Public Report

FRC Financial Reporting Council

February 2015

Grant Thornton UK LLP

Audit Quality Inspection

The FRC is responsible for promoting high quality corporate governance and reporting to foster investment. We set the UK Corporate Governance and Stewardship Codes as well as UK standards for accounting, auditing and actuarial work. We represent UK interests in international standard-setting. We also monitor and take action to promote the quality of corporate reporting and auditing. We operate independent disciplinary arrangements for accountants and actuaries; and oversee the regulatory activities of the accountancy and actuarial professional bodies.

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1. Background information and key messages

1.1. Introduction

This report sets out the principal findings arising from the 2014/15 inspection of Grant Thornton UK LLP ("Grant Thornton" or "the firm") carried out by the Audit Quality Review team of the Financial Reporting Council ("the FRC"). This inspection is referred to as the 2014/15 inspection and was conducted at various times in the period from December 2013 to September 2014 (referred to as "the time of our inspection"). We now inspect Grant Thornton annually (previously this was approximately every two years); our previous inspection report was published on 21 March 2013. The objectives of our work are set out in Appendix A.

Our inspection comprised reviews of individual audit engagements and a review of the firm's policies and procedures supporting audit quality.

We reviewed eight audit engagements undertaken by the firm, of which one was a further review of an audit reviewed in our previous inspection, selected on a risk basis utilising a risk model. These related to FTSE 100, FTSE 250, other listed and other major public interest entities, with financial year ends between March 2013 and March 2014. Each review covered only selected aspects of the relevant audit. The further review included an assessment of the extent to which our previous findings on that audit had been addressed.

Our responsibility is to monitor and assess the quality of the audit work performed by the UK firm. Accordingly, our reviews of group audits covered the planning and control of the audit by the group engagement team, including their evaluation of the adequacy of the work performed by component auditors, and selected aspects of other work performed by the UK firm at group and/or component level. Our reviews did not cover audit work relating to components undertaken by other firms within or outside Grant Thornton's international network.

Our review of the firm's policies and procedures supporting audit quality covered the following areas:

- Tone at the top and internal communications
- Transparency report
- Independence and ethics
- Performance evaluation and other human resource matters
- Audit methodology, training and guidance
- Client risk assessment and acceptance/continuance
- Consultation and review
- Audit quality monitoring
- Other firm-wide matters

We exercise judgment in determining which findings to include in our public report on each inspection, taking into account their relative significance in relation to audit quality, both in the context of the individual inspection and in relation to any areas of particular focus in our overall inspection programme for the relevant year. Where appropriate, we have commented on themes arising or issues of a similar nature identified across more than one audit.

Further information on the scope of our work and the basis on which we report is set out in Appendix A.

All findings requiring action set out in this report, together with the firm's proposed action plan to address them, have been discussed with the firm. Appropriate action may have already been taken by the date of this report. The adequacy of the actions taken and planned will be reviewed during our next inspection.

The firm was invited to provide a response to this report for publication. The firm's response is set out in Appendix B.

We acknowledge the co-operation and assistance received from the partners and staff of Grant Thornton in the conduct of our 2014/15 inspection.

1.2. Background information on the firm

Grant Thornton UK LLP is a limited liability partnership with 26 offices. It is a member of Grant Thornton International Limited, a global network of firms using common audit methodology and audit software. The firm is a unitary partnership and, as such, there are no non-equity partners.

For the year ended 30 June 2014, the firm's turnover was £512 million, of which £135 million related to audit. There were 192 partners, of whom 62 were authorised to sign audit reports, and in addition 52 employees (audit directors and associate directors) were also authorised to sign audit reports[1]. Over the last three years, the number of employees authorised to sign audit reports has been increasing and the number of partners authorised to do so has been decreasing. As a result, the number of employees authorised to sign audit reports is about 45% of all those authorised to do so.

2015 will see a new CEO at Grant Thornton. The firm announced details in December 2014 with the successful candidate taking up her role in June 2015.

We estimate that the firm audited 227 UK entities within the scope of independent inspection as at 31 December 2013. Of these entities, our records show that 63 had securities listed on the main market of the London Stock Exchange, including one FTSE 100 company and three FTSE 250 companies.

Audits of entities incorporated in Jersey, Guernsey or the Isle of Man whose securities are traded on a regulated market in the European Economic Area are inspected by us under separate arrangements agreed with the relevant regulatory bodies in those jurisdictions. The firm and relevant bodies have informed us that the firm was not registered to conduct audit work in any of these jurisdictions.

Grant Thornton is the largest supplier of audit services to local authorities and the NHS. Whilst we review audits of public sector entities undertaken by firms (Local Public Audits - LPAs), this is done under separate arrangements agreed with the Audit Commission. The results of these reviews are not included in this report, because the LPA inspections fulfil a different purpose to those considered in this report. The reviews of LPAs, which we undertake for the Audit Commission, form part of their assessment of the quality of contracted-out audits. The Audit Commission publishes its assessment both in overall terms and individually by firm. The most recent report can be found on the Audit Commission's website.

[1] As disclosed in the annual return to the ICAEW as at December 2013

1.3. Overview

We focus in this report on matters where we believe improvements are required to safeguard and enhance audit quality. We set out our key messages to the firm in this regard in section 1.4. While this report is not intended to provide a balanced scorecard, we highlight certain matters which we believe contribute to audit quality, including the actions taken by the firm to address findings arising from our prior year inspection.

The firm places considerable emphasis on its overall systems of quality control and, in most areas, has appropriate policies and procedures in place for its size and the nature of its client base. Nevertheless, we have identified certain areas where improvements are required to those policies and procedures. These are set out in this report.

Our findings relating to the review of individual audits, as set out in section 2, largely relate to the application of the firm's procedures by audit personnel, whose work and judgments ultimately determine the quality of individual audits. In response to the findings arising from our previous inspection, the firm considerably strengthened its internal communications about audit quality. In addition, the firm's training in relation to professional scepticism has improved. Nonetheless, a number of our more significant findings still relate to a lack of appropriate professional scepticism or challenge of management and therefore further action is required to ensure the proper application of these attributes in the firm's audits.

In respect of two audits requiring significant improvement, we requested that the firm carry out further audit work. In both cases the firm has confirmed that further work has been performed and that it considers that the audit reports remain appropriate.

1.4. Key messages

The firm should pay particular attention to the following areas in order to enhance audit quality and safeguard auditor independence:

- Identify the root causes of the continuing deficiencies identified in the performance of the firm's audits.

- Ensure that actions taken by the firm to improve the quality of individual audits, following both internal and external quality reviews, address the causes of any deficiencies and are applied effectively by individual audit teams. The changes should be implemented on a more timely basis.

- Take further action to embed the proper application of professional scepticism and challenge of management in the firm's audits.

- Strengthen the firm's quality control procedures related to the direction, supervision and review of individual audits, including improving the effectiveness of Engagement Quality Control Reviews.

- Strengthen the link between high quality audit work and reward.

2. Principal findings

The comments below are based on our reviews of individual audits and the firm's policies and procedures supporting audit quality.

2.1. Reviews of individual audits

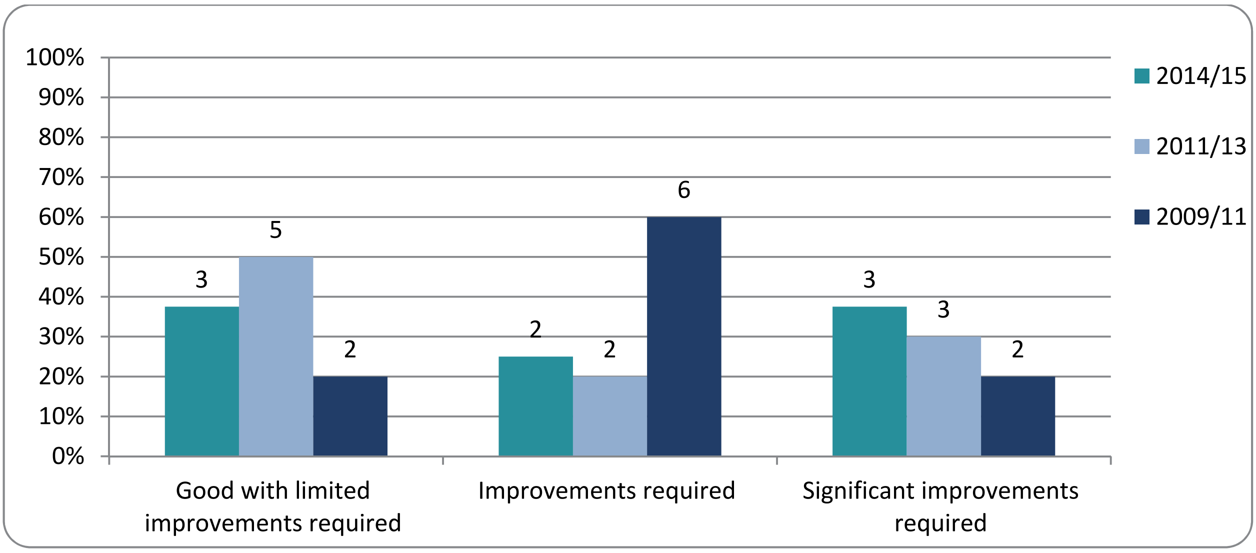
We reviewed and assessed the quality of selected aspects of eight audits (2011/13: 10 audits), of which one was a further review of an audit reviewed in our last inspection which included an assessment of how findings previously raised had been addressed (2011/13: one follow-up review was also undertaken).

Three of the audits we reviewed were performed to a good standard with limited improvements required and two audits required improvements. Three audits required significant improvements in relation to one or more of the following areas: insufficient involvement in and supervision, direction and control of group audits; lack of management challenge or professional scepticism in a number of areas of judgment or estimate; and insufficient evidence of appropriate reporting to audit committees. Further details are set out below.

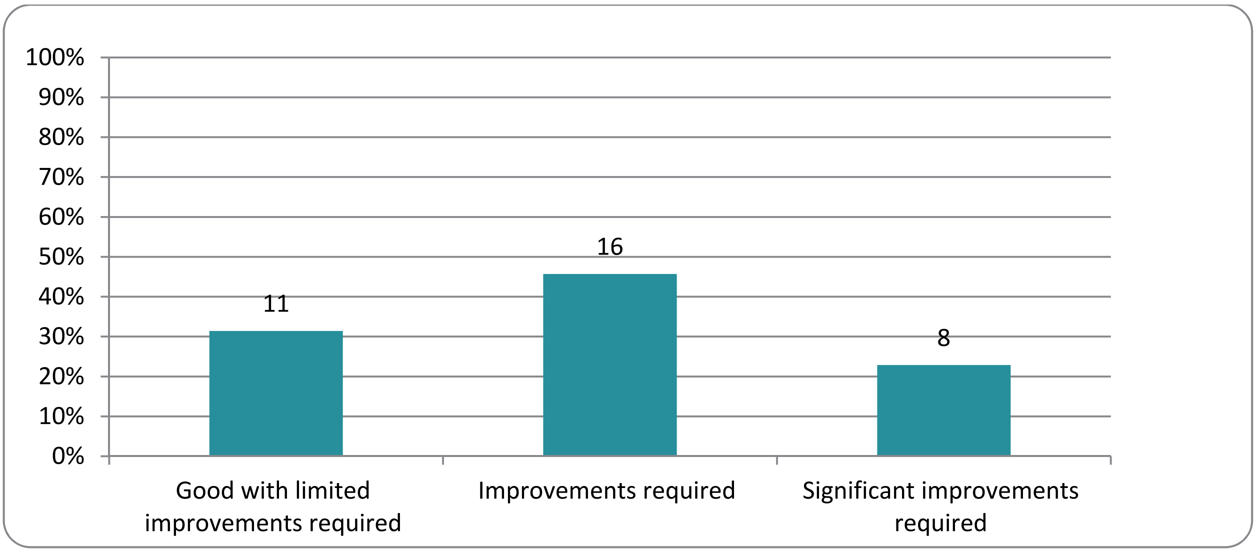
An audit is assessed as requiring significant improvements if we had significant concerns in relation to the sufficiency or quality of audit evidence or the appropriateness of significant audit judgments in the areas reviewed or the implications of other matters are considered to be individually or collectively significant. This assessment does not necessarily imply that an inappropriate audit opinion was issued.

We were disappointed by the number of audits, out of the eight reviewed, assessed as requiring significant improvements and that our further review of an audit assessed as requiring significant improvements during the last inspection again fell within this category. In respect of two of the three audits concerned, we requested that the firm carry out further audit work to determine whether the audit opinion it issued remains appropriate. In both cases the firm has confirmed that further work has been performed and that it considers that the audit reports remain appropriate.

The bar chart below shows the results of our assessment of the quality of the audits we reviewed in 2014/15, with comparatives for 2011/13 and 2009/11. The number of audits within each category is shown at the top of each bar.



Changes to the proportion of audits falling within each category from year to year reflect a wide range of factors, which may include the size, complexity and risk of the individual audits selected for review and the scope of the individual reviews. For this reason, and given the sample sizes involved, changes from one year to the next are not necessarily indicative of any overall change in audit quality at the firm. In the bar chart below, we have therefore provided summary information over a longer period and, consequently, based on a larger number of audits. This shows the proportion of audits reviewed falling within each category in the four inspections up to and including 2014/15. The number of audits is shown at the top of each bar.



Findings in relation to audit evidence and judgments

Our reviews focused on the audit evidence and related judgments for material areas of the financial statements and areas of significant risk. We draw attention to the following findings which the firm should ensure are addressed appropriately in future audits.

The significance of these findings in the context of an individual audit reviewed, and therefore the implications for our grading of that audit, will vary. However, whatever the implications for the specific audits reviewed, we nevertheless include the relevant findings in this report if we consider them important in the broader context of improving audit quality at the firm.

Challenge of Management

We identified concerns on four audits regarding the level of professional scepticism or challenge of management applied in key audit areas.

On two audits, management used cash flow models to assess impairment. In these cases the audit team did not challenge certain assumptions sufficiently; obtain audit evidence to support some of the inputs into the model (for example, forecast prices); or, in one case, follow-up identified weaknesses in the evidence to support the extent of impairment.

On four audits management were not sufficiently challenged in one or more of the following areas:

- to support their view that none of the balance of an outstanding tax claim, in an overseas jurisdiction, should have been provided for, rather than disclosed as a contingent liability, given that available correspondence indicated that the balance would need to be paid;

- regarding the recoverability of a corporation tax asset. The forecasts supporting recoverability were prepared by the audit team and not, as we would expect, by management;

- to provide evidence to support the recoverability of work in progress. An error was identified which, when extrapolated by the audit team, suggested the existence of a material error. Whilst the audit team agreed with management's view that the extrapolation method was not appropriate, it did not request further evidence to support management's assertion;

- regarding the recognition of only 50% of a tax reclaim as a contingent asset, rather than recognising the full amount or none of it; and

- regarding the non-consolidation of a 60% equity interest investment treated as an associate and the adequacy of related disclosures.

Independent third party confirmations

We raised issues in our previous inspection concerning confirmations requested from third parties but not received and for which there were no adequate follow up procedures. On this inspection, there were two audits where the audit team did not maintain control over the external confirmation process or evaluate the reliability of evidence provided. On one audit direct responses were not received to solicitors' letters and, on the other, a bank balance confirmation was received by email via the audited entity rather than being sent directly to the audit team. In both audits, certain letters requesting confirmations were sent out by the audited entity and not, as they should have been by the audit team.

Group audit matters

On one audit the involvement in and supervision, direction and control of the group audit by the group audit team was inadequate. On this audit, where all the audited entity's operations are overseas, the component auditor failed to set out the planned audit procedures on high risk areas; did not complete the audit procedures instructed by the group audit team; or submit the requested group reporting documents. The group audit team did not challenge the inadequate reporting by the component auditor. The group engagement leader placed significant reliance on the review of the component auditor's files by a senior manager. The scope and findings of this review, however, were not recorded in sufficient detail to clarify or challenge the nature and extent of the component auditor's work. Furthermore, there was no evidence that the Engagement Quality Control Reviewer (EQCR) had challenged the approach to this audit and the basis upon which the audit opinion was signed.

IT general and application controls

On three audits we reviewed the application of the firm's methodology in relation to the audit of IT general and application controls. We identified certain concerns over aspects of the testing, which included: inadequate consideration of completeness of exception reports, with no follow up of the exceptions identified; using a predefined sample size without rationale; not testing the completeness and accuracy of data; excluding certain, apparently, key systems from the scope of work; and not keeping screenshots as evidence of work done.

Inventory

On one audit, there was insufficient justification for only visiting four sites given that all 12 sites had material stock balances and some sites had not been visited since 2003 or 2008. Without testing the effectiveness of internal controls, there was insufficient audit evidence of the existence and condition of inventory at the eight sites not visited.

The firm's audit methodology did not include relevant guidance on the extent of audit testing required for multiple stock locations such as the number of sites to visit or the number of items to select for testing at each site. We have been informed by the firm that such guidance has now been developed.

Other findings

Materiality

On four audits, we identified concerns with the level of materiality set by the audit team and/or the rationale for the level set.

On one audit the level of materiality was based on a percentage of EBITDA[2] that although in-line with the firm's guidance was, in our view, too high. On two further audits there was insufficient justification recorded for the levels selected. The firm's guidance in this area should be revised.

On another audit, there was no consideration of aspects of the audit (in this case directors' remuneration and related party balances and transactions) to which lower levels of materiality should be applied.

Audit report and disclosures

On three audits, an extended audit report was issued[3]. On two of these audits the level of audit work described in the audit report was inconsistent with the actual work performed and may have given more assurance to readers of the report than was appropriate.

In addition, on three audits there were disclosure omissions and/or audit report wording errors which had not been identified by the firm's quality control procedures.

Communicating with Audit Committees

Since our last inspection, the firm has introduced new templates for reporting to Audit Committees, at both the planning and completion stage, and this has improved the quality of most communications. The use of these templates is, however, not mandatory. We recommend that the new templates are made mandatory.

Certain aspects of reporting to Audit Committees, or their equivalent, required improvement on four audits; for example, disclosure omissions were either not reported to the Audit Committee or they were not requested to correct errors, as required. In one audit, the communication of risks did not separately highlight some of those risks as 'significant risks', as encouraged by the Auditing Standards.

On one audit, there was insufficient evidence of sufficient and appropriate communication and discussion with the Audit Committee. Although we understand that the audit plan was sent to all

[2] Earnings before interest, taxation, depreciation and amortisation.
[3] ISA (UK and Ireland) 700 - The independent auditor's report on financial statements (revised June 2013).

the members of the committee, there was no formal audit planning meeting and therefore no opportunity for the committee members to discuss or challenge the proposed audit approach with the auditors. The group engagement leader did not address the full Audit Committee until a closing conference call.

2.2. Review of the firm's policies and procedures

The firm's policies and procedures are developed in the UK, within the context of the minimum requirements of the Grant Thornton International Limited (GTIL) guiding principles. The firm's audit methodology is built by GTIL with input from member firms. It is a tool made available by GTIL to member firms, but it remains the responsibility of Grant Thornton and other member firms to decide how that tool is used to conduct individual audits. In 2014, GTIL and Grant Thornton commenced two projects to design and develop a new global audit methodology and supporting technologies and a global training platform. We understand that the projects will be progressively phased over the next three years, with global audit training rolled out through early 2015.

The firm developed an overall strategy for the three years to 2015 ("Ambition 2015"). Emphasis is placed on the quality of the firm's work as a means of achieving that growth and messages relating to audit quality are regularly communicated to partners and staff. These messages have been strengthened since our last inspection.

While the review of public sector audit work is outside the scope of this report, we note that Grant Thornton became the largest supplier of audit services to local authorities and the NHS, when the Audit Commission awarded contracts in 2012. The five year contracts began in September 2012. To date the integration and training of the 300 professional staff that transferred, from the Audit Commission to Grant Thornton, appears to have been successful.

Improvements made since our last inspection

In response to our last inspection findings, the firm strengthened considerably its internal communications about audit quality. In addition, the firm's training in relation to professional scepticism has improved. The most significant improvement from a firm-wide perspective is the launch of a new integrated HR system; this links appraisals with personal development plans and allows attendance at training and other learning activities to be monitored more effectively.

Prior inspection findings not adequately addressed

The number of prior inspection findings that have recurred during the current review is disappointing. The firm should consider whether the actions taken to date adequately address the actual root cause of the findings and how those actions can be made more effective. The most significant of these findings are set out below.

Partner appraisals

In response to our previous inspection, partners and staff were reminded that specific comments relating to selling non- audit services to audit clients should not be included in appraisal documentation.

A number of the partner appraisals reviewed still included references to non-audit fees, either in the objectives or the comments on performance. In some cases the references were in relation to audit clients and in others it was unclear whether they related to audit clients or not. The firm has informed us that these remarks were not taken into account when evaluating performance, or making promotion or remuneration decisions. There was, however, no evidence that these comments had been challenged.

The firm needs to ensure that its partners and staff understand that no recognition will be given for selling non-audit services to their own audit clients, and that such recognition should not be sought.

Passwords

As previously reported, in October 2012, the firm discovered that an individual had abused the process for changing and re-setting electronic passwords, within the audit software system. The firm's investigations did not suggest that inappropriate password resetting was a systemic issue. We requested in our previous report that the underlying system weakness be addressed.

The firm undertook to carry out six-monthly reviews of their audit system, to identify inappropriate changes to passwords until other controls had been considered. At the time of our inspection, whilst the results of the January 2013 review were available, the results of later testing were not. We understand that subsequent reviews have now been carried out and that detection controls continue to operate, with no further issues arising. However, we remain concerned that no preventative controls have been considered.

Use of the ethics queries system

E-mail queries continue to be raised directly with the Ethics Partner alongside the dedicated ethics query system. Whilst we have not identified incorrect ethical judgments having been reached as a result of this approach, we highlight the risks it presents. These risks include e-mail queries being less formal and potentially not including all the facts and inconsistent advice being given. We understand that a new system is to be designed to manage all auditing, accounting and ethics queries which will also become a database of advice given. Steps should be taken to ensure that this new system is appropriately used.

Rotation

The firm identified that there were four (non-public interest) audits where the respective audit partners have been involved for 20 years or more, with the only safeguards being manager rotation and the appointment of an independent review partner. While these are a very small part of the firm's portfolio and there are safeguards in place, rotation is likely to be the only way to safeguard auditor independence, as the significance of the threat increases the longer the audit engagement partner's period of involvement. The firm should address this issue by promptly re-allocating the engagements to different partners.

Audit Quality Monitoring - Grading of file reviews

The firm's annual quality review processes are detailed with a well-structured moderation process. We commented in our previous report that some grades awarded on individual file reviews did not appear to be consistent with the number and significance of the findings identified.

The grading process would be further enhanced if the firm issued guidance to reviewers to help them to take account of the number and importance of findings when proposing an overall grade for moderation.

Current year findings

We identified certain further areas, as set out below, where improvements to the firm's policies and procedures are required. In addition, section 2.1 sets out findings identified in our reviews of individual audits, a number of which should also be addressed in the firm's methodology.

Monitoring of prohibited investments

Ethical Standards require partners to dispose of any financial interests in audited entities immediately, or as soon as possible after, the relevant person has actual knowledge of, and the right to dispose of, the interest[4]. The firm's application guidance, which also applies to staff or indirect investments in audited entities, is that any such holdings must be disposed of within 14 days of the individual being notified that the interest has become restricted. The firm should reconsider this policy in light of the requirements of the Ethical Standards.

There were nine breaches of the firm's policy, including a case where a partner and their spouse held an investment in an audited entity and did not dispose of it within the 14 days the firm required.

Partner rotation extensions

There were 19 requests for extensions to partner rotation periods during the 12 months to May 2014. 11 of these were granted and the remaining eight were either fully declined, had to be resubmitted or a one year extension only was granted. In our view, this level of requests and extensions is too high. The firm should review whether the level of extensions granted is appropriate given the requirements of the Ethical Standards.

Audit Quality Objectives

Of the 10 appraisals reviewed, three were in respect of partners who had the lowest audit quality rating (a poor AQR inspection assessment will have informed such ratings). We are concerned that where audit quality issues have been identified for particular partners, focused objectives to address these concerns are not always evident from the appraisal. Such objectives should reflect the targeted intervention we understand that the firm has agreed with those individuals (eg refresher training, reduction of responsibility or limitation to lower risk audits). When setting objectives, individuals should record specific audit quality-related objectives.

Performance ratings

Of the 10 partner appraisals reviewed, the three partners who had an audit quality rating of five (Serious shortcomings) had an overall performance rating of two (Good contribution - i.e. the individual performs to a good standard meeting the requirements of the role).

We are concerned that other performance measures are allowed to mitigate significant audit quality shortcomings in arriving at the overall appraisal ratings. In our view, more emphasis should be given to the audit quality grading so as to limit the overall performance rating. Notwithstanding their appraisal grade, we note that the firm did take specific action in response to the low audit quality grade of these three partners, including financial penalties.

[4] APB Ethical Standard 2, Financial, Business, Employment and Personal Relationships – Paragraph 14.

Audit update training

The annual audit update training was incorporated into the annual audit conference. Although the training was not compulsory, all relevant partners and staff who were unable to attend were subsequently invited to attend office-based versions of the core training; A small number of individuals did not attend either the conference or the office training.

Regular audit update training is important for maintaining audit quality and helping partners and staff to undertake relevant continued professional development. We are concerned that there was no mandatory audit update training in the past year and that there is no central monitoring to ensure that all audit training is completed. We understand that the new integrated HR system will allow central monitoring of training.

Assignment of personnel to audits

On one audit, an individual had been assigned as the engagement leader despite obvious barriers to their involvement in the group audit due to language issues and a medical condition that restricted the individual's ability to travel to the main component's country of operation; these factors do not appear to have been considered as part of the engagement allocation process.

Letterbox companies

In May 2013, we wrote to the major audit firms regarding concerns arising from our reviews of audits of "letterbox companies"[5] and the need for them to take action to achieve improvements in their approach to such audits.

The firm informed us that by reference to the full definition (including the geographical location of group senior management) it did not believe that it had any such audit clients. However, we have identified a number of the firm's audit clients that meet much of the definition (for example all economic activity being based elsewhere resulting in the firm performing little of the underlying audit work themselves). We reviewed one audit of this type and have commented on this group audit above.

Whilst the firm responded promptly to alert the audit practice of our concerns regarding letterbox companies, and has recently updated its guidance for partners and staff, we were disappointed that the firm's guidance was not updated on a more timely basis.

IT general and application controls

We reviewed the firm's methodology, guidance and training in relation to the audit of IT general and application controls and had no significant findings in this area. We considered the application of the methodology in three audits and our findings in relation to these audits are detailed in section 2.1.

Engagement Quality Control Reviews

In December 2012 the firm launched the Engagement Quality Review Team (EQRT) concept for immediate implementation on audits within the scope of AQR. The team for any particular audit consists of a partner and manager, sharing aspects of the review. This was intended to allow the partner acting as the Engagement Quality Control Reviewer (EQCR) to focus on the challenge of

[5] Letterbox companies are those groups or companies that have little more than a registered office in their country of registration, with management and activities being based elsewhere. In such situations, the auditor is usually based in the country of legal registration, rather than where management is based.

significant risks and judgments, with the manager taking responsibility for more routine parts of the review.

A number of our review findings related to issues around judgments, evidence and processes that were not challenged and addressed by the EQRT review process.

The firm should reconsider the current and future allocation of EQCRs to certain audits, in particular, ensuring that the EQCR is sufficiently experienced or senior to challenge the engagement partner.

Audit Quality Monitoring - Audit reports

The firm's own 2013 audit quality monitoring process identified audit report wording errors in over 30% of the files reviewed. Whilst these errors were all assessed as minor, they indicate a failure by audit partners and staff to review critically the wording of reports. These results are consistent with the findings of certain of our reviews of individual audits.

Other matters

Banking thematic review

In December 2013 the FRC announced that during 2014 it would perform a thematic review of the quality of bank and building society audits, focusing on the audit of loan loss provisions and related IT controls. The thematic review sought to identify why progress in improving audit quality in these areas had been slow and what further action was needed to achieve the necessary improvements. As part of the thematic review, we reviewed the policies and procedures applied by the firm in conducting bank audits.

Grant Thornton only has a small share of the banking sector audit market. Nonetheless, the firm should ensure that audit engagement leaders and staff who are involved in these audits maintain a level of practical and technical knowledge that is required for effective audits of the institutions that are audit clients.

The firm should also take action to ensure that appropriate succession plans are in place for partners and senior staff on the firm's bank audit clients.

The FRC published a report in December 2014 setting out the principal findings of the thematic review and identifying key messages arising for both auditors and audit committees.

Transparency report

We reviewed the firm's transparency report for the year to 30 June 2013 which was published in September 2013, to assess whether the information in the report was consistent with our understanding of the firm's quality control and independence procedures. We did not identify any inconsistencies with our understanding of the firm's quality control and independence procedures.

Andrew Jones

Director

Audit Quality Review

FRC Conduct Division

February 2015

Appendix A – Objectives, scope and basis of reporting

Scope and objectives

The overall objective of our work is to monitor and promote improvements in the quality of auditing. As part of our work, we monitor compliance with the regulatory framework for auditing, including the Auditing Standards, Ethical Standards and Quality Control Standards for auditors issued by the FRC and other requirements under the Audit Regulations issued by the relevant professional bodies. The standards referred to in this report are those effective at the time of our inspection or, in relation to our reviews of individual audits, those effective at the time the relevant audit was undertaken.

Our reviews of individual audit engagements and the firm's policies and procedures supporting audit quality cover, but are not restricted to, the firm's compliance with the requirements of relevant standards and other aspects of the regulatory framework. Our reviews place emphasis on the appropriateness of key audit judgments made in reaching the audit opinion together with the sufficiency and appropriateness of the audit evidence obtained. We also assess the extent to which the firm has addressed the findings arising from our previous inspection.

We seek to identify areas where improvements are, in our view, needed in order to safeguard audit quality and/or comply with regulatory requirements and to agree an action plan with the firm designed to achieve these improvements. Accordingly, our reports place greater emphasis on weaknesses identified which require action by the firm than areas of strength and are not intended to be a balanced scorecard or rating tool.

Our inspection was not designed to identify all weaknesses which may exist in the design and/or implementation of the firm's policies and procedures supporting audit quality or in relation to the performance of the individual audit engagements selected for review and cannot be relied upon for this purpose.

The professional accountancy bodies in the UK register firms to conduct audit work. Their monitoring units are responsible for monitoring the quality of audit engagements falling outside the scope of independent inspection but within the scope of audit regulation in the UK. Their work, which is overseen by the FRC, covers audits of UK incorporated companies and certain other entities which do not have any securities listed on the main market of the London Stock Exchange and whose financial condition is not otherwise considered to be of major public interest. All matters raised in this report are based solely on the work which we carried out for the purposes of our inspection.

Basis of reporting

We exercise judgment in determining those findings which it is appropriate to include in our public report on each inspection, taking into account their relative significance in relation to audit quality, in the context of both the individual inspection and any areas of particular focus in our overall inspection programme for the year. Where appropriate, we have commented on themes arising or issues of a similar nature identified across more than one audit.

While our public reports seek to provide useful information for interested parties, they do not provide a comprehensive basis for assessing the comparative merits of individual firms. The findings reported for each firm in any one year reflect a wide range of factors, including the number, size and complexity of the individual audits selected for review which, in turn, reflects the firm's client base. An issue reported in relation to a particular firm may therefore apply equally to other firms without having arisen in the course of our inspection fieldwork at those other firms in the relevant year. Also, only a small sample of audits is selected for review at each firm and the findings may therefore not be representative of the overall quality of each firm's audit work.

The fieldwork at each firm is completed at different times during the year and rigorous quality control procedures are applied. These procedures include a peer review process at staff level and a final review by independent non-executives who approve the issue of all reports. These processes are designed to ensure both a high quality of reporting and that a consistent approach is adopted across all inspections.

We also issue confidential reports on individual audits reviewed during an inspection. While these reports are addressed to the relevant audit engagement partner or director, they are copied to the chair of the relevant entity's audit committee (or equivalent body).

Purpose of this report

This report has been prepared for general information only. The information in this report does not constitute professional advice and should not be acted upon without obtaining specific professional advice.

To the full extent permitted by law, the FRC and its employees and agents accept no liability and disclaim all responsibility for the consequences of anyone acting or refraining from acting in reliance on the information contained in this report or for any decision based on it.

Appendix B – Firm's response

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29 January 2015

Dear Mr Jones

Grant Thornton UK LLP: FRC Public Report on the 2014/15 Inspection

We welcome the opportunity to respond to the report on the AQRT's 2014/15 inspection of Grant Thornton UK LLP. We appreciate the insights provided by the review team members that enable us to further enhance and improve our reputation for audit quality.

We are pleased to see recognition of the significant strengthening of our internal communications about audit quality and of the improvements to our training in relation to professional scepticism. We have already implemented new or enhanced policies and procedures designed to address other recurring issues identified in the report and the impact of these developments is beginning to be evidenced in the findings of internal quality reviews.

The grades allocated to the small sample of our in-scope engagements that were selected for the 2014/15 review were not as favourable as the grades allocated by the preceding review. However, even where an inspection concluded that 'significant improvements' were required to an audit, the further audit work that we have performed in response to the review findings confirmed that our audit opinion was appropriate.

As noted in Section 1.2, the report does not include the results of two recent reviews by the AQRT of financial statement audits on behalf of the Audit Commission which were reported as being "acceptable with limited improvements required".

The achievement of the firm's ambitions for the short to medium term depends critically on the quality of our audit service. Our approach to the delivery of audit quality is set out in our Transparency Report that can be accessed at http://www.grant-thornton.co.uk/Documents/transparency-report-2014.pdf.

Yours sincerely

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