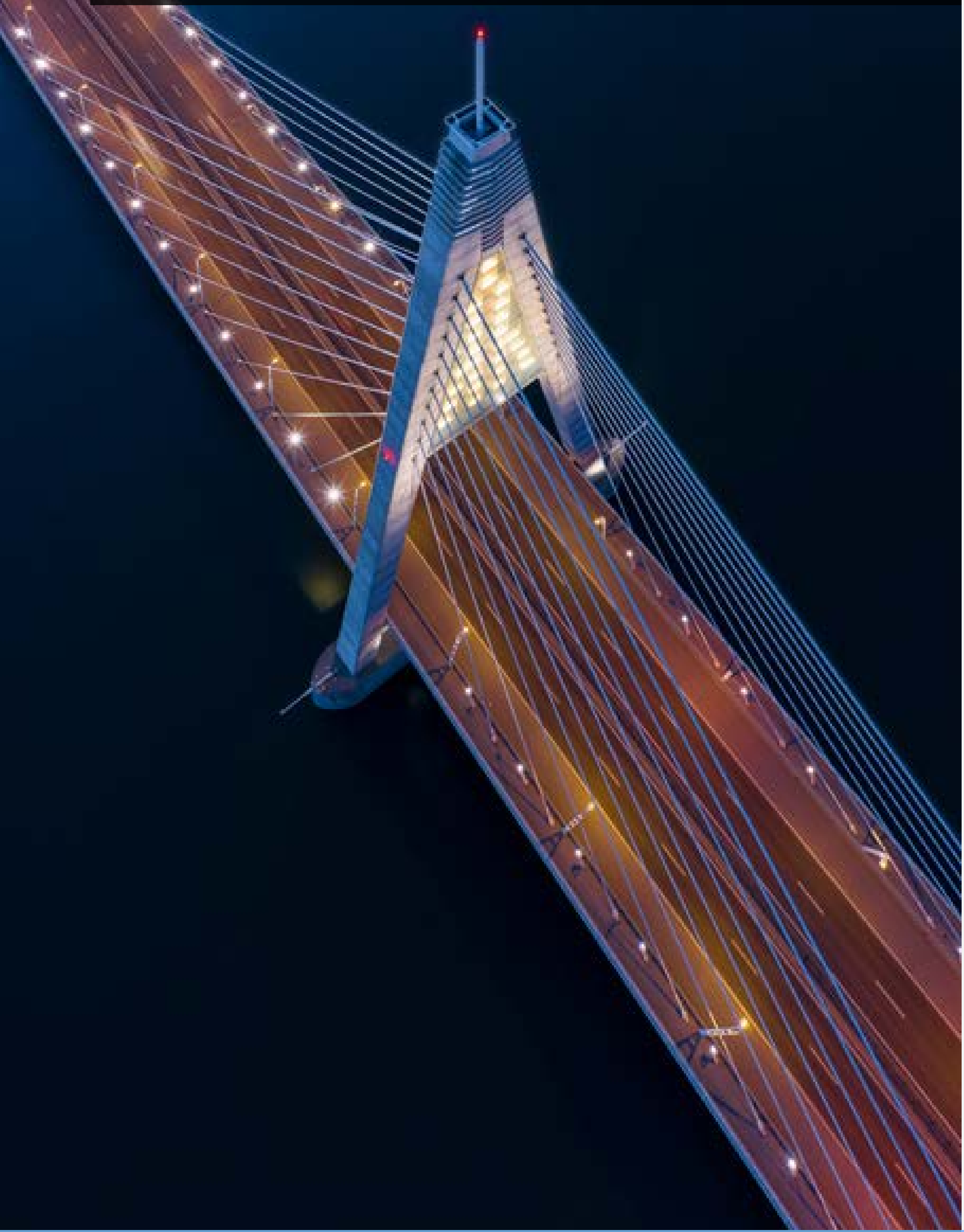
FRC

Financial Reporting Council

Mazars LLP

Audit Quality Inspection and Supervision



July 2021

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Appendices

This report sets out the FRC's findings on key matters relevant to audit quality at Mazars LLP (Mazars or the firm). It is based on inspection and supervision work undertaken in our 2020/21 cycle, primarily our review of a sample of individual audits and our assessment of elements of the firm's systems of quality control.

The FRC's focus is on the audit of public interest entities (PIEs[1]). Our selection of individual audits and the areas within those audits for inspection continues to be risk-based focusing, for example, on entities which: are in a high-risk sector; are experiencing financial difficulties; have material account balances with high estimation uncertainty; or, where the auditor has identified governance or internal control weaknesses. The majority of individual audits that we inspect are of PIEs but we also inspect a small number of non-PIE audits on a risk-based basis.

Higher-risk audits are inherently more challenging as they will require audit teams to assess and conclude on complex and often judgemental issues, for example in relation to future cash flows underpinning assessments of impairment and going concern. Rigorous challenge of management and the application of professional scepticism are especially important in such audits.

Our increasing focus on higher risk audits means that our inspection findings may not be representative of audit quality across a firm's entire portfolio of audits or on a year-by-year basis. Our inspection findings cannot therefore be taken as a balanced scorecard of the overall quality of the firm's audit work. However, our forward looking supervision work now provides us with a holistic picture of the firm's approach to audit quality and the future development of its audit quality improvement initiatives.

As well as risk-based selections, we aim to review all FTSE 350 audits periodically.

To provide a more holistic assessment of audit quality, the report also includes reference to other measures of quality at the firm. The Quality Assurance Department (QAD) of the Institute of Chartered Accountants in England and Wales (ICAEW) did not inspect a sample of the firm's non-PIE audits this year in accordance with its planned rotational inspection of the firm and therefore there are no results included in this report.

The firm does, however, conduct annual internal quality reviews. A summary of the firm's internal quality review results is included at Appendix 1, together with the actions that the firm is taking in response.

At Appendix 2 are further details of our objectives and approach to audit supervision.

1 Public interest entity – in the UK, PIEs are defined in the Companies Act 2006 (Section 494A) as: - Entities with a full listing (debt or equity) on the London Stock Exchange (Formally "An issuer whose transferable securities are admitted to trading on a regulated market". In the UK, "issuer" and "regulated market" have the same meaning as in Part 6 of the Financial Services and Markets Act 2000); - Credit institutions (UK banks and building societies, and any other UK credit institutions authorised by the Bank of England); - Insurance undertakings authorised by the Bank of England and required to comply with the Solvency II Directive.

1 Overview

Commentary on our inspection work at the largest audit firms

We completed more audit inspections at the largest seven firms in 2020/21 (103) than in 2019/20 (88). Our overall inspection findings are similar to last year, with 71% of audits (73 out of 103 inspections) requiring no more than limited improvements compared to 67% last year (59 out of 88 inspections).

The number of audits that we have assessed as requiring improvements remains unacceptably high. This year the results varied more between firms and we found inconsistencies, with good practice in some audits but deficiencies in the same areas in other audits at the same firm.

The most common key findings in our public reports are in relation to revenue, impairment of assets and group audit oversight. These are recurring issues but we also identified good practice in these areas in some audits.

We also identified good practice during our 2020/21 thematic review of the audit of going concern, where we found that firms had responded positively to the increased risk arising from Covid-19, by enhancing their procedures in this area[2].

Four of the largest firms (Deloitte, EY, Grant Thornton and PwC) had a year-on-year improvement in their overall inspection results, with around 80% or more of audits requiring no more than limited improvements. While this is encouraging, these improved results still fall short of our expectations.

Overall inspection results at KPMG did not improve and it is unacceptable that, for the third year running, we found that improvements were required to KPMG's audits of banks and similar entities. In addition, our firm-wide work on KPMG's IFRS 9 procedures and guidance identified that further improvements are required to provide a stronger basis for KPMG's banking audit teams to deliver high quality audits in this area. KPMG has already invested significantly in its banking audit practice and considers that, based on steps it has already taken, it will be able to demonstrate improvements in 2020 year-end audits. In response to our findings this year, the firm's senior leadership has committed to make the further changes necessary to improve audit quality in time for 2021 year-end audits. We will monitor these closely to assess on a timely basis the extent to which they address our findings.

This year, we increased the sample of audits we selected for review at BDO and Mazars, given their growth, with a focus on complex audits. Five of the nine audits that we reviewed at BDO and three of the seven audits that we reviewed at Mazars needed more than limited improvements. These firms have grown the size of their PIE audit practices and have plans to grow further, which will increase competition and choice in the market. Our engagement indicates that these firms are genuinely committed to improving audit quality but they must put in place the necessary building blocks for the consistent execution of high quality audits as they grow.

71%

Overall, the number of inspections requiring no more than limited improvements fell short of our expectations.

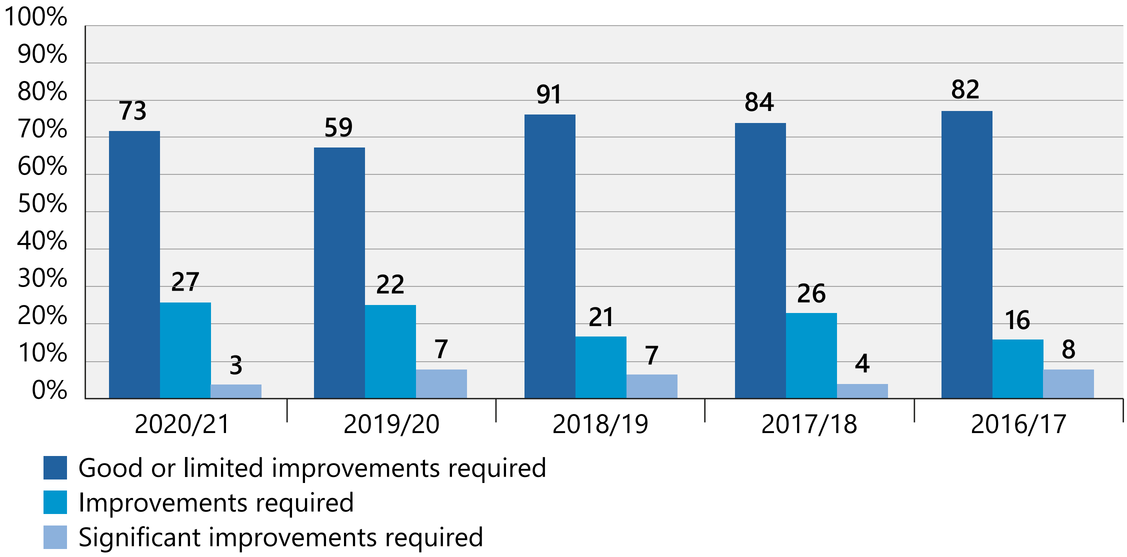
This year, results varied more between firms and we found inconsistencies, with good practice in some audits but deficiencies in the same areas in other audits at the same firm.

2 https://www.frc.org.uk/getattachment/953261bc-b4cb-44fa-8566-868be0ff48dc/FRC-going-concern-review-letter.pdf; and https://www.frc.org.uk/getattachment/c1ec4c8f-0eb3-44b9-a4c7-5fe5e4c0e0f1/FRC-going-concern-review-letter-(phase-2).pdf

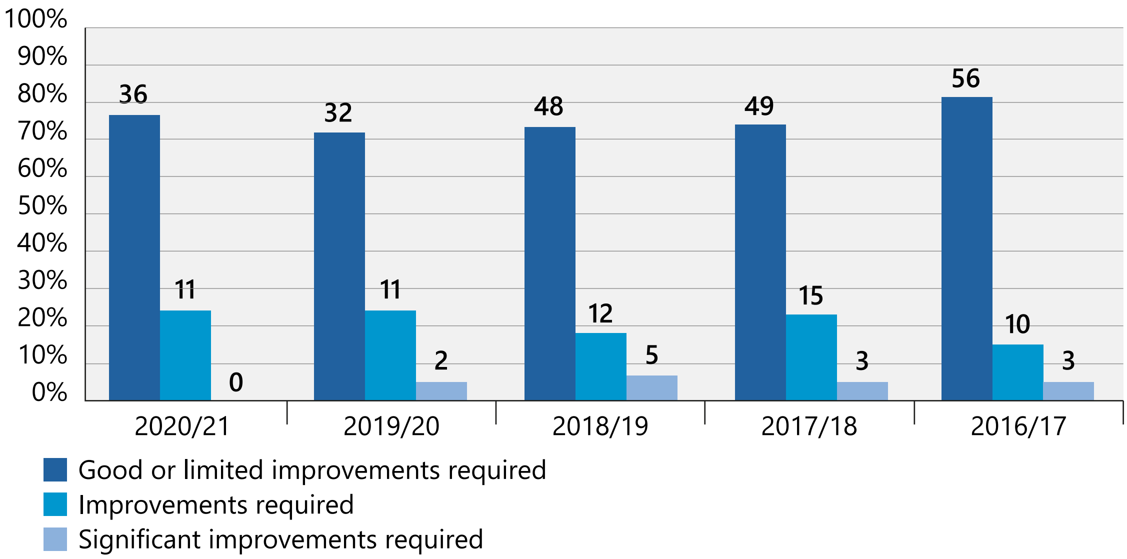
Central to achieving consistent audit quality is a healthy culture within the audit practice that encourages challenge and professional scepticism, as we set out in our letter to Heads of Audit in December 2020. We have a major project underway to examine audit culture, including an international conference held in June this year on the subject. Operational separation of audit practices from the rest of the firm should help the largest firms to focus on developing an appropriate audit culture.

Our supervision teams[3] are increasing the range of pro-active and forward-looking work they are carrying out with the largest seven firms in areas such as audit quality plans, root cause analysis, quality control procedures and audit quality indicators with a focus on how firms are responding to recurring findings. We report privately to firms on our findings in these areas, in order to share good practice. In 2021/22 we will continue to focus our inspections on KPMG banking audits and we will increase audit inspections at BDO and Mazars. Our 2021/22 inspections will also focus on and take into account the impact of Covid-19 on audits.

All reviews



FTSE 350



3 Our approach to supervision is set out in the March 2021 publication, https://www.frc.org.uk/getattachment/db4ef2e0-72f6-4449-bda0-c8679137d1b1/FRC-Approach-to-Audit-Supervision-FINAL.pdf

Our supervision teams are increasing the range of pro-active and forward-looking work.

In 2021/22 we will continue to focus our inspections on KPMG banking audits and we will increase audit inspections at BDO and Mazars.

Mazars overall assessment

We reviewed seven individual audits this year which was an increase from last year in response to the growth in the number of PIE audits carried out by the firm. We assessed four (57%) of them as requiring no more than limited improvements.

The number of audits requiring improvement or significant improvement is unacceptable. The firm needs to update its audit quality plan significantly to improve quality. A key part of the plan must be the appropriate resourcing of the central functions that support audit quality and resilience.

The firm has taken steps to address the firm-wide findings raised in the prior year in relation to partner and staff appraisals. The firm has also made some progress in the areas of acceptance and continuance, with further action required. We also identified good practice in the audits we reviewed (including delaying signing the auditor's report to address quality issues).

All findings in section 2 of this report contributed to our assessment of the audits requiring more than limited improvements.

The one recurring finding from prior year was in auditing areas of judgement including expected credit loss (ECL) for financial services audits.

Similar to the prior year, we identified findings in all of the firm-wide areas reviewed in the current year which the firm needs to address urgently.

Mazars' Audit Quality Plan (AQP) focuses on the key drivers of audit quality (including the right team and resources, integrity, scepticism and technical expertise) and was devised in conjunction with its "No Compromise" programme, which focuses on developing a culture of quality in the firm's audit practice.

The firm has entered into a new four year strategic cycle which places PIE audits as a key priority, and appointed a new Head of Audit. The context and content of the AQP is being revisited to ensure that they are appropriately aligned with the strategic objectives. There is a focus on improving quality through the new audit operations team and key transformation initiatives. The Head of Audit has overall responsibility for the plan, both in terms of identifying the key drivers to be included and ensuring that it is implemented.

The AQP needs to be embedded into the management of the audit practice to ensure delivery by the broader business, with monitoring remaining with the central team. Further actions are required to address concerns raised last year, to resource and develop the plan, and align it with the new audit strategy and growth plan. Further investment in central quality and risk functions is required.

The firm has linked the plan to its "No Compromise" culture programme and to the RCA actions which is good practice, but more work is required to develop the audit culture and embed it into key processes. Making the assessment of the impact of actions taken part of the plan from its early development is also good practice.

In response to our findings last year, the firm has developed a more independent approach to RCA as well as introducing further enhancements, including significantly expanding the scope and coverage of RCA conducted. The firm has also begun to develop an impact assessment process which we consider to be good practice.

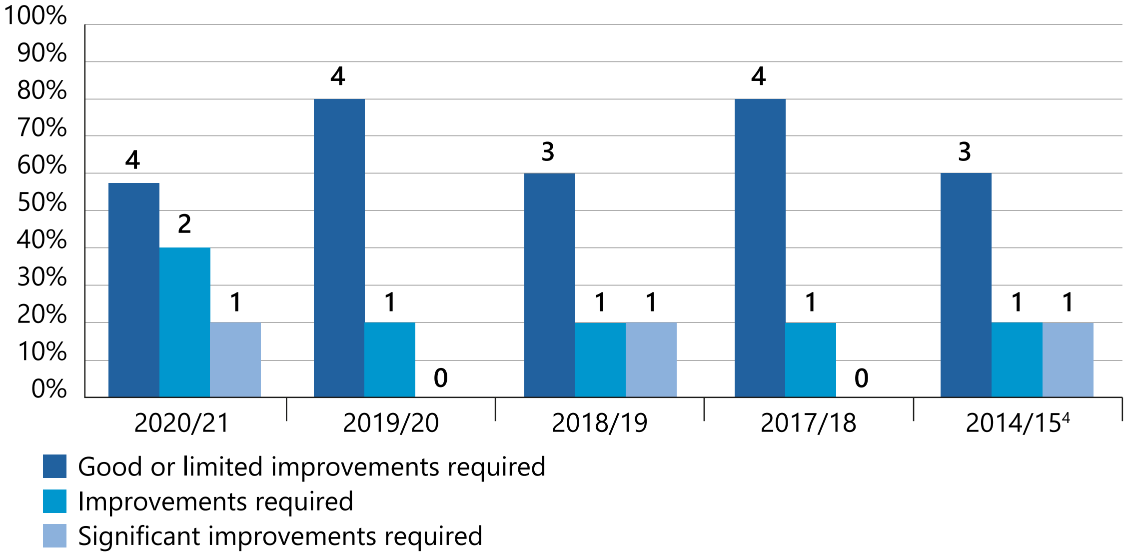
In order to develop the RCA process further the firm should focus on the key findings that we have raised in relation to further extending the coverage and scope of its RCA activities, ensuring that a sufficient number and quality of new people are dedicated to RCA and providing additional training and support.

57%

At Mazars, the level of audits reviewed that required no more than limited improvements is unacceptable.

In the prior year we recommended that the firm take action to improve the robustness of its quality control systems in response to the significant growth in its audit portfolio and its appointment as auditor on larger and more complex audits. Given this recommendation and the audit quality results in 2021, the firm now urgently needs to address the firm-wide and audit inspection review findings with a substantial update of its audit quality plan and initiatives to ensure that the pace of growth does not exceed the pace at which the firm is remediating audit quality findings raised.

Our assessment of the quality of audits reviewed: Mazars LLP



The audits inspected in the 2020/21 cycle included above had year ends ranging from 31 December 2019 to 31 March 2020.

Changes to the proportion of audits falling within each category reflect a wide range of factors, including the size, complexity and risk of the audits selected for review and the scope of individual reviews. Our inspections are also informed by the priority sectors and areas of focus as set out in Appendix 2. For these reasons, and given the sample sizes involved, changes from one year to the next cannot, on their own, be relied upon to provide a complete picture of a firm's performance and are not necessarily indicative of any overall change in audit quality at the firm.

Any inspection cycle with audits requiring more than limited improvements is a cause for concern and indicates the need for a firm to take action to achieve the necessary improvements.

4 FRC included Mazars in Audit Quality Review annual inspection scope first time as part of the 2017/18 inspection cycle. Before then the firm was within a triennial inspection cycle.

Review of individual audits

Our key findings related primarily to the need to:

- Improve the challenge of management's impairment assessments in relation to goodwill and other assets.
- Strengthen the quality and effectiveness of audit work on revenue.
- Enhance the oversight of component audit teams by the group auditor.
- Take further steps to strengthen the quality of audit work on areas of judgement, including ECL.

Good practice observations

We identified examples of good practice in the audits we reviewed, including the following:

- Delaying sign-off of the auditor's report and robust reporting to the Audit Committee in relation to the difficulties encountered during the audit.

- Robust approach to test inventory existence considering the challenges relating to Covid-19.

Review of firm-wide procedures

This year, our firm-wide work focused primarily on the following areas:

- Audit quality initiatives.
- RCA process.
- Audit methodology and training.

The reason for the focus on RCA and audit quality initiatives is the importance of taking effective action to address recurring inspection findings. On both of these areas we have assessed the firm's progress on the findings set out in last year's public report and re-assessed overall progress.

Audit quality initiatives

Our key findings in this area were related to the need to:

- Appropriately resource central functions.
- Embed the AQP in the management of the audit business.
- Further develop the audit culture of the firm.

RCA process

Our key findings in this area were related to the need to:

- Ensure there is sufficient quantity and quality of any new dedicated resource.
- Develop the RCA process further and increase the depth of interviews with training and support.
- Further expand the scope and coverage of the RCA.

Audit methodology and training

Our key firm-wide findings in these areas related principally to the need to:

- Increase the amount of mandatory training audit practitioners are required to complete.
- Introduce post course assessments for technical training to evaluate whether learning objectives have been met.
- Improve the guidance issued to audit teams in relation to auditing lease accounting and financial instruments accounting (non-banking entities) under IFRS 16 and IFRS 9 respectively.
- Improve the quality and extent of IFRS 9 methodology and guidance relating to banking audits.

Good practice observations

We identified examples of good practice in our review of firm-wide areas, including the following:

- **Audit quality initiatives** – The clear link from inspection findings and RCA to the AQP at an engagement level; and the inclusion of impact assessment in the AQP from its early development.

- **RCA process** – The use of key measurement points in the audit process as part of the RCA process; a mechanism to assign weight to causal factors identified; and an impact assessment is used to assess the whether the actions developed from the RCA have worked.

Firm's overall response and actions

Following the firm's positive findings in the prior year, we are disappointed by this year's FRC's findings and are determined to address the issues which have been identified. Mazars is dedicated to quality; it is a central pillar of the firm's values and strategy; and there will be significant further investment in, and focus on, quality in the future; both culturally and operationally. Our firm has grown significantly in recent years and we have invested heavily in our team throughout 2020 despite the pandemic and we will continue to do so. Our investment has been made across auditors and related specialists to further equip the firm to operate in the PIE market. We have also invested in our support teams to further strengthen our focus on quality and risk management.

We are fully supportive of the FRC's efforts in holding our sector to account, and in demanding improvements in the quality of audit work. The firm is committed to the PIE market and we will be continuing our investment in this sector. This investment forms part of a long-term plan across the UK and International firm.

Mazars has embarked on a journey of embedding the principles of our robust Audit Quality Plan and we expect that it will see the impact of this over the coming years, acknowledging the time delay between quality initiatives being introduced and the impact being seen in FRC inspections. During the year, the firm has launched a review of the culture within audit with a view to enhancing our existing culture of quality. This project has been incorporated into our 'No Compromise' initiative, which is designed to re-evaluate our approach to delivering audit, identify barriers to delivering high quality audit and design and implement solutions. The delivery of this project is scheduled to start during the summer of 2021.

We have also invested in quality control processes and systems during the year with a particular focus on developing a more robust client take on process, further investment in our new global audit platform 'Atlas' the deployment of which is in progress. The firm has augmented the key controls around the take on of clients to ensure that there is increased focus on our ability to deliver quality audits. As an example, the firm introduced a 'Bid/No Bid' procedure during the year whereby all significant potential clients had to be appropriately approved within the Service Line, with approval based upon a number of criteria such as reputational risk, appropriate skills and resources etc. In conjunction with these stricter client acceptance criteria, the firm has begun the process of reviewing our existing client base to ensure that we continue to act for businesses aligned with our focus on quality.

We are also continually investing in our central audit quality team resource so that we have the requisite skills and resources to support client teams in their delivery of 'high quality' audits. This team has already grown significantly within the past year and will continue to grow substantially over the next 12 months.

We are revising our Audit Quality Plan to ensure that it appropriately addresses all underlying threats to quality, and fully reflects the importance of a culture of challenge, which we believe to be a critical element in the delivery of quality audits.

As committed in the prior year we also have launched our root cause analysis programme in the year and have finalised our reviews of the files inspected in this cycle. The findings of these reviews have resulted in a number of key actions to remedy them now incorporated into our Audit Quality Plan and include for example the creation of a centre of excellence to deliver the audits of complex impairment reviews and amendments to our procedures relating to departing partners Through this process we are identifying the underlying challenges to consistently delivering audit quality and designing and implementing relevant initiatives to address these.

The firm has also implemented its first suite of Audit Quality Indicators, and while these are anticipated to evolve over the next few years, they now provide key metrics upon which we are able to measure quality and identify potential areas of concern prior to significant issues arising.

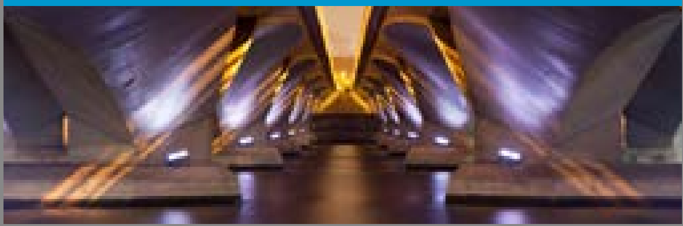
Over the past year we have enhanced our training requirements and programme including introducing post course assessments to measure their effectiveness. These adaptations have been introduced to not only improve technical knowledge but to also equip teams with the relevant skills to create a culture of challenge. We have also been developing our audit methodology, with a particular focus on establishing a robust IFRS9 banking methodology further over the past year in all areas identified by the FRC.

The Covid-19 pandemic has brought in an unprecedented challenge to the entire profession during the last inspection cycle, and we are thankful for the monumental efforts and adaptability exhibited by our teams, and the finance teams of the entities we audit, to overcome this. We have reacted quickly to the challenges presented by delivering remote audits with appropriate guidance including a sharply increased focus on going concern considerations, so it is pleasing that the FRC noted no significant findings in relation to going concern on any of our audits. It should be noted that 4 of the files reviewed were first year audits delivered in these challenging conditions.

We welcome the FRC's review and challenge, which we believe to be an invaluable tool for learning and improving. We would like to thank the FRC for its engagement and support throughout the review, and alignment in the shared goal of improving audit quality within the firm and across our sector.

Our supervisory approach

The **AFS, AMS** and **AQR** teams in the FRC's Supervision Division work closely together to develop an overall view of the key issues for each firm to improve audit quality. We also collaborate to develop our plans for future supervision work.



The supervisory staff producing our reports

70+

The **AFS, AMS** and **AQR** teams comprise over **70** experienced professional and support staff assessing the risks to audit quality and resilience at each firm and the actions needed to address those risks.

Mazars[4]

RIs **72**

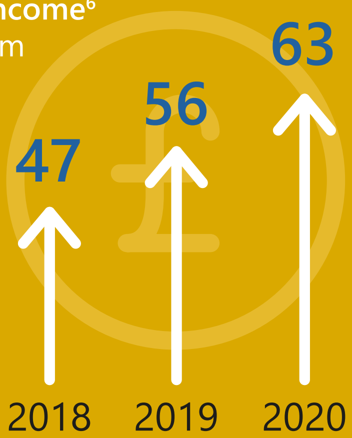
Offices **17**

1,780 Professional Staff

Mazars
Audits within the FRC's inspection scope

Inspection Cycle[5]	FTSE 100 audits	FTSE 250 audits	Total audits in FRC scope
2021-22	0	0	60
2020-21	0	0	46
2019-20	0	0	45

Mazars
Audit fee income[6]
£m



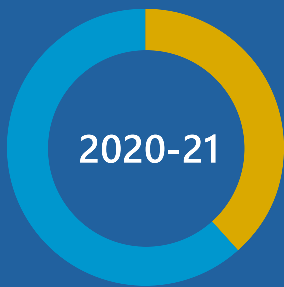
Mazars
Audits inspected by the FRC[7]

2020-21 **7**

2019-20 **5**

2018-19 **5**

Mazars
Local audits[8]



Major audits **43**
Non-Major audits **69**
Major audits inspected by the FRC **4**

4 Source – the ICAEW's 2021 QAD report on the firm.
5 Based on data compiled by the FRC, dated 31 December 2020, 2019 and 2018 respectively and used to select audits for inspection in the relevant inspection cycle.
6 Source – the FRC's 2019, 2020 and 2021 editions of Key Facts and Trends in the Accountancy Profession.
7 Excludes the inspection of local audits.
8 The FRC's inspection of Major Local Audits are published in a separate annual report to be issued later in 2021. The October 2020 report can be found here.

2 Review of individual audits

We set out below the key areas where we believe improvements in audit quality are required. As well as findings on audits assessed as requiring improvements or significant improvements, where applicable, the key findings can include those on individual audits assessed as requiring limited improvements but are considered a key finding in this report due to the extent of occurrence across the audits we inspected. We asked the firm to provide a response setting out the actions it has taken or will be taking in each of these areas.

Improve the challenge of management's impairment assessments in relation to goodwill and other assets

The impairment assessment for goodwill and other assets is inherently subjective and complex, with resulting impairment charges being susceptible to material misstatement including as a result of management bias or error. Changes in the key assumptions used in management's assessments could result in additional impairment charges being recognised. Auditors should obtain sufficient and appropriate evidence to assess the reasonableness of cash flows and other judgements made by management to support their conclusions over these areas.

We identified issues in relation to challenge by audit teams of aspects of management's impairment assessments.

Key findings

We reviewed the audit of impairment of goodwill and other assets in all of the audits that we inspected, and we identified the following findings in four audits:

- On one audit the audit team's procedures to test impairment and conclude that there was not a material misstatement were not adequate. In particular, the audit team did not obtain sufficient evidence to assess the reasonableness of management assumptions or support its conclusion that a material impairment charge should not be recorded.
- On another audit the audit team obtained insufficient evidence to conclude that further impairments of internally generated assets were not required and did not adequately corroborate the forecasts used to support the carrying value of projects selected for testing.
- On two audits the audit team did not sufficiently challenge the reasonableness of management's assumptions in relation to cash flow forecasts. On another audit where the impairment assessment was sensitive to small changes in assumptions, the audit team did not sufficiently challenge management on the reasonableness of the multiple used to determine recoverable value.

Firm's actions

During the year, the firm's roll out of *No Compromise*, to further develop a culture of quality in the audit service line, has been stalled by Covid. It is restarting in June 2021. This initiative will re-enforce the importance of audit teams to challenge management judgements, both internally and externally. We consider that developing a culture of challenge is critical to the delivery of high-quality audits.

For our 31 December 2021 year ends we will be trialling a centre of excellence for impairment reviews to ensure that these reviews are performed to a consistently high standard. This change is to reflect the specialised nature of the work required to appropriately review and challenge management impairment reviews and so we feel it is critical that this is handled by an appropriately trained and experienced team.

As part of our mandatory annual technical training programme for 2021 we will provide a reminder of the firm's methodology in relation to challenging management impairment analysis. This will include a focus on:

- What constitutes appropriate evidence and challenge of the reasonableness of management assumptions;
- The relevant procedures required to corroborate management cash flow forecasts; and
- The importance of robust sensitivity analysis and the implications on the extent of testing to be performed where forecasts are considered to be particularly sensitive to 'minor' changes in assumptions.

Strengthen the quality and effectiveness of audit work on revenue

Revenue is a material component of the income statement and is often identified as a key performance indicator on which investors and other users of financial statements focus. The audit team should design an approach which is responsive to the identified risk and ensure that they obtain sufficient and appropriate audit evidence over revenue recognised.

We reviewed the audit of revenue on all audits inspected and identified a number of issues on two of them.

Key findings

We reviewed the audit of revenue on all audits inspected and identified the following broad range of issues associated with revenue on two of those audits, including:

- On one audit:
  - the audit team failed to perform sufficient procedures to assess the completeness and accuracy of revenue in relation to inventory invoiced but not dispatched. In addition, the impact of the estimated unrealised gross margin on these transactions on the entity's statement of financial position was not adequately evaluated.
  - there was insufficient evidence to support the team's cash to revenue reconciliation and inadequate challenge of the sufficiency of the reserve for irrecoverable trade receivables.
  - we also identified weaknesses, in the testing of related party revenue. The audit team did not sufficiently consider whether a related party confirmation was appropriate and independent evidence to substantiate a material revenue balance. Furthermore, the audit team did not adequately assess whether the trading arrangement was at arm's length and did not challenge management's inaccurate and incomplete related party disclosures.

- On another audit where the group audit team directly tested revenue for the UK component there was insufficient evidence to conclude on the inputs and judgements used in determining the stage of completion for certain component revenue contracts nor in relation to the inputs and assumptions used in the team's substantive analytical procedures.

Firm's actions

The issues noted above arose on first year audits and so the firm will be enhancing its guidance in relation to the consideration of fraud and related party transactions, with a particular focus on the increased scepticism and challenges associated with performing a first-year audit.

We will also be reviewing and updating our risk management procedures, including the role and scope of EQCR engagement on audits. More directive guidance will be issued to our EQCR teams to ensure a greater level of consistency in review, challenge and documentation requirements of the role.

In our mandatory annual technical programme for 2021 we will include a dedicated session to remind audit teams of the requirements in relation to auditing revenue. In particular, we will cover:

- How to address the completeness and accuracy of revenue;
- The circumstances, and procedures required, in order to deliver an effective cash to revenue reconciliation;
- Issues associated with testing related party revenue. This will include which confirmations from related parties constitute reliable third-party evidence and consideration of whether related party trading relationships are at arm's length;
- The firm's methodology in respect of auditing the stage of completion for long term contracts; and
- The appropriateness of evidence obtained to corroborate assumptions used in substantive analytical review procedures.

Enhance the oversight of component audit teams by the group auditor

The group audit team is responsible for the direction, supervision and coordination of the group audit, including work completed by component audit teams and therefore needs to demonstrate sufficient involvement throughout the audit process.

For all group audits, we reviewed the level of involvement of the group audit partner and other group audit team members in the direction, supervision and review of the component audits. In four audits, there was insufficient evidence of the group audit team's involvement and oversight of aspects of the component auditors' work:

Key findings

- On two audits there was insufficient evidence of oversight of certain procedures performed by the component auditors in assessing the appropriateness of the capitalisation of development costs and weaknesses in the procedures performed to test financial investments.
- On one audit there was insufficient evidence of the group audit team's oversight of revenue cut-off, in particular around consideration of the appropriateness of the different component auditor approaches of the testing of pre and post year-end credit notes.
- On another audit there was insufficient evidence of the group audit team's oversight of the component auditor's work on a material and complex revenue stream.
- On two audits the group audit team did not demonstrate how the combined procedures performed by the group audit team and the component auditors met the requirements of a full scope audit for the overseas component.

There was insufficient evidence of the group audit team's involvement and oversight of aspects of the component auditors' work in four audits.

Firm's actions

During 2021 we will provide further guidance to teams to clarify the requirements associated with demonstrating the group audit team's sufficient involvement and oversight of the component auditor's work. A particular focus will be placed on the additional requirements associated with a first-year audit and the importance of the group team obtaining a detailed understanding of the operating and business models of the groups they audit. This is critical to ensuring that the group team has the appropriate knowledge to devise a tailored audit strategy for each component and to evaluate the work of each component to ensure that this strategy has been appropriately delivered.

As part of the firm's development of its new global audit platform 'Atlas', specific functionality is intended to support the seamless cross review of working papers in group scenarios. This functionality will assist group teams to improve the quality of oversight of component auditors.

In addition, we will cover this guidance during our mandatory audit technical training programme and provide illustrative case studies as to how this guidance should be applied in practical situations.

Take further steps to strengthen the quality of audit work on areas of judgement, including ECL

On all audits, audit teams should assess whether management's judgements and estimates are reasonable. In particular, ECL, where relevant, involves significant management assumptions and estimation uncertainty. Auditors should provide challenge over management's judgements and obtain sufficient and appropriate audit evidence to corroborate them.

Key findings

Last year we reported that the firm needed to improve the consideration of judgements in key areas, including the assessment of ECL and to strengthen its methodology in this area in order to achieve consistent, high quality audit work and a robust approach to the audit of larger, more complex entities.

For all inspections in the current inspection cycle, we reviewed the audit team's work on key areas of management judgement. We identified weaknesses in the audit procedures performed on ECL on one audit. The weaknesses identified were broader and had a more significant impact on audit quality in comparison to the findings in the prior year for a similar entity. We also identified deficiencies in other areas in three audits.

- For one audit there were weaknesses relating to ECL testing, in particular we had concerns with the nature and extent of certain key audit procedures performed and the sufficiency of audit evidence. These primarily related to the Significant Increase in Credit Risk (SICR) and the appropriateness and sufficiency of the audit approach over all SICR criteria (including management judgement) and specific stage allocation. On this audit, the audit team also performed inadequate procedures and did not retain sufficient evidence to support their testing of multiple-economic scenarios.

- On two audits we identified issues in relation to the level of challenge and the sufficiency of evidence obtained to corroborate management's assumptions in key areas of judgement. In particular, there was insufficient evidence of procedures to challenge management's assumptions and assessment of:
  - a material uncertain tax position; and
  - management's forecasts supporting the recoverability of a deferred tax asset.

The firm should take action to improve the quality of its audit work over areas of judgement and closely monitor the progress of its audit quality initiatives with an urgent focus on banking methodology to safeguard audit quality across the firm's growing public interest entity audit portfolio.

Firm's actions

We are disappointed that continued issues have been identified in relation to consideration of judgements in key areas, particularly in relation to the valuation of ECL.

As noted in the impairment section above we are focusing on the further development of a culture of challenge to support audit teams to strengthen the quality of audit work on areas of judgement.

In response to the prior year findings, over the past year we have developed a revised methodology in relation to IFRS 9 for banking. It should be noted that this revised methodology was released post the delivery of the file reviewed. We consider that this methodology is proportionate to our client base and the associated risks. We will continue to monitor our methodology in this area and ensure that this evolves in line with any changes in the risk profile of our client base.

Our revised methodology provides teams with additional guidance and tools to address the concerns noted above. There will be a particular focus on SICR and the level of involvement of our economists to support testing of multiple-economic scenarios.

We continue to identify instances of insufficient evidence and challenge by audit teams of certain key judgements, including related to the Expected Credit Loss allowance.

This guidance will have been released and will be incorporated into our mandatory banking training for autumn 2021. In relation to other areas of management judgement, as part of our mandatory annual technical training programme for 2021 we will provide a reminder of the firm's methodology in relation to challenging management judgements. This training will encompass case studies to enable the team to practically apply our guidance and understand the challenges associated with its application in practice.

Good practice

We identified examples of good practice in the audits we reviewed, including the following:

- **Delayed sign-off:** The engagement partner delayed signing the auditor's report to ensure that sufficient audit evidence was obtained. Furthermore, the reporting to the Audit Committee in relation to the difficulties encountered during the audit was robust.

- **Robust inventory testing:** The audit team's audit approach to test inventory existence was robust considering the challenges relating to Covid-19 and the fact that this was a first-year audit. Senior members of the audit team including the engagement partner attended post year-end inventory stock takes covering all locations.

Good practice examples included procedures relating to inventory existence and robust reporting to the Audit Committee when difficulties were encountered during the audit.

3 Review of firm-wide procedures

We review firm-wide procedures, based on those areas set out in International Standard on Quality Control (UK) 1 (ISQC1), in some areas on an annual basis and others on a three-year rotational basis. The table below sets outs the areas we have covered this year and in the previous two years:

Annual	Current year 2020/2021	Prior year 2019/2020	Two years ago 2018/2019
• Audit quality initiatives, including action plans to improve audit quality. • RCA process. • Audit quality focus and tone of the firm's senior management. • Complaints and allegations processes.	• Audit methodology and training.	• Partner and staff matters. • Acceptance and Continuance (A&C) procedures.	• Ethics and Independence. • Internal Quality Monitoring. • Quality Control matters (including consultation and EQCR). • Audit documentation and data security.

In this section we set out the key findings and good practice we identified in the firm-wide work we have conducted this year, and a summary of our findings reported publicly in the previous two years, and the firm's related actions, with updates where relevant, as follows:

- Audit quality initiatives.
- RCA process.
- Audit methodology and training.
- Firm-wide findings and good practice in prior inspections.

Audit quality initiatives

Background

Firms should develop audit quality plans that drive measurable improvements in audit quality. Audit quality plans should include initiatives which respond to identified quality deficiencies as well as forward-looking measures which contribute directly or indirectly to audit quality.

Mazars' AQP focuses on the key drivers of audit quality (including the right team and resources team, integrity, scepticism and technical expertise). It was devised in conjunction with its "No Compromise" programme, which in turn is to develop a culture of quality in the firm's audit service line.

Audit quality plans should include forward-looking measures which contribute directly or indirectly to audit quality.

When we reviewed the audit quality plan last year, we found that the firm should improve the plan and/or quality initiatives by:

- Accelerating the AQP to address the FRC's and the firm's own quality monitoring file review and firm-wide findings; as well as to respond to the audit division's business growth, including where applicable resourcing and formalisation of sector-specific audit methodology.
- Formalising monitoring of the implementation of and on-going governance over the plan, including prioritisation of key initiatives, implementation of specific projects and consideration of milestones.
- Formalising the resourcing requirements plan for the audit division. The plan at that time considered only the composition of the audit quality team and needed to incorporate and consider the overall resourcing requirements and expertise necessary for the audit division. A clear link to the firm's acceptance and continuance and risk management procedures was also required.
- Assessing the scope and role of hot reviews to enhance audit quality and to meet the requirements of the firm's growing audit division.

The firm's response to these findings indicated a variety of actions being or to be taken. Our review has confirmed that the firm has begun to address the findings. We have raised key findings below where significant further action is required to address our concerns fully.

This year, we have not conducted a detailed benchmarking of all firms' AQPs and quality initiatives, but at each of the seven firms we have brought our view up to date by work including:

- Assessing any key changes to the firm's AQP, arising from the actions taken in response to our findings last year, or for other reasons.
- Undertaking meetings with the firm to discuss and challenge aspects of the AQP.
- Considering the oversight of the AQP at the firm including presentations made to the Independent Non-Executives (INEs) and any audit oversight body.
- Assessing the extent to which culture and the culture of challenge have been incorporated into the AQP.
- Considering, in hindsight, the effectiveness of the AQP and key initiatives with reference to current year findings and observations.

As a result of our work, we have observed that:

- The firm has entered into a new four year strategic cycle which places PIE audits as a key priority, and appointed a new Head of Audit. The context and content of the AQP is being revisited to ensure that they are appropriately aligned with the strategic objectives. There is a focus on improving quality through the new audit operations team and key transformation initiatives. The firm needs to further develop the AQP so that it is comprehensive and cohesive, and aligned to its overall audit strategy and growth plan in terms of the timing and expansion of initiatives.
- The Head of Audit has overall responsibility for the plan, both in terms of identifying the key drivers to be included and monitoring its delivery. The firm's Audit Executive is responsible for monitoring, on a monthly basis, the implementation, progress and on-going governance of the plan.

- The AQP covers all audits and therefore covers FRC scope entities and local audit and incorporates audit services provided by specialists and experts within the firm.
- In addition to the AQP, there are parallel initiatives linked to audit quality including the continued roll-out of the RCA strategy and reporting, the development of a new suite of AQIs and the firm's separate project on ISQM (UK) 1.
- Mazars has developed its hot review process into coaching-based reviews to provide support and encourage further engagement in the process and its usefulness.

Key findings

We identified the following key findings where the firm needs to:

- Appropriately resource central functions: The resourcing of central functions including technical teams, hot reviews teams, IQM and RCA is included within the plan, but they currently remain under resourced. These functions need to be appropriately resourced, in skills, seniority and numbers, to support the growth and ensure continuous improvement.
- Embed the AQP in the management of the audit business: The AQP should be central to and embedded in the management of the audit business within the firm. As recognised by the firm, everyone in audit needs to take responsibility for improving audit quality. There should be clear accountabilities and communication.
- Further develop the audit culture of the firm: Whilst culture is the foundation of the overall AQP because it was devised in conjunction with the "No Compromise" programme and behaviours driving audit quality, further work is required to develop the audit culture of the firm and embed it into key processes.

Mazars' audit quality plan needs to be further developed. Further investment in central quality and risk functions is also required.

Good practice

We identified the following areas of good practice:

- **Clear link between RCA and AQP:** There is a clear link from inspection findings and the firm's RCA to the engagement level actions within the AQP.
- **Impact assessment:** Impact assessment as well as monitoring progress on implementing actions has been included within the AQP from its early development.

We will continue to assess the AQP and encourage all firms to develop or continue to develop their audit quality plans including the focus on continuous improvement and measuring the effectiveness of the key initiatives.

Firm's response and actions

We are pleased that the FRC has acknowledged the progress the firm has made in relation to developing our Audit Quality Plan (AQP) and Audit Quality Initiatives. We are committed to further developing these programmes to address the issues noted above.

In relation to the specific issues raised, during the last 12 months the firm has grown its central audit functions by approximately 33% and have similar plans for continued investment going forwards.

We are introducing processes to ensure that the AQP is embedded in the management of the audit business. For example, the AQP is now reviewed on a monthly basis by the Audit Executive to ascertain progress and areas where intervention is required to ensure the AQP is delivered on a timely basis.

As noted earlier in our responses, we consider that culture is critical to the delivery of 'high quality' audits and we're investing significant resources to establish and communicate our vision of this culture. The primary vehicle for this is 'No Compromise'.

RCA process

Background

The RCA process is an important part of a continuous improvement cycle designed to identify the underlying causes of specific audit quality issues (whether identified from internal or external quality reviews, or other sources) so that appropriate responses can be taken that address the risk of repetition.

Root cause analysis is an important part of a continuous improvement cycle.

The firm has undertaken RCA for a number of years as part of its internal quality monitoring process. This is the first year that a new independent approach has been followed. The global firm does not set out methodology or guidance. The firm's 'independent' RCA process is still in the early stages of development relative to other firms.

When we reviewed the firm's RCA process last year and the RCA conducted on our 2019/20 inspection findings, we focused on certain key improvements necessary given the firm's stage of RCA development. We found that the firm should:

- Review and formalise the firm's RCA plan and ensure it is aligned to the firm's growth strategy, recurring quality findings and the Audit Quality Plan.
- Extend the scope and level of coverage of RCA reviews for external inspection findings as it is narrower than some other firms and does not currently include firm-wide findings.
- Identify themes arising from inspection findings and good practice.
- Increase the level of detail in the actions reported to the firm's leadership.

Mazars' response to these findings indicated that it would take a variety of actions to improve the process and make it more independent of other functions. Our review has confirmed that the firm has largely addressed the findings.

This year, we have not conducted a detailed benchmarking of all firms' RCA processes, but at each of the seven firms we have brought our view up to date by performing work including:

- Assessing any key changes to the firm's RCA process, arising from the actions taken in response to our findings last year, or for other reasons.
- Conducting follow-up meetings with firm to discuss and challenge aspects of the RCA process including new initiatives.
- Considering the oversight of RCA at the firm and communication of key findings.
- Considering, in hindsight, the efficacy of the historical RCA process and the actions taken with reference to current year inspection findings.

As a result of our work, we have observed that:

- The RCA function has been made more independent by separating it from other quality initiatives and central quality support and ensuring a direct reporting line to the Audit Executive and any future Audit Board.
- The Audit Executive Committee is responsible for monitoring the delivery of this RCA plan and assessing progress monthly. It will also be responsible for ensuring that it is aligned with the overall Audit Quality Plan as that plan is further developed.
- The approach to RCA has been revised to involve a comprehensive assessment of the drivers behind both poor and good audit quality on individual files. This new RCA process factors in the findings and conclusions from the quality monitoring process and challenges any underlying themes or risk factors identified to arrive at an independent assessment.
- The coverage and scope of RCA has been significantly enhanced. At an engagement level, the firm includes all external inspections (FRC, ICAEW and PCAOB (although this year there were only FRC inspections to consider)) and all poorer graded internal reviews. The FRC reviews of public sector audits are also subject to RCA. The process is focused on both good practices and key findings. Thematic reviews are also being undertaken focusing on identifying risks to audit quality in certain audits/sectors.
- The actions included in the RCA report on our findings are sufficiently detailed to enable the firm's leadership to monitor their progress and effectiveness. There is a clear link in the report from findings to causal factors and recommended actions.
- The RCA reporting could be improved if the more overarching root cause themes, such as the resourcing matters, project management, mind-set and integration of specialists, were more explicitly pulled out from the RCA and linked to the firmwide rather than engagement level actions in the AQP. Whilst there currently is regular reporting on each of the different sources of RCA, there would also be benefit in some regular RCA reporting, across all sources, including the firm's Internal Quality Monitoring, to compare themes and assess the progress of actions as the findings evolve through the course of each year, rather than the current separate reporting.

Key Findings

We identified the following key findings where the firm needs to:

- Expand the RCA team: The firm needs to ensure that a sufficient number and quality of people are devoted to carrying out RCA as the team is currently disproportionally small when compared to other firms, the size of the audit practice and the future growth plans. This can be done both by expanding the RCA team and by drawing on the firm's experienced audit partners and subject matter experts.
- Develop the RCA process further: Further training and support is required to develop the RCA process further and increase the depth of the interviews. Training from behavioural specialists or their involvement in the process would allow more cultural/behavioural root causes to be identified and acted upon.
- Further expand the scope and coverage of the RCA: The scope and coverage should be further expanded to capture good practices identified from internal quality monitoring reviews and findings from reviews of firmwide procedures.

Mazars should expand both the resource devoted to carrying out root cause analysis and the scope and coverage of the process.

Good practice

We identified the following areas of good practice:

- **Key measurement points:** The RCA process requires the audit team to consider key measurement points in the audit process, such as time spent by the audit partner and quality control reviewer as part of the considerations of root causes.
- **Weighting causal factors:** A mechanism to assign weight to causal factors identified in the RCA process has been developed, which creates a clear link between the quality failing and the cause.
- **Impact assessment:** The RCA team have started to consider whether the actions developed from the RCA have worked. To make this impact assessment as efficient as possible, the monitoring of the action is being considered at the RCA and action setting stage. Assessments following training are already in place to check whether the training has been successfully embedded.

We will continue to assess the firm's RCA process. We encourage all firms to continue to develop their RCA techniques as well as focus on measuring the effectiveness of the actions taken as a result.

Firm's response and actions

We are pleased that the FRC has acknowledged the advancements we have made this year in relation to RCA and that we have largely addressed the findings raised from the prior year. We consider that RCA is a critical element of our quality control procedures and have plans in place to increase the size of the team in the coming year. Our approach was first to develop and embed a robust methodology to the RCA and now that we have that in place, we will move to the second stage and expand the team and application of RCA across the audit service line.

During the current RCA cycle a number of key initiatives have direct links to this process, for example the implementation of a centre of excellence for the audit of complex impairment reviews, the development of a 'milestone' programme to assist teams in relation to project management and assessing the status of completion of audits and revised tools, templates to assist with the integrations of specialists/experts into the audit team and a change in our archiving policy with the implementation of a 7 day archiving deadline.

Audit methodology and training

Background

The firm's audit methodology and the guidance provided to auditors on how to apply it are important elements of the firm's overall system of quality control. Our inspection primarily evaluated key changes to the firm's methodology and guidance including how it had been updated to incorporate recent changes to auditing and accounting standards, including:

- ISA 540 revised (Auditing accounting estimates and related disclosures).
- ISA 570 revised (Going concern).
- IFRS 9 (Financial instruments) with a focus on the audits of banks, building societies and other credit institutions (banking audits).
- IFRS 16 (Leases).

The firm's audit methodology and the guidance provided to auditors on how to apply it are important elements of the firm's overall system of quality control.

We also considered other key topics such as the policies for using specialists and experts on audits and updates to audit software. We performed the majority of this work on methodology and guidance in place on 31 March 2020, including a consideration of the firm's initial response to the impact of Covid-19.

Firms' training arrangements must provide auditors with the knowledge and skills necessary to fulfil their role effectively, and as such, are also an important element of the firm's overall system of quality control. Our inspection included an evaluation of the amount of training provided by the firm in the year ended 31 March 2020, the subjects covered and how the training was delivered. We also considered the firm's processes for monitoring course attendance and evaluating whether participants had met the learning objectives by conducting post-course assessments.

Key findings

We identified the following key findings where the firm needs to:

- Increase the amount of mandatory training audit practitioners are required to complete: The firm provides training on certain key topics where attendance is highly recommended. This training should be mandatory with processes to ensure completion on a timely basis with clear, enforced consequences where individuals are non-compliant. In addition, the firm should increase the amount of industry-specific training provided to practitioners on banking audits.

- Introduce post-course assessments for technical training to evaluate whether learning objectives have been met: To ensure training has been effective, the firm should introduce post-course assessments to test the knowledge of all participants.

- Improve the guidance issued to audit teams in relation to auditing lease accounting and financial instruments accounting (non-banking entities) under IFRS 16 and IFRS 9 respectively: The firm has issued work programmes, templates and related guidance in relation to IFRS 16. These should be enhanced to ensure audit teams receive clear guidance on auditing complex scenarios under the standard. The firm should also develop and issue work programmes, templates and guidance, for auditing financial instruments (on non-banking entities) to ensure that audit teams consider all key aspects of IFRS 9 that might be relevant to the audit.

- Improve the quality and extent of IFRS 9 methodology and guidance relating to banking audits: The firm should issue a comprehensive IFRS 9 methodology including clear baseline expectations of the procedures audit teams are required to perform on banking audits, to ensure consistency and quality across IFRS 9-related audit work. This should be integrated into the firms' core methodology, supplemental guidance and audit programmes/checklists. The firm has been expanding the size and complexity of its banking audits in recent years so prompt action is required.

In addition to the firm-wide procedures above, we performed a thematic review on the enhanced audit policies and procedures at the seven largest firms in relation to going concern, given the impact of Covid-19. The themes we observed were publicly reported in June 2020 and November 2020 and have not been included here.

We identified findings in all the firm-wide areas reviewed in the current year which the firm needs to address.

Firm's response and actions

Over the past year we have enhanced our training requirements. As part of this process we have:

- Removed our highly recommended category and made these sessions mandatory. Attendance at these sessions is monitored, with non-attendance considered to be a disciplinary matter and factored into each individual's year-end performance assessment.

- Implemented post course assessments to assess the impact of the mandatory training that we are providing.

We are in the process of enhancing our methodology in relation to IFRS 16 and IFRS 9. The specific areas of consideration are noted below:

- During the second half of 2021 we will be releasing additional guidance in relation to IFRS 16 support complex scenarios under the standard, for example how to deal with embedded derivatives. Alongside this, we will release additional guidance and associated tools relating to IFRS 9 for non-financial services entities.

- As noted above the firm has revisited our IFRS 9 banking guidance and tools during the year to ensure that they are appropriate for our current client base. This revised guidance has been issued prior to the publication of this report. We are committed to the continued improvement of our methodology in this area and we will look to continuously ensure that our guidance is appropriate to the needs of our audit portfolio and risk profile of the companies we audit. To assist in the process, we are actively recruiting additional banking specialists into our central audit quality team.

Firm-wide key findings and good practice in prior inspections

The following table summarises the firm-wide findings included in our previous two public reports, as well as the actions taken by the firm in response to our key findings, in those areas of ISQC 1 which we review on a rotational basis. We consider that the firm is appropriately responding to these findings based on the actions taken and to be taken.

Key findings in previous public report	Update on firm's actions in response	Good practice
Partner and staff matters (2019/20): Processes relating to the appraisal and remuneration of partners and staff are a key element of a firm's overall System of Quality Control and are integral to supporting and appropriately incentivising audit quality. Our inspection included an evaluation of the firm's policies and procedures and their application to a sample of partners and staff for the FY18 appraisal year, across the following areas: Appraisals and remuneration; Promotions; Recruitment; and Portfolio and resource management.		
• There was a lack of compliance with the firm's requirements around objective setting and appraisal completion in staff appraisals, which was around 50% and 40% respectively as of April 2019. A sample review of staff appraisals identified several instances where there was no or only limited evidence of the appraisal performed or of how audit quality had been considered. There is also no formal process to ensure that all relevant quality metrics (including the results of internal or external inspections) were appropriately reflected in senior staff appraisals and objective setting.	Changes to monitoring and metrics implemented for both teams and partners in FY19 include: • Ensuring that performance reviews and objective setting are more closely monitored in terms of prompt and complete documentation and the quality of the metrics and processes that impact remuneration decisions. For FY19 almost 100% of performance reviews and FY20 objectives were included within the firm's HR system. • The requirement for specific quality objectives to be included for those senior audit team members or partners with adverse quality control reviews in the prior period or with additional audit quality responsibilities.	No specific good practice examples raised.

• Adjustments to the firm's processes, partner performance ratings and variable remuneration as a result of audit quality were typically limited in their size and impact. In the majority of cases in FY18, adverse audit quality findings did not result in an overall deduction to remuneration. There was also insufficient evidence in the firm's FY19 pay review process to demonstrate how audit quality had affected biennial decisions taken over movements in partner fixed pay. We also identified concerns around the tailoring of annual quality objectives to respond to previously identified adverse quality findings.	• The determination and collation of a broader range of audit quality metrics will be included as part of FY20 performance reviews. • With effect from FY20, we have instigated changes to ensure that the impact of audit quality is more clearly embedded and documented within the process, with improved tracking of the impact on final remuneration for all partners. This includes greater direct impact on remuneration for adjustments related to quality and partner assessment documentation amended to facilitate a much clearer and increased focus on quality for partners in all service lines. • The firm has continued to closely monitor compliance, with 100% of partner and 99.5% of team performance reviews completed for FY20. The firm has further developed relevant KPIs and more clearly recognised the impact of quality on performance reviews. Developments continue to be made on an ongoing basis to further embed audit quality. • The following have been especially significant in achieving these improvements: enhanced monitoring at a senior leadership level; and transparency with the full partner group across all service line of the impact of quality on performance reviews for the FY20 year end	No specific good practice examples raised.

Key findings in previous public report	Update on firm's actions in response	Good practice
Acceptance and continuance procedures (2019/20): ISQC1 requires firms to have detailed policies and procedures relating to acceptance and continuance decisions for audited entities. We reviewed the firm's processes as at October 2019 and their application. We also discussed with senior leadership proposed changes to these processes together with each firm's strategic decisions. In addition, we considered firms' policies relating to withdrawal / dismissal from audits and, for a sample of audits, the statements provided to the public, successor auditors and the regulatory authority in connection with withdrawal / dismissal.		
• The firm's internal review noted that some audit continuance assessments were not completed on time and consequently staff were performing work on engagements before the continuance decision had been approved. The process should be strengthened and monitored to ensure that an audit cannot commence until the continuance approval process has been completed. • The firm's continuance form contains a set of pre-defined responses, often without supporting narrative to explain, for example, why previous risk factors are no longer relevant and why it is appropriate to continue acting for the audited entity. It does not give sufficient prominence to the assessment of the potential impact on the firm's brand and reputation risk or the resources required to undertake the engagement.	• Our internal monitoring had identified that improvements to our continuance procedures were required and we agree with the FRC's comments made. • Over the last year we have strengthened the controls around audit acceptance decisions and further enhancements will be made in 2020 with regards to both acceptance and continuance. These will include improvements in the documentation of conclusions reached based on each of the factors considered. • In addition to the actions above, the firm is further enhancing the acceptance and continuance procedures for all service lines. These changes include the centralisation of key elements of acceptance and continuance which will provide greater challenge of decisions and improved monitoring and compliance with policies and procedures.	No specific good practice examples raised.

Key findings in previous public report	Update on firm's actions in response	Good practice
Ethics and independence (2019/20 and 2018/19) Firms should have appropriate systems and procedures to ensure compliance with the revised Ethical Standard, including in relation to the monitoring of financial interests.		
• The firm should improve its monitoring procedures for staff financial interests. There is reliance on annual fit and proper declarations and no compliance testing is performed on financial interests and there is no system in place to record and track staff interests. Since our last public report, the firm has taken appropriate action to improve its systems and procedures for monitoring personal independence compliance for partners.	We have reviewed our personal independence processes for staff and are making the following positive changes to strengthen them further: • Sample testing of the financial interests of non-partner RIs; • Requiring quarterly independence confirmation for all managers and above within the audit service line; and • Central monitoring of the independence confirmation for all partners and team members on PIE audits at the planning and completion stage. • These changes have further enhanced compliance with regards to personal independence. • In addition, the firm has commenced a project to provide additional safeguards in respect of financial interests in the context of the wider Mazars group.	No specific good practice examples raised.

We did not raise any other key findings in 2018/19 or 2019/20.

Appendix 1

Firm's internal quality monitoring

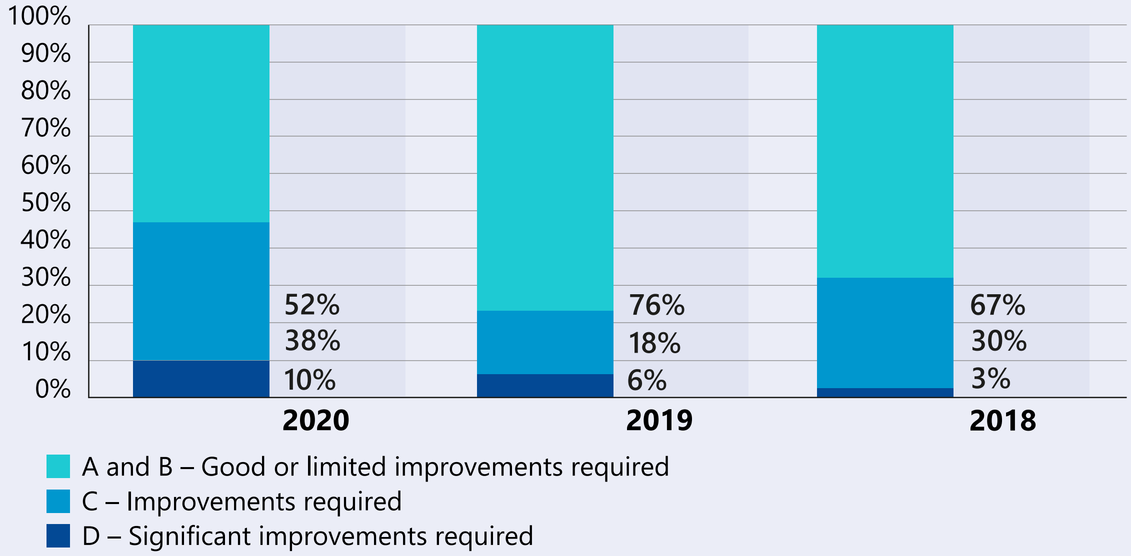
This appendix sets out information prepared by the firm relating to its internal quality monitoring for individual audit engagements. We consider that publication of these results provides a fuller understanding of quality monitoring in addition to our regulatory inspections, but we have not verified the accuracy or appropriateness of these results.

The appendix should be read in conjunction with the firm's Transparency Report for 2020, and the firm's report to be published in 2021, which provide further detail of the firm's internal quality monitoring approach and results and its wider system of quality control.

Due to differences in how inspections are performed and rated, the results of the firm's internal quality monitoring may differ from those of external regulatory inspections and should not be treated as being directly comparable to the results of other firms.

Results of internal quality monitoring

The results of the firm's most recent Internal Quality Monitoring (iQM) program, which comprised internal inspections of 31 individual audits with periods ending between 1 October 2019 and 30 September 2020, are set out below along with the results for the previous two years.



* The firm's iQM program uses the same grading categories as the FRC. Decisions on grading are aligned as closely as possible to those that would result from the FRC process.

Firm's approach to internal quality monitoring

The firm's internal inspection program considers the full population of audits performed. The program is designed to cover each Responsible Individual (RI) at least once every two years. Audit files are selected for review based on a number of criteria, including risk and public interest. Reviews are supervised by the Director of Audit Standards and are conducted by appropriately trained and experienced reviewers, with specialist technical support where required. The Director of Audit Standards reviews all findings to ensure that the firm's processes and grading criteria are applied appropriately and consistently, and proposed grades are reviewed by the Partner responsible for Quality Monitoring before signing out final findings to the RI and audit team.

Action plans are prepared for each inspection to address key findings at an engagement level in the subsequent year's audit, which are followed up as part of the iQM programme. Where significant deficiencies are noted, the Partner responsible for Quality Monitoring will meet with the RI to discuss the findings.

Independent RCA is being undertaken for those files where improvements and significant improvements required are noted. This is being done outside the iQM review process by an independent team of RCA investigators.

Internal quality monitoring themes arising

The key themes arising from the firm's internal quality monitoring programme include:

- Insufficient auditor challenge in areas of management judgement, in areas such as the valuations of PPE specific to the public sector, investments and pension scheme liabilities.
- Insufficient audit evidence in journal testing to address management override of controls. This included lack of evidence to support the completeness of the journal population tested and failure to agree journals to source documentation.
- Poor quality documentation and review. This related to files where the number of documentation related findings indicated a requirement to improve the overall standard of documentation and review although each finding in isolation was not significant.
- Insufficient evidence in relation to cash and cash equivalents. In a number of file reviews the audit teams had either failed to obtain third party confirmations in relation to cash balances or undertake sufficient testing of reconciling items.

Firm's response and actions:

- The firm operates a robust internal iQM review programme, aiming to at least match the challenge shown by the FRC in its file reviews. We are proud of an uncompromising approach to quality monitoring as a key part in continually striving to improve audit quality, and we seek to raise the bar in these reviews year on year.
- We are disappointed by any file that required anything other than limited improvements as our objective is to ensure we have no files within that category. We acknowledge that the results in this year's cycle show an increase in files requiring improvement and we are working hard to address this as set out in our Audit Quality Plan.
- The iQM review process requires that individual file findings are discussed with the relevant audit team who are asked to document their consideration of the cause for any finding, and reflect that in their planned actions to address. In addition, these files are also subject to an independent RCA review in order to understand the underlying drivers behind the poor quality file.
- The internal quality monitoring findings are reported three times a year to the Audit Board. Included in this reporting are the Audit Quality Team's responses to the key themes and findings which may include the delivery of additional training or supplementary guidance. The frequency of reporting means that responses can be put in place quickly to address findings at a firm wide level.
- All iQM findings are communicated in an iQM briefing session to audit staff as part of the mandatory annual audit masterclass training.

Appendix 2

FRC audit quality objective and approach to audit supervision

Audit quality objective

The FRC is the Competent Authority for statutory audit in the UK and is responsible for the regulation of UK statutory auditors and audit firms, and for monitoring developments, including risk and resilience, in the market. We aim, through our supervision and oversight, to develop a fair, evidence-based and comprehensive view of firms, to judge whether they are being run in a manner that enhances audit quality and supports the resilience of individual firms and the wider audit market. We adopt a forward-looking supervisory approach to audit firms, and we hold firms to account for making the changes needed to safeguard and improve audit quality.

Auditors play a vital role in upholding trust and integrity in business by providing opinions on financial statements. The FRC's objective is to achieve consistently high audit quality so that users of financial statements can have confidence in company accounts and statements. To support this objective, we have powers to:

- Issue ethical, audit and assurance standards and guidance;
- Inspect the quality of audits performed;
- Set eligibility criteria for auditors and oversee delegated regulatory tasks carried out by professional bodies such as qualification, training, registration and monitoring of non-public interest audits; and
- Bring enforcement action against auditors, if appropriate, in cases of a breach of the relevant requirements.

In March 2021 the Department for Business Energy & Industrial Strategy (BEIS) published a consultation document, Restoring Trust in Audit and Corporate Governance, which proposes broader supervisory powers for the FRC/ARGA covering auditors, audit committees and directors. The legislation that follows the consultation process will create ARGA and provide it with further powers.

Approach to audit supervision

In March 2021 we published Our Approach to Audit Supervision which explains the work that our audit supervision teams do.

These reports published in July 2021 provide an overview of the key messages from our supervision and inspection work during the year ended 31 March 2021 (2020/21) at the seven largest audit firms[9], and how the firms have responded to our findings.

In accordance with our commitment to transparency, for the first time we will also be publishing later this year anonymised details of the key inspection findings and good practice points on the individual audits we reviewed.

In addition to our public reporting, we report our findings in more detail privately to the firms and also to their Recognised Supervisory Body for the purposes of its decision on their audit registration. From 2022, the FRC will be assuming responsibility for the registration of all firms which audit PIEs.

9 The seven largest firms are: BDO LLP, Deloitte LLP, Ernst & Young LLP, Grant Thornton UK LLP, KPMG LLP, Mazars LLP, PricewaterhouseCoopers LLP. We have published a separate report for each of these seven firms.

Our inspection and supervisory work in 2020/21 included:

- 103 statutory audits conducted by the largest seven firms, 16 at smaller firms and four at the National Audit Office. These audits were of financial statements for years ended between 30 June 2019 and 2 May 2020. We also inspected 22 local audits, which we report on separately later in the year, three other audits at the National Audit Office and one Third Country Audit, making an overall 149 inspections.

- Certain areas of the firms' quality control procedures (against the requirements of ISQC 1). We review these on a three year rotation basis at the seven largest audit firms and periodically for smaller firms.

- A focus on the firms' audit quality plans and RCA, both of which are important means of addressing audit quality issues and driving continuous improvement.

In 2020/21 our inspections focused on the following priority sectors and audit areas[10]:

Sectors	Audit areas
• Financial Services • Retail, including Retail Property and Travel & Leisure • Construction and Materials • Manufacturing	• Going concern and the viability statement • The Other Information in the Annual Report • Long-term contracts • The impairment of non-financial assets • Fraud risk • Application of new accounting standards (IFRS 15: revenue and IFRS 16: Leasing)

Our firm-wide inspection work in 2020/21 focused on audit firms' methodology and training, particularly relating to: revised auditing standards on going concern and the audit of estimates; and new or recently issued accounting standards on financial instruments (IFRS 9), revenue (IFRS 15) and leasing (IFRS 16).

At the conclusion of all individual audit inspections that are assessed as requiring more than limited improvements, we will consider whether the audit should be referred for consideration under the FRC's enforcement procedures. UK statutory audits may be referred to FRC's Case Examiner for consideration under the Audit Enforcement Procedure (AEP)[11]. The Case Examiner then decides on the appropriate course of action, which may involve Constructive Engagement with the audit firm to resolve less serious potential breaches of auditing standards and other requirements or referral to the FRC's Conduct Committee to consider whether an investigation should be opened. An investigation may result in financial and non-financial sanctions being imposed on an individual statutory auditor and/or the statutory audit firm. The FRC publishes details of all sanctions imposed. From our 2020/21 inspections, 18 audits have so far been referred to the Case Examiner (compared to 13 from our 2019/20 inspection cycle). The FRC's Annual Enforcement Review, published annually in July, contains further details of audits considered under the AEP.

As well as planned supervision and inspection activities, we also respond quickly to emerging issues. For example, during 2020/21 we responded to Covid-19 by issuing guidance to audit firms (and companies) and carrying out a thematic review of the audit of going concern which included inspecting samples of audit work. Our findings were that firms had reacted well to the new challenges. Our 2021/22 inspections will also focus on and take into account the impact of Covid-19 on audits.

10 https://www.frc.org.uk/news/december-2019-(1)/frc-announces-its-thematic-reviews-of-corporate-re

11 Other procedures apply to audits of non-UK entities (such as those incorporated in the Crown Dependencies)

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