

UK Transparency Report 2021
PricewaterhouseCoopers LLP
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Audit quality – Our system of quality management

This forms part of our FY21 Transparency Report

- Firmwide governance
- Independence and ethics
- People
- Audit quality**
 - Inspections and investigations on our audits
 - **Our system of quality management**
 - Our programme to Enhance Audit Quality, and our Root Cause Analysis
 - FRC Report on PwC UK's audit quality
- Our Audit methodology
- Finances and other disclosures



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Audit quality

Our system of quality management



Our system of quality management and monitoring processes

PwC UK's Audit internal quality control systems are based on International Standard on Quality Control (UK) 1 – 'Quality control for firms that perform audits and reviews of financial statements and other Assurance and Related Services Engagements' (ISQC (UK) 1). ISQC (UK) 1 applies to firms that perform audits of financial statements, report in connection with investment circulars and provide other assurance services where they relate to activities that are reported in the public domain and are therefore in the public interest.

The objective of ISQC (UK) 1 is for the firm to establish and maintain a system of quality control to provide it with reasonable assurance that:

- the firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and
- reports issued by the firm, or by engagement leaders, are appropriate in the circumstances

It is also important to note ISQC (UK) 1 is being replaced by two new quality management standards: International Standard on Quality Management (ISQM) (UK) 1 and ISQM (UK) 2. These two new standards require that the system of quality management is designed and implemented in line with these standards by 15 December 2022 and evaluated within one year of that date. ISQM (UK) 1 introduces a new quality management approach that is focused on proactively identifying and responding to risks to quality. This new approach requires a firm to customise the design, implementation and operation of its system of quality management based on the nature and circumstances of the firm, using an integrated approach that reflects upon the quality management system as a whole.

The UK firm implemented the QMSE framework in 2017 which is largely consistent with the requirements of ISQM 1 as issued by the IAASB. In preparation for the new standards, we have performed a comprehensive gap analysis to identify aspects of the new standards which may require additional consideration ahead of the implementation date. Whilst we are well progressed with the ISQM (UK) 1 transition plan, some of the changes (eg those which rely on developments across the PwC global network) will require further work and require some time to implement in advance of the implementation deadline.

In addition to compliance with ISQC (UK) 1, the FRC's International Standards on Auditing (UK) requires PwC UK to have quality control systems. Further:

- as a Registered Auditor regulated by the Institute of Chartered Accountants in England and Wales (ICAEW), we are required to comply with the Audit Regulations and Guidance ('Audit Regulations') issued by the ICAEW. Compliance with the Audit Regulations is required to enable the firm to retain its audit licence in the UK and Ireland¹;
- we are registered with the ICAEW as a Licensed Practitioner for the reporting on ATOL returns, and there are a number of individually Licensed Practitioners in the firm;
- we are registered with the ICAEW as a Local Auditor for the delivery of public sector audit work, there are a number of individuals registered as Key Audit Partners in the firm; and
- we are required to comply with the policies and regulations of a number of other regulatory bodies which PwC UK is either registered with, as a condition of ongoing registration to perform audits of certain entities, or regulated by. These regulatory bodies include the Financial Reporting Council, Public Sector Audit Appointments Limited, NHS Improvement, the Financial Conduct Authority and the Prudential Regulation Authority in the UK

In addition, each PwC Network firm is required to have in place a rigorous system of quality management (SoQM), to annually complete a SoQM performance assessment and to communicate the results of these assessments to global leadership. These results are then discussed in detail with the leadership of each local firm and if they are not at the level expected, a remediation plan is agreed, with local leadership taking responsibility for its successful implementation.

As our services change and develop, and the needs and expectations of our stakeholders also change, we are continually reviewing and updating the scale, scope and operations of our SoQM and investing in programmes to enhance the quality of the services that we provide.

¹ Following new requirements of the IAASA the registration that the ICAEW held in Ireland as a Recognised Accountancy Body in Ireland to undertake Irish statutory audits ceased on 30 June 2021.

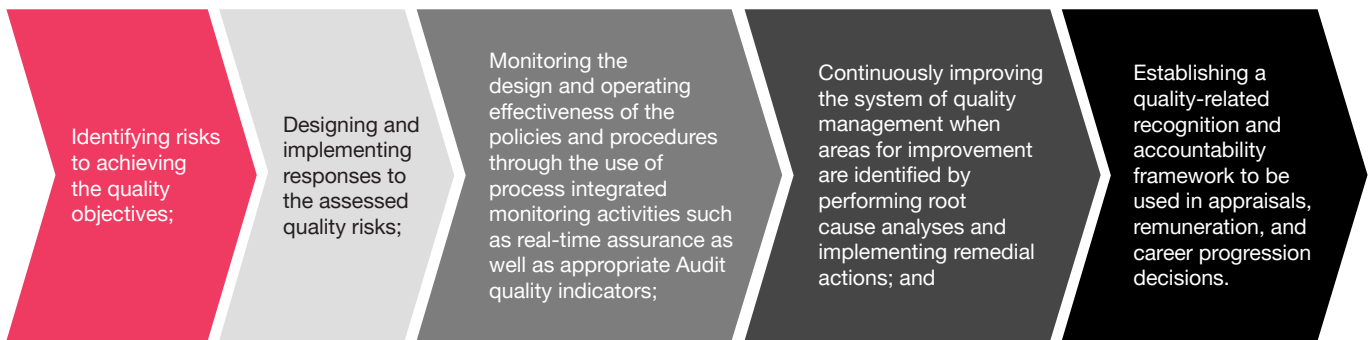


Quality Management for Service Excellence (QMSE)

The PwC Network has established a framework for quality management which integrates quality management into business processes and the firmwide risk management process. The framework introduces an overall quality objective for the Audit practice focused on having the people and processes to deliver services in an effective and efficient manner that meets the expectations of the entities we audit and other stakeholders.

This overall quality objective is supported by a series of underlying quality management objectives and our SoQM is designed and operated so that these objectives are achieved with reasonable assurance. The achievement of these objectives is supported by a quality management process established by our firm and Audit leadership, business process owners, partners and staff. The QMSE review covers the calendar year, i.e, 1 January - 31 December.

This quality management process includes:



One important component of the SoQM is that of monitoring. The below summarises the principles of our internal monitoring processes.

Quality Management Review (QMR)

Each PwC Network firm completes their internal monitoring procedures, the ECR and QMSE, annually. These processes are then reviewed annually by the PwC Network as part of the Quality Management Review (QMR) programme. The QMR scope is determined and agreed between the International Team Leader (the ITL provides oversight for all phases including scoping, execution and the overall classification and assessment of findings in the QMR and ECR) and the Member Firm and approved by the Global Assurance Quality – Inspections Leader. Reviews take place each year, ensuring that each of the 15 quality objectives are covered at least once every three years. The QMR monitors progress on remediation of any control issues raised in the last review and assesses the impact of any new developments on the internal quality control systems. The QMR is led and resourced from other PwC Network firms. No significant quality management findings have been self-identified by PwC UK, or identified by the 2021 QMR review which covered the period 1 January 2020 - 31 December 2020.

The Member Firm Report

A Member Firm Report is prepared annually by the International Team Leader assigned to PwC UK. The report includes the results of both the QMR and ECR for that year and an overall conclusion on the firm's quality control systems. Based on our analysis of the results of the activities described above, as well as our consideration of regulator reviews and the results of other internal monitoring activities, we are satisfied that our internal quality control system provides us with reasonable assurance of performing and reporting in conformity with applicable standards and PwC Audit in all material respects. The report also summarises the main points arising from the QMR and ECRs that merited attention. PwC UK responded to the points raised within the 2020 Member Firm Report as well as the from the root cause performed on the ECR and external regulator reviews and developed an action plan to address the matters noted. These actions were assigned to specific individuals and



significant progress has been made in addressing these matters. The 2021 Member Firm Report will be issued in Autumn 2021 to the Head of Audit, the Audit Risk & Quality leader, the governance bodies of the firm, and PwCIL. The Financial Reporting Council read the prior year Member Firm Report as part of their annual inspection and the 2021 report will be shared with the FRC in due course.

Engagement Compliance Reviews (ECR)

The key features of the annual ECR programme are:

- a cold review of completed audit engagements of individuals in the firm who are authorised to sign audit reports (known as Responsible Individuals);
- an audit engagement of each Responsible Individual is reviewed at least once every three years as required by the ICAEW Audit Regulations;
- completed audit engagements of market-traded companies incorporated in the Crown Dependencies (i.e. Jersey, Guernsey and the Isle of Man) are reviewed once every three years as required by the Crown Dependencies' Audit Rules and Guidance;
- in addition, the firm maintains a list of clients with a high public profile and the audits of these clients are reviewed twice in a six year period;
- a review of a sample of completed non-audit assurance engagements under the international and UK assurance standards and regulatory frameworks. The sample aims to reflect the range of different non-audit assurance work and its significance to the firm;
- engagement compliance reviews are led by experienced partners, supported by teams of partners, directors and senior managers who are all independent of the office, business unit and engagement leader being reviewed;
- follow-up reviews take place if significant deficiencies are identified;
- adverse findings and examples of high quality, where relevant, are taken into consideration in determining the reward and promotion of engagement leaders; and
- the results are reported to the Audit Executive, the Audit Oversight Body, and to PwCIL. The Financial Reporting Council and ICAEW also obtain these results as part of their annual inspections.

Each engagement reviewed is assessed using the following categories:

- 'Best in class' – All relevant auditing, assurance, accounting and professional standards have been complied with in all material respects and key aspects of the work made the engagement stand out from others as an example of best practice
- 'Compliant' – relevant auditing, assurance, accounting and professional standards have been complied with in all material respects;
- 'Compliant with improvement required' – the following circumstances would generally lead to this conclusion:
 - required assurance procedures relating to a significant account or area not performed or not documented substantially in accordance with standards, but it is determined that due to the audit evidence in other sections of the archived work papers no additional procedures are required to be performed;
 - assurance procedures that failed to detect a departure from applicable accounting standards that was considered both quantitatively and qualitatively insignificant; or
 - evaluation of control weaknesses was not performed substantially in accordance with professional standards, but the impact was not considered to be sufficiently significant to require modification to the audit report on internal control over financial reporting if applicable and/or adequate consideration was not given to any necessary modifications to the substantive approach applied due to the control weaknesses;

but in all cases, sufficient audit work has been performed in all other respects.

- 'Non-compliant' – relevant auditing, assurance, accounting and professional standards or documentation requirements were not complied with in respect of a material matter.

In the case of a 'best in class' engagement, there is a mechanism to ensure that the high quality work is recognised as part of key personnel's annual performance appraisals.



In the case of a non-compliant engagement, follow up reviews are undertaken in the same cycle, the engagement leader will be reviewed again in the subsequent year's ECR and there are financial implications for the individual Engagement Leader. Following root cause analysis, consideration is also given as to whether additional support, training or monitoring of the engagement leader is required.

The circumstances giving rise to non-compliant findings are also considered in order to assess whether additional work is needed to support the report, if the auditor's report needs to be withdrawn or if the entity's financial statements for the current period of the following period need to be restated.

For engagements which were found compliant with improvement required, the engagement leader is included in the following year's ECR, and this may also lead to financial implications depending on that engagement leader's previous quality track record.

The firm undertakes root cause analysis ("RCA") for all inspections with non-compliant outcomes and a number of compliant with improvement required and compliant engagements, including engagements identified as 'best in class'. The best in class analysis helps identify success factors that inform potential actions. Following RCA, a Quality Improvement Plan ("QIP") is developed to respond to the drivers of systemic issues and specific matters arising from the ECR. Responsive actions may be identified at either the engagement delivery and/or line of service levels. Completion of the ECR and Regulatory finding action plans are monitored by the Audit Risk and Quality leadership, the Audit Executive and the firm's Public Interest Body.

