FIRST, FOURTH & FIFTH CROSS-CLAIM
AMENDED COMMERCIAL LIST CROSS-CLAIM STATEMENT

COURT DETAILS

Court	Supreme Court
Division	Equity
List	Commercial List
Registry	Sydney
Case number	2017 / 00081927

TITLE OF PROCEEDINGS

Plaintiff	**DSHE Holdings Ltd (ACN 166 237 841) (receivers and managers appointed) (in liquidation)**
First defendant	**Nicholas Abboud**
Number of defendants (if more than two)	8

TITLE OF THIS CROSS-CLAIM

Cross-claimants	**Robert Murray** (First cross-claimant / Fourth defendant) **Lorna Kathleen Raine** (Second cross-claimant / Sixth defendant) **Robert Ishak** (Third cross-claimant / Seventh defendant) **Jamie Clifford Tomlinson** (Fourth cross-claimant / Eighth defendant) **William Paul Renton Wavish** (Seventh cross-claimant / Fifth defendant) **Phillip John Cave** (Eighth cross-claimant / Third defendant)
First cross-defendant	**David Robert White and others trading as Deloitte Touche Tohmatsu (ABN 74 490 121 060)**
Number of defendants (if more than two)	454

FILING DETAILS

Filed for	**Robert Murray, Lorna Kathleen Raine, Robert Ishak, Jamie Clifford Tomlinson**, First to Fourth cross-claimants **William Paul Renton Wavish**, Seventh cross-claimant **Phillip John Cave**, Eighth cross-claimant
	First to Fourth cross-claimants
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Legal representative	Reay McGuinness, Webb Henderson
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	Eighth cross-claimant
Legal representative	Guy Hamilton Foster, Allens
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A. NATURE OF DISPUTE

1. The first, second, third, fourth, seventh and eighth cross-claimants, being Robert Murray (**Murray**), Lorna Kathleen Raine (**Raine**), Robert Ishak (**Ishak**), Jamie Clifford Tomlinson (**Tomlinson**), William Paul Renton Wavish (**Wavish**) and Phillip John Cave (**Cave**) respectively, (together, the **NED Cross-Claimants**), are, or were, the non-executive directors and officers of the plaintiff in the main proceedings, DSHE Holdings Ltd (receivers and managers appointed) (in liquidation) (**DSH**).

2. Unless otherwise indicated, terms defined in the third amended commercial list statement filed by DSH on 19 March 2018 (**TACLS**) have the same meaning in this commercial list cross-claim statement.

3. Among other things, DSH alleges (and the NED Cross-Claimants deny) that:

   (a) from at least July 2014 until 1 December 2015, DSH adopted what is alleged to be the "Rebate Accounting Approach" (see TACLS, paragraph 38-39);

   (b) the Rebate Accounting Approach did not comply with Australian Accounting Standards, in particular AASB 102 Inventories (TACLS, paragraph 40);

   (c) DSH had "Inadequate Inventory Management" (TACLS, paragraph 41);

   (d) in light of (among other things) the Rebate Accounting Approach and the Inadequate Inventory Management, there was no proper or adequate basis for the directors of DSH (**DSH Directors**) to approve the financial statements of DSH for the half year ended 28 December 2014 (**HY15 Financial Report**) or the financial statements of DSH for the financial year ended 28 June 2015 (**FY15 Financial Report**) and form the view that each report:

      (i) gave a true and fair view of the financial position and performance of DSH and the DSE Group;

      (ii) complied with the Corporations Act;

      (iii) complied with Australian Accounting Standards (TACLS, paragraphs 52 and 67).

4. DSH alleges, which is denied, that the NED Cross-Claimants breached their duties owed to DSH to exercise reasonable care and diligence (**Alleged Duties**), including by:

   (a) implementing and maintaining the "Rebate Maximisation Policy" without appropriate systems to prevent "Rebate Driven Buying Practices" developing at all or to a significant degree;

   (b) failing to implement systems that prevented employees of DSH and the DSE Group from engaging in "Rebate Driven Buying Practices";

   (c) adopting and implementing the "Rebate Accounting Approach", including permitting "over and above rebates" to be taken directly into DSH's profit on negotiation;

   (d) failing to implement systems that prevented employees of DSH and the DSE Group from engaging in the "Rebate Uplift Practice";

   (e) failing to implement systems to address "Inadequate Inventory Management" and ensure that:

      (i) adequate internal controls existed to prevent or minimise the purchase of inventory which was not likely to be saleable for an appropriate margin within an appropriate timeframe;

      (ii) regular and comprehensive reporting of inventory levels was received by the NED Cross-Claimants;

      (iii) regular and comprehensive stocktakes occurred;

      (iv) inventory which was obsolete or near end-of-life was promptly written off in whole or in part in DSH's accounts and, in any event, before the half year and full year accounts were prepared;

   (f) in relation only to Cave, Wavish, Murray, Raine and Ishak, participating in the resolution to declare and pay the 2015 Interim Dividend, in circumstances where there was no proper or adequate basis to do so;

   (g) in relation only to Murray, Raine, Ishak and Tomlinson, participating in the resolution to declare and pay the 2015 Final Dividend, in circumstances where there was no proper or adequate basis to do so;

(h) in relation only to Cave, Wavish, Murray, Raine and Ishak, participating in the resolution to approve the HY15 Financial Report in circumstances where there was no proper or adequate basis to do so;

(i) in relation only to Murray, Raine, Ishak and Tomlinson, participating in the resolution to approve the FY15 Financial Report in circumstances where there was no proper or adequate basis to do so;

(j) in relation only to Cave, Wavish, Murray, Raine and Ishak, failing to consider, with reasonable care and diligence or at all, whether the payment of the 2015 Interim Dividend would comply with section 254T of the Corporations Act and, in particular, whether the payment would materially prejudice DSH's ability to pay its creditors;

(k) in relation only to Murray, Raine, Ishak and Tomlinson, failing to consider, with reasonable care and diligence or at all, whether the payment of the 2015 Final Dividend would comply with section 254T of the Corporations Act and, in particular, whether the payment would materially prejudice DSH's ability to pay its creditors,

(**Alleged Breaches**).

5. DSH alleges, which is denied, that the Alleged Breaches caused DSH to suffer loss or damage and that the NED Cross-Claimants are liable to compensate DSH for that loss and damage (**Alleged Loss**). DSH alleges that the Alleged Loss consists of:

   (a) loss or damage that DSH has suffered by reason of it acquiring and accumulating "Bad Stock";

   (b) loss or damage that DSH has suffered by reason of the payment of the 2015 Interim Dividend; and

   (c) loss or damage that DSH has suffered by reason of the payment of the 2015 Final Dividend.

6. The cross-defendants are partners trading as Deloitte Touche Tohmatsu (ABN 74 490 121 060) (**Deloitte**).

7. Deloitte was obliged to develop, and represented that it had developed, a comprehensive understanding of the Dick Smith business over a number of years. For example:

(a) Deloitte audited the financial statements for the period ended 30 June 2013 and stated in its audit strategy document dated January 2014 that *"[o]ver the 30 June 2013 audit period we have developed a comprehensive understanding of Dick Smith ..."*; and

(b) an entity wholly owned by Deloitte was the investigating accountant in relation to the prospectus issued by DSH on 21 November 2013.

8. At all material times, Deloitte:

(a) reviewed the financial statements of DSH for the half year ended 29 December 2013;

(b) audited the financial statements of DSH for the financial year ended 29 June 2014 (**FY14 Financial Report**);

(c) reviewed the HY15 Financial Report; and

(d) audited the FY15 Financial Report.

9. In the course of the audits and reviews referred to in paragraph 8(b) to (d) above, Deloitte:

(a) made representations to the DSH Directors and DSH; and/or

(b) engaged in conduct that had the effect of conveying certain matters to the DSH Directors and DSH.

10. The representations made by Deloitte were misleading or deceptive or likely to mislead or deceive.

11. The conduct engaged in by Deloitte was in breach of its duties to DSH.

12. The NED Cross-Claimants and/or DSH relied on the representations and/or conduct of Deloitte referred to at paragraph 9 above.

13. According to DSH, the documents which are said to record the "Rebate Accounting Approach" include emails to and from Deloitte.

14. As described further below (among other things), Deloitte specifically signed off on DSH's accounting treatment of rebates and the appropriateness of DSH's provisions for inventory.

15. The NED Cross-Claimants deny they are liable to DSH as set out in each of their commercial list responses (as amended) (**Commercial List Responses**). However, if, which is denied, the NED Cross-Claimants are liable to DSH in respect of the Alleged Breaches, the NED Cross-Claimants cross-claim against Deloitte for damages and/or contribution. As will be apparent, the allegations in this cross-claim are made in the alternative to the allegations made in the Commercial List Responses and are only applicable in the event that the NED Cross-Claimants are liable to DSH (which is denied). As such, the allegations contained herein are made solely for the purposes of this cross-claim and without admission. For the avoidance of doubt, where the NED Cross-Claimants make allegations based on allegations made by the plaintiff or evidence served by the plaintiff, or refer to and rely on that evidence, the NED Cross-Claimants do so only for the purpose of this cross-claim and do not thereby admit those allegations or accept the accuracy of that evidence.

16. Among other things, if (which is denied), there was no proper or adequate basis for the DSH Directors to form the views referred to in paragraph 3(d) above, there was no proper or adequate basis for Deloitte to form those views.

B. ISSUES LIKELY TO ARISE

1. Did Deloitte make the alleged representations and/or engage in the alleged conduct?

2. Did Deloitte engage in misleading or deceptive conduct in:

   (a) making the alleged representations concerning the FY14 Financial Report, HY15 Financial Report and/or FY15 Financial Report (together, **DSH Financial Reports**); and/or

   (b) engaging in the alleged conduct?

3. Did the NED Cross-Claimants and/or DSH rely on the work performed by Deloitte and the representations made by Deloitte?

4. Have the NED Cross-Claimants suffered loss or damage by reason of Deloitte's misleading or deceptive conduct?

5. In the event only that the NED Cross-Claimants are found liable to DSH for compensation for any Alleged Breaches:

(a) are the NED Cross-Claimants entitled to damages from Deloitte, such loss or damage being the amount of any liability of each respective NED Cross-Claimants to DSH plus legal costs?

(b) further or alternatively, are the NED Cross-Claimants entitled to contribution from Deloitte in relation to any liability that the NED Cross-Claimants might have to compensate DSH pursuant to section 5 of the *Law Reform (Miscellaneous Provisions) Act 1946* (NSW) (**LRMPA**) or in equity?

C. THE NED CROSS-CLAIMANTS' CONTENTIONS

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Introduction

1. This pleading is filed only on behalf of the first, second, third, fourth, seventh and eighth cross-claimants, being the NED Cross-Claimants.

2. In the event only that the NED Cross-Claimants are found liable to DSH for the loss pleaded in the TACLS (which is denied), then solely for the purpose of this cross-claim and without admission, the NED Cross-Claimants make the allegations set out below. As indicated, these allegations are made without admission. For the avoidance of doubt, where the NED Cross-Claimants make allegations based on allegations made by the plaintiff or evidence served by the plaintiff, or refer to and rely on that evidence, the NED Cross-Claimants do so only for the purpose of this cross-claim and do not thereby admit those allegations or accept the accuracy of the evidence.

I. THE PARTIES

NED Cross-Claimants

3. The first cross-claimant, Murray, was:

   (a) a natural person able to sue or be sued in his own name;

   (b) a director and officer of DSH within the meaning of section 9 of the Corporations Act at all times between on or about 12 August 2014 and 4 January 2016; and

   (c) the chairman of the board of DSH (**Board**) at all times between on or about 28 February 2015 and 4 January 2016.

4. The second cross-claimant, Raine, was:

   (a) a natural person able to sue or be sued in her own name;

   (b) a director and officer of DSH within the meaning of section 9 of the Corporations Act at all times between on or about 25 October 2013 and 4 January 2016; and

   (c) a member of DSH's finance and audit committee (**FAC**) at all times between on or about 25 October 2013 and 4 January 2016.

5. The third cross-claimant, Ishak, was:

   (a) a natural person able to sue or be sued in his own name;

(b) a director and officer of DSH within the meaning of section 9 of the Corporations Act at all times between on or about 25 October 2013 and 4 January 2016; and

(c) a member of the FAC at all times between on or about 25 October 2013 and 4 January 2016.

6. The fourth cross-claimant, Tomlinson, was

(a) a natural person able to sue or be sued in his own name;

(b) a director and officer of DSH within the meaning of section 9 of the Corporations Act at all times between on or about 10 April 2015 and 4 January 2016; and

(c) the chairman and a member of the FAC at all times between on or about 10 April 2015 and 4 January 2016.

7. The seventh cross-claimant, Wavish, was:

(a) a natural person able to sue or be sued in his own name;

(b) a director and officer of DSH within the meaning of section 9 of the Corporations Act at all times between on or about 25 October 2013 and 25 March 2015; and

(c) the chairman and a member of the FAC until on or about 25 March 2015.

8. The eighth cross-claimant, Cave, was:

(a) a natural person able to sue or be sued in his own name;

(b) a director and officer of DSH within the meaning of section 9 of the Corporations Act at all times between on or about 25 October 2013 and 28 February 2015; and

(c) the chairman of the Board between on or about 25 October 2013 and 28 February 2015

DSH

9. DSH:

(a) is duly registered as a corporation under the Corporations Act;

(b) was the parent company of the DSE Group;

(c) carried on business itself and through its trading subsidiaries comprising the DSE Group as a retailer of entertainment, communications, computer and electronics products and related accessories; and

(d) was admitted to the official list of the Australian Securities Exchange (**ASX**) on 4 December 2013 following an initial public offering, after which its shares commenced trading.

10. On 4 January 2016:

(a) DSH was placed into voluntary administration by resolution of its directors;

(b) Joseph Hayes, Jason Preston, William Harris and Matthew Caddy of McGrath Nicol were appointed as voluntary administrators of DSH; and

(c) James Stewart, Jim Sarantinos and Ryan Eagle of Ferrier Hodgson were appointed as, and remain, the receivers and managers of DSH.

11. On 25 July 2016, Joseph Hayes and Jason Preston of McGrath Nicol were appointed as the liquidators of DSH.

DSH Management

12. The first defendant in the main proceedings, Nicholas Abboud (**Abboud**), was:

(a) the chief executive officer of DSH between on or about 25 October 2013 and 4 January 2016; and

(b) a director and officer of DSH within the meaning of section 9 of the Corporations Act at all times between on or about 25 October 2013 and 4 January 2016.

13. The second defendant in the main proceedings, Michael Potts (**Potts**), was:

(a) the finance director and chief financial officer of DSH between on or about 25 October 2013 and 4 January 2016;

(b) a director and officer of DSH within the meaning of section 9 of the Corporations Act at all times between on or about 12 August 2014 and 4 January 2016; and

(c) the company secretary of DSH between on or about 25 October 2013 and 12 August 2014.

Deloitte

14. The cross-defendants, jointly described as "Deloitte":

    (a) are, and at all material times were an Australian partnership;

    (b) are natural persons able to sue and be sued;

    (c) carried on business in Australia as providers of audit, tax, consulting and financial advisory services under the partnership name "Deloitte Touche Tohmatsu" and "Deloitte";

    (d) are and were the supplier of services, including audit, tax and advisory services, for a fee;

    (e) are and were members of one of the four largest professional services networks in accountancy and professional services in Australia;

    (f) at all material times included, among their partners and employees practising in New South Wales, persons who were registered auditors, including David White (**White**); and

    (g) were the auditors of DSH and its controlled entities at all material times including in the period from at least 13 December 2013 up to and including 17 August 2015.

15. At all material times, Deloitte had, and held itself as having, professional expertise and competence in the provision of auditing and accounting services.

16. The first cross-defendant, White:

    (a) is and at all material times was a qualified chartered accountant and a registered company auditor;

    (b) is and at all material times was a partner of Deloitte; and

    (c) was the signing partner for each of the DSH Financial Reports.

17. In addition to White, the employees of Deloitte who were involved in the audits and review of the DSH Financial Reports included in respect of:

    (a) the financial year ended 29 June 2014 (**FY14**), Brad Pollock (**Pollock**), Damien Cork (**Cork**), Andrew Park, Harsh Sood (**Sood**), Lakshitha Perera, Vanessa

Komlos (**Komlos**), Abhimanyu Gupta, Connie Leong, Megan Ormes, Christine Kanjian, Michael Fitzgerald, Sarah Yeung, Lucy Peng, Cheng Chen, Kamlee Coorey (**Coorey**), Tina Zgela, Nathan Caprara, Jane Ma, Christophe Bergeron, Renault Phong, Leo Hua, Debbie Hankey, Safia Schonberger, Prashant Shetty, Tapan Parekh (**Parekh**) and Dave Pearson;

(b) the half year ended 28 December 2014 (**HY15**), Pollock, Cork, Sood, Komlos, Steve Millar (**Millar**) and Arunima Chandel; and

(c) the financial year ended 28 June 2015 (**FY15**), Pollock, Cork, Sood, Komlos, Coorey, Parekh, Millar, Liz Brown, Emilie Stenbeck, Monica Trieu, Dion Bavaresco, Charles Permezel, Janine Forlee, Alex Lee, Jason Tran, Lammert Vos and Raffi Mavlian.

II. DSH'S CONTENTIONS

18. In Part II of these contentions, the NED Cross-Claimants repeat the allegations made by DSH against the DSH Directors in the main proceedings against Deloitte, mutatis mutandis. For the avoidance of doubt, as with the entirety of this cross-claim, these allegations are made without admission, solely for the purpose of this cross-claim, and only in the event that the NED Cross-Claimants are found liable for the Alleged Loss (which is denied).

19. By at least May 2014, DSH had implemented a policy across the DSE Group of maximising the vendor rebates obtained from its suppliers (**Rebate Maximisation Policy**), including "over and above" rebates (**O&A rebates**).

20. At all material times, Deloitte knew that the Rebate Maximisation Policy had been implemented across the DSE Group.

21. The O&A rebates obtained by DSH and the DSE Group comprised a number of different categories including:

(a) rebates from suppliers outside the standard agreements between the suppliers and DSH and other entities in the DSE Group;

(b) rebates from suppliers of private label (Dick Smith own brand) and some branded goods;

(c) rebates, by way of cash payment or credit, in consideration for the extension of contracts with service providers;

(d) contributions by suppliers to the cost of fitout of some DSE Group stores for fittings which would not become the property of DSH or the DSE Group.

22. The Rebate Maximisation Policy continued from at least May 2014 until around December 2015.

23. The Rebate Maximisation Policy led to:

(a) employees of DSH and the DSE Group who were responsible for buying inventory engaging in buying practices which focused on and prioritised maximising rebates, at the expense of focusing on current or likely future customer demand and whether the inventory purchased would be saleable for an appropriate margin within an appropriate timeframe;

(b) employees of DSH and the DSE Group who were otherwise responsible for entering into or extending contracts on behalf of DSH or the DSE Group doing so based on whether rebates would be maximised, at the expense of focusing on whether entering into or extending the contracts was in the best interests of DSH or the DSE Group,

(**Rebate Driven Buying Practices**).

24. The Rebate Driven Buying Practices resulted in:

(a) the DSE Group acquiring and accumulating Bad Stock from at least May 2014 onwards;

(b) DSH directly or indirectly paying for or becoming liable to pay for Bad Stock, which had the consequence that DSH's cash outflows from trading exceeded its cash inflows from trading over time;

(c) the DSE Group acquiring or ordering substantial quantities of Bad Stock shortly before the half year reporting date of 28 December 2014;

(d) the DSE Group acquiring or ordering substantial quantities of Bad Stock shortly before the full year reporting date of 28 June 2015.

25. The Rebate Driven Buying Practices also resulted in DSH taking a $60 million impairment in November 2015 with respect to Bad Stock (see paragraph 74 below).

26. From as early as December 2014, the DSE Group engaged in a practice of uplifting invoices for private label (Dick Smith own brand) and some branded goods (**Rebate Uplift Practice**) which involved:

(a) in some cases, directing or requesting the supplier to cancel previously issued invoices that had been issued without rebates;

(b) directing or requesting the supplier to issue invoices showing a rebate and an equivalent increase in the cost of the goods;

(c) directing, requesting or accepting subsequent invoices from the supplier issued in a similar structure (that is, with a higher price for the goods combined with a rebate);

(d) accounting for the rebate in accordance with paragraph 27 below.

27. From at least July 2014 until 1 December 2015, DSH adopted an accounting approach in relation to rebates through which certain types of rebates, including O&A rebates and rebates obtained through the Rebate Uplift Practice, were recognised in the accounts of DSH:

(a) immediately upon being negotiated with suppliers (that is, potentially prior to the sale of inventory, payment for the inventory and/or any receipt of the rebate);

(b) directly so as to increase gross profit, EBITDA and net profit,

(**Rebate Accounting Approach**).

28. The Rebate Accounting Approach:

(a) did not comply with AASB 102 because it resulted in certain rebates, including O&A rebates, being applied so as to increase profit in circumstances where the rebates should have been applied so as to decrease the costs of purchase of inventory and therefore its carrying value;

(b) facilitated DSH reporting gross profit, EBITDA and net profit of an amount higher than DSH should have reported had it complied with Australian Accounting Standards and in particular AASB 102.

29. At all material times, DSH and the DSE Group did not have in place or implement any adequate procedures, practices or systems to detect, value or (where necessary)

provision for or write-off (in whole or in part) obsolete or near end-of-life inventory, or perform stock takes (**Inadequate Inventory Management**).

30. During the course of the period from May 2014 to around December 2015:

    (a) the Rebate Maximisation Policy and the Rebate Driven Buying Practices continued, and continued to result in the purchase of Bad Stock, in circumstances where there was an underlying decline in "like for like" retail sales;

    (b) the Rebate Accounting Approach continued to be applied;

    (c) at least until June 2015, the number of stocktakes performed by DSH declined;

    (d) declining "like for like" retail sales and increased levels of inventory (including increased levels of Bad Stock) resulted in the cash flow of DSH becoming strained;

    (e) DSH became reliant upon increasing external borrowings in order to fund its cash flow requirements (including using external borrowings to fund the purchase of Bad Stock).

31. By no later than 28 December 2014, DSH should have made, but failed to make, provisions and write-offs with respect to Bad Stock held or likely to be held as at 28 December 2014.

32. As at 12 February 2015, DSH's financial position was such that in the previous six months:

    (a) DSH had from time to time exceeded the limit of its finance facility with Westpac Banking Corporation (**Westpac**) and otherwise breached the facility by failing to comply with required clean downs;

    (b) DSH had, in order to meet its debts as and when they fell due, required extensions of its finance facility with Westpac;

    (c) DSH had, in order to meet its debts as and when they fell due, required extensions of its finance facility with Macquarie Bank Limited (**Macquarie**);

(d) DSH had requested certain suppliers defer delivery of goods ordered before Christmas 2014 to January 2015 or later because DSH had insufficient funds to pay for that inventory;

(e) DSH had placed a volume of orders that resulted in an increased inventory holding by January 2015, a significant cause of which was the Rebate Driven Buying Practices and the desire to maximise the amount of rebates recognised immediately as profit through the Rebate Accounting Approach before the end of the half year on 28 December 2014;

(f) DSH had approached certain suppliers to seek, and from time to time had obtained, extensions of the time for payment of certain invoices;

(g) DSH had delayed paying certain invoices.

33. As at 12 February 2015, the DSE Group had acquired excessive inventory substantially in excess of the projections provided to the DSH Directors in the board papers for the meeting of 25 November 2014.

34. As at 12 February 2015, DSH's cash flow projections were unreliable or there was no proper or adequate basis for them.

35. As at 12 February 2015, in order to pay an interim dividend of 7 cents (and to make other creditor payments in March and April 2015) DSH required an extension to its overdraft limit which had not, at that date, been agreed to by Westpac.

36. As at 12 February 2015 or, alternatively, 16 February 2015, Deloitte knew or ought reasonably to have known all or some of the matters set out in paragraphs 19, 23, 24(a) to (c), 27, 28 and 29 to 35 above and 40 below.

37. On 12 February 2015, the FAC met and resolved to recommend to the DSH Board that:

(a) an interim dividend of 7 cents be paid;

(b) the consolidated accounts of DSH and the DSE Group for the half year ended 28 December 2014 be adopted.

38. On 16 February 2015, a meeting of the DSH Directors was held at which:

(a) Wavish presented a dividend discussion paper and advised that:

(i) an interim dividend of 7 cents was consistent with the 60% to 70% payout ratio adopted by the DSH Board in its resolution of July 2014;

(ii) an appropriate amount for the interim dividend was 7 cents;

(iii) a record date of 12 March 2015 and a payment date of 30 April 2015 would be appropriate taking into account cash flow requirements;

(b) Abboud, Potts, Cave, Murray, Wavish, Raine and Ishak passed a resolution as DSH Directors that DSH pay an interim dividend of 7 cents with a record date of 12 March 2015 and a payment date of 30 April 2015 (**2015 Interim Dividend**);

(c) Abboud, Potts, Cave, Murray, Wavish, Raine and Ishak passed a resolution as DSH Directors that the consolidated accounts of DSH for the half year ended 28 December 2014 be adopted.

39. On 16 February 2015, DSH issued the consolidated accounts of DSH and the DSE Group for the half year ended 28 December 2014 in the form approved by the DSH Directors on 16 February 2015.

40. The HY15 Financial Report:

(a) applied the Rebate Accounting Approach;

(b) failed to account for inventory at its net realisable value, as required by AASB 102;

(c) incorrectly capitalised overhead costs into inventory, contrary to the requirements of AASB 102;

(d) failed to disclose the existence of uncertainties as to DSH's ability to continue as a going concern, contrary to the requirements of AASB 101;

(e) incorrectly recognised deferred tax assets, contrary to the requirements of AASB 112;

(f) failed to impair DSH's property, plant and equipment as required by AASB 136;

(g) failed to recognise onerous lease provisions, as required by AASB 137.

41. In the light of the Rebate Maximisation Policy, the Rebate Accounting Approach, and the matters set out in paragraphs 19, 23, 24(a) to (c), 27, 28, 29 to 35 and 40 above,

there was no proper or adequate basis for Deloitte to provide an unqualified review report in respect of the HY15 Financial Report or form the view that the HY15 Financial Report:

(a) gave a true and fair view of the financial position and performance of DSH and the DSE Group;

(b) complied with the Corporations Act;

(c) complied with Australian Accounting Standards.

42. Not used.

43. On 20 April 2015, a meeting of the DSH Directors was held at which it was agreed that the management of DSH should tender to refinance the debt facilities of DSH and the DSE Group with the goal of securing more favourable margins and covenants and less onerous security arrangements.

44. On 30 April 2015, DSH paid the 2015 Interim Dividend to shareholders in the total amount of $16,555,000 pursuant to the authorisation by the DSH Directors given by passing the resolution set out in paragraph 38(b) above or otherwise.

45. Not used

46. By 30 April 2015, in addition to the matters set out in paragraphs 32 to 35 above, DSH had since 12 February 2015:

(a) exceeded the limit of its finance facility with Westpac on further occasions;

(b) in order to meet its debts as and when they fell due, required further extensions of its finance facility with Westpac;

(c) in order to meet its debts as and when they fell due, required further extensions of its finance facility with Macquarie;

(d) failed to pay certain suppliers as and when it was required to such that at least one supplier (Samsung) had refused to supply DSH until its account was regularised;

(e) approached further suppliers to seek, and from to time had obtained, extensions of the time for payment of certain invoices;

(f) delayed paying certain invoices;

(g) failed to reduce its inventory levels in accordance with its plans and projections;

(h) continued to produce cash flow projections which were unreliable or for which there was no proper or adequate basis.

47. On 19 May 2015, the FAC met and agreed that management would review the obsolescence methodology then used in the half-year accounts to ensure it more accurately reflected the markdown provision required.

48. On 16 June 2015, a meeting of the DSH Directors was held at which approval was given for refinancing with NAB and HSBC to secure more favourable margins at less onerous financial covenants.

49. On 22 June 2015, DSH entered into loan agreements with each of NAB and HSBC.

50. By no later than 28 June 2015, DSH should have made, but failed to make, provisions and write-offs with respect to Bad Stock held or likely to be held as at 28 June 2015.

51. By 17 August 2015, in addition to the matters set out in paragraphs 32 to 35 and 46 above, DSH had since 30 April 2015:

(a) used certain of the funds advanced by or on behalf of NAB and HSBC to repay Westpac, rather than for the purpose of capital expenditure which was the purpose given to HSBC in connection with the advance of the funds;

(b) insufficient cash reserves or available cash inflows from trading to purchase high turnover and attractive inventory;

(c) failed to pay further suppliers as and when it was required;

(d) approached further suppliers to seek; and from time to time had obtained, extensions of the time for payment of certain invoices;

(e) delayed paying certain invoices;

(f) failed to reduce its inventory levels in accordance with its plans and projections;

(g) continued to produce cash flow projections which were unreliable or for which there was no proper or adequate basis.

52. As at 17 August 2015, Deloitte knew or ought reasonably to have known all or some of the matters set out in paragraphs 19, 23, 24(a) to (d), 27, 28, 29 to 35, 46, 49, 50 and 51 above and 55 below.

53. On 17 August 2015, a meeting of the DSH Directors was held at which:

(a) Abboud, Potts, Murray, Tomlinson, Raine and Ishak passed a resolution as DSH Directors, that DSH pay a final dividend of 5 cents with a record date of 30 September 2015 and a payment date of 30 September 2015 (**2015 Final Dividend**);

(b) Abboud, Potts, Murray, Tomlinson, Raine and Ishak passed a resolution as DSH Directors, that the consolidated accounts of DSH for the full year ended 28 June 2015 be adopted.

54. On 17 August 2015, DSH issued the consolidated accounts of DSH for the full year ended 28 June 2015 in the form approved by the DSH Directors on 17 August 2015.

55. The FY15 Financial Report:

(a) applied the Rebate Accounting Approach;

(b) failed to account for inventory at its net realisable value, as required by AASB 102;

(c) incorrectly capitalised overhead costs into inventory, contrary to the requirements of AASB 102;

(d) failed to disclose the existence of uncertainties as to DSH's ability to continue as a going concern, contrary to the requirements of AASB 101;

(e) incorrectly recognised deferred tax assets, contrary to the requirements of AASB 112;

(f) failed to impair DSH's property, plant and equipment as required by AASB 136;

(g) failed to recognise onerous lease provisions, as required by AASB 137.

56. On 17 August 2015, each of Abboud and Potts gave a declaration pursuant to section 295A of the Corporations Act for the year ended 28 June 2015 that:

(a) the financial records of DSH for the financial year had been properly maintained in accordance with section 286 of the Corporations Act;

(b) the FY15 Financial Report complied with Australian Accounting Standards;

(c) the FY15 Financial Report gave a true and fair view of the financial position and performance of DSH.

57. In the light of the Rebate Maximisation Policy, the Rebate Accounting Approach, and the matters set out set out in paragraphs 19, 23, 24(a) to (d), 27, 28, 29 to 35, 46, 49, 50, 51 and 55 above, there was no proper or adequate basis for Deloitte to provide an unqualified audit report in respect of the FY15 Financial Report or form the view that the FY15 Financial Report:

(a) gave a true and fair view of the financial position and performance of DSH and the DSE Group;

(b) complied with the Corporations Act;

(c) complied with Australian Accounting Standards.

58. Not used.

59. On or around 25 September 2015, DSH retained Mike Holtzer and Andy Powell to advise in relation to its inventory issues.

60. On 30 September 2015, DSH paid the 2015 Final Dividend in the total amount of $11,826,000 pursuant to the authorisation by the DSH Directors given by passing the resolution set out in paragraph 53(a) above or otherwise.

61. Not used.

62. By way of circular resolution made on or around 22 October 2015, the DSH Directors resolved that:

(a) DSH request a short-term increase of $20 million in its finance facility;

(b) Potts be authorised to make the necessary arrangements and execute on behalf of DSH any documentation required by the financiers.

63. On or around 26 October 2015, Mike Holtzer and Andy Powell advised DSH (through Potts) and it was, in effect, the fact that:

(a) over a third of the current inventory held by DSH and the DSE Group was Bad Stock;

(b) Bad Stock exceeded $100 million and was increasing rapidly;

(c) it was highly likely that the value for Bad Stock included margin already taken into DSH's accounts as profit from O&A rebates;

(d) $21 million worth of end of life inventory was ordered in the previous three months;

(e) $76 million of total inventory was ordered more than six months ago.

64. On 26 October 2015, a meeting of the DSH Directors was held, at which:

(a) cash flow requirements up to Christmas 2015 were discussed, given the circular resolution made on or around 22 October 2015 referred to in paragraph 62 above;

(b) the likelihood of a cash flow deficit in October 2015 was discussed;

(c) Mark Scott, Director of Operations, Buying and Marketing presented on what he described as approximately $56 million of overstocked inventory;

(d) the Rebate Accounting Approach as it applied to O&A rebates was confirmed with any change to be considered at a future board meeting, following a discussion that any change to it could have an impact on profitability.

65. On 27 October 2015, a meeting of the DSH Directors was held at which:

(a) Abboud and Potts advised that the October 2015 trading shortfall to budget was approximately $5 million net profit after tax;

(b) Abboud and Potts indicated that management's projections for profit for the 2016 financial year were in a range between $33 million and $45 million, with a most likely range of $37 million to $43 million;

(c) Potts indicated that these ranges did not include any clearance of overstocked inventory or the adjustment to the Rebate Accounting Approach as it applied to O&A rebates;

(d) the DSH Directors requested management to prepare a trading update for lodgement with the ASX for consideration by the DSH Directors.

66. On 28 October 2015, a meeting of the DSH Directors was held at which:

(a) Abboud and Potts updated the DSH Directors on actual October 2015 performance, noting that the month's net profit after tax was approximately $5 million below expectations, as a result of lower sales and adverse gross margin;

(b) Abboud noted that November 2015 had commenced trading consistent with October 2015 with a commensurate concern regarding Christmas trading;

(c) the DSH Directors noted the requirement for an increase in DSH's debt facility and requested a detailed inventory analysis be presented at the November 2015 board meeting;

(d) the DSH Directors reviewed and approved the trading update prepared by management for lodgement with the ASX.

67. On 28 October 2015, DSH lodged with the ASX the trading update approved by the DSH Directors on 28 October 2015, which stated that DSH presently anticipated that net profit after tax for the 2016 financial year could be $5 to $8 million below the previous guidance of $45 to $48 million.

68. By 13 November 2015, Mike Holtzer and Andy Powell had identified (and it was, in effect, the fact) that DSH had $152 million of Bad Stock which was 44% of total inventory.

69. On 16 November 2015, HSBC increased the limit of the finance facility on a temporary basis by $20 million at the request of DSH.

70. By 23 November 2015, Andy Powell had:

(a) identified, and validated with Chris Borg, DSH's Head of Merchandising Planning, (and it was, in effect, the fact) that the DSE Group had $189 million of Bad Stock which was 56% of total inventory;

(b) concluded (and it was the fact) that Rebate Driven Buying Practices had driven a lot of the extreme excess inventory and some end of life inventory.

71. On 24 November 2015, a meeting of the DSH Directors was held at which:

(a) Abboud provided the DSH Directors with an update on the trading performance of DSH and the DSE Group in October and November 2015;

(b) the DSH Directors discussed the relationship between excess inventory and O&A rebates and the impact on cash flow and debt levels;

(c) the DSH Directors requested an updated inventory analysis be provided to them as soon as available.

72. On Sunday, 29 November 2015, a meeting of the DSH Directors was held at which:

(a) Potts provided the DSH Directors with an analysis of inventory as at October 2015;

(b) Potts stated that DSH's internal analysis indicated clearing excess inventory and reducing inventory could impact the carrying value of inventory by around $20 million;

(c) Potts advised that the external consultants engaged (Mike Holtzer and Andy Powell) had indicated in their preliminary findings that the carrying value of the inventory could be impacted by up to $60 million.

73. On or around 29 November 2015, DSH booked a non-cash impairment of $60 million before tax with respect to obsolete or unsaleable inventory.

74. On 30 November 2015, DSH lodged with the ASX an announcement stating that:

(a) a review of inventory had been commenced after the DSH annual general meeting on 28 October 2015 and this review, which was being conducted with the assistance of external consultants, remained in progress;

(b) while the review had not been concluded, the DSH Directors had determined that a non-cash impairment of $60 million before tax was required and that a further impairment may be required depending on Christmas trading.

75. On 7 December 2015, a meeting of the DSH Directors was held at which:

(a) the DSH Directors discussed the inventory purchasing model, including how the performance of buyers was measured by reference to rebates and, in particular, O&A rebates;

(b) the DSH Directors requested management develop and implement plans to reduce range and manage inventory to approximately $200 million by June 2016, including potentially implementing changes to the accounting treatment of O&A rebates from 1 December 2015;

(c) the DSH Directors directed management to formally request an extension until February 2016 of the $20 million temporary facility from HSBC;

(d) the DSH Directors discussed DSH's solvency and the DSH Directors concluded that they were sufficiently confident with DSH's cash flow forecast.

76. On 14 December 2015, a meeting of the DSH Directors was held at which Potts updated the DSH Directors on trading in November 2015 and reported a net loss after tax of approximately $0.4 million in November 2015, resulting in a year-to-date net loss after tax of approximately $3.8 million.

77. On 21 December 2015, a meeting of the DSH Directors was held at which:

(a) the DSH Directors discussed the economic sustainability of DSH's prevailing model in circumstances where O&A rebates were at lower levels;

(b) Potts updated the DSH Directors on cash flow performance and advised that current cash flow was below expectations;

(c) the DSH Directors discussed DSH's cash position and concluded that they were comfortable that DSH was solvent.

78. On 22 December 2015, a meeting of the DSH Directors was held at which:

(a) the position of NAB and HSBC was discussed;

(b) the DSH Directors directed that management retain McGrath Nicol to provide independent advice on DSH's solvency and cash flow.

79. On 29 December 2015, a meeting of the DSH Directors was held at which McGrath Nicol presented on its current findings with respect to DSH's solvency and cash flow.

80. On 1, 3 and 4 January 2016, the DSH Directors met on a number of occasions to discuss the solvency of DSH, which culminated in a resolution at a meeting, which commenced at 5pm on 4 January 2016, that DSH be placed in voluntary administration.

FY14 AUDIT

III. FY14 AUDIT OBLIGATIONS

DSH's FY14 Statutory Obligations

81. For the financial year ended 29 June 2014, DSH:

(a) was required, by section 286(1)(b) of the Corporations Act, to keep written financial records that would enable true and fair financial statements to be prepared and audited;

(b) was required, by section 292(1)(a) of the Corporations Act, to prepare a financial report;

(c) was required, by sections 295(1) and (2) of the Corporations Act and by AASB 127, to include in the financial report:

(i) the financial statements for the year in relation to DSH and the Consolidated Entity presented as those of a single economic entity, that were required by the accounting standards (if DSH elected to present them as a Consolidated financial statement);

(ii) the notes to those financial statements; and

(iii) the directors' declaration about the statements and notes;

(d) was required, by section 295(4) of the Corporations Act, to include, inter alia, a declaration by the DSH Directors whether, in the directors' opinion:

(i) there were reasonable grounds to believe that DSH and the Consolidated Entity would be able to pay their debts as and when they became due and payable; and

(ii) the financial statements and notes were in accordance with the Corporations Act, including s 296 (compliance with accounting standards) and s 297 (true and fair view); and

(e) prepared the FY14 Financial Report, in compliance with the obligations pleaded in paragraphs (b) to (d) above, which included the financial statements in relation to DSH and the Consolidated Entity, the notes to those statements and the directors' declaration.

82. Pursuant to section 301 of the Corporations Act, DSH was required to have the FY14 Financial Report audited in accordance with Division 3 of the Corporations Act and to obtain an auditor's report.

83. The FY14 Financial Report was required to:

(a) comply with the accounting standards pursuant to section 296 of the Corporations Act; and

(b) give a true and fair view of the financial position and performance of DSH and of the consolidated entity pursuant to section 297 of the Corporations Act.

84. The accounting standards with which the FY14 Financial Report needed to comply were the Australian Accounting Standards issued by the Australian Accounting Standards Board (**AASB**) (as in force at the relevant time), including:

(a) AASB's *"Framework for the Preparation and Presentation of Financial Statements*" (**Framework**);

(b) AASB Standard 101 "*Presentation of Financial Statements"* (**AASB 101**);

(c) AASB Standard 102 "*Inventories*" (**AASB 102**);

(d) AASB Standard 112 "*Income Taxes*" (**AASB 112**);

(e) AASB Standard 116 "*Property, Plant and Equipment*" (**AASB 116**);

(f) AASB Standard 118 "*Revenue*" (**AASB 118**);

(g) AASB Standard 127 "*Separate Financial Statements*" (**AASB 127**);

(h) AASB Standard 136 "*Impairment of Assets*" (**AASB 136**); and

(i) AASB Standard 137 "*Provision, Contingent Liabilities and Contingent Assets*" (**AASB 137**),

(**Full Year Accounting Standards**).

Deloitte's FY14 Statutory Auditing Obligations

85. As auditor of DSH for the financial year ended 29 June 2014, Deloitte was required:

(a) pursuant to section 307 and section 308 of the Corporations Act to form an opinion as to whether:

(i) the FY14 Financial Report was in accordance with the Corporations Act, including whether it complied with the accounting standards, and whether it gave a true and fair view of the financial position and performance of DSH and of the consolidated entity; and

(ii) it had been given all information, explanation and assistance necessary for the conduct of the audit; and

(b) pursuant to section 307A of the Corporations Act to conduct the audit of the FY14 Financial Report in accordance with applicable auditing standards (as that term is defined in section 9 of the Corporations Act);

(c) to report in accordance with section 308 of the Corporations Act;

(d) through White, to report to the Australian Securities and Investments Commission (**ASIC**) in accordance with section 311 of the Corporations Act; and

(e) to, and had the powers set out in sections 310, 323A and 323C of the Corporations Act to, obtain information,

(**FY14 Statutory Auditing Obligations**).

86. The auditing standards with which Deloitte needed to comply included:

(a) Auditing Standard ASA 200 "*Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Accounting Standards*" (**ASA 200**);

(b) Auditing Standard ASA 230 "*Audit Documentation*" (**ASA 230**);

(c) Auditing Standard ASA 240 "*The Auditors Responsibilities Relating to Fraud in an Audit Report*" (**ASA 240**);

(d) Auditing Standard ASA 260 "*Communication with Those Charged with Governance*" (**ASA 260**);

(e) Auditing Standard ASA 265 "*Communicating Deficiencies in Internal Control with those Charged with Governance and Management*" (**ASA 265**);

(f) Auditing Standard ASA 300 "*Planning an Audit of a Financial Report*" (**ASA 300**);

(g) Auditing Standard ASA 315 "*Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*" (**ASA 315**);

(h) Auditing Standard ASA 330 "*The Auditor's Responses to Assessed Risks*" (**ASA 330**);

(i) Auditing Standard ASA 500 "*Audit Evidence*" (**ASA 500**);

(j) Auditing Standard ASA 501 "*Audit Evidence – Specific Considerations for Inventory and Segment Information*" (**ASA 501**);

(k) Auditing Standard ASA 520 "*Analytical Procedures*" (**ASA 520**);

(l) Auditing Standard ASA 530 "*Audit Sampling*" (**ASA 530**);

(m) Auditing Standard ASA 540 "*Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*" (**ASA 540**);

(n) Auditing Standard ASA 570 "*Going Concern*" (**ASA 570**);

(o) Auditing Standard ASA 580 "*Written Representations*" (**ASA 580**);

(p) Auditing Standard ASA 600 "*Special Considerations – Audits of a Group Financial Report (Including the Work of Component Auditors)*" (**ASA 600**);

(q) Auditing Standard ASA 700 "*Forming an Opinion and Reporting on a Financial Report*" (**ASA 700**);

(r) Auditing Standard ASA 701 "*Modifications to the Auditor's Report*" (**ASA 701**),

as in force, at the relevant time (together the **Full Year Auditing Standards**).

FY14 Deloitte Retainer

87. On or about 13 December 2013, DSH retained Deloitte to, inter alia, perform the audit, as required by section 301 of the Corporations Act, of the FY14 Financial Report (**FY14 Audit**) (**FY14 Deloitte Retainer**).

88. It was a term of the FY14 Deloitte Retainer that Deloitte would report whether in its opinion the FY14 Financial Report was in accordance with the Corporations Act including:

(a) giving a true and fair view of the consolidated entity's financial position as at 29 June 2014 and of its performance for the period ended on that date; and

(b) complying with Australian Accounting Standards and the *Corporations Regulations 2001* (Cth) (**Corporations Regulations**).

89. It was a term of the FY14 Deloitte Retainer that Deloitte would provide its services pursuant to the FY14 Deloitte Retainer with the degree of skill, care and diligence expected of a professional providing services of the same kind.

90. Further, or in the alternative to paragraph 89 above, it was a term of the FY14 Deloitte Retainer that Deloitte would use reasonable skill and care in providing services pursuant to the FY14 Deloitte Retainer.

91. It was a term of the FY14 Deloitte Retainer that Deloitte would perform its audit of the FY14 Financial Report in accordance with Australian Auditing Standards.

92. It was a term of the FY14 Deloitte Retainer that Deloitte would evaluate the appropriateness of DSH's accounting policies.

93. It was a term of the FY14 Deloitte Retainer that Deloitte would evaluate the reasonableness of accounting estimates made by DSH's management.

94. It was a term of the FY14 Deloitte Retainer that Deloitte would communicate to the chairman of the FAC in writing concerning any significant deficiencies in internal control relevant to the audit of the FY14 Financial Report that Deloitte identified during the audit.

IV. DELOITTE'S CONDUCT OF THE FY14 AUDIT

FY14 Audit Strategy

95. In or about January 2014, Deloitte provided DSH with its audit strategy in respect of the financial period ending 29 June 2014 (**FY14 Audit Strategy**).

96. In the FY14 Audit Strategy, Deloitte stated, inter alia, that:

(a) over the 30 June 2013 audit period Deloitte had developed a comprehensive understanding of DSH and an appreciation of the changing environment, both internal and external, that DSH had faced and was currently facing;

(b) through Deloitte's detailed knowledge of DSH's business, discussions with management and review of monthly CFO reports and board minutes, Deloitte had focussed its audit strategy on specific areas which were detailed, along with its proposed responses, in Section 3 of the FY14 Audit Strategy Presentation;

(c) Deloitte's "*Quality Imperatives*" included, inter alia:

(i) exercising professional scepticism – audit procedures must clearly reflect acting as an evaluator with an attitude of professional scepticism not just an explainer;

(ii) becoming experts in internal controls – demonstrating expertise in understanding process flows and testing internal controls where applicable;

(iii) becoming experts in risk assessments and audit responses – Deloitte's deep understanding of Dick Smith and its environment results in improved application of the risk assessment procedures.

97. Deloitte stated that its audit would be focused on the key audit and business risks facing the DSE Group, and was designed to ensure:

(a) overall integrity of DSH's financial statements, as well as any subsidiary financial statements that were required to be issued;

(b) appropriate consideration was given to focus areas identified;

(c) appropriate accounting for significant transactions undertaken by DSH;

(d) consistent application of DSH's accounting policies;

(e) all audit and accounting issues were resolved on a timely basis in consultation with management and that its audit provided "no surprises" to either management or the Board;

(f) both management and the Board received early warning of proposed changes to accounting standards and their potential impact on DSH; and

(g) compliance with ASX and ASIC regulatory requirements.

98. Deloitte stated that in respect of the financial period ending 29 June 2014, the key audit and business risks facing the DSE Group included:

(a) AASB 102 costing;

(b) rebates and vendor allowances;

(c) the stock obsolescence provision;

(d) other inventory provisions.

99. Deloitte stated that its audit procedures would be focused on the key audit and business risks identified at paragraph 98 above.

FY14 AASB 102 costing audit procedures

100. In respect of AASB 102 costing, Deloitte stated that its audit procedures would include:

(a) reviewing the assumptions made in estimating the overhead allocations which are applied to stock on hand;

(b) assessing these assumptions in the context of the changing business model and conditions of the DSE Group to ensure that they remain relevant to and appropriate for the business; and

(c) reviewing the methodology for the allocation of rebates prepared by management and perform procedures to assess the reasonableness of the rebate amounts applied.

FY14 rebate audit procedures

101. In respect of rebates and vendor allowances, Deloitte stated that:

(a) rebates form a significant part of Dick Smith's business. The timeliness and accuracy of capturing and recording rebates may have a significant impact on the company's results; and

(b) its audit procedures would include:

(i) confirming the key controls associated with the completeness and validity of the recording of rebate revenues;

(ii) performing substantive testing on a sample of rebates recorded in the year;

(iii) assessing the provision for any disputed claims which are expected to be granted by the vendors.

FY14 inventory provision audit procedures

102. In respect of the stock obsolescence provision, Deloitte stated that its audit procedures would include:

(a) reviewing the inventory costing and provisioning methodologies adopted as required under AASB 102;

(b) reviewing management's evolving provision methodologies and provide guidance as to the appropriateness of the methodology for both pre- and post-acquisition inventory balances;

(c) analysing reports developed by management to track actual selling prices for stock sold during the period and the allocation of 'scan' provision utilisation rates; and

(d) reviewing management's allocation of 1.0% of purchases to ensure that the appropriate amount had been taken to profit or loss relating to inventory purchases.

FY14 other inventory provisions audit procedures

103. In respect of other inventory provisions, Deloitte stated that its audit procedures would include:

(a) assessing each inventory provision, subject to materiality, to determine the appropriateness of any provisions recognised under AASB 102;

(b) analysing the level of stock written off as a result of stocktakes throughout the year to determine the reasonableness of the shrinkage provision;

(c) analysing consumable stock to determine the appropriate provisions raised on these items.

Internal control and system procedure reporting

104. Deloitte stated that it would provide an Audit Committee Report which would report "*findings from performance of internal control and system procedures*".

Performance of the FY14 Audit

105. For the purpose of performing the FY14 Statutory Auditing Obligations and its obligations pursuant to the FY14 Deloitte Retainer, Deloitte performed the FY14 Audit in about May to August 2014.

106. For the purposes of completing the FY14 Audit, Deloitte:

(a) attended the premises at which books of DSH were held;

(b) attended inventory counts and stocktakes;

(c) required officers and employees of DSH to provide Deloitte with and obtained:

(i) access to the books of DSH and the consolidated entity; and

(ii) information, explanation and assistance to enable Deloitte to form opinions about the books of DSH and the consolidated entity;

(d) had access to and reviewed board papers (**Board Papers**) and board minutes (**Board Minutes**) of DSH;

(e) had access to and reviewed the books and other documents of DSH including in relation to inventory and rebates;

(f) understood and appreciated the need to consider the reliability of representations made by the executive management team of DSH and to corroborate those representations by reviewing supporting evidence; and

(g) had access to standard tests and guidance relevant to the accounting treatment of inventory and rebates.

Discussions between Deloitte and DSH in relation to the accounting treatment of O&A rebates

107. In order for Deloitte to provide its view on the accounting treatment of O&A rebates, Deloitte requested, and DSH provided to Deloitte, information about the manner in

which O&A rebates were, and were to be, recognised and treated in the accounts of DSH.

108. On or around 23 May 2014, Cork had a discussion with Potts about a change in treatment of O&A rebates.

109. As at 26 May 2014, Deloitte understood DSH's treatment of O&A rebates to be as follows:

(a) at HY14, O&A rebates were entered into the cost of doing business (**CODB**) line in the profit and loss, resulting in a net marketing income;

(b) while O&A rebates were sometimes negotiated at the same time as inventory purchases, they were generally for advertising and promotion support rather than a volume or price protection rebate;

(c) O&A rebates were previously recognised immediately when agreed by the vendor through the month end accrual/claim process;

(d) DSH's proposed change was to continue to recognise the rebates immediately, however, shift the rebate received from CODB to within cost of sales (**COS**), having the impact of increasing gross margin but also increasing CODB.

110. On 26 May 2014, Deloitte advised DSH that:

(a) generally, where a rebate was negotiated as part of a purchase of inventory, and the purchase was conditional on the rebate being provided, then the rebate should be taken up into the cost of inventory and recognised in the profit and loss only when the inventory was sold (through COS);

(b) if there was no condition and the two negotiations were separate, then the rebate may be recognised immediately but should be entered through CODB rather than COS;

(c) ordinarily, it would be inconsistent to recognise the rebate immediately and through COS;

(d) given the potential for a significant impact to the gross margin and/or profit, Deloitte required some commentary/justification in the treatment which Deloitte could then corroborate with the buying team and perform some testing around;

(e) it appeared that DSH's focus had shifted to a "conditional purchase" model which would indicate deferral in inventory.

111. On 6 June 2014, Potts provided Deloitte with a position paper entitled "*Position Paper – Vendor Rebates – Profit/Loss and Balance Sheet Recognition*" dated 28 May 2014 and prepared by DSH's financial controller and finance manager, Nigel Mills (**Mills**) (**O&A Position Paper**).

112. In relation to O&A rebates, the O&A Position Paper stated that whilst the majority of O&A rebates are described as "Marketing", they were ad hoc in nature and were usually not supported by formal agreements. If these rebates related specifically to marketing support in the form of paying for additional or preferential space, it was generally applied against the marketing cost in CODB. However, if the rebate related to additional support to clear product, or assisted in promoting a product via discount, then it would be applied to the gross profit line to offset the loss in margin.

113. On 6 June 2014, Potts provided Deloitte with a paper entitled "*Vendor Rebates – O&A*" in relation to the movement of $17.6 million in O&A rebates from CODB to gross margin which stated:

(a) DSH received a large amount of support from suppliers in the form of O&A rebates that are negotiated on an ad hoc basis;

(b) these O&A rebates had generally been treated as an offset to marketing expenses in CODB;

(c) these rebates were often described as marketing support, but also related to additional vendor support to clear inventory or offer price protection on discounts or promotions;

(d) if the O&A rebates did relate to support to clear or promote inventory, then they should be applied to the gross margin line rather than the CODB line;

(e) in the first half of FY14, DSH moved approximately $1 million from CODB to gross margin to more accurately reflect the treatment of O&A rebates;

(f) in the second half of FY14, there had been a more concerted effort to increase the level of O&A support received from vendors and all of the O&A rebates collected at this point had been allocated to the marketing expense line as an offset;

(g) a large amount of price protection support in the form of O&A rebates ($17.6 million) had been incorrectly allocated to marketing expense distorting gross margin and O&A rebates; and

(h) a reallocation of $17.6 million was required to normalise both of these lines for the second half of FY14.

114. On 10 June 2014, Deloitte stated to DSH that:

(a) the concept as described by DSH in the documents referred to in paragraphs 111 to 113 above made sense;

(b) Deloitte's main concern was whether any of the rebates should be deferred in inventory;

(c) these types of rebates were essentially extra product-based rebates and theoretically should be deferred into inventory and only recognised when the product was sold;

(d) Deloitte could test this by selecting samples of claims in the last two months of the year and examining the support to determine whether there should be any deferral, although the documentation may not be that specific.

115. Between 10 June 2014 and 9 July 2014, Deloitte agreed to the transfer of O&A rebates from CODB to gross profit.

FY14 FAC Report

116. On or about 6 August 2014, Deloitte reported to the FAC (inter alia) that:

General

(a) (based on the work it had done to date) nothing had come to its attention that caused it to believe that the financial information as presented in the FY14 Financial Report was materially misstated;

(b) there had been significant improvement in the accounting records and financial reporting processes over the last 12 months. Rebates was an area for further improvement, which management was in the process of addressing;

(c) it had not identified any significant deficiencies in internal controls relating to the prevention and detection of fraud and error which would impact on its ability to provide its opinion on the FY14 Financial Report;

Inventory provision

(d) during FY14 management had reviewed its methodology for calculating its inventory provision in light of the continued evolution of the business operating model. As at 29 June 2014, a process was undertaken to assess the inventory obsolescence provision based on:

(i) inventory status;

(ii) inventory ageing;

(iii) sell through rates and months cover;

(iv) negative margins at current selling prices; and

(v) current promotions or other adjustments;

(e) this process also included investigation of major product lines with the buying team to understand the expected future sell through and potential future write-downs;

(f) the new methodology would be adopted in FY15;

(g) the new methodology for calculating the inventory obsolescence and shrinkage provisions took into account the improved quality and ageing of inventory;

(h) Deloitte had audited the assumptions underlying both methodologies and concurred that the new approach was more appropriate as at 29 June 2014 and with the new methodology generally;

(i) inventory balances had increased from FY13 as a result of additional stores open at 29 June 2014 and increased buying activity at the conclusion of FY14. The obsolescence provisions had decreased due to the improved quality and ageing of inventory;

Inventory costing

(j) in accordance with AASB 102, the value of inventory should include the cost of purchase inclusive of costs incurred in bringing the inventory to its required location and condition net of purchase rebates. In calculating AASB 102 costs, management had included warehouse costs and the costs of the buying team;

(k) it had audited the calculations and estimates made by management and concurred with the inventory costing adjustments recognised at 29 June 2014;

Rebates

(l) vendor receivables remained a key element of DSH's strategy for growth in gross margin and overall profitability;

(m) management had undertaken a program of maximising the vendor rebates obtained, either through price protection, advertising subsidies or O&A rebates. Where these rebates relate to stock purchases held in inventory at the end of the year or promotions in FY15, the rebate income should be deferred into the future period. As at 6 August 2014, Deloitte was still completing its audit procedures in respect of the O&A rebates and would provide a further update at the meeting of the FAC (**FAC Meeting**) on 12 August 2014;

(n) the procedures that Deloitte had undertaken in relation to the accounting treatment of rebates in the FY14 Financial Report included:

   (i) discussing the rebates with key members of DSH's management;

   (ii) analysing the various types of rebates recognised;

   (iii) performing detailed testing of a sample of rebates recognised throughout the year, with a focus on the rebates accrued as at 29 June 2014; and

   (iv) assessing whether any of these rebates represented amounts which should be deferred and recognised in profit or loss in the next financial year;

(o) it concurred with management's revised treatment of O&A rebates within COS rather than as a recovery of marketing and sales expenses;

(p) the reclassification did not have a material impact on the comparatives reported;

(q) it had recommended that management perform a review at each reporting date to identify any O&A rebates which related to ongoing promotions or volume discounts and these should be recognised as deferred income until the promotional period is completed or the stock is sold;

Asset impairment testing

(r) in accordance with AASB 136, tangible assets such as property, plant and equipment held by DSH were assessed for indicators of impairment at least annually;

(s) management had performed an assessment of impairment indicators at 29 June 2014 based on a simplified value in use model, and identified a number of stores which exhibited indicators of impairment. As a result of this analysis, further detailed analysis was performed by management and an impairment provision of $0.7 million recorded;

(t) it had performed an analysis of the model, identified a number of areas where the assumptions and methodologies were incorrect, and re-worked the model with corrected assumptions. It had also applied sensitivities to determine if the impairment recorded by management was correct; and

(u) based on the additional work performed on the model, Deloitte was satisfied that the impairment recorded by management was appropriate. However, Deloitte had provided management with a number of recommendations to further improve the impairment model to ensure it complied with Australian Accounting Standards and reflected more accurately the projected cash flows of the CGUs.

FAC Meeting on 12 August 2014

117. White and Cork attended the FAC Meeting on 12 August 2014 (**FY14 FAC Meeting**).

118. At the FY14 FAC Meeting on 12 August 2014, Deloitte stated to the FAC that:

(a) Deloitte's audit of the FY14 Financial Report was substantially complete. Subject to the adoption of the accounts by the DSH Directors, review of any subsequent events and receipt of the signed management representation letter, Deloitte anticipated issuing an unqualified audit report;

(b) there had been an improvement in the financial reporting process compared to the year ended 30 June 2013. Of particular note was the improvement in the quality of reconciliations, accounting records and financial reporting processes. There still remained a number of areas that could still be improved such as rebates and statutory reporting which have been communicated to management;

(c) included in the cost of inventory were capitalised rebates and supply chain costs which had been recognised in the total cost of inventory under AASB 102. Management had further refined the methodology for calculating the inventory obsolescence and shrinkage provisions which takes into account the improved quality and ageing of inventory, and Deloitte concurred with this methodology. The new calculation resulted in a provision $1.5 million lower than under the old methodology, but it had not been adopted for the FY14 Financial Report. Deloitte had audited the assumptions underlying both methodologies and concurred that the new approach was more appropriate as at 29 June 2014, and had therefore included a $1.5 million adjustment in the unadjusted differences summary. Deloitte understood that the new methodology would be implemented for the 2015 financial year;

(d) management had undertaken a program of maximising the vendor rebates obtained, either through price protection, advertising subsidies or "over and above rebates". Where these rebates relate to stock purchases held in inventory at the year-end or promotions in the 2015 financial year, the rebate income should be deferred into the future period. A small element of rebates collected during the 2014 financial year related to 2015 financial year resulting in a $1.1 million extrapolated variance that was noted in the unadjusted differences summary;

(e) the DSE Group's fixed assets had been assessed for indicators of impairment and an impairment provision of $0.7 million had been recorded, which related to the property, plant and equipment of five stores. Deloitte had audited the assumptions underlying the impairment assessment and concurred with the impairment provision recorded.

Board Meeting on 18 August 2014

119. White attended the Board meeting held on 18 August 2014, by telephone (**FY14 Board Meeting**).

120. At the FY14 Board Meeting, Deloitte confirmed that it had received the representation letter from Abboud and Potts, declared the auditors' independence and gave clearance on the accounts.

121. At the FY14 Board Meeting, the DSH Directors adopted the FY14 Financial Report and authorised DSH's company secretary to release the approved documents to the ASX, subject to Potts and Abboud doing a final review of the accounts prior to the release.

FY14 Audit Report

122. On 18 August 2014, Deloitte issued its independent audit report in respect of the FY14 Financial Report (**FY14 Audit Report**).

123. In the FY14 Audit Report, Deloitte stated that:

(a) Deloitte had audited the FY14 Financial Report;

(b) Deloitte had conducted its audit in accordance with Australian Auditing Standards;

(c) the Australian Auditing Standards required, inter alia, Deloitte to plan and perform the audit to obtain reasonable assurance whether the FY14 Financial Report was free from material misstatement;

(d) in Deloitte's opinion:

(i) the FY14 Financial Report was in accordance with the Corporations Act, including:

(A) giving a true and fair view of the consolidated entity's financial position as at 29 June 2014 and of its performance for the year ended that date;

(B) complying with Australian Accounting Standards and the Corporations Regulations 2001; and

(ii) the consolidated financial statements also complied with International Financial Reporting Standards as disclosed in Note 2.

FY14 Financial Report

124. On 19 August 2014, DSH issued the consolidated accounts of the DSE Group for the full year ended 29 June 2014 which included the FY14 Financial Report audited by Deloitte.

125. The consolidated statement of profit or loss and other comprehensive income in the FY14 Financial Report (**FY14 P&L**) in respect of the DSE Group, recorded inter alia:

(a) total revenue of $1,227.604 million;

(b) total COS of $919.602 million;

(c) gross profit of $308.002 million;

(d) marketing and sales costs of $130.544 million;

(e) net profit (after tax) of $19.826 million.

126. The consolidated statement of financial position in the FY14 Financial Report (**FY14 Balance Sheet**) in respect of the DSE Group, recorded inter alia:

(a) trade and other receivables of $46.88 million;

(b) inventories of $253.814 million.

127. The segment information in Note 4 of the FY14 Financial Report recorded in respect of Australia:

(a) revenue from sale of goods of $1,048.583 million;

(b) COS of $785.406 million;

(c) net profit for the period of $32.253 million.

(d) unallocated net loss of $15.592 million.

FY14 Inventories

128. In the FY14 FAC Report, DSH recorded inventory of $253.8 million in respect of the consolidated DSE Group which was the net of:

(a) gross inventory of $278.1 million as an asset; less

(b) AASB 102 costs net of rebates of $13.4 million; less

(c) a total provision of $11 million, comprising:

(i) provision for obsolescence of $8.7 million; and

(ii) provision for shrinkage of $2.3 million.

129. DSH was obliged by AASB 102 [9] to record stock in the FY14 Financial Report at the lower of cost and net realisable value (**NRV**).

130. In the year to 29 June 2014, the provision for inventory obsolescence recorded in DSH's general ledger (**General Ledger**) involved the application to various categories of stock of a provision based upon a set percentage (**Old Methodology**), as follows:

Status	Percentage Applied to Category of Stock
Active	2%
End of Life	2%
No Reorder	20%
Discontinued	20%
Quit Stock	50%
Non PLU (i.e. spare parts)	100%

131. As at 29 June 2014, DSH's management had designed a refined methodology for calculating inventory obsolescence and shrinkage provisions (**Revised Obsolescence Methodology**), which purported to take into account the improved quality and ageing of inventory.

FY14 Rebates

O&A rebates recognised as assets in the FY14 Balance Sheet

132. In accordance with AASB 101 and the Framework:

(a) a rebate that has not been received by the DSH could not be accounted for as a receivable (i.e. as an asset of DSH) unless it met the definition of an asset and was properly regarded as a resource controlled by DSH as a result of past events and from which future economic benefits are expected to flow to the entity;

(b) rebates were required to be accounted for in accordance with their underlying substance and economic reality and not merely in accordance with their economic form or label.

133. The trade and other receivables recorded in the FY14 Balance Sheet included receivables from suppliers in relation to rebates as assets in the amount of $26.126 million as follows in respect of Australia:

(a) $10.186 million (40%) in relation to business volume rebates; and

(b) $15.94 million (60%) in respect of O&A rebate income from DSH's inventory and other suppliers which was unclaimed by DSH as at 29 June 2014.

134. The rebates referred to in paragraph 133(a) above were recorded in Account 1237 "*Receivable vendor rebates – business volume rebates*" (**Account 1237**).

135. For rebates recorded in Account 1237, a credit was recognised in the "*Inventories*" line of the FY14 Balance Sheet.

136. The rebates referred to in paragraph 133(b) above were recorded in Account 1392 "*Receivables – Rebate Deals*" (**Account 1392**).

137. Account 1392 was a new account utilised by DSH to record O&A rebates during FY14.

138. For rebates recorded in Account 1392, on entering the receivable into Account 1392 a credit was recognised immediately in the FY14 P&L in marketing costs.

O&A rebates recognised in the FY14 P&L

139. DSH credited O&A rebate income of $49.972 million (**FY14 O&A Rebates**) in respect of Australia in the FY14 Financial Report.

140. In recognising and accounting for the FY14 O&A Rebates, DSH was obliged to comply with Australian Accounting Standards.

141. In accordance with AASB 102, FY14 O&A Rebates relating to inventory could not be recognised immediately in the FY14 P&L until the inventory to which it related had been sold.

142. In accordance with the Framework, FY14 O&A Rebates relating to promotional support could not be recognised immediately in the FY14 P&L until the promotional activity to which it related had been completed.

143. Of the $49.972 million FY14 O&A Rebates recognised in the FY14 P&L in respect of Australia:

(a) $21.662 million was recorded in COS; and

(b) $28.310 million was recorded in CODB.

144. The FY14 O&A Rebates which were recorded in COS were recorded as a credit in Account 3324 "*Purchase Rebates Allocated*" (**Account 3324**).

145. Account 3324 was a COS account with a credit balance reflected in the COS line in DSH's FY14 P&L.

146. Account 3324 was a new account utilised by DSH to record FY14 O&A Rebates immediately in the FY14 P&L.

147. The FY14 O&A Rebates which were recorded in CODB in respect of Australia were recorded as follows:

(a) $21.069 million was recorded in Account 4232 "*O&A Rebate Collect*" (**Account 4232**);

(b) $1.683 million was recorded in Account 4219 "*Private Label Adv Rebate - 5%*" (**Account 4219**);

(c) $2.690 million was recorded in Account 4296 "*O&A Dick Live rebate*" (**Account 4296**); and

(d) $2.619 million was recorded in Account 4297 "*O&A All Stars rebate*" (**Account 4297**).

148. Account 4232 was a General Ledger account utilised by DSH to record FY14 O&A Rebates immediately in the FY14 P&L.

149. Account 4232 recognised (inter alia) the credit side of those unclaimed FY14 O&A Rebates recorded in Account 1392.

150. Account 4232 was classified in CODB, reducing the FY14 marketing costs recorded in the FY14 P&L.

Transfer from CODB to COS

151. FY14 was the inaugural year in which the proposed reclassification of O&A rebates from CODB to COS was implemented.

152. DSH's classification of rebates, and any reclassification from CODB to COS, had the potential to significantly impact DSH's gross margin, because any amount reclassified would result in an increase in the recorded gross profit.

V. FY14 RISKS OF HARM

FY14 risks relating to rebates

153. In respect of FY14, there was a risk that:

(a) rebate amounts had been recognised inappropriately, including where they did not meet the accounting definition of an asset or where rebate income should be deferred from the FY14 P&L to the consolidated statement of profit or loss and other comprehensive income in the FY15 Financial Report (**FY15 P&L**);

(b) rebates had not been accounted for in accordance with the requirements of the Australian Accounting Standards, including the Framework, AASB 101 and AASB 102;

(c) claims had been raised or recognised which were not approved rebates;

(d) DSH's internal controls in relation to rebates were inadequate;

(e) the Rebate Maximisation Policy had led to the Rebate Driven Buying Practices which had resulted in the consequences alleged in paragraphs 24 and 25 above;

(f) as a result of one or more of the matters referred to in this paragraph:

(i) the FY14 Financial Report:

(A) would not be free from material misstatement;

(B) further, or in the alternative, would not comply with the Corporations Act, including that it would not:

(1) give a true and fair view of the financial position and performance of DSH and the DSE Group;

(2) comply with Australian Accounting Standards and the Corporations Regulations 2001;

(ii) further, or in the alternative, DSH and/or the NED Cross-Claimants would suffer economic loss.

154. Deloitte knew, or ought to have known, of the risks alleged in paragraph 153 above.

155. The risks alleged in paragraph 153 above were not insignificant.

Recognition of O&A rebates as receivables

156. O&A rebates were rebates that were outside vendor trading agreements.

157. The O&A rebates recorded in Account 1392 were unclaimed O&A rebates.

158. In respect of FY14, there was a risk that:

(a) the transactions recorded in Account 1392:

(i) did not meet the accounting definition of an asset;

(ii) should not have been recognised as an asset in the FY14 Balance Sheet;

(iii) would not be accounted for in accordance with the requirements of the Australian Accounting Standards, including the Framework and AASB 101;

(b) as a result of one or more of the matters referred to in this paragraph:

(i) the FY14 Financial Report:

(A) would not be free from material misstatement;.

(B) further, or in the alternative, would not comply with the Corporations Act, including that it would not:

(1) give a true and fair view of the financial position and performance of DSH and the DSE Group;

(2) comply with Australian Accounting Standards and the Corporations Regulations 2001;

(ii) further, or in the alternative, DSH and/or the NED Cross-Claimants would suffer economic loss.

159. Deloitte knew, or ought to have known, of the risks alleged in paragraph 158 above.

160. The risks alleged in paragraph 158 above were not insignificant.

Rebate treatment risks

161. In respect of FY14, there was a risk that:

(a) rebates, including O&A rebates, had been applied so as to increase profit in circumstances where the rebates should have been applied so as to decrease the costs of purchase of inventory and therefore its carrying value;

(b) DSH had failed to correctly defer the profit impact of rebates until the inventory to which they related was sold;

(c) where it was appropriate to apply a rebate so as to increase profit, that DSH had incorrectly classified rebates as part of COS rather than CODB, or would incorrectly reclassify rebates from CODB to COS;

(d) further or alternatively, DSH had failed to defer some O&A rebates from FY14 to FY15 including where they related to promotional support and the promotional activity to which they related had not been completed;

(e) as a result of one or more of the matters referred to in this paragraph:

(i) the FY14 Financial Report:

(A) would not be free from material misstatement;

(B) further, or in the alternative, would not comply with the Corporations Act, including that it would not:

(1) give a true and fair view of the financial position and performance of DSH and the DSE Group;

(2) comply with Australian Accounting Standards and the Corporations Regulations 2001;

(ii) further, or in the alternative, DSH and/or the NED Cross-Claimants would suffer economic loss.

162. Deloitte knew, or ought to have known, of the risks alleged in paragraph 161 above.

163. The risks alleged in paragraph 161 above were not insignificant.

FY14 risks relating to COS

164. In respect of FY14, there was a risk that:

(a) COS had been misstated due to:

(i) transactions being included in COS that had not occurred;

(ii) amounts being included in COS relating to fictitious or unauthorised transactions; or

(iii) COS transactions had not been recognised in the correct period;

(b) as a result of one or more of the matters referred to in this paragraph:

(i) the FY14 Financial Report:

(A) would not be free from material misstatement;

(B) further, or in the alternative, would not comply with the Corporations Act, including that it would not:

(1) give a true and fair view of the financial position and performance of DSH and the DSE Group;

(2) comply with Australian Accounting Standards and the Corporations Regulations 2001;

(ii) further, or in the alternative, DSH and/or the NED Cross-Claimants would suffer economic loss.

165. Deloitte knew, or ought to have known, of the risks alleged in paragraph 164 above.

166. The risks alleged in paragraph 164 above were not insignificant.

FY14 risks relating to inventory

167. DSH operated in a market in which there was an ongoing risk of obsolete inventory.

168. In respect of FY14, there was a risk that:

(a) inventory obsolescence existed but had not been recorded against inventory;

(b) inventory had been misstated due to cost price changes not being accurately recorded in DSH's computer system "AS400" (**AS400**) and not appropriately approved;

(c) DSH had Inadequate Inventory Management;

(d) inventory had not been correctly valued (adjustments and related COS adjustments not being correctly recorded or recorded at all) due to the lower of NRV or cost not being applied;

(e) DSH had acquired Bad Stock against which provision needed to be made;

(f) the Rebate Maximisation Policy had led to the Rebate Driven Buying Practices which had resulted in the consequences alleged in paragraphs 24 and 25 above;

(g) DSH had incorrectly capitalised overhead costs into inventory, contrary to AASB 102;

(h) as a result of one or more of the matters referred to in this paragraph:

(i) the FY14 Financial Report:

(A) would not be free from material misstatement;

(B) further, or in the alternative, would not comply with the Corporations Act, including that it would not:

(1) give a true and fair view of the financial position and performance of DSH and the DSE Group;

(2) comply with Australian Accounting Standards and the Corporations Regulations 2001;

(ii) further, or in the alternative, DSH and/or the NED Cross-Claimants would suffer economic loss.

169. Deloitte knew, or ought to have known, of the risks alleged in paragraph 168 above.

170. The risks alleged in paragraph 168 above were not insignificant.

FY14 risks relating to journal entries

171. In respect of FY14, there was a risk that:

(a) journal entries had been made without appropriate support or otherwise inappropriately;

(b) journal entries had been overridden by management;

(c) there had been fraud at the assertion level;

(d) as a result of one or more of the matters referred to in this paragraph:

(i) the FY14 Financial Report:

(A) would not be free from material misstatement;

(B) further, or in the alternative, would not comply with the Corporations Act, including that it would not:

(1) give a true and fair view of the financial position and performance of DSH and the DSE Group;

(2) comply with Australian Accounting Standards and the Corporations Regulations 2001;

(ii) further, or in the alternative, DSH and/or the NED Cross-Claimants would suffer economic loss.

172. Deloitte knew, or ought to have known, of the risks alleged in paragraph 171 above.

173. The risks alleged in paragraph 171 above were not insignificant.

VI. FY14 AUDIT DEFICIENCIES

FY14 recognition of unclaimed FY14 O&A Rebates as assets

174. Paragraphs 153 to 155 and 156 to 160 above are repeated.

175. Deloitte's testing of Account 1392 for the purpose of the FY14 Audit:

(a) initially involved a sample size of 15 but, due to errors, the sample size was increased to 55; and

(b) ultimately involved testing of 55 transactions, totaling $8.037 million (50%) of the balance of Account 1392 of $15.94 million in respect of Australia.

176. For the purpose of conducting its testing of rebates recorded in Account 1392 during the FY14 Audit, Deloitte:

(a) relied upon the assertions contained in emails from the vendors to DSH buyers as supporting DSH's accounting treatment, provided that the email cited as support for the transaction:

(i) mentioned an amount that was consistent with the amount being recognised;

(ii) used words such as "*marketing support*", "*product training support*", "*promotional support*", "*catalogue support*", "*promotional activity*" or some other variant, which was consistent with the accounting treatment; and

(iii) mentioned a date or period occurring prior to 29 June 2014; and

(b) in doing so, assumed that assertions in the said emails reflected the substance of the transaction,

(**FY14 Rebate Asset Evidence**).

177. In accordance with ASA 200 [17], Deloitte was required to obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and thereby enable Deloitte to draw reasonable conclusions on which to base its opinion.

178. In accordance with ASA 500 [7], Deloitte was required to consider the relevance and reliability of the information to be used as audit evidence.

179. In accordance with ASA 500 [9], when using information provided by DSH, Deloitte was required to evaluate whether the information was sufficiently reliable for Deloitte's purposes.

180. Paragraph 132 above is repeated.

181. The entries in Account 1392 should only have been recognised as receivables when a valid invoice or debit note was raised by DSH.

182. Because it did not constitute valid invoices or debit notes raised by DSH, the FY14 Rebate Asset Evidence was insufficient audit evidence to justify the recognition of the entries in Account 1392 as receivables.

183. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 200 or ASA 500.

184. A reasonable auditor acting in accordance with the applicable Auditing Standards and with the degree of skill, care and diligence of a professional person providing professional services of the same kind (**Reasonable Auditor**), in the position of Deloitte, would not have recognised the unclaimed O&A rebates in Account 1392 (or the FY14 Balance Sheet) as assets until DSH had raised a valid invoice or debit note in respect of that income.

185. Deloitte did not conduct the FY14 Audit in accordance with paragraph 184 above.

186. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

187. Had Deloitte conducted the FY14 Audit in accordance with paragraph 184 above, it would have:

(a) not recognised the O&A rebates in Account 1392 as a receivable in the FY14 Balance Sheet;

(b) advised the FAC that DSH's current assets and total assets should be $15.94 million less than reported;

(c) advised the FAC that DSH's gross profit and net profit after tax should be $15.94 million less than reported;

(d) not provided an unqualified opinion in relation to the FY14 Financial Report unless the O&A rebates in Account 1392 were removed from the FY14 Balance Sheet and the FY14 P&L;

(e) advised the FAC in writing that:

(i) the entries in Account 1392 should only have been recognised as receivables when a valid invoice or debit note was raised by DSH;

(ii) DSH had been recognising the entries in Account 1392 in the absence of a valid invoice or debit note raised by DSH; and

(iii) it was necessary for DSH to implement new controls to ensure that the entries in Account 1392 were only recognised as receivables when a valid invoice or debit note had been raised by DSH.

188. Further, a Reasonable Auditor in the position of Deloitte would have included as part of its design and implementation procedures and tested as part of the HY15 Review that DSH had implemented new controls in accordance with the advice referred to above.

FY14 inadequate testing of Account 1392

189. Paragraphs 153 to 163 above are repeated.

190. In accordance with ASA 315 [25], Deloitte was required to identify and assess the risks of material misstatement at the financial report level and the assertion level for classes of transactions, account balances and disclosures to provide a basis for designing and performing further audit procedures.

191. By reason of the matters referred to in paragraphs 101(a), 107 to 115, 134 to 152 and 189 above, in accordance with ASA 315 [25], Account 1392 was at risk of material misstatement.

192. A Reasonable Auditor in the position of Deloitte would have tested the credit side of transactions selected from Account 1392 to:

(a) determine in which account the credit had been recorded, namely CODB Account 4232 or COS Account 3324 or some other account (whether a balance sheet or profit and loss account);

(b) conclude whether there was justification for crediting the rebate in the respective account; and

(c) obtain reasonable assurance about whether DSH's treatment of O&A rebates complied with AASB 102.

193. Deloitte did not take the steps referred to in paragraph 192 above.

194. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

195. Had Deloitte taken the steps referred to in paragraph 192 above, it would have:

(a) assessed the economic substance of the rebates recorded in Account 1392 and whether they related to inventory or "marketing support";

(b) assessed whether rebates relating to inventory could be recognised immediately in the FY14 P&L or needed to be deferred until the inventory to which it related had been sold;

(c) assessed whether rebates relating to promotional support could be recognised immediately in the FY14 P&L or needed to be deferred until the promotional activity to which it related had been completed;

(d) determined, based on those assessments, that O&A rebates were being applied by DSH so as to increase profit in circumstances where the rebates should have been applied so as to decrease the costs of purchase of inventory and therefore its carrying value;

(e) not recognised O&A rebates in DSH's profit and loss account but instead would have recognised them as a reduction in the cost of the purchase of inventory;

(f) not provided an unqualified opinion in relation to the FY14 Financial Report unless O&A rebates improperly credited to the profit and loss account were instead recognised as a reduction in the cost of the purchase of inventory;

(g) advised the FAC in writing that:

(i) DSH had been applying O&A rebates so as to increase profit in circumstances where the rebates should have been applied so as to decrease the costs of purchase of inventory and therefore its carrying value;

(ii) this accounting treatment was not in accordance with AASB 102;

(iii) it was necessary for DSH to adopt a new accounting treatment for O&A rebates that complied with Australian Accounting Standards.

FY14 inadequate testing of Account 4232

196. Paragraphs 153 to 155 and 161 to 163 above are repeated.

197. Paragraph 190 is repeated.

198. By reason of the matters referred to in paragraphs 101(a), 107 to 115, 134 to 152 and 189 to 195 above, in accordance with ASA 315 [25], Account 4232 was at risk of material misstatement.

199. To reduce the risks referred to in paragraph 196 above, Deloitte should have tested the O&A rebate transactions recorded in Account 4232 to:

(a) obtain reasonable assurance that crediting the rebate in that account was appropriate; and

(b) obtain reasonable assurance whether DSH's treatment of O&A rebates complied with AASB 102.

200. Deloitte's testing of Account 4232 consisted of 6 samples which:

(a) represented $255,817, being 1.3% of the total account balance of $19.125 million;

(b) were all dated prior to 21 January 2014, and so no transactions were selected or tested for the period February 2014 to June 2014;

(c) related to only three vendors; and

(d) were all subject to a vendor trading agreement,

(**FY14 4232 Sample**).

201. The FY14 4232 Sample was not based on large value items in accordance with ASA 500.

202. The FY14 4232 Sample was not based on random selection, systematic selection or haphazard selection in accordance with ASA 530.

203. Further, contrary to ASA 530 [A12], the FY14 4232 Sample was not a representative sample because of the matters alleged in paragraph 200 above.

204. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 500 or ASA 530 or ASA 315.

205. Further, or in the alternative, the NED Cross-Claimants repeat paragraphs 177 to 179 above and say that, in testing the FY14 4232 Sample, Deloitte:

(a) relied upon the assertions contained in emails from vendors to DSH buyers as sufficient audit evidence supporting DSH's accounting treatment, provided that the email cited as support for the transaction:

(i) mentioned an amount that was consistent with the amount that was recognised;

(ii) used words such as "*marketing support*", "*product training support*", "*promotional support*", "*catalogue support*", "*promotional activity*" or some other variant, which was consistent with the accounting treatment; and

(iii) mentioned a date or period occurring prior to 29 June 2014; and

(b) in doing so, assumed that assertions in the said emails reflected the substance of the transaction,

(**FY14 4232 Evidence**).

206. The FY14 4232 Evidence was not sufficient audit evidence, because:

(a) the emails and other support provided to Deloitte lacked adequate descriptions of the rebates, terms and conditions applicable to the rebates, and did not describe the substance of the rebate;

(b) the wording in the emails from vendors (including "*marketing support*" or "*product training support*") was insufficient to assess the substance of the transaction; and

(c) Deloitte was aware, or ought to have been aware, that the economic substance of the rebates recorded in Account 4232 was that that they related to inventory and that their description as "marketing support" did not properly reflect their economic substance.

207. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 200 or ASA 500.

208. A Reasonable Auditor in the position of Deloitte would have:

(a) tested Account 4232 using large value items or haphazard selection;

(b) ensured that the sample selected was representative of the population being tested including testing transactions in respect of different vendors and for the entire period including February 2014 to June 2014.

209. Deloitte did not take the steps in paragraph 208 above.

210. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

211. Further, or in the alternative, a Reasonable Auditor in the position of Deloitte would have:

(a) not regarded the FY14 4232 Evidence as sufficient audit evidence by which to obtain reasonable assurance that:

(i) crediting the O&A rebates in Account 4232 was appropriate; or

(ii) DSH's treatment of O&A rebates complied with AASB 102;

(b) not recognised the O&A rebates in Account 4232 unless it obtained sufficient audit evidence to obtain reasonable assurance about the matters referred to in sub-paragraph (a) above;

(c) not provided an unqualified opinion in relation to the FY14 Financial Report unless it had obtained sufficient audit evidence in respect of the O&A rebates in Account 4232 or the FY14 accounts were restated to account properly for that income.

212. Deloitte did not take the steps in paragraph 211 above.

213. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

FY14 inadequate testing of COS

214. Paragraphs 164 to 166 above are repeated.

215. In accordance with ASA 315 [25], Deloitte was required to identify and assess the risks of material misstatement at the financial report level and the assertion level for classes of transactions, account balances and disclosures to provide a basis for designing and performing further audit procedures.

216. By reason of the matters referred to in paragraphs 143 to 152 and 214 above, in accordance with ASA 315 [25]:

(a) accounts comprising COS; and

(b) transactions reclassifying rebates from CODB to COS,

were at risk of material misstatement.

217. As part of its conduct of the FY14 Audit, Deloitte determined that it would conduct testing of "*other items posted to COGS which do not form part of the standard cost of goods sold*".

218. The total balance identified by Deloitte of the "*other items posted to COGS which do not form part of the standard cost of goods sold*" in respect of Australia was $29.412 million.

219. Deloitte's testing of accounts comprising COS:

(a) included testing of "*other items posted to COS which do not form part of the standard cost of goods sold*", and in that regard:

(i) purported to comprise testing of a sample of 12 transactions, but did not in fact do so (sample 5 was omitted);

(ii) comprised testing of a sample of 11 transactions, from a total population of $29.412 million, as follows:

(A) 5 samples from Account 3317 "*Freight Express – DC Store*" which had a total balance of $6.096 million;

(B) 4 samples from Account 3290 "*Warehouse Purchase Rebate*" which had a total balance of ($4.494 million); and

(C) 2 samples from Account 3431 "*Private Label Stock write off*" which had a total balance $2.045 million; and

(b) resulted in a conclusion described as "*No issued noted with testing*".

220. Account 3324:

(a) was used to record rebates reclassified from CODB from COS;

(b) was the largest account within COS constituting "*other items posted to COS which do not form part of the standard cost of goods sold*";

(c) comprised a balance of $21.662 million, being 73% of the total of $29.412 million of "*other items posted to COS which do not form part of the standard cost of goods sold*" being the population tested by Deloitte.

221. Deloitte did not conduct any testing on Account 3324.

222. In the premises, in breach of Auditing Standards, Deloitte failed in the conduct of the FY14 Audit to:

(a) select samples for testing that included samples from Account 3324, so as to provide a reasonable basis to draw conclusions about the entire population from which the sample was selected, as required by ASA 530; and

(b) determine means of selecting items for testing that were effective in meeting the purpose of the audit procedure, as required by ASA 500.

223. A Reasonable Auditor in the position of Deloitte, having determined to test "*other items posted to COS which do not form part of the standard cost of goods sold*", would have included testing of Account 3324, including because:

(a) Account 3324 was the largest account balance included in, and constituted 73% of the population tested, and thus was a high value or key item within the meaning of ASA 500 [A54]; and

(b) in the absence of testing of Account 3324, the sample selected for testing would not be a representative sample, and would not provide:

(i) a reasonable basis for an auditor to draw conclusions about the entire population from which the sample was selected, as required by ASA 530 [4] and [15B]; and

(ii) a means of selecting items for testing that was effective in meeting the purpose of the audit procedure, as required by ASA 500 [10] and [A54]-[A55].

224. Further, or in the alternative, a Reasonable Auditor in the position of Deloitte would have:

(a) included Account 3324 as part of testing of COS, in order to obtain reasonable assurance that the immediate recognition of the rebate income in that account was appropriate and there was justification for recording the rebate income in that account; and

(b) tested the substance of transactions reclassified from CODB to COS in order to:

(i) obtain reasonable assurance about whether the reclassifications were in accordance with the requirements of AASB 101 and 102;

(ii) determine whether the advice that Deloitte had provided referred to in paragraphs 107 to 115 above was correct;

(iii) further or alternatively, determine whether the advice that Deloitte had provided referred to in paragraphs 107 to 115 above had been complied with; and

(iv) gain reasonable assurance in relation to the risks referred to in paragraph 214 above.

225. Deloitte did not take the steps referred to in paragraphs 223 or 224 above.

226. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

227. On or around 3 July 2014, DSH reclassified $20.5 million worth of rebates from CODB Account 4232 to COS Account 3324 in respect of the period to 29 June 2014 via journal entry number 390865 (**Journal No 390865**).

228. Journal No 390865 comprised 94.6% of the balance of COS Account 3324 in respect of Australia.

229. Had Deloitte taken the steps referred to in paragraph 223 or 224 above, Deloitte would have:

(a) discovered that 94.6% of the balance of Account 3324 comprised Journal No 390865 for $20.5 million;

(b) selected Journal No 390865 for testing, and requested a copy of the journal and the documents substantiating the journal;

(c) identified that $20.5 million of O&A rebate income had been reclassified from CODB Account 4232 to COS Account 3324;

(d) discovered some or all of the matters described in the First Mills Affidavit at [130]-[149];

(e) identified the $20.5 million in COS (and hence gross profit) as a potential error and sought sufficient audit evidence in relation to the transactions to obtain reasonable assurance that the amounts reclassified satisfied the criteria for recognising the O&A rebate income in COS;

(f) not provided an unqualified opinion in relation to the FY14 Financial Report unless it had obtained sufficient audit evidence in respect of the $20.5 million reclassification or the FY14 accounts were restated to account properly for the $20.5 million rebate income;

(g) advised the FAC in writing:

(i) of the matters referred to in sub-paragraphs (c), (d) and (e) above; and

(ii) that it is necessary for DSH to implement new controls to ensure that material journals were posted only when it was appropriate to do so.

230. Further, a Reasonable Auditor in the position of Deloitte would have included as part of its design and implementation procedures, and tested as part of the HY15 Review, that DSH had implemented new controls in accordance with the advice referred to above.

FY14 inadequate testing of Account 3324

231. Paragraphs 161 to 163 and 164 to 166 above are repeated.

232. In accordance with ASA 315 [25], Deloitte was required to identify and assess the risks of material misstatement at the financial report level and the assertion level for classes of transactions, account balances and disclosures to provide a basis for designing and performing further audit procedures.

233. By reason of the matters referred to in paragraphs 143 to 152 and 231 above, in accordance with ASA 315 [25]:

(a) Account 3324 was at risk of material misstatement;

(b) Deloitte was required to conduct testing of Account 3324.

234. Paragraph 221 is repeated.

235. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 315.

236. A Reasonable Auditor in the position of Deloitte would have tested Account 3324.

237. Deloitte did not take the steps referred to in paragraph 236 above.

238. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

239. Had Deloitte taken the steps referred to in paragraph 236 above, Deloitte would have discovered the matters and taken the steps referred to in paragraph 229 above.

FY14 inadequate journal testing

240. Paragraphs 161 to 163, 164 to 166 and 171 to 173 above are repeated.

241. In accordance with ASA 240 [32(a)(i)], Deloitte was required to test journal entries.

242. Further, in accordance with ASA 240 [32(a)(ii)], Deloitte was required to select journal entries and other adjustments made at the end of a reporting period.

243. Further, in accordance with ASA 240 [A43], when identifying and selecting journal entries and other adjustments for testing and determining the appropriate method of examining the underlying support for the items selected, Deloitte was required to consider matters including the following:

(a) the fact that inappropriate journal entries or other adjustments often have unique identifying characteristics, which may include entries:

(i) made to unrelated, unusual, or seldom-used accounts;

(ii) made by individuals who typically do not make journal entries;

(iii) recorded at the end of the period or as post-closing entries that have little or no explanation or description;

(iv) made either before or during the preparation of the financial report that do not have account numbers;

(v) containing round numbers or consistent ending numbers;

(b) in relation to journal entries or other adjustments processed outside the normal course of business, the fact that non-standard journal entries may not be subject to the same level of internal control as those journal entries used on a recurring basis to record transactions such as monthly sales, purchases and cash disbursements.

244. On 25 July 2014, Deloitte documented that:

(a) DSH utilised various types of journal entries, with the main distinction being between automatic journal entries (automatically posed by the AS400 system based on data inputs to the system) and manual journal entries (manually performed by individuals);

(b) from an audit point of view, manual journal entries posed a risk of material misstatement and potential fraud due to the ease of management override, probability of error and the risk of fraud;

(c) therefore, journal entry testing formed an important part of an audit.

245. Deloitte's journal entry testing program:

(a) presumed a risk of material misstatement due to fraud related to management override of controls;

(b) acknowledged that management was in a unique position to perpetrate fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively;

(c) classified the said risk as "significant";

(d) required Deloitte to test the completeness of the journal entry testing population;

(e) required Deloitte to test the appropriateness of journal entries recorded in the general ledger, including by selecting journal entries and other adjustments made at the end of a reporting period; and

(f) when using information provided by DSH, required Deloitte to evaluate whether the information was sufficiently reliable for Deloitte's purposes, including as necessary obtaining audit evidence about the accuracy and completeness of the information.

246. Deloitte's approach to journal entry testing was that sample journals were to be selected for testing if they were non-systematic journals having criteria including the following:

(a) large values;

(b) round and absolute numbers;

(c) concerning areas of significant risk, such as rebates;

(d) an appearance of being unusual; and

(e) relating to revenue (given the presumed risk of fraud).

247. Paragraphs 227 and 228 above are repeated.

248. In accordance with ASA 240, Deloitte was required to test Journal No 390865.

249. Further:

(a) although Deloitte purported to obtain a complete journal extraction for FY14, in fact Deloitte obtained a journal extraction for the financial year to 29 June 2014 based on the posting date of the journal entry, not the period to which the journal entry related; and

(b) Journal No 390865 was posted after 29 June 2014, on 3 July 2014, and as such fell outside the population sequence of the journal extraction tested by Deloitte for the year to 29 June 2014.

250. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 240.

251. A Reasonable Auditor in the position of Deloitte would have:

(a) known that entities input journal entries relating to the period under review subsequent to year-end;

(b) ensured that the journal extraction was based upon parameters that included all relevant journal entries, including those posted after the close of the relevant financial period in respect of FY14;

(c) in the premises, detected the existence of Journal No 390865 by testing the journal entry population for completeness;

(d) further or alternatively, would have selected Journal No 390865 for testing.

252. Deloitte did not take the steps referred to in paragraph 251 above.

253. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

254. Had Deloitte taken the steps referred to in paragraph 251 above, it would have discovered the matters and taken the steps referred to in paragraph 229 above.

FY14 failure to inform those charged with governance

255. During the conduct of the FY14 Audit, in its work paper titled "*23303 Memo - Vendor receivables and disputed claims*", Deloitte documented that:

(a) in relation to the processes around receiving O&A rebates, Deloitte had identified areas of deficiency which could pose risks of material misstatements;

(b) in relation to the posting of accounting (rebate) journals by the category buyers:

(i) the buyers had been given responsibility of their portfolio and the management and the accounting for the rebates that had been earned;

(ii) there was no oversight from a management point of view other than the review of subsequent receipts related to these rebate accruals;

(iii) there were two major risks associated with this activity:

(A) the buyers had the incentive to inflate the accruals to meet targets as there was no review; and

(B) the buyers would not have appropriate accounting knowledge of Australian Accounting Standards which would result in the incorrect treatment of rebates;

(c) the above matters posed a risk of fraud or material misstatement in the financial statements;

(d) there was no oversight or approval from management over the recognition and recording of rebates:

(i) since the responsibility for the recognition and recording of rebates had been transferred to the category buyers, there was no considerable oversight from the management in the buying/procurement team or the finance team regarding the recognition and recording of rebates;

(ii) the numbers produced by the buyers were highly summarised which prevented the buying/procurement team or the finance team from conducting a proper review;

(iii) the finance team posted the monthly journals purely based on the numbers produced by the buyers without any formal review which posed the risk of incorrect accounting treatment of rebates as the buyers did not possess appropriate accounting knowledge;

(e) there were no proper records or support for the posted rebate accruals:

(i) it was noted that a large number of rebate deals were agreed verbally/through e-mail correspondence and there was no formal support/evidence trail available;

(ii) upon request for audit testing, the buyers had to manually search through their records (i.e. email inboxes) to obtain the appropriate evidence for the sampled rebate items;

(iii) there needed to be support readily available for every accrual journal posted due to the fact that all the accruals were immediately recognised in profit and loss;

(iv) absence of proper documentation could result in fraudulent, duplicate and incorrect amounts which could get posted in the accounting books being unable to be substantiated;

(f) incorrect classification of rebates:

(i) it was noted that some accruals that were selected for testing were incorrectly classified:

(A) rebates that were based on purchases volume and had characteristics of volume rebates were classified as O&A rebates instead of volume rebates;

(B) rebates that related to agreements which had periods that exceeded FY14 were not deferred and the whole revenue was recognised in FY14;

(ii) this was the result of inadequate oversight and approvals from the buying/procurement and the finance teams as the buyers posted the journals for accruals and did not possess appropriate accounting knowledge;

(iii) in summary, Deloitte noted that there were considerable deficiencies around the Over and Above rebates process.

256. In accordance with ASA 265, Deloitte was required to:

(a) determine whether it had identified one or more deficiencies in internal control and whether, individually or in combination, they constitute significant deficiencies [ASA 265, [7]-[8]]; and

(b) communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis [ASA, 265, [9]).

257. The matters alleged at paragraph 255 above (**Rebate Control Deficiencies**) were deficiencies in internal control within the meaning of ASA 265.

258. The Rebate Control Deficiencies, individually or in combination, constituted significant deficiencies within the meaning of ASA 265.

259. For the purposes of ASA 265 and ASA 260 [3], [5], [13] and [A39], "*those charged with governance*" at DSH included:

(a) Cave;

(b) Wavish;

(c) Raine;

(d) Ishak; and

(e) Murray (from 12 August 2014).

260. Deloitte advised the FAC that it would provide the FAC with an audit report which would report "*findings from performance of internal control and system procedures*".

261. At no time during or following the FY14 Audit did Deloitte communicate in writing to Cave, Wavish, Raine, Ishak or Murray:

(a) the Rebate Control Deficiencies; or

(b) that the Rebate Control Deficiencies were deficiencies in internal control which, individually or in combination, constituted significant deficiencies.

262. Further, at no time during or following the FY14 Audit did Deloitte otherwise disclose to Cave, Wavish, Raine, Ishak or Murray:

(a) the Rebate Control Deficiencies; or

(b) that the Rebate Control Deficiencies were deficiencies in internal control which, individually or in combination, constituted significant deficiencies.

263. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 265.

264. A Reasonable Auditor in the position of Deloitte would have communicated to Cave, Wavish, Raine, Ishak and (from 12 August 2014) Murray, in writing and on a timely basis:

(a) the Rebate Control Deficiencies; and

(b) that the Rebate Control Deficiencies were deficiencies in internal control which, individually or in combination, constituted significant deficiencies.

265. Deloitte did not take the steps referred to in paragraph 264 above.

266. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

267. Further, a Reasonable Auditor in the position of Deloitte, would have advised the FAC in writing:

(a) of the Rebate Control Deficiencies;

(b) that the Rebate Control Deficiencies were deficiencies in internal control which, individually or in combination, constituted significant deficiencies; and

(c) that it was necessary for DSH to implement new controls to address each of the Rebate Control Deficiencies.

268. Further, a Reasonable Auditor in the position of Deloitte would have included in its design and implementation procedures for, and tested as part of, the HY15 Review that DSH had implemented new controls in accordance with the advice referred to above.

269. Deloitte did not take the steps referred to in paragraph 267 above.

270. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

FY14 failure to understand and test controls surrounding the Revised Obsolescence Methodology

271. Paragraphs 167 to 170 above are repeated.

272. In accordance with ASA 315 [18], Deloitte was required to obtain an understanding of DSH's information systems, including the related business processes, relevant to the FY14 Financial Report.

273. In accordance with ASA 500 [4] and [6], Deloitte was required to design and perform audit procedures that were appropriate in the circumstances for the purposes of obtaining sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base its opinion in relation to the risk of material misstatement in relation to the provision for obsolescence.

274. In forming its opinion about the reasonableness of the provision for obsolescence in the FY14 Financial Report, Deloitte relied upon and used as audit evidence the provision determined by using the Revised Obsolescence Methodology.

275. The following matters were central to the operation of the Revised Obsolescence Methodology:

(a) the selection and recording of sales data;

(b) the process by which stock was classified or allocated to stock categories (i.e. "Active", "End of Life", "No Reorder", "Discontinued", "Quit"), to which percentages for obsolescence were applied;

(c) the recorded number of months cover for stock in the "Active" and "End of Life" categories; and

(d) the recorded age of the stock.

276. In accordance with ASA 500 [7], Deloitte was required to consider the relevance and reliability of the Revised Obsolescence Methodology which it used as audit evidence.

277. In accordance with ASA 315 [18], Deloitte was required to understand each of the matters pleaded at paragraph 275 above.

278. In accordance with ASA 315 [13], Deloitte was required to evaluate the design and implementation of controls in relation to the Revised Obsolescence Methodology.

279. In relation to the FY14 Audit, Deloitte's understanding, and testing, of the design and implementation of the key control activities in the Revised Obsolescence Methodology was as documented in its work paper entitled "*22201 Expenditure & Inventory Management Business Cycle - D&I Testing*" (**Inventory Management Business Cycle Work Paper**).

280. The Inventory Management Business Cycle Work Paper does not document:

(a) any review of the print off of all sales for the year along with the COS component, to which management claimed to have had regard in assessing the calculations underlying the negative margin provision;

(b) any understanding of the process by which stock was classified to the categories to which percentages for obsolescence were applied; or

(c) any testing of the controls designed and implemented to ensure the accuracy of the allocation of stock to each category.

281. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 200, 315 or 500.

282. In evaluating the design of controls and the implementation of controls, a Reasonable Auditor in the position of Deloitte would have tested the basis (being the source of the inputs and the calculation of those items) of the matters central to the operation of the Revised Obsolescence Methodology, including:

(a) the selected sales data used in the calculations;

(b) the allocation of stock to each category;

(c) the number of months cover for stock in the "Active" and "End of Life" categories used in the calculations; and

(d) the recorded age of the stock used in the calculations.

283. Deloitte did not take the steps referred to in paragraph 282 above.

284. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

285. A Reasonable Auditor in the position of Deloitte, having taken the steps referred to in paragraph 282 above, would have determined that the Revised Obsolescence Methodology was flawed because:

(a) it did not take into account whether DSH held excess inventory which was unlikely to be realised for its cost;

(b) DSH should have, but failed to, analyse the number of weeks cover it held for each SKU and make an assessment of whether that stock amount was likely to be saleable given the nature of the product;

(c) it depended on the appropriate categorisation applied to each product line, and DSH may not have been categorising its Active stock correctly; and

(d) the trigger for the provision policy for Active and End of Life was flawed and did not calculate NRV because it applied a lookback method, rather than considering likely realisable value of the inventory based on future sales.

286. Further, a Reasonable Auditor in the position of Deloitte, having determined the matters at paragraph 285 above, would have:

(a) concluded that the Revised Obsolescence Methodology was not operating effectively;

(b) not provided an unqualified opinion in relation to the FY14 Financial Report unless an adequate provision in respect of inventory in accordance with AASB 102 was included in the FY14 Financial Report;

(c) advised the FAC in writing:

(i) of the matters referred to in paragraph 285 above;

(ii) that DSH's methodology for calculating the provision for inventory was inadequate and not in accordance with AASB 102;

(iii) it was necessary for DSH to implement new systems to ensure that inventory was accounted for in accordance with AASB 102; and

(iv) that DSH should adopt the provisioning methodology referred to in Basford at [160] or some other alternative methodology that complied with Australian Accounting Standards, including AASB 102.

287. Further, a Reasonable Auditor in the position of Deloitte would have included as part of its design and implementation procedures, and tested as part of the HY15 Review, that DSH had implemented new systems in accordance with the advice referred to above.

FY14 inadequate testing of the Revised Obsolescence Methodology

288. Paragraphs 167 to 170 above are repeated.

289. In accordance with ASA 240 [5], Deloitte was responsible for obtaining reasonable assurance that the FY14 Financial Report taken as a whole was free from material misstatement, whether caused by fraud or error.

290. In accordance with ASA 500 [4], Deloitte was required to design and perform audit procedures so as to enable it to obtain sufficient appropriate audit evidence to be able to draw a conclusion that the FY14 Financial Report accounted for inventory in accordance with AASB 102.

291. In accordance with ASA 540, Deloitte was required to obtain sufficient appropriate audit evidence regarding accounting estimates.

292. In relation to the FY14 Audit, Deloitte's testing of stock valuation and stock obsolescence, including the Revised Obsolescence Methodology, was documented in the following Deloitte work papers:

(a) tab 7 of the work paper entitled "*23401AU Inventories - Leadsheet and testing – Australia*";

(b) "*23401AU Inventories - Leadsheet and testing - Australia_Detail View*"; and

(c) "*23403 Inventory Obsolescence Memo*",

(together the **Stock Testing Work Papers**).

293. Deloitte:

(a) did not include in the Stock Testing Work Papers any documentation of audit procedures testing the assumptions on which the Revised Obsolescence Methodology was based;

(b) assumed that the quantum of stock allocated to each category was correct, without conducting any procedures to audit those allocations;

(c) relied upon the output of the spreadsheet at tab 7 of the Stock Testing Work Paper to perform analytical review procedures, including:

(i) comparing stock categories for FY14 to FY13; and

(ii) comparing provisions for each category for FY14 to FY13,

without audit evidence in respect to the reasonableness and accuracy of the status, ageing, months cover and other assumptions upon which the Revised Obsolescence Methodology was based;

(d) tested the ageing of stock by applying a formula which quantified the days between 29 June 2014 and the date of last receipt of the stock, without testing the ageing of each item of stock within the SKU;

(e) did not obtain reasonable assurance to enable Deloitte to draw conclusions that the output of the calculations comprising the Revised Obsolescence

Methodology were accurate and were a reliable cross check for concluding that the provision for inventory obsolescence recorded in the general ledger (which was based on the Old Methodology) was not materially misstated;

(f) did not design and perform audit procedures so as to enable it to obtain sufficient appropriate audit evidence to be able to draw a conclusion that the FY14 Financial Report accounted for inventory at the lower of cost and NRV in accordance with AASB 102.

294. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 240, ASA 500 or ASA 540.

295. A Reasonable Auditor in the position of Deloitte would have designed and performed procedures to obtain sufficient and appropriate audit evidence to obtain reasonable assurance of the appropriateness of the Revised Obsolescence Methodology, including:

(a) the selected sales data used in the calculations, including by obtaining audit evidence of:

(i) current and forecast sales of each stock item selected for testing; and

(ii) recent sales generated by the stock item, to ensure the stock item was realisable;

(b) the allocation of stock to each category, including by:

(i) auditing the accuracy of the quantum of stock allocated to each category;

(ii) challenging management's estimates for the percentages allocated to each stock category;

(iii) looking at historic write-down of stock items and assessing the status to which those stock items were allocated;

(c) the number of months cover for stock in the "Active" and "End of Life" categories used in the calculations by:

(i) obtaining forecast sales for stock items by unit and value and dividing the units on hand by the forecast units to be sold;

(ii) in the absence of forecast sales data:

(A) obtaining monthly units sold in the period to the date of the FY14 Audit;

(B) reviewing trends of sales of units for increases and decreases; or

(C) applying professional judgement to quantify months cover based on average monthly units sold (if a consistent number of units were sold in that period);

(d) the recorded age of the stock used in the calculations by testing the ageing of the items of stock by SKU and not just the date of last receipt of the stock.

296. Deloitte did not take the steps referred to in paragraph 295 above.

297. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

298. A Reasonable Auditor in the position of Deloitte, having taken the steps referred to in paragraph 295 above, would have:

(a) determined that the Revised Obsolescence Methodology was flawed because:

(i) it did not take into account whether DSH held excess inventory which was unlikely to be realised for its cost;

(ii) DSH should have, but failed to, analyse the number of weeks cover it held for each SKU and make an assessment of whether that stock amount was likely to be saleable given the nature of the product;

(iii) it depended on the appropriate categorisation was applied to each product line, and DSH may not have been categorising its Active stock correctly; and

(iv) the trigger for the provision policy for Active and End of Life was flawed and did not calculate NRV because it applied a lookback method, rather than considering likely realisable value of the inventory based on future sales;

(b) not provided an unqualified opinion in relation to the FY14 Financial Report unless an adequate provision in respect of inventory in accordance with AASB 102 was included in the FY14 Financial Report;

(c) advised the FAC in writing:

(i) of the matters referred to in sub-paragraph (a) above;

(ii) that DSH's methodology for calculating the provision for inventory was inadequate and not in accordance with AASB 102;

(iii) that it was necessary for DSH to implement new systems to ensure that inventory was accounted for in accordance with AASB 102; and

(iv) that DSH should adopt the provisioning methodology referred to in Basford at [160] or some other alternative methodology that complied with Australian Accounting Standards, including AASB 102.

299. Further, a Reasonable Auditor would have included as part of its design and implementation procedures, and tested as part of the HY15 Review, that DSH had implemented new systems in accordance with the advice referred to above.

FY14 failure to advise in relation to improper capitalisation of overhead costs into inventory

300. Paragraph 168(g) above is repeated.

301. AASB 102 [10] provided that the cost of inventories should comprise all costs of purchase, costs of conversion, and other costs incurred in bringing the inventories to their present location and condition.

302. AASB 102 [16(b)-(c)] provided that examples of costs excluded from the cost of inventories and recognised as expenses included:

(a) storage costs, unless those costs were necessary in the production process before a further production stage; and

(b) administrative overheads that did not contribute to bringing inventories to their present location and condition.

303. Paragraphs 289 to 291 above are repeated.

304. DSH had a policy of capitalising:

(a) freight costs;

(b) costs of warehousing; and

(c) some costs of the buying department,

(**Capitalisation Policy**).

305. Deloitte was aware, or ought reasonably to have been aware, of the Capitalisation Policy.

306. The capitalisation of costs alleged in paragraphs 304(b) and 304(c) above was not in accordance with AASB 102.

307. In accordance with ASA 315 [11], Deloitte was required to obtain an understanding of DSH's selection and application of accounting policies, and evaluate whether DSH's accounting policies were appropriate for its business and consistent with the applicable financial reporting framework and accounting policies used in the relevant industry.

308. Deloitte did not advise DSH of the matter alleged at paragraph 306 above.

309. In the premises, Deloitte did not conduct the FY14 Audit in accordance with ASA 315.

310. A Reasonable Auditor in Deloitte's position would have:

(a) determined that the Capitalisation Policy was not in accordance with AASB 102;

(b) not provided an unqualified opinion in relation to the FY14 Financial Report until the costs referred to in paragraphs 304(b) and 304(c) above were excluded from the capitalisation;

(c) advised the FAC in writing of the matter referred to in sub-paragraph (a) above.

311. Deloitte did not take the steps referred to in paragraph 310 above.

312. In the premises, Deloitte did not conduct the FY14 Audit in accordance with the applicable Auditing Standards or with the degree of skill, care and diligence of a professional person providing professional services of the same kind.

VII. FY14 MISREPRESENTATIONS & MISLEADING CONDUCT

FY14 representations, opinions and conduct

First FY14 inventory representations, opinions and conduct

313. On or about 6 August 2014, Deloitte represented that:

(a) the quality and ageing of inventory had improved;

(b) the improvement in the quality and ageing of inventory had led to a reduction in the inventory provision;

(c) the new methodology that had been developed by management (being the methodology referred to in paragraph 131 above, which, for convenience only, is referred to in these representations as the "Revised Obsolescence Methodology") took into account the improved quality and ageing of inventory;

(d) Deloitte had reviewed and audited the assumptions and methodology applied in the Revised Obsolescence Methodology and concurred with it;

(e) the Revised Obsolescence Methodology was appropriate for adoption by DSH to determine its inventory provision in accordance with AASB 102;

(f) the inclusion of warehouse costs and the costs of the buying team in the cost of inventory was appropriate and complied with AASB 102;

(g) inventory balances had increased from FY13 as a result of additional stores opened as at 29 June 2014 and increased buying activity at the conclusion of FY14;

(h) the manner in which DSH accounted for inventory (including the value of inventory and the level of provisioning) was appropriate and complied with Australian Accounting Standards, including AASB 102,

(**First FY14 Inventory Representations**).

314. Further, or in the alternative, on or about 6 August 2014, Deloitte represented that it held opinions to the effect set out in paragraph 313 above and:

(a) it had acted with the degree of skill, care and diligence expected of a professional providing services of the same kind and/or exercised reasonable skill and care in reaching those opinions; and

(b) further, or in the alternative, it had reasonable grounds for reaching those opinions based upon sufficient appropriate audit evidence and a proper interpretation of the Australian Accounting Standards,

(**First FY14 Inventory Opinion Representations**).

315. Further, or in the alternative to paragraphs 313 and/or 314 above, on or about 6 August 2014, Deloitte engaged in conduct that had the effect of conveying the matters referred to at paragraphs 313 and/or 314 above (**First FY14 Inventory Conduct**).

First FY14 rebate representations, opinions and conduct

316. On or about 6 August 2014, Deloitte represented that:

(a) Deloitte concurred with management's revised treatment of O&A rebates within COS rather than as a recovery of marketing and sales expenses;

(b) management's revised treatment of O&A rebates within COS rather than as a recovery of marketing and sales expenses was appropriate and complied with Australian Accounting Standards, including AASB 102;

(c) the reclassification from CODB to COS did not have a material impact on the comparatives reported;

(d) the manner in which DSH accounted for rebates (including the reclassification from CODB to COS and the value of rebates recognised by DSH), was appropriate and complied with Australian Accounting Standards, including AASB 102,

(**First FY14 Rebate Representations**).

317. Further, or in the alternative, on or about 6 August 2014, Deloitte represented that it held opinions to the effect set out in paragraph 316 above and:

(a) it had acted with the degree of skill, care and diligence expected of a professional providing services of the same kind and/or exercised reasonable skill and care in reaching those opinions; and

(b) further, or in the alternative, it had reasonable grounds for reaching those opinions based upon sufficient appropriate audit evidence and a proper interpretation of the Australian Accounting Standards,

(**First FY14 Rebate Opinion Representations**).

318. Further, or in the alternative to paragraphs 316 and/or 317 above, on or about 6 August 2014, Deloitte engaged in conduct that had the effect of conveying the matters referred to at paragraphs 316 and/or 317 above (**First FY14 Rebate Conduct**).

FY14 internal control deficiencies representation and non-disclosure

319. On or about 6 August 2014, Deloitte represented that it had not identified any significant deficiencies in internal controls relating to the prevention and detection of fraud and error which would impact on Deloitte's ability to provide its opinion on the FY14 Financial Report (**FY14 No Internal Control Deficiencies Representation**).

320. Further, or in the alternative to paragraph 319 above, at no time did Deloitte advise the NED Cross-Claimants that during the FY14 Audit it had identified significant deficiencies in internal controls relating to the preventing and detection of fraud and error which would impact on Deloitte's ability to provide its opinion on the FY14 Financial Report (**FY14 Internal Control Deficiencies Non-Disclosure**).

321. The NED Cross-Claimants and DSH had a reasonable expectation that the matters referred to in paragraph 320 above would be disclosed by Deloitte.

322. Further or in the alternative, by reason of the matter alleged in paragraph 94 above, Deloitte had a duty to disclose the matters referred to in paragraph 320 above to the FAC in writing.

Second FY14 inventory representations, opinions and conduct

323. On or about 12 August 2014, Deloitte represented that:

(a) included in the cost of inventory were capitalised rebates and supply chain costs which had been recognised in the total cost of inventory under AASB 102;

(b) the inclusion of supply chain costs complied with AASB 102;

(c) the quality and ageing of inventory had improved;

(d) DSH's management had further refined the methodology for calculating the inventory obsolescence and shrinkage provisions which took into account the improved quality and ageing of inventory;

(e) Deloitte concurred with this methodology;

(f) Deloitte had audited the assumptions underlying both the Old Obsolescence Methodology and the Revised Obsolescence Methodology;

(g) Deloitte concurred that the Revised Obsolescence Methodology was more appropriate as at 29 June 2014, and therefore had included a $1.5 million adjusted difference summary;

(h) the Revised Obsolescence Methodology was appropriate for adoption by DSH to determine its inventory provision in accordance with AASB 102;

(i) the manner in which DSH accounted for inventory (including the value of inventory and level of provisioning) was appropriate and complied with Australian Accounting Standards, including AASB 102,

(**Second FY14 Inventory Representations**).

324. Further, or in the alternative, on or about 12 August 2014, Deloitte represented that it held opinions to the effect set out in paragraph 323 above and:

(a) it had acted with the degree of skill, care and diligence expected of a professional providing services of the same kind and/or exercised reasonable skill and care in reaching those opinions; and

(b) further, or in the alternative, it had reasonable grounds for reaching those opinions based upon sufficient appropriate audit evidence and a proper interpretation of the Australian Accounting Standards,

(**Second FY14 Inventory Opinion Representations**).

325. Further, or in the alternative to paragraphs 323 and/or 324 above, on or about 12 August 2014, Deloitte engaged in conduct that had the effect of conveying the

matters referred to at paragraphs 323 and/or 324 above (**Second FY14 Inventory Conduct**).

Second FY14 rebate representations, opinions and conduct

326. On or about 12 August 2014, Deloitte represented that:

(a) where rebates relate to stock purchases held at year end or promotions in FY15, the rebate income should be deferred into the future period;

(b) a small element of rebates collected during FY14 related to FY15 resulting in a $1.1 million extrapolated variance that was noted in the unadjusted differences summary;

(c) other than the $1.1 million extrapolated variance, none of the rebates recognised in the FY14 Financial Report should have been deferred into FY15; and

(d) the manner in which DSH accounted for rebates (including the value of rebates recognised by DSH) was appropriate and complied with Australian Accounting Standards, including AASB 102,

(**Second FY14 Rebate Representations**).

327. Further, or in the alternative, on or about 12 August 2014, Deloitte represented that it held opinions to the effect set out in paragraph 326 above and:

(a) it had acted with the degree of skill, care and diligence expected of a professional providing services of the same kind and/or exercised reasonable skill and care in reaching those opinions; and

(b) further, or in the alternative, it had reasonable grounds for reaching those opinions based upon sufficient appropriate audit evidence and a proper interpretation of the Australian Accounting Standards,

(**Second FY14 Rebate Opinion Representations**).

328. Further, or in the alternative to paragraphs 326 and/or 327 above, on or about 12 August 2014, Deloitte engaged in conduct that had the effect of conveying the matters referred to at paragraphs 326 and/or 327 above (**Second FY14 Rebate Conduct**).

FY14 anticipated unqualified audit report representations and conduct

329. On or about 12 August 2014, Deloitte represented that:

(a) Deloitte's audit of the FY14 Financial Report was substantially complete;

(b) subject to the directors adopting the accounts, review of any subsequent events and receipt of the signed management representation letter, Deloitte anticipated issuing an unqualified audit report;

(c) in reaching the conclusion that (subject to the matters specified) it would issue an unqualified audit report, Deloitte:

(i) had acted with the degree of skill, care and diligence expected of a professional providing services of the same kind and/or exercised reasonable skill and care; and

(ii) further, or in the alternative, it had reasonable grounds for reaching that conclusion based upon sufficient appropriate audit evidence and a proper interpretation of the Australian Accounting Standards,

(**FY14 Anticipated Unqualified Audit Report Representations**).

330. Further, or in the alternative to paragraph 329 above, on or about 12 August 2014, Deloitte engaged in conduct that had the effect of conveying the matters referred to at paragraph 329 above (**FY14 Anticipated Unqualified Audit Report Conduct**).

FY14 clearance representations, opinions and conduct

331. On or about 18 August 2014, Deloitte, by its audit partner, White, represented that:

(a) Deloitte "*gave clearance on the accounts*" of DSH for the period ended 29 June 2014;

(b) the FY14 Financial Report was appropriate for adoption by DSH;

(c) the FY14 Financial Report was in accordance with the Corporations Act, including:

(i) giving a true and fair view of the consolidated entity's financial position as at 29 June 2014 and of its performance for the year ended that date;

(ii) complying with Australian Accounting Standards and the Corporations Regulations 2001;

(d) the manner in which DSH accounted for rebates (including the value of rebates recognised by DSH) was appropriate and complied with Australian Accounting Standards, including AASB 102; and

(e) the manner in which DSH accounted for inventory (including the value of inventory and level of provisioning) was appropriate and complied with Australian Accounting Standards, including AASB 102,

(**FY14 Clearance Representations**).

332. Further, or in the alternative, on or about 18 August 2014, Deloitte by its audit partner, White, represented that it held opinions to the effect set out in paragraph 331 above and:

(a) it had acted with the degree of skill, care and diligence expected of a professional providing services of the same kind and/or exercised reasonable skill and care in reaching those opinions; and

(b) further, or in the alternative, it had reasonable grounds for reaching those opinions based upon sufficient appropriate audit evidence and a proper interpretation of the Australian Accounting Standards,

(**FY14 Clearance Opinion Representations**).

333. Further, or in the alternative to paragraphs 331 and/or 332 above, on or about 18 August 2014, Deloitte engaged in conduct that had the effect of conveying the matters referred to at paragraphs 331 and/or 332 above (**FY14 Clearance Conduct**).

<u>*FY14 Corporations Act compliance representation, opinion and conduct*</u>

334. On 18 August 2014, Deloitte represented that the FY14 Financial Report was in accordance with the Corporations Act, including:

(a) giving a true and fair view of the consolidated entity's financial position as at 29 June 2014 and of its performance for the year ended that date;

(b) complying with Australian Accounting Standards and the Corporations Regulations 2001, (**FY14 Corporations Act Compliance Representation**).

335. Further, or in the alternative, on or about 18 August 2014, Deloitte represented that it held opinions to the effect set out in paragraph 334 above and:

(a) it had acted with the degree of skill, care and diligence expected of a professional providing services of the same kind and/or exercised reasonable skill and care in reaching those opinions; and

(b) further, or in the alternative, it had reasonable grounds for reaching those opinions based upon sufficient appropriate audit evidence and a proper interpretation of the Australian Accounting Standards,

(**FY14 Corporations Act Compliance Opinion Representation**).

336. Further, or in the alternative to paragraphs 334 and/or 335 above, on or about 18 August 2014, Deloitte engaged in conduct that had the effect of conveying the matters referred to at paragraphs 334 and/or 335 above (**FY14 Corporations Act Compliance Conduct**).

FY14 audit compliance representation, opinion and conduct

337. On 18 August 2014, Deloitte represented that it had conducted its audit of the FY14 Financial Report in accordance with Australian Auditing Standards (**FY14 Audit Compliance Representation**).

338. Further, or in the alternative, on or about 18 August 2014, Deloitte represented that it held opinions to the effect set out in paragraph 337 above and:

(a) it had acted with the degree of skill, care and diligence expected of a professional providing services of the same kind and/or exercised reasonable skill and care in reaching those opinions; and

(b) further, or in the alternative, it had reasonable grounds for reaching those opinions based upon sufficient appropriate audit evidence and a proper interpretation of the Australian Accounting Standards,

(**FY14 Audit Compliance Opinion Representation**).

339. Further, or in the alternative to paragraphs 337 and/or 338 above, on or about 18 August 2014, Deloitte engaged in conduct that had the effect of conveying the

matters referred to at paragraphs 337 and/or 338 above (**FY14 Audit Compliance Conduct**).

FY14 trade/commerce, financial product and financial services

340. Each of the:

(a) First FY14 Inventory Representations;

(b) First FY14 Inventory Opinion Representations;

(c) First FY14 Inventory Conduct;

(d) First FY14 Rebate Representations;

(e) First FY14 Rebate Opinion Representations;

(f) First FY14 Rebate Conduct;

(g) FY14 No Internal Control Deficiencies Representation;

(h) FY14 Internal Control Deficiencies Non-Disclosure;

(i) Second FY14 Inventory Representations;

(j) Second FY14 Inventory Opinion Representations;

(k) Second FY14 Inventory Conduct;

(l) Second FY14 Rebate Representations;

(m) Second FY14 Rebate Opinion Representations;

(n) Second FY14 Rebate Conduct;

(o) FY14 Anticipated Unqualified Audit Report Representations;

(p) FY14 Anticipated Unqualified Audit Report Conduct;

(q) FY14 Clearance Representations;

(r) FY14 Clearance Opinion Representations;

(s) FY14 Clearance Conduct;

(t) FY14 Corporations Act Compliance Representation;

(u) FY14 Corporations Act Compliance Opinion Representation;

(v) FY14 Corporations Act Compliance Conduct;

(w) FY14 Audit Compliance Representation;

(x) FY14 Audit Compliance Opinion Representation;

(y) FY14 Audit Compliance Conduct,

constituted conduct by Deloitte:

(z) in trade or commerce within the meaning of section 18 of the ACL; and/or

(aa) in relation to a financial product or a financial service within the meaning of section 1041H of the Corporations Act; and/or

(bb) in trade or commerce in relation to financial services within the meaning of section 12DA of the ASIC Act.

FY14 misleading or deceptive conduct

First FY14 inventory representations, opinions and conduct

341. The First FY14 Inventory Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

342. The First FY14 Inventory Opinion Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

343. The First FY14 Inventory Conduct was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

First FY14 rebate representations, opinions and conduct

344. The First FY14 Rebate Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

345. The First FY14 Rebate Opinion Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

346. The First FY14 Rebate Conduct was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

FY14 internal control deficiencies representation and non-disclosure

347. The FY14 No Internal Control Deficiencies Representation was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

348. The FY14 Internal Control Deficiencies Non-Disclosure was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

Second FY14 inventory representations, opinions and conduct

349. The Second FY14 Inventory Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

350. The Second FY14 Inventory Opinion Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

351. The Second FY14 Inventory Conduct was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

Second FY14 rebate representations, opinions and conduct

352. The Second FY14 Rebate Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

 (a) section 1041H(1) of the Corporations Act; and/or

 (b) section 12DA of the ASIC Act; and/or

 (c) section 18 of the ACL.

353. The Second FY14 Rebate Opinion Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

 (a) section 1041H(1) of the Corporations Act; and/or

 (b) section 12DA of the ASIC Act; and/or

 (c) section 18 of the ACL.

354. The Second FY14 Rebate Conduct was misleading or deceptive or likely to mislead or deceive in contravention of:

 (a) section 1041H(1) of the Corporations Act; and/or

 (b) section 12DA of the ASIC Act; and/or

 (c) section 18 of the ACL.

FY14 anticipated unqualified audit report representations and conduct

355. The FY14 Anticipated Unqualified Audit Report Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

 (a) section 1041H(1) of the Corporations Act; and/or

 (b) section 12DA of the ASIC Act; and/or

 (c) section 18 of the ACL.

356. The FY14 Anticipated Unqualified Audit Report Conduct was misleading or deceptive or likely to mislead or deceive in contravention of:

 (a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

FY14 clearance representations, opinion and conduct

357. The FY14 Clearance Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

358. The FY14 Clearance Opinion Representations were misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

359. The FY14 Clearance Conduct was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

FY14 Corporations Act compliance representation, opinion and conduct

360. The FY14 Corporations Act Compliance Representation was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

361. The FY14 Corporations Act Compliance Opinion Representation was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

362. The FY14 Corporations Act Compliance Conduct was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

FY14 audit compliance representation, opinion and conduct

363. The FY14 Audit Compliance Representation was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

364. The FY14 Audit Compliance Opinion Representation was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

365. The FY14 Audit Compliance Conduct was misleading or deceptive or likely to mislead or deceive in contravention of:

(a) section 1041H(1) of the Corporations Act; and/or

(b) section 12DA of the ASIC Act; and/or

(c) section 18 of the ACL.

FY14 reliance

First FY14 inventory representations, opinions and conduct

366. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the First FY14 Inventory Representations.

367. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the First FY14 Inventory Opinion Representations.

368. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the First FY14 Inventory Conduct.

First rebate representations, opinions and conduct

369. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the First FY14 Rebate Representations.

370. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the First FY14 Rebate Opinion Representations.

371. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the First FY14 Rebate Conduct.

FY14 internal control deficiencies representation and non-disclosure

372. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the FY14 No Internal Control Deficiencies Representation.

Second FY14 inventory representations, opinions and conduct

373. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the Second FY14 Inventory Representations.

374. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the Second FY14 Inventory Opinion Representations.

375. Each of Wavish, Cave, Raine, Ishak, Murray and DSH relied on the Second FY14 Inventory Conduct.