**IN THE MATTER OF:**

**THE EXECUTIVE COUNSEL TO THE FINANCIAL REPORTING COUNCIL**

**- and –**

**1. TIMOTHY WHISTON**
**2. JOHN WHELAN**

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**FORMAL COMPLAINT**

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## INTRODUCTION

### The FRC and the Accountancy Scheme

1. The Financial Reporting Council ("the FRC") is the independent disciplinary body for the accountancy and actuarial professions in the UK. The FRC's rules and procedures relating to accountants are set out in the Accountancy Scheme ("the Scheme") and the Accountancy Regulations ("the Regulations"), both dated 8th December 2014.

2. By paragraph 7(11) of the Scheme, if having reviewed any representations received for the purposes of paragraph 7(10) of the Scheme, the Executive Counsel to the FRC ('Executive Counsel") considers that there is a realistic prospect that a Tribunal will make an Adverse Finding against a Member or Member Firm and that a hearing is desirable in the public interest, then the Executive Counsel shall deliver a Formal Complaint against the Member or Member Firm to the Conduct Committee.[1]

[1] References to "Member" in this document relate to the definition as set out in paragraph 2(1) of the Scheme. References to "member" denote separate membership of the ICAEW (as to which, see post).

3. This is the Executive Counsel's Formal Complaint in respect of:

- Timothy Whiston, who was at all material times a member of the Institute of Chartered Accountants in England and Wales ("ICAEW"); and

- John Whelan, also a member at all material times of the ICAEW,

(together, "the Respondents").

4. By virtue of their membership of the ICAEW, the Respondents are also Members for the purposes of the Scheme.

5. This Formal Complaint concerns the conduct of the Respondents in relation to the recognition of revenue and cash in the interim accounts and annual financial statements of their employer, iSoft Group plc (iSoft") during the period 2003-2005.

6. There was no legitimate basis for this recognition and the Executive Counsel's case (as set out in Allegations 1-5, post is that the Respondents acted recklessly by causing or permitting it to happen. In conducting themselves in this way, they also acted with a lack of integrity.

7. A summary of the allegations is set out below. In providing this summary, the Executive Counsel does not refer to every aspect of the evidence.

**BACKGROUND**

**Part 1: The business of iSoft and the role played by the Respondents**

8. Prior to its incorporation in 1999, iSoft operated as a partnership within KPMG called "KPMG Health Systems". The business sought to address the administrative and clinical needs of healthcare provider organisations such as hospitals and NHS Trusts. This involved the provision and implementation of specialist software under licence, and also on-going customer support.

9. On incorporation, the company severed its ties with KPMG and traded in its own right. It was successful, achieving a full listing on the London Stock Exchange on

19th July 2000. In addition, it acquired FTSE 250 status following the merger with Torex on 23rd December 2003.

10. Mr Whiston joined the company as Finance Director in August 1997. In April 2000, he was appointed both company secretary and a statutory director of iSoft, positions he maintained throughout the period with which this case is concerned. In July 2003, he was made Chief Executive Officer designate, being formally appointed to that position in February 2004. He remained in this role until his departure from the company in 2006.

11. Mr Whelan joined iSoft on 6 January 2003 as European Financial Director. He attended some Board meetings by invitation throughout 2003, before being formally promoted to Group Finance Director in February 2004 (i.e. when Mr Whiston was himself promoted, see above). Mr Whelan was also made a statutory director of the company on that date. He left iSoft on 5th November 2004.

12. The following individuals are also referred to in this document and central to events as they unfolded:

[redacted]

Ian Storey: Mr Storey joined iSoft in 2001 as Group Accountant, becoming European Financial Controller in July 2003. He was responsible for the finance function of the UK and Ireland business units and for the production of monthly management accounts.

[redacted]

Glyn Williams: Mr Williams worked for Robson Rhodes, the firm of accountants responsible for auditing the iSoft accounts during the relevant period. Mr Williams was the audit engagement partner on the iSoft account.

Richard Baldwin: Mr Baldwin was the senior audit manager at Robson Rhodes with responsibility for the iSoft account.

13. In relation to this matter, Mr Storey (formerly a member of the ICAEW) has previously admitted Misconduct (as defined under the Scheme, see post), as have Mr Williams (a member of the ICAEW) and Robson Rhodes (a member firm of the ICAEW). Those admissions were made in proceedings in 2010 (Mr Storey) and 2011 (Mr Williams and Robson Rhodes).

14. As regards Robson Rhodes and Mr Williams it should be noted that the relevant allegations (i.e. those relating to cash and revenue recognition) were limited to a failure to obtain sufficient audit evidence in relation to the Irish Contract, and/or to test that evidence adequately. It should further be said, however, that the auditors were seriously hampered in this regard by the misleading information and material provided to them by iSoft (see post).

## Part 2: iSoft's interim accounts for the period ending 31st October 2003

### *The Irish Contract*

15. On 7th February 2003, the South Eastern Health Board in Ireland ("SEHB") wrote to iSoft to inform the company that it had been selected as the preferred supplier of software for the 'Multi-Agency Hospital Information Systems Project' ("the HIS Project"), following a lengthy tender process, commenced in 2000.[2] This concerned a major IT upgrade for the provision of healthcare in Ireland. It was in relation to the HIS Project that a contract ("the Irish Contract") was to be negotiated and, assuming terms could be agreed, later signed.

16. The Irish Contract envisaged an initial licence fee for the software provided by iSoft, following which there would be additional fees payable for upgrades and support services. The lifespan of the agreement was 10 years and the total potential sum payable under it was €56 million plus VAT.

[2] See volume 1 of the Hearing Bundle ("HB1") at p.1

17. Early communications from SEHB made a number of matters plain:

i) Although SEHB would be taking the lead, it was representing the interests of a number of institutions in Ireland, including other regional Health Boards, the so-called 'Eastern Hospitals' and the Health Boards Executive ("HeBE"). It was envisaged that some or all of these bodies may in due course be party to the Irish Contract, either immediately on its completion or on a phased basis thereafter.

ii) There was a degree of resistance to iSoft's selection from the Dublin Academic Teaching Hospitals ("the DATHs"), who wished to retain their own IT systems and who questioned the ability of one company to provide a suitable national system.

iii) The viability of the HIS Project was entirely dependent on the receipt of funding from the Irish Department of Health & Children ("DHC"). If that was not forthcoming, no agreement could be signed.

18. ISoft hoped initially that contractual negotiations would be completed by the end of May 2003, but in the event matters progressed slowly. By early autumn, there was an anxiety at iSoft that the Irish Contract might not be signed before 31st October 2003 (i.e. the end of the company's half year accounting period).

19. In the light of forecasts previously provided to the City, the Respondents recognised the negative impact that this may have on the company. In an email dated 9th September 2003, entitled *"Half Year Out-turn without Ireland"*, Mr Whelan informed Mr Whiston and [redacted] that if the Irish Contract was not signed by period end, a forecast profit before tax of £9.5 million would be converted into a loss of £11 million.[3]

20. Mr Whelan concluded his email by making reference to the impact that failure to sign would have on the company's cash position as well. Whilst he had held preliminary discussions with a third party funder about a factoring agreement, the lead-in time on this arrangement was such that the Irish Contract would need to be signed by mid-October if this was to come to fruition.

[3] HB1, p.24-25

21. Over the weeks which followed, iSoft redoubled its efforts both to get the Irish Contract signed and also to assist SEHB in its attempts to secure funding from the DHC. There was an issue particularly over the latter, with concerns being voiced in correspondence that it might never be forthcoming, even if terms between the contracting parties could be agreed.

22. The Respondents were closely involved in this process, engaging directly in correspondence with their counterparts in the iSoft Operations Department, and also being forwarded emails and documents generated by those in Ireland. The importance of having the Irish Contract signed (as opposed to merely agreed in principle) dominated the communications.

23. As the deadline of 31st October 2003 approached, however, this goal had still not been achieved, with the result that matters became increasingly fraught. Notwithstanding the considerable pressure being applied by [redacted] and his team on SEHB, it proved impossible to accelerate the progress of the negotiations and, shortly before the expiry of the deadline, iSoft resigned itself to the fact that the Irish Contract would not be signed by that date.

24. As a result, iSoft wrote to SEHB on 29th October 2003, seeking to persuade it to enter into binding Heads of Agreement at least, and forwarding a draft 7 paragraph document for that purpose.[4] SEHB, however, was not willing to go that far. Instead, it amended the Heads of Agreement to make it clear that the contractual negotiations were not completed, inserting a new paragraph 8 for this purpose, as follows:

> "For the avoidance of doubt, the parties acknowledge that these Heads of Agreement are only a statement of the parties' current intentions. These Heads of Agreement are of no legal effect and are not binding on the parties. No legally binding relations exist or will exist until such time as a formal agreement providing for the transaction has been negotiated, executed by the parties and delivered. This Heads of Agreement is separate from iSoft's letter to the Health Agencies dated 29th October 2003 attaching the first draft of this Heads of Agreement and such letter does not form part of this Heads of Agreement in any way." [5]
>
> [Emphasis added].

[4] HB1, p.136-140
[5] HB1, p.150-153

It was in this form that the Heads of Agreement ("the non-binding Heads of Agreement") were signed by Mr Whiston on 31st October 2003.[6] Mr Whelan was also familiar with the terms of this document, writing on the copy in his possession *"Unhelpful but expected"* next to the paragraph cited above.[7]

25. To the certain knowledge of the Respondents, therefore, this was the state of play as at 31st October 2003, namely unfinished negotiations, no signed contract and Heads of Agreement which expressly disavowed any contractual relationship. In addition, no funding for the project had been agreed by the DHC, which meant that the entire deal remained provisional only at this stage.

26. It was against this background that the Respondents caused or permitted iSoft to recognise revenue from the Irish Contract ("the Irish revenue") in its half year accounts to 31st October 2003. It is the Executive Counsel's case that, by reference to the most basic principles of accountancy, there was no legitimate basis for doing so. The position is set out below.

***The relevant principles of accounting***

27. Financial reporting in the UK is governed by Generally Accepted Accounting Practice in the UK ('UK GAAP'), which comprises relevant legislation in force at the material time (for present purposes, the Companies Act 1985), the Listing Rules issued by the London Stock Exchange and the Accounting Standards and other guidance issued by the UK Accounting Standards Board ('ASB').[8]

28. The Companies Act 1985 contained a variety of requirements relating to accounting. Most importantly, for present purposes, it sets out the fundamental requirement that accounts shall give a 'true and fair view' of the state of affairs at the end of the year and of the profit or loss for that year (sections 226 and 227). This is an overriding requirement. It is generally the case that compliance with other parts of the Act and with accounting standards gives rise to accounts that give a true and fair view.

[6] HB1, p.184-185
[7] HB1, p.158-159

29. Accounting Standards meanwhile, seek to introduce appropriate accounting treatments and uniformity into the methods used to measure the financial consequences of commercial transactions and also the manner in which this information is presented in a company's financial statements. In turn, this is designed to ensure that such information is reliable, and that it is also comprehensible to shareholders, investors and others who may be interested in a company's performance.

30. By virtue of paragraph 36A of Schedule 4 of the Companies Act 1985, the financial statements of companies such as iSoft must therefore state whether they have been prepared in accordance with applicable Accounting Standards and give details of any material departure from those standards, along with the reasons for such departure.

31. The Accounting Standards issued by the ASB for this purpose are called Financial Reporting Standards ('FRS's'). The most relevant for the purposes of recognising revenue is FRS5, as examined below.

***The recognition of revenue***

32. By reference to the basic principle of accruals accounting, revenue from a contract should only be recognised in a company's financial statements to the extent that the sale of goods or services has taken place during the course of the accounting period under consideration. This will occur, generally, when all of the following conditions have been met:

    i) There is a signed contract or other right to the consideration;

    ii) The delivery or performance relating to the revenue has occurred in the relevant period; and

    iii) The collectability of the resulting receivable is probable.[9]

33. Prior to 23rd December 2003, these criteria were reflected in UK GAAP by a combination of FRS5 and also Schedules 4 and 4A of the Companies Act 1985.

[9] There may be cases where one of these criteria is not fully met, but where the other two are complied with to such a degree that the overall substance of the transaction allows for the revenue to be recognised. That exception does not arise on the facts of this case.

34. FRS5 is entitled *"Reporting the substance of transactions"*. The objective of it is to ensure that the substance of a company's transactions is reported in its financial statements. A key step in meeting this test is to identify whether the transaction in question has given rise to new assets for the company (i.e. whether future economic benefits will flow as a result of that transaction).

35. This is consistent with the requirements of paragraph 9 of Schedule 4 to the Companies Act 1985 which, in so far as relevant, reads as follows:

> "The amount of any item shall be determined on a prudent basis, and in particular –
>
> i. only profits realised at the balance sheet date shall be included in the profit and loss account."

Profits will only be realised once held by the company in the form of cash or of other assets, the ultimate cash realisation of which can be assessed with reasonable certainty.[10]

36. Whilst this guidance encompasses the basic principles of revenue recognition, prior to 23rd December 2003, there were no UK Accounting Standards which dealt with the position in so far as it related specifically to short term software contracts. That fact was reflected in the revenue recognition policy in place at iSoft for the period ending 31st October 2003, which read as follows:

> "Turnover
>
> The Group's revenues are derived from the sale of software product licences, the attendant installation, maintenance and support service revenues, supplies of third party hardware and software and the provision of PFI compliant finance facilities offered by third party funders. All revenue is reported exclusive of value added tax and other sales taxes.
>
> In the absence of a United Kingdom accounting standard on revenue recognition, the Group believes that the best guidance is set out under US GAAP, in particular SOP 97-2 and SAB 101. The Group's approach to revenue recognition closely mirrors US GAAP, with revenue only recognised when:

[10] FRS 18, para 28

- persuasive evidence of an arrangement exists
- physical delivery has occurred or services have been rendered
- the price to the customer is fixed or determinable
- any services deliverable under the supply arrangement are clearly separable from the software supply; and
- collectability is reasonably assured and there are no material outstanding conditions or contingencies attaching to the receipt of the monies due.

Recognition of profit

Turnover from the sale of software product licences is recognised at the time that the software licence is granted in accordance with agreed contractual triggers, typically the supply of the software product to the customer. Revenues from the attendant installation, maintenance and support services are recognised proportionally over the period that the services are provided with due regard for future anticipated costs. Payments received in advance of services are recorded in the balance sheet as deferred income."

37. This policy (which was approved by the Board of iSoft when signing off the interim accounts on 10th December 2003) broadly reflected the requirements of the US Accounting Standards on which it was based (i.e. Statement of Position 97-2 ("SOP 97-2") and SEC Staff Accounting Bulletin 101 ("SAB 101")).

38. SOP 97-2 was issued by the American Institute of Certified Public Accountants ("AICPA") in 1997 and is entitled *"Software Revenue Recognition"*. It provides guidance as to when revenue should be recognised in connection with activities which involve licensing, selling, leasing or otherwise marketing computer software.

39. Paragraphs 15-17 of SOP 97-2 are significant, in that they provide guidance of what constitutes *"persuasive evidence of an arrangement"*, as follows:

"If the vendor operates in a manner that does not rely on signed contracts to document the elements and obligations of an arrangement, the vendor should have other forms of evidence to document the transaction (for example, a purchase order from a third party or on-line authorisation). If the vendor has a customary business practice of utilizing written contracts, evidence of the arrangement is provided only by a contract signed by both parties.

Even if all other requirements set forth in this SOP for the recognition of revenue are met (including delivery), revenue should not be recognised on any element of the arrangement unless persuasive evidence of an arrangement exists."

40. The criteria for revenue recognition under SAB 101 are identical to those under SOP 97-2. The bulletin gives additional guidance, however, on the issue of delivery, confirming that this will not occur until the licence term begins. Accordingly, if a licensed product is physically delivered to the customer but the licence term has not yet begun, revenue should not be recognised prior to the inception of the licence term.

41. These US Accounting Standards were broadly consistent with their corresponding principles under UK GAAP, albeit that they reflected a more conservative approach to booking revenues than was generally adopted in the UK. In any event, there was nothing wrong in principle with iSoft's reliance on US GAAP for additional guidance on the issue, even if (as was the case) the position was in fact sufficiently dealt with under UK GAAP, as above.

42. What was important, however, was that, whichever model was adopted, iSoft ensured that it followed the relevant guidance when making decisions on recognising revenue. At the very least, it was bound to observe the basic principles of revenue recognition, as set out at paragraph 34 above. These issues are considered next in the context of the Irish Contract.

***Analysis of the iSoft decision to recognise revenue from the Irish Contract***

43. The preconditions for recognising revenue set out in iSoft's published accounting policy (which, as set out above, reflected the requirements of US GAAP) are to be conjunctively construed. In order to recognise the Irish revenue on 31st October 2003, iSoft needed to be sure that all such preconditions were satisfied as at that date.[11] However, only one such precondition could be met (it is accepted that the proposed price for the software and related services was effectively determined by this date).

44. As to the remaining applicable criteria:

[11] Subject to the observations at footnote 9, above.

i) There was no 'persuasive evidence of an arrangement' with SEHB and/or the remaining Health Boards. In relation to the Irish Contract, no such arrangement would have been concluded until the agreement had been signed by both parties. This is evidenced by the following matters:

a) A clear acknowledgement by iSoft that selection as preferred supplier in February 2003 was only a part of the process, and that getting the contract signed was the ultimate objective. For example, in an email sent on 10th February 2003 [redacted] to the Respondents (amongst others), [redacted] stated as follows:

*"Whilst 'the fat lady' has cleared her throat she has not sung until we get ink on the contract so we must continue with the good work in all the Irish sites*."[12]

b) The extent of the efforts subsequently made by iSoft to get the Irish Contract signed prior to 31st October 2003;

c) The express acceptance by iSoft in the Heads of Agreement dated 31st October 2003 that there would be no binding agreement between the parties unless and until the Irish Contract had been executed (see above);

d) The extent of the continuing efforts after 31st October 2003 to execute the document (see post);

e) The significance placed by iSoft on the signature itself (e.g. the email later sent from Mr Whelan to the prospective funders of the Irish Contract, Hanover Asset Finance Limited, dated 12th November 2003):

"*Still waiting for the magic signature*"[13]

[12] HB1, p.2-3
[13] HB1, p.229

f) The fact that someone at iSoft thought the signature sufficiently important to have provided the auditors with a forged copy of the Irish Contract, purporting to have been signed by all parties on 31st October 2003 (as to which, see more below).

In addition to the failure to secure a signed contract, the further failure to secure funding from the DHC was in itself fatal to the prospects of an arrangement having been reached.

ii) In relation to the delivery criterion, no software had been supplied under the Irish Contract as at 31st October 2003, which meant that the risks and rewards of ownership had not passed to the customer (critical to 'delivery' for the purposes of FRS5). Equally, no services had by that stage been provided by iSoft to SEHB or the other Health Boards.

iii) As regards collectability, this might have been reasonably assured in the event that the Irish Contract had been signed, on the basis that the debtor would have been the Irish government. The collectability of any debt, however, is founded on the prior existence of an obligation to pay over such sum. For the reasons set out above, the Irish government was under no such obligation.

45. In those circumstances, and whether by reference to iSoft's published accounting policy, UK GAAP or the basic principles of accruals accounting, as at 31st October 2003 there was no basis for recognising the Irish revenue: iSoft had not delivered any software to SEHB under the contract in question, which in return was under no obligation to make payment to the company. In other words, no sale had been made.

46. Notwithstanding this state of affairs, the Respondents recklessly took the decision to press on and recognise the revenue in any event. Worse still, in doing so they recklessly misled the auditors as to the true factual situation and failed to put the auditors, the Audit Committee and the Board fully in the picture. These matters are considered below.

***The Respondents' dealings with the auditors, the Audit Committee and the Board***

47. In providing information to the auditors for the purposes of the half year accounts, the Respondents had a clear professional duty to ensure that such information was accurate. This was an obligation which they recklessly failed to discharge.

48. For example, in a telephone call made on 2nd December 2003 by Mr Whelan to Richard Baldwin, Mr Whelan told Mr Baldwin that the licence had already passed to the Irish Health Board and that the software had been installed. Even the most cursory of checks by Mr Whelan would have revealed that this was not so. Moreover, making such checks would have involved minimal effort on his behalf – he had a clear line of contact with both the iSoft operational team in Manchester and also with iSoft personnel in Ireland [redacted]. He simply failed to make any proper enquiries before providing incorrect information to Mr Baldwin.

49. Similar observations apply to Mr Whiston. He was present with Mr Whelan at a meeting later on 2nd December 2003 when the auditors were also told that the Irish Contract had been signed on 31st October 2003 and yet neither of the Respondents saw fit to clarify that so far only iSoft had applied its signature to the document and that even iSoft had not signed the document until a meeting in Ireland on 12th November 2003 (see below).

50. The net result was that the auditors were left with a completely misleading impression as to the state of affairs. This was compounded by the fact that they had been provided with a forged signed copy of the Irish Contract, as set out above. Whilst it is not alleged that the Respondents were party to this forgery, or that they knew that it had been provided to the auditors, the fact of the forgery provides additional context to the decision by the auditors to sanction the revenue recognition.

51 In addition to being misled, recklessly by the Respondents and deliberately by others, the position of the auditors was made even more invidious by the failure of the Respondents to supply them with material information. This was particularly so in relation to the non-binding Heads of Agreement. Notwithstanding the meetings which took place between 31st October 2003 and 10th December 2003, and notwithstanding the correspondence during that period, the Respondents failed to

make any mention of this critical document. They had ample opportunity to do so. Without it, the auditors were deprived of the opportunity to make an informed decision about the legitimacy of iSoft's decision to recognise the revenue in its half year accounts.

52. If the Respondents had been acting diligently and in accordance with their professional duties, they would not only have ensured that the auditors had seen a copy of this document, but they would also have ensured that the auditors understood the following:

i) That the Irish Contract had not been signed by the end of the accounting period and that even after the end of the accounting period only iSoft had applied its signature to the document;

ii) That no goods or services had been provided by iSoft under the proposed terms of the Irish Contract, and that SEHB and the other Irish Health Boards were under no obligation to make payment in relation to the same;

iii) That no funding had been approved from the DHC and the Irish Contract could not be signed by the Irish unless and until such approval was given; and

iv) That, notwithstanding this state of affairs, it was proposed to recognise the Irish revenue in any event.

The failure to clarify matters on this basis illustrates the reckless approach taken by the Respondents in relation to revenue recognition on the Irish Contract. This manifested itself also in relation to the Respondents' dealings with the Audit Committee and the Board.

53. By virtue of the provisions of the Combined Code ("the Code") issued by the Hampel Committee in 1998, the management of a company (and in particular its directors) must supply the Board and the Audit Committee with timely and appropriate

information in order to enable those bodies to discharge their respective functions.[14] They should therefore also have been fully informed as to the true position.

54. Instead, the Respondents failed to make any proper mention to the Board of these salient issues, despite having manifest opportunities to do so (for example the Board meeting on 19th November 2003, at which the half year figures were discussed).[15]

55. As regards the Audit Committee, both Respondents attended a meeting of this Committee on 5th December 2003, at which Robson Rhodes innocently disseminated the inaccurate representations made to them by the Respondents on 2nd December 2003, as above. At no stage, either before or after the Audit Committee meeting, did the Respondents make any effort to verify the accuracy of this information. Had they done so, the Audit Committee could have been made aware of the true position. .

56. This was a serious abrogation of their professional responsibilities. The purpose of the Audit Committee is to bring independent oversight to the proposed composition of company accounts. Reviewing decisions on revenue recognition plays an important part in the discharge of that function. The Audit Committee meeting on 5th December 2003 was an opportunity to discuss in full the proposed recognition of the revenue for the Irish Contract and for all parties to have assessed the merits of any such decision. That opportunity was denied to the Audit Committee by the reckless failure of the Respondents to put its members fully in the picture.

***The Executive Counsel's case***

57. In all the circumstances set out above (e.g. the non-binding Heads of Agreement, the outstanding ministerial consent, the failure of the Irish to sign the contract and the corresponding lack of any obligation to pay), the Respondents must have appreciated the plain and obvious risk that there was no legitimate basis for the recognition of any revenue.

[14] The Code was updated in July 2003 in the form of the 'Revised Code'. Technically, this only applied to iSoft's financial statements for the year ending April 2005. The company claimed, however, that it was taken into account and complied with at an earlier point in time (see notes to the Financial Statements for the period ended 30.4.04).

[15] HB1, p.267-271. Note that the only indication ever given to the Board that the Irish Contract may not yet have been concluded, came in paragraph 38 of the Verification Notes issued by iSoft on 12th November 2003 in relation to the Torex merger. This reference, however, was fleeting, appearing as it did in the middle of an otherwise dense and lengthy document. It is denied that this could ever have been sufficient to discharge the Respondents' duties of disclosure.

58. Moreover, given the size of the sums in question, the Respondents must further have appreciated that any such improper recognition would inevitably result in a material overstatement of the company's profits, thereby misleading its creditors, shareholders and potential investors.

59. In those circumstances, it was heavily incumbent upon the Respondents to take all necessary steps to confirm that the recognition was appropriate. As a bare minimum, this would have involved ensuring that all relevant parties (in particular, the auditors, the Audit Committee and the Board) were fully cognisant of the situation as regards the Irish Contract. It also would have involved seeking advice from those bodies as to the appropriate course of action to take.

60. The Respondents made no effort to discharge their responsibilities in this regard despite the fact that they must have been aware of the obvious risk that the auditors, the Audit Committee and the Board had failed to properly understand the position. On the contrary, the Respondents proved themselves entirely indifferent to this state of affairs. In particular, they took no steps to ensure that their erroneous understanding of the status of delivery of the software in Ireland was correct and they made no effort to ensure that these various bodies knew that the Irish Contract remained unsigned. They further failed to take any advice on the many issues which arose.

61. Instead, spurred on by the overwhelming desire to record a profit, and notwithstanding their appreciation of the risk that any recognition would be impermissible, they unreasonably caused or permitted iSoft to recognise the revenue in any event. In doing so, they acted recklessly and with a lack of integrity (Allegation 1).

***The wrongful recognition of cash***

62. Prior to 31st October 2003, iSoft sought to enter into a factoring arrangement with Hanover Asset Finance Limited ("HAF"), such that it could sell any receivables due under the Irish Contract once that document had been signed.

63. HAF itself acted as agent in such transactions for the underlying funder. On this occasion, a Luxembourg bank, Dexia Banque Internationale à Luxembourg SA ("Dexia"), agreed to provide that finance.

64. Preliminary discussions took place between iSoft, HAF and Dexia for the purposes of entering into this arrangement. The Respondents were both involved in this process (particularly Mr Whelan) and at all times familiar with it.

65. By 31st October 2003, however, no meaningful progress had been made in those discussions; neither HAF nor Dexia would fund the deal unless and until the arrangements between iSoft and SEHB had been finalised and the Irish Contract had been signed.

66. As a result, as at 31st October 2003, iSoft had received no cash from HAF, nor was HAF under an obligation to provide any monies. The Respondents nonetheless caused or permitted iSoft to include in its half year accounts £16.9 million representing such a sum. There was no basis for that decision, which was, as before, driven by a reckless desire to improve the financial standing of the company.

***The principles of cash recognition***

67. The definition of cash is governed by Financial Reporting Standard 1 ("FRS1"), which states as follows:

> "[Cash is] cash in hand and any deposits repayable on demand with any qualifying financial institution, less overdrafts from any qualifying institution repayable on demand. Deposits are repayable on demand if they can be withdrawn at any time without notice and without penalty or if a maturity or period of notice of not more than 24 hours or one working day has been agreed."

68. In order to include cash sums in its balance sheet, it is therefore a requirement (whether under this definition of 'cash' or under the definition of an 'asset' under FRS5) that the 'cash' is either held by the company in question, or that it is represented in bank balances owned or controlled by the company. It does not include cash or cash facilities which have been 'earmarked' by a bank to be made available in due course (as to which, see below).

69. In those circumstances, even if (which is not admitted) Dexia had earmarked funds for use in the proposed iSoft/HAF factoring arrangement, iSoft had no legal or beneficial interest in that sum, nor did it have any control over that money. As a

result, it did not meet the definition of 'cash' for the purposes of FRS1, nor did it meet the definition of an 'asset' for the purposes of FRS5.

70. Accordingly, the company had no right to include this sum in its balance sheet as at 31st October 2003. In causing or permitting the cash to be recognised in any event, the Respondents again recklessly failed to confirm matters properly for themselves, or to ensure that the auditors, the Audit Committee or the Board were properly in the picture or party to any discussions or the decision.

***Recognition of the HAF cash –dealings with the auditors, the Audit Committee and the Board***

71. As part of the half year end audit process, and in order to provide the auditors with evidence upon which the cash recognition could be justified, Mr Whelan arranged for HAF to produce a letter dated 27th November 2003 ("the First HAF Letter"), which informed the reader that Dexia had set funds aside for iSoft on 31st October 2003 and that interest was accruing to the benefit of the company in relation to that capital sum[16]. This letter was in due course provided by iSoft to the auditors.

72. In making the representations contained within that letter, neither Mr Whelan nor Mr Whiston made any effort to confirm whether those representations were accurate or not. They had equally made no effort to confirm with the auditors whether, even if the representations were correct, this would have provided sufficient justification for recognising the case (which it would not, see above).

73. Their reckless failure to take advice on this issue was made all the worse by the plain appreciation on their part that the recognition may indeed be impermissible. For example, an email from Mr Whelan to Mr Storey dated 27th November 2003 attached the proposed final draft of the First HAF Letter (iSoft had been involved in the process and it had been though a number of iterations)[17]. In his email, Mr Whelan posed the following question of Mr Storey:

*"Sufficient audit evidence if placed on Hanover Letterhead?"*

The response from Mr Storey read as follows:

[16] HB1, p.316-317
[17] HB1, p.308-310

*"In two minds about this one.*

*I guess the issue I've got is that it doesn't really say that it is our cash at year end, however, if you raise an argument which states we are entitled to receive interest from this then you could argue it is our cash.*

*I think it's the best we will get out of them though so we'll have to go with it and decide what to present to the auditors after.*"[18]

74. This approach manifested itself also in the failure of the Respondents to put the auditors properly in the picture. In the event, the only evidence provided to the auditors in relation to the cash recognition was the First HAF Letter. As must have been obvious to the Respondents, that letter failed to inform the auditors that the Irish Contract remained unsigned, or that no formal agreement had been reached with HAF in relation to the factoring agreement. This was vital information without which the auditors were precluded from making a proper assessment of the situation.

75. Similar observations apply in relation to the Board and the Audit Committee. Despite ample opportunity to do so (see above), no effort was made by the Respondents to ensure that these bodies fully understood the situation.

***The Executive Counsel's case***

76. In all the circumstances set out above (the failure of the Irish to sign the contract, the refusal of HAF to sign a separate contract with iSoft and the ensuing lack of any obligation on the part of HAF to fund the deal), the Respondents must have appreciated that there was a risk that there was no legitimate basis for recognising the cash. Indeed, the exchange between Mr Whelan and Mr Storey set out above is the clearest possible evidence of that appreciation.

77. Given the size of the sums in question, any such improper recognition would render the interim accounts materially inaccurate, thereby misleading the company's creditors, shareholders and potential investors as to the true position, as well as the shareholders in Torex (see above).

[18] HB1, p.311

78. As a result, it was heavily incumbent on the Respondents to take all necessary steps to confirm that the recognition was appropriate. As a bare minimum, this would have involved confirming that all relevant parties (in particular, the auditors, the Audit Committee and the Board) were fully aware of the funding position. It also would have involved taking advice from those various bodies.

79. As set out above, the Respondents failed to take any of those steps. On the contrary, they simply pressed on and caused or permitted iSoft to recognise the cash in any event. In view of the Respondents' awareness of the risk that there was no legitimate basis for recognising the cash, it was unreasonable for them to take such a risk. In doing so, they acted recklessly and with a lack of integrity (Allegation 2).

***The impact of the improper cash and revenue recognition on the interim accounts***

80. Although there was no statutory requirement for iSoft to prepare interim accounts at half year end, it was obliged by the FSA to do so by virtue of its listing on the London Stock Exchange ("LSE").

81. The form and content of interim accounts is governed by the Statement 'Interim Reports', issued by the Accounting Standards Board in 1997. As interim reports are only abbreviated financial statements, there is no requirement for them to show a true and fair view of the group's financial performance and condition. They are intended, however, to enable shareholders and investors to monitor the progress of a business from its last set of annual financial statements, and to assess the impact of recent events on the operating performance of the business.

82. With that in mind, the LSE Listing Rules require that interim accounts must (unless expressly stated otherwise) be compiled on the basis of the accounting policies used in the most recent financial statements, and also that they be presented in such a way as to be comparable with those statements.

83. ISoft's interim accounts for the period ended 31st October 2003 were approved by the Audit Committee on 4th December 2003 and signed off by the Board on 10th December 2003. In approving the accounts in that way, the Board was under a duty

to ensure that they presented an understandable and balanced assessment of the company's position and prospects.[19]

84. It is in that light that the impact of recognising the Irish revenue and cash can be considered. In relation to the revenue, the decision to recognise this in the group interim accounts for the 6 months ending 31st October 2003, meant that the profit and loss account showed an operating profit of £7.4 million, whereas in fact the company had sustained an operating loss of £11.9 million. In relation to the balance sheet, the effect of recognising the HAF cash was that the figure for 'cash and bank balances' was overstated by £16.9 million.

85. The Executive Counsel contends therefore that the information published in iSoft's interim accounts for the 6 months ended 31st October 2003 was materially misstated. This in turn meant that the company's creditors and shareholders, the shareholders in Torex and potential investors in the business were all misled as to the company's financial position.

86. The case advanced by the Executive Counsel is that the reckless manner in which the Respondents had conducted themselves led to this state of affairs.

87. The Respondents were jointly responsible in this regard. Whilst it is correct that Mr Whelan was not a director of the company at this stage, and so not directly responsible in law for the accounts (at least not as principal), this did not absolve him from his ethical responsibilities in this regard.[20] During this period, he held a senior financial position within the company and was well placed to ensure that the interim accounts accurately reflected the company's true position. At the very least, he had a duty to report any misgivings which he had on this issue.

88. He did nothing, however. On the contrary, he caused or permitted the inappropriate recognition of revenue and cash and acted recklessly in doing so as set out above. That was in direct breach of his professional responsibilities.

[19] Section 1 of the Code
[20] Per the relevant provisions of the 2004-5 Guide to Professional Ethics issued by the ICAEW (see post).

**Part 3: The Financial Statements for the year ending 30th April 2004**

***The on-going failure to sign the Irish Contract and recognition of the Irish revenue***

89. As soon as the initial deadline of 31st October 2003 had passed, iSoft set about trying to secure signature of the Irish Contract as soon as possible.

90. At first, it appeared that progress was being made and by 12th November 2003 the main contractual provisions were agreed in principle. At that stage, iSoft signed the Irish Contract and lodged a copy with its lawyers in Ireland for counterpart signature by SEHB and the other Irish Health Boards.

91. This provisional agreement between the parties was not binding, however, as nothing could be signed by SEHB unless and until ministerial assent was given and the requisite funding approved. Despite robust efforts over the next few months by both SEHB and by iSoft, ministerial assent was not forthcoming and so the contract remained unsigned. Indeed, as before, SEHB would not even enter into prior binding Heads of Agreement.

92. The net result was that, as at 30th April 2004, the risk that there was no legitimate basis for recognising the revenue would have been even clearer to the Respondents than had been the case at half year end. Several months had elapsed since the revenue had been recognised in the interim accounts and yet, as the Respondents well understood, there was still no signed contract and no ministerial funding. Equally, had the Respondents bothered to make any enquiries into the situation, they would have known that there had still been no delivery of product to SEHB under the contract in question and no liability on the part of that body to pay.

93. Moreover, it was clear that no progress would be made on finalising the arrangements until well after the end of year accounts had been published. In a weekly sales report emailed to iSoft on 28th May 2004, [redacted] stated as follows:

*"The National HIS Procurement is crawling along and the Health Services Executive (HSE) has advised that they will 'get back' to SEHB during the week commencing 7*

*June 2004. The general consensus around the hospitals is that a 'go ahead' by August is likely."*[21]

94. The Respondents nonetheless permitted iSoft to recognise the Irish revenue in its year end financial statements. This decision was confirmed by way of letter dated 23rd June 2004, signed by Mr Whelan in his capacity as Group Financial Director[22].

95. As before, in allowing this situation to develop, the Respondents recklessly:

i) caused or permitted the auditors to be misled;

ii) failed to put Robson Rhodes, the Board or the Audit Committee properly in the picture; and

iii) failed to take advice from any of those bodies.

***Dealings with the auditors, the Audit Committee and the Board***

96. During the course of audit clearance meetings held on 28th May 2004 (attended by Mr Whelan, [redacted] and Mr Whiston (in part)) and on 4th June 2004 (attended by Mr Whelan and Mr Storey), the auditors were told by iSoft that the software had already been installed at SEHB and that it would shortly be rolled out to the other Health Boards as well.[23] In due course, the Audit Committee and the Board were consequentially misled as well.

97. This information was incorrect – no such software had yet been installed in relation to the Irish Contract. Notwithstanding the passage of time since the half year accounts had been signed off in December 2003, the Respondents had made no effort to check the accuracy of this vital representation. As a result, the auditors were left with an entirely misleading impression as to the true position.

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[21] HB2, p.520-523
[22] HB2, p.572-575
[23] HB2, p.508 (meeting on 28th May 2004) and HB2, p.526 (meeting on 4th June 2004). In relation to the meeting on 28th May 2004, it is not possible to say whether or not Mr Whiston was present when the misleading information was given to the auditors. The case advanced by the Executive Counsel, however, is that even if he wasn't present for that part of the meeting, Mr Whiston had a responsibility to liaise effectively with his senior executives and to ensure the accuracy of significant representations being made to Robson Rhodes for the purposes of the year-end audit. This was particularly so given the close attention which he had paid to the Irish Contract and the ease with which he could have clarified matters with Messrs Whelan and [redacted]. This was a responsibility which he failed to discharge.

98. More importantly, the Respondents again failed to bring to the attention of the auditors the existence of the non-binding Heads of Agreement, the fact that no ministerial approval had yet been given and that no funding was yet forthcoming from the DOHC.

99. In due course, the Audit Committee was also left in the dark when it met on 15th June 2004. As for the Board, the Respondents had every opportunity to ensure that its members were fully apprised of the situation. The Respondents attended Board meetings on 11th May and 9th June 2004 and yet no attempt was made to obtain or provide the essential information upon which proper and informed decisions on revenue recognition could be made.

***The Executive Counsel's case***

100. In all the circumstances, the Respondents must have appreciated the risk that there was no legitimate basis for the recognition of the Irish revenue, yet they unreasonably went ahead and caused or permitted this to happen anyway, without first ensuring that the auditors, the Audit Committee or the Board were fully in the picture, and without taking advice from any of those bodies. For the avoidance of repetition, the Executive Counsel adopts his observations at paragraphs [57] to [61] above in this regard.

101. In conducting themselves in this way, the Respondents acted recklessly and with a lack of integrity (Allegation 3).

***The impact of the revenue recognition on the accounts***

102. The company's financial statements for the year ended 30th April 2004 were signed off under cover of a letter from Mr Whelan dated 23rd June 2004. In doing so, both he and his fellow directors had an obligation under s.227 Companies Act 1985 to ensure that:

i) The balance sheet as at the last day of the financial year gave a true and fair view of the group's state of affairs on that date; and

ii) The profit and loss account similarly gave a true and fair view of the company's profit or loss for the financial year.[24]

103. In addition, the directors were further required under Schedules 4 and 4A of the Companies Act 1985 to do as follows:

i) Select suitable accounting policies and apply them consistently;

ii) Make judgments and estimates that were reasonable and prudent; and

iii) Prepare financial statements in accordance with the accruals concept (i.e. by recognising transactions only in the period to which they related).

104. As a result of the decision to recognise the Irish revenue, iSoft's published consolidated profit and loss account gave the impression that the group had generated a profit on ordinary activities before tax of some £17.6 million whereas, in reality, it had incurred a loss on ordinary activities before tax of some £2.5 million.

105. As a consequence of those shortcomings, the year end financial statements failed to give a true and fair view of the company's position. On the contrary, they were materially misstated so as to be misleading. The case advanced by the Executive Counsel is that the Respondents were reckless as to whether this was so.

## Part 4: The interim accounts for the period ending 31st October 2004

### *The on-going failure to sign the Irish Contract*

106. Between 30th April 2004 and 31st October 2004 (i.e. iSoft's next interim reporting date), [redacted] the Respondents continued to push both for signature and for funding from the DHC, all to no avail. It was now nearly a year since the revenue had been recognised and iSoft were no further forward than they had been in October 2003.

[24] Section 227 Companies Act 1985

107. Indeed, further opposition from the DATHs meant there was even a chance that iSoft's appointment might unravel completely. The risk of this occurrence was compounded by the requirement for the company's appointment to be approved by the Health Services Executive ("the HSE") (successor body to the Health Boards Executive).

108. As the Respondents well knew, delays in obtaining ratification of the Irish Contract from the HSE continued beyond the half year end. It was equally obvious to them that there was no guarantee that the outcome of these deliberations would be that the Irish Contract would be signed.

109. For example, in relation to a meeting of the HSE Board on the evening of 3rd November 2004, when the Irish Contract was on the agenda, [redacted] had undertaken to inform [redacted] of the outcome. It would appear that Mr Whiston was sufficiently anxious about the result to email [redacted] at 5pm to ask when [redacted] might be in touch. On being told by [redacted] that he didn't know, Mr Whiston replied:

*"Just wondering whether or not dare go out between 9 and 10."*[25]

110. In the event, no decision was made by the HSE about the Irish Contract at that meeting. On the contrary, queries were raised about the pricing structure which had previously been agreed in principle between iSoft and SEHB. The matter was adjourned until the next HSE meeting on 9th December 2004.

111. In all the circumstances, there was no legitimate basis for the prior recognition of the Irish revenue in the iSoft accounts, and those entries should have been reversed. Indeed, it is clear from the evidence that the possibility of reversal was on the agenda for the Executive Team meeting held on 5th November 2004. Whether or not it was eventually discussed at that meeting, the decision was at some point taken not to do so.

112. That decision, which was both reckless and plainly wrong, was made in the absence of any attempt to ensure that the auditors, the Audit Committee or the Board were

[25] HB2, p.689-690

fully in the picture, not even to the extent of telling them that a reversal of the revenue had been contemplated.

113. Mr Whelan resigned immediately after the Executive Team meeting on 5th November 2004. Although the half year accounts were signed off after that date, this does not absolve him from joint responsibility for the failure to ensure that the prior revenue recognition was reversed. He was fully informed as to the position, had been party to email correspondence canvassing the possibility of reversal and knew by the time he left iSoft that there was a real and significant risk that the decision would be taken not to reverse the earlier recognition. It was open to him to bring this situation to the attention of the auditors, the Audit Committee, the Board or his professional body but he failed to do so. Instead, he recklessly stood by, thereby permitting the erroneous accounts to be published in due course.

114. Meanwhile, following Mr Whelan's departure and prior to the interim accounts being signed off and published on 14th December 2004, matters did not improve. A meeting was arranged on 9th November 2004 between iSoft representatives and the in-coming CEO of the HSE, [redacted]. In an email sent on 8th November 2004 to Mr Whiston (amongst others), [redacted] highlighted the points he felt should be made at that meeting. These included the following:

- *We are all ready to go and have been for over a year (pre NPfIT)*
- *They are getting a bloody good deal from us*
- *The only hurdle seems to be getting the Health Service Executive (HSE) Board to let it through to the Minister (who is supportive)*
- *Next HSE Board meeting is on 9 December 2004, at which they need to get their act together and action it*
- *If they don't action the HIS contract before 31 December 2004, the whole thing could collapse and there will be blood on the carpet.*[26]

115. It is not known whether or not the meeting took place. In the event, it was academic as [redacted] unexpectedly announced on 15th November 2004 that he was not going to take up his post. The fall-out from this decision, and the inevitable further delay that it would cause in concluding the Irish Contract, were spelled out by

[26] HB2, p.718

[redacted] in his weekly sales report dated 18th November 2004.[27] His prediction proved accurate in that the contract wasn't in the end even discussed at the HSE meeting which took place on 9th December 2004 (see above). Mr Whiston was fully aware of this sequence of events but still allowed the half year accounts to be signed off in any event.

**The Executive Counsel's case**

116. It must have been obvious to the Respondents that there was a risk that the prior recognition of the Irish revenue in the accounts had been inappropriate. Instead of taking steps to remedy that situation, the Respondents unreasonably failed to do anything about it.

117. In do conducting themselves, they acted recklessly and with a lack of integrity (Allegation 4).

***The inappropriate recognition of cash***

118. As at October 2004, there was still no effective funding in place for the Irish contract. Mr Whelan, in the full knowledge of Mr Whiston, therefore engaged in dialogue with HAF about a similar factoring arrangement to that which had been contemplated 12 months earlier. On this occasion it was anticipated that HAF would provide the finance itself (albeit as part of a back to back arrangement with another funder, Lombard Finance plc). As before, however, and in the absence of a signed contract with SEHB, no progress had been made on those discussions by the end of the accounting period.

119. Nonetheless, the decision was made by the Respondents to recognise the cash in iSoft's half year accounts. Mr Whelan, in conjunction with Mr Storey, engaged again with HAF to produce a similar letter ("the Second HAF Letter") to that which had been provided to the auditors the previous year. Two versions of the letter were provided by HAF. The first, dated 5th November 2004, was received by Mr Whelan on the day he left the company.[28] The second, dated 17th November 2004, was received by Mr Whiston.[29]

[27] HB2, p.740-743
[28] HB2, p.700-703
[29] HB2, p.730-733

120. As had been the position 12 months earlier, no effort was made by the Respondents to confirm that the contents of these letters were accurate. Nor did they seek to confirm whether or not this would give rise to permissible recognition of the cash in any event – simply no advice was sought on the issue.

121 As before, the auditors were also not told of the latest problems in Ireland or that the Irish Contract remained unsigned. The Board and the Audit Committee remained similarly under-informed – no effort was made by the Respondents to bring those bodies up to speed.

**The Executive Counsel's Case**

122. The risk that there was no basis for this entry must have been obvious to the Respondents, as must the risk that the auditors had failed to understand the position properly on the basis of the Second HAF Letter. In unreasonably continuing to recognise the sums in any event, the Respondents acted recklessly and with a lack of integrity (Allegation 5).

***Impact of the cash recognition on the accounts***

123. The events set out above led to the sum of £17,077,101.98 being included in the company's consolidated balance sheet at 31st October 2004. It should not have been so included. If it had not been reported as an asset of the group, the cash and bank balance figure would have been reduced by a corresponding amount.

124. These sums were such that the published interim accounts for the period ending 31st October 2004 were materially misstated and misleading.

**Part 5: Signature of the Irish Contract**

125. In the event, the Irish Contract was finally approved by the HSE on 18th February 2005, subject to the receipt of a satisfactory financial due diligence report on iSoft (see below). Right up until that point, however, there continued to be doubt as to whether or not consent from the HSE would ever be forthcoming, thereby further invalidating any previous decision to recognise the revenue from the contract. For

example, in his weekly sales report dated 23rd January 2005, [redacted] stated as follows:

*"HIS will be discussed on 3 February and documentation will be provided then but it is now clear that it will be at the HSE Board meeting in March* ***when the decision to proceed or not*** *will be made."*[30]

[Emphasis added]

126. The notes of the HSE meeting on 3rd February 2005, which were emailed to [redacted] on 7th February 2005, made plain that some members of the Board had significant reservations about concluding the arrangements with iSoft, and that they had asked for a demonstration of the software.[31] It was left that this would be arranged and that iSoft would respond to the queries in writing, which they did. Any suggestion therefore that the Irish Contract was already a "done deal" by this date (let alone by 31st October 2003) is plainly untenable.

127. Even after agreement from the HSE had been secured on 18th February 2005, various potential barriers still stood between iSoft and a signed contract with the Irish. Firstly, there was the issue of the financial due diligence report, which was undertaken on behalf of the HSE by Deloitte.[32] In due course, Deloitte forwarded the final draft of the report to iSoft for confirmation that the financial information provided by the company was accurate. The task of providing that confirmation ultimately fell to Mr Whiston.

128. The purpose of commissioning the report was set out in Appendix 1, which stated as follows:

*"Our Report will be prepared from our work for your confidential use, solely for the purpose of assisting you [i.e. the HSE] with your due diligence enquiries* ***prior to making your decision whether or not to proceed*** *with the contract for services with iSoft plc ("the Transaction").*"[33]

[Emphasis added]

[30] HB3, p.818-821
[31] HB3, p.833-837
[32] HB3, p.898-912
[33] HB3, p.910

129. In those circumstances, it should have been obvious to Mr Whiston that finalisation of the Irish Contract was dependent on a satisfactory outcome to the due diligence enquiries.

130. In any event, it was at the very least incumbent on him to make it plain that the financial statements provided by iSoft to Deloitte already accounted for revenue from the Irish Contract. If that information was not forthcoming, then the picture painted of the company's financial position was entirely misleading.

131. No such attempt was made, however, to clarify the position, despite Deloitte making it clear in correspondence that full and frank answers were required to their enquiries. Instead, Mr Whiston simply signed off on the draft Deloitte report without making any reference to the accounts or to the Irish revenue contained within them. In doing so, the risk that the HSE would misapprehend the true position must have been an obvious one and Mr Whiston's conduct in this regard provides a further indication of the reckless manner in which he conducted himself throughout the relevant period.

132. The report was subsequently presented to the HSE at its Board meeting on 7th April 2005 and the relationship with iSoft thereby ratified.

133. Aside from this issue, there were other late developments which had the potential to derail the process and which equally invalidated any prior decision to recognise the revenue. For example, the DATH's continued to cause problems. In his weekly report for the period leading up to 1st April 2005, [redacted] stated as follows:

*"It is clear that they* [the DATH's] *know what happened at the HSE meeting on 18th February and they….will be opposed to it. It remains to be seen if they can move any more obstacles in front of the HIS procurement in order to stop it. While they are funded by HSE, the Voluntary Hospitals unfortunately don't report to HSE. While HSE appear to be comfortable that the DATH's issue is now dead, my concern is that they have an uncanny way of resurrecting themselves!!"*[34]

134. The final potential barrier to completion arose in the form of a late intervention from the Attorney General of Ireland, who wanted to be satisfied that the correct EU

[34] HB3, p.887-892

procurement procedures had been followed by SEHB before awarding the contract to iSoft. This approval was not viewed as being a formality, either by the HSE or by iSoft. The HSE put in a written document setting out the steps which had been followed in the selection process, whilst [redacted] stated as follows in his weekly sales report dated 24th April 2005:

*"HSE **must*** [his emphasis] *still receive approval of the contract review exercise currently in progress by the Attorney General's office. This is critical and is expected to finish next week."*[35]

135. In the event, all outstanding issues (including that of ministerial consent) were resolved and the Irish Contract was signed on 30th April 2005.[36] The first invoices under the agreement were raised by iSoft on 26th April 2005 so that they could be sent out on the day that the document was executed.[37] Until that point in time, neither the HSE nor its proposed predecessors in title (i.e. the Irish Health Boards) had been liable to pay anything to iSoft.

136. The software which was the subject matter of the licence itself was supplied to the HSE on 26th May 2005.

137. A factoring arrangement was also finally negotiated with HAF which enabled the Irish Contract to be funded. Monies were first received by iSoft under this arrangement on 4th May 2005.

## THE RELEVANT STANDARDS

### *The Relevant Standards of Conduct*

138. The standards of conduct reasonably to be expected of the Respondents included those set out in the Fundamental Principles and Statements contained in the 2004-5 Guide to Professional Ethics issued by the ICAEW ("the Guide").[38] The Executive

[35] HB3, p.950-953
[36] HB3, p.964-972
[37] HB3, p.962-963
[38] This version covers the period with which this case is concerned, containing as it does the Statements in force from August 2001 until post-May 2005.

Counsel will refer to and rely upon the applicable Fundamental Principles and Statements as extracted and appended to this Complaint at Annex A.[39]

139. The Fundamental Principles and Statements contained in the Guide are made in the public interest and they are designed to maintain a high standard of efficiency and professional conduct by all members of the ICAEW. Fundamental Principle 1 states as follows:

> "A member should behave with integrity in all professional and business relationships. Integrity implies not merely honesty but fair dealing and truthfulness. A member's advice and work must be uncorrupted by self-interest and not be influenced by the interests of other parties."

It is the Executive Counsel's case that, through their actions as outlined above, the Respondents have been in breach of this Principle.

***The Respondents' Misconduct***

140. Paragraph 2(1) of the Scheme provides that an Adverse Finding (as referred to in paragraph 2 of this document, above) is a finding by a Disciplinary Tribunal that a Member has committed *"Misconduct"*, which in turn is defined as:

> "an act or omission or series of acts or omissions, by a Member or Member Firm in the course of his or its professional activities (including as a partner, member, director, consultant, agent, or employee in or of any organisation or as an individual) or otherwise, which falls significantly short of the standards reasonably to be expected of a Member or Member Firm or has brought, or is likely to bring, discredit to the Member or Member Firm or to the accountancy profession."

141. The alleged Misconduct in this case is summarised in the short particulars of the allegations which follow.

[39] Namely 1.220 (Guidance on Ethical matters for Members in Business) and 1.220 (Additional Guidance on Ethical Matters for Members in Business) (the latter only in force from 2nd July 2004)).

**Allegation 1 – Failing to act with integrity**

**Between 31st October 2003 and 11th December 2003, the conduct of Timothy Whiston and John Whelan fell significantly short of the standards reasonably to be expected of a Member, in that, contrary to Fundamental Principle 1 and the ICAEW Guide to Professional Ethics, they failed to act with integrity, namely by recklessly causing or permitting iSoft to recognise the Irish revenue in its group interim accounts for the period ended 31st October 2003, when there was no legitimate basis for such recognition.**

**Particulars of Allegation 1**

1) In order to recognise the Irish revenue in its interim group accounts for the period ending 31st October 2003, iSoft needed to be satisfied that the requirements for revenue recognition under its published accounting policy and/or under UK GAAP and/or pursuant to basic accounting principles had been satisfied.

2) As at 31st October 2003, the Irish Contract remained unsigned, ministerial consent was outstanding, the Heads of Agreement were explicitly non-binding, no goods or services had been delivered under the contract and the Irish were under no obligation to pay.

3) In those circumstances, it must have been obvious to the Respondents that there was a risk that there was no legitimate basis for the recognition of the Irish revenue, whether under iSoft's published accounting policy, UK GAAP or basic accounting principles. As a result, before recognising this sum, the Respondents were under a duty to take all necessary steps to confirm that the recognition was appropriate. This included ensuring that the auditors, the Audit Committee and the Board were fully cognisant of the true status of the Irish Contract, and seeking their advice on the matter.

4) The Respondents failed to do any of these things. Instead, they unreasonably pressed on and caused or permitted the recognition of the revenue anyway. In so conducting themselves, they acted recklessly and with a lack of integrity.

5) In support of this allegation, the Executive Counsel relies upon:

i) All of the facts and matters set out in the main body of this document, in particular those cited at paragraphs [47] to [61] above; and

ii) The version in force at the material time of section 1.220 of the Guide ('Guidance on Ethical Matters for Members in Business'), in particular paragraphs 2.0-2.1, 2.4, 2.6, 6.3 and 6.4.

**ALLEGATION 2 – Failing to act with integrity**

**Between 31st October 2003 and 11th December 2003, the conduct of Timothy Whiston and John Whelan fell significantly short of the standards reasonably to be expected of a Member, in that, contrary to Fundamental Principle 1 and the guidance in section 1.220 of the Guide, they failed to act with integrity, namely by recklessly causing or permitting iSoft to recognise £16.9 million of cash in its group interim accounts for the period ended 31st October 2003, when there was no legitimate basis for such recognition.**

**Particulars of Allegation 2**

1) To the knowledge of the Respondents, as at 31st October 2003:

   i) The Irish Contract had not been signed;

   ii) The contract between iSoft and the proposed funder of the Irish Contract, Dexia Bank, had not been signed (either by the Bank, or by its agent, HAF); and

   iii) No cash had been received from Dexia under the terms of the proposed arrangements with iSoft, nor was it under any obligation to provide any such cash.

2) In those circumstances, it must have been obvious to the Respondents that there was a risk that there was no legitimate basis for the recognition of this cash under either UK GAAP or basic accounting principles. As a result, before recognising this sum, they were under a duty to take all necessary steps to confirm that the recognition was appropriate. This included ensuring that the auditors, the Audit Committee and the Board were fully cognisant of the true status of the Dexia funding, and seeking their advice on the matter.

3) The Respondents failed to do any of these things. Instead, they unreasonably pressed on and caused or permitted iSoft to recognise the cash anyway. In so conducting themselves, they acted recklessly and with a lack of integrity.

4) In support of this allegation, the Executive Counsel relies upon:

i) All of the facts and matters set out in the main body of this document, in particular those cited at paragraphs [71] to [79] above; and

ii) The version in force at the material time of section 1.220 of the Guide ('Guidance on Ethical Matters for Members in Business'), in particular paragraphs 2.0-2.1, 2.4, 2.6, 6.3 and 6.4.

**Allegation 3 – Failing to act with integrity**

**Between 30th April 2004 and 24th June 2004, the conduct of Timothy Whiston and John Whelan fell significantly short of the standards reasonably to be expected of a Member, in that, contrary to Fundamental Principle 1 and the ICAEW Guide to Professional Ethics, they failed to act with integrity, namely by recklessly causing or permitting iSoft to recognise the Irish revenue in its financial statements for the period ended 30th April 2004, when there was no legitimate basis for such recognition.**

**Particulars of Allegation 3**

1) In order to recognise the Irish revenue in its financial statements for the period ending 30th April 2004, iSoft needed to be satisfied that the requirements for revenue recognition under its published accounting policy and/or under UK GAAP and/or pursuant to basic accounting principles had been satisfied.

2) As at 30th April 2004, the Irish Contract remained unsigned, ministerial consent was outstanding, the Heads of Agreement were explicitly non-binding, no goods or services had been delivered under the contract and the Irish were under no obligation to pay.

3) In those circumstances, it must have been obvious to the Respondents that there was a risk that there was no legitimate basis for the recognition of the Irish revenue, whether under iSoft's published accounting policy, UK GAAP or basic accounting principles. As a result, before recognising this sum, the Respondents were under a duty to take all necessary steps to confirm that the recognition was appropriate. This included ensuring that the auditors, the Audit Committee and the Board were fully cognisant of the true status of the Irish Contract, and seeking their advice on the matter.

4) The Respondents failed to do any of these things. Instead, they unreasonably pressed on and caused or permitted iSoft to recognise the revenue anyway. In so conducting themselves, they acted recklessly and with a lack of integrity.

5) In support of this allegation, the Executive Counsel relies upon:

i) All of the facts and matters set out in the main body of this document, in particular those cited at paragraphs [89] to [100] above; and

ii) The version in force at the material time of section 1.220 of the Guide ('Guidance on Ethical Matters for Members in Business'), in particular paragraphs 2.0-2.1, 2.4, 2.6, 6.3 and 6.4.

**ALLEGATION 4 – Failing to act with integrity**

**Between 31st October 2004 and 15th December 2004, the conduct of Timothy Whiston and John Whelan fell significantly short of the standards reasonably to be expected of a Member, in that, contrary to Fundamental Principle 1 and the ICAEW Guide to Professional Ethics, they failed to act with integrity, namely by recklessly causing or permitting the continued recognition in the iSoft group interim accounts for the period ended 31st October 2004 of the Irish revenue previously recognised in the iSoft group financial statements for the period ended 30th April 2004, when there had been no legitimate basis for such recognition.**

**Particulars of Allegation 4**

1) In order to have recognised the Irish revenue in its financial statements for the period ended 30th April 2004, iSoft needed to have been satisfied that the requirements for revenue recognition under its published accounting policy and/or under UK GAAP and/or pursuant to basic accounting principles had been satisfied on that date.

2) As at 30th April 2004, the Irish Contract remained unsigned, ministerial consent was outstanding, the Heads of Agreement were explicitly non-binding, no goods or services had been delivered under the contract and the Irish were under no obligation to pay.

3) In those circumstances, it must have been obvious to the Respondents that there was a risk that there had at that date been no legitimate basis for recognition of the Irish revenue, whether under iSoft's published accounting policy, UK GAAP or basic accounting principles. In those circumstances, the Respondents were under a duty to take all necessary steps to confirm that the recognition had been appropriate. This included ensuring that the auditors, the Audit Committee and the Board were fully cognisant of the true status of the Irish Contract, and seeking their advice on the matter.

4) The Respondents did not do any of these things. Instead, they unreasonably caused or permitted the continued recognition of the Irish revenue. In so conducting themselves, they acted recklessly and with a lack of integrity.

5) In support of this allegation, the Executive Counsel relies upon:

i) All of the facts and matters set out in the main body of this document, in particular those cited at paragraphs [106] to [117] above;

ii) The version in force at the material time of section 1.220 of the Guide ('Guidance on Ethical Matters for Members in Business'), in particular paragraphs 2.0-2.1, 2.4, 2.6, 6.3 and 6.4; and

iii) The supplemental version in force from 2nd July 2004 of section 1.220 of the Guide ('Additional Guidance on Ethical Matters'), in particular paragraphs 1.2, 1.3, 1.4, 1.6, 1.7, 4.1-4.9 and 5.1-5.5.

**ALLEGATION 5 – Failing to act with integrity**

**Between 31st October 2004 and 15th December 2004, the conduct of Timothy Whiston and John Whelan fell significantly short of the standards reasonably to be expected of a Member, in that, contrary to Fundamental Principle 1 and the ICAEW Guide to Professional, they failed to act with integrity, namely by recklessly causing or permitting iSoft to recognise £17.08 million of cash in its group interim accounts for the period ended 31st October 2004, when there was no legitimate basis for such recognition.**

**Particulars of Allegation 5**

1) To the knowledge of the Respondents, as at 31st October 2004:

   i) The Irish Contract had not been signed;

   ii) The contract between iSoft and the proposed funder of the Irish Contract, HAF, had not been signed; and

   iii) No cash had been received from HAF under the terms of the proposed arrangements with iSoft, nor was it under any obligation to provide any such cash.

2) In those circumstances, it must have been obvious to the Respondents that there was a risk that there was no legitimate basis for the recognition of this cash under either UK GAAP or basic accounting principles. As a result, before recognising this sum, they were under a duty to take all necessary steps to confirm that the recognition was appropriate. This included ensuring that the auditors, the Audit Committee and the Board were fully cognisant of the true status of the HAF funding, and seeking their advice on the matter.

3) The Respondents failed to do any of these things. Instead, they unreasonably pressed on and caused or permitted iSoft to recognise the cash anyway. In so conducting themselves, they acted recklessly and with a lack of integrity.

4) In support of this allegation, the Executive Counsel relies upon:

i) All of the facts and matters set out in the main body of this document, in particular those cited at paragraphs [118] to [122] above;

ii) The version in force at the material time of section 1.220 of the Guide ('Guidance on Ethical Matters for Members in Business'), in particular paragraphs 2.0-2.1, 2.4, 2.6. 6.3 and 6.4; and

iii) The supplemental version in force from 2nd July 2004 of section 1.220 of the Guide ('Additional Guidance on Ethical Matters'), in particular paragraphs 1.2, 1.3, 1.4, 1.6, 1.7, 4.1-4.9 and 5.1-5.5.

**Signed:**

**GARETH REES QC**
**EXECUTIVE COUNSEL**

**Date:**

## ANNEX A

## THE APPLICABLE FUNDAMENTAL PRINCIPLE AND STATEMENTS

**Extracts from the ICAEW Guide to Professional Ethics 2004-2005**

**1.200**

**Introduction and Fundamental Principles** (Revised with effect from 1 August 2001)

**Fundamental Principle 1 – 'Integrity'**

A *member* should behave with integrity in all professional and business relationships. Integrity implies not merely honesty but fair dealing and truthfulness. A *member*'s advice and work must be uncorrupted by self-interest and no be influenced by the interests or other parties.

**Extracts from Guidance on Ethical Matters for Members in Business** (Revised with effect from 1 August 2001)

**1.220**

**Fundamental Principles**

2.0 ***Members* should behave with integrity in all professional and business relationships. Integrity implies not merely honesty but fair dealing and truthfulness.**

2.1 While employed *members* should observe the terms of their employment, these cannot require them to be implicated in any dishonest transaction. If they are instructed or encouraged to engage in any activity which is unlawful they are entitled and required to decline. For example *members* should not be party to the falsification of any record or knowingly or recklessly supply any information or make any statement which is misleading, false or deceptive in any material particular.

2.2 When *members* become aware that their employers have committed an unlawful act which could compromise them, every effort should be made to

persuade the employer not to perpetrate the unlawful activity and to rectify the matter.

2.3 An employer may also be identified in taking the right decision if it is made clear by the member that it will not be possible to continue as an employee if matters are not righted.

2.4 If a *member* would feel uncomfortable defending an action in open Court or to the Press then it is likely that such a course of action should be avoided on ethical grounds.

2.5 It is not always clear whether an activity is indeed unlawful and how best to deal with the situation. Advice on these matters is given separately in Statement 1.405, *Professional Conduct in relation to Defaults or Unlawful Acts by or on behalf of a Member's Employer.*

2.6 *Members* should take particular care to observe this guidance in the context of corporate finance activities especially when making public statements and commenting on takeover situations. For example, any document whether for private or public use should be prepared in accordance with normal professional standards of integrity and objectivity and with a proper degree of care. *Members* involved in corporate finance advice should refer to Statement 1.203, *Corporate Finance Advice,* paragraphs 1.1 to 1.9.

**General**

6.0 The following paragraphs summarise those sections of Statement 1.200, Introduction and Fundamental Principles not included above.

6.1 *Members* should be guided by the spirit of the Guide and not just the specific terms of the Guide. *Members* are expected in normal circumstances to follow the Guide as part of the ethical standards expected of them as chartered accountants. Failure to follow the Guide does not of itself constitute misconduct but in answer to a complaint *members* may be called upon to justify any departure from the guidance.

6.2 *Members* should act in a manner consistent with the good reputation of the profession. The Institute requires its *members* to refrain from any conduct which might bring discredit to the Institute, especially with regard to their responsibilities towards employers, clients, third parties, other *members* of the accountancy profession, employees and the general public.

**Objectives of the Guide**

6.3 Professional accountants are expected to work to the highest standards of professionalism, to attain the highest standards of performance, to observe the highest standards of conduct and integrity and generally to meet the requirements of the public interest. The aim of this Guide is to assist *members* to achieve these aims.

**The Public Interest**

6.4 A distinguishing mark of a profession is acceptance of its responsibility to the public. The accountancy profession's public consists of clients, providers of credit, governments, employers, employees, investors, the business and financial community, and others who rely on the objectivity and integrity of professional accountants to contribute towards the orderly function of commerce. This reliance imposes a public interest responsibility on the accountancy profession.

**Extracts from Additional Guidance on Ethical Matters for Members in Business** (in force from 2 July 2004)

**1.220**

SECTION 1 **Introduction**

1.1 Members are engaged in an executive or non-executive capacity in such areas as commerce, industry, the public and service sectors (including public sector audit bodies), education, the non for profit sector, regulatory bodies or professional bodies.

1.2 Investors, creditors, employers and other sectors of the business community, as well as governments and the public at large, may all rely on the work of members. Members may be solely or jointly responsible for the preparation and reporting of financial and other information, which both their employing organisations and third parties may rely on. They may also be responsible for providing effective financial management and competent advice on a variety of business-related matters including reviewing internal controls.

1.3 Members may be salaried employees, directors (whether executive or non-executive), owner managers, consultants, partners, volunteers or others engaged in one or more employing organisation. The legal form of the relationship with the organisation in which they are engaged has no bearing on the ethical responsibilities incumbent on members.

1.4 Members have a responsibility to further the legitimate aims of their employing organisation. This statement does not seek to hinder members from properly fulfilling that responsibility, but considers circumstances in which conflicts may arise with their duty to comply with the fundamental principles.

1.6 Members often occupy senior positions within employing organisations. The more senior they become, the greater will be their ability and opportunity to influence events, practices and attitudes. Members in such positions are expected, therefore, to encourage an ethics-based culture in their employing organisations.

1.7 A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. Therefore, the member's responsibility is not exclusively to satisfy the needs of an employer. The term 'public interest' relates to matters of legitimate public concern, not public curiosity. Public concern extends to the concerns of clients, government, financial institutions, employers, employees, investors, the business and financial community and others who rely upon the objectivity and integrity of the accounting profession to support the propriety and orderly functioning of commerce.

## SECTION 4 **Application of framework approach in ethical dilemma resolution**

4.1 Members have a professional obligation to comply with the fundamental principles. There may be times, however, when their responsibilities to an employing organisation and their professional obligations to comply with the fundamental principles are in conflict. Ordinarily, members should support the legitimate and ethical objectives established by their employers and the rules and procedures drawn up in support of those objectives. Nevertheless, where compliance with the fundamental principles is threatened, members must consider their response to the circumstances.

4.2 As a consequence of their responsibilities to their employing organisation, members may find themselves under pressure to act or behave in ways that could directly or indirectly threaten compliance with the fundamental principles. Such pressure may be explicit or implicit; it may come from supervisors, managers, directors or other individuals within the employing organisation. Members may find themselves under pressure to:

- act contrary to law or regulation;
- act contrary to technical or professional standards;
- facilitate unethical or unlawful earnings management strategies;
- lie to, or otherwise intentionally mislead (including misleading by keeping silent) others, in particular:

(i) those acting as auditors to the employing organisation; or

(ii) regulators.

- Issue, or otherwise be associated with, a financial or non-financial report that materially misrepresents the facts, including statements in connection with, for example:
  - (i) the financial statements;
  - (ii) tax compliance;
  - (iii) legal compliance; or
  - (iv) reports required by regulators.

4.3 The significant of threats arising from such pressures, such as intimidation threats, should be evaluated and, if they are other than clearly insignificant, safeguards should be considered and applied as necessary to reduce them to an acceptable level. Safeguards that might mitigate such pressures include:

- obtaining advice where appropriate from within the employing organisation, an independent professional advisor or a relevant professional body;

- the existence of a formal dispute resolution process within the employing organisation;
- seeking legal advice.

4.4 When initiating an ethical dilemma resolution process, members should consider the framework below;

- gather the facts and identify the problem;
- define the fundamental principles involved;
- identify the affected parties;
- identify who should be involved in the conflict resolution process;
- consider courses of action and associated consequences;
- decide on a course of action;
- evaluate your course of action;
- implement the course of action.

4.5 When resolving an ethical dilemma, it may be in the member's best interest to document the substance of the issue and details of any discussions held or decisions taken, concerning that issue.

4.6 Members may find it useful to discuss the ethical conflict issue within the organisation with the following parties:

- immediate superior;
- the next level of management;
- a corporate governance body, for example, the audit committee;
- other departments in the organisation which include, but are not limited to, legal, audit and human resources departments.

4.7 In addition, members may wish to consult the Ethical Advisory Services in the Institute which may be able to provide guidance on ethical issues without breaching confidentiality (www.icaew.co.uk/ethicsadvice). They may also consider seeking legal advice.

4.8 If, after exhausting all relevant possibilities, the matter remains unresolved, members should, where possible, disassociate themselves from the matter. They may also consider whether, in the circumstances, it is appropriate to withdraw from the specific project or in the extreme circumstances resign from the organisation in which they are engaged.

4.9 To assist members to determine an appropriate course of action when faced with a situation which could threaten their compliance with the fundamental principles the following sections (preparing and reporting of information; acing with sufficient expertise; financial information; inducements and disclosing confidential information) give examples of specific areas of activity which could give rise to ethical dilemmas and the action which could be taken in response. This is not a comprehensive list of examples but aims to cover the key areas most likely to be encountered by members.
Illustrative case studies of how the guidance might be applied in example situations is given in the appendix to this guidance.

## SECTION 5 **Preparation and reporting of information**

5.1 Members are often involved in the preparation and reporting of information that may either be made public or used by others inside or outside the employing organisation. Such information may include but is not limited to financial or management information, for example, financial statements, management discussion and analysis, and the management letter of representation provided to the auditors as part of an audit of financial statements. Members should prepare of present such information fairly, honestly and in accordance with relevant professional standards so that the information will be understood in its context. Members should maintain information for which they are responsible in a manner that:

- describes clearly the true nature of business transactions, assets or liabilities;
- classifies and records information in a timely and proper manner, and
- does not materially misrepresent the facts.

5.2 Threats to compliance with the fundamental principles, for example self-interest or intimidation threats to objectivity, competence and performance, may arise where members may be pressurised (either externally or by the possibility of personal gain to allow themselves to be associated with misleading information or to become associated with misleading information through the actions of others.

5.3 Accordingly, members should not be associated with reports, returns, communications or other information where they believe that the information:

- contains a materially false or misleading statement;
- contains statements or information furnished recklessly;
- omits or obscures information required to be included where such omission or obscurity would be misleading.

5.4 The significance of such threats will depend on factors such as the source of the pressure and the degree to which the information is, or may be misleading. The significance of the threats should be evaluated and, if they are other than clearly insignificant, safeguards should be considered and applied as necessary to reduce them to an acceptable level. Such safeguards might include consultation with superiors within the employing organisation, for example, the audit committee of other body responsible for governance, or with a relevant professional body.

5.5 Where it is not possible to reduce the threat to an acceptable level, members should refuse to remain associated with information they consider is or may be misleading. Should they be aware that the issue of misleading information is either significant or persistent, they should consider information appropriate authorities in line with the guidance in Section 9. They may also wish to take legal advice or consider resignation.