

Audit Inspection Unit

Annual Report 2010/11



19 JULY 2011



This report is issued by the Audit Inspection Unit of the UK's Professional Oversight Board ("the Oversight Board"), part of the Financial Reporting Council. It has been approved for publication by the Oversight Board.

Contents	Page
----------	------

ONE

Introduction key issues and concerns	5
--------------------------------------	---

TWO

Summary of activities	11
-----------------------	----

THREE

Overview of AIU findings	19
--------------------------	----

APPENDIX A

Inspection process and basis of reporting	30
---	----

APPENDIX B

Scope of inspections 2010/11	33
------------------------------	----

Introduction key issues and concerns

1.1 Introduction

This report provides an overview of the activities and findings of the Audit Inspection Unit (“the AIU”) of the Professional Oversight Board (“the Oversight Board”), a part of the Financial Reporting Council (“the FRC”), for the year ended 31 March 2011.

The AIU reviews the quality of the statutory audits of listed and other major public interest entities that fall within its scope, as determined each year by the Oversight Board, and of the firms’ policies and procedures supporting audit quality¹.

Firms which audit more than ten entities within the AIU’s scope are subject to full scope AIU inspections covering both the review of policies and procedures supporting audit quality and the review of a sample of individual audits. There are currently ten such firms (“the major firms”) as follows:

Baker Tilly UK Audit LLP	Grant Thornton UK LLP
BDO LLP	KPMG LLP and KPMG Audit PLC
Crowe Clark Whitehill LLP	Mazars LLP
Deloitte LLP	PKF (UK) LLP
Ernst & Young LLP	PricewaterhouseCoopers LLP

Firms that audit between one and ten entities falling within the AIU’s scope are referred to as “smaller firms” in this report. The AIU’s inspections of smaller firms are limited to a review of a sample of individual audits falling within its scope².

1.2 Structure of this report

This report is set out under the following sections:

- **Section 1** details key issues and concerns and discusses the effectiveness of AIU inspections,
- **Section 2** summarises the inspection and other activities undertaken by the AIU in 2010/11,

¹ The Companies Act 2006, as amended, requires the independent inspection of auditors undertaking statutory audits of listed companies and other entities in whose financial condition there is considered to be major public interest. This latter category is determined from time to time by the Oversight Board.

² The Companies Act 2006, as amended, permits the Oversight Board to delegate inspection activities to the monitoring units of the Professional Accountancy Bodies for those firms conducting ten or fewer audits within the AIU scope. The Oversight Board has chosen to delegate the monitoring of firm-wide procedures in relation to these firms.

Introduction

key issues and concerns

- **Section 3** provides an overview of findings arising from the AIU's inspections at major and smaller firms in 2010/11,
- **Appendix A** provides information on the AIU's inspection process and basis of reporting, and
- **Appendix B** details the scope of inspections for 2010/11 as determined by the Oversight Board.

1.3 Key issues and concerns

Inspection results are as good as, or slightly better than, those of last year. In particular, the AIU has seen a reduction in the number of FTSE 350 audits assessed as requiring significant improvement³. While this is encouraging, the AIU cannot confirm that this is a positive underlying trend until it is replicated more consistently across all types and size of engagement.

Set out below are a number of key issues and concerns arising from the AIU's inspection activities which it believes should be addressed in order to improve audit quality. These matters are discussed further in Section 3.

Professional scepticism

- The AIU's findings continue to identify the need for firms to ensure that both partners and staff exercise appropriate professional scepticism, particularly in respect of key areas of audit judgment such as the valuation of assets and the impairment of goodwill and other intangible assets.
- A number of actions have been taken, or are in the process of being taken, by firms to address the AIU's concerns in respect of professional scepticism. Since many of these actions were taken subsequent to the completion of the audits reviewed in the 2010/11 inspections, any improvements that might be expected are, therefore, not reflected in the AIU's findings.

Focus on audit quality

- Given the current economic climate which has led to a decline in fee income⁴, when seeking to grow their businesses and obtain further efficiencies in the conduct of audits, firms must ensure that this is not at the expense of audit quality. The importance of audit quality should be reinforced, and its achievement appropriately rewarded at all levels within audit firms.

³ The AIU assesses the quality of each audit it reviews to arrive at an overall grade. For public reporting the AIU uses three grades: good with limited improvements required; acceptable but with improvements required; and significant improvements required. These grades are discussed further in Section 3.2.1.

⁴ See Professional Oversight Board: Key Facts and Trends in the Accountancy Profession, June 2011

Auditor independence

- The proper identification and assessment of threats and safeguards is crucial to the effectiveness of the Ethical Standards in maintaining auditor independence. Firms must recognise that this is particularly important at a time when the need for more specific prohibitions is being debated.
- Partners and staff must be in no doubt that auditor independence must not be compromised by an inappropriate focus on selling non-audit services to audited entities. This continues to be an area of concern.

Group audits

- Firms, and in particular smaller firms, should carefully consider whether they have the appropriate resources, expertise and involvement to undertake audits of multi-national groups to the required standard.
- When performing the audit of a UK subsidiary of a large overseas group where the audit approach is designed for the group as a whole, firms must ensure that they obtain sufficient audit evidence to support their statutory audit opinion on the UK subsidiary. This issue is particularly relevant to the audits of UK components of international financial institutions.

Audit committee reporting

- Audit committee reporting should include a clear and unequivocal statement of the auditor's views on key areas of audit judgment.

Engagement quality control review

- Engagement quality control reviewers have an important role to play in improving audit quality and ensuring that management's assertions are appropriately challenged. The AIU's findings suggest that the full benefits of this important safeguard have yet to be realised.

Audit of disclosures

- Greater attention should be given to the audit of the disclosures in financial statements, especially those in respect of key areas of judgment, to ensure that sufficient appropriate disclosures to meet the needs of users have been made.

Introduction

key issues and concerns

1.4 Effectiveness of AIU inspections

Inspection process

The AIU's inspection process continues to be both rigorous and challenging for firms. On reviews of individual audits the AIU reports its findings in writing, and requires written responses to the more significant of these. Firms are expected, however, to take action to deal with all such findings, and this is tested by the AIU on a number of follow-up reviews in subsequent years. Such findings, together with findings in respect of a firm's quality control policies and procedures, are summarised in the AIU's private report on each firm to the Audit Registration Committee of the relevant professional body (acting in its statutory capacity as the Recognised Supervisory Body). This report is accompanied by the firm's action plan to deal with matters raised. Implementation of each firm's action plan is tested subsequently by the AIU.

Inspections and audit quality

The actions taken by firms in response to the AIU's inspection findings continue to contribute to an improvement in the overall quality of audit work in the UK. This view is supported by the results of follow-up reviews of individual audits undertaken by the AIU, where it usually finds that all or most matters identified previously have been satisfactorily addressed. While improvement in the overall quality of audits is more difficult to assess, the AIU notes that the proportion of audits assessed as good with limited improvements required has been approximately 50% of all audits reviewed in the last two years. The number of major listed company audits assessed as requiring significant improvement has declined this year, with only one FTSE 350 audit in this category compared with four in each of the previous two years. However, overall the proportion of audits assessed as requiring significant improvement, particularly at smaller firms, remains of concern.

Where the AIU has identified that improvements are required in firms' policies and procedures supporting audit quality, the AIU has generally been satisfied with the progress made by firms in addressing these matters.

These results suggest that audit firms take the AIU's findings very seriously. Specific evidence of this may be seen in the fact that in some cases the reviews of individual audits have contributed to decisions regarding the composition of audit engagement teams and the remuneration of the audit engagement partners. The picture here however, is not consistent (see Section 3.3.21), but it is clear that quality assessments can be incorporated successfully within performance and appraisal systems for partners and staff.

Notwithstanding this, the AIU believes that having a wider range of specific actions, such as sanctions, available to the FRC would assist in promoting audit quality and in ensuring appropriate action is taken to reduce the number of audits requiring significant improvement.

Improving professional standards

An important aspect of the AIU's inspections is its ability to gain an understanding of how firms are interpreting and applying the requirements of both the Auditing and Ethical Standards, and to suggest changes to the standard-setters where it believes these would enhance overall audit quality. In this respect the AIU has worked closely with the Auditing Practices Board ("APB"), including in a number of joint responses to consultations by the International Auditing and Assurance Standards Board ("IAASB"). The AIU has also contributed to the recent revisions to the Ethical Standards and to the APB's August 2010 discussion paper, "Auditor Scepticism: Raising the Bar". This is discussed in more detail in Section 2.8.

Assisting audit committees

The AIU issues a short report on the significant matters arising on each audit reviewed. Although this is a confidential report addressed to the audit firm, it is expected that the firm will make a copy available to the directors of the audited entity. The aim is to assist the audit committee to assess the effectiveness of the audit. A number of audit committee chairs have recently been asked for their views on the effectiveness of the AIU's work, including the usefulness of these reports. Responses received are generally positive, while also suggesting some areas for improvement, including placing even more emphasis on the reporting of matters relating to key audit judgments. The AIU will consider how it can further improve its reporting for the benefit of audit committees.

It was clear from comments received that audit committee chairs sometimes had difficulty in assessing the significance of some of the matters raised. This difficulty could be caused by firms characterising some of the AIU's findings as relating to the sufficiency of documentation rather than the underlying audit evidence and judgments and therefore of less significance. The AIU assesses the evidence obtained to support key areas of audit judgment and disagrees with this characterisation of its findings. Furthermore, inadequate documentation may well indicate that unrecorded work has not in fact been undertaken, or that the work has not been undertaken properly. Documentation has an important part to play not only in the quality and comprehensiveness of audit work but also as an effective mechanism for collecting one's thoughts and ultimately improving audit judgment.

Introduction

key issues

and

concerns

Review of scope and approach

The AIU reviews the scope and focus of its inspections annually to ensure that these continue to reflect the economic climate and other relevant matters. As a result, for example, the list of public interest entities whose audits make up the population from which the AIU draws its sample for review was amended in 2010/11 to include all UK incorporated banks; previously banks within scope were predominantly listed UK incorporated banks and only certain UK subsidiaries of overseas banks. This change resulted in ten bank audits being reviewed in 2010/11 compared with five in 2009/10.

The AIU has a policy to regularly review its inspection approach and regards contacts and co-operation with overseas regulators as opportunities to compare inspection approaches and exchange good practice.

Summary of activities

2.1 Introduction

This section provides a summary of the AIU's inspection and other activities undertaken in 2010/11.

2.2 Scope and coverage of inspections

In 2010/11, the AIU completed full scope inspections, comprising a review of policies and procedures supporting audit quality and individual audits within its scope, at the "Big Four" firms⁵, BDO LLP and Grant Thornton UK LLP. Reports summarising the findings from the inspections at each of these firms will be published in July 2011.

Inspections were also carried out at 12 smaller firms, comprising reviews of one listed or other major public interest entity audit. A report summarising the findings of these inspections will be published later this year.

The AIU currently inspects the Big Four firms on an annual basis. These firms audit approximately 80% of the entities within the AIU's scope, including over 95% of UK incorporated FTSE 350 companies. The AIU's inspections at the other major firms are undertaken over an extended period of approximately two years. Reports on the findings of inspections at Baker Tilly UK Audit LLP, Crowe Clark Whitehill LLP, Mazars LLP and PKF (UK) LLP will therefore be published in 2012.

The AIU undertook a further inspection of the Audit Commission on a contractual basis in 2010/11, covering certain policies and procedures supporting audit quality and selected individual audits. The audits reviewed included some undertaken by its Audit Practice and some conducted by firms appointed by the Audit Commission ("Appointed Firms"). Audits undertaken by two Appointed Firms were reviewed in 2010/11.

The AIU also undertook an inspection of the National Audit Office on a contractual basis and for the purpose of the Oversight Board's statutory role as Independent Supervisor⁶. This inspection covered progress in addressing findings identified from the previous inspection in respect of policies and procedures supporting audit quality and a review of selected individual audits. Public sector inspections are discussed in more detail in Section 2.4.

⁵ The Big Four firms comprise Deloitte LLP, Ernst & Young LLP, KPMG LLP & KPMG Audit PLC, and PricewaterhouseCoopers LLP.

⁶ The AIU's inspections at the National Audit Office include the monitoring of the performance of its statutory audit work on behalf of the Professional Oversight Board as required by section 1229 Companies Act 2006. The statutory audits reviewed are outside the AIU's normal scope of inspection.

Summary of activities

Each year the AIU selects a number of areas of particular focus. For 2010/11, these were the fair value measurement of assets and liabilities, the impairment of assets (including goodwill and other intangible assets), revenue recognition and fraud risks, segmental reporting, the evaluation of going concern and compliance with the Ethical Standards.

Emphasis was also given to the audit of banks, given the inclusion for the first time of all UK incorporated banks as a separate category within the AIU's scope of inspections. This resulted in all UK subsidiaries of overseas banks being brought within the AIU's scope of inspection, as the Oversight Board took the view that this was appropriate, given the level of public interest in the banking sector following the financial crisis. Previously, banks within scope were predominantly listed UK incorporated banks and only certain UK subsidiaries of overseas banks.

Areas of focus for the AIU's 2011/12 reviews of individual audits are fair value accounting estimates and disclosures, the impairment of assets, revenue recognition and going concern, and related parties. The AIU will give particular consideration to whether appropriate professional scepticism has been applied in these areas. It will also place emphasis on the quality of reporting to audit committees and assess how the revised Auditing Standards that became effective for December 2010 financial year-ends ("Clarified ISAs") are being applied by firms and individual audit teams in practice. The AIU's focus on banks will continue, together with an increased focus on UK building societies.

The scope of audits subject to AIU inspection has widened following arrangements agreed with the regulatory authorities in Jersey, Guernsey and the Isle of Man ("Crown Dependencies"), which bring companies registered there with securities that are traded on a regulated market in the EEA within the scope of AIU inspection. This is discussed in more detail in Section 2.5. While these new arrangements together with the AIU's scope of inspections as determined by the Oversight Board result in all UK and Crown Dependency companies listed on the London market being subject to AIU inspections, there are still other entities listed in London but incorporated elsewhere, that fall outside the scope of AIU inspections.

2.3 Analysis of audits reviewed by the AIU

In the year to 31 March 2011, including reviews performed under contractual arrangements with the Audit Commission and the National Audit Office, the AIU completed the review of 107 audits, compared with 109 in 2009/10. The audits reviewed in 2010/11 related to financial years ending between December 2008 and July 2010, with the majority being 31 December 2009 year ends.

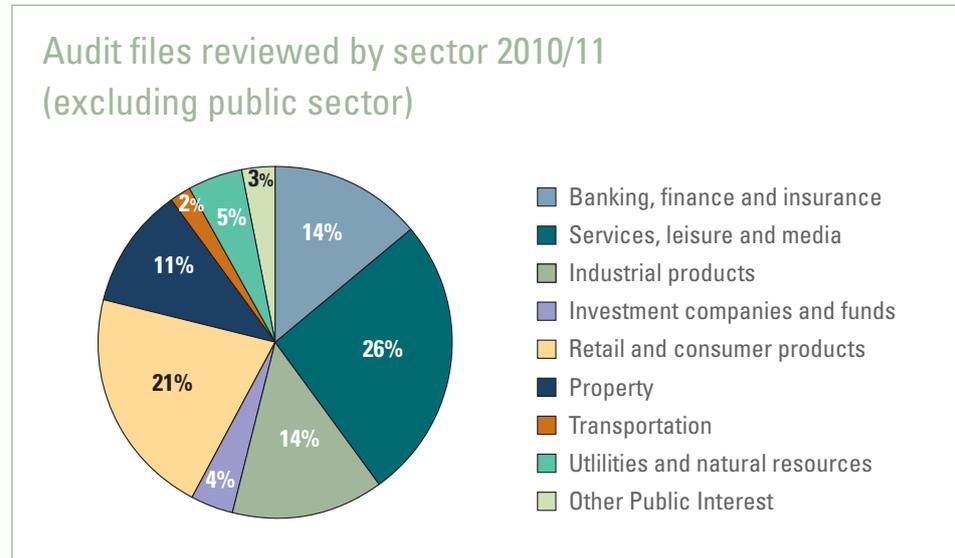
An analysis of audits reviewed by type of firm is set out in the following table.

Firm type		File reviews 2010/11	File reviews 2009/10
Major firms	Big Four firms	61	68
	Other major firms	19	12
Smaller firms		12	13
Total excluding public sector		92	93
Public sector	Audit Commission	4	4
	Audit Commission – appointed firms	5	7
	National Audit Office	6	5
Overall total		107	109

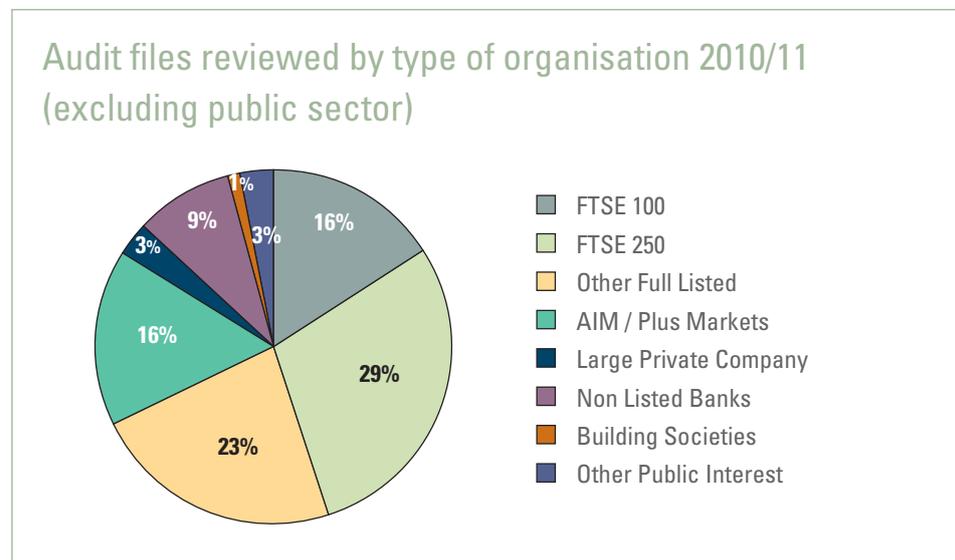
The above totals include 11 follow-up reviews (2009/10: 12 follow-up reviews).

Summary of activities

An analysis by sector of the audits reviewed by the AIU in 2010/11 is set out below:



An analysis by type of organisation of the audits reviewed by the AIU in 2010/11 is set out below:



In the seven years since the AIU commenced its inspection activities in 2004, it has reviewed in excess of 600 audits, including the audits of over 250 FTSE 350 companies⁷.

⁷ References to FTSE 350 companies relates to their status at the time the audits were reviewed by the AIU.

The AIU has developed a risk model covering listed companies, including AIM, which it uses to inform its selection of audits to be reviewed each year. The majority of audits selected for review by the AIU were drawn from those identified as higher risk within its risk model.

2.4 Public sector inspections

Audits of public sector entities fall outside the normal scope of the AIU's inspections. The AIU's public sector inspections, comprising the Audit Commission and its "Appointed Firms" and the National Audit Office, are therefore undertaken on a contractual basis. The findings from these inspections are not subject to public reporting.

The cost of these inspections is met directly by the bodies concerned. They are undertaken in the first quarter of each calendar year, the period in which the AIU undertakes less inspection fieldwork at the major firms. Public sector inspections therefore contribute to the overall efficiency and cost-effectiveness of the AIU's inspection activities.

The future regulatory structure for audits undertaken by the Audit Commission and its Appointed Firms is currently the subject of consultation by the Department for Communities and Local Government, following the Government's decision to abolish the Audit Commission.

2.5 Crown dependency inspections

Firms undertaking the audits of companies incorporated in the Crown Dependencies, with securities that are traded on a regulated market in the EEA, are now required to be subject to independent inspection. This requirement is derived from the EU's Statutory Audit Directive and the arrangements that have been put in place are designed to ensure that the Crown Dependencies have auditor oversight arrangements that are considered equivalent to those in place in EEA member countries.

The AIU, in conjunction with the monitoring units of the professional bodies in the UK which register firms to conduct audit work, has entered into arrangements with the Crown Dependency regulatory authorities to undertake these inspections on their behalf. The AIU will be responsible for inspecting all major UK audit firms undertaking the audits of relevant Crown Dependency entities, together with Crown Dependency audit firms with more than ten relevant audits. The AIU commenced these inspections with effect from 1 April 2011. The cost of these inspections will be met by the individual audit firms concerned.

Summary of activities

The AIU has worked closely with the Crown Dependency regulatory authorities over the last year in developing these arrangements. One benefit is that the audits of companies incorporated in one of the Crown Dependencies which are listed in the UK are now subject to AIU inspection. The audits of a number of major FTSE 350 companies, including six FTSE 100 companies, will be covered by these arrangements.

2.6 Oversight of inspections by the professional bodies

On behalf of the Oversight Board, the AIU undertakes certain oversight activities in relation to inspections undertaken at smaller firms by the monitoring units of the professional bodies. It approves the inspection methodology used to assess a firm's policies and procedures supporting audit quality and the assignment of inspectors to undertake this work. The AIU also provides input to the monitoring units' inspection reports on each smaller firm.

2.7 International liaison

Independent audit regulation continues to develop and expand internationally. As part of the FRC's on-going commitment to liaise with other independent audit regulators, the AIU meets on a regular basis with similar organisations. It also participates in the International Forum of Independent Audit Regulators ("IFIAR") plenary meetings, working groups and inspection workshops and plays a leading role in the newly formed European Audit Inspection Group, comprising independent audit regulators from within the EU. The AIU notes that there is considerable commonality between its inspection findings and those of audit regulators in other major jurisdictions.

Changes to the way firms are structured, in particular the emergence of Europe-wide firms such as KPMG Europe LLP and Ernst & Young Europe LLP, have required the AIU to work closely with other regulators. To respond to these developments, the AIU has led the establishment of a college of regulators, to facilitate the sharing of information and efficient inspection processes across these European firms.

An important development during the year was the Statement of Protocol entered into between the Oversight Board and the Public Company Accounting Oversight Board ("PCAOB"). This information sharing agreement, which builds on the positive working relationship between the two organisations, is a statutory requirement necessary to facilitate more effective cooperation and joint inspections, including exchanges of information and interviews of firm personnel. The agreement is designed to improve access to relevant information, for example relating to US audit firms registered in the UK and UK firms registered in the US. This will both strengthen and streamline the process of audit inspections, increasing the efficiency and effectiveness of the oversight regime.

Following on from this agreement, the AIU and the PCAOB have commenced joint inspections at PricewaterhouseCoopers LLP and Ernst & Young LLP as part of the AIU's 2011/12 inspection cycle.

2.8 Input to standard-setting process

An important aspect of the AIU's work is its ability to gain an overall understanding of how firms are interpreting and applying the requirements of both the Auditing and Ethical Standards, and to recommend changes to the standard-setters which it believes would enhance overall audit quality or safeguard auditor independence.

In this respect the AIU has worked closely with the APB and provided it with regular feedback on issues arising from its inspections in relation to the interpretation and application of Standards. Recent amendments to the Ethical Standards, including those clarifying the definition of contingent fees and that the provision of certain tax services to listed entities is prohibited, were influenced by the AIU's findings.

The AIU contributed to the August 2010 APB discussion paper, "Auditor Scepticism: Raising the Bar", which helped to focus attention on this key issue both in the UK and internationally. It has also developed joint responses with the APB to a number of important IAASB consultations, including using the work of internal audit, the audit of complex financial instruments and the audit of disclosures. The AIU also met representatives of the IAASB, including its Chairman, during the year to set out its views and experience on using the work of internal audit.

The AIU will continue to work closely with the APB and other standard-setters with a view to ensuring that the findings of its inspections are taken into account in the standard-setting process.

2.9 Collaboration with the Financial Services Authority

There is a strong mutuality of interest between the FRC and the Financial Services Authority ("FSA") in many aspects of corporate reporting and governance, including the role of audit. This resulted in a Memorandum of Understanding ("MoU") being entered into in January 2011 relating to the co-operation and information sharing between the FSA and the AIU. The purpose of the MoU was to assist each body in the proper performance of their respective functions. The MoU states that the FSA and the AIU will meet regularly and at least four times a year.

Summary of activities

A number of meetings between relevant FSA and AIU staff have now been held which have focused primarily on bank audits. The AIU has provided the FSA with details of its findings from those 2010/11 reviews of interest to the FSA. The AIU will also provide the FSA with details of its findings from each review conducted in 2011/12 of interest to the FSA.

The AIU welcomes the opportunity to work more closely with the FSA to improve the overall quality of audits of financial institutions. How these arrangements are working in practice will be commented on in the future.

2.10 Basis of AIU funding

The AIU operates as a discrete unit within the Professional Oversight Board of the FRC. It has a staff of approximately 20 full-time equivalents. The direct costs of the AIU's inspection activities falling within its normal scope are funded by the relevant professional accountancy bodies. Inspection activities outside the AIU's normal scope, such as those relating to public sector bodies and the auditors of Crown Dependency entities, are subject to separate funding arrangements designed to recover in full the costs of these inspections.

Overview of AIU findings

3.1 Introduction

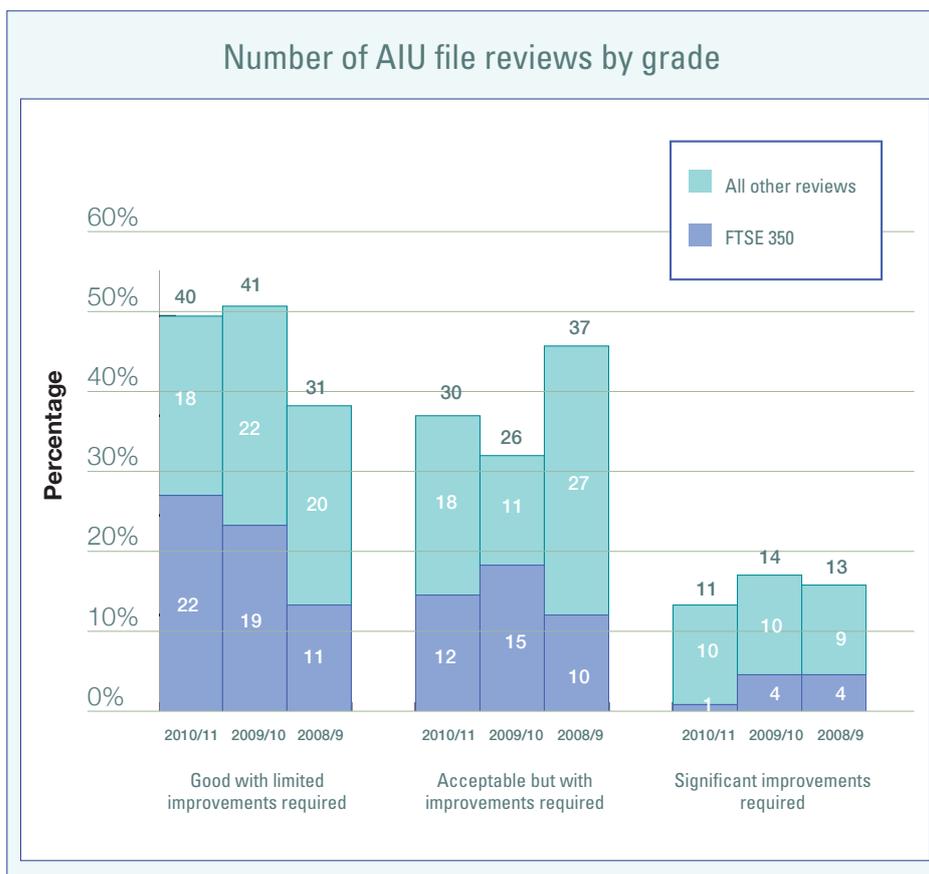
This section provides an overview of the principal findings arising from the AIU's inspections in 2010/11 at major and smaller firms, including an overall assessment of the individual audits reviewed.

3.2 Assessment of audits reviewed

3.2.1 Overall findings

The AIU reviewed selected aspects of 92 audits in 2010/11 (2009/10: 93 and 2008/9: 92) at major and smaller firms, including 11 follow-up reviews (2009/10: 12 and 2008/9: 11).

The AIU assesses the quality of each audit it reviews and arrives at an overall grade. The AIU's file review gradings at major and smaller firms excluding follow-up reviews (81 audits in each of 2010/11, 2009/10 and 2008/9) are summarised in the table below.



Overview of AIU findings

The above table indicates that approximately 50% of the audits reviewed by the AIU in 2010/11 were assessed as good with limited improvements required. This is consistent with the AIU's findings in 2009/10 and maintains the overall improvement recorded last year over 2008/9. This improvement is less evident at smaller firms where only approximately a third of the audits reviewed were assessed as good with limited improvements required. However, the number of audits requiring significant improvement, particularly outside the FTSE 350, while slightly lower than in prior years, remains of concern.

An audit is assessed as requiring significant improvement if the AIU had significant concerns in relation to the sufficiency or quality of audit evidence or the appropriateness of audit judgments in one or more key audit area or the implications of concerns relating to other areas are considered to be individually or collectively significant. This assessment does not necessarily imply that an inappropriate audit opinion was issued.

3.2.2 Audits requiring significant improvements

Of the 11 audits (13.5%) requiring significant improvements in 2010/11, six were listed or AIM companies. In 2009/10 all 14 audits (17%) requiring significant improvements were listed or AIM companies. The number of large listed company audits assessed as requiring significant improvements has declined (one FTSE 350 in 2010/11 compared with four in each of 2009/10 and 2008/9).

The audits of three unlisted subsidiaries of overseas banks (out of 10 bank and building society audits reviewed) were assessed as requiring significant improvements in 2010/11.

The number of audits undertaken by major firms assessed as requiring significant improvements in 2010/11 was seven (10%), compared with eight audits (11%) in both 2009/10 and 2008/9.

The proportion of audits undertaken by smaller firms assessed as requiring significant improvements, while lower than in the prior year, continues to be higher than at major firms (four out of nine audits (44%), compared with 55% in 2009/10 and 45% in 2008/9). Issues relating to group audits, including insufficient participation in the audit of multinational groups, continue to be the main factor contributing to these findings. In one case, the AIU considered the quality of audit work undertaken on a group audit to be seriously deficient and has recommended that the Audit Registration Committee refer the firm's audit for possible disciplinary action.

3.2.3 Follow-up reviews

In relation to the 11 follow-up reviews undertaken in 2010/11 (2009/10: 12 follow-up reviews), the AIU considered that all or most matters identified previously had been satisfactorily addressed in the subsequent audits. In respect of these individual audits, it is therefore clear that improvements in audit quality have been achieved in the relevant areas.

3.3 Principal findings

3.3.1 Introduction

The principal findings from the AIU inspections in 2010/11 are discussed below. Findings arising from reviews of individual audits relate to the AIU's inspections at both major and smaller firms, while findings related to policies and procedures supporting audit quality relate to the AIU's inspections at major firms only.

A number of the matters noted below reflect the importance the AIU attaches to firms observing the principles underlying Auditing and Ethical Standards as well as the specific requirements thereof. The AIU continues to have concerns that firms focus primarily on the specific requirements of the Standards and do not give sufficient attention to the underlying principles.

It is clear from the AIU's review of appraisals and partner admission procedures that senior audit staff at some firms continue to believe that success in the selling of non-audit services to audited entities is a significant contributory factor to promotion and remuneration decisions. Further action is needed to change this perception.

Another general concern is the potential implications of an increased emphasis within a number of major firms on achieving greater efficiencies in the conduct of audit work. Firms need to ensure that initiatives of this nature do not have an adverse effect on audit quality. Similarly, the culture within firms must strike an appropriate balance between strategies to grow the business and the need to maintain and improve audit quality.

The AIU also notes the growth in off-shoring, whereby certain audit tasks and processes are undertaken on behalf of the audit team in off-shore locations. While the proportion of audit work undertaken through off-shoring currently remains very small, it is anticipated that it will continue to increase in the future. The AIU will therefore monitor its effect on audit quality.

Other examples of efficiency measures implemented by firms include changes to their guidance on materiality, which may have the effect of reducing the levels of testing performed, and specific programmes designed to reduce audit hours and costs.

3.3.2 Professional scepticism

The AIU continued to identify cases where it believed insufficient professional scepticism had been exercised in key areas of judgment. In response to these concerns, firms have undertaken or are in the process of undertaking a number of initiatives to reinforce the importance of exercising professional scepticism in the conduct of their audit work. These include additional training and specific communications to staff from key management personnel. The extent to which these initiatives have been successful in changing behaviours will not be clear to the AIU for some time but it does expect to see some evidence of improvement in its 2011/12 inspections. Some firms have more work to do than others to demonstrate that professional

Overview of AIU findings

scepticism is appropriately embedded in their processes and culture. The AIU will again give particular consideration to the application of professional scepticism in its 2011/12 inspections.

3.3.3 Revised auditing standards

Revised Auditing Standards known as “Clarified ISAs” became effective in the UK for December 2010 financial year ends. An assessment of the state of preparedness for the revised Standards was an important component of the AIU’s inspections at major firms in 2010/11. Firms have expended considerable resources to ensure that they are in a position to implement the revised Standards. In a number of cases, the changes made coincided with major upgrades or replacement of firms’ audit systems. None of the audits reviewed by the AIU in 2010/11 had been performed under the revised Standards. The AIU will review the application of the revised Standards as part of its 2011/12 inspections.

3.3.4 Banks and building societies (“Banks”)

The AIU’s scope of inspections for 2010/11 was amended to include all banks incorporated in the UK and an increased focus was given to banking audits. In total 10 audits of banks were reviewed, including seven that fell within the AIU’s scope for the first time. Most of the audits reviewed were the UK trading subsidiaries of major international banks. It should be noted that overseas banks often operate in the UK through branches rather than separate legal entities and are therefore outside the scope of the AIU’s inspections.

The observations and findings set out below are the more significant areas of concern arising from the AIU’s review of bank audits in 2010/11. It should be emphasised that these findings have been influenced significantly by auditors’ performance of banking subsidiary audits rather than of major listed UK banking groups.

Of particular concern was the audit of loan loss provisions where improvements were required in the majority of the audits reviewed. Insufficient evidence of the challenge and testing by audit teams of the techniques adopted by management to assess the level of collective provisions was a common issue. The adequacy of audit evidence supporting the audit team’s assessment and challenge of specific loan impairments was also a recurring issue.

Issues were also identified in respect of the quality of evidence obtained to support judgments in relation to both the measurement of financial assets and the adequacy of related disclosures. These included the sufficiency of evidence supporting the valuation of certain distressed asset-backed securities and private equity fund investments, and the appropriateness of audit testing of customer deposits and loans.

The audit approach adopted for the UK subsidiaries of major international banks had often been developed from a group audit perspective. As a result, the level of materiality set by the audit teams for the UK subsidiary was of concern in a number of cases. Furthermore, the adequacy of audit procedures performed for the entity under review was sometimes difficult to assess due to the complexity of the audit approach and the interaction between controls and other testing conducted at a group level designed to cover the international banking group as a whole. Firms should ensure that the audit approach adopted for a UK subsidiary results in sufficient appropriate audit evidence being obtained to support the firm's audit opinion on that entity.

As would be expected for entities which process high volumes of transactions, the audit approach for the banks reviewed involved testing the effectiveness of certain key controls. Concerns were identified in relation to the quality of controls effectiveness testing, including the extent to which reliance was placed on management's own testing of controls. In some cases, the audit response where controls were found not to be operating effectively appeared insufficient. Auditors of banks should consider how to improve their testing and assessment of control effectiveness to ensure that sufficient audit evidence is obtained to support the level of reliance placed by them on key controls.

All firms provide bespoke training in relation to the audit of banks. However, the depth of specific guidance available to audit teams on the application of Auditing Standards and the firm's methodology and guidance to audits of banks varies significantly. Furthermore, not all firms provide audit programmes tailored specifically to financial institution audits and existing software at some firms has not been recently updated. Firms should consider whether their methodology, guidance and standard audit programmes in relation to the audit of banks need to be enhanced and/or updated.

3.3.5 Group audit arrangements

Auditing Standards regarding group audits have recently been strengthened to include greater specification of the audit procedures to be performed and require greater involvement by the group auditor in the audit of significant components.

The AIU identified issues in relation to group audits at both major and smaller firms, including cases where the group auditor had insufficient involvement in the audit of significant components. The revised Auditing Standards clarify what is expected of firms when undertaking group audits. In light of this, firms need to consider carefully whether to accept or continue with certain group audit engagements, for which they might not have the required resources, expertise or involvement in the underlying audit work.

Overview of AIU findings

The AIU also noted that the division of work between the group auditor and the component auditor was not always clear. Group audit instructions were not always issued and the group auditor did not always ensure that the component auditor had performed sufficient work on key audit areas.

3.3.6 Impairment of goodwill and other intangibles

The AIU continued to review a number of audits where goodwill and other intangible assets were material, in order to assess the quality of audit evidence obtained to support the carrying value of these assets. Consistent with previous years a significant number of issues were identified including insufficient evidence of challenge of the key assumptions and concerns regarding the adequacy of the related disclosures.

The impairment of goodwill and intangibles remains an area of focus for the AIU's 2011/12 inspections. The AIU expect that its inspections in 2011/12 will provide evidence of the extent to which initiatives undertaken by firms to reinforce the importance of exercising professional scepticism in this area have been effective.

3.3.7 Going concern

While the AIU continued to identify issues in relation to the audit of going concern, fewer issues arose overall this year, although this pattern was not uniformly spread across all firms. The extensive guidance issued both by firms and the APB has, in the AIU's view, resulted in improvements in audit quality in this area. Issues identified included the extent of work performed on financial projections supporting the going concern assessment, the adequacy of the disclosures relating to going concern uncertainties and insufficient evidence of parental support which was material to the going concern conclusion.

3.3.8 Use of experts

Appropriate use by firms of internal or external experts in more complex audit areas contributes to audit quality. The AIU identified very significant variations amongst the largest firms in the extent to which internal experts were used by audit teams. One firm which has used internal experts extensively in the past issued new guidance on this area which, in our view, is likely to have given rise to some confusion on the part of audit teams regarding their use.

In some audits, the audit team had not given proper consideration to the need to use the work of an expert in order to obtain sufficient appropriate audit evidence in areas such as asset valuations and assessing whether goodwill or other intangible assets had become impaired. Where internal experts were used, the AIU continued to identify cases where the expert's views and advice were not properly considered and followed-up, particularly where they indicated a need for valuations determined by management to be challenged, and cases where there was insufficient evidence of the work performed and the extent of verification undertaken by the experts.

3.3.9 Revenue recognition

Revenue recognition was an area of focus in 2010/11 in response to the economic climate and the resultant pressure on businesses, which increases the risk of manipulation of revenues. A range of issues were identified including insufficient testing of underlying data used to calculate the revenue recognised on long term contracts; not following up discrepancies between revenue recognised in the accounting system and underlying contracts; insufficient challenge of management's explanations in relation to key judgments used to determine revenue recognition; and insufficient consideration of differences in accounting treatment for differing revenue streams. The number and nature of these issues indicates that the audit of revenue recognition is an area where further improvement is required. Revenue recognition remains an area of focus for the AIU's inspections in 2011/12.

3.3.10 Segmental reporting

Segmental reporting was an area of focus in light of the changes in financial reporting requirements following the introduction of IFRS 8: Operating Segments. In some cases, there was no evidence that appropriate consideration had been given by audit teams to the requirements of this Standard. Most issues identified in this area related to inconsistencies between the information in the front half of an annual report and the segmental disclosures in the financial statements. Firms need to obtain appropriate evidence to support judgments related to the number of reportable segments, particularly where only one segment has been identified and disclosed and management's assessment of performance in the front half of the annual report clearly distinguishes between different activities.

3.3.11 Substantive analytical review

Substantive analytical review is a key procedure on many audits and often the main form of audit evidence for items in the income statement. While substantive analytical review can provide valuable audit evidence, it is frequently not performed well. Issues were identified in many audits reviewed by the AIU across firms of all sizes. Often audit teams confuse overall analytical review procedures, which are generally limited to a comparison of current year figures with the prior year, with substantive analytical review procedures which require far more precision, including the setting of expectations and the establishment of thresholds for investigating differences. Even where firms have prescriptive methodologies for the performance of substantive analytical review, audit teams often fail to justify the rationale for the expectations set and frequently fail to investigate properly discrepancies above thresholds or to corroborate explanations provided by management. This may have implications for the overall adequacy of the audit evidence obtained in particular areas and firms must take further action to address this issue.

Overview of AIU findings

3.3.12 Controls effectiveness testing

The audit approach for the largest listed entities, large retailers and financial institutions, where sufficient audit evidence often cannot be obtained on a timely basis from substantive testing alone, generally includes testing the effectiveness of controls. In respect of other types of audits, auditors often rely primarily on substantive audit procedures, with only limited testing of the effectiveness of internal controls. Issues relating to controls effectiveness testing at banks, in particular over-reliance on the testing of controls by management, are discussed in Section 3.3.4 above. Other issues identified included a lack of justification regarding sample selection and sizes. This is an area the AIU will be reviewing in more detail in 2011/12.

3.3.13 Letters of representation

Auditing Standards state that written representations from management or those charged with governance do not provide sufficient audit evidence on their own in respect of any of the matters with which they deal. The AIU has come across cases where management representations were the main source of audit evidence obtained to support conclusions that no impairment of assets such as goodwill and other intangibles was required. Over-reliance on management representations is a further example of insufficient professional scepticism being applied in the conduct of audit work.

3.3.14 Audit of disclosures

In a number of cases improvements were required in the audit of disclosures relating to key judgments and assumptions, particularly in respect of the valuation of assets and going concern. In respect of a significant provision relating to miss-selling, there was insufficient evidence of the consideration of the adequacy of the related disclosures.

The audit of disclosures is sometimes primarily focused on the completion of various checklists. Such an approach fails to recognise the increased importance of disclosures in financial reporting. Firms should give greater emphasis to assessing the quality and sufficiency of the disclosures in key areas of judgment, to ensure they enable the users of the financial statements to understand the assumptions used and the extent of estimation uncertainty.

3.3.15 Accounting records maintained by service organisations

Auditors must ensure that they obtain sufficient audit evidence where all or part of the entity's accounting records are maintained by a service organisation. Issues arose in the audits of pension schemes and charities where investment managers or custodians, from whose reports the financial statements were compiled, hold the investments and maintain the associated accounting records.

Of particular concern was the practice of obtaining direct confirmation from either the investment manager or custodian as the sole evidence of the year end investment valuations in the financial statements. Where the financial statements are compiled directly from the reports provided by the investment manager or custodian, direct confirmations of this type do not provide adequate independent evidence as they are simply copies of the accounting records. Additional evidence is therefore required and must be obtained from alternative sources.

3.3.16 Non-audit services

Policies and procedures designed to ensure that firms comply with the requirements and underlying principles of the Ethical Standards, together with their application on individual audits, continue to be an important focus for the AIU's inspections.

In most respects major firms have appropriate policies and procedures in place. However, these policies and procedures or their application in practice continue to focus on compliance with the specific requirements of the Standards and do not necessarily give sufficient consideration to the principles underlying them.

A range of ethical issues continued to be identified, the more significant of which related to the provision of non-audit services. Incomplete identification of the nature and extent of the threats to independence and objectivity, inadequate consideration and application of appropriate safeguards to mitigate these threats, and inadequate communication with audit committees continue to be common issues. The proper identification of threats and safeguards is crucial to the effectiveness of Ethical Standards in maintaining independence. The AIU would have expected firms to be more conscious of the importance of applying appropriate safeguards at a time when the need for more specific prohibitions is being debated.

Examples of areas in which issues were identified relating to the consideration or nature of non-audit services provided to audit clients included the provision of IT consulting services to a FTSE 100 audit client, and the provision of prohibited legal services to an audit client.

Ethical Standards require contingent fee arrangements to be disclosed in writing to the audit committee of a listed audit client. The AIU notes that on occasion fees which were contingent in nature have not been classified as such and were therefore deemed to fall outside the requirements of the Ethical Standards extant at the time. This illustrates how firms do not always consider appropriately the principles underlying the Ethical Standards. The AIU raised this matter with the APB and recent amendments to the Ethical Standards have tightened the definition of a contingent fee.

Overview of AIU findings

The AIU also raised with the APB the fact that some firms were interpreting the Ethical Standards as permitting the provision of certain tax services to listed entities when, in its view, they were not permitted. The APB has subsequently amended the relevant ethical requirement and guidance to preclude such an interpretation and remove any doubt that the tax services concerned are prohibited for listed audited entities.

3.3.17 Extended audit services

Extended audit services provided to audit clients were the subject of much publicity last year. The AIU continued to monitor developments in this area as part of its 2010/11 inspections, including the application and effectiveness of safeguards in practice.

The AIU reviewed certain audits of entities where such services had been provided. It did not identify any relevant requirements of the Ethical Standards applicable at the time that had not been met or any adverse impact on audit quality.

3.3.18 Communicating with audit committees

While the standard of reporting to audit committees at larger firms is often good or of an acceptable standard, improvements are required regarding how firms communicate their views on key areas of judgment. In the AIU's view, there should be a clear statement as to whether the auditor concurs with management's judgments in key areas or whether further discussion with the audit committee is required. In some cases firms have restricted their comments to a description of the matter and management's views thereon. On one FTSE 100 audit reviewed by the AIU, the audit committee reporting cross-referred to management papers, and as a consequence there was no statement of the firm's views on key areas of judgment.

Given the importance of effective communication between auditors and audit committees, in particular in respect of key audit judgments, the Oversight Board is undertaking a separate exercise to review the quality of auditors' reporting to audit committees of FTSE 100 companies.

3.3.19 Engagement quality control review

Auditing Standards require that all listed company audits have an Engagement Quality Control Review (EQCR) and that firms have policies and procedures in place specifying which other audits require an EQCR. A number of firms use the AIU's scope of inspections as set out in Appendix B as the basis for their EQCR policy.

The AIU is concerned that there is a lack of evidence that the EQCR is providing an effective and appropriate level of challenge to key audit judgments. The EQCR often appears to be viewed primarily as a compliance function, with insufficient time devoted to the review, and policies in place at many firms which dictate that little or no evidence of review is retained on the audit files.

The AIU notes that at many firms there is a centrally controlled list of approved individuals who are permitted to undertake the reviews, although the extent of training provided is often limited and the specific requirements for an individual to gain approval varies across firms. At one firm, a small group of senior audit partners have now been assigned responsibility for the EQCR review of all the firm's FTSE 350 clients. At another firm "EQCR assistants" are used for certain aspects of the review process to enable the experienced quality control reviewer to focus on key matters of judgment, although there remains insufficient evidence of the level of challenge provided.

The AIU will continue to review the operation and effectiveness of the EQCR process during its 2011/12 inspections.

3.3.20 Quality control and audit finalisation

There was little or no evidence of review by the audit engagement partner or the engagement quality reviewer in key areas of audit judgment in a number of audits reviewed. Weaknesses were also identified in audit finalisation procedures, including undetected clerical drafting errors in financial statements.

There were also instances of work papers in significant areas of the audit that were either completed or evidenced as reviewed after the date of the audit report. This was a particular concern in respect of some of the bank audits reviewed. It is possible that targets for reporting to shareholders may be placing undue pressure on audit teams to complete audit procedures to a tight reporting timetable, leaving the audit team to evidence their work at a later date. While Auditing Standards permit the administrative process of assembling the final audit file after the date of the audit report, this should not include the retrospective evidencing of key areas of audit judgment. Firms should reinforce their policy regarding the timely review of work papers, particularly in areas of complexity or significant audit judgment.

3.3.21 Performance evaluation

While the AIU has identified examples of good practice, it remains concerned that performance evaluation processes do not always give sufficient consideration to audit quality. Examples of this included audit personnel being awarded top performance gradings or being promoted, notwithstanding audit quality issues having been identified in internal quality reviews.

The AIU also continues to see evidence in appraisal and promotion documentation that senior staff believe, contrary to the requirements of the Ethical Standards, that success in selling non-audit services to audited entities is a factor influencing remuneration and promotion decisions. The AIU is particularly concerned at the lack of evidence of any challenge by their superiors to the inclusion of references to success in selling non-audit services to audited entities in appraisal and promotion documentation for senior staff.

Appendix A – Inspection process and basis of reporting

Inspection process

The overall objective of the AIU's work is to monitor and promote improvements in the quality of auditing. As part of its work, the AIU monitors firms' compliance with the regulatory framework for auditing, including the Auditing Standards, Ethical Standards and Quality Control Standards for auditors issued by the FRC's Auditing Practices Board 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 the AIU's inspections or, in relation to the reviews of individual audits, those effective at the time the relevant audit was undertaken.

The AIU's inspections of the major firms comprise a review of the firms' policies and procedures supporting audit quality and a review of the quality of selected audits of listed and other major public interest entities that fall within the scope of independent inspection, as determined each year by the Oversight Board. The scope of AIU inspections for 2010/11 is set out in Appendix B.

The AIU's inspections of smaller firms are limited to a review of the quality of selected audits of listed and other major public interest entities that fall within the AIU's scope.

The monitoring units of the professional accountancy bodies in the UK which register firms to conduct audit work are responsible for monitoring the quality of audit engagements falling outside the scope of independent inspection by the AIU but within the scope of audit regulation in the UK. Their work, which is overseen by the Oversight Board, 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. They also review smaller firms' policies and procedures supporting audit quality.

The AIU's review of the policies and procedures supporting audit quality of major firms covers the following areas:

- Tone at the top and internal communications
- Transparency reports
- 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

The AIU's reviews of individual audit engagements and policies and procedures supporting audit quality of major firms cover, but are not restricted to, compliance with the requirements of relevant standards and other aspects of the regulatory framework. Reviews of individual audit engagements 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.

The AIU seeks to identify areas where improvements are, in its view, needed in order to safeguard audit quality and/or comply with regulatory requirements and to agree action plans with the firms designed to achieve these improvements. Accordingly, the AIU's reports place greater emphasis on weaknesses identified requiring action by the firms than areas of strength and are not intended to be a balanced scorecard or rating tool. The AIU also assesses the extent to which each firm has addressed the findings arising from the previous AIU inspection.

The AIU's inspections are not designed to identify all weaknesses which may exist in the design and/or implementation of a firm's policies and procedures supporting audit quality or in relation to the performance of the individual audit engagements selected by it for review and cannot be relied upon for this purpose.

When reviewing individual audits, the AIU does not carry out a detailed technical review of the financial statements. Such reviews are the responsibility of the FRC's Financial Reporting Review Panel ("FRRP"). The AIU's focus in relation to financial reporting issues is on the appropriateness of audit judgments exercised and any underlying deficiencies in the firm's audit work and quality control procedures. Accounting and disclosure issues identified are therefore raised with firms in an audit context rather than a financial reporting context. However, the AIU challenges audit judgments on financial reporting issues, where appropriate, as an integral part of its work.

If the AIU considers there is sufficient doubt as to whether an accounting treatment adopted and/or disclosures provided comply with the applicable accounting framework, it may draw the matter to the attention of the FRRP. The FRRP considers such matters in accordance with its Operating Procedures.

Similarly, if during the course of its inspections the AIU identifies a significant concern as to the conduct of an individual or firm relevant to the public interest, it may draw the matter to the attention of the FRC's Accountancy and Actuarial Discipline Board ("AADB") or recommend that the matter be investigated by the relevant professional body. The AADB or the professional body concerned will then determine what, if any, action to take in relation to the matter.

In accordance with its confidentiality operating procedures, the AIU shares certain information obtained through its inspections with the FRRP and the AADB where relevant to their respective responsibilities. Information sharing arrangements with the FSA are discussed in Section 2.9.

Basis of reporting

The AIU provides the Audit Registration Committees of the relevant professional accountancy bodies in the UK with a private report on its inspections at each major firm⁸ registered by them to conduct audit work.

The private reports to the Audit Registration Committees contain the AIU's findings relating to safeguarding or improving audit quality, together with an overall recommendation on whether the firm's audit registration should be continued. These reports form the basis of the AIU's public reports on each major firm.

The AIU also issues private reports to the Audit Registration Committees on the significant findings arising from its review of individual audits undertaken by smaller firms together with an overall assessment of the quality of the audit. A separate report summarising these findings, but not identifying the individual firms reviewed, is published annually.

The AIU exercises judgment in determining those findings which it is appropriate to include in its 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 areas of particular focus in the AIU's overall inspection programme for the relevant year. In relation to reviews of individual audits, the AIU has generally reported its findings by reference to important matters arising on one or more audits. Where appropriate, the AIU has commented on themes arising or issues of a similar nature identified across a number of audited entities.

While the AIU's 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 by the AIU 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 the AIU's 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 comprehensive quality control procedures are applied before the AIU's private and public reports are finalised. As a result, there may be a significant period of elapsed time between completion of the AIU's inspection fieldwork at firms and the publication of reports on the inspection findings.

The AIU also issues confidential reports on individual audits reviewed by it. These reports are addressed to the relevant audit engagement partner or director but firms are expected to provide copies of the reports to the directors of the relevant audited entities.

⁸ Baker Tilly UK Audit LLP is currently registered with the Institute of Chartered Accountants of Scotland ("ICAS"). All other major firms are currently registered with the Institute of Chartered Accountants in England and Wales ("ICAEW").

Appendix B – Scope of inspections 2010/11

Audits of the following entities were within the scope of the AIU's inspections in 2010/11.

- All UK incorporated companies with listed equity and / or listed debt.
- AIM or Plus-quoted companies incorporated in the UK with a market capitalisation in excess of £50 million.
- Unquoted companies, groups of companies, limited liability partnerships or industrial and provident societies in the UK which have either:
 - Group turnover in excess of £500 million; or
 - Group long term debt in excess of £250 million and turnover in excess of £100 million.
- UK incorporated banks not already included in any other category.
- Private sector pension schemes with either more than £1,000 million of assets or more than 20,000 members.
- Charities with incoming resources exceeding £100 million.
- Friendly Societies with total net assets in excess of £1,000 million.
- Building Societies with assets exceeding £1,000 million.
- UK Open-Ended Investment Companies and UK Unit Trusts managed by a fund manager with more than £1,000 million of UK funds under management.
- Mutual Life Offices whose "With-Profits" fund exceeds £1,000 million.

UK incorporated companies do not include those incorporated in the Crown Dependencies of Jersey, Guernsey or the Isle of Man.

The above criteria were applied as at the start of the period in identifying entities within the AIU's scope for its 2010/11 inspections. Further details relating to the AIU's scope of inspections, including the criteria applied for the 2011/12 inspections, is available on the FRC's website: <http://www.frc.org.uk/pob/press/pub2548.html>

© **The Financial Reporting Council Limited 2011**

The Financial Reporting Council Limited is a company limited by guarantee.

Registered in England number 2486368.

Registered Office: 5th Floor, Aldwych House, 71-91 Aldwych, London WC2B 4HN



Printed on 100% Recycled paper

