



# The Audit Failures of the Wirecard Scandal

Examining the Role of the Auditor  
in Regulatory Oversight

Edgar Löw · Reinhard Heyd

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# Preface

Wirecard is the biggest economic scandal in Europe since the Second World War—comparable to the Enron scandal in the USA and the Satyam Computer Services scandal in India. In around twenty years, the payment service provider went from a rather dubious start-up company to a German technology group that supposedly wanted to catch up with global companies such as Apple or Microsoft—only in a different field. Wirecard ousted Commerzbank, which was more than one hundred and fifty years old, from the DAX 30, and at one point was worth more than Deutsche Bank, which it even wanted to take over.

Suddenly, within just one week, Wirecard collapsed. Board members and senior executives were arrested or evaded arrest by fleeing. What remained was a fraud on an enormous scale—thousands of shareholders lost their savings and lawsuits were filed against Wirecard, the supervisory authorities, the management board, and the auditor.

This book is dedicated to the role of Wirecard's auditors—Ernst & Young. They audited Wirecard's consolidated financial statements over ten years and used different partners. The basis for an audit of the financial statements of a German group was the auditing standards of the Institute of Public Auditors in Germany (IDW PS) applicable in the years in question. They are usually based on the International Standards on Auditing (ISA) but are specifically adapted to German legal conditions. In addition, standards were issued in certain specialized areas in which no ISA (yet) existed. Ernst & Young has undertaken to comply with the IDW PS in its auditing practice fully.

We will demonstrate that compliance with the existing auditing standards would have meant that fraud could have been detected at a very early stage. Numerous indicators of fraud, which are listed in one of the auditing standards, were identified at Wirecard. However, this did not have a sufficient impact on Ernst & Young's risk-oriented audit approach. On the contrary, the company was often satisfied with oral statements provided by Wirecard. In our investigation, we focused on the business activities of third-party acquiring in the Asian region, which have been precisely those activities that ultimately almost did not exist but were largely invented. Ernst & Young was familiar with Wirecard's business model. Nevertheless, it was admitted that the risk situation was completely misrepresented in the Group risk reports and that the reported segment reports did not even begin to reflect reality correctly. On the contrary, numerous disclosure requirements of the International Financial Reporting Standards (IFRS) were violated without the auditor raising any objections.

We are focusing intensively on the financial years from 2015 to 2018. No consolidated financial statements were published for the 2019 financial year. We chose 2015 as the start of our investigations for various reasons. The Financial Times began this year with a series of very intensive allegations in a series of articles, first on the Internet and then in the print version. At this point at the latest, there was an additional external reason for the auditor to investigate particular allegations against Wirecard. In 2015, a huge acquisition was made, the value of which was repeatedly called into question. In the same year, the German securities regulator became active for the first time—ultimately in Wirecard's favor. And finally, a German court in Munich implied that Wirecard's consolidated financial statements had been falsified since at least 2015.

We have structured our book in such a way that we first provide a brief chronicle of Wirecard, the allegations and the demise of the company (Chapter 1). There has been a whole series of alarm signals with high relevance for the preparation of the risk-oriented audit approach by the auditor. We then provide a legal introduction to the Fundamental Principles of an Audit, which include German law and, above all, German auditing standards (Chapter 2). Two standards are of fundamental importance for the planning and execution of an audit—on the one hand, the risk-oriented audit approach and principle of materiality and, on the other, how to deal with risks of inaccuracies and violations.

The basis of every audit is knowledge of the business model and an examination of its impact on the audit planning. In the case of Wirecard, the auditor cannot be criticized for not having examined the business model

carefully enough. Certain accounting consequences were discussed with him in detail and possibly even proposed by the auditor. We therefore devote a detailed discussion to the presentation of the business model against the background of the accounting effects (Chapter 3). Given that Ernst & Young knew Wirecard's business model very well, as the reader carefully goes through our book it becomes even less clear that the audit procedures were not geared toward this during the numerous years of auditing.

The fraud at Wirecard took place in Asia through business activity with third-party acquirers. The scandal resulted in 1.9 billion Euro in payment funds not being available. They were allegedly held in escrow accounts. We will therefore first deal with types of fiduciary relationships and accounting consequences and then go into the necessary audit procedures (Chapter 4). We show which audit procedures had to be carried out to ensure that the cash shown in the balance sheet actually existed. If the audit would have been provided properly, the fraud could have been discovered very quickly. We uncover the massive deficiencies in the audit procedures. We then look at the question of accounting, assuming that Wirecard had control over the assets, and consider whether they should be recognized as trade receivables or as cash and cash equivalents (Chapter 5).

Every audit firm has to pay particular attention to the audit of sales. The relevant auditing standard already explicitly mentions that revenues are particularly subject to the risk of fraud. In this respect, we show under which conditions Wirecard should have recognized gross revenues and that commissions were predominantly to be shown in the income statement in the acquirer business (Chapter 6). We conclude this analysis with the necessary audit procedures to clarify—as in the previous chapters—which paragraphs of the relevant auditing standards were violated. Without disregarding the legal requirements of the relevant auditing standards, it would have been revealed that numerous transactions did not exist at all—the fraud would have been discovered much earlier.

While the balance sheet and the income statement provide an overall overview of the asset/liability and earnings situation, the notes have the task of, on the one hand, breaking down these figures in more detail and, on the other hand, explaining them verbally. We deliberately do not want to dive into these small-scale details, since it has already been proven in the previous chapters that the overall picture is not correct. However, since the business activity in its entirety has to be conveyed to the reader of the financial statements by fulfilling two additional accounting standards under specific aspects, we address the disclosure according to these two special standards separately. This is the obligation to present and explain the company's situation across

individual business areas (segments) (Chapter 7) as well as the obligation to show and make transparent the risks from business activities to which a company is exposed in a differentiated form (Chapter 8).

In full knowledge of the actual business model, the Group segment reporting presented to the reader of the financial statements was absolutely incomplete and materially incorrect. Wirecard massively violated the relevant accounting standard. The auditor should have objected to this. Instead, the addressees of the consolidated financial statements were deliberately misled—without any reaction from the auditor, which is a fundamental breach of his professional duties.

The same applies to risk reporting, which we differentiate between financial risks and other risks. The obligation to present financial risks is essentially based on an International Accounting Standard, while the other risks had to be presented largely based on a supplementary national standard. Both accounting standards were seriously breached. Once again, despite his knowledge of the business model, the auditor did not insist on reflecting the reality of Wirecard's risk situation. Instead, he allowed the actual risks not to be addressed at all in some cases and the overall risk situation of the group to be completely concealed, which again represents a massive breach of his professional duties.

At the end of an audit, the auditor is obliged to form an opinion, which is expressed in an auditor's report. The audit opinion can be issued without any objections, as was the case with Wirecard by Ernst & Young. However, it can also be qualified or refused altogether. Based on the previous chapters, we explain in a further section that there were sufficient grounds for refusing the audit opinion (Chapter 9). If the auditor's report would have been refused at an early stage, which—as we demonstrate—would have been the inevitable consequence if the audit had been carried out properly, the negative financial effects for shareholders and other investors would have been significantly less and the reputation of Germany as a financial market would have been less damaged. For the reputation of the auditing profession, the inadequate audit procedures were a catastrophe that was clearly avoidable.

In our concluding remarks (Chapter 10), we outline further developments following the discovery of the fraud. Some measures, in particular to strengthen governance, appear to make sense. As far as the role of the auditor in the Wirecard scandal is concerned, we show that the failure of Ernst & Young in the Wirecard financial statements could not have been prevented by new or stricter requirements for the auditor. Simple compliance with the existing rules and regulations and a careful audit by Ernst & Young, as is to be expected of a conscientious auditor,



could have uncovered Wirecard's fraud, which had been going on for years, at an early stage. An optimistic and positive conclusion can be drawn for both young students and experienced auditors. Anyone who carries out their work seriously in the interests of the public and behaves professionally, carefully, straightforwardly, and uprightly toward the audited company does not need to worry about liability regulations.

The book is not a lurid novel that delves into the abysses of secret service activities. Instead, the numerous and very massive breaches of accounting standards on the part of Wirecard and of auditing standards on the part of Ernst & Young are demonstrated factually and it is shown at least where there is a blatant failure on the part of the auditor. We only deal with subject areas in which we can clearly demonstrate the auditor's failures. With regard to the takeover of an Indian payment company, Wirecard was heavily criticized from various sides for the extremely high purchase price, because around 90% of the assets acquired were only customer relations and goodwill and the acquired company had only been worth around 10% of the purchase price just a short time before. Personal interests of Wirecard's key personnel may have been behind this acquisition. Violations of the relevant accounting standards, IFRS 3, IFRS 10, IFRS 12, and IAS 24, cannot be identified in the consolidated financial statements. The extent to which the auditor violated his professional duties in this transaction cannot be assessed as an outsider without an insight into internal documents. Since we do not speculate, we have not addressed this issue in our book. Only the reader can judge whether the book can therefore be considered dry. We particularly recommend reading it to members of the auditing profession, students who are still very interested in the attractive and very interesting profession of auditing and all those affected by the Wirecard scandal (like shareholders and other investors) and—especially—the judges.

We use verbatim quotations in our book. Where these originate from German examination standards or German literature, we have translated them into English to the best of our knowledge and belief. Even if, strictly speaking, it is no longer a literal quotation in the academic sense, we have retained the inverted commas.

We would like to thank the two reviewers who recommended that the publisher support our idea of a factual book on the role of the auditor in the case of Wirecard and the courage of Tula Weis from the publishing house Palgrave Macmillan to realize the project with us. We would also like to thank the two employees of Palgrave Macmillan, Saranya Siva and Supraja Yegnaraman, for their technical support. Very special thanks are due to Raphael Klei. He is an alumnus of the Master in Auditing program

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Frankfurt, Ulm  
June 2024

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# Abbreviations

AAA	triple A, Rating category
AfD	Alternative für Deutschland
AG	Aktiengesellschaft; Stock corporation
AktG	Aktiengesetz; Stock corporation law
AO	Abgabenordnung
APAS	Abschlussprüferaufsichtsstelle, Auditor Oversight Authority
ASCG	Accounting Standards Committee of Germany
BAFA	Bundesamt für Wirtschaft und Ausfuhrkontrolle, Federal Office of Economics and Export Control
BaFin	Bundesanstalt für Finanzdienstleistungsaufsicht; Federal Financial Supervisory Authority
BC	Basis of Conclusion
BIN	Bank Identification Number
BKR	Zeitschrift für Bank- und Kapitalmarktrecht
BLZ	Berliner Zeitung
BMJV	Bundesministerium für Justiz und Verbraucherschutz, Federal Ministry of Justice and Consumer Protection
BS	Berufssatzung; Professional Statute (for Public Auditors)
CDU	Christlich Demokratische Union Deutschlands
CEO	Chief Executive Officer
CF	Conceptual Framework
cf.	confere, compare
CFO	Chief Financial Officer
CG	Corporate Governance
CG Code	Recommendations of the Government Commission German Corporate Governance Code

## **xiv**      **Abbreviations**

CSU	Christlich Soziale Union
DAX	Deutscher Aktienindex; German Stock Index
DB	Der Betrieb
DE	Deutschland; Germany
DGAP	Deutsche Gesellschaft für Auswärtige Politik; German Council on Foreign Affairs
DOI	Digital Object Identifier
dpa	Deutsche Presseagentur; German Press Agency
DRS	Deutscher Rechnungslegungsstandard; German Accounting Standard
EBIT	Earnings before Interest and Taxes
EBITDA	Earnings before Interest, Taxes, Depreciation and Amortisation
EBS	Electronic Billing Systems
ECON	European Parliament's Committee on Economic and Monetary Affairs
ed	editor
EGOV	Economic Governance Support Unit
ejbmr	European Journal of Business and Management Research
ESMA	European Securities and Market Authority
EU	European Union
EY	Ernst & Young
F.A.Z.	Frankfurter Allgemeine Zeitung
FAQ	Frequently asked questions
FBI	Federal Bureau of Investigation
FDP	Freie Demokratische Partei
FinTech	Financial Technology
FISG	Finanzmarktintegritätsstärkungsgesetz; Financial Market Integrity Strengthening Act
FREP	Financial Reporting Enforcement Panel
FT	Financial Times
FYI	For Your Information
GAAP	Generally Accepted Accounting Principles
GAS	German Accounting Standards
GmbH	Gesellschaft mit beschränkter Haftung; Limited company (Ltd.)
GoA	Grundsätze ordnungsmäßiger Abschlussprüfung, Generally Accepted Standards on Auditing
GoMoPa	Goldman Morgenstern & Partners
HGB	Handelsgesetzbuch; German Commercial Code
i.e.	exempli gratia, for example
IAS	International Accounting Standards
ibid.	ebenda; Article that has already been mentioned
ICS	Internal Control System
IDW	Institut der Wirtschaftsprüfer; Institute of Public Auditors in Germany

IDW QS	Qualitätssicherungsstandards des Instituts der Wirtschaftsprüfer; Quality Standards of the Institute of Public Auditors in Germany (Requirements for Quality Assurance in Auditing Practice)
IFRS	International Financial Reporting Standards
Inc	Incorporated
ISA	International Standards on Auditing
ISA DE	International Standards on Auditing (Fassung für Deutschland; German version)
ISO	International Organization for Standardization
IT	Information Technology
KoR	Zeitschrift für kapitalmarktorientierte und internationale Rechnungslegung
KPMG	Klynfeld Peat Marwick Goerdeler
KWG	Kreditwesengesetz; Credit law
LLC	Limited Liability Company
Ltd	Limited
MI5	Military Intelligence, Section 5 (British Secret Service)
mm	Manager Magazin
n.F.	neue Fassung; new version
NDR	Norddeutscher Rundfunk
NGZ	Neue Zeitschrift für Gesellschaftsrecht
no.	number
No.	Number
OLB	Oldenburgische Landesbank
p.	page
para	Paragraph
pdf	Portable Document Format
PH	Prüfungshinweis; Auditing Guideline
PIE	Public Interest Entity
pp.	pages
PS	Prüfungsstandards; German Standards on Auditing
PSP	Payment Service Provider
R&T	Rajah & Tann
RegE	Regierungsentwurf; Government Draft
RMS	Risk Management System
SAFE	Leibniz Institute for Financial Research
SdK	Schutzgemeinschaft für Kapitalanleger
SG/HFA	Schmalenbachgesellschaft/Hauptfachausschuss des Instituts der Wirtschaftsprüfer
SMSG	European Securities and Markets Stakeholder Group
SPD	Sozialdemokratische Partei Deutschlands
StaRUG	Corporate Stabilization and Restructuring Act
StuB	Unternehmenssteuern und Bilanzen

**xvi      Abbreviations**

TecDAX	Deutscher Aktienindex für Technologiewerte
thes.	same source
TPA	Third Party Acquiring
UK	United Kingdom
US	United States
USD	United States Dollars
vol.	Volumen; volume
WA	Washington
WDR	Westdeutscher Rundfunk
WDT/WDB	Abbreviation used by EY for Wirecard
WHU	Otto Beisheim School of Management
WM	Wertpapier-Mitteilungen
WPg	Die Wirtschaftsprüfung
WP-Handbuch	Wirtschaftsprüferhandbuch
WpHG	Wertpapierhandelsgesetz
WPK	Wirtschaftsprüferkammer
WPO	Wirtschaftsprüferordnung; German Auditors' Code
ZCO	Business Referral and Commission Agreement
ZHR	Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht
ZWIRN	Zentrum für wissenschaftliches, interdisziplinäres Risikomanagement und Nachhaltigkeit





# 1

## Wirecard: Chronicle, Public Allegations, and the Downfall of the Company

Wirecard was founded in 1999 by Detlev Hoppenrath and Peter Herold and was a pioneer in the processing of digital payments. The company specialized in linking a credit card and the Internet by developing corresponding software as an interface between credit card companies, online merchants, and the merchants' customers. The company initially became known for processing payments for online gambling and porn sites. "In the early phase of e-commerce, European gambling sites accounted for a high proportion of payments processed via the Internet, and by 2004, it was probably almost 50 per cent of all real-time transactions," admitted Markus Braun, the long-standing CEO. "In this respect, Wirecard was a mirror of the overall market at the time." Later, the share of gambling in payment processing fell to less than ten percent.<sup>1</sup>

Detlev Hoppenrath became the first Chairman of Wirecard, and Peter Herold acted as Chairman of the Supervisory Board for one year after the company was founded. Hoppenrath hired Jan Marsalek back in 2000. He had developed online stores and a cell phone payment application at his previous employer. A major project by Marsalek to reprogram the entire platform failed and is said to have cost around DM 2 billion, jeopardizing Wirecard's existence at the time. KPMG was then commissioned to support the project. KPMG sent Markus Braun as a consultant, hired by Wirecard as Chief Technology Officer shortly afterwards. In May of the following year, i.e., in 2001,

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<sup>1</sup> Hesse (April 30, 2016): Finanzmärkte: Die Schlacht um Wirecard - Wette auf den Absturz (D. Spiegel, ed.); Der Spiegel (18/2016), pp. 65–67.

the previous CEO, Hoppenrath, moved to the Supervisory Board, and Wirecard relocated its Headquarters to Aschheim. After some turbulence, which almost led to insolvency,<sup>2</sup> Hoppenrath resigned from the Supervisory Board in October of the same year. Wirecard was taken over by Electronic Billing Systems (EBS) in January 2002. Between 2002 and 2004, the company was reorganized and listed on the stock exchange as Wirecard AG.<sup>3</sup>

To go public, Wirecard used a company called InfoGenie, which had been listed since 2000. A subsidiary of EBS acquired more than 25% of InfoGenie's shares in March 2002. InfoGenie's shares expired on the stock exchange and were supposed to be delisted. However, the courts prohibited Deutsche Börse from doing so. In December 2004, it was decided to contribute Wirecard to InfoGenie as of 1 January 2005, in return for a contribution in kind. InfoGenie was renamed Wire Card, which became Wirecard in June 2006. In this way, Wirecard became a listed company, and Markus Braun became Chairman of the Management Board (CEO). In January 2006, Wirecard acquired a bank and developed into a full-service payment company providing software and systems.<sup>4</sup> Wirecard was admitted to the TecDAX in 2006. "Wirecard's rapid rise in the German stock market was due to a perception that Wirecard services were growing worldwide, particularly in Asia."<sup>5</sup>

The first allegations of irregularities in Wirecard's balance sheet were made as early as 2008.<sup>6</sup> Markus Straub, Chairman of the German Protective Community for Investors (shareholders' association, Schutzgemeinschaft für Kapitalanleger (SdK)), made vehement allegations at Wirecard's Annual

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<sup>2</sup> Cf. Betz/Kim: Economic regulation and corporate governance: The case of Wirecard Institute for policy models, Seattle, WA, USA, Department of International Business, Keimyung University, Keimyung University, Daegu, South Korea *Modern Economy*, 2021, 12, pp. 1386–1423, <https://www.scirp.org/journal/me>, p. 1387.

<sup>3</sup> See Hesse (April 30, 2016): Finanzmärkte: Die Schlacht um Wirecard – Wette auf den Absturz (D. Spiegel, ed.); *Der Spiegel* (18/2016), pp. 65–67.

<sup>4</sup> See McCrum (June 25, 2020): Wirecard: The timeline (T. F. Times, ed.); retrieved on July 23, 2020 from <https://www.ft.com/content/284fb1ad-ddc0-45df-a075-0709b36868db>. Cf. Orlandi: The Wirecard case: Challenges for German and European supervision, working paper Luiss University Rome, Department of Economics and Finance, Chair of Market Law and Regulation, Coordinator Prof. Paola Lucantoni, Advisor Prof. Mirella Pellegrini, Academic Year 2020/2021.

<sup>5</sup> Cf. Betz/Kim: Economic regulation and corporate governance: The case of Wirecard Institute for policy models, Seattle, WA, USA, Department of International Business, Keimyung University, Keimyung University, Daegu, South Korea *Modern Economy*, 2021, 12, pp. 1386–1423, <https://www.scirp.org/journal/me>, p. 1388.

<sup>6</sup> See Krüger (July 23, 2020): EY, was soll das? FAQ on the Wirecard scandal (t. V. GmbH, ed.); retrieved on July 29, 2020 from <https://taz.de/FAQ-zum-Wirecard-Skandal/!5695456/?goMobile2=159408000000>. See also Möllers: The Wirecard accounting scandal in Germany, and how the financial industry failed to spot it; *The International Lawyer*, vol. 54, no. 3, 2021, pp. 325–360, 328.