

PAC ANNUAL CONFERENCE
PROFESSIONAL ACCOUNTING FUTURES

The Carillion Bankruptcy Case: Where it Led
a fireside chat with

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Carillion Bankruptcy: A Nightmare that Challenged the Foundations of the U.K. Accounting Profession, Brooks & Dunn, 9e, p. 473

- Very large multinational company, construction & services
- March 31, 2017, clean audit opinion – bankrupt in Jan. 2018
- Workers unemployed, jobs & services stop, retirement plans unfunded
- Organic losses hidden by acquisitions – overpaid, goodwill
- Debt financing used for acquisitions & unfounded bonuses
- Aggressive revenue recognition policies (% of completion), losses not included
- Reverse factoring deal – borrowing misstated & hidden
- Auditors (KPMG) were “mere spectators”, had conflicts of interest, “failed to exercise & voice professional scepticism” regarding client’s aggressive accounting judgements. Instead, they were complicit with them.
- Internal auditors (Deloitte) failed to identify major bad debts – one of £200 million
- Advisors on cost reduction (E&Y) paid for advice not used
- **Dash for cash ... mere spectators ... poor professional scepticism ... failed to protect the public interest**

Professionalism involves ...

*Professional values, ethics, and attitudes include a commitment to **technical competence, ethical behavior** (e.g., independence, objectivity, confidentiality, and integrity), **professional manner** (e.g., due care, timeliness, courteousness, respect, responsibility, and reliability), **pursuit of excellence** (e.g., commitment to continual improvement and life-long learning), and social responsibility (e.g., awareness and consideration of **the public interest**).*

Professional values, ethics and attitudes, IAESB Glossary of Terms, p. 29.

Plus mindset factors – **skepticism** and **moral courage**

Carillion Bankruptcy: A Nightmare ..., 9e, p. 473

Overview – Clean audit opinion, bankrupt 10 months later, auditors mere spectators

Carillion Bankruptcy – Analysis of Audit & Prof. Acc. Professionalism Deficiencies

Deficiencies (selected)	Technical Competence	Ethical Behavior	Professional Manner	Pursuit of Excellence	Social Resp. - Public Interest	Prof Skepticism, Morale Courage
Overpayment for competitors acquired creating too much goodwill on books to give impression of growth	Auditors & Co. Prof. Acc.	Integrity?	Due care?		Both failed	Both failed
Failure to analyse and challenge excess accumulated goodwill value created – it was impaired	Both failed	Integrity?	Due care, responsibility ?		Both failed	Both failed
Failure to consider (FTC) <ul style="list-style-type: none"> Excess debt impact of acquisitions Borrowed to pay bonuses, dividends, but not pension commitments Lack of coherent acquisition strategy 	Failed to understand significance	Integrity?	Due care, responsibility ?		Both failed	Both failed
FTC aggressive accounting policies: <ul style="list-style-type: none"> Recording profit on construction contracts before client approval Ignored problem costs in % of completion calcs., overstating profits Reverse factoring arrangement disguised actual cost of bank financing Were these policies sustainable? 	Failed to understand significance and to check basis of rev. recognition	Integrity? Objectivity? Independence?	Due care, responsibility?		Both failed	Both failed
Did not know of: <ul style="list-style-type: none"> £200 million dispute (£400 mil impact) Carillion was most shorted stock 	Failed to understand significance		Due care lacking		Both failed	Both failed
Conflicts of interest <ul style="list-style-type: none"> KPMG audits Co. and pensions plan Deloitte (int. audit), EY (consulting) 	Failed to understand vulnerability	Independence lacking	Respons-ibility lacking		External Acc's failed	Conflicts may have left vulnerable