



Financial Reporting Council



What Makes a Good...

Smaller PIE Audit Firm

**Sharing good practice and expectations of
audit firms seeking to scale up in or enter
the PIE audit market**

May 2023

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Foreword



Sarah Rapson
Deputy Chief Executive and Executive Director of Supervision

The FRC is an improvement regulator and is committed to supporting firms build their capacity and capability in the public interest entity (PIE¹) statutory audit market. This is vitally important in order to improve audit quality, competition and choice.

As we reported in our December 2022 [Tier 2 and Tier 3 Audit Firms Inspection and Supervision report](#), while currently only 13% of PIE audits are conducted by these firms, their share of the market is growing. Opportunities in the PIE market are increasing as more entities are inviting a wider range of firms to tender for audits and larger audit firms are adjusting their audit portfolios for commercial, resource-related or other reasons. We also reported that, based on our inspection of a sample of audits, there is an unacceptable gap in audit quality between the PIE audits conducted by Tier 2 and Tier 3 firms and those conducted by Tier 1 firms.

The FRC wishes to see a more resilient market with a pipeline of firms capable of entering and growing in the PIE audit market, including taking on audits of greater complexity, while performing high-quality audits. However, firms tell us that they do not understand enough about what good looks like and that they feel daunted by the FRC's regulatory approach.

To address these challenges we are increasing our support for Tier 2 and Tier 3 firms and expanding it to firms that are looking to enter the PIE audit market (which we refer to as Tier 4). A key element of this additional support is the Audit Firm Scalebox, which we announced in December 2022. We are launching the Scalebox project along with this publication. We are also developing additional ways to drive quality improvements, by sharing more good practice and forward-looking insights from our work at all firms.

High-quality audit requires all elements of the audit ecosystem to be functioning effectively. At the same time as calling on audit firms to rise to the challenge of conducting high-quality audits, we also call on the preparers of financial statements, to focus on producing high-quality information, and on their Audit Committees to focus on prioritising audit quality. The firms at whom this publication is aimed often rely on third-party service providers to conduct quality control and other functions and we also call on such providers to ensure that their services meet the quality standards that we expect.

¹ In the UK, PIEs are defined in Section 494A of the Companies Act 2006 and Regulation 2 of The Statutory Auditors and Third Country Auditors Regulations 2016 (Satcar).



We wish to see a strong pipeline of firms capable of performing high-quality PIE audits and we are increasing the support we offer to firms

1. Introduction

This document is aimed at firms that plan to enter the PIE audit market, or currently have a small PIE audit portfolio. It provides:

- An overview of what we expect firms to focus on to ensure that their audit practice is capable of performing high-quality audits. This includes insights from our supervision of audit firms and areas for firms to focus on as they grow - both in terms of what they should do and things to avoid doing (section 2).
- A guide to how the FRC regulates PIE audit firms covering:
 - What firms need to do to register with the FRC as a PIE auditor and their ongoing obligations (section 3). Registering with the FRC is the first step that a firm must take before it becomes the statutory auditor of any PIEs.
 - What to expect from supervision and inspection by the FRC, including how our inspections of a firm's audits or its quality monitoring system may differ from the approach taken by a firm's Recognised Supervisory Body (RSB) (section 4).
 - How the FRC's Enforcement process works, and how to manage some of the challenges an investigation may bring (section 5).
 - New initiatives from the FRC to provide more support to firms, including our new Tier 4 and the Audit Firm Scalebox (section 6).

While the focus of this document is on PIE audits, the FRC expects high-quality standards to be applied to all audits. These should be underpinned by a robust system of quality management developed in accordance with International Standard on Quality Management (UK) 1 (ISQM 1) and in compliance with the ethical standards (currently the Revised Ethical Standard 2019).

Nothing in this document should be interpreted as suggesting that it is acceptable for quality standards to vary between PIE and non-PIE audits or that it replaces or qualifies the requirements of UK auditing standards and associated guidance issued by the FRC.

The FRC is keen to engage openly with firms. Registered PIE audit firms may contact their Supervisor or our Registration team to discuss any queries they have about the FRC's regulatory approach and our expectations. Firms thinking of registering as PIE audit firms for the first time may contact our Registration team (registration@frc.org.uk) or the Scalebox team (scalebox@frc.org.uk) to find out more about the registration requirements and the help that the Scalebox may be able to offer.

Firms may also consult the wealth of resources published by the FRC covering our inspection and supervision findings and our enforcement outcomes (both identifying issues to avoid), and what good looks like. Links to recent relevant publications are included in the Appendix.



Aimed at firms that plan to enter the PIE audit market, or currently have a small PIE audit portfolio

2. Delivering high-quality PIE audits

Introduction and context

What is high audit quality

The FRC defines high-quality audits as those that:

- Provide investors and other stakeholders with a high level of assurance that financial statements give a true and fair view.
- Comply both with the spirit and the letter of auditing regulations and standards.
- Are driven by a robust risk assessment, informed by a thorough understanding of the entity and its environment.
- Are supported by rigorous due process and audit evidence, avoid conflicts of interest, have strong audit quality processes, and involve the robust exercise of judgement and professional scepticism.
- Challenge management effectively and obtain sufficient audit evidence for the conclusions reached; and
- Report unambiguously the auditor's conclusion on the financial statements.

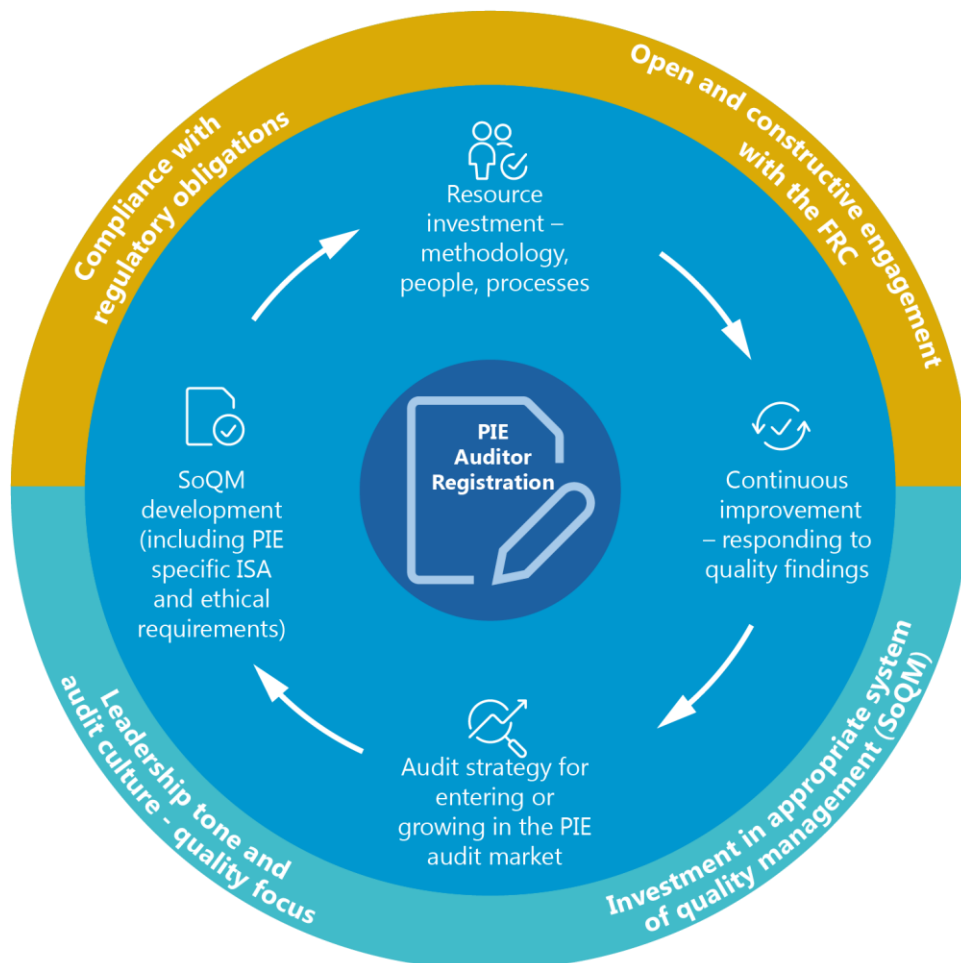
These fundamental quality principles apply to all audits, whether of a PIE or a non-PIE. While all audits must be approached individually, particular factors to consider in the planning and execution of a PIE audit may include:

- The **size and complexity** of the entity including, for example, its structure and the existence of overseas components.
- The **nature of the entity's business**, internal control environment and transactions, and the **basis of accounting** (potentially International Financial Reporting Standards (IFRS) rather than UK Financial Reporting Standards (FRS)).
- The extent and types of **technical and sector-specific knowledge** and skills needed.
- The need for **expert or specialist input**, including technical support for the audit team.
- The audit approach including when a **controls-based approach** may be appropriate.
- The extent of **judgements and estimates** in the financial statements.
- The **laws and regulations** applicable to an entity that is listed or operating in a regulated area such as banking, financial services and insurance.
- The level of **sophistication of the entity's management**, including the adequacy of the information they prepare for their internal reporting and for the audit.

Findings in the above areas feature heavily in our inspections of audits at firms with smaller PIE audit portfolios.

The foundations that will enable a firm to deliver consistently high-quality audits across its entire audit portfolio include:

- The firm's leadership demonstrating an appropriate '**tone from the top**' that focuses on embedding an environment that **develops audit as a specialism** and **is focused on audit quality and continuous improvement**. The firm's culture must **support the development and exercise of the right mindset and behaviours** by audit teams to **ensure appropriate professional scepticism and challenge**. Poor quality auditing of judgement and estimates, which require audit teams to gather evidence to corroborate management's representations and apply appropriate professional scepticism and challenge, is one of the most common areas of findings in inspection work carried out by the FRC and the RSBs.
- A system of quality management (SoQM), developed in accordance with each of the elements of ISQM 1, that is **appropriate to the firm's current and prospective audit portfolio**. While a firm's historical approach under International Standard on Quality Control (UK) 1 (ISQC 1) may provide a reasonable platform for its SoQM under ISQM 1, the latter is more principles-based and requires in-depth thought, rather than a checklist approach.



Our supervision and inspection work has demonstrated that, before a firm enters or scales up in the PIE audit market, it must also:

- Develop a cohesive audit strategy and business plan, including ensuring that audit acceptance and continuance decisions are appropriately targeted and within the firm's capacity and capability.
- Develop its SoQM to accommodate the changing nature of its audit portfolio. When entering the PIE audit market, this will include developing and embedding appropriate procedures to comply with:
 - More **stringent ethical requirements**, in particular regarding: the nature and level of allowable non-audit services (NAS); rotation requirements for the firm; the Responsible Individual (RI) and other members of the engagement team.
 - Expanded review requirements, including the need for an **Engagement Quality Control Review (EQCR)** to be conducted (in accordance with ISQM (UK) 2 Engagement Quality Reviews, also effective from 15 December 2022).
 - Additional **reporting requirements** in relation to both the content of the audit report, reporting to those charged with governance and, potentially, to a regulator.
- Ensure that it has adequate capital to make the necessary **investment in new or additional resources** including: **methodology** - many of our inspection findings are linked to deficiencies in a firm's audit methodology, such as the approach to controls testing and data analytics that may be more relevant in audits with greater complexity; and **people** resources, both front-line audit teams and the support available to them.

In the following section we look at the requirements of ISQM 1 in more detail. These are complex and it is beyond the scope of this document to provide a comprehensive analysis of every aspect of what makes a good audit firm.

In the table on page 9 we set out a selection of specific good practices we have seen and we consider likely to be most impactful in improving audit quality.



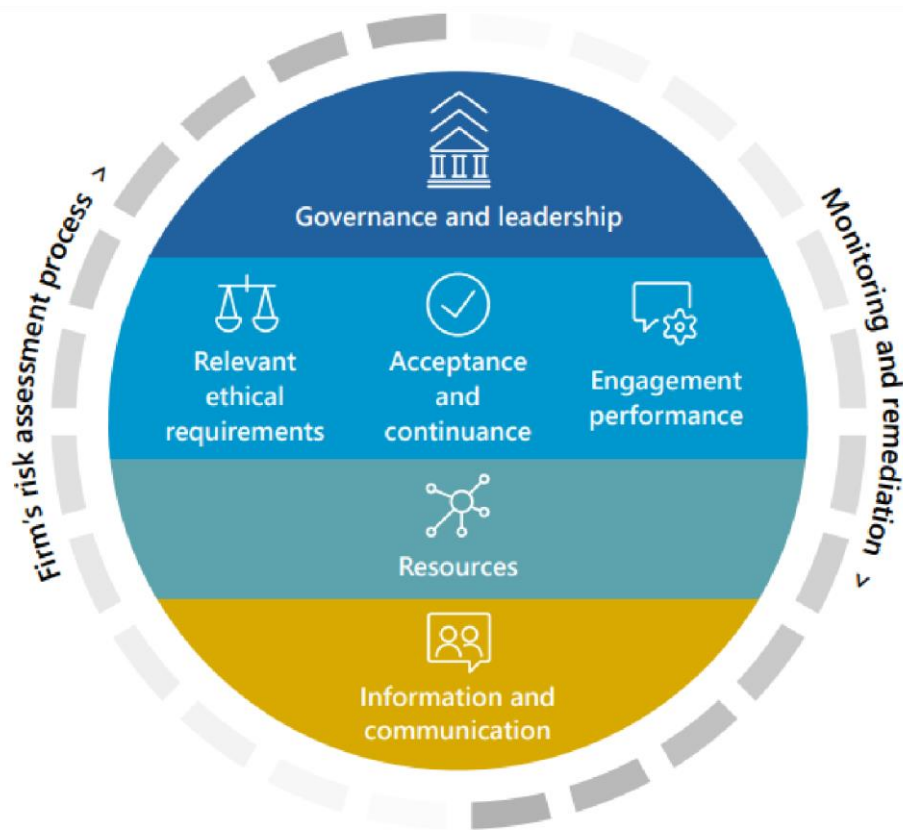
Firms must ensure that they have fully understood and embedded procedures to comply with PIE-specific ethical requirements

Aspect	Good practice
Culture	<ul style="list-style-type: none"> • A desired culture that promotes the purpose of audit and supports challenge by audit teams, as well as an internal 'speak up' culture. • Leaders exhibit the desired culture, and the employee experience is aligned to it. • The culture is regularly assessed and action taken to remove barriers to embedding the desired culture.
Governance and leadership	<ul style="list-style-type: none"> • Individuals in key governance roles are not overstretched (for example, by also having sizeable audit portfolios). • Leaders have sufficient management information to assess and oversee audit quality both across the audit practice and on specific engagements.
Ethical requirements	<ul style="list-style-type: none"> • The ethics function has well-documented roles and processes, particularly around NAS and length of tenure. • Consultation requirements are clearly mandated and consultations are properly recorded.
Acceptance and continuance	<ul style="list-style-type: none"> • Audit growth is targeted to types of entity and sectors where the firm has sufficient available resources and the necessary expertise. • Regular reviews are undertaken to assess whether the audit portfolio is aligned to the firm's risk appetite and its resources (quantity and experience).
Resources - methodology	<ul style="list-style-type: none"> • Guidance for audit teams is readily accessible and embedded within the audit methodology where possible. • Off-the-shelf audit methodology is augmented by bespoke procedures for more complex audit areas, PIE-specific requirements and entity-specific issues.
Resources - people	<ul style="list-style-type: none"> • Individual RI portfolios are regularly reviewed and aligned to their skills and capacity. • Audit quality is assessed as part of partner and staff appraisals and linked to reward and recognition. • A holistic, mandatory training programme covers technical and soft skills, including how to challenge management.
Audit team support	<ul style="list-style-type: none"> • Investment in sufficient, appropriately experienced technical resources and other processes that support audit quality, such as risk panels, in-flight or cold reviews, with appropriate action taken to address findings. • Where services are outsourced, evidence as to the quality of the service provider is gathered and assessed.
Root cause analysis (RCA)	<ul style="list-style-type: none"> • A structured approach that drills down sufficiently to the real underlying root cause (e.g., a '5 whys' approach) and is conducted on a timely basis. • Openness and honesty in the process, not apportioning blame. • Including successful audits in the process to understand what went well. • A clear feedback loop into remedial actions and the assessment of their effectiveness.

We are developing additional workshops and briefings focused on the above areas and others where we have common findings, such as the audit of revenue, to provide more information on what good looks like. All firms in Tier 2 and Tier 3 will be invited to these events. The Scalebox will also be able to provide support in these areas to Tier 4 firms (refer to section 6).

ISQM 1 in more detail

ISQM 1, which applies to all firms from 15 December 2022, introduced a new framework and requirements for a SoQM applicable to all audit firms, as summarised in the diagram below.



In the following tables we look at each element of ISQM 1 and highlight areas of focus for firms seeking to enter or grow at the smaller end of the PIE audit market. Our commentary below is not intended to be exhaustive or directional. Firms must take account of all the relevant requirements and should consult other sources of information, including FRC publications and guidance issued by their RSBs to develop a system appropriate to their audit practice.

Recent FRC publications of particular relevance include:

- [Tier 2 and Tier 3 Audit Firms: Audit Quality Inspection and Supervision Report](#): this report sets out findings and good practice in audits conducted by Tier 2 and Tier 3 firms (December 2022).
- [What Makes a Good Environment for Auditor Scepticism and Challenge](#): this report sets out the key attributes of an environment that supports professional scepticism and challenge (November 2022).
- [Professional Judgement Guidance](#): this report provides a framework to assist audit teams to improve their understanding of areas where the application of professional judgement is most critical, and the quality of their judgements (June 2022).

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- [What Makes a Good Audit](#): this report sets out examples of good practices we have seen across the elements now within ISQM 1 (November 2021).

Governance and leadership

Governance and leadership structures and behaviours are key for all audit firms. In particular:

- The individuals assigned ultimate responsibility and oversight for the SoQM must be sufficiently senior and knowledgeable about the ISQM1 requirements and functioning of the firm's SoQM.
- There must be mechanisms for those deemed responsible for the SoQM to be held accountable, including reflection in their appraisals and remuneration.
- Leaders are expected to prioritise quality in their strategy, communications and business decisions.
- A firm moving into the PIE audit space must ensure that its strategy and investment in human and technical resources is aligned with attaining audit quality objectives.
- The firm must embed a culture that promotes and incentivises audit quality, including through its remuneration and promotion processes.

Risk assessment process

All audit firms must identify their quality objectives and perform a full assessment of possible risks to their objectives, considering their likelihood and impact, and then identify mitigating responses. Firms looking to enter or grow in the PIE audit market must ensure that their quality objectives and risks clearly reflect their intended strategy and that:

- Risks identified are sufficiently granular so that the firm can fully identify what could go wrong and develop appropriate responses.
- Responses are mapped to all risks to show how the nature and frequency of the response mitigates the risk to an acceptable level.
- There is a process to regularly revisit the risk assessment in light of issues that arise, changes to the firm's circumstances and audit portfolio (including an increase or decrease in PIE audits) and changes in the wider macro-environment.

Acceptance and continuance

While the overarching principles are the same for PIE and other audits, when accepting and continuing PIE audits a firm must assess the additional risks and challenges to ensure that they have, or will be able to, develop or access sufficient and appropriate resources. Firms must also consider their ability to comply with the additional ethical requirements for PIE audits (see above).

Further additional considerations for PIE audits may include:

- Assessing the capacity and expertise of RIs and staff, to ensure they have the right experience, training and access to necessary specialists and experts.
- The RI being registered with the FRC and, along with the audit team, having sufficient relevant experience, including in relation to IFRS where this applies. Where there are experience gaps, the firm must upskill the team.
- Whether the firm has sufficient technical resources to support the audit team.
- Ensuring the firm has appropriate methodology and guidance covering all the requirements of the UK's International Standards on Auditing (ISAs) including the PIE-specific requirements and additional augmentations to cover any entity-specific issues, such as complex transactions.
- Whether the entity has international operations, which may be more likely for PIEs. The firm must assess component auditors and consider carefully how it will instruct, supervise and review a component auditor's work, particularly if it is not part of the firm's network.
- Considering the governance and control framework, the integrity of management and those charged with governance, and the ability to rely on information prepared by the entity. This may include understanding why management are looking to change auditors, obtaining sufficient understanding of the entity's business and public profile, and assessing any attendant risks.

Engagement performance

Focus areas for supporting high-quality PIE audit engagement performance include:

- Developing policies on when consultations are required and embedding a culture of consultation, so that the audit team obtains input from relevant specialists in relation to, for example, audit or accounting technical matters, ethical considerations, disclosures and the contents of the extended audit reports required for PIEs. Consultations must be evidenced and procedures must be in place to ensure that the outcomes have been appropriately actioned.
- Ensuring there is a culture of timely and engaged review of audit work by senior staff and partners and that processes, guidance and training are in place to promote this.
- Developing a "hot" or "in-flight" review programme to support audit teams, with an appropriate focus on complex audits and areas of historical quality findings.
- Having access to a pool of appropriately trained and skilled EQCRs. The firm must also have adequate processes to identify which audits require EQCRs (all PIE audits) and to allocate an appropriate EQCR to each one, taking into account the nature of the audited entity and the EQCR's experience.
- Ensuring that audit teams are equipped to prepare the extended reporting required for PIE audits to those charged with governance. Reports must be timely and sufficiently informative.

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- Ensuring that audit procedures are completed by the date of signing the audit report with no further changes to the audit file made after the archiving date, except for administrative purposes, over which there must be adequate controls and transparency.
 - Ensuring that the firm's audit software enables an audit file to be frozen at the archiving date.

Resources

Adequate resources are essential for all audit firms. When entering or growing in the PIE audit market, firms must consider specifically how their resources are appropriate for PIE audits.

This will include:

People

- Ensuring that audit staff and partners are appropriately trained, with sufficient ongoing training to respond to changes in technical accounting and auditing standards, and to quality issues and findings that arise. Where firms are looking to enter or grow in the PIE audit market, they need to ensure that sufficient staff and partners receive training on the technical, ethical and regulatory requirements for PIEs, including IFRS requirements.
- Monitoring the content and effectiveness of training, to ensure it is responsive to the needs and activities of the audit practice, reflecting changes to the firm's audit portfolio.
- Providing staff and partners within the audit team with soft skills training to ensure their ability to challenge management and to raise challenges internally.
- Developing appraisal, remuneration and promotion processes that incentivise audit quality above commercial factors so that people can see what the firm values. Firms should also consider using ad-hoc and non-financial recognition schemes to encourage a culture of calling out and rewarding quality on an ongoing basis.
- Actively assessing and monitoring their own culture to ensure it promotes quality and challenge.

Technology

- Ensuring the audit software and methodology used by the firm drives compliance with the ISA requirements and the firm's policies, for example through embedded audit workpapers and prompts for key planning and completion procedures. The audit software should prompt additional audit and reporting requirements for PIE audits. If this is not in-built, the firm must develop additional PIE-specific procedures.
- Developing audit workpapers that adequately address considerations specific to the entity and prompt the audit team to develop entity-specific procedures as well as evidencing the work they have performed and the conclusions reached. Checklist approaches are unlikely to be sufficient.
- Developing specific workpapers for complex audit areas to support engagement performance in terms of the extent and depth of procedures required and how these are evidenced.

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- Developing templates for audit reports and reporting to those charged with governance, including ones that address the additional reporting requirements for PIEs.
 - Ensuring disclosure checklists are high quality and easy to use and that sufficient procedures are performed (and evidenced) to support complex or significant disclosures.
 - Ensuring audit software can be, and is, consistently used to monitor changes to audit files after the audit report is signed.
 - Ensuring compliance with archiving deadlines and that archived files can only be amended in limited circumstances, for administrative purposes.
 - Considering what audit tools would be beneficial to the audit practice, for example, for data analytics, planning and concluding analytical procedures, and facilitating access to relevant market, industry and financial information.

Network resources and service providers

- Smaller audit firms may be more likely to rely on external service providers (or their international networks) in relation to, for example, audit software, methodology, EQCR services and quality monitoring.
- Firms must identify all such providers that form part of the firm's system of quality management, understand how they are used in the system and assess their significance.
- For each provider, the quality risks must be adequately assessed to ensure the service can be relied upon for the purpose used and that action is taken to mitigate any quality risks.
- Firms will need to consider what information they need from service providers and networks, or other sources, to perform this assessment.

Monitoring and remediation

This is an area of focus under ISQM 1, with new requirements to monitor the effectiveness of the firm's responses to risks, consider a range of sources to identify deficiencies, and undertake RCA to understand and assess deficiencies. A firm must:

- Strengthen its internal quality monitoring (IQM or cold file reviews) of completed audit files to ensure adequate coverage of PIEs and other high-risk audits as well as higher-risk audit areas, such as those involving judgements and estimates, and areas of historical quality findings. The monitoring process must include a focus on the extent and adequacy of how the audit team has challenged management. Cold file reviews should be graded and remedial actions devised to address quality issues. Good practice should also be identified and appropriately shared.
- Test the effectiveness of its responses to quality risks to ensure these are operating effectively.
- Consider a wide range of inputs, including internal and external quality reviews, claims and complaints, and feedback from audit staff and partners when assessing its system of quality management.
- Undertake RCA to understand why quality findings and good practice have arisen. RCA must be undertaken on a timely basis and involve a range of individuals and perspectives.
- Design and implement remedial actions to address the root causes of findings or share and embed the key factors driving good practice. The effectiveness of actions taken must be monitored.

Information and communication

Particular considerations under this section of ISQM 1 include:

- Ensuring the firm's policies, guidance and templates are easy to access and navigate. Policies must clearly reflect procedures relating to PIE and non-PIE audits. Firms should also aim to develop firm-specific policies and guidance, not merely replicating the contents of the ISAs, the Ethical Standard or other requirements.
- Promoting the sharing of information and insights across the audit practice, for example through regular bulletins, training sessions or other events. The use of 'real time' examples or case studies, in relation both to lessons learned and good practice identified, can be beneficial.
- Ensuring the firm's leadership has sufficient management information to monitor the system of quality management and identify concerns on a timely basis.
- Developing appropriate audit quality indicators (AQIs) in order to monitor individual audit engagements and the audit practice as a whole.

3. Registering as a PIE Audit Firm

Introduction and context

The FRC is now responsible for the registration of all firms that carry out statutory audit work on PIEs, in addition to the ongoing requirement for firms and RIs to register with their RSB. The FRC's registration remit includes firms and relevant RIs that audit one or more entities that are: UK incorporated and listed on the London Stock Exchange; a UK registered bank, building society or other credit institution; or, a UK insurance entity that is required to comply with the Solvency II regulations.

Firms must ensure that they have adequate procedures to identify whether an entity to be audited is a PIE. If there is any doubt about the status of an entity, you should discuss this with the management of the entity and, if you are unable to resolve the matter, contact the FRC.

All firms and RIs carrying out statutory audit work on PIEs were required to register with the FRC by 5 December 2022 under a set of transitional provisions.

Thereafter, any firm that plans to take on a PIE audit, or remain auditor to an entity that is to become a PIE, for example, if it obtains a listing on the London Stock Exchange, must register with the FRC, together with relevant RIs, before undertaking any PIE audit work.

In this section we summarise the key elements of the initial registration process, the steps a firm must take to maintain its registration and how the FRC may respond if we have concerns about audit quality at a registered PIE Audit Firm.

Further information on the registration process and requirements, including the PIE Auditor Registration Regulations (the Regulations), the PIE Auditor Registration Guidance (the Guidance) and other supporting documents may be found [here](#). There is also a link to the searchable PIE Auditor Register (the Register), which contains the names of all of the firms and RIs registered with us.

Registering for the first time

You must plan your registration application in good time before accepting an appointment to audit a PIE, or well in advance of an existing audited entity becoming a PIE if the intention is for your firm to remain in office. No audit work may be undertaken on a PIE until the FRC has granted a firm's registration. If any PIE audit work is undertaken while a firm is not registered, in breach of the Regulations, the FRC will consider if any action against the firm is warranted.

We aim to process registration applications within 25 working days of receiving all the information that we require. However, if there is complexity with the registration application, the process may take longer.



A firm must register with the FRC before conducting any audit work on a PIE

You should familiarise yourself with the [registration process](#), and contact our Registration team at registration@frc.org.uk to request an application form as soon as the firm decides to enter a tender process for a PIE audit, or as soon as it becomes aware that an existing audited entity will become a PIE.

When contacting us initially, you must provide us with the details of the PIE(s) and supply the name of the Principal Authorised Contact (PAC), who must be an RI registered with the firm's RSB and who is the person authorised by the firm to be the main FRC contact for registration purposes. The PAC will be provided with access to the FRC's Registration Sharepoint site for the purpose of uploading the completed application documents as set out below.

You will need to complete:

- A short application form in MS Forms format.
- A spreadsheet of RIs that the firm wishes to register. We expect firms to seek to register only those RIs that currently, or are scheduled to, act on PIE audits (additional RIs may be added after the firm becomes registered if circumstances change). Each RI must complete an MS Forms RI application and supply details of their experience as well as the Continuing Professional Development (CPD) they have completed and plan to complete.
- A spreadsheet showing all the firm's current and potential PIE audits (so far as known at the time) over the next 24 months and the RI that will be allocated to each audit.
- A supporting statement to explain in further detail how the firm meets the Registration Requirements in section 4 of the Regulations including:
 - The competence and experience of the firm in relation to PIE audits; details of fit and proper procedures in place.
 - The process to ensure that all staff involved in PIE audits are aware of the Regulations.
 - Details of how the firm ensures that it has sufficient financial and non-financial resources to enable it to undertake PIE audits; how the firm complies with ISQM 1.
 - Details of the firm's governance arrangements to ensure that it is suitable to operate a firm undertaking PIE audits.

Firms must ensure that they provide sufficient information in their supporting statement (not merely affirming that they meet the requirements). The Registration team will request further details if insufficient information has been provided and full processing of the firm's application will not begin until complete information has been given.

The FRC may determine that an application may only be granted if the firm (or an RI) accepts one or more Undertakings and/or Conditions on its registration.

The FRC may also refuse an application if there are concerns that the firm does not meet the registration requirements.

Maintaining your PIE Audit Firm or RI registration

Once a firm (and relevant RIs) have registered with the FRC, the firm must ensure that it complies with the Regulations at all times. If the registration has been granted with Undertakings and/or Conditions, the firm and/or RI must ensure that requirements relating to these Undertakings or Conditions are fully satisfied.

It is essential that the firm and audit staff remain familiar with, and meet, all the provisions in the Regulations. In particular, firms and RIs should be mindful of the following obligations (with reference to relevant sections of the Regulations):

- The registration requirements set out in Parts 4 and 5.
- If any additional RIs are required to undertake PIE audit work, each one must apply for registration via the MS Forms RI application and provide details of their competence and CPD (refer to Parts 6 and 7).
- If the firm ceases to undertake PIE audits, it should request its entry on the Register to be removed (and all of the RIs will also be removed). If an RI is leaving the firm or will no longer be undertaking PIE audit work, the firm should request that the RI's entry is removed (refer to Part 13).
- The firm must notify the FRC every six months of changes to information relevant to the registration requirements, including changes in the PIE audit portfolios of its registered RIs (refer to Part 15). The FRC will notify the firm of the dates that these updates are required when registration is granted.
- All PIE audit appointments and resignations should be notified to registration@frc.org.uk, and for resignations also to auditorresignation@frc.org.uk, within 10 working days of the change.
- Firms are required to submit an Annual Return to the FRC (refer to Part 16). The firm will be notified of the date that its Annual Return is required when its registration is granted. The Annual Return must be completed via MS Forms and accompanying information must be uploaded via Sharepoint. The FRC will conduct reviews of a firm's registration at regular intervals.

Further details of the ongoing registration requirements may be found in the Guidance. See also the panel below, which sets out additional ongoing obligations on PIE audit firms.



You must notify the FRC of any information relevant to your ongoing registration

As well as complying with its formal obligations, including the Regulations, relevant legislation, auditing standards, ethical standards and quality management standards, and any other regulations, procedures or rules published by the FRC, the FRC expects a firm to:

- Engage with the FRC in an open, cooperative and timely manner.
- Be transparent in its dealings with the FRC including disclosing at the earliest possible opportunity any issues that may be pertinent to the firm's registration or its conduct of PIE audits to a high-quality standard.
- Respond to FRC requests and enquiries in a complete, accurate and timely manner.

If a firm is unsure about any of the requirements, please contact us at registration@frc.org.uk.

How the FRC may respond to quality concerns

The FRC will monitor, on an ongoing basis, the circumstances of all PIE audit firms and RIs and will take into account information provided directly to the Registration team and evidence gathered through our supervision, inspection and other functions.

If the FRC becomes aware that a firm has failed to notify us of a change required by Part 15, or there is evidence that a registered firm or RI may no longer meet one or more of the registration requirements, it can consider:

- Agreeing Undertakings with the firm or RI.
- Attaching Conditions on the firm's or RI's registration.
- Suspending or involuntarily removing the firm's or RI's registration.

Which option is adopted will be dependent on the nature and seriousness of the issue.

Additional ongoing obligations

PIE audit firms have a number of specific obligations including:

- **Reporting breaches of ethical requirements to the FRC:** Firms must have in place appropriate procedures to prevent and detect breaches of ethical requirements, including the specific (and more restrictive) requirements for PIE audits. Firms must submit ethics breach reports biannually to the FRC (within two months) and make interim reports if significant breaches are identified. Details of the process for submitting ethical breach reports to the FRC may be found [here](#). We review all the ethical breach reports we receive and may make further enquiries with a firm to understand more about a breach or its causes. Significant breaches may be referred to the FRC's Case Examiner to consider whether further action should be taken (refer to page 27 for more information on the work of the Case Examiner).
- **Preparing and publishing an annual Transparency Report:** The Transparency Report must comply with rules mandated by EU Regulation 537/2014 Article 13 (which have been retained by the UK on leaving the European Union) and the reporting requirements set out in the **Audit Firm Governance Code 2022 (AFGC)** if it is adopted by the firm. If a firm has issued an audit report on one or more major local audits, it must also comply with The Local Auditors (Transparency) Regulations 2020. The Transparency Report must be published within four months of the firm's year end. The FRC regularly reviews whether firms have complied with their Transparency Reporting obligations. As well as providing firms with feedback on their reports, the FRC may take more formal action if there is significant non-compliance.
- **Applying to the FRC for exemptions or extensions:** Firms may apply to the FRC to request an exemption to the cap on NAS or to extend the maximum duration of an audit engagement. Such applications are expected to be rare and must be made in advance of any actual breach of the requirements. We cannot approve retrospective applications. More details of the FRC's policy and processes in this area, as well as details of exemptions previously granted, may be found [here](#).

The FRC also expects firms that audit 20 or more PIEs (or one or more FTSE 350 entities) to apply the **AFGC**. If a firm chooses to apply the AFGC it must comply with all the principles, and it must 'comply or explain' in relation to each of the provisions. Firms should consider carefully the principles and provisions and where they may be able to enhance their governance processes. Particular parts of the AFGC where firms considering applying it may need to develop their structures or processes include:

- Appointing Independent Non-Executives (INEs) and developing and publishing the firm's policy for dealing with disagreements between the firm's executives and its INEs. The firm's Transparency Report should also disclose the remuneration of its INEs.
- Conducting evaluations of the performance of key individuals and governance bodies.
- Making additional disclosures in the firm's Transparency Report, and developing the underlying processes where necessary, including the names of individuals on the firm's governance bodies, the key performance indicators used to assess the effectiveness of the firm's governance, and details of the firm's code of conduct.

More information on the requirements of the AFGC may be found [here](#).

4. What to expect from supervision and inspection by the FRC

Introduction and context

As the UK Competent Authority for statutory audit, the FRC is required by law to oversee the conduct of UK statutory audits and the firms that undertake them. The FRC has retained responsibility for PIE audits and PIE audit firms (as well as certain other categories of audits) with monitoring of the remaining audits and firms (including their registration) having been delegated to the RSBs.

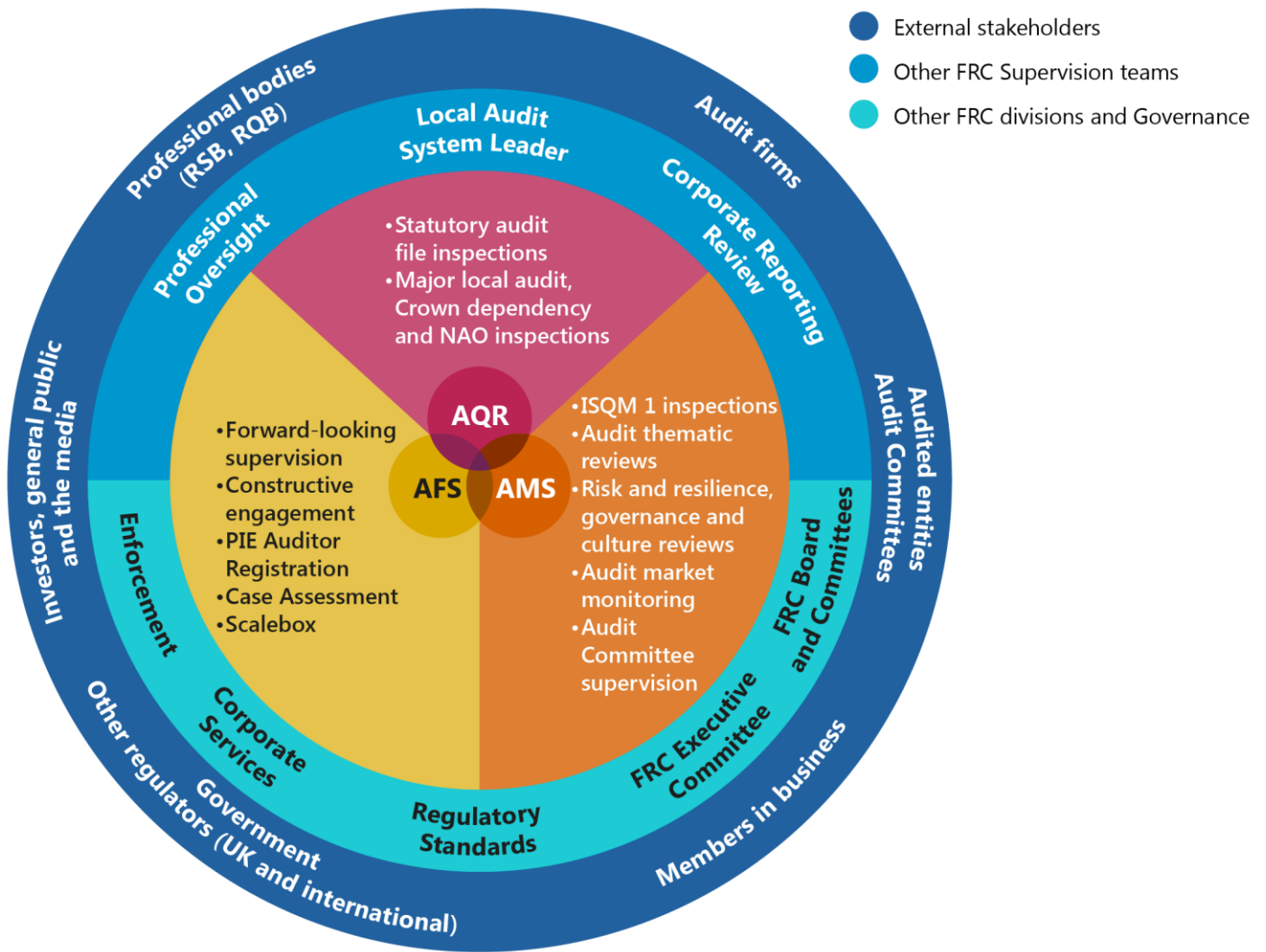
Non-PIE audit firms will be accustomed to monitoring visits by their RSB. These visits include the review of individual audits, the firm's quality monitoring procedures and other aspects of the RSB's regulations.

The FRC's Professional Bodies Supervision team ([PBS](#)) conducts an in-depth programme of work with the RSBs so that the FRC may be satisfied that the work performed by the RSBs meets the delegated requirements. PBS tailors its oversight work to explore the existence of perceived differences between the RSB and FRC oversight regimes. Where differences are identified, the impact will be assessed, and proportionate actions proposed to bring greater consistency.

The FRC conducts a range of supervision and inspection activities with PIE audit firms, which may differ in process and scope to those conducted by the RSBs.

For example, on average, it takes approximately one month to complete the fieldwork for an inspection of a PIE audit conducted by the FRC's Audit Quality Review team (AQR). Firms may find that our inspection takes longer than one conducted by their RSB. Reasons for this include differences in the underlying nature and complexity of PIE audits and the extent of our interactions with the audit firm and the RI. During the inspection, AQR inspectors will have numerous formal and informal meetings with the RI and engagement team.

The [Our Approach to Audit Supervision](#) document, republished by the FRC in March 2023, provides an overview of the FRC's audit supervision teams and processes. The diagram below shows how these teams work together, with other FRC stakeholders and external stakeholders, to enable the FRC to obtain and communicate a holistic view of firms and PIE audit quality.



In the following sections we set out further details of our supervision and inspection work with a focus on what firms entering or acting at the smaller end of the PIE audit market should expect. We also draw out where our processes may differ from those of the RSBs.

Supervision

The Audit Firm Supervision (AFS) team was set up in 2020 and has developed a comprehensive approach to supervision that will be new to firms that have previously been regulated only by their RSB.

AFS now comprises four separate functions:

- The Supervisor team, which leads our forward-looking supervision work and also conducts constructive engagement enquiries.
- The Registration team (refer to section 3).
- The Case Assessment team led by the FRC's Case Examiner (refer to the panel below).
- The new Audit Firm Scalebox team (refer to section 6).

The Supervisor team develops evidence from its own work and brings together the work of all other relevant FRC teams, as well as external parties such as the RSBs, to:

- Develop a holistic picture of audit quality at a firm.
- Assess where a firm needs to improve, deliver relevant supervisory messages to the firm and hold the firm's leadership to account for acting on those messages.
- Share lessons and good practice from our work across the PIE audit market.

To reflect the differing nature of PIE audit firms, their PIE audit portfolios and their impact on the UK public interest, we adopt a scaled, proportionate approach to supervision by dividing the firms we supervise² into three tiers - Tier 1, Tier 2 and Tier 3.

In the following sections we explain in more detail how we allocate a firm's tier, how we supervise Tier 2 and Tier 3 firms, and what we expect from firms.

Tier 4 firms are not subject to any formal supervision or inspection work. How we engage with Tier 4 firms is explained further in section 6.

Tier allocation

Firms are divided into tiers primarily to reflect their impact on the UK public interest.

Tier 1 firms will be those whose audit portfolio has a significant impact, both in terms of the number of PIE audits it conducts and the nature of those audits. Current Tier 1 firms audit, between them, the majority of the FTSE 100 and a significant majority of the FTSE 250, as well as some of the largest banks and insurance entities. While certain Tier 1 firms' PIE audit portfolios may not be larger than some firms in Tier 2, their inclusion in Tier 1 reflects their presence in sectors of systemic importance (such as banks and major local audits) and other factors such as growth plans and our assessment of risk.

Tier 2 firms will be those that do not meet the criteria for Tier 1 but have a significant presence in the PIE audit market, usually at least 10 PIE audits and often more than 20 (meaning that the firm falls within the scope of the AFGC). Our assessment also takes account of risk factors specific to the firm or its audit portfolio.

Remaining UK PIE audit firms are allocated into Tier 3. The majority of Tier 3 firms at present have fewer than 10 PIE audits, with many of them having only one.

² AFS's supervision work is directed at UK audit firms. AFS does not currently supervise non-UK firms that audit UK PIEs or the National Audit Office (NAO) and its RIs. These latter entities are required to register with the FRC as PIE audit firms and are subject to formal inspection.



Our supervision teams focus on developing a holistic picture of audit quality at a firm, holding firms to account for making the necessary improvement and sharing good practices

We reassess a firm's tier on an annual basis and inform the firm accordingly, usually in or around April in any calendar year. Where we anticipate that a firm may move up or down a tier, we will aim to discuss this with the firm at the earliest opportunity to help it prepare for a change in status. For example, while our supervision work is approached on a proportionate basis, moving from Tier 3 to Tier 2 will entail more interaction between the firm and the FRC and so require the firm to commit additional resources to engagement with the FRC (albeit significantly less than the requirement on a Tier 1 firm).

We seek to avoid a situation where a firm frequently moves between tiers and will take a firm's longer-term plans into account in our decision-making.

How we supervise Tier 2 and Tier 3 firms

When a UK firm becomes a PIE audit firm for the first time, we will write to the firm explaining the tier that it has been allocated to (which will usually be Tier 3), drawing attention to key elements of our supervision process and reminding the firm of its ongoing obligations.

This first letter will also provide the firm with the names of its allocated supervision team, usually comprising a Supervisor and one other person. We will inform the firm should there be a change in its supervision team members.

The FRC works on years to 31 March and in the months leading up to that will plan the specific supervision (and inspection) activities to be conducted in the coming year. With the exception of statutory inspection work (where only short notice is given), we will usually write to all Tier 2 and Tier 3 firms in or around March of every calendar year to advise them of our anticipated programme of work for the year ahead.

This programme of work may be varied during the year to respond to risks or issues that arise. The specific work conducted at Tier 2 or Tier 3 firms may also vary to address firm-specific risks, for example where there are conditions or undertakings on the firm's registration that require closer monitoring.

The table on page 26 sets out an overview of what Tier 2 and Tier 3 firms can expect from our supervision activities.

In terms of how we report our supervisory work, most of our work at Tier 2 and Tier 3 firms is privately reported to the firm and may also be reported to other relevant FRC teams (including the Registration team) or third parties (including the firm's RSB). Specific audit inspection reports are also shared with the relevant Audit Committee Chair.

Tier 2 and Tier 3 firms will all receive an Annual Supervisory Letter (ASL), which sets out our view of the priority actions the firm needs to take to improve audit quality. We expect firms to respond to the ASL by putting forward an action plan to address each area that includes specific actions, a timeframe and who is



Firms that audit PIEs are divided into three tiers for supervision purposes - our supervision work in each tier is tailored and proportionate

accountable for the actions. We will monitor the progress on ASL actions periodically.

At present our public reporting comprises an annual report providing an overview of our inspection activities at Tier 2 and Tier 3 firms. This does not comment specifically on our work or findings at specific firms.

What we expect from firms

In contrast to our statutory obligations regarding registering PIE audit firms and RIs (refer to section 3) and inspecting PIE audits and PIE audit firms' systems of quality monitoring (which we explain in the next sections), our supervision work is not currently a statutory requirement.

However, we expect firms to acknowledge the benefit that FRC supervision may bring to their audit quality and the resilience of the firm and to engage with us openly, transparently and promptly.



We expect firms to engage with our supervision teams in a transparent and open manner

	Tier 2 firms	Tier 3 firms
Supervision		
Reviewing a firm's audit strategy and audit quality plans	We will aim to discuss these aspects with a Tier 2 firm at least once per year	At our discretion
Reviewing the process and actions being taken by a firm to monitor and remediate quality findings	We will aim to discuss the process aspects with a Tier 2 firm at least once per year and follow up on specific findings more frequently	We focus on how the firm is addressing specific quality findings
Constructive engagement, other audit-specific enquiries and non-financial sanctions monitoring	As required	As required
Formal engagement meetings	At least one meeting per year with the firm's Senior Partner/CEO, head of audit and INEs (where applicable)	At our discretion
Pre-appointment meetings	Head of audit, INEs	Not required
Risk Reporting Protocol (a requirement for the firm to report to us specific risks or issues as they arise)	Yes	No
Thematic reviews and reviews under our supervisory pillars (for example, relating to governance, risk and resilience, culture)	Typically, the inclusion in one or two reviews per year	Not typically included
Inspection		
PIE audit file inspections	Typically, we aim to inspect one audit per year or every other year, subject to our assessment of risk	Typically, one or two audits over a six-year cycle, with additional inspections to address risk
Inspections of the firm's system of quality management (ISQM 1)	Typically, we inspect a firm's complete system over a three-year cycle	Typically, we inspect a firm's complete system over a six-year cycle

The Case Assessment team

Responsibilities

The Case Examiner manages the Case Assessment team, which is responsible for:

- **Intelligence gathering activities:** identifying from publicly available information, referrals from other FRC teams (including in relation to individual audits and ethical breaches), and from complaints and referrals from third parties, including other regulators, whether there is information to suggest that an audit or any conduct by an audit firm or individual auditor warrants consideration under one of the FRC's enforcement schemes, usually the Audit Enforcement Procedures (AEP) or the Accountancy Scheme (the Scheme)³.
- **Making initial enquiries:** obtaining evidence sufficient to enable the Case Examiner, and the FRC's Conduct Committee, to conclude whether a matter should be referred to the FRC's Enforcement Division for an investigation (refer to section 5), is suitable for resolving by the firm's Supervisor through constructive engagement or whether no further action is required.

What to expect from an enquiry by the Case Assessment team

The primary steps in an enquiry by the Case Assessment team are as follows:

- The team will write to a firm when it opens an enquiry, to inform the firm and set out the next steps.
- We may request an initial meeting with the firm to clarify relevant aspects or may make a formal request for a firm to provide information and documentation by a certain date. Requests under the AEP are usually made by way of a Statutory Notice (a Notice).
- Further requests for information and documentation may be made at any time during the enquiry.
- We will consider all the information provided and consult with relevant parties within the FRC, including the Conduct Committee, about the appropriate outcome.
- If the outcome is that a matter should be referred formally to the Conduct Committee to consider opening an investigation, then the team will prepare a referral paper. Refer to section 5 for more information about the Conduct Committee and investigation process.
- If the outcome is that a matter is suitable for resolution through constructive engagement, the team will refer it to the relevant AFS Supervisor to resolve and the firm will be notified accordingly. AFS will make further enquiries with the firm and seek appropriate remedial actions to address and mitigate the risk of the issue recurring.
- If the outcome is that no further action is necessary, the firm will be notified and the enquiry will be closed.

What we expect from firms

Firms must co-operate fully with an enquiry by the Case Assessment team and provide the information requested in full and on a timely basis. If a firm considers that it may not be able to comply, it must inform the team at the earliest opportunity and not, for example, wait until the deadline for satisfying the request has been reached. We will take into account all reasonable requests for the extension of a deadline. The FRC may take formal action if the requirements of a Notice are not complied with.

Inspection of audit files

The FRC has a statutory responsibility to inspect the audit work conducted by firms. This inspection work on PIE audits is conducted by AQR. The FRC has delegated responsibility for the inspection of non-PIE audits to the RSBs. The RSBs are responsible for planning their inspection work but we engage with them with the aim of avoiding, where possible, FRC and RSB inspection visits occurring at the same time.

At Tier 2 firms, we aim to inspect at least one audit file a year or every other year, but this may vary according to our assessment of risk. At Tier 3 firms, our inspection work is usually cyclical and we will conduct an inspection at least every three or six years (in accordance with statutory requirements). Interim audit file inspections may also be undertaken to assess the firm's progress where there are conditions imposed on a firm's registration.

To the extent possible for firms with smaller PIE audit portfolios, our selection of audits for inspection will be informed by the areas of focus published by the FRC each year (most recently in [December 2022](#)). We will also take account of areas where we have common findings (for example the audit of judgements and estimates, going concern and revenue) and any audit or firm-specific risks we identify.

Our process and what we expect

A summary of our inspection process is set out on the next page. We assess completed inspections as falling into one of the following four categories:

- Good
- Limited improvements required
- Improvements required
- Significant improvements required

Audits assessed as requiring more than limited improvements are considered to have fallen below the standard we expect.

To ensure consistency across our inspections, all inspection reports are subject to a rigorous internal quality control process by an independent team within AQR. The process will challenge the views reached by the inspection team to ensure that the final conclusions reached are consistent, robust and appropriate

Notifying a firm

- Issue of a formal Notice to the firm with details of the file being inspected and the inspection timing.
- Arrangements made for delivery to the FRC of a laptop containing a copy of the audit files.
- Issue of a pre-inspection questionnaire that the firm must complete and return, together with supporting documents.



The file inspection

- An opening meeting with the engagement team to discuss the inspection (we also meet with the entity's Audit Committee chair).
- Regular informal meetings to discuss the inspector's questions as they arise.
- At the end of the inspection, formal queries are sent to the engagement team and we will take into account the firm's responses in finalising our findings.



Reporting

- We issue the firm with a draft report summarising our findings, the firm has the opportunity to comment on the findings before the report is finalised.
- The firm must develop appropriate remedial actions to address our findings.
- We hold a closing meeting which will explore any areas where the firm needs to strengthen its action plan.
- We then issue a confidential report containing the findings, the firm's actions and the grading of the inspection to the firm and Audit Committee chair.



During the inspection process firms are given various opportunities to respond to our inspection findings, and we will carefully consider all the points raised by a firm. If, at the conclusion of an inspection, a firm continues to have concerns regarding our final assessment, the firm may request a reconsideration. Reconsiderations are assessed by a panel of advisers independent to the FRC and a decision is reached by the Executive Director of Supervision.

Other important aspects of an inspection to bear in mind:

- Firms must comply with the requirements of a Notice and the FRC may take formal action if a Notice is not complied with.
- We will not notify a firm of a file inspection until after the archiving window has closed. It is important that firms comply with the requirements of their archiving policy which, in turn, must be compliant with ISQM 1 regarding engagement file archiving. Only fully archived files may be sent to the AQR team for inspection.
- While we accept that firms should defend their audit work where appropriate, we expect firms to engage openly with the FRC during the inspection process and listen to the messages that are being communicated by the inspection team.
- A common issue arising during inspections relates to the extent of audit procedures performed and judgements reached compared to the evidence on the audit files. We expect audit work to be fully detailed on the audit file and sufficient evidence recorded of the considerations taken into account to support the conclusion reached.
- We expect a firm to develop specific, appropriate and measurable actions that clearly address the inspection findings. Actions that do not meet these criteria, for example merely stating that a firm will 'consider' the point raised by AQR when conducting the following year's audit, are not sufficient.
- We engage with an entity's Audit Committee Chair during an inspection and share with them our inspection report. Firms can expect the Audit Committee Chair to engage with them to understand how the firm is addressing any inspection findings.
- We do not publicly report the outcomes of individual inspections but we publicly report a summary of [inspection findings at our Tier 2 and Tier 3 firms](#), as well as, from time to time, publishing specific, anonymised [findings and good practice](#).

Inspection of a firm's systems of quality management

The FRC has a statutory responsibility to inspect the design, implementation and effectiveness of firms' systems of quality management. For Tier 2 and Tier 3 firms, this work is conducted by our AQR team, alongside our Audit Market Supervision (AMS) team.

Our inspections under ISQC 1 have typically been conducted on a cyclical basis, usually every 3 years for Tier 2 firms and every 6 years for Tier 3 firms.

Our inspection approach under ISQM 1 is currently being developed but we will review how a firm:

- Has implemented ISQM 1.
- Has tailored its SoQM to its own circumstances, structure and audit portfolio, how this compares to our expectations and understanding of the firm, and how it compares to other firms.
- Monitors and evaluates its own system of quality management.

We will also focus our review on elements of the system that have changed since our previous review and areas we assess to be of higher risk.

We will notify a firm of a forthcoming inspection of its quality monitoring procedures. Our inspection process then includes the principal steps set out on the next page.

Important aspects of the inspection process to bear in mind include:

- The process is likely to be intensive and may extend over several weeks. We are likely to require a significant amount of time from the firm to gather and provide us with the documents we require and to respond to our questions. It is helpful for the firm to nominate a principal contact for the inspection and for all functional heads within the firm (for example, the Human Resources and Ethics and Independence personnel) to be available to fulfil any requests for information and provide explanations.
- We provide a firm with plenty of opportunity to discuss our findings and insights, which the firm may then use to develop appropriate actions.
- Consistent with the file inspection process, we follow a stringent internal quality control process that reviews all the findings we have raised.



We inspect all aspects of a Tier 2 and Tier 3 firms' system of quality management and will follow up on firms' action plans to address our findings

Information request

- The firm is notified about the inspection and an information request list is sent to the firm. In this information request list, we request copies of relevant policies, procedures and internal controls.
- For example, the firm's strategy document, governance structures, minutes of meetings, internal communications, training materials, internal monitoring reports, RCA reports, and its quality and remediating plan. We will also reviews the firm's annual evaluation required by ISQM 1.



The firm inspection

- We test the application of certain policies and procedures and request evidence for selected samples.
- For example, appraisal and promotion documents, remuneration processes, results of IQM and RCA, ethics consultations, technical consultations.
- We may test some of the firm's internal controls within its system of quality management.



Reporting

- We issue the firm with a report summarising our findings and recommendations (based on good practice we have identified at other firms) for discussion.
- The firm must develop remedial actions to address our findings.
- We also identify good practices that we have seen at the firm.
- We will discuss the firm's proposed actions, including timing.
- Once agreed, we will issue a final report to the firm.
- At a later date we may request evidence of these actions.



5. Enforcement at the FRC

Introduction and context

The FRC's [Enforcement Division](#) is responsible for investigating and taking enforcement action in relation to breaches of requirements or misconduct by auditors during the course of statutory audit work.

The FRC's primary regime for the enforcement of statutory audit-related matters is the [AEP](#), introduced in 2016. Certain audit-related matters may also be investigated under the [Scheme](#)⁴. Both the AEP and the Scheme differ significantly from the disciplinary schemes operated by the RSBs.

The work of the FRC's Enforcement Division is summarised and published annually in the Annual Enforcement Review (AER), usually in July. The AER provides a valuable insight into our approach to enforcement, the structure of the Enforcement Division, the outcomes of concluded investigations and the themes and trends identified.

The most recent and previous AERs may be found [here](#).

In this section we provide an overview of our investigation process, focusing on the AEP, and draw out key points in relation to how a firm may prepare for an investigation and what we expect from firms during the process.

Investigations

Once the FRC's Conduct Committee has decided that an investigation should be opened, a Notice of Investigation will be sent to the subjects of the investigation (usually the firm but individuals such as the RI may also be investigation subjects). A copy is also sent to the relevant RSB(s).

The case is referred to the FRC's Enforcement Division, which will set up a case team typically comprising one or two lawyers, one or two forensic accountants and a legal assistant.

How the investigation will proceed

One of the first actions the case team will take is to schedule a scoping meeting with the firm. The primary purpose of this meeting is to introduce the case team, provide high-level information about the scope and initial focus of the investigation, outline how the investigation will proceed and set out the expectations of the firm and individuals during the investigation.

The case team will also issue one or more Notices requiring the firm to provide relevant documents and information.

⁴ The FRC operates separate enforcement schemes relating to Local Audit, audits conducted by the NAO and audits of Crown Dependency entities. Further details may be found on our website.



The FRC's Conduct Committee is responsible for deciding whether an investigation is opened

We commonly request the following items:

- The relevant audit file(s) (including any review notes) both (a) on a laptop or Virtual Desktop Infrastructure, and (b) in a format that may be uploaded to our e-discovery platform.
- Details of any related files or documents other than those located on the audit file(s), including handwritten notes and workbooks.
- Details of the audit engagement partner (RI), EQCR and audit team members who worked more than a certain number of hours on the audit(s).
- Copies of relevant electronic communications (including emails, SMS and instant messages) relating to key individuals.
- Details of any advice or guidance sought from the firm's in-house technical department or other specialist departments in respect of the audit(s).
- Details of any other non-audit work carried out for the audited entity by the firm.

Additional information may be requested as an investigation proceeds.

The FRC also has powers under the AEP to compel individual auditors to attend the FRC's premises to be interviewed.⁵ The case team will provide details of the interview process and relevant documents in advance of an interview, to help individuals prepare.

Once the case team has obtained and reviewed all relevant available material and established the necessary facts, in most cases an independent expert opinion will be sought to assess whether there have been breaches of relevant requirements or misconduct.

If potential breaches or misconduct are identified, these will be set out in a report that is served on the firm. It will then have an opportunity to make representations. Following receipt of any representations, the FRC's Executive Counsel (which leads the Enforcement Division) will decide whether to pursue enforcement action. This could result in a public hearing before an independent Tribunal hearing. However, settlement is encouraged under both the AEP and the Scheme, and significant discounts to financial sanctions are available to firms where early admissions are made.

⁵ The FRC is also able under the Scheme, which is a contractual arrangement between the FRC and relevant professional bodies, to compel firms and individuals that are Members of relevant professional bodies to provide information and attend interviews.



We have powers to compel production of documents and information, and for individuals to attend for interview

Our expectations

Parties under investigation are expected to cooperate fully. This includes the need to:

- Comply with the requirements and deadlines set by the FRC in correspondence and in Notices.
- Proactively inform us, with full reasons, as soon as a party becomes aware that it may not be able to comply with a Notice, either in terms of supplying the information requested or meeting the deadline in the Notice. Requests for extensions to deadlines must be reasonable and adequately justified.
- Provide all documents and information in a format that complies with our technical and other requirements. Normally this means providing information in an electronic format that allows documents to be directly uploaded to our e-discovery platform. We provide firms with full details of our technical specifications.
- Develop a suitable process for identifying all the material that is responsive to our Notices so that the provision of information to the FRC is complete and timely.
- Ensure that any material subject to legal professional privilege (whether of the firm, the audited entity or any other party) is identified and handled accordingly.
- Respond to all FRC communications and requests in an open, transparent and timely manner (and request clarification should anything be unclear).
- Make time available to prepare for and attend interviews in accordance with the interview timetable and keep us apprised of any planned or unexpected unavailability of key members of staff during the course of the investigation.
- Allocate sufficient time and resources to the investigation.

Inadequate cooperation may be considered an aggravating factor when considering any sanctions to be imposed. The FRC may also take civil action to address non-compliance with a Notice issued under the AEP and in certain circumstances failure to comply may amount to a criminal offence⁶.

Conversely, where a party provides exceptional cooperation, such as self-reporting breaches, producing and sharing RCA and volunteering information or documentation not specifically requested but which may assist the investigation, this may be regarded as a mitigating factor that will reduce any financial sanction. An explanation of how sanctions are determined may be found in the [AEP Sanctions Policy](#) and the [Scheme Sanctions Guidance](#).

⁶ Under Schedule 2 of Satcar



Full cooperation during an investigation is essential and may have an impact on any sanction that is imposed

We understand that individuals subject to investigation may find the process unsettling and that our requirements during an investigation may pose issues for a firm that has fewer resources and less developed technology. It is therefore vital that any party under investigation communicates openly with us if they expect to experience, or are experiencing, issues so that a way forward may be agreed.

The scoping meeting will be the first opportunity to discuss any factors that the firm is already aware of that may pose issues, for example if the firm uses a paper-based audit system or if information likely to be relevant to the investigation is missing.

Matters to consider at the outset of an investigation also include:

Early instruction of legal representatives: It is advisable to seek legal advice as soon as possible once an investigation has been opened. In addition to providing legal advice, legal representatives can assist in various areas that may otherwise cause a delay to the investigation, for example identifying and dealing with privileged or personal data in the audit files and other responsive documents. Legal advisers may also be able to provide personnel to assist with reviewing documents before they are provided to the FRC.

Production of audit files: It is important to ensure that all aspects of an audit file, including checklists and sign-offs, are captured promptly and provided to us in compliance with our technical requirements. The case team will provide our incoming data specifications, and we can arrange for our forensic accountants or other technical specialists to speak directly to an individual within, or engaged by, the firm with relevant technical expertise to ensure that the firm understands the FRC's requirements.

Preservation of documents and other relevant material: On notification of an investigation, parties must take steps to preserve all potentially relevant documents and other materials, both paper-based and electronic. Individuals must ensure that they preserve all material in their possession, including on personal devices. A firm must ensure that it preserves the electronic communications of all staff who worked on the audit. Depending on the nature and size of the case, the FRC may initially request counts of emails (rather than the emails themselves) from which to identify a subset of emails that may be relevant to the investigation. This process is likely to involve rolling requests to produce email correspondence identified through the application of search terms and other analytical tools. A firm should consider at an early stage whether an external provider with the necessary technical expertise (or the firm's legal representative) should be engaged so that the capture, extraction and deduplication of relevant electronic communications proceeds smoothly.

6. New FRC support initiatives

Introduction and context

The FRC is an Improvement Regulator. We want to improve the ability of firms to conduct high-quality audits and promote competition and choice in the PIE audit market.

We know that firms with smaller PIE audit portfolios or those new to the PIE audit market face challenges in meeting the FRC's high-quality expectations and in understanding how the FRC regulates PIE audit firms.

As well as issuing this document, we have launched some important initiatives to assist firms to develop and maintain audit quality as they start out and grow in the PIE audit market.

Tier 4

Up until now, the FRC has engaged primarily with firms that audit PIEs and we have engaged most intensively with firms that have a significant presence in the PIE audit market, our Tier 1 firms, with less intensive supervision for firms in Tier 2 and Tier 3.

We recognise that it is important to have a pipeline of firms that are equipped to enter the PIE audit market and conduct a high-quality audit from the start. We have therefore created a Tier 4 for firms that are not yet PIE auditors but are seeking to enter the PIE audit market.

We plan to engage with these firms through inviting them to participate in briefings, roundtables and other events run by the FRC. Tier 4 firms will also be able to apply to participate in our new Scalebox initiative.

Audit Firm Scalebox

The objectives of the Scalebox include:

- Improving audit quality at Tier 2 firms, Tier 3 firms and firms contemplating taking on the statutory audit of PIEs or other entities or audits within the FRC's scope, including major local audits.
- Promoting resilience in relevant sectors of the audit market.
- Supporting the FRC's role as an Improvement Regulator.
- Enhancing the FRC's ability to fulfil its regulatory objectives.

The Scalebox will operate separately to the FRC's formal supervision and Inspection work and will work with individual firms to help them understand how to improve and grow.



Our new Scalebox initiative will provide bespoke input to suitable firms in Tier 2, Tier 3 and our new Tier 4

The Scalebox will also work with firms to help them understand in more detail the FRC's regulatory expectations and our approach to supervision and inspection.

Details of how the Scalebox will operate, how to apply and the criteria we are looking for may be found [here](#).

Other FRC initiatives

Audit & Assurance Sandbox: The Sandbox is a recent innovation from our Regulatory Standards Division and is designed to lead a collaborative and innovative approach to identifying and developing solutions to technical and policy issues in the audit and assurance space. Details of current Sandbox projects can be found [here](#). Participation in the Sandbox is usually by invitation, but applications to be considered for individual Sandbox projects can be submitted to sandbox@frc.org.uk.

Technology & Digital Hub: Technology is at the forefront of discussions on the future of audit. Our new hub provides useful information on the topic and the FRC's priority areas, as well as opportunities for firms to get involved in the debate. You can find out more about this initiative [here](#), including how to take part.

Research project: Our Competition Policy team has launched a research project that seeks information from a range of firms, including audit firms at the smaller end of the PIE market and those who are not currently PIE audit firms. The aim of the research is to better understand the challenges and barriers to entering or growing in the PIE audit market, and to assist the FRC to develop policy solutions.

Appendix 1

Reference material: recent FRC publications

[Our Approach to Audit Supervision \(March 2023\)](#)

[What Makes a Good Annual Report and Accounts \(December 2022\)](#)

[Tier 2 and Tier 3 Audit Firms: Audit Quality Inspection and Supervision Report \(December 2022\)](#)

[Feedback Statement: Firm-level Audit Quality Indicators \(December 2022\)](#)

[What Makes a Good Environment for Auditor Scepticism and Challenge \(November 2022\)](#)

[PIE Auditor Registration Regulations and Guidance](#)

[Major Local Audits: Audit Quality Inspection \(October 2022\)](#)

[Annual Review of Corporate Reporting 2021/22 \(October 2022\)](#)

[Auditor reporting: A review of current practice \(August 2022\)](#)

[Annual Enforcement Review 2022 \(July 2022\)](#)

[Thematic Review: Judgements and Estimates Update \(July 2022\)](#)

[Tier 1 Overview and Firm-Specific Inspection and Supervision Reports \(July 2022\)](#)

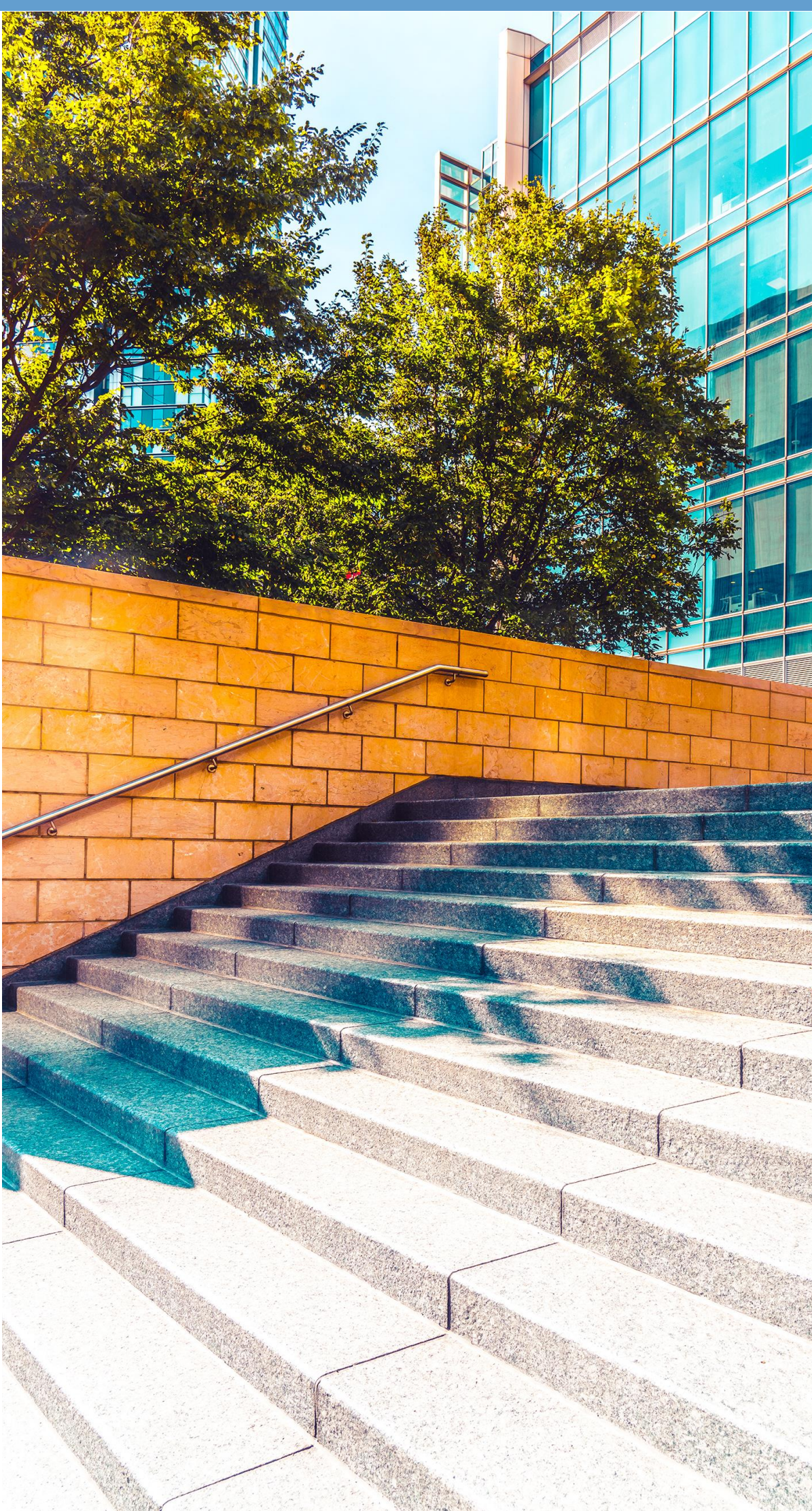
[Professional Judgement Framework \(June 2022\)](#)

[Key Inspection Findings and Good Practices \(May 2022\)](#)

[What Makes a Good Audit? \(November 2021\)](#)



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