

Firm-level Audit Quality Indicators

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Comments from ACCA
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GENERAL COMMENTS

We commend the FRC for these proposals, which elevate the audit landscape and will ensure Audit Committee Chairs and other interested parties have meaningful benchmark data to assess an audit firm's quality management. We support the scope and range of Audit Quality Indicators (AQIs) proposed, which ACCA considers to be broadly consistent with ISQM (UK) 1.

We recognise there is a high degree of variation in AQIs adopted by other jurisdictions, with differing regulatory approaches to AQIs as a tool to promote audit quality; indeed, the definition of "audit quality" can vary considerably between countries. Wherever possible, these AQIs should be consistent with the International Standards of Quality Management (ISQMs) issued by the International Auditing and Assurance Standards Board (IAASB) to ensure comparable and consistent decision-useful information for Audit Committee Chairs. The FRC has a unique opportunity to shape the future uptake and application of AQIs not just in the United Kingdom, but globally.

Our report [Tenets of a quality audit](#) found that auditors, by nature, are subject to a number of constraints and the tension between those constraints needs to be managed in achieving a high quality audit. AQIs, where sufficiently defined, provide relevant insight into how successfully an audit firm balances those constraints to drive audit quality, compared to its peers.

As noted in [our response to the European Commission consultation on Strengthening corporate reporting and its enforcement](#), we find it useful to mandate specific indicators to measure the quality of statutory audit, in addition to specific indicators to measure corporate reporting and the effectiveness of supervision. We believe it is possible to have clear and reliable indicators that promote audit quality.

Ultimately, AQIs can give a good, but not absolute, indication of audit quality, as not all aspects of audit quality can be measured in quantitative terms.

We encourage the FRC to work in consort with the Department for Business, Energy & Industrial Strategy (BEIS) in determining the scope and extent of these AQIs. We note that BEIS will adopt a different definition of Public Interest Entities (PIEs) to the International Ethics Standards Board for Accountants (IESBA) and support the FRC in continuing to advocate for international consistency.

SPECIFIC COMMENTS

1. Do you agree that the firms reporting their AQIs should be aligned to the scope of the revised 2022 Audit Firm Governance Code? If not, what scope would you prefer and why?

We agree that firms in scope of the revised 2022 AFGC should report their AQIs. It is appropriate that any firm auditing more than 20 PIEs, or one or more FTSE 350 companies, is in scope of these requirements. As we noted in our [November 2021 response](#) to the FRC's revisions to the AFGC, we are concerned at the possibility of additional firms coming within the scope of the 2022 revised AFGC and the respective costs that this could incur for firms

moving in and out of scope. Given the extensive data collation at scale that is required under both the AFGC and these proposals for firm-level AQIs, significant costs could be incurred under such circumstances; based on the most recent BEIS definition of a PIE, we believe that firms should be able to adequately determine whether they are close to the threshold for coming in scope of the AFGC and these proposals.

We note that the consultation document does not address instances where the lead auditor engages one or more component auditor(s); we recommend that the FRC addresses this area in future consultations. It may be appropriate for the component auditor to report their AQIs to the lead auditor, and those AQIs to be reported by the lead auditor in its transparency report as though the AQIs were their own, although this may not be feasible on large engagements with multiple component auditors. We recommend that the FRC takes an approach that is practicable while reinforcing the responsibility of the senior statutory auditor to ensure audit quality.

2. Do you agree that the AQIs should include all audit engagements, but segmented between PIE and non-PIE audits? If not, which engagements do you think should be included?

We are hesitant to support this proposal on the grounds that a firm's commitment to audit quality should be consistently high, irrespective of whether the client is a PIE or non-PIE; we are concerned that such segmentation could suggest that non-PIE audits require less rigour and attention to audit quality. It is appropriate that all audit engagements of a firm under the 2022 AFGC are in scope of these AQIs; however, segmenting this information for PIE audits and non-PIE audits risks overwhelming AQI users and Audit Committee Chairs by doubling the number of disclosures. We believe such segmentation could be appropriate for management information purposes but would question the value of this disclosure to external AQI users, other than the FRC.

3. Do you expect any additional costs to be incurred by firms reporting over a period which is not aligned with their financial years? Are there ways to minimise these costs?

The expansion in scope of the 2022 AFGC will create unavoidable additional costs for most, if not all, Tier 1 and 2 firms. Many of the AQIs proposed will likely be calculated and collected on a weekly or monthly basis by firms' time recording systems; from a cost perspective, we see little difference in reporting on the basis proposed (1 April to 31 March) and a firm's financial year. We would expect additional, marginal costs to be incurred for more qualitative-focused AQIs such as annual staff survey responses, where the period covered by such activities does not coincide with the period proposed by the FRC.

The primary consideration in assessing these proposals is to promote audit quality and facilitate meaningful comparison between audit firms. For this reason, we support the FRC's proposal to require a consistent reporting period.

4. Do you agree that it would be useful to include supporting narrative? Please provide suggestions to ensure that the information is concise and useful for users of audit services.

While it is important that firms explain their AQIs and the key drivers of those AQIs, it is vital that Audit Committee Chairs and other AQI users can readily compare firms' AQIs. We do not support restrictions or limitations on the supporting narrative, given the unique characteristics of each firm and different prevailing risks affecting their approach to audit quality. We support the inclusion of a distinct 'statement of AQIs' in the transparency report, as was proposed in the FRC's 2020 Thematic Review. At this stage, we suggest the FRC provides an indicative word count, accompanied by guidance that any narrative focuses on the key drivers and any remedial actions to be taken by the firm. We believe that publishing these AQIs in a transparency report provides Audit Committee Chairs with both qualitative and quantitative decision-useful information.

5. Do you agree with our proposed AQIs? If not, or in addition, do you prefer some of the alternatives presented above? Please explain, using the reference numbers.

We commend the FRC on its proposal for a wide range of AQIs, broadly aligned with ISQM (UK) 1; we concur that the number of AQIs proposed is appropriate and that detailed definitions will be required to ensure consistency and comparability across Tier 1 and 2 firms. As noted in our general comments above, it is vital that AQIs are aligned to ISQMs to ensure internationally consistent and comparable decision-useful information. In mandating firm-level AQIs, the FRC has a tangible platform to influence regulators' selection and application of AQIs in other jurisdictions.

In providing our feedback on the AQIs proposed, we recognise the FRC will provide further clarification and definitions later in 2022, and we welcome the FRC's iterative approach in this regard. Our views on the specific AQIs proposed are detailed below:

AQI 1 – Audit staff responses to certain annual staff / culture survey questions: percentage of favourable and unfavourable responses to the survey questions

We strongly agree with the conceptual basis for including this AQI, given the clear link between a firm's culture and audit quality; however, we note a variety of culture survey questions that are currently disclosed in the PRG firms' transparency reports. We recommend that the FRC explicitly phrases the standard question(s) that firms should ask their audit staff.

AQI 2 – Completion of audit planning phase: percentage of audits meeting key planning milestones by the target completion date

We support the inclusion of this AQI, given the correlation established between a lack of timely planning and poor audit quality, but note that ISQM (UK) 1 does not expressly consider this as a factor of audit quality. It is challenging to identify a pragmatic and low-cost basis for firms to record and monitor this AQI on a consistent basis, given that:

- the timing of audit milestones can often be subject to client staff availability;
- a standardised approach to this AQI would likely force a 'one-size-fits-all' approach on firms with differing milestones in their audit methodology; and

- permitting firms to define their own planning milestones based on their audit methodology reduces comparability and could increase the risk of firms adopting a more relaxed policy to achieve higher compliance.

We also believe this measure could also penalise audit firms taking on new clients, or engagements where the client has incorporated a new subsidiary or completed a business combination late in the financial year.

Recognising the fine balance between undue costs on firms and the need for comparability, if this AQI were to be included in the final AQI requirements, we recommend the definition:

- provides a Year 1 exemption for new audit engagements, to be applied at the client legal entity level; and
- specifies the precise audit milestones, aligned to UK ISAs wherever possible.

We suggest that the introduction of this AQI is delayed by a year so as not to penalise engagements where audit scheduling in 2023-2024 has already been agreed, to account for client staff availability and other factors outside firms' control.

AQI 3a – Proportion of audit effort by audit phase: average audit hours spent before the financial year-ends of audits in scope, as a percentage of total audit hours

We support the FRC's rationale behind this AQI, but will welcome a clear definition when published, given the practical challenges that can arise in identifying distinct phases of an audit. As with AQI 2 above, scheduling of audit planning or interim fieldwork can often be more a factor of client availability than a lack of audit planning. This can also be a grey area, particularly on soft close audits and audits of SEC registrants with quarterly interim reviews where work performed may be repurposed in the annual audit engagement. For audits of less complex entities, the proportion of time needed to be spent before the financial year-end will most likely be lower, considering efficiency and efficacy expectations.

We note that this area is not expressly considered in ISQM (UK) 1 and have similar concerns to the practicality of recording and monitoring this AQI at a firm-wide level. If this AQI were to be introduced, we suggest that it is delayed by a year so as not to penalise audit firms for factors beyond their control.

AQI 3b – Proportion of audit effort by audit phase: average percentage of audit hours spent in the two weeks before sign-off

We support the concept of this AQI but are sceptical at the practicality of recording and monitoring this data at the firm-level. If the FRC were to proceed with an AQI of this nature, and subject to the data being available at the firm-level, we suggest that there would be value in refocusing this AQI on the time incurred *after* audit report sign-off; this would reinforce the expectation that audit fieldwork and completion procedures have been completed to a high standard at the time of sign-off.

We note that ISQM (UK) 1.A83 specifies an appropriate time limit of 60 days after signoff to complete the assembly of the final engagement file. Compliance with this metric may be an appropriate AQI for the FRC to consider, although presenting this data as a histogram

showing percentage of engagements completing file assembly by number of days post-signoff may be a more appropriate presentation of this metric than a single firm-wide percentage.

AQI 4 – Extent of review by firms’ internal quality review teams: internal quality review hours as a percentage of total audit hours

We support the rationale behind this AQI, but note that internal quality review hours can be a blunt instrument, particularly given the variation in audit risk between engagements; a low risk engagement would likely require less internal review time than a higher risk engagement. This could penalise firms with a lower risk client portfolio and increase the barriers to entry for challenger firms.

If this AQI is to be implemented, we recommend the FRC develop a detailed definition consistent with the UK ISAs and ISQM (UK) 1, describing the activities regarded as ‘internal review’ and who should perform them. This would allow for comparability across the sector.

AQI 5 – Results of external inspections of the audit firm: percentage of audits inspected, by quality grading

We firmly support the implementation of this AQI, which will provide meaningful, relevant information to Audit Committee Chairs and other AQI users. To ensure comparability and consistency, while maintaining client confidentiality, we propose the following enhancements:

- Permitting Tier 2 firms to disclose this AQI privately to the FRC, to avoid individual clients being publicly identified where a firm has just a few PIE audits; and
- Requiring firms to segment their inspection results by regulator, given the difference in methodologies and grading structures between the FRC, ACCA, ICAEW and PCAOB.

AQI 6 – Coverage and results of internal inspections by the audit firm: number of audits internally reviewed as a percentage of total number of audits completed during the period, with quality grading

Conceptually, we support the ambition behind this AQI, given the robust monitoring and remediation process that ISQM (UK) 1 is aiming to drive, but are concerned that differing internal grading systems between firms could reduce comparability for Audit Committee Chairs and other AQI users. As an alternative to a quantitative AQI, we suggest that firms are required to provide qualitative disclosures describing the overall coverage of their internal inspections, the lessons learned and overarching themes from their internal reviews. Such disclosures would assist Audit Committee Chairs in concluding on whether firms’ systems are fit for purpose.

AQI 7 – Involvement by Engagement Quality Reviewers in audits: EQR hours as a percentage of total audit hours

We support the concept behind this AQI, but question the inferred connection between time incurred by an EQR and audit quality; the necessary time to understand the specific drivers of audit risk will naturally vary considerably between entities. As with AQI 4, EQR hours can be a blunt instrument; if the audit work is completed to a high standard prior to EQR review, then the time incurred by an EQR will naturally be lower. Similarly, EQR involvement from planning through to completion will naturally result in a more efficient, effective and higher

quality audit than instances where an EQR intervenes only in the final stages of an audit, prior to signoff.

We would suggest that it is not necessarily the number of hours spent in review, but the timing of EQR involvement, the quality of questions posed, and audit assumptions challenged, with robust follow up of review points, that allow the EQR process to improve the quality of an audit. It is possible for some firms with high quality EQR procedures to incur fewer hours on EQR activities than those with poorer quality reviews.

It is challenging to identify an alternative to this AQI for measuring the extent of an EQR's involvement at the firm-level. We suggest that the FRC requires qualitative disclosures in the transparency report around the procedures and systems in place to ensure that EQRs are involved throughout the audit process.

AQI 8 – Extent of involvement of and/or supervision in audits by engagement partners: average hours spent on audits as a percentage of total audit hours by engagement partners and key audit partners

Conceptually we support this measure, as it demonstrates the critical role of leadership involvement in the audit engagement. In addition to this AQI, we suggest the FRC, if not already planning to do so, considers whether leadership involvement on an audit – and critically, the *quality* of leadership involvement – could be assessed through other means, such as the annual staff survey.

AQI 9 – Number of hours worked per week, as a percentage of contracted hours: average staff utilisation rate by grade (or group of grades) in the audit practice

Utilisation is a key metric in assessing the workload, and stress levels, of audit staff; as the FRC has noted, work overload may reduce staff performance. We support the inclusion of this AQI as an essential metric of audit quality, and would suggest the following enhancements:

- Given the varying nature of financial year-ends across the sector, requiring disclosure of this AQI for each quarter of the year under review rather than focusing on January to March in isolation; and
- Recognising that audit firms have different grade structures, segmenting this AQI by (a) trainees/unqualified staff, (b) qualified management/supervisory staff, and (c) those with a leadership role on the engagement (typically the engagement partner or key audit partner).

AQI 10 – The rate at which staff leave the firm's audit practice – average staff attrition rates by grade in the audit practice

We support the inclusion of this AQI, together with AQIs 8 and 9, but note that many accountants' careers begin in a firm's audit practice before transferring to different parts of the firm or its network. In our view, this progression contributes to a diverse and dynamic profession. Staff attrition rates are both a contributor to, and a product of, resourcing pressures, together with other factors. We recognise that grading structures differ between firms and recommend that this information is segmented consistent with our proposal for AQI 9 above.

AQI 11 – Extent of involvement of specialists, by types of specialised skills generally used in audits: average hours spent by specialists on audits as a percentage of total audit hours

We agree with the FRC's objective for this AQI, and support its inclusion; however, we believe that AQIs 8 to 10 provide greater insight into the relationship between audit quality and an audit firm's resource planning and people management.

AQI 12 – Capacity of audit partners and managers to supervise junior audit staff in the firm, and the level of professional support for audit partners and managers: average number of audit staff managed by an audit partner / manager

We concur that an appropriate span of control is important to ensure audit quality, but note that the level of supervision required is driven primarily by audit risk; a low risk, controls-based audit approach may require less direct supervision than a high risk, fully-substantive audit, for example. Audit firms and their principals naturally have differing risk appetites when taking on audit clients and vary the span of control accordingly. We believe that AQIs 8 to 10 are better indicators of a firm's resource planning and people management, although this AQI may provide limited decision-useful information on an average basis at the firm level.

AQI 13 – To demonstrate the level of investment in training offered to partners and staff: average number of mandatory training hours per person

We fully support the inclusion of an AQI in relation to training hours, but encourage the FRC to include an additional AQI requiring disclosure of *verifiable* or *assessed* training hours on *technical audit* training. ACCA requires its registered auditors to maintain competence in audit work via their CPD hours.

AQI 14 – Gender and ethnic diversity of the firm's audit leadership: percentage of individuals in the audit leadership, by gender and ethnicity

We concur with the link between diverse and inclusive leadership and audit quality; however, gender and ethnicity are just two protected characteristics of many intersectional attributes that contribute to rich and effective leadership. For the UK market, we recommend that the definition of "audit leadership" for this AQI is expanded to include all audit partners and directors, and that firms are requested to anonymously survey these staff on other protected characteristics, such as age, sexual orientation and disability. Such surveys should also provide a "prefer not to answer" option. We were pleased to note that the Financial Reporting Advisory Board provided this data on board diversity in its [2021/22 annual report to Parliament](#).

It is important to note that this AQI alone will not improve equity and representation in the profession, nor is that the primary objective of this AQI; but advocacy, sharing stories and enlightening others are important steps, as noted in our 2021 report [Leading Inclusion](#).

6. Do you think there are any other firm-level AQIs that we should consider? If so, please explain.

We broadly agree with and support the range of AQIs proposed by the FRC. As noted in our response to question 5 above, we have identified additional AQIs that could provide valid decision-useful information to Audit Committee Chairs and other AQI users, namely:

- histogram showing percentage of audit file assembly completions by number of days post-audit signoff; and
- average number of verifiable or assessed training hours in technical audit matters per person.

We have reviewed the AQIs considered but not proposed by the FRC in the consultation paper, together with the AQIs noted in the FRC's Thematic Review in 2020:

PRG AQI – Audit Committee Chair impact: results of the Audit Committee Chair survey on audit quality

If the Audit Committee Chair survey were to be standardised across the sector as a 'net promoter score' metric in relation to audit quality, we believe this AQI could provide meaningful data.

AQIs listed in the FRC's Thematic Review (2020) and not considered in this consultation paper

We are conscious of the need to be mindful of the overall volume of data to be collected and reported, and the capacity of the intended audience to absorb the AQIs. So whilst we consider that the following AQIs identified in the FRC's Thematic Review and not considered in this consultation paper could provide meaningful insight into audit quality at a firm-wide level, it is correct that they are a lower priority to those proposed by the FRC in the consultation document:

- Internal hot reviews
- Partner quality ratings
- Hot review of financial statements

7. Are there any other comments you wish to make about these proposals, including concerning costs, benefits or impacts not discussed above?

We fully support and commend the FRC for these proposals, which, taken together, provide a holistic and meaningful view of audit quality at a firm-wide level. We have concerns at the scale of practical challenges firms may experience in implementing some of these AQIs, as identified in our response to question 5 above.

We note that the FRC does not explicitly mandate the publication of a firm-level transparency report in its proposals; we believe that incorporating standardised AQI definitions into requirements for a transparency report would strengthen the auditor selection process for Audit Committee Chairs, and allow for meaningful comparison between audit firms' quality metrics. ACCA [supported the introduction of the Audit and Assurance Policy](#) (AAP) proposed by BEIS; audit firms may wish to consider obtaining assurance over their published AQIs and

the transparency report. We encourage the FRC to review firms' AQI data systems and controls when inspecting firms' practice-wide arrangements to support audit quality. This approach would reinforce the importance of these disclosures and their consistent application across Tier 1 and 2 firms.

As explained in our response to question 1, the costs associated with the expansion of the 2022 revised AFGC, and the risk of a firm moving in and out of scope of these proposals could be significant; however, based on the latest definition of a PIE from BEIS we believe that firms should be able to determine whether they are at risk of coming into scope.