

Edited for publication

IN THE MATTER OF:

**THE EXECUTIVE COUNSEL OF THE FINANCIAL
REPORTING COUNCIL**

-and-

(1) MacIntyre Hudson LLP

(2) Deborah Weston

(3) Geeta Morgan

FINAL SETTLEMENT DECISION NOTICE
Pursuant to Rule 108 of the Audit Enforcement Procedure

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

This document has been edited for publication in line with the FRC's Publication Policy (Audit Enforcement Procedure). Clarificatory words have been added for the purposes of publication.

I. INTRODUCTION

1. The Financial Reporting Council (the "**FRC**") is the competent authority for statutory audit in the UK and operates the Audit Enforcement Procedure, effective 5 January 2022 (the "**AEP**"). The AEP sets out the rules and procedure for the investigation, prosecution and sanctioning of breaches of *Relevant Requirements*.
2. The AEP contains a number of defined terms and, for convenience, those defined terms are also used within this document. Where defined terms are used, they appear in italics.
3. This *Final Settlement Decision Notice* also uses the following definitions:
 - 3.1. "**MHA**" means MacIntyre Hudson LLP;
 - 3.2. "**MRG UK**" means MRG Finance UK PLC;
 - 3.3. "**MRG SAM**" means Monaco Resources Group S.A.M.;

- 3.4. “**FP2018**” means the period 3 May 2018 to 31 December 2018;
- 3.5. “**FY2019**” means the year ended 31 December 2019;
- 3.6. “**FP2018 Audit**” means the statutory audit of the financial statements of MRG UK for FP2018; and
- 3.7. “**FY2019 Audit**” means the statutory audit of the financial statements of MRG UK for FY2019 (together “the **Audits**”).
4. In accordance with Rule 102 of the AEP, Executive Counsel entered into settlement discussions with MHA, Deborah Weston (“**Ms Weston**”) and Geeta Morgan (“**Ms Morgan**”).
5. A *Proposed Settlement Decision Notice* was issued by Executive Counsel on 8 November 2023 pursuant to Rule 103 of the AEP in respect of the conduct of:
 - 5.1. MHA in relation to the FP2018 and FY2019 Audits. MHA was the *Statutory Audit Firm* for the Audits.
 - 5.2. Ms Weston, a former *partner* of MHA, in relation to the FP2018 Audit. Ms Weston was the *Statutory Auditor* of MRG UK for FP2018 and signed the FP2018 Auditor’s Report on behalf of MHA.
 - 5.3. Ms Morgan, a former Audit Director employed by MHA, in relation to the FY2019 Audit. Ms Morgan was the *Statutory Auditor* of MRG UK for FY2019 and signed the FY2019 Auditor’s Report on behalf of MHA.
6. In this *Final Settlement Decision Notice*, Ms Weston and MHA are referred to as the “**FP2018 Respondents**”. Ms Morgan and MHA are referred to as the “**FY2019 Respondents**”. The three parties together are referred to as the “**Respondents**”.
7. The Respondents provided written agreement to the *Proposed Settlement Decision Notice*, pursuant to Rule 105 of the AEP, on 8 November 2023. The *Convenor* subsequently appointed an *Independent Reviewer*, pursuant to Rule 106 of the AEP, to consider the *Proposed Settlement Decision Notice*.
8. On 22 November 2023, the *Independent Reviewer* approved the issuance of a *Final Settlement Decision Notice* pursuant to Rule 107(a) of the AEP.

9. In accordance with Rule 108 of the AEP this *Final Settlement Decision Notice* sets out:
 - 9.1. the breaches of *Relevant Requirements*, with reasons;
 - 9.2. the *Sanctions* imposed on the Respondents with reasons; and
 - 9.3. the amount payable by the Respondents in respect of Executive Counsel's Costs.
10. This *Final Settlement Decision Notice* is divided into the following sections:
 - 10.1. Section II: *Relevant Requirements* to which the breaches relate;
 - 10.2. Section III: Executive Summary of Breaches of the *Relevant Requirements*.
 - 10.3. Section IV: Background;
 - 10.4. Section V: Breaches of the *Relevant Requirements*;
 - 10.5. Section VI: Sanctions; and
 - 10.6. Section VII: Costs

II. RELEVANT REQUIREMENTS

11. Rule 1 of the AEP states that *Relevant Requirements* has the meaning set out in regulation 5(11) of the Statutory Auditors and Third Country Auditors Regulations 2016 ("**SATCAR**"). The *Relevant Requirements* include, but are not limited to, the International Standards on Auditing (UK) ("**ISAs**") issued by the International Auditing and Assurance Standards Board, International Standard on Quality Control (UK) 1 ("**ISQC 1**") and the Revised Ethical Standard 2016 (the "**Ethical Standard**").
12. The *Relevant Requirements* referred to in this *Final Settlement Decision Notice* are the following:
 - 12.1. ISA 220 (Quality Control for an Audit of Financial Statements)
 - 12.2. ISA 230 (Audit Documentation)
 - 12.3. ISA 250 (Obtaining an understanding of the regulatory framework applicable)
 - 12.4. ISA 260 (Reporting to those charged with Governance)
 - 12.5. ISA 300 (Identifying characteristics of the Engagement)

- 12.6. ISA 315 (Identifying and Assessing the Risks of Material Misstatement)
- 12.7. ISA 330 (Presentation of Financial Statements)
- 12.8. ISA 500 (Audit Evidence)
- 12.9. ISA 570 (Going Concern)
- 12.10. ISA 700 (Forming an Opinion and Reporting on Financial Statements)
- 12.11. ISA 701 (Communicating Key Audit Matters in the Auditor's Report)
- 12.12. The Ethical Standard
- 12.13. ISQC 1 (Quality Control for Firms)
- 13. Extracts from the ISAs, ISQC 1 and Ethical Standard setting out those parts which are of particular relevance to the breaches of *Relevant Requirements* are set out in Appendix 1 hereto.

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

- 14. The Breaches set out in this *Final Settlement Decision Notice* concern the FP2018 and FY2019 Audits of MRG UK and fall into two categories.

Category 1

- 15. Breaches concerned with the failure to conduct the Audits on the basis that MRG UK was a public interest entity (a "**PIE**"). In failing to do so the Respondents breached paragraph 11 of ISA 315 (read with paragraph 13 of ISA 250A) which required them to gain an adequate understanding of MRG UK and the regulatory framework applicable to it. The Respondents also breached paragraph 8(a) of ISA 300 which requires auditors, when establishing an overall audit strategy, to identify the characteristics of the engagement that define its scope. MRG UK being a PIE was such a characteristic.
- 16. There are breaches which then flowed directly from the Respondents' failure to conduct the Audits on the correct basis. Where the financial statements of a PIE are being audited, auditors are required to:
 - 16.1. ensure that an engagement quality control review is performed before the Auditor's Report is signed (ISQC 1, paragraph 36R-1),
 - 16.2. refrain from providing non-audit services to the PIE (Ethical Standard, Section 5); and

- 16.3. present certain prescribed information in the Auditor’s Report (ISA 700).
17. The Audits did not meet these three requirements. In both Audits, no engagement quality control reviewer (“EQCR”) was appointed (and so no EQCR review was performed), non-audit services were provided, and required information was omitted from (or materially incorrect information relating to the provision of non-audit services was included in) the Auditor’s Reports. The failure to conduct the Audits on the basis that MRG UK was a PIE also indicates that inadequate work was performed on acceptance and continuance processes.

Category 2:

18. Breaches which concern other matters in the Audits. These relate to:
- 18.1. reviews of audit work;
 - 18.2. audit work on bank balances;
 - 18.3. audit work on an intercompany loan;
 - 18.4. audit work on the going concern assumption;
 - 18.5. use of the correct Accounting Standards; and
 - 18.6. audit documentation.

IV. BACKGROUND

Audited Entity

19. MRG SAM (a Monaco-based corporation) is the holding company for several other companies which together form the Monaco Resources Group (the “Group”). The Group’s business is focused on natural resources and extends into agribusiness, logistics and technology.¹ MRG SAM incorporated MRG UK on 3 May 2018 as a special purpose vehicle (“SPV”) to raise finance for the Group’s business.
20. On 26 October 2018, MRG UK issued €50 million in Medium Term Notes (the “Notes”) for purchase by investors.² The Notes are, essentially, a promise made by MRG UK to repay the amount stated on each Note (€1,000) on a specified date (26

¹ See, B.16 (p.8) of the Drawdown Prospectus published by the Group.

² The terms “notes” and “bonds” are often used interchangeably. Both refer to the same type of financial instrument – a means of borrowing money from investors. Bonds usually have longer periods than notes, but usage is inexact.

October 2023³), as well as to make annual interest payments of 8.75% to noteholders on 26 October each year. The payments are guaranteed by MRG SAM.⁴ Investors can buy and sell the Notes until they mature; they are listed on the Main Market of the London Stock Exchange and on the Frankfurt Stock Exchange.

21. In order to allow the Group to make use of the money raised by issuing the Notes, MRG UK transferred virtually all of the proceeds to MRG SAM by way of a loan. MRG SAM has agreed to pay interest on the amount borrowed at 9.25%, a rate 0.5% higher than the rate offered by MRG UK to investors. The final repayment of the loan by MRG SAM is intended to fully fund the payments due from MRG UK to the noteholders. Accordingly, MRG UK's ability to repay the Notes is ultimately a matter of MRG SAM's ability to repay the loan to MRG UK prior to the repayment date in 2023.
22. This *Final Settlement Decision Notice* concerns the audit of the financial statements for MRG UK (not its parent company, MRG SAM) for two periods, FP2018 and FY2019.

Auditors

23. MHA was initially approached by the Group Auditor (a member of the same network of firms) on 6 April 2019 to conduct the FP2018 Audit. The Group Auditor was the auditor of the Group's consolidated financial statements in both FP2018 and FY2019.
24. Ms Weston was appointed to be the *Statutory Auditor* for the FP2018 Audit. Ms Weston was a Partner at the time of the FP2018 Audit and had over 30 years of audit experience. Ms Weston was co-head of MHA's financial services audit team.
25. The audit engagement letter for the FP2018 Audit was issued and signed on 18 April 2019, twelve days before the deadline for completing the FP2018 Audit. Ms Weston signed the Auditor's Report for the FP2018 Audit on 30 April 2019.
26. MHA were subsequently re-appointed as auditors for FY2019, and a planning meeting was held with MRG UK's management on 14 January 2020. As Ms Weston was due to retire from MHA in May 2020, Ms Morgan was appointed to be the *Statutory Auditor* for the FY2019 Audit. Accordingly, both Ms Weston (as outgoing

³ Which has since been extended to 26 October 2026.

⁴ The details of the Notes are set out in the Base Prospectus, Terms and Conditions of the Notes and a supplemental Drawdown Prospectus, published by the Group.

Statutory Auditor) and Ms Morgan (as incoming *Statutory Auditor*) attended the planning meeting with management. Ms Morgan had joined MHA on 4 November 2019 as an Audit Director and was to take on a number of Ms Weston's audit engagements. At the time of the FY2019 Audit Ms Morgan had over 16 years of experience in financial services audit.

27. MHA prepared an engagement letter dated 3 March 2020 setting out a schedule of services to be provided and the terms of the engagement. Ms Morgan then reviewed and signed the engagement letter. The engagement letter was sent to MRG UK on 5 March 2020 and counter-signed on 4 April 2020. Ms Morgan signed the Auditor's Report for the FY2019 Audit on 30 April 2020.
28. At that time MHA had an internal policy requiring that three audit engagements (where the individual had acted as the Responsible Individual⁵ ("RI")) be reviewed by the firm's technical team, before a newly appointed RI was permitted to sign an Auditor's Report on behalf of the firm. The policy applied to all newly appointed RIs at MHA, so applied to Ms Morgan, notwithstanding that she had acted as an RI at her previous firm. The policy was not adhered to in this case, as only one such review was completed before the FY2019 Auditor's Report was signed.

Responsibility of Statutory Audit Firms and Statutory Auditors

29. As the *Statutory Audit Firm* responsible for the Audits, MHA is responsible for any breaches of *Relevant Requirements* on the part of its partners or employees.
30. As the *Statutory Auditor* responsible for the FP2018 Audit Ms Weston was responsible for the overall quality of the FP2018 Audit⁶ and the direction, supervision and performance of the FP2018 Audit in compliance with professional standards and applicable legal and regulatory requirements⁷. Accordingly, together with MHA as the *Statutory Audit Firm*, Ms Weston is responsible for any breaches of the ISAs in relation to the FP2018 Audit. The same is true of Ms Morgan in relation to the FY2019 Audit. The *Statutory Auditor* is also under a personal obligation to consider whether sufficient appropriate audit evidence has been obtained to support the conclusions in the Auditor's Report⁸.

⁵ Being a principal or employee responsible for audit work and designated as such under Audit Regulation 4.01.

⁶ ISA 220, paragraph 8

⁷ ISA 220, paragraphs 9, 10 and 15

⁸ ISA 220, paragraph 17

31. As noted above, at the time of the FY2019 Audit Ms Morgan was an Audit Director, not a partner in MHA. However, that does not affect her statutory responsibility for the conduct of the FY2019 Audit.
32. There is disagreement between the Respondents (MHA and Ms Weston on the one hand, and Ms Morgan on the other) about some aspects of the FY2019 Audit. This includes differing factual accounts regarding some conversations that are said to have taken place between Ms Morgan and Ms Weston, and disagreement as to whether MHA's technical team was consulted by Ms Morgan (or at her request) about whether an EQCR review was required for the FY2019 Audit and whether MRG UK was a PIE. This does not impact the statutory responsibilities of MHA and Ms Morgan (as set out at paragraphs 28-29 above) for the conduct of the FY2019 Audit.

V. BREACHES OF RELEVANT REQUIREMENTS

Category 1: Failure to audit MRG UK as a PIE

Failure to identify MRG UK as a PIE

33. Paragraph 13 of ISA 250 Section A requires that, as part of obtaining an understanding of an entity in accordance with ISA 315, an auditor must obtain a general understanding of the regulatory framework applicable to the entity. Understanding whether or not MRG UK was a PIE was an essential part of understanding the regulatory framework applicable to it. Further, paragraph 8(a) of ISA 300 requires auditors, when establishing an overall audit strategy, to identify the characteristics of the engagement that define its scope. MRG UK's status as a PIE was such a characteristic.
34. The FP2018 and FY2019 audit teams failed to ultimately identify that MRG UK was a PIE. Accordingly, the FP2018 Respondents (re the FP2018 Audit) and FY2019 Respondents (re the FY2019 Audit) breached paragraph 11 of ISA 315, paragraph 13 of ISA 250 and paragraph 8(a) of ISA 300 as, in both Audits, there was a failure to gain an adequate understanding of MRG UK and the regulatory framework applicable to it, or to identify one of the characteristics of the audit engagement that defined its scope.

Acceptance and continuance of the Audits

35. At the time of the FP2018 Audit, MHA had a policy of not auditing PIEs, so the FP2018 Audit engagement should not have been accepted. The decision to accept the FP2018 Audit engagement, resulting from the erroneous assumption by Ms Weston that MRG UK was not a PIE, was therefore inappropriate. Further, the FP2018 Audit was accepted a matter of weeks before providing an Auditor's Report. Ms Weston (re the FP2018 Audit) failed to perform adequate work to determine that conclusions reached regarding the acceptance of the FP2018 Audit were appropriate. Accordingly, the FP2018 Respondents (re the FP2018 Audit) breached paragraph 12 of ISA 220.
36. By the time of the FY2019 Audit, MHA had resolved to enter the PIE audit market. However, as MRG UK was a PIE, it would only have been appropriate to continue the relationship and conduct the FY2019 Audit on terms appropriate for the audit of a PIE. This did not occur, and the FY2019 Audit was performed on an incorrect basis.

Consequences of the failure to audit MRG UK as a PIE

Provision of non-audit services

37. In breach of paragraph 5.167R of the Ethical Standard, the FP2018 Respondents (re the FP2018 Audit) and FY2019 Respondents (re the FY2019 Audit) provided MRG UK with non-audit services in the period between the beginning of the period audited and the issuing of the Auditor's Report in relation to both the FP2018 and FY2019 Audits, as MHA prepared MRG UK's financial statements.
38. Ms Weston (re the FP2018 Audit) and Ms Morgan (re the FY2019 Audit) consequently did not take appropriate action to eliminate the threat to the independence of the Audits created by providing non-audit services. MRG UK being a PIE, the only appropriate action would have been to refrain from providing this non-audit service, as required by the Ethical Standard. Accordingly, the FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit) breached paragraph 11(c) of ISA 220.

No EQCR

39. Ms Weston (re the FP2018 Audit) and Ms Morgan (re the FY2019 Audit) did not determine that an EQCR should have been appointed for the Audits (and therefore dated the respective Auditor's Reports before an EQCR review had been

completed), where the audited entity was both a listed entity and PIE. Accordingly, the FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit) breached paragraph 19 of ISA 220.

Auditor's Report and Audit Committee Report

40. In breach of paragraph 45R-1 of ISA 700 and paragraph 13R-1(a) of ISA 701, the FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit) did not include statements required to be made in the FP2018 and FY2019 Auditor's Reports, being audits of complete sets of general-purpose financial statements of a PIE.
41. The additional report explaining the results of the audit carried out required by ISA 260 that was sent by the FP2018 Respondents (re the FP2018 Audit) and by the FY2019 Respondents (re the FY2019 Audit) to the body performing the equivalent functions to an audit committee consequently did not comply with the requirements of paragraph 16R-2 of ISA 260 and was sent after the audit report in breach of paragraph 21R-1 of ISA 260. In FY2019 the version of the additional report sent did not comply with the requirements of paragraph 20.R-1(b) of ISA 260 as it was not signed.

Particulars of the Breaches

Failure to identify MRG UK as a PIE

42. Auditors must determine whether an entity is a PIE before conducting an audit of that entity's financial statements. The issue is of fundamental importance. The Auditing Standards require additional review of audit work and additional reporting to be performed for the audit of PIEs than for other companies, as further indicated below. This provides a greater level of reassurance to third parties that the financial statements are fair and accurate.
43. There are various reasons why it is necessary for auditors to identify whether the entity is a PIE before performing an audit. When auditing the financial statements of a PIE, the auditor must ensure that an EQCR review is performed. In short, that is a process in which another qualified, experienced, auditor within the same *Statutory Audit Firm*, but independent of the audit team, reviews the audit work conducted to ensure that the conclusions reached are reasonable. Auditors are also prohibited from providing non-audit services (e.g. bookkeeping or preparing accounting

records) to PIEs when providing audit services, and the Auditor's Report accompanying the audited financial statements of a PIE is required to include specific disclosures which go beyond those required for other types of audits.

44. For the purposes of regulation by the FRC, the term "public interest entity" has a precise technical definition. A PIE is defined as "*an issuer whose transferable securities are admitted to trading on a regulated market*".⁹
45. MRG UK was (and remains) a PIE. The Notes issued by MRG UK are freely transferable securities and were admitted to trading on the London Stock Exchange, a regulated market.¹⁰
46. The source of the error in the FP2018 Audit is clear. At the time the FP2018 Audit was accepted, Ms Weston was involved in auditing two other SPVs which had been incorporated for the purpose of issuing bonds. Ms Weston contacted the MHA technical team and was told, correctly, that those SPVs did not meet the technical definition of a PIE. This was because their bonds were listed on non-regulated markets. Ms Weston then assumed, incorrectly, that MRG UK was in a similar position and determined that it was not a PIE. There is no evidence to suggest that the MHA technical team were asked to consider the classification of MRG UK in the FP2018 Audit. Ms Weston proceeded to conduct the FP2018 Audit on the incorrect basis that MRG UK was not a PIE, and no EQCR review was performed prior to the FP2018 Auditor's Report being signed.
47. It appears that the incorrect approach taken in the FP2018 Audit was also a strong driving factor in the FY2019 Audit team not treating MRG UK as a PIE.
48. The facts relating to the FY2019 Audit are more complex. Ms Morgan's evidence is that she understood Ms Weston did not regard MRG UK as a PIE. Ms Morgan's evidence (with which Ms Weston disagrees) is also that, at a meeting in December 2019, shortly after it had been decided that Ms Morgan would take over as *Statutory Auditor*, Ms Weston informed her that MRG UK did not meet the definition of a listed entity contained within the Ethical Standard because its securities were not transferable. Ms Weston's evidence is that she does not recall making such a

⁹ See the FRCs "*Glossary of Terms—Ethics and auditing*", January 2018. PIEs also include certain credit institutions. However, that part of the definition is irrelevant to this *Final Settlement Decision Notice*.

¹⁰ <https://www.londonstockexchange.com/stock/59AY/mrg-finance-uk-plc/company-page>

statement, although Ms Weston has since confirmed that, at the time, she did not believe MRG UK was a PIE. There is evidence that shows a general planning meeting taking place in December 2019. However, there is no documentation on the FY2019 Audit file recording the content of the meeting.

49. On 5 March 2020, in an email to another member of the FY2019 audit team, Ms Morgan identified that the Notes were listed on the London Stock Exchange and that the FY2019 Audit should be subject to an EQCR review.
50. Ms Morgan's evidence is that a member of MRG UK's management informed her that the Notes were not transferable, although that member of MRG's management has since clarified that they understood this discussion to concern the ability to transfer the liability of the Notes, not the transfer of Notes between investors¹¹. Notwithstanding this, as Ms Morgan relied on this conversation to inform her determination of whether MRG UK was a PIE, it would have been important to document this. However, there is no record of this conversation in the FY2019 Audit file.
51. Ms Morgan's evidence is that she then had further discussions regarding the issue of whether MRG UK was a PIE (and the need for an EQCR review) with Ms Weston and Ms Weston suggested that the approach in FY2019 should follow that taken in FY2018. Ms Weston's evidence is that she has no recollection of such discussions. Ms Morgan's evidence is also that she separately discussed whether an EQCR review would be performed with a senior member in MHA's technical team, who she says told her that an EQCR was not required and that following these discussions she was satisfied that no EQCR review was required and that MRG UK was not a PIE. The evidence of that senior member in MHA's technical team is that they made no such statements to Ms Morgan. There is no documentation on the FY2019 Audit file (or elsewhere) recording conversations with the technical team that are the subject of Ms Morgan's evidence¹².
52. A few days later, when the same member of the technical team read an email from Ms Morgan which mentioned that MRG UK's debt was listed on the London Stock

¹¹ The Notes could not have been listed on the London Stock Exchange unless they were freely transferable.

¹² The FY2019 One Form Audit Memo, marked as reviewed by Ms Morgan on 28 April 2020, records "A EQCR will be required This has been confirmed with the MHA technical dept." Ms Morgan's evidence is that this text was a 'typo' error made by her when seeking to follow the approach from FP2018 and the text should have read "EQCR will not be required. This has been confirmed with the MHA technical dept" which is the wording that appeared in the FP2018 version of the document.

Exchange Main Market, they emailed two other colleagues (in relation to preparation of MHA's Transparency Report¹³) to inform them that MRG UK was a PIE, as referred to at paragraph 55.2 below. Neither the sender of the email or the two recipients were members of the FY2019 Audit team.

53. Ms Morgan's evidence is that she considered whether or not MRG UK was a PIE. However, there is no contemporaneous documentary evidence on the FY2019 Audit file (or elsewhere) of Ms Morgan recording her own consideration of the definition of a PIE. Neither is there any documentary evidence of Ms Morgan holding a formal meeting with a member of MHA's technical team or asking a direct written question to the MHA technical team as to whether MRG UK was a PIE. A workpaper relating to the audit team's evaluation of the need for any review of audits by MHA's technical team "*405-1 MH Hot Review Criteria*" was marked as completed by Ms Morgan on 14 May 2020. This workpaper included questions regarding whether an EQCR was required (one of which Ms Morgan answered positively), but this was not completed until two weeks after the FY2019 Auditor's Report was signed.
54. Ms Morgan did not perform adequate work to determine whether or not MRG UK was a PIE. Ms Morgan's evidence is that she was uncertain as to MRG's status as a PIE in the early stages of the FY2019 Audit. However, any confusion should have been resolved to Ms Morgan's satisfaction prior to substantive audit work commencing,
55. Notwithstanding the conflicting accounts of the facts, it is clear that the FY2019 Audit ultimately proceeded on the incorrect basis that MRG UK was not a PIE, and no EQCR review was performed prior to the Auditor's Report being signed on 30 April 2020.
56. Shortly before the FY2019 Auditor's Report was signed, on 27 April 2020, Ms Morgan sent an email to the MHA technical team requesting a review of the draft financial statements of MRG UK. In her email, Ms Morgan included information which made it clear that the Notes were listed on the London Stock Exchange. As stated above at paragraph 50, Ms Morgan's evidence is that this email followed a telephone call with a member of the technical team who confirmed that no EQCR was required, however, there is no evidence documenting this call, or what is said to have been

¹³ A Transparency Report is a report, prepared and published by an auditing firm, which lists, among other things, the PIEs for which the firm has issued an Auditor's Report. The auditors of certain PIEs are legally required to produce a Transparency Report each year.

discussed. As noted at paragraph 50 above, the evidence of the relevant member of MHA's technical team is that they made no such statements. Ms Morgan's evidence is that the email of 27 April 2020 was intended to draw the technical team's attention to the fact that the Notes were listed in order to ensure that the technical team considered once more whether an EQCR was required. However, Ms Morgan's email did not actively raise the question of whether MRG UK was a PIE (or whether an EQCR was required). Following the sending of her email to the technical team inbox:

56.1. Ms Morgan's request for a review of the draft financial statements was acknowledged by one of the technical team and was referred to another individual to perform the review.

56.2. On seeing Ms Morgan's email the following day the senior member in MHA's technical team referred to above at paragraphs 50 to 51 informed two other colleagues (one being a senior member of MHA's Audit department) that MHA would need to record MRG UK in its list of PIE audit clients, for the purposes of preparing its Transparency Report. Neither the sender of the email or the two recipients were members of the FY2019 Audit team or involved in the review of financial statements that had been requested. However, the sender's evidence is that they did not know that the FY2019 Audit was being conducted on the basis that MRG UK was not a PIE, and being unaware of this they did not communicate to Ms Morgan (or any other member of the FY2019 audit team) that MRG UK was, in fact, a PIE.

56.3. As set out at paragraph 55.1 above, a different member of the technical team performed the review of the draft financial statements. Their review was not intended to address the matter of whether the entity was a PIE (their task was focused only on reviewing the draft financial statements). They were not informed of their colleague's identification of MRG UK as a PIE.

Acceptance and continuance of the Audits

57. Audit firms have in place policies and procedures for determining whether to accept or to continue a specific audit engagement. Those policies and procedures are designed to ensure that firms only conduct work when they are competent to do so and where the engagement team has the necessary capability, including time and resources, are satisfied that they can comply with the relevant ethical requirements,

and do not have information which indicates that the client lacks integrity.¹⁴ The policies require firms to obtain necessary information, address potential conflicts of interest and document any issues identified and how they were resolved.¹⁵

58. The Engagement Partner is responsible for implementing the audit firm's policies and procedures. Paragraph 12 of ISA 220 requires the Engagement Partner to be satisfied that appropriate procedures regarding the acceptance and continuance of relationships and audit engagements have been followed. The Engagement Partner must determine that conclusions reached about whether to accept or continue an engagement are appropriate.
59. As noted above, the Group Auditor first approached MHA regarding the FP2018 Audit on 6 April 2019. The Group Auditor communicated a deadline of 30 April 2019 for receipt of the audited financial statements for MRG UK, on the basis that this was the deadline for MRG SAM to file its own annual accounts. The request from the Group Auditor was initially sent to another partner at MHA. When the request was forwarded to Ms Weston, the question was raised *"Can you fit this in allowing for completion by the end of the month?"*.
60. On 17 April 2019 Ms Weston provided an Audit Planning Letter to MRG UK. The letter noted that *"Due to the proximity of the 30 April deadline for delivery of the audited financial statements all key matters were covered on the call yesterday"* and *"We do not have much time to complete the audit and it will be very important to receive all the information we need from you by return and all by Tuesday morning 23 April at the latest"*. Assuming all the required information was received by this time, only one week would then remain before the deadline of 30 April 2019.
61. In the audit workpaper *"Criteria for use of small, non-complex audit profile"* the FP2018 audit team responded to questions concerning acceptance and continuance of the audit engagement. Question 2 of this workpaper asked: *"Does acceptance or continuance of this client engagement require consultation in accordance with the firm's client acceptance and continuance policy?"*. Question 12 asked: *"Is there any other information that has come to our attention that indicates the entity is above low risk?"* Responses to both questions were *"No"*. There is no consideration of timing in this document. Notwithstanding that this workpaper concerns matters regarding acceptance and risk, it was only completed by a member of the FP2018 Audit team

¹⁴ ISQC 1, paragraph 26.

¹⁵ ISQC 1, paragraph 27.

on 26 April 2019. There is no record within the audit software that Ms Weston reviewed this document.

62. The One Form Audit Memo for the FP2018 Audit (the “**Memo**”) (a key document recording the audit team’s approach to the FP2018 Audit, and a summary of the substantive audit work planned and completed) simply recorded the fact that a deadline of 30 April [2019] had been imposed. There is no comment regarding timing under “Firm competencies” or “Timing of Engagement”, where the issue of timing could have been considered and documented. Whilst under “Engagement Risk Assessment” there is a comment “*There are no...unrealistic timeframes...which would impact engagement continuance*”, there is no explanation or comment regarding timing. It is also unclear why the FP2018 audit team make reference to “*continuance*” in the response, when the FP2018 Audit was an entirely new engagement. The Memo goes on to state, “*Based on the information and risk factors identified above, this engagement is assessed as low risk and it is acceptable for MH to accept the engagements [sic]*”. The “Engagement Acceptance” box at the top of the Memo was signed by a member of the FP2018 audit team on 3 May 2019, three days after the FP2018 Auditor’s Report was signed. There is no record within the audit software that Ms Weston reviewed this document.
63. Ms Weston clearly appreciated that the deadline provided by the Group Auditor was potentially challenging. However, Ms Weston considered that MRG UK was a small, non-complex entity, which she believed was not a PIE, and for which she expected the audit to be relatively straightforward. Nevertheless, there is no evidence on the FP2018 Audit file of what work was done to consider what risks the deadline might raise for MHA or the appropriateness of accepting a new audit engagement in these circumstances, without making adequate reference in the engagement terms communicated to management as to the achievability of the timetable, or whether the deadline provided by the Group Auditor could be extended. Consideration of these issues should have taken place prior to any substantive audit work being commenced. Ms Weston did not perform the work required to determine that appropriate conclusions had been reached as to whether MHA should accept the FP2018 Audit engagement.
64. At the time of the FP2018 Audit MHA did not conduct PIE audits. That was MHA’s policy. The policy changed in May 2019, when MHA resolved to enter the PIE audit market. However, even though MHA was then able to accept PIE audit engagements and the FY2019 Audit was accepted after this change of policy, it remained important

for MHA to identify whether any potential audit engagement would involve a PIE because, as explained above, there are specific ethical and auditing requirements which apply to the audit of a PIE.

65. In relation to the FP2018 Audit, the workpaper “405X *Small audit - Acceptance/continuance criteria*” asked “*Is the entity is [sic] regulated, a public interest entity or otherwise high profile?*”. The response to this question was “*No plc but not public interest entity*”. No further explanation is provided. There is no evidence within the audit software that Ms Weston reviewed this document.
66. Ms Weston asked the technical team whether PIE status attached to two audited entities that she was working on which had listed bonds, but Ms Weston did not refer the question of whether MRG UK was a PIE to the technical team, and she did not document her specific reasoning as to why it was not, in her view, a PIE. Rather, Ms Weston proceeded on the basis of an erroneous assumption that MRG UK’s status was the same as two other audited entities she had been working on at around the same time. That was clearly an insufficient basis on which to reach appropriate conclusions and, in that regard, Ms Weston did not perform the work required to satisfy herself that MHA’s acceptance procedures (including, at that time, the decision not to accept engagements to audit PIEs) had been followed.
67. As explained above, by the time of the FY2019 Audit, MHA had resolved to enter the PIE audit market. However, the FY2019 Audit was conducted on the incorrect basis that MRG was not a PIE. Ms Morgan reviewed the continuation and acceptance paperwork that had been prepared by MHA prior to Ms Morgan joining. Ms Morgan's evidence is that she understood MRG UK had been contacted and that there were no material relevant changes from the FP2018 Audit. Whilst Ms Morgan’s review of the continuation and acceptance paperwork was adequate, as discussed above, Ms Morgan did not perform adequate work to determine whether or not MRG UK was a PIE. This led to the FY2019 Audit being continued on an incorrect basis and incorrect information being recorded in the continuation and acceptance paperwork for the FY2019 Audit.
68. For the reasons set out above the Audits were conducted on the incorrect basis that MRG was not a PIE. A number of consequences flowed directly from the failure to appreciate that MRG was a PIE.

Provision of non-audit services

69. Section 5 of the Ethical Standard addresses the provision of non-audit services.¹⁶ The provision of non-audit services could threaten an auditor's objectivity. For example, an auditor may feel pressured to provide an unqualified Auditor's Report in order to maintain lucrative non-audit work with an entity under audit, or an auditor may be auditing financial statements that it had a significant role in preparing, to some extent, marking its own homework. That said, the provision of non-audit services is often convenient, efficient and unproblematic. The purpose of Section 5 is therefore to guide auditors as to when it is appropriate to provide non-audit services to an entity at the same time as providing audit services, and what safeguards may be necessary when doing so.
70. The requirements are particularly strict as regards PIEs. Paragraph 5.167R of the Ethical Standard requires that audit firms carrying out the statutory audit of a PIE do not provide the audited entity with any "*prohibited non-audit services*" in the period between the beginning of the period audited and the issuing of the Auditor's Report, or in the financial year immediately preceding that period.¹⁷ "*Prohibited non-audit services*" include, among many other things, "*bookkeeping and preparing accounting records and financial statements*".¹⁸
71. The Engagement Partner also has responsibility for ensuring that prohibited services are not provided. An Engagement Partner must identify and evaluate circumstances that create threats to independence¹⁹ and take appropriate action to eliminate such threats.²⁰ As explained above, the provision of non-audit services to an entity under audit is a threat to the auditor's independence, and the only appropriate action in relation to a PIE (as explained in paragraph 5.167R of the Ethical Standard) is to refrain from performing those services. So, where a firm provides prohibited services, the Engagement Partner has failed to identify the threat and/or failed to take appropriate action to eliminate the threat.

¹⁶ In this matter, 'non-audit services' comprise any engagement in which MHA provided professional services to MRG UK other than the audit of its financial statements: Ethical Standard, para 5.8.

¹⁷ Paragraph 5.168R sets out an exception to that prohibition. The exemption relates to tax and valuation services which are not at issue in this matter.

¹⁸ Paragraph 5.167R (c).

¹⁹ ISA 220, paragraph 11(a)

²⁰ ISA 220, paragraph 11(c)

72. Alongside its work on the FP2018 Audit, MHA prepared the financial statements of MRG UK. While that may have been appropriate if MRG UK was not a PIE, doing so was a breach of the Ethical Standard given that MRG UK was, in fact, a PIE.
73. As regards the FY2019 Audit, Ms Morgan's evidence is that MRG UK did not pay for the preparation of financial statements. The engagement letter for the FY2019 Audit (dated 3 March 2020) noted that the engagement was to include the preparation of financial statements. Internal emails indicate that the fee charged by MHA was calculated by reference to the previous year's fee (which included £4,500 for the preparation of financial statements) plus a small inflation-related increase.
74. Ms Morgan's evidence is that, during the conduct of the FY2019 Audit, it was agreed that the total fee referred to in the engagement letter would be for audit work only, as the audit work for FY2019 was proving to be more onerous than for FP2018 (and that there was no charge for the FY2019 audit team transposing figures from a trial balance into financial statement format). Ms Morgan's evidence is that MRG UK agreed to the increased fee solely for the audit work. There is no documentary evidence of this conversation or the terms of the agreement to alter the fee arrangements. However, the Planning Letter sent to MRG UK on 3 April 2020 did not refer to a fee for accounts preparation and the final invoice issued to MRG UK did not contain a separate fee for accounts preparation.
75. The evidence shows that MHA used information in a trial balance provided by MRG UK (together with other supporting financial information) to prepare the FY2019 financial statements. This was done by uploading the trial balance to the audit software and using the software to generate a set of draft financial statements. Although Ms Morgan has explained that this was a mechanical process, the exercise still amounted to non-audit work prohibited by Paragraph 5.167R(c) of the Ethical Standard. MHA should not have prepared the financial statements of a PIE for which it was also conducting audit work and Ms Morgan ought to have taken appropriate action to ensure that those services were not provided.

No EQCR

76. Both an audit firm and an Engagement Partner have responsibilities in relation to EQCR reviews. ISQC 1 deals with a firm's responsibilities for its system of quality control for audits and reviews of financial statements, and other assurance and related services engagements. ISQC 1 requires that an EQCR review be performed for audits of financial statements of PIEs, in order to assess whether the

Engagement Partner could reasonably have come to the opinion and conclusions expressed in the draft Auditor's Report.

77. ISA 220 deals with the specific responsibilities of the Engagement Partner regarding quality control procedures for an audit of financial statements and addresses, where applicable, the responsibilities of the EQCR.²¹ In particular, paragraph 19 of ISA 220 requires that, for audits of financial statements of listed entities (including listed entities which are PIEs), the Engagement Partner shall determine that an EQCR has been appointed and not date the Auditor's Report until the completion of the EQCR review. Accordingly, Ms Weston and Ms Morgan were obliged to ensure that an EQCR review was performed before the respective Auditor's Reports were signed, but (in consequence of their failures to identify that MRG UK was a PIE) they did not do so.

Auditor's Report and Audit Committee Report

78. When an audit concerns a PIE, the Auditor's Report is required to contain certain information²². Auditors are required to submit an additional report to the entity's audit committee (or body performing equivalent functions within the entity).²³ As both the FP2018 and FY2019 Audits were conducted on the incorrect basis that MRG UK was not a PIE, there was a consequential failure to ensure the Auditor's Reports contained the requisite information and a failure to issue additional reports.
79. The Auditor's Report for each Audit failed to:
- 79.1. indicate the period of total uninterrupted engagement including previous renewals and reappointments of the firm;
 - 79.2. explain to what extent the audit was considered capable of detecting irregularities, including fraud;
 - 79.3. confirm that the audit opinion was consistent with the additional report to the MRG UK audit committee (or body performing equivalent functions within MRG UK); and

²¹ ISA 220, paragraph 1.

²² ISA 700, paragraph 45R-1.

²³ ISA 260, paragraph 16R-2.

- 79.4. include a description of the most significant assessed risks of material misstatement (whether or not due to fraud).
80. The Auditor's Report for each Audit also declared, wrongly, that no prohibited non-audit services had been provided to MRG UK. This was not correct, as a result of the failure by the audit team to appreciate that MRG UK was a PIE.
81. The additional report explaining the results of the audit carried out required by ISA 260 that was sent by the FP2018 Respondents (re the FP2018 Audit) and by the FY2019 Respondents (re the FY2019 Audit) to the body performing the equivalent functions to an audit committee did not comply with the requirements of paragraph 16R-2 of ISA 260 and was sent only after the audit report in breach of paragraph 21R-1. In FY2019 the version of the additional report sent also did not comply with the requirements of paragraph 20.R-1(b) of ISA 260 as it was not signed.

Category 2: Other matters in the Audits

Reviews of Audit Work

82. Ms Weston (re the FP2018 Audit) failed to take adequate steps to take responsibility for the reviews of the audit workpapers being performed as required by MHA's policies and procedures. Accordingly, the FP2018 Respondents (re the FP2018 Audit) breached paragraph 16 of ISA 220.
83. Ms Weston (re the FP2018 Audit) and Ms Morgan (re the FY2019 Audit) failed to perform an adequate review of audit documentation as required in order to properly be satisfied that sufficient, appropriate audit evidence had been obtained to support the conclusions reached and for the respective Auditor's Reports to be issued. In the event, several of the conclusions reached were not supported by adequate evidence. The FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit) breached paragraph 17 of ISA 220.

Particulars of the Breaches

84. The Engagement Partner is responsible for reviews of audit work being performed in accordance with the firm's policies and procedures.²⁴ "Reviews" in this context are

²⁴ ISA 220, para 16.

instances where the work of less experienced team members is reviewed by more experienced team members.²⁵

85. Paragraph 17 of ISA 220 requires Engagement Partners to satisfy themselves, on or before the date of the Auditor's Report, through a review of the audit documentation and discussion with the engagement team, that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the Auditor's Report to be issued.²⁶
86. In each of the Audits the teams used audit software to record the audit work completed. Depending on the profile selected by the audit teams the software generated a number of different workpapers for the audit teams to complete. In the Audits the "*non-complex case profile*" was selected. The workpapers generated by the software for that profile had spaces for preparation and review to be recorded. In order to sign off the workpaper the reviewer electronically 'stamps' their initials and the date of review in a designated 'Review' box at the top of the workpaper.
87. All work on an audit file should have at least one level of review by a more experienced engagement team member²⁷. In smaller audits, this would be the Engagement Partner. In larger audits, senior members of the audit engagement team (usually audit managers) might review the work of more junior members without a need arising for the Engagement Partner to conduct a further review of that work. In that context, it is normal for an audit partner to have reviewed only certain workpapers, those which present a particular complexity, relate to areas of higher risk, or are important for other reasons.
88. In the FP2018 Audit, there was scope for review by a senior member of the team other than Ms Weston. Therefore, she was not required to review every audit workpaper produced by her junior colleagues. Ms Weston's evidence is that she was in regular discussion with the audit senior throughout the period in which the audit work was completed, and she sat with them to review the FP2018 Audit file on their computer. Due to the nature of MRG UK's business, the FP2018 Audit was small in scale and the FP2018 Audit file did not contain many audit papers. However, there is no evidence in the audit software (i.e. by the electronic "stamping" of her initials and dating of that entry) that Ms Weston reviewed the FP2018 workpapers prior to

²⁵ ISA 220, para A16.

²⁶ ISA 220, para 17.

²⁷ ISA 220, 16 and A16 and ISQC 1.33

signing the FP2018 Auditor's Report, including those which were marked as "mandatory" for review by the Engagement Partner.

89. In the FY2019 Audit, there was no scope for review by another senior member of the team other than Ms Morgan as the Engagement Partner, as the other members of the team were a junior auditor, who had only recently qualified, and an unqualified apprentice. Whilst the junior auditor might review the work of the apprentice, Ms Morgan ought to have then reviewed and signed-off all of the audit workpapers prepared by the junior auditor, as otherwise these would not be reviewed at all. There is documentary evidence that Ms Morgan reviewed and signed-off the majority of the workpapers prepared by the junior auditor, albeit some of the audit software records are unclear in the FY2019 Audit file. However, Ms Morgan failed to review and sign-off all workpapers in the audit software that supported the conclusions reached in the FY2019 Audit.
90. The failure of Ms Weston, in the FP2018 Audit, to perform and document adequately a review of the workpapers in the audit software involved a failure to ensure that reviews of audit work were performed in accordance with the firm's policies and procedures. In the FY2019 Audit Ms Morgan failed to review and sign-off all of the audit workpapers prepared by the junior auditor. Having not adequately reviewed the relevant audit workpapers, Ms Weston (re the FP2018 Audit) and Ms Morgan (re the FY2019 Audit) could not properly satisfy themselves that sufficient appropriate audit evidence had been obtained for the purposes of signing the Auditor's Reports.²⁸

Bank Balances

91. In breach of paragraph 6 of ISA 500, the FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit) failed to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence to be able to draw reasonable conclusions in relation to MRG UK's stated cash balance:

91.1. In the FP2018 Audit, the FP2018 Respondents failed to seek external confirmation of the balance from MRG UK's bank and, instead, performed the inadequate procedure of agreeing the balance to a bank statement provided by management.

²⁸ As explained elsewhere in this *Final Settlement Decision Notice*, sufficient appropriate audit evidence was not obtained in relation to some important aspects of the audits.

91.2. In the FY2019 Audit, the FY2019 Respondents sought external confirmation of the balance from MRG UK's bank. However, no response was received. Instead, the FY2019 Respondents performed the same inadequate procedure as in the FP2018 Audit, agreeing the balance to a bank statement provided by management.

Particulars of the Breaches

92. Auditors are required to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions upon which to base their opinion. ISA 500 deals generally with audit evidence. It explains what constitutes audit evidence in an audit of financial statements, and deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence.²⁹
93. External confirmations (i.e. audit evidence obtained by the auditor as a direct written response to the auditor from a third party) are often used to confirm account balances.³⁰ For example, in order to confirm the cash balance expressed in the financial statements, an auditor will usually seek confirmation of an entity's bank balance directly from the entity's bank. External confirmations are more reliable than evidence obtained from sources within an entity or evidence obtained indirectly or by inference.
94. It is common for auditors to seek external confirmations from banks. An auditor will request that the entity expressly communicates to its bank (usually by way of an "authorisation letter") that the bank should comply with requests for information from the auditor. The auditor will then contact the bank directly, asking for confirmation of balance on the entity's account(s) at the date of the financial statements. The figure in the financial statements can then be compared against the figure(s) stated in the confirmation(s) provided by the bank(s). If the bank (or other third-party) does not respond to a request for an external confirmation, an auditor is required to perform alternative audit procedures to obtain relevant and reliable audit evidence.
95. In both the FP2018 and FY2019 Audits, MHA intended to seek such confirmations from MRG UK's bank. When performing the FP2018 Audit, MHA obtained an authorisation letter from MRG UK on 26 April 2019 (four days before the Auditor's

²⁹ ISA 500, paragraph 1.

³⁰ ISA 500, paragraph A18.

Report was signed). The letter authorised MRG UK's bank to release information to MHA. However, the audit team did not then contact MRG UK's bank (an institution based in Switzerland) to obtain external confirmations. Instead, MHA reviewed a copy of a bank statement as at 31 December 2018, which was provided by management.

96. When performing the FY2019 Audit, MHA sent a letter requesting confirmation of funds to MRG UK's bank in Switzerland on 20 January 2020, well ahead of the 30 April 2020 deadline for completing the FY2019 Audit. Ms Morgan's evidence is that she called the bank to follow up on a response, but was not able to elicit one. Ultimately, no response was received and there is no record that the audit team attempted to follow up with the bank prior to the Auditor's Report being signed. Despite no confirmation being received the relevant section of the "Cash" audit workpaper (to obtain a bank confirmation for all selected bank accounts) was incorrectly marked as "*completed, no exceptions*" on 9 March 2020.
97. As in the FP2018 Audit, rather than obtaining the bank confirmation the audit team instead reviewed a copy of a bank statement provided by management. Reviewing a copy of a bank statement provided by management does not provide a similar level of reassurance as an external confirmation would provide and was not an adequate alternative to having received an external confirmation directly from MRG UK's bank. In both Audits, the bank statements were not obtained from a party independent of MRG UK and the audit teams had no assurance of their authenticity (nor is there any evidence that the audit teams sought any such assurance, for example, by performing further work to follow-up with MRG UK's relationship manager or another appropriate contact at the bank).
98. The FP2018 audit team would have known from the outset that external confirmations of bank balances were likely to be needed but did not obtain an authorisation letter from management until just four days before the FP2018 Auditor's Report was due to be signed.
99. In the FY2019 Audit the audit team were aware that no bank confirmation had been obtained in the FP2018 Audit, making it even more important to verify the position with strong audit evidence in the FY2019 Audit.
100. In FY2019, whilst Ms Morgan's evidence is that she did consider the control environment, including how transactions were verified between the two entities on

the intercompany ledgers, and was satisfied that the risk of fraud was low, the alternative procedures performed in respect of the material bank balance were still insufficient (and this work was not adequately documented in the FY2019 Audit file).

101. The cash balance in both FP2018 and FY2019 was well above the materiality threshold determined by the audit teams. In those circumstances, an auditor may decide that no alternative to an external confirmation is acceptable, and the *Statutory Auditor* may have to delay the signing of the Auditor's Report.
102. Having failed to obtain confirmations from MRG UK's bank or to have performed adequate alternative procedures, the Respondents failed, in both Audits, to design and perform adequate audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions in relation to MRG UK's stated cash balance.

The loan from MRG UK to MRG SAM

103. In breach of paragraph 6 of ISA 500 the FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit) failed to design and perform audit procedures that were appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence to be able to draw reasonable conclusions in relation to the implied assertion that the loan was recoverable and therefore appropriately valued in the financial statements.
104. In breach of paragraph 24 of ISA 330, the FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit) failed to perform audit procedures to evaluate whether the overall presentation of the financial statements was in accordance with the applicable financial reporting framework. As explained below, the financial statements did not comply with the balance sheet format prescribed in the Companies Act 2006.³¹ The Respondents failed to note or correct the discrepancy with the applicable framework, and it is therefore inferred that they failed to conduct the evaluation required by paragraph 24 of ISA 330.

Particulars of the Breaches

³¹ Whilst the FP2018 and FY2019 Financial Statements did not comply with the prescribed balance sheet format which required correct classification of the intercompany loan in the balance sheet as explained at paragraph 118 below, this issue did not impact the actual recoverability of the loan or the reported net asset balance and profit of MRG.

105. MRG UK received money paid by investors for the Notes issued in October 2018. It then loaned that money to MRG SAM. The loan balance was reported as £43,384,680 at 31 December 2018. The loan is central to MRG UK's purpose. It is the mechanism by which the money raised by issuing the Notes was passed on to its parent company (MRG SAM) for use by the wider Group.
106. In both the FP2018 and FY2019 Audits it was important that the loan was adequately considered by the auditors. Firstly, MRG UK's ability to continue to operate depended almost entirely on the repayment of the loan and the interest upon it. Secondly, the loan was not an arm's length transaction. It was a transaction between a parent company and its subsidiary, a transaction between related parties. The Companies Act 2006 requires amounts owed by a group undertaking to be separately disclosed in financial statements.
107. The loan agreement indicates that the loan was effective as of 26 October 2018. The original terms of the loan state the amount lent as €49,149,972.60 with interest to accrue at a rate of 9.25% per year on that amount. The terms state that the entire principal sum plus interest is to be repaid on 25 October 2023. The principal sum of the loan was later amended by an agreement executed on 31 March 2019 to €48,499,972.60, backdated to 26 October 2018 (a material reduction).
108. The terms of the loan appear to be calibrated to allow MRG UK to pay noteholders. The interest paid to MRG UK is intended to exceed the interest owed to noteholders, and the repayment date would allow MRG UK to repay the principal amount to the noteholders when the Notes mature. However, the terms do not quite achieve their apparent purpose. While the terms of the loan envisage a single repayment (of interest accrued and the principal sum) at the end of the loan period, the terms of the Notes require annual interest payments to bondholders. Therefore, the loan terms, as written, do not provide MRG UK with sufficient cash flow to make the annual interest payments as they become due.
109. In practice, MRG UK and MRG SAM appear not to have adhered strictly to the repayment terms of the loan agreement. Instead, MRG SAM took responsibility for making interest payments to noteholders and paying other of MRG UK's expenses. The net effect of those payments was accounted for by adjusting the outstanding loan balance between MRG SAM and MRG UK. As a result, the loan balance for FY2019 was lower than the loan balance reported in FP2018. In both years, there

was a discrepancy between how the loan was accounted for in practice and the documented terms of the loan.

110. In the FP2018 financial statements, the loan is stated in two amounts (converted into GBP from EUR)³², a current asset of £759,431 being the interest receivable in the current financial year,³³ and a non-current asset of £42,625,249 being the balance of the loan amount. The figures set out in the FP2018 Financial Statements were confirmed by reference to communication between MRG UK and MRG SAM. The loan was not identified by the FP2018 Respondents as a significant risk for the FP2018 Audit, and the Strategic Report section of the FP2018 financial statements did not address the loan when considering principal risks and uncertainties.
111. Ms Weston's evidence is that she believed MRG SAM to be financially sound and able to meet its obligations under the loan and that the loan was therefore recoverable. The recoverability of the loan was not given any consideration at all in the FP2018 audit workpapers and there was no challenge of management as to why the loan was not stated as a principal risk in MRG UK's Strategic Report. The FP2018 Respondents therefore failed to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions in relation to the recoverability of the loan (including the implied assertion that the loan was recoverable and therefore appropriately valued in the financial statements). Consequently, the FP2018 Respondents acted in breach of paragraph 6 of ISA 500.
112. In the FY2019 financial statements, the loan is also stated in two amounts, a current asset of £677,686, being the interest receivable in the current financial year, and a fixed asset of £40,805,140.
113. In the FY2019 Audit inconsistent information was recorded as to whether the loan presented a significant risk. The loan was not recorded as a risk in a workpaper entitled "*Risk report – Risk assessment*". However, the Planning Letter sent by MHA to MRG UK on 3 April 2020³⁴ did list lending as a significant risk. Ms Morgan's

³² The EUR figure was €47,651,000.

³³ Accounting for a portion of the loan as a current asset suggests, as explained above, that MRG SAM is paying interest annually rather than (as the written agreement would dictate) in a lump sum at the end of the loan period.

³⁴ It appears the Planning Letter was prepared on 3 March 2020 but was not provided to MRG UK until 3 April 2020.

evidence is that the loan was not considered a risk because the parent company was “*extremely solvent*”.³⁵

114. Audit procedures were performed on the loan balance in the FY2019 Audit. The figure set out in the FY2019 financial statements was confirmed by reference to communication between the accountants for MRG UK and MRG SAM, and the solvency of the wider Group was considered in order to determine whether there was any indication that the loan would not be recoverable by MRG UK. The FY2019 audit workpapers record that the draft consolidated balance sheet of MRG SAM for FY2019 showed net assets of €685,770,000 including a cash balance of €154,541,000.
115. The FY2019 audit team reviewed the net asset position of MRG SAM and Ms Morgan’s evidence is that the group cash balance was also reviewed. However, even with a strong net asset position and adequate cash balance, the risk that the Group would be unable to make repayments if its assets were illiquid or there were other calls on that cash should have been considered. Accordingly, the procedures performed were insufficient.
116. Ms Morgan’s evidence (and that of MRG UK’s management) is that a support letter from MRG SAM to MRG UK stating MRG SAM’s intention to provide continued financial support to MRG UK was provided to the FY2019 audit team. However, this support letter did not refer specifically to the repayment of the loan and no copy was retained on the FY2019 Audit file.
117. The FY2019 Respondents therefore failed to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions in relation to the recoverability of the loan (including the implied assertion that the loan was recoverable and therefore appropriately valued in the financial statements).
118. The work conducted on the intercompany loan also engages paragraph 24 of ISA 330 which requires auditors to perform audit procedures to evaluate whether the overall presentation of the financial statements is in accordance with the applicable financial reporting framework. The prescribed balance sheet format in the Companies Act 2006 required the intercompany loan to be identified in the financial statements as an amount owed by a group undertaking. The Respondents failed to

³⁵ A loan is impaired if it is likely that it will not be repaid in full.

ensure that the FP2018 and FY2019 financial statements complied with the prescribed format.³⁶

Going Concern

119. In breach of paragraph 10 of ISA 570, the FP2018 Respondents (re the FP2018 Audit), and the FY2019 Respondents (re the FY2019 Audit), when performing risk assessment procedures as required by ISA 315, failed adequately to consider whether events or conditions existed that may cast significant doubt on MRG UK's ability to continue as a going concern³⁷.

Particulars of the Breaches

120. Under the going concern assumption, an entity is viewed as continuing in business for the foreseeable future. The term 'going concern' applies to any entity unless its management intends to liquidate the entity or to cease trading or if the entity has no realistic alternative to liquidation or cessation of operations. Paragraph 10 of ISA 570 requires that auditors consider whether there are events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.
121. The main issue affecting whether MRG UK had the ability to continue as a going concern was whether it would be able to service payments due to noteholders. The timing of those payments was set out in the terms of the Notes. There would be five annual interest payments with the final repayment of the Notes due on 26 October 2023. MRG UK would be insolvent if it did not have cash to pay the noteholders. Since MRG UK's ability to pay the noteholders depends on whether MRG SAM is able to service the loan (considered above), the appropriateness of the going concern assumption in each of the Audits depended on whether the loan was impaired.
122. The FP2018 Audit file does not record that adequate audit procedures were, in fact, performed. An audit memo stated that the "*company appears to be solvent and made a small profit*". However, the FP2018 Respondents do not appear to have considered

³⁶ Whilst the FP2018 and FY2019 Financial Statements did not comply with the prescribed balance sheet format which required correct classification of the intercompany loan in the balance sheet, this issue did not impact the actual recoverability of the loan or the reported net asset balance and profit of MRG.

³⁷ Although breaches are identified in relation to the audit work performed on the going concern assumption it is not alleged that MRG UK's FP2018 and FY2019 financial statements in fact contained a material misstatement in this regard (or that the conclusion reached regarding going concern in either year was ultimately incorrect).

the matter of going concern any further than that, for example, there is no record indicating that any discussion took place with management regarding the going concern assumption, or a record of a conclusion as to whether a material uncertainty existed related to events or conditions that may cast significant doubt on MRG UK's ability to continue as a going concern or reviewing future plans for MRG UK.

123. The consideration of whether there were events or conditions that may have cast significant doubt on MRG UK's ability to continue as a going concern was therefore inadequate. Moreover, the FP2018 Respondents ought to have considered whether there were indicators that the intercompany loan was impaired (on which, see above). Consequently, the consideration of the going concern assumption was inadequate in the FP2018 Audit.
124. In relation to the FY2019 Audit, Ms Morgan's evidence is that, due to the intercompany loan arrangement, MRG UK's continuing ability to operate was contingent upon MRG SAM's financial strength and MRG SAM was a profitable company with a positive net asset position.
125. The recoverability of the loan was relevant to an adequate consideration of the going concern assumption. The documentation shows that Ms Morgan requested a support letter from MRG SAM concerning MRG UK's going concern assessment. The evidence from MRG UK's management is that this support letter was produced by MRG SAM and sent on to MHA by MRG UK's management on 28 April 2020. Ms Morgan's evidence is that this support letter was considered prior to signing the FY2019 Auditor's Report. However, no copy of the support letter was retained on the FY2019 Audit file and there is no documentary evidence of Ms Morgan's review.
126. Further, there is no documentary evidence on the FY2019 Audit file recording that management provided the FY2019 audit team with an assessment of the going concern assumption. There is also no documentary evidence that the FY2019 audit team made any enquires in relation to such an assessment (or about the ultimate repayment of the intercompany loan). The question of whether MRG UK would be able to repay the Notes when they matured was plainly relevant to whether MRG UK would be a going concern for the foreseeable future and all available information about the future performance of MRG UK should have been considered to inform the FY2019 audit team's conclusion on the going concern assumption.

127. Whilst post year-end subsequent events testing, including issues relating to going concern³⁸, was performed in the FY2019 Audit, some of this work appears to have been performed between 14 – 26 May 2020 (including provision of information from management after the FY2019 Auditor’s Report was signed), with additional information being added to the file up until 26 May 2020, some four weeks after the FY2019 Auditor’s Report was signed. Audit work performed after an Auditor’s Report is signed cannot be relied upon to support that report. Ms Morgan has explained that she did not consider this work was necessary to reach her conclusions in the FY2019 Audit and that this evidence was not relied upon for the purposes of supporting the 2019 Auditor’s Report.
128. The Covid-19 pandemic also affected consideration of the going concern assumption in the FY2019 Audit. In response to commercial difficulties and widespread uncertainty caused by the pandemic, MHA developed a Covid-19 Checklist for use in audit engagements. One of the points on that checklist required audit teams to consider whether the pandemic had any impact on the going concern assumption. Time records indicate that Ms Weston reviewed a version of the Covid-19 Checklist on 28 April 2020. Ms Weston reviewed the document again, adding comments and queries regarding the underlying audit work, on 14 May 2020 (two weeks after the Auditor’s Report was signed) and sent it by email to Ms Morgan. It appears that, as at 14 May 2020, Ms Weston’s comments and queries had not been resolved. Ms Morgan’s evidence is that she had discussed the issues documented by Ms Weston prior to the FY2019 Auditor’s Report being signed on 30 April 2020 and considered the Covid-19 Checklist before signing the FY2019 Auditor’s Report on 30 April 2020. Ms Morgan’s review and acceptance of the Covid-19 Checklist is documented on the audit software with her sign off on 30 April 2020. Ms Morgan’s evidence is that she also received oral confirmation from Ms Weston that Ms Weston was satisfied. However, the Covid-19 Checklist (or the FY2019 Audit file) does not record this discussion.
129. In the FP2018 and FY2019 Audits, inadequate procedures relating to the going concern assumption were carried out. For the reasons explained above, going concern warranted far greater consideration than it received in each Audit.

³⁸ The FY2019 Planning Letter stated “*We will consider profit projections, business developments and other relevant factors, **including events subsequent to the date of the Statement of Financial Position, in order to conclude on the appropriateness of the financial statements being prepared on this basis***” [emphasis added]

Accounting Standards

130. In breach of paragraph 11 of ISA 315, the FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit), failed to gain an adequate understanding of MRG UK insofar as they failed to identify that the appropriate accounting standard to apply was IFRS.
131. It follows that the Respondents are responsible for a breach of paragraph 11 of ISA 315 in relation to each Audit.

Particulars of the Breaches

132. As noted above in relation to the identification of MRG UK as a PIE, paragraph 11 of ISA 315 required the Respondents to gain an adequate understanding of MRG UK. The issue of the Notes was fundamental to an adequate understanding of MRG UK (a company set up for that purpose alone). The Respondents failed to gain an understanding of two further aspects of the business, independent of the PIE issue.
133. The Respondents failed, in both Audits, to appreciate that the appropriate accounting standard to apply was IFRS. Instead, MRG UK's management's decision to adopt UK GAAP and apply FRS102 was accepted.³⁹
134. The requirement to prepare MRG UK's accounts in accordance with IFRS ought to have been clear from the Base Prospectus issued by MRG UK to explain the Notes to potential investors. Part VI of the Base Prospectus contained a description of MRG UK, including a short section on its financial statements. That section made clear that its accounts would be prepared in accordance with IFRS.
135. The Base Prospectus was not on the Audit file for either of the Audits, whether received from MRG UK's management, or otherwise. It is unclear whether the Respondents read that document at the time of the Audits. Instead, the FP2018 and FY2019 Audit files contained a Drawdown Prospectus, a document which explained the issuance of a particular tranche of Notes⁴⁰. The Drawdown Prospectus makes numerous references to the Base Prospectus and explicitly incorporates many of the terms contained in that document. As the Respondents had not received the Base

³⁹ It was incorrect for the FP2018 and FY2019 Financial Statements to be prepared in accordance with UK GAAP and apply FRS102. MRG's FY2020 Financial Statements were prepared in accordance with IFRS and the adjustments required to the FP2018 and FY2019 Financial Statements in accordance with IFRS were explained in Note 17 to the FY2020 Financial Statements.

⁴⁰ As it happens, only one tranche of Notes has been issued.

Prospectus, they ought to have asked to be provided with it. The Base Prospectus was also a publicly available document. It ought, therefore, to have been clear to the Respondents that IFRS should have been used to prepare the financial statements, rather than applying FRS102.

136. The FY2019 audit team relied on the documents obtained by the FY2018 audit team and did not request further documents as there had been no further issuances in FY2019.

Documentation and Archiving

137. In breach of paragraph 8 of ISA 230, the FP2018 Respondents (re the FP2018 Audit) and the FY2019 Respondents (re the FY2019 Audit) failed to prepare audit documentation that was sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the nature and extent of the audit procedures performed in each Audit, the results of those procedures, the audit evidence obtained, significant matters arising during the audit, the conclusions reached thereon, and the significant judgments made in reaching those conclusions.
138. In breach of paragraph 14 of ISA 230, the FY2019 Respondents failed to archive the FY2019 Audit file within the time period required.

Particulars of the Breaches

139. It is important for auditors to document their work. Audit documentation is fundamental to the conduct of the audit process itself. The completion and review of audit workpapers are processes which enable auditors to produce reliable work and demonstrate the basis on which audit conclusions are reached.
140. Paragraph 8 of ISA 230 requires auditors to prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand: the nature, timing and extent of the audit procedures performed to comply with the ISAs and applicable legal and regulatory requirements; the results of the audit procedures performed, and the audit evidence obtained; and significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions. There were deficiencies in documentation in both Audits. The list below is not exhaustive but provides examples of how the documentation of the Audits fell short of the required standard.

141. In the FP2018 Audit:

- 141.1. No note of the planning call between the FP2018 audit team and management on 16 April 2019 was kept on the FP2018 audit file, despite that call covering what Ms Weston characterised in the FP2018 Audit Planning Letter as “*all key matters*”.
- 141.2. The One Form Audit Memo for the FP2018 Audit stated: “*No auditors expert or EQCR will be required as entity is a ‘vanity’ plc. This has been confirmed with the MHA technical dept.*”. This statement was incorrect and reflected the confusion and error mentioned above arising from the enquiry made by Ms Weston of the technical department in relation to two other bond issuers. There is no record of Ms Weston or the FP2018 audit team consulting MHA’s technical team regarding the classification of MRG UK (or the use of auditor’s experts or EQCR).
- 141.3. A copy of the original loan agreement between MRG UK and MRG SAM was retained on the FP2018 Audit file. However, the FP2018 Audit file does not contain a copy of the subsequent amendment to the loan agreement.
- 141.4. The assessment of going concern was incorrectly recorded as a significant risk in the workpaper ‘520E Risk Report’.
- 141.5. Inadequate documentation relating to client acceptance consideration was on the FP2018 Audit file. Such documentation would be necessary for an auditor, having no previous connection with the audit, to understand the acceptance decision and its absence is particularly notable given the issue of MRG UK not being identified as a PIE.

142. In the FY2019 Audit:

- 142.1. Ms Morgan’s evidence (and that of MRG UK’s management) is that a support letter from MRG SAM to MRG UK was provided to the FY2019 audit team. However, no copy was retained on the FY2019 Audit file and there is no record on the FY2019 Audit file of Ms Morgan’s review of this audit evidence.
- 142.2. Audit evidence obtained in the FP2018 Audit appears on the FY2019 Audit file. In a work paper on the FY2019 Audit file concerning “*payables, trade creditors and unrecorded liabilities*”, work performed in the FP2018 Audit in relation to “*unrecorded liabilities*” is documented. This was due to the FP2018

Audit work on “*unrecorded liabilities*” not being updated to reflect the position for FY2019.

142.3. There was a discrepancy in the audit documentation concerning significant risks. Whilst management override was recorded as a significant risk in the FY2019 Audit Planning Letter, the “*risk assessment*” workpaper did not record it as a significant risk.

142.4. Correspondence between MHA and MRG UK was poorly recorded. For example, the version of the post-audit letter sent to MRG UK retained on the FY2019 Audit file was an unsigned Word version.

142.5. Time records for the FY2019 Audit suggest that a version of the Covid-19 Checklist was reviewed by Ms Weston on 28 April 2020. There is no documentary record of this review. Ms Morgan’s evidence is that Ms Weston’s comments were addressed orally (although this was not recorded on the FY2019 Audit file). Ms Morgan reviewed and signed off the Covid-19 Checklist before the FY2019 Auditor’s Report was signed. However, the copy of the Covid-19 Checklist retained on the FY2019 Audit file appears to be a further draft containing unresolved comments and queries from Ms Weston regarding the underlying audit work which were added after the FY2019 Auditor’s Report was signed.

143. Auditors are also required to archive their audit files. This is to ensure that a record of the audit work performed prior to the release of the Auditor’s Report is appropriately retained for monitoring compliance with ISAs and other applicable legal requirements. Paragraph 14 of ISA 230 requires auditors to assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file no later than 60 days from the date of the auditor’s report. The FY2019 Respondents did not archive the FY2019 Audit file within the required time period.

VI. SANCTIONS

MHA

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

- 143.1. to declare and uphold proper standards of conduct amongst *Statutory Auditors* and *Statutory Audit Firms* and to maintain and enhance the quality and reliability of future audits;
 - 143.2. to maintain and promote public and market confidence in *Statutory Auditors* and *Statutory Audit Firms* and the quality of their audits and in the regulation of the accountancy profession;
 - 143.3. to protect the public from *Statutory Auditors* and *Statutory Audit Firms* whose conduct has fallen short of the *Relevant Requirements*; and
 - 143.4. to deter *Statutory Auditors* and *Statutory Audit Firms* from breaching the *Relevant Requirements* relating to *Statutory Audit*.
144. Paragraph 12 of the Policy provides that the primary purpose of imposing *Sanctions* for breaches of the *Relevant Requirements* is not to punish, but to protect the public and the wider public interest.

Identification of *Sanction*

145. Executive Counsel imposes the following *Sanctions* against MHA:
- 145.1. a financial sanction of £200,000, adjusted for aggravating and mitigating factors by a reduction of 7.5%, and further discounted for admissions and early disposal by 35% so that the financial sanction payable is £120,250. The financial sanction shall be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;
 - 145.2. a published statement in the form of a Severe Reprimand;
 - 145.3. a declaration that the FP2018 and FY2019 Audit reports signed on behalf of MHA did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*; and
 - 145.4. an order to take action to prevent recurrence of the breaches as follows:
 - 145.4.1. Within one month of the date of this *Final Settlement Decision Notice* Executive Counsel and the Executive Director of Supervision will select a sample of MHA's PIE audit engagements to be the subject of targeted reviews by MHA's Audit Quality Improvement Team, with the aim of assessing whether and to what extent certain remedial

steps taken by MHA (including those described at para 160 below) have impacted audit quality (the “**Targeted Reviews**”). The sample will include at least one PIE audit engagement for each Responsible Individual included in MHA’s entry on the PIE Auditor Register at the time the sample is agreed.

145.4.2. Within three months of the date of this *Final Settlement Decision Notice* provide Executive Counsel and the Executive Director of Supervision with a proposal for (i) the details and specification of the Targeted Reviews (including which remedial steps will be the subject of those reviews); and (ii) the timeline for performing the Targeted Reviews.

145.4.3. Within two months of completing the Targeted Reviews, provide to Executive Counsel and the Executive Director of Supervision a report evaluating the effectiveness of the relevant remedial steps in the audit engagements selected for Targeted Review. Such report to include a summary of the review work carried out, an evaluation of the remedial steps in the relevant audit engagements, conclusions as regards the impact on quality of audit work and proposals to address any remaining areas for improvement.

145.4.4. If Executive Counsel or the Executive Director of Supervision consider that an additional report is required to address further issues, such a report to be provided within three months of any such request.

146. In reaching this decision, Executive Counsel has considered the following matters in accordance with the Policy.

Nature, seriousness, gravity, and duration of the breaches

147. The breaches of *Relevant Requirements* occurred in two consecutive audit years. Whilst there are differences in the specific facts and details in each year, the breaches are broadly of the same nature and engage many of the same *Relevant Requirements*.

148. The primary failing, of not identifying MRG UK as a PIE, was a fundamental failing. Conducting the Audits on the incorrect basis led to further consequential breaches

including a failure to ensure an EQCR review was performed and the provision of non-audit services in breach of the FRC Ethical Standard.

149. The breaches of *Relevant Requirements* also include failures in the performance of substantive audit work in each Audit, including audit work on the going concern assumption and confirmation of bank balances.
150. Although breaches are identified in relation to the audit work performed on the going concern assumption and bank balances it is not alleged that the FP2018 and FY2019 financial statements in fact contained a material misstatement in this regard (or that the conclusion reached regarding going concern in either year was ultimately incorrect).
151. In relation to the intercompany loan from MRG UK to MRG SAM, in both years the financial statements contained a material misstatement as the intercompany loan and interest were incorrectly described.
152. The breaches concerned *Relevant Requirements* that were designed to ensure the quality and effectiveness of the Audits.
153. The breaches of *Relevant Requirements* undermine confidence in the standards of conduct of *Statutory Auditors* and *Statutory Audit Firms* in general.
154. MRG UK is a small SPV that was created to issue the Notes. Accordingly, it is not alleged that the breaches of *Relevant Requirements* in this matter adversely affected, or potentially adversely affected, a significant number of people in the United Kingdom (such as the public, investors or other market users). Notwithstanding this, the failure to conduct the Audits in accordance with *Relevant Requirements* could harm investor, market and public confidence in the truth and fairness of the financial statements published by *Statutory Auditors* or *Statutory Audit Firms*.
155. It is not suggested that the breaches were intentional, dishonest, deliberate or reckless.
156. The quality procedures applied at MHA were not effective to prevent the breaches of *Relevant Requirements* outlined in this *Final Settlement Decision Notice*.
157. Whilst MHA was paid audit fees for each engagement, it did not stand to gain any profit or benefit from the breaches.

158. MHA is not a large audit firm. MHA's total UK fee income for the financial year ended March 2022 was £81.6 million and its total audit fee income was £37.7 million.
159. MHA has a good compliance history and disciplinary record with no prior sanctions under the AEP or Accountancy Scheme⁴¹.
160. MHA have taken remedial steps to seek to address the issues relevant to the breaches outlined in this *Final Settlement Decision Notice* and to seek to improve audit quality more generally. These include (i) an updated Audit & Assurance Policy Manual which contains new procedures across the lifespan of an audit; (ii) the introduction of sector and entity specific licensing policy for RIs; (iii) establishment of an Engagement Risk Assessment Panel, which is required to approve all prospective audit engagements that fall within its scope, including all audits within the scope of the FRC inspection regime (such as PIEs); (iv) establishment of a specialist audit team to manage all PIE engagements (and engagements for other entities within the scope of the FRC inspection regime), to seek to ensure that risks associated with PIEs are properly addressed; and (v) introduction of enhanced EQCR procedures. The assessment of effectiveness of these measures will be part of the agreed non-financial sanction. However, notwithstanding the remedial steps taken, Executive Counsel considers there is a risk that the same types of breaches could recur.

Aggravating factors

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

Mitigating factors

162. MHA has demonstrated contrition for the breaches.
163. MHA brought breaches of *Relevant Requirements* in the FY2019 Audit to the attention of the FRC's Audit Quality Review (**AQR**) inspection team.
164. As paragraph 69 of the Policy explains:

"In order for cooperation to be considered as a mitigating factor at the point of determining appropriate sanction it will therefore be necessary for the Statutory Auditors and Statutory Audit Firms to have provided an exceptional level of cooperation."

⁴¹ MHA only came within the scope of the AEP in 2016.

165. MHA provided an exceptional level of co-operation during the investigation of the breaches by Executive Counsel in that MHA voluntarily provided its own internal review of the FY2019 Audit (including details of its findings) to Executive Counsel and liability was agreed, at an early stage.

166. In light of the mitigating factors, Executive Counsel considers that a discount to MHA's financial sanction of 7.5% is appropriate.

Deterrence

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

Discount for Admissions and Settlement

168. Having taken into account the admissions by MHA and the stage at which those admissions were made (at an early point within Stage 1 for the purposes of paragraph 84 of the Policy), Executive Counsel determined that a reduction of 35% to the financial sanction for early disposal is appropriate, such that a financial sanction of £120,250 is payable.

Other considerations

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

Ms Weston

Identification of Sanction

170. Executive Counsel imposes the following *Sanctions* against Ms Weston:

170.1. a financial sanction of £30,000, adjusted for aggravating and mitigating factors, and discounted for admissions and early disposal by 35% so that the financial sanction payable is £19,500. The financial sanction shall be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;

170.2. a published statement in the form of a Severe Reprimand; and

170.3. a declaration that the FP2018 Audit report signed by Ms Weston did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*.

171. In reaching this decision, Executive Counsel has considered the following matters in accordance with the Policy.

Nature, seriousness, gravity and duration of the breaches

172. The factors noted at 148 – 155 above are repeated.

173. The failure to conduct the FP2018 Audit on the correct basis arose from a misunderstanding on the part of Ms Weston as regards the status of MRG UK.

174. The FP2018 Audit was accepted as a new audit engagement at a time when MHA had a policy of not undertaking PIE audits.

175. Ms Weston was a senior member of the Audit Department (being the co-head of the financial services audit team) with over thirty years of experience at the time of the FP2018 Audit.

176. Ms Weston did not stand to gain any profit or benefit from the breaches of the *Relevant Requirements*.

177. Ms Weston has now retired from MHA and is no longer a *Statutory Auditor*.

178. At the time of her retirement Ms Weston had a clean disciplinary record with the FRC and ICAEW.

Aggravating factors

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

Mitigating factors

180. Ms Weston has expressed contrition and apologised for the breaches. There are no other mitigating factors that have not already been considered in the context of the seriousness of the breaches.

Deterrence

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

Discount for Admissions and Settlement

182. Having taken into account the admissions made by Ms Weston and the stage at which those admissions were made (at an early point within Stage 1 for the purposes of paragraph 84 of the Policy), Executive Counsel determined that a reduction of 35% to the financial sanction for early disposal is appropriate, such that a financial sanction of £19,500 is payable.

Ms Morgan

Identification of Sanction

183. Executive Counsel imposes the following *Sanctions* against Ms Morgan:

183.1. a financial sanction of £25,000, adjusted for aggravating and mitigating factors, and discounted for admissions and early disposal by 25% so that the financial sanction payable is £18,750. The financial sanction shall be paid no later than 28 days after the date of this *Final Settlement Decision Notice*;

183.2. a published statement in the form of a Severe Reprimand;

183.3. a declaration that the FY2019 Audit report signed by Ms Morgan did not satisfy the *Relevant Requirements*, as set out in this *Final Settlement Decision Notice*; and

183.4. an order that:

183.4.1. Ms Morgan provide Executive Counsel and the Executive Director of Supervision with any ICAEW inspection outcomes in the next three inspections of her non-PIE audit engagements; and

183.4.2. Ms Morgan provide Executive Counsel and the Executive Director of Supervision with written confirmation of at least 40 hours of verifiable CPD for each of the next three years following the date of this *Final Settlement Decision Notice*. Such training shall include at least one session on the scope of RI duties in audit and other areas relevant to the breaches in this case, to be agreed with the FRC.

184. In reaching this decision, Executive Counsel has considered the following matters in accordance with the Policy.

Nature, seriousness, gravity and duration of the breaches

185. The factors noted at 148 - 155 above are repeated.

186. Ms Morgan did not stand to gain any profit or benefit from the breaches of the *Relevant Requirements*.

187. Ms Morgan is not on the PIE Auditor Register at present but remains a *Statutory Auditor*.

188. Ms Morgan has a clean disciplinary record with the FRC and ICAEW

Aggravating factors

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

Mitigating factors

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

Deterrence

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

Discount for Admissions and Settlement

192. Having taken into account the admissions made by Ms Morgan and the stage at which those admissions were made (within Stage 1 for the purposes of paragraph 84 of the Policy, but at a later point than those made by MHA and Ms Weston), Executive Counsel determined that a reduction of 25% to the financial sanction for early disposal is appropriate, such that a financial sanction of £18,750 is payable.

VII. COSTS

193. Executive Counsel requires that the Respondents pay her costs in full in this matter, being £330,000. Such costs shall be paid no later than 28 days after the date of this *Final Settlement Decision Notice*.

Signed:

[Redacted.]

**CLAUDIA MORTIMORE
DEPUTY EXECUTIVE COUNSEL**

Date: 4 December 2023

APPENDIX 1 – EXTRACTS OF RELEVANT REQUIREMENTS

ISA 220 – Quality Control for an Audit of Financial Statements

Paragraph 11(c) of ISA 220 states that *“The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall:*

...

- c) *Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is possible under applicable law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action.”*

Paragraph 12 of ISA 220 states that *“The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed, and shall determine that conclusions reached in this regard are appropriate.”*

Paragraph 16 of ISA 220 states that *“The engagement partner shall take responsibility for reviews being performed in accordance with the firm’s review policies and procedures.”*

Paragraph 17 of ISA 220 states that *“On or before the date of the auditor’s report, the engagement partner shall, through a review of the audit documentation and discussion with the engagement team, be satisfied that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued.”*

Paragraph 19 of ISA 220 states that *“For audits of financial statements of listed entities, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required, the engagement partner shall:*

- a) *Determine that an engagement quality control reviewer has been appointed;*
- b) *Discuss significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer; and*
- c) *Not date the auditor’s report until the completion of the engagement quality control review.”*

ISA 230 – Audit Documentation

Paragraph 8 of ISA 230 states that *“The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:*

- a) The nature, timing and extent of the audit procedures performed to comply with the ISAs (UK) and applicable legal and regulatory requirements;*
- b) The results of the audit procedures performed, and the audit evidence obtained; and*
- c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.”*

Paragraph 14 of ISA 230 states that *“The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor’s report.*

In the UK, the assembly of the final audit file shall be completed no later than 60 days from the date of the auditor’s report.”

ISA 250 – Obtaining and understanding of the regulatory framework applicable

Paragraph 13 of ISA 250 states that *“As part of obtaining an understanding of the entity and its environment in accordance with ISA (UK) 315 (Revised June 2016), the auditor shall obtain a general understanding of:*

- a) The legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates; and*
- b) How the entity is complying with that framework.”*

ISA 260 – Reporting to those charged with Governance

Paragraph 16R-2 of ISA 160 states that *“For audits of financial statements of public interest entities, the auditor shall submit an additional report to the audit committee of the entity explaining the results of the audit carried out and shall at least:*

- a) Include the declaration of independence required by paragraph 17R-1(a);*
- b) Identify each key audit partner(s) involved in the audit;*
- c) Where the auditor has made arrangements for any of the auditor’s activities to be conducted by another firm^{1f} that is not a member of the same network, or has used*

the work of external experts, the report shall indicate that fact and shall confirm that the auditor received a confirmation from the other firm and/or the external expert regarding their independence;

- d) Describe the nature, frequency and extent of communication with the audit committee or the body performing equivalent functions within the entity, the management body and the administrative or supervisory body of the entity, including the dates of meetings with those bodies;*
- e) Include a description of the scope and timing of the audit;*
- f) Where more than one auditor has been appointed, describe the distribution of tasks among the auditors;*
- g) Describe the methodology used, including which categories of the balance sheet have been directly verified and which categories have been verified based on system and compliance testing, including an explanation of any substantial variation in the weighting of system and compliance testing when compared to the previous year, even if the previous year's audit was carried out by another firm;*
- h) Disclose the quantitative level of materiality applied to perform the audit for the financial statements as a whole and where applicable the materiality level or levels for particular classes of transactions, account balances or disclosures, and disclose the qualitative factors which were considered when setting the level of materiality;*
- i) Report and explain judgments about events or conditions identified in the course of the audit that may cast significant doubt on the entity's ability to continue as a going concern and whether they constitute a material uncertainty, and provide a summary of all guarantees, comfort letters, undertakings of public intervention and other support measures that have been taken into account when making a going concern assessment;*
- j) Report on any significant deficiencies in the entity's or, in the case of consolidated financial statements, the parent undertaking's internal financial control system, and/or in the accounting system. For each such significant deficiency, the additional report shall state whether or not the deficiency in question has been resolved by management;*
- k) Report any significant matters involving actual or suspected non-compliance with laws and regulations or articles of association which were identified in the course of the audit, in so far as they are considered to be relevant in order to enable the audit committee to fulfil its tasks;*

- l) *Report the valuation methods applied to the various items in the annual or consolidated financial statements including any impact of changes of such methods;*
- m) *In the case of an audit of consolidated financial statements, explain the scope of consolidation and the exclusion criteria applied by the entity to the nonconsolidated entities, if any, and whether those criteria applied are in accordance with the financial reporting framework;*
- n) *Where applicable, identify any audit work performed by component auditors in relation to an audit of consolidated financial statements other than by members of the same network to which the auditor of the consolidated financial statements belongs;*
- o) *Indicate whether all requested explanations and documents were provided by the entity;*
- p) *Report:*
 - i) *Any significant difficulties encountered in the course of the audit;*
 - ii) *Any significant matters arising from the audit that were discussed or were the subject of correspondence with management; and*
 - iii) *Any other matters arising from the audit that in the auditor's professional judgment, are significant to the oversight of the financial reporting process.*

Where more than one auditor has been engaged simultaneously, and any disagreement has arisen between them on auditing procedures, accounting rules or any other issue regarding the conduct of the audit, the reasons for such disagreement shall be explained in the additional report to the audit committee.”

Paragraph 20R-1(b) of ISA 260 states that *“For audits of financial statements of public interest entities:*

...

- b) *The additional report to the audit committee shall be signed and dated by the engagement partner.”*

Paragraph 21R-1 of ISA 260 states that *“For audits of financial statements of public interest entities, the auditor shall submit the additional report to the audit committee not later than the date of submission of the auditor’s report.”*

ISA 300 – Identifying characteristics of the Engagement

Paragraph 8(a) of ISA 300 states that *“In establishing the overall audit strategy, the auditor shall:*

- a) Identify the characteristics of the engagement that define its scope;”*

ISA 315 – Identifying and Assessing the Risks of Material Misstatement

Paragraph 11 of ISA 315 states that *“The auditor shall obtain an understanding of the following:*

- a) Relevant industry, regulatory, and other external factors including the applicable financial reporting framework.*
 - b) The nature of the entity, including:
 - i) its operations;*
 - ii) its ownership and governance structures;*
 - iii) the types of investments that the entity is making and plans to make, including investments in special-purpose entities; and*
 - iv) the way that the entity is structured and how it is financed*
*to enable the auditor to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements.**
- c) The entity’s selection and application of accounting policies, including the reasons for changes thereto. The auditor shall evaluate whether the entity’s accounting policies are appropriate for its business and consistent with the applicable financial reporting framework and accounting policies used in the relevant industry.*
 - d) The entity’s objectives and strategies, and those related business risks that may result in risks of material misstatement.*
 - e) The measurement and review of the entity’s financial performance.”*

ISA 330 – Presentation of Financial Statements

Paragraph 24 of ISA 330 states that *“If the auditor plans to use audit evidence from a previous audit about the operating effectiveness of specific controls, the auditor shall establish the continuing relevance of that evidence by obtaining audit evidence about whether significant changes in those controls have occurred subsequent to the previous audit. The auditor shall*

obtain this evidence by performing inquiry combined with observation or inspection, to confirm the understanding of those specific controls, and:

- a) *If there have been changes that affect the continuing relevance of the audit evidence from the previous audit, the auditor shall test the controls in the current audit.*
- b) *If there have not been such changes, the auditor shall test the controls at least once in every third audit, and shall test some controls each audit to avoid the possibility of testing all the controls on which the auditor intends to rely in a single audit period with no testing of controls in the subsequent two audit periods.”*

ISA 500 – Audit Evidence

Paragraph 6 of ISA 500 states that *“The auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.”*

ISA 570 – Going Concern

Paragraph 10 of ISA 570 states that *“When performing risk assessment procedures as required by ISA (UK) 315 (Revised June 2016), the auditor shall consider whether events or conditions exist that may cast significant doubt on the entity’s ability to continue as a going concern. In so doing, the auditor shall determine whether management has already performed a preliminary assessment of the entity’s ability to continue as a going concern, and:*

- a) *If such an assessment has been performed, the auditor shall discuss the assessment with management and determine whether management has identified events or conditions that, individually or collectively, may cast significant doubt on the entity’s ability to continue as a going concern and, if so, management’s plans to address them;*
or
- b) *If such an assessment has not yet been performed, the auditor shall discuss with management the basis for the intended use of the going concern basis of accounting, and inquire of management whether events or conditions exist that, individually or collectively, may cast significant doubt on the entity’s ability to continue as a going concern.”*

ISA 700 – Forming an Opinion and Reporting on Financial Statements

Paragraph 45R-1 of ISA 700 states that *“For audits of complete sets of general purpose financial statements of public interest entities, the auditor’s report shall:*

- a) State by whom or which body the auditor(s) was appointed;*
- b) Indicate the date of the appointment and the period of total uninterrupted engagement including previous renewals and reappointments of the firm;*
- c) Explain to what extent the audit was considered capable of detecting irregularities, including fraud;*
- d) Confirm that the audit opinion is consistent with the additional report to the audit committee. Except as required by paragraph 45R-1(d), the auditor’s report shall not contain any cross-references to the additional report to the audit committee;*
- e) Declare that the non-audit services prohibited by the FRC’s Ethical Standard were not provided and that the firm remained independent of the entity in conducting the audit; and*
- f) Indicate any services, in addition to the audit, which were provided by the firm to the entity and its controlled undertaking(s), and which have not been disclosed in the annual report or financial statements.”*

ISA 701 – Communicating Key Audit Matters in the Auditor’s Report

Paragraph 13R-1(a) of ISA 701 states that *“For audits of financial statements of public interest entities, in describing each of the key audit matters in accordance with paragraph 13, the auditor’s report shall provide, in support of the audit opinion:*

- a) A description of the most significant assessed risks of material misstatement, (whether or not due to fraud);*

...

Where relevant to the above information provided in the auditor’s report concerning each of the most significant assessed risks of material misstatement (whether or not due to fraud), the auditor’s report shall include a clear reference to the relevant disclosures in the financial statements.”

The Revised Ethical Standard 2016

5.167R of the Ethical Standard states that *“An audit firm carrying out the statutory audit of a public interest entity, or any member of the network to which the statutory auditor or the audit firm belongs, shall not directly or indirectly provide to the audited entity, to its parent undertaking or to its controlled undertakings within the Union any prohibited non-audit services in:*

- a) the period between the beginning of the period audited and the issuing of the audit report; and*
- b) the financial year immediately preceding the period referred to in point (a) in relation to the services listed in point (e) of the second subparagraph.*

For these purposes of this Article, prohibited non-audit services shall mean:

...

- c) bookkeeping and preparing accounting records and financial statements;”*

ISQC 1 – Quality Control for Firms

Paragraph 36R-1 of ISQC 1 states that *“For audits of financial statements of public interest entities, before the auditor’s report and the additional report to the audit committee are issued, the firm shall require that an engagement quality control review shall be performed to assess whether the key audit partner(s) could reasonably have come to the opinion and conclusions expressed in the draft of those reports.”*