forensics-to-create-global-accounting-practice/

Continued

Possible issues post publication

FRC has opened an investigation into PwC for its audit work on the Eurasian Natural Resources Corporation (ENRC).
https://economia.icaew.com/news/december-2018/frc-investigates-pwc-over-enrc-audit
KPMG to face FRC misconduct hearing over Silentnight
https://www.accountancydaily.co/kpmg-face-frc-misconduct-hearing-over-silentnight
Patisserie Valerie faces FRC audit probe (Auditor: Grant Thornton)
https://www.accountancydaily.co/patisserie-valerie-faces-frc-audit-probe

Other opinions and developments

Call to 'think small' on audit standards
https://www.accountancydaily.co/call-think-small-audit-standards
Woolf: auditors need to go back to basics
https://www.accountancydaily.co/woolf-auditors-need-go-back-basics
Software license auditing risks conflict of interest
https://www.accountancydaily.co/software-license-auditing-risks-conflict-interest
Deloitte takes over from PwC at Lloyds Bank after 153 years
https://www.accountancydaily.co/deloitte-takes-over-pwc-lloyds-bank-after-153-years
ICAEW says tougher FRC sanctions bad for audit competition
'Despite several high-profile corporate collapses and audit failures in recent years, we are sceptical that the number of competitors - as such - available in the market for large corporate and public interest entity (PIE) audits has a direct causal link to auditor performance.'
Then they would say that wouldn't they. Our analysis and evidence disagrees. An increase in largish competitors (such as splitting the Big Four audit divisions) would improve performance and quality.
https://www.accountancydaily.co/icaew-says-tougher-frc-sanctions-bad-audit-competition