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## Consultation Document: Firm-level Audit Quality Indicators

Dear Shamima,

Grant Thornton (Ireland) welcomes the opportunity to comment on the Financial Reporting Council (FRC) Consultation Document: Firm-level Audit Quality Indicators.

We set out below our detailed response to FRC's questions presented in the consultation document. In summary, we are of the opinion that further data needs to be presented to audit firms of the potential benefits of the proposed AQIs to stakeholders before the introduction of any mandatory AQIs. Exploration is required as to whether the proposed firm-level AQIs in the consultation document truly do reflect requirements of all stakeholders and what stakeholder decisions would be impacted by the provision of firm-level AQIs.

The information to be published may be useful but FRC should consider that it may be challenging to find the right balance between greater coverage (more firms, more data, and more granularity) and not over-burdening firms. We understand that widening the scope of AQI data may be beneficial but may also be counter-productive as it may lead to a ranking table within the industry.

Whilst the provision of narrative may reduce the risk, there is a risk that stakeholders will simply use the table of AQI scores to determine which firm to appoint as auditor, irrespective of other key factors. The provision of data in a table form of rankings may create unnecessary conflict with open market competition and inadvertently create an even bigger gap between the largest firms and challenger firms. We would request that the FRC provide more detailed considerations of the benefits of including a comparison table amongst firms and also the risk associated with it.

Overall, these AQIs are not very clear in defining quantitative measures that allow the determination of high, low, average or potential 'outliers', supporting the overall purpose of AQIs to identify potential quality issues. If qualitative measures were used without appropriate definition of terms, then it will be difficult to compare between firms and the data produced could be subject to misinterpretation. Clear quantitative measures will help to avoid any language or translation issues for AQIs, as these AQIs may be reviewed locally as well as internationally.

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

In principle, we agree that the firms reporting AQIs should be aligned to the scope of the revised Audit Firm Governance Code. However, we request that the FRC also consider the market perspective and the impact that compliance with the requirements will have on the different PIE firms.

From a market perspective, firms that audit the greatest number of entities in the PIE population are likely to be of most interest to stakeholders.

From an impact perspective, it is likely that the largest four firms already have the most advanced systems in place. It will require time and financial investment by firms to enable them to report the required AQIs. While a manual solution can be developed, there will also be a disproportionate ongoing cost associated with this and potential disruption to engagement teams, as well as the inherent risk associated with manually preparing data.

**Question 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 of the opinion that this raises the question as to whether the AQIs which are reported should be based on the entire audit practice, or only on each firm's PIE engagements. Reporting and segmenting both PIE and non-PIE may be useful, but some indicators are difficult to compare across all firms with different proportions of PIE and non-PIE audit clients. Given the wide range of sizes and structure of many audit firms, including the data from non-PIE engagements may not reflect the true image of audit quality within the firm. Segmenting the audit quality indicators between PIE and non-PIE will effectively double the amount of information presented without a guarantee that the data will be useful to different stakeholders (including users of audit services, investors, audit firms, etc.).

It is difficult to see how reporting AQIs for non-PIE audits is in public interest given they are not considered to be of public interest under the applicable definitions. We would like to understand whether stakeholders in non-PIE entities will be sufficiently interested in this data to warrant the time and cost of preparing such segmented AQI information.

As noted in the consultation document, investors and Audit Committee Chairs were not always aware that AQIs are reported in firms' Transparency Reports; it would be helpful to understand the benefits that these and other stakeholders have obtained from the publication of Transparency Reports to better inform the FRC's decisions on firmwide AQIs.

The nature of the proposed AQIs set out in the consultation document indicate that some would be beneficial only to PIEs (e.g. AQI number 6 Inspection results – internal) whereas others would not as they cannot by nature be segmented (e.g. AQI number 1 Staff/culture survey results, AQI number 9a Staff utilization, AQI number 10 Staff attrition and AQI number 13 Training).

We fully appreciate the intention of FRC is to have wider coverage but we do not fully see the benefit of the proposed approach of providing information for each AQI segmented between PIE audits and non-PIE audits.

**Question 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?**

We are of the opinion that reporting to a period that is not aligned to our financial year is unlikely to add significant additional cost beyond reporting to our financial period, although as raised in above comments, costs may be incurred to develop system-based solutions for a number of AQIs and it is expected that these will be substantial. In this regard, we would welcome a later date to allow for the most recent AQI data. A later date would also provide time for data collation and presentation happening outside of the traditional 'busy season' for many audit firms.

**Question 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.**

The proposal to include narratives in AQIs seems to be appropriate given that narratives can provide further information to AQI data being reported and explain directly what the numbers can't. With relevant narratives, the AQI is going to be more understandable and useful to the stakeholders.

We are of the opinion that supporting narrative is included to provide users with specific contextual information. Because of the differing nature of the client base of the firms proposed to be in scope for mandatory AQI reporting, without detailed narrative, the reader will only have a quantitative comparison between firms that could be misleading and result in poor decisions on auditor appointment being made which is counter-productive in nature.

Due to the importance of such narrative, we do not agree with the suggestion of a maximum word count to supporting narrative. However, we would suggest that a sample list of what should be included in the narrative be published as guidance to drive consistency across firms.

**Question 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.**

Generally, we agree with the 'proposed' AQIs however, we make the following specific comments:

- **AQI 1 Staff / Culture Survey results - Audit staff responses to certain annual staff / culture survey questions. The proposed indicator is "Percentage of favourable and unfavourable responses to the survey questions."**

In the context of Consultation Document AQI 1, it is unclear what "favourable and unfavourable responses to survey questions" mean. The AQI needs to be very specific on how the surveys will be structured. To ensure consistency, does the FRC propose to specify the exact

wording to be used by all firms in the staff survey? Without clear guidance, there is an inherent risk that firms may tweak the survey questions to produce favourable responses.

The survey guidance should be composed of highly objective audit quality questions by using concrete and straight-forward terminologies. If this AQI relies on overly subjective survey questions by firms, results may be less reliable and unverifiable. We are of the opinion that this AQI is unclear and susceptible to bias.

Lastly, is there an expectation that the annual survey will be undertaken at a specific point in time, to align with the reporting period of the 12 months to 31 March? We believe that each firm should be able to choose the timing of the annual surveys as it can provide important information that the firm can use for other processes.

- **AQI 2 Audit planning milestones - Completion of audit planning phase. The proposed indicator is “Percentage of audits meeting key planning milestones by the target completion date.”**

We believe that this AQI needs to be more clearly refined. The proposed indicator refers to the ‘target completion date’. Is there an expectation that each firm has the same ‘target completion date’?

Based upon the AQI description and proposed indicator, it is unclear on how this “Audit planning milestones” data should be collected. Each engagement has its own milestone depending on various factors such as timing of audit fieldwork based on client’s availability for the year, date when the client and the firm agreed to proceed with the engagement, possibility of delay in audit fieldwork due to client or auditor unavailability as a result of sickness, etc. The proposal should clearly lay down which specific milestones need to be reported.

We believe that there will be additional costs implications not just to produce the data in this AQI but to actually implement system-based solutions before the reporting period.

- **AQI 3a Proportion of audit hours by phases of audit - Proportion of audit effort by audit phase. The proposed indicator is “Average audit hours spent before the financial year-ends of audits in scope, as a percentage of total audit hours.”**

The AQI suggests that a higher percentage of hours spent upfront at the planning phase may indicate that audits are better planned, however, the term “higher percentage” was not clearly defined. Different engagements have their different profiles. One engagement may require more hours than another even when some of metrics are the same (e.g. audit fee or number of team members) because of different factors to consider. We believe that the AQI needs to clearly specify the parameters to be used. The AQI should also provide a clear cut-off date of “Audit planning” as firms may have different terminologies of same which could cause inconsistent comparative data.

- **AQI 3b the proposed indicator is “Average percentage of audit hours spent in the two weeks before sign-off.”**

This AQI suggests that high percentage of hours spent two-weeks before sign off date may impact audit quality, however, we are of the opinion that this may not produce accurate results. As mentioned above, different engagements have different profiles and considerations. For instance, the scheduling and availability of staff members should be factored in. Data to capture audit hours spent towards the last two weeks of the audit engagement may indicate impact to audit quality but there are numerous instances that are not.

- **AQIs 7, 8, 9a and 9b – extent of involvement of engagement team members to the audit by considering the average hours spent of total audit hours by each team members.**

These AQIs are standard indicators of how to measure of the involvement of each team members particularly the more senior members of the team such as the engagement partner, however, cleansing of data on a regular basis may be needed to make this effective which entails cost (extraction of data, analysis per engagement, resources assigned, etc.).

Further, the AQI should clearly specify the definition of “Higher involvement” of EQCR and partners to avoid any confusion and bias. Again, different engagements have different profiles, which means that there might be engagements that require higher involvement of staff members due to volume of audit procedures but will not require more time of EQCR and partner. Conversely, there are engagements that may require high number of hours from EQCR and partner because of complexity and high level of judgment required.

In AQI 9a staff utilization, the description refers to the ‘number of hours worked per week’; is there an expectation that weekly utilization data is presented? Would an annual utilization data using the following grading groups be more meaningful: Engagement leaders (partners and directors), managers (of all grades) and others.

- **AQI 10 Staff attrition - The rate at which staff leave the firm’s audit practice. The proposed indicator is “Average staff attrition rates by grade in the audit practice.”**

In the context of why this indicator is important, it is unclear what “high attrition levels” mean. The AQI needs to provide specific definitions specially that these terms will be used to measure AQIs in conjunction to audit quality. Using vague or undefined words will only cause more confusion to stakeholders rather than help them understand the data being reported.

The proposed AQI implies that high attrition levels may be indicative of resourcing pressure in completing audits, and therefore lower audit quality, however, there are various exceptions to be considered to reflect a more accurate data, for instance, there are staff members who leave the firm due to end of employment contract. Also, how is moving from one department to another to be measured and reported in this AQI as many firms encourage mobility within the organization? There also needs to be clear definition of which people are included in this AQI; for example, will this include non-fee earners, audit and accounting technical teams etc.?

- **AQI 11 Use of specialists - Extent of involvement of specialists, by types of specialised skills generally used in audits. The proposed indicator is “Average hours spent by specialists on audits as a percentage of total audit hours.”**

The AQI suggests that hours spent by specialists on audits be determined based on total audit hours as appropriate use of specialists improves the level of technical input, challenge, and quality of audits. This is in fact true and a valid AQI but clearly impossible to measure because of wide range of engagement profiles. The way the AQI should be measured should clearly be defined because not all audits need an engagement specialists.

- **AQI 13 Training - To demonstrate the level of investment in training offered to partners and staff. The proposed indicator is “Average number of mandatory training hours per person.”**

The AQI suggests that audit firms should have significant investment in training of people in the audit practice. Additionally, the AQI mentions that type, quality and relevance of the training are important considerations, however, it is unclear on what trainings to be reported and how to classify them. It should be considered that there are number of trainings invested by firms that are indirectly related to audit quality (e.g. soft skill trainings that are indirectly related to audit quality). The AQI should provide a clear guidance on this aspect so the data to be collected will be accurate and comparable across firms.

- **AQI 14 Diversity and inclusion - Gender and ethnic diversity of the firm’s audit leadership. The proposed indicator is “Percentage of individuals in the audit leadership, by gender and ethnicity.”**

We believe that diversity and inclusion is broader than gender and ethnic diversity. The AQI should be extended beyond the visible factors, to include areas such as social mobility, which would give greater insight to stakeholders. We support the principle, however, the AQI description was not able to demonstrate the direct connection to audit quality and hence, needs to be clarified.

**Question 6 - Do you think there are any other firm-level AQIs that we should consider? If so, please explain. (If relevant, please refer to the list of AQIs we have considered but not proposed, in Appendix 1.)**

Overall, we are of the view that the AQIs should be limited to those that are designated as 'proposed'. The AQIs marked as 'alternative/additions' are likely to be highly diverse depending on the nature of each firms' portfolio and hence will be less value to the reader.

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

The proposed AQIs will require time and financial investment by firms to enable them to report the required data. The FRC should consider this in their development of AQIs.

If you have any questions, please do not hesitate to contact me at [louise.barry@ie.gt.com](mailto:louise.barry@ie.gt.com)

Yours sincerely,



Partner - Head of Risk and Quality