PUBLIC NOTICE

Enforcement Action

IRISH AUDITING AND ACCOUNTING SUPERVISORY AUTHORITY (IAASA)

IN THE MATTER OF

Brian Hughes

Respondent

1. Following an investigation by the Irish Auditing and Accounting Supervisory Authority ('the Authority'), a Settlement Agreement has been agreed and the Authority has decided to impose a **reprimand** and the respondent is further **fined €10,500**.

2. The contraventions were admitted by the respondent.

Background

3. This matter concerned the statutory audit of the financial statements of Greenlight Reinsurance Ireland DAC for the year end 2018 (herein the entity). The respondent was the statutory auditor for the statutory audit of those financial statements. As Engagement Partner, he was required to take responsibility for the overall quality of each audit engagement, for the supervision and performance of the audit engagement and for the auditor's report being appropriate in the circumstances. Further he was required, through a review of the audit documentation and discussion with the engagement team, to be satisfied that sufficient appropriate audit evidence had been obtained.

4. Although the entity was a subsidiary of a Cayman Islands domiciled company which is quoted on the NASDAQ stock exchange in the United States, the respondent was required to conduct the audit for the entity on its statutory financial statements in accordance with the relevant applicable auditing standards (ISA's Ireland) as it is registered in Ireland.

The Relevant Standards of Conduct

5. As a result of the deficiencies identified in the audit file reviewed, a number of contraventions were identified.

6. Auditors are required to conduct an audit in accordance with applicable technical and professional standards, the relevant auditing standards, were the International Standards on Auditing (Ireland) ("**ISAs**"). The purpose of ISAs is to establish standards and general principles with which auditors are required to comply. Together they form a body of standards that should be applied before an auditor

can express an opinion that financial statements give a 'true and fair view' within the meaning of the Companies Act 2014.

7. Aspects of the following ISAs are referred to in this document:

ISA (Ireland) 200 - Overall objectives of the independent auditor and the conduct of an audit in accordance with international standards on auditing

ISA (Ireland) 220 - Quality Control for an Audit of Financial Statements

ISA (Ireland) 260 - Communication with Those Charged with Governance

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

ISA (Ireland) 700 - Forming an opinion and reporting on financial statements

ISA (Ireland) 701 - Communicating Key Audit Matters in the Independent Auditor's Report

1. You did not ensure sufficient appropriate audit evidence was obtained to support the conclusion reached in the auditor's report in that:

There was no or no sufficient evidence:

(i) **(a) that the work undertaken by BDO network firm and/or BDOC Actuarial team was directed and/or supervised by you in the audit work it performed in accordance with US GAAS.**

(b) that you considered in detail the differences between the requirements of US GAAS and ISAs Ireland.

ISA 220 (Ireland) the following paragraphs are of relevance:

14. The engagement partner shall be satisfied that the engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to:

(a) Perform the audit engagement in accordance with professional standards and applicable legal and regulatory requirements; and

(b) Enable an auditor's report that is appropriate in the circumstances to be issued.

15. The engagement partner shall take responsibility for:

(a) The direction, supervision and performance of the audit engagement in compliance with professional standards and applicable legal and regulatory requirements; and

(b) The auditor's report being appropriate in the circumstances.

16. The engagement partner shall take responsibility for reviews being performed in accordance with the firm's review policies and procedures.

17. 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.

ISA 200 (Ireland) paragraph 20 states:

The auditor shall not represent compliance with ISAs (Ireland) in the auditor's report unless the auditor has complied with the requirements of this ISA and all other ISAs (Ireland) relevant to the audit.

8. There was insufficient audit evidence on the audit file that steps were taken by the respondent to ensure that the audit work was performed in accordance with the requirements of ISAs (Ireland).

9. The BDO network firm performed the audit of the parent company based in United States and the entity's accounts were consolidated into this company. The majority of the audit work on this audit was performed by the BDO network firm based in the United States. BDO network engaged BDOC actuarial (BDO US Internal Actuary) team to examine the overall adequacy of the loss reserve for the parent company. The audit work performed by the BDO network firm was performed in accordance with US GAAS (US Generally Accepted Auditing Standards), not ISAs (Ireland). Further there was insufficient evidence on the audit file to indicate that the audit was performed in accordance with the relevant standards for Ireland. In the planning document on the audit file there was a note stating that "*none of the limited differences noted between US GAAS and ISA's would lead to insufficient audit testing".* This statement was recorded on the audit file and does not evidence how each relevant ISA was assessed or how it was complied with.

(ii) of considerations and conclusions to test the significant risk account Gross premium written regarding the sampling rationale and its sufficiency.

(iii) that an evaluation was undertaken as to the appropriateness of BDOC-Actuarial's work in relation to the significant account - Total loss reserves; in particular; BDOC-Actuarial performed their work and stated their conclusions with reference to the parent company's materiality threshold of $7.5m whereas the materiality for the audited Entity was $672k.

10. Ground 1(ii) and 1(iii) are dealt with together. ISA 220 (Ireland) paragraph 15 as set out above is relevant.

<u>Premiums</u>

11. The BDO network firm tested a sample of six contracts related to the entity. There was no rationale recorded on the audit file as to why it was concluded that the sample of six contracts was sufficient. The engagement team examined two of these six contracts tested by the BDO network firm. One of the steps performed by the BDO network firm was an "examination of accounting treatment". This was done with reference to US GAAP (US Generally Accepted Accounting Principles). There was no evidence that the treatment in accordance with the entity's accounting framework was reviewed. Further, the work performed by the BDO network firm was performed with reference to the parent company's materiality levels, which were far higher than the materiality levels set for the entity.

<u>Technical reserves</u>

12. The respondent's expert, BDOC-Actuarial, was engaged by the BDO network firm to examine the overall adequacy of the loss reserve for the parent company by evaluating methods, data, and significant assumptions used in developing estimates. BDOC-Actuarial performed its work and stated its conclusions with reference to the parent company's materiality thresholds. The parent company's materiality level was $7.5m compared to the materiality level for the audit of the entity which was $672k. In those circumstances there was no explanation on the audit file as to how any of the conclusions reached by BDOC-Actuarial could have been used as evidence in the audit of the entity.

(iv) that the audit approach taken to test internal controls relevant to the audit of the significant accounts- Gross premiums written and total loss reserves was communicated with

those charged with governance (TCWG), including an assessment of the control deficiencies identified by the BDO network firm as to whether these constituted significant deficiencies in relation to the Irish entity.

ISA260 states:

> *15. The auditor shall communicate with those charged with governance an overview of the planned scope and timing of the audit, which includes communicating about the significant risks identified by the auditor.*
>
> *When the auditor is required or decides to communicate key audit matters in accordance with ISA (Ireland) 701, the overview of the planned scope and timing of the audit shall also include communicating about the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditor, including those that had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team.*

13. A controls-testing approach was performed to the audit of Gross premiums written and provision Technical reserves, both of which were significant risk areas. However, the controls testing approach was not communicated in the report to TCWG. The BDO network firm had identified two deficiencies in internal controls and these were communicated to those charged with governance of the parent company. However, the respondent did not evidence that he had assessed whether these constituted a significant deficiency for the purposes of the entity and he did not communicate these issues to TCWG of the entity.

(v) of the rationale for the determination as to whether certain matters that required significant attention were key audit matters.

ISA701 paragraph 18 states:

> *The auditor shall include in the audit documentation:*
>
> *(a) The matters that required significant auditor attention as determined in accordance with paragraph 9, and the rationale for the auditor's determination as to whether or not each of these matters is a key audit matter in accordance with paragraph 10;*

14. There was a lack of documentation on the audit file to demonstrate the rationale for the determination as to whether certain matters that required significant attention were key audit matters.

(vi) that the disclosures in the financial statements for (a)the significant risk account Loss reserves (Note 16 – Technical provisions) was audited and/or (b) that the disclosures regarding the auditor's remuneration were in compliance with the requirements of the Companies Act 2014.

ISA700 paragraph 12 states:

> *The auditor shall evaluate whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework. This evaluation shall include consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgments.*

15. There was a lack of sufficient appropriate audit evidence on the audit file in respect of relevant disclosures in the financial statements. For example;

- On the audit file in order to demonstrate compliance with the disclosure requirements of the applicable Financial Reporting Standard, there was a checklist and in the section marked "Disclosure" every item was ticked whether or not it was relevant to the audit.
- in order to demonstrate compliance with the European Union (Insurance Undertaking: Financial Statements) Regulations 2015, the Statutory Instrument was attached and a number of items were ticked or marked as not applicable. However, many disclosure requirements had no mark beside them and therefore there was a lack of evidence to demonstrate that these disclosure requirements were assessed.
- the entity disclosed an amount for "Auditors' remuneration- tax" in the financial statements. However, no tax compliance services were provided by the audit firm to the entity. As such the respondent's remuneration disclosure in the financial statements was not compliant with the requirements of the Companies Act 2014.
- Finally, there was no evidence on the audit file that the disclosures in Note 16 – Technical provisions were audited.

(vii) as to how procedures to gain an understanding of the entity and its environment, including its internal control, were sufficient to identify and assess the risks of material misstatement in the Entity's financial statements.

The following paragraphs of ISA 315 are relevant:

> *11. 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.*
>
> *12. The auditor shall obtain an understanding of internal control relevant to the audit. Although most controls relevant to the audit are likely to relate to financial reporting, not all controls that relate to financial reporting are relevant to the audit. It is a matter of the auditor's professional judgment whether a control, individually or in combination with others, is relevant to the audit.*
>
> *25. The auditor shall identify and assess the risks of material misstatement at:*
>
> *(a) the financial statement level; and*

(b) the assertion level for classes of transactions, account balances, and disclosures to provide a basis for designing and performing further audit procedures.

16. The BDO network firm performed procedures to gain an understanding of the parent company and its environment. The respondent as the statutory auditor for the entity in Ireland used these procedures as the basis for understanding the Irish entity and its environment. There was insufficient evidence on the audit file to demonstrate how BDO network's procedures were sufficient to:

- gain an understanding of relevant Irish industry, regulatory, and other external factors; or
- understand the nature of the entity, including its operations, its ownership structure and governance, or the type of investments the entity plans to make.

17. In addition the audit file had not sufficiently evidenced the procedures utilised concerning the entity's selection and application of accounting policies or the respondent's understanding of the entity's objectives and strategies and those related business risks that may result in risks of material misstatement.

18. The BDO network firm also performed procedures to gain an understanding of the internal controls of the parent company. It was apparent from the audit file that a significant portion of the procedures performed by the BDO network firm were not relevant to the entity. There was insufficient evidence on the audit file to demonstrate which parts of this work related to the entity and which parts did not.

19. Further, there was a lack of evidence to demonstrate an understanding of the financial reporting process. This process should have included reference to the fact that the preparation of the accounts in accordance with the Irish accounting framework had been applied.

20. There was evidence on the audit file that at the planning meeting a number of significant risks at the financial statement level were identified. However, the majority of the audit work was performed by the BDO network firm, and it was performed with reference to a different set of risks. The respondent had not identified any risks at the assertion level. All the risks identified in the planning meeting agenda were at the financial statement level.

(viii) that an identification and an assessment was undertaken of risks of material misstatement at the assertion level for classes of transactions, account balances, and disclosures.

ISA 315 paragraph 25 as set out above is relevant.

21. The relevant evidence concerning this ground is already set out above.

Sanction

22. The sanction imposed must be proportionate balancing the need to protect the public with the respondents' own interests.

23. The purpose of sanction is to declare and uphold proper standards of conduct amongst statutory auditors and statutory audit firms and to maintain public and market confidence in statutory auditors and statutory audit firms and their regulators. In addition, the purpose of sanction is to protect the public from statutory auditors and statutory audit firms whose standard of work falls short of the high-quality audit expected of statutory auditors and statutory audit firms.

24. In coming to the appropriate and proportionate sanction the Authority took into account the Authorities sanctions guidance (effective from 8 March 2021) : The Authority also had regard to its published policy on settlement agreements. The Authority had regard to:

(a) The gravity and duration of the relevant contravention;

(b) The degree of responsibility of the specified person;

(c) The financial strength of the specified person;

(d) The amount of profits gained or losses avoided by the specified person in consequence of the contravention;

(e) The level of cooperation of the specified person with the Supervisory Authority;

(f) Previous relevant contraventions committed by the specified person.

25. In considering the appropriate sanction in this case the Authority took into account a number of factors.

26. In mitigation the respondent has engaged from the outset of the preliminary investigation with the Authority. The respondent’s timely admissions demonstrate his insight into the contraventions that were identified. The Authority has also taken into account that the respondent has no previous disciplinary history.

27. In considering the level of engagement of the respondent with the Authority, an early settlement discount was also applied to any fine imposed. The Authority took into account the timing of the admissions and it considered that it was appropriate to apply an early settlement discount of 30% to the level of the fine imposed.

28. The Authority considered the sanction options open to it in ascending order of seriousness and it concluded that the appropriate and proportionate sanction in respect of the respondent is a **reprimand** and that he be further **fined €10,500**.

Dated: 28 March 2023