



Financial Reporting Council

Key findings and good practice – Appendix

Audit Quality Review

October 2025

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This is the Appendix to the [Key findings and good practice report](#), which contains the detailed anonymised key findings and good practice for each section listed below. The report provides a summary of each section.

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1. Impairment of non-current assets

Challenge and evaluation of management assumptions

Impairment reviews are inherently subjective and changes in key assumptions could result in impairment charges. Auditors should perform sufficient procedures to evaluate the impairment models prepared by management and corroborate and challenge the key assumptions applied within those models.

Background	Issue
The audit team had identified a significant risk and Key Audit Matter over the recoverability of goodwill for one cash generating unit (CGU). Management forecasted notable growth in revenue and earnings before interest and taxes (EBIT) margins in years one to five. The CGU operates in a number of different countries and markets. It has certain revenue streams where a significant risk was identified over the timing of revenue recognition. The CGU also had a history of optimism in its forecasts and low growth in recent years. Audit procedures performed over the years one to five cash flows included holding inquiries with management, benchmarking to analyst, comparable company and industry forecasts, and sensitising cash flows.	The audit team performed insufficient procedures to corroborate and challenge the reasonableness and achievability of management's Years one to five cash flow forecasts. In particular given: • The reduction in headroom, optimism and lack of accuracy in management's previous forecasting ability and past trends in recent performance. • No detailed analysis of the assumptions underpinning the CGU forecasts was performed.
Cash generating unit 1 An impairment reversal was recorded in this CGU. Significant revenue growth was projected in management's forecasts, despite historical underperformance. Cash generating unit 2 CGU2 had an operational leasehold property and had been loss-making at an earnings before interest, taxes, depreciation and amortisation (EBITDA) level in FY2X. An EBITDAR (EBITDA after adjusting for external rent) multiple-based test was performed to assess for impairment.	The audit team did not adequately evaluate or evidence its challenges over aspects of management's impairment assessment. In particular, the audit team did not adequately: • Challenge management over the growth assumptions used in the impairment assessment for CGU1. • Evaluate the appropriateness of the EBITDAR multiple used in the impairment assessment for CGU2. • Understand the reasons for the ongoing EBITDA losses for CGU2 and challenge whether this was an indicator of impairment.

Background	Issue
The audit team's challenge of the initial cash flow model assumptions resulted in a material impairment, which was reported in the auditor's report. The updated impairment models on the audit file, used to calculate value in use (VIU) for a CGU included the actual cash flows of FY2X. The audit team explained to us that this was to compensate for using year-end discounting, instead of mid-year discounting. However, this was not explained on the audit file and, if this was not the case, there would have been an additional material impairment charge if management removed the FY2X cash flows and continued to apply year-end discounting. In addition, the FY2X actual cash flows were included in the audit team's alternative sensitivities testing results that discounted the cash flows using mid-year discounting and were therefore calculated incorrectly.	There was insufficient evidence of the audit team's evaluation of aspects of a CGU impairment model prepared by management, and the sensitivities prepared by the audit team were incorrectly calculated. In particular, the audit team did not: • Challenge management about including FY2X actual cash flows to compensate for a year-end discounting approach and evidence its assessment as to why this approach was appropriate. • Evidence its independent calculation of the impairment model using mid-year discounting. • Evidence that the approach was discussed with management and the Audit Committee and that there was consideration of additional disclosures about it.
Management prepared a valuation of the CGU based on a discounted multiple of forecast FY30 EBITDA. The EBITDA forecasts used in the valuation assumed significant customer growth at a multiple of 37 times from that seen in the current period. The audit team obtained two alternative valuations, prepared by an expert firm, used by management: • A draft indicative assessment of the CGU's market value, prepared at year-end, which incorporated the same underlying EBITDA forecasts and which was not prepared for impairment purposes. • An alternative use land valuation, over which no further audit procedures were performed.	The audit team did not obtain sufficient, appropriate audit evidence to support its conclusion that the carrying value of the CGU was not impaired. In particular, the audit team did not perform sufficient procedures to evaluate and challenge the methodology, EBITDA forecasts and other assumptions used in management's valuation, or adequately consider the level of assurance provided by the alternative valuations.

Background	Issue
Accounting Standards state that, in measuring value in use, an entity shall use a steady or declining growth rate for cash flow projections beyond the most recent budget/forecast period, unless an increasing rate can be justified. They also state that this growth rate shall not exceed the long-term average growth rate for the products, industries, or countries in which the entity operates, or for the market in which the asset is used, unless a higher rate can be justified. Management's value in use calculations for a CGU group were based on five-year cash flow forecasts extrapolated to nine-years before applying the long-term growth rate assumptions. The growth rates assumed after year five were based on the average forecasted growth for the global market the CGU operated in. As a result of the audit team's challenge, there was a goodwill impairment charge of over £100 million for the CGU in the group. However, the impairment model included significant revenue growth from two years' time onwards following a downturn in recent years.	There was inadequate evaluation and challenge by the audit team of the extrapolated cash flow forecasts used in the value in use calculations. In particular, there was insufficient justification and support for the revenue growth assumptions used for the CGUs.
During the year, goodwill attributable to a CGU was fully impaired, but management determined the recoverable value was sufficient not to impair other assets in that CGU. The audit team's testing of management's impairment assessment involved developing its own range for the recoverable values. The audit team's range included revenue from a new contract that was not in management's model.	The audit team did not adequately evaluate or challenge management's impairment assessment for goodwill and other assets, resulting in insufficient evidence to conclude on the recoverability of the other assets. The audit team did not sufficiently challenge or corroborate the reasonableness of certain forecasted cash flow assumptions, specifically the revenue growth and margin assumptions included in both management's model and the audit team's range.

Background	Issue
There was a material impairment charge recognised during the year, reflecting the impact of the significant decline in the company's operational market and key commodity prices in 202X.	The audit team did not obtain sufficient, appropriate audit evidence to support its conclusions over the impairment of tangible fixed assets. In particular, the audit team did not sufficiently evaluate, corroborate and challenge the methodology, cash flow forecasts and other key related assumptions in management's impairment models. As a result of these deficiencies, there was an unacceptable risk of a material misstatement not being detected.
Management identified three CGUs including CGU1. Management assessed the VIU of CGU1 using forecast income and costs derived from management estimates and data.	The audit team did not obtain sufficient, appropriate audit evidence to support its conclusions over the carrying value of goodwill attributable to CGU1. Specifically, the audit team did not sufficiently evaluate, corroborate and challenge the forecast income used by management in its VIU impairment assessment.
The group held non-current assets at non-operational sites at year-end. In the prior year, management engaged an expert to provide cash flow models to support the carrying value of these and other operations. In the current year, management relied on these models, applying updated inputs and assumptions to assess potential impairment as at year-end.	The audit team did not perform sufficient procedures to evaluate and challenge the modelling assumptions applied in management's impairment assessments for the non-operational sites. In particular, the audit team did not perform sufficient procedures to assess whether the prior year models prepared by an expert continued to be appropriate to use as a basis for the current year assessment.
The cash flow forecasts used in the impairment assessment for property, plant and equipment, assumed that the group would generate operating profits from 202X onwards, despite the group having operated at a gross loss for the previous five years. The key driver of this forecast was a contract with a new supplier, which had more favourable terms compared to contracts with other suppliers.	The audit team did not perform adequate procedures to support its conclusions over the impairment of property, plant and equipment. In particular, the audit team did not adequately evaluate and challenge the cash flow forecasts used in management's impairment assessment.

Background	Issue
Management performed annual impairment assessments for certain operating assets. These were carried out separately for each CGU, which management identified as being at the acquisition level. There was no evidence of any audit procedures being performed over the cash flow forecasts and assumptions for one of the CGUs, other than high-level inquiries with management.	The audit team did not perform sufficient substantive procedures to test management's impairment assessments for certain operating assets. In particular, the audit team did not: • Adequately evaluate or challenge the appropriateness of the identification of CGUs at the acquisition level. • Perform sufficient procedures to evaluate and challenge the cash flow forecasts used in a CGU's impairment assessment.
Management prepared a discounted cash flow model to support its assessment that there was no impairment in a CGU. This model included short-term growth assumptions that were above certain market data and relied on management implementing their business improvement plan. Management's calculation of the discount rate did not include an entity-specific risk premium that related to the growth rates.	There was insufficient evaluation and challenge by the audit team of the short-term growth and related discount rate assumptions used in management's goodwill impairment assessment for a CGU. The audit team also did not sufficiently challenge management on the related sensitivity and significant estimate disclosures.
The group had experienced a significant reduction in its net revenue due to the challenging macro-economic environment. A VIU model was prepared by management to determine the recoverable amount for goodwill impairment testing. This model incorporated significant revenue growth and margin improvements in the short-term forecasts. The audit team did not analyse the feasibility of the revenue growth and margin improvement predictions, nor challenge the recovery from macro-economic environment factors.	The audit team did not challenge or corroborate certain key assumptions used in management's impairment assessment. In particular, the short-term forecast revenue growth predictions and margin improvements that were sensitive in assessing whether an impairment was required.

Background	Issue
Management identified impairment indicators in both the current and preceding year, for a property with a carrying value of £X million. It recognised an impairment of 50% of that value as a prior year adjustment. The audit team requested that management recognise the impairment as a current year charge and therefore raised an audit adjustment to reverse management's accounting treatment. Planning consent for the property was previously rejected and rejected again following appeal a year later, during the financial period. The prior year impairment assessment relied upon an analysis of the net present value of the scheme, based on planning permission being granted. There was no quantification of the value of the land under alternative uses.	The audit team performed inadequate procedures and obtained insufficient evidence to conclude it was appropriate to recognise the impairment charge in the current period, rather than as a prior year adjustment. There was no evidence of how the audit team had concluded there was no fundamental accounting error in the prior year, given the basis of the impairment assessment and the refusal of planning consent.
Management engaged an external expert to perform the valuation of derivatives at the year-end. The audit team performed an assessment of the expert's competency, objectivity and independence. In addition, the audit team prepared a high-level memo evidencing its considerations and conclusions in respect to the key valuation assumptions.	The audit team did not perform sufficient audit procedures to assess the fair value of the derivative financial instruments at the year-end. Specifically, the audit team did not corroborate and challenge key valuation assumptions and did not test the integrity of the valuation model.

Accuracy of management's impairment models

Auditors should perform robust procedures to evaluate the integrity of impairment models prepared by management and corroborate and challenge the key assumptions applied within these to ensure there is no material impairment in the asset.

Background	Issue
The audit team's procedures on impairment of a CGU included testing management's VIU model, which indicated an impairment. Our inspection identified errors in the VIU model that were not identified during the audit process. The impairment indicated by the VIU model was not recognised, as it was concluded that the fair value less costs of disposal (FVLCD) of the CGU was higher than its carrying value. Management did not prepare a formal FVLCD model. The audit team considered two sources to support this position: a feasibility study and an analysis of recent market transactions in the surrounding area.	The audit team did not obtain sufficient and appropriate audit evidence to support its conclusion that no impairment was required for the CGU. In particular, the audit team performed inadequate procedures to challenge: • The methodology and key assumptions applied in the feasibility study. • The comparability of the recent market transactions. In addition, the audit team did not identify factual errors in the VIU model.

Background	Issue
Management's impairment assessment for a CGU was performed on a VIU basis. The cash flow forecasts used in the model included some overseas tax reliefs that management assumed would be claimable over a period of 15 years. These were erroneously extrapolated into perpetuity in the model cash flows. Furthermore, as the group was also not itself eligible for these reliefs, these should have been excluded in full from the VIU model. The cash flow forecasts used in the model also included significant revenue growth, driven in part by the launch of a new product and improvements in margins over the forecasting period.	The audit team did not obtain sufficient, appropriate evidence to support its conclusions over the CGU impairment assessment. In particular, the audit team did not adequately evaluate and challenge the model methodology, cash flow forecasts and related assumptions, and failed to identify a material factual error in the impairment model. As a result of these deficiencies, there was an unacceptable risk of a material misstatement not being detected.

Use or evaluation of experts and data

Auditors should obtain adequate reporting from its expert to be able to challenge, corroborate and conclude on the appropriateness of the key assumptions used in the valuation.

Background	Issue
The audit team used an expert from the firm's real estate team to review certain key assumptions such as discount and yield rates. No formal scope, written report or conclusion from the expert was obtained. The detailed calculations supporting the discount rates and exit yields were not obtained from management's expert. For some operational and investment properties, the audit team developed its own acceptable range for certain valuation assumptions using comparable properties. A very wide range was determined, and the audit team concluded that the valuation was reasonable as it fell within this range.	The audit team performed inadequate procedures and challenge over the valuation of freehold and investment properties. In particular: - The audit team did not obtain adequate reporting from its expert to be able to challenge, corroborate and conclude on the appropriateness of the key assumptions used in the valuation of the freehold properties. - The audit team failed to perform sufficient procedures over the precision of the acceptable range and suitability and representativeness of the comparator data sets used in assessing the valuation of the operational and investment properties.

Recoverability of the parent company's investments in subsidiary undertakings

Investments in subsidiaries should be assessed to ensure there is no material impairment in their carrying value. Any impairment can have a material impact on distributable reserves.

Background	Issue
The parent company held a material investment in subsidiary undertakings. Management's VIU calculation, as part of their impairment assessment, did not take into consideration the impact of external debt and lease liabilities, held via indirect subsidiary undertakings. Subsequent to the audit, management agreed that the debt held by the company's subsidiaries should have been deducted from the value in use calculation and that this would result in a material impairment.	The audit team did not perform sufficient audit procedures over the recoverability of the parent company's investments in subsidiary undertakings. In particular, it did not challenge management to deduct debt held by the company's subsidiaries from the VIU calculation. As a result, the audit team did not identify a material misstatement in the carrying value of the parent company's investment in subsidiary undertakings.
Neither management's assessment of the recoverability of the investments held by the company nor an evaluation of this by the audit team were evidenced on the audit file. The audit team considered these matters and confirmed that management had updated its impairment calculation. Based on this calculation, the total impairment should have materially higher.	The audit team did not adequately assess and challenge the carrying value of the parent company's investments in subsidiary undertakings. In particular, the audit team did not: • Obtain an impairment model that supported the disclosed impairment charge and the reporting to the Audit Committee. • Evidence a review of management's impairment assessment assumptions. • Challenge the appropriateness of the lack of any adjustments for external debt cash flows or inter-company cash flows.

Background	Issue
At the time of the audit, management assessed the recoverability of the parent company's investments in subsidiary undertakings by considering the FVLCD. This was not determined to be lower than carrying value, so no impairment was made. The audit team's review focused on FVLCD. The impairment assessment did not consider the impact of an intercompany receivable. Management reassessed the FVLCD and prepared a VIU calculation for the entities below the parent company, incorporating the intercompany receivable. The VIU was higher than the amended FVLCD and management estimated that a material impairment was needed to the recoverable value of the parent company's investment in subsidiary undertakings as at year-end.	The audit team did not adequately assess the recoverability of the parent company's investments in subsidiary undertakings. In particular, it did not consider the impact of the intercompany receivable due to the parent company on the impairment assessment.
At the year-end, the carrying value of the investment in a subsidiary undertaking was considerably above the entity's market capitalisation and an impairment assessment was performed. Management prepared a VIU model, which included revenue growth assumptions that were above the external market forecasts, for a particular territory.	The audit team did not sufficiently assess and challenge the carrying value of the parent company's investment in the subsidiary undertaking. In particular, it did not sufficiently challenge or corroborate the appropriateness and achievability of the revenue forecasts in light of the lower external regional market forecast growth rates.

Impairment of non-current assets: good practice points

Robust challenge of management assumptions

- The audit team extensively challenged management on the appropriateness of the assumptions included in the goodwill impairment assessment, including instances of where 'within an acceptable range' was most appropriate, which resulted in management recognising a material impairment charge. The extent of challenge was clearly communicated to the Audit Committee.
- The impairment calculation prepared by management was complex and reflected multiple transformation initiatives. The audit team's assessment and challenge of the evidence obtained over the multiple uncertainties within the assumptions was robust and clearly evidenced.
- The audit team robustly challenged management's regional revenue and EBIT growth rate assumptions used in the goodwill impairment model. The team achieved this by disaggregating the revenue for each country and obtaining future sales contracts to corroborate the individual growth rate assumptions.
- The audit team robustly challenged management's key inputs and assumptions used in the two goodwill impairment models. This included:
 - Performing audit procedures over the order books for each of the CGUs to corroborate revenue growth assumptions.
 - Challenging management's downside scenarios, including whether it was appropriate to include certain revenue streams in the models.
- The audit team challenged management over the impairment of patents, requesting them to perform a line-by-line review of each of these. This review resulted in a further impairment charge of approximately three and a half times materiality being made.
- The audit team challenged the consistency of the CGUs used for the segmental reporting disclosures and the valuation of goodwill assessment, leading to management updating the CGUs used for the valuation of goodwill.
- The audit team's procedures over the valuation of goodwill included additional sensitivities covering scenario analysis of changes in a key contract within the material CGU to assess any adverse impact on the value of goodwill.
- The audit team made site visits, led by the engagement partner, to certain overseas businesses. The extent of the procedures performed provided additional assurance regarding its evaluation and corroboration of short-term cash flows used in the impairment assessment for a specific CGU.

Use of specialists and tools

- The group considered each unit to be a CGU and the impairment assessment covered over 100 individual CGUs. Given the high number of CGUs included in the impairment assessment, the audit team used a tool to analyse possible impairment to perform sensitivities. This software enabled the audit team to perform sensitivities tests over all the CGUs in an effective way.
- In response to the significant risk identified, the audit team involved the audit firm's impairment specialist when designing the approach. The specialist assisted them in challenging management in respect of key assumptions in the VIU models. The audit team further benchmarked key assumptions used in the models to industry experts' reports.
- As part of the goodwill impairment testing, the audit team completed sensitivities tests using assumptions independently determined by their valuation specialist, evidencing the basis for each sensitivity and the conclusion on each scenario.
- The audit team performed independent recalculation and validation, including the use of internal specialists, over management's onerous lease and impairment model. This provided assurance over the accuracy of the model formulas and ensured the audit team had identified and understood each input used in the model. Given deficiencies in the control environment in the group, this demonstrated an appropriate application of professional scepticism.
- There was robust challenge of management over its assumptions in the goodwill impairment model. This resulted in management updating both the contingency for known losses and forecast win rates. In addition, the audit team used its own net present value model based on combined sensitivities to develop an independent headroom expectation.

Use of external data and benchmarking

- The audit team demonstrated a detailed knowledge and understanding of the group's products. This knowledge, together with the extensive use of third-party data, allowed the audit team to target its intangibles impairment testing and robustly evaluate the assumptions used in the impairment models.
- In the audit of goodwill impairment, the audit team made good use of third-party research/data and benchmarking. Discussions were held with colleagues in the audit firm and management to gain insight into the market where the entity operated and the prospects for the company. There was robust challenge of the management expert used to calculate discount rates and the level of sensitivity disclosures made in the financial statements.
- The audit team performed extensive procedures to evaluate the group's brand impairment testing. Particular focus was given to the revenue forecasts used, including analysing market research of changes in consumer behaviour to identify demand trends within individual brands.
- The audit team responded effectively to the risk of recoverability of goodwill by performing specific procedures to challenge and corroborate management's assertions. The procedures included consulting internally with industry experts for a specific market, verifying the popularity of the customer-facing software application by checking third party customer reviews, and formally consulting on the appropriateness of the treatment of working capital in the cash flows and in the carrying value of the CGU.
- The audit team performed extensive challenge over the key inputs and assumptions used in management's impairment model. It prepared its own downside scenario model to assess growth rates against third-party research and whether there was sufficient headroom in the model.
- The team also held discussions with colleagues who possessed industry expertise, including the firm's specialist, to gain market insights and help assess whether the growth rates were achievable.
- The audit team performed extensive external source analysis, demonstrating clearly both corroboratory and contradictory evidence in relation to revenue growth rates.
- The audit team also demonstrated a clear linkage between the nature and extent of the sensitivities applied in relation to goodwill impairment and the substantive work performed over the relevant assumptions.

2. Provisions including expected credit losses

Provisions

The assessment of provisions requires judgement and evaluation of facts and circumstances. Auditors should appropriately assess and challenge management's judgements to assess the completeness and accuracy of provisions.

Background	Issue
Management did not recognise a provision at year-end for certain building work changes required by legislation. Commitments were disclosed in the financial statements. While the group had committed with third parties to complete certain works and disclosed this in the financial statements, the audit team concluded there was no constructive obligation as this had not been individually communicated to affected individuals.	The audit team performed insufficient procedures to assess and challenge the completeness of the year-end disclosed commitments and the judgement on the recognition of a provision. The audit team did not sufficiently challenge the conclusion that there was no legal or constructive obligation to perform building works, despite contradictory evidence existing (such as communications with individuals via the group's website and disclosure of commitments within the accounts).
The X provision reflected the impact of volatility in certain used asset residual values. The provision was computed by adjusting the estimated market value of assets and historical re-sale performance using certain assumptions. A relatively small change in these assumptions could have resulted in a material change to the provision. The audit team challenged management over various aspects of the provision and obtained their responses. No assessment or evaluation of those responses was performed and the relevant working paper was not retained in the archived audit file.	The audit team performed insufficient audit procedures to corroborate and challenge the assumptions used by management in computing the X provision.

Insurance technical provisions

The valuation of insurance technical provisions is complex and may be subject to conscious or unconscious management bias. Auditors should test the data inputs and assumptions used in valuing the provisions and where they rely on external experts, evaluate their work and assess whether it provides sufficient appropriate audit evidence.

Background	Issue
The audit team engaged an actuarial firm, as its expert, in connection with the valuation of the insurance technical provisions.	The audit team did not perform adequate procedures to confirm the completeness and accuracy of members' data, a key element of the valuation of the technical provisions. It did not evidence an appropriate understanding of the data flows between the parties, what data files were exchanged between them or identify which aspects of members' data were key to the reserving process. In addition, it did not sufficiently evaluate the appropriateness of the expert's work and conclude whether its final report could be treated as audit evidence.

Expected credit losses

Determining the level of expected credit losses (ECL) involves significant management assumptions and estimation uncertainty. Audit teams should consider the subjectivity of management's judgements and evidence appropriate procedures commensurate with the associated risks.

Background	Issue
Management applied models to determine the ECL allowance on loans and advances to customers. Post model adjustments (PMAs) were applied to the modelled ECL to arrive at the final ECL recognised in the financial statements. PMAs were recognised to address model limitations as at year-end. The audit team performed substantive audit procedures over critical data elements, significant increase in credit risk (SICR), multiple economic scenarios, modelled ECL and post-model adjustments and concluded that the ECL recognised in the financial statements was appropriate.	The audit team did not obtain sufficient audit evidence to support the appropriateness of the ECL allowance recognised. Several weaknesses in the audit work performed across ECL were identified, including: • Risk assessment. • The identification and testing of the completeness and accuracy of critical data elements used in the ECL model. • The assessment and testing of significant increase in credit risk. • Multiple economic scenarios. • ECL models. • Post-model adjustments. • Quality control and review procedures over ECL.
The audit team engaged an auditor's expert (firm X) to assist in the audit of ECL and the fair valuation of financial instruments.	The audit team did not perform sufficient procedures to be able to rely on the work of the auditor's expert. As a result, the audit team did not obtain sufficient, appropriate audit evidence in the areas of the audit where firm X was engaged. The audit team did not: • Sufficiently assess the competency and capabilities of firm X to perform the required procedures over ECL and the valuation of financial instruments. • Scope the work of firm X sufficiently between audit-related roles and specialist responsibilities. • Direct and supervise the work of firm X. • Assess the appropriateness of the underlying work performed or reporting from firm X.

Background	Issue
Determining the level of ECL involves significant management assumptions and estimation uncertainty. Audit teams should consider the subjectivity of management's judgements and evidence appropriate procedures commensurate with the associated risks.	On two inspections, the separate firm audit teams did not perform adequate procedures to test ECL and consequently failed to obtain sufficient, appropriate evidence that the ECL allowance was free from material misstatement. There were pervasive deficiencies in the audit team's testing approach and the quality of evidence obtained in this area.
Management individually assessed certain exposures and applied models to determine the ECL allowance on loans and advances to customers. The audit team performed substantive audit procedures over key data elements, SICR, multiple economic scenarios, modelled ECL and the need for post-model adjustments and concluded that the ECL recognised in the financial statements was appropriate.	The audit team did not perform sufficient audit procedures to test the valuation of ECL. Several weaknesses were identified in the audit work performed across ECL, in particular, the completeness and accuracy of data inputs and the challenge of estimates and assumptions. This included the work over key data elements testing, individually assessed exposures, SICR and stage allocation testing and in the modelled macroeconomic scenarios.
Amounts due from customers under a particular scheme (receivables) were recognised as financial assets at amortised cost, using their nominal value (based on the receivable being payable on demand). The group assessed the ECL on the receivables based on an estimate of scheme values compared with the receivable. The audit team did not obtain or analyse the contract terms for the customer arrangements.	The audit team did not perform sufficient and appropriate procedures to challenge and evaluate the accounting treatment of the receivables and assess their recoverability. In particular, the audit team did not adequately assess the judgements made relating to the initial recognition and subsequent measurement of the receivables.

Background	Issue
The audit team engaged its experts and specialists to evaluate and challenge the appropriateness of key assumptions in the computation of ECL allowance. These included loss given default (LGD) rates, exposure at default (EAD), probability of default (PD) and macroeconomic variables.	The audit team did not perform adequate audit procedures to evaluate and challenge the approach and the appropriateness of key assumptions applied by management in the computation of the ECL allowance. The audit team did not adequately: • Assess and justify the appropriateness of management's application of LGD rates as per regulatory guidelines across the portfolio. • Assess the approach to determining EAD, including considering whether this should have been discounted across the portfolio(s) depending on the stage of the loan or if further adjustments were necessary. • Assess and justify why there was no risk of error as a result of the entity not adjusting for borrower specific risks and staging in PD.

Provisions including expected credit losses: good practice points

Use of specialists and experts

- The audit team involved forensic specialists who performed an extensive analysis, considering the probability of success in detail for individual items making up the claim value, and determined an independent range for assessing the appropriateness of the legal provision.
- The audit team's actuaries demonstrated a good understanding of the entity's business and the rationale for the level of technical provisions. They combined independent projections with a review of the entity's methodology and assumptions in assessing the reasonableness of the provisions.
- The audit team performed extensive work in response to potential fraud risks identified relating to the overseas operations. This included engaging the audit firm's forensic team to analyse communications between certain individuals, holding a quality control panel (which included the relevant risk partner) and engaging an additional UK audit partner to take direct responsibility for the overseas operations audit work. They responded well to specific audit challenges, performing extensive work relating to the onerous contract provision identified as a key audit matter.
- The procedures in relation to completeness of uncertain tax positions included a detailed analysis of the register of unprovided tax risks by the firm's tax specialists; engagement of the firm's specialists to review the transfer pricing arrangements for unprovided risks; and regular interactions with the group and component audit teams' tax specialists during the audit.
- The firm's credit modelling specialists assessed and challenged a large number of ECL models, resulting in the independent recalculations using replication tools of a significant amount of the modelled ECL across the group. This allowed the audit team to challenge management's ECL calculation and where appropriate, the impact of key ECL assumptions.

Robust risk assessment

- The audit team performed a detailed risk assessment of management's assumptions used in the restoration and decommissioning provisioning. This led the team to robustly challenge management on the assumptions and to test the integrity of the models used. Consequently, material errors were found in relation to both the modelling and the accounting treatment that were communicated to the Audit Committee.
- The audit team performed extensive audit procedures over closure provisions. This included a detailed risk assessment of management's assumptions, challenge of these assumptions and the work of management's experts.
- The audit team comprehensively demonstrated how it had performed its ECL model risk assessment and how this linked to the substantive procedures performed to address those risks. This ensured appropriate procedures were performed.
- The group audit team utilised a detailed benchmarking exercise across the firm's bank audits. This allowed the group audit team to assess the risks and pinpoint the risk criteria at an appropriately disaggregated level. As part of this process, the group audit team considered any potential inconsistencies across the various global audits and what impact this should have on the audit of the group.

Thorough process understanding and challenge

- The audit team held direct inquiries with a third-party law firm during its audit of a provision. The level of detail captured in the minutes of the call, including a range of pertinent probing questions raised by the audit team, was well evidenced and demonstrated professional scepticism in response to the identified significant risk.
- Claims were administered by a service organisation. The audit team held a meeting with its representatives and performed a thorough and detailed walkthrough of the relevant process. Alongside inquiries around the process, this included a detailed examination of relevant documents.
- The audit team's procedures, in relation to the completeness of onerous contract provisions within a division, were thorough and included clear evidence of challenge, resulting in changes to management's models. The level of detail in the file note demonstrated good professional scepticism in response to the identified significant risk.
- The group audit team designed a comprehensive credit rating review template based on its understanding of the group's processes and risks and sent it to all component audit teams. This enabled consistency in the quality of evidence obtained across the group for credit rating review testing.

3. Revenue recognition

Contract accounting

Accounting for long-term contracts is highly judgemental and can be susceptible to management bias. Auditors should therefore exercise appropriate professional scepticism when challenging management's significant judgements.

Background	Issue
The group recognised revenue relating to service contracts over time. The service revenue represented income from two customers. The audit team requested management to prepare a paper to explain the appropriateness of its revenue recognition policy. Management included personnel-related costs supporting the service contracts in research and development expenditure.	There was insufficient evidence that the audit team considered whether customer approvals may have represented performance obligations, contrary to management's policy of recognising revenue over time. The audit team did not challenge management over whether personnel costs, relating to the service contract revenue, should have been included in cost of sales.
The audit team identified that revenue recognition involved key judgements, such as the allocation of revenue to performance obligations. The audit team's testing included recalculating revenue and any accrued or deferred revenue, based on a sample of invoices. The audit team stated that all sample items were tied back to signed contracts tested in prior years, but this was not evidenced (except for certain transactions).	The audit team performed inadequate procedures over revenue recognition, so the risk of an undetected material misstatement remained unacceptably high. In particular, the audit team did not: • Adequately assess and challenge management on the key accounting judgements made. • Obtain external evidence to substantiate recurring license and maintenance revenue.

Background	Issue
The entity recognised a revenue stream based on the percentage of completion method and calculated it based on labour hours worked at each reporting period compared to the estimated total labour hours required to deliver the service over the contract life (forecast hours). A significant risk and key audit matter was identified over the estimation of forecast labour hours. To test the appropriateness of management's forecast labour hours for each contract, the audit team performed a high-level review of the movements of forecast hours at different points in time.	The audit team performed inadequate procedures to conclude on the appropriateness of the contract revenue recognised for a specific revenue stream. The audit team did not perform adequate procedures to corroborate and challenge the level of forecast hours for each contract. In particular, the audit team's procedures did not provide sufficient assurance over the estimate, given it did not: • Challenge the forecast hours at a sufficiently granular level for each contract. • Corroborate management's explanations by obtaining supporting evidence over the accuracy and completeness of forecast hours.
Certain contracts typically have a duration of X months and have multiple performance obligations. The overseas component auditor's testing for a sample of contracts focused on obtaining corroborative evidence to validate year-on-year changes in contract value, holding inquiries with project managers on contract performance, and agreeing costs to third party invoices. The primary procedure performed by the overseas component auditor over this revenue was a cash-to-revenue substantive analytical procedure (SAP). The overseas component auditor developed an expectation from cash receipts in the year, adjusted for certain transfers, non-revenue items and movements in accounts receivable.	The group auditor failed to ensure that sufficient, appropriate audit evidence was obtained over the overseas revenue. There were multiple deficiencies in the underlying work over revenue performed by the overseas component auditor. Most significantly, these included: • Insufficient validation that contract revenue was recognised in accordance with underlying performance obligations and that the fair value of performance obligations were appropriate. • No testing performed over the stage of completion and associated costs to complete for contracts not completed at year-end. • No audit procedures performed over the residual population of contracts. • Insufficient testing over the accuracy of the allocation of costs to contracts. • Insufficient precision in the cash-to-revenue SAP performed for other revenue and no audit procedures to validate the reliability of key listings supporting this analysis.

Background	Issue
The group accounts for long-term contracts following the percentage of completion method, measured by the percentage of total costs incurred. The group's Quantity Surveyors (QS) record adjustments where necessary to ensure all costs relevant to the period have been accrued, for example, in cases where third-party certifications have been provided at different times to the year-end date. Additional costs may be incurred from when projects commence, resulting in changes to the forecast cost to complete for contracts.	The audit team performed insufficient audit procedures over estimation uncertainty in the accounting for long-term contracts. For costs incurred on contracts, the audit team did not perform sufficient audit procedures to: • Test the completeness of QS adjustments made to subcontractor costs. • Validate the accuracy of subcontractor costs recognised at year-end. For costs to complete, the audit team performed insufficient procedures to assess, corroborate and challenge the accuracy and completeness of forecast costs to complete for contracts that were not substantially complete at the year-end.

Testing over complex revenue streams and arrangements

Auditors should undertake sufficient procedures and obtain appropriate supporting evidence to confirm that revenue is not materially misstated.

Background	Issue
Gross fund fees represented a significant proportion of the group's total revenue. As part of the audit procedures performed, the audit team agreed a sample of gross fund fees recorded to Excel reports provided by management, who had received these from third-party fund administrators (TPA). The audit team also reviewed service organisation assurance reports for the TPAs and identified no control weaknesses.	The audit team did not perform adequate testing over the gross fund fees and, therefore, obtained insufficient audit evidence over that revenue. In particular, the audit team did not: • Justify why the TPA reports were considered to be an independent and reliable source of audit evidence. • Verify sufficiently the authenticity of the TPA reports or obtain them directly from the TPAs. • Agree the revenue to bank statements or set out the reasons for not doing so. The audit procedures performed were not accurately stated in the auditor's report or the reporting to the Audit Committee, given that the gross fund fees were not agreed to bank statements.

Background	Issue
The group's revenues are earned through participation in pooled arrangements with other entities, based on items created in a collective. The group recognises revenue when the reward received has been allocated from the pool and credited to it.	The audit team performed insufficient procedures to test the allocated rewards and transaction fees awarded from its operations.

Rebates and deferred revenue

Sales rebates have a high level of judgement and estimation applied in their computation and recognition, and management are able to override related controls. This gives rise to a fraud risk relating to manipulation of profits.

Estimating deferred revenue based on future customer behaviour requires significant judgement. Auditors should perform sufficient procedures to assess whether the adjustments for deferred revenue are appropriate.

Background	Issue
The year-end rebate accrual balance included historical accruals in excess of materiality that related to prior year discounts not subject to testing in the current year audit. The audit approach involved a combination of authorisation controls and substantive sample testing. For a sample of rebates, relating to verbally agreed sales promotions, the audit team agreed the data inputs from the rebates schedule back to the internal system.	The audit team did not obtain sufficient, appropriate audit evidence to conclude that the accrued sales rebates balance at the year-end was free from material misstatement. The audit team's testing did not cover a material proportion of the rebate accrual, which was over 12 months old. The audit team did not corroborate, to independent evidence, the inputs used in management's computation of the rebate balance. The combination of substantive and controls testing performed did not provide sufficient audit evidence for the accrued rebates balance.
The group defers revenue based on a sales incentive scheme, with a deduction for certain assumptions.	The audit team did not perform sufficient audit procedures, or raise sufficient challenge, in relation to the completeness and accuracy of the calculation of deferred revenue.

Background	Issue
The group recognised a contract asset relating to a certain operation, which runs for a period of five to 10 years. The group receives both customer revenue and subsidy revenue for operating this contract. The valuation of the contract asset is highly sensitive to assumptions applied when estimating future customer revenue. The effect of the expiration of a subsidised unit price scheme at the end of the following year was a key assumption in the valuation of the contract asset. Management forecast that customer revenues would increase by 50% in two years, reflecting price increases following the end of the subsidised unit price scheme and no change in customer volumes.	The audit team performed inadequate audit procedures in relation to the forecast revenue supporting the valuation of the contract asset. In particular, the audit team did not sufficiently corroborate and challenge the extent to which future customer volumes and revenue could be adversely impacted by the subsidised unit price scheme ending, resulting in significant price increases for customers.

Revenue: good practice points

Risk assessment
• The audit team's analysis of contracts, in response to the significant risk identified, was sufficiently granular and precise to allow for the design and performance of tailored testing procedures. It incorporated multiple risk factors and demonstrated a detailed understanding of the entity and the operations of the overall business. • There were clearly articulated risk criteria that led to the identification of contracts where audit testing was targeted. The use of comprehensive template workpapers allowed the team to demonstrate a detailed knowledge and understanding of those contracts, including key operational features and KPIs. This granular assessment enabled the audit team to robustly evaluate the assumptions and data used in the financial models, which determined onerous contract provisions, resulting in misstatements being identified. • The audit team designed and performed extensive revenue procedures in response to potential fraud risks. This included challenging management on the business rationale for entering contracts with customers in countries with high-risk ratings and evaluating management's processes on how they had considered bribery and corruption risks. • For certain components where revenue was significant by size, the group audit team requested a summary from component audit teams of the key elements of revenue recognition, supported by a review of the contracts with customers, to help inform their risk assessment.

Contract accounting

- There was good evidence of detailed testing of the open contracts at year-end, including tracing key inputs to support evidence. For example, agreeing secured costs to signed contracts and discussions with commercial directors. The audit team also challenged management over their forecasting accuracy and corroborated unsecured costs.
- The audit team demonstrated a detailed knowledge and understanding of the group's commercial programmes and contracts. This knowledge enabled the audit team to target its testing of long-term contract revenue and margin. This included robustly evaluating the assumptions and data used in the financial models that determined revenue recognition, and checking to ensure consistency with the underlying contracts and specific contract terms.
- The audit team's assessment of a significant risk contract for a component was supported by extensive discussions with the customer, and with project and operational management. There was robust evidence of the audit team's evaluation and challenge of the contract accounting and consideration of possible management bias.

Data analytics and substantive analytic review

- The audit team performed a comprehensive analysis of the development of income from X for prior financial years to inform its expectation for the 202X. This work enabled the audit team to identify two misstatements, which it requested management to correct.
- The audit team performed a detailed data analytic procedure that built upon its revenue work. This procedure enhanced and supplemented the understanding the team had obtained of the rebate process and focused the audit procedures to review agreements and test accruals in an effective manner.
- The audit team used bespoke analytics to recalculate income to a sufficiently precise level. The standard three-way correlation analysis complemented the bespoke analytics to reduce the risk of residual misstatements and management override. In particular, the audit team performed extensive work reconciling items that exceeding testing thresholds and used in-house tools to corroborate its understanding of these items.
- The group's revenue is comprised of high-volume, low-value transactions. The audit team designed and performed data analytics to verify the completeness and accuracy of the revenue efficiently. The work performed over reconciling items was extensive in nature.
- The audit team performed a substantive analytical review on revenue that used data (volumes) from a third-party report. This was an effective, bespoke procedure to support the accuracy and completeness of revenue.
- The audit team analysed the commission rates of individual deals compared to the expected standard rates and investigated the outliers. This ensured the audit team's testing focused on those transactions that were not consistent with its expectations.
- To gain and test its understanding of the revenue process in the first year of audit, the group audit team performed an aggregated correlation review of revenue at all in-scope component entities. This procedure ensured that variances in different jurisdictions were understood and explained, in addition to the analysis performed by local component teams.

Third party and independent sources of data

- The audit team obtained details of the dividends announced for all investments from independent sources and verified they were accurately reflected within the recognised revenue.
- The audit team responded effectively to the risk of revenue overstatement, verifying total revenue to bank statements.
- The audit team designed and performed robust procedures to test revenue. These procedures included sending revenue and trade debtor confirmations to all key customers, covering over 99% of total revenue.
- The audit team requested management obtain the policy level breakdown and relevant supporting evidence from a material TPA. This was requested to support the testing of the completeness and accuracy of policies underwritten by the TPA. The audit team performed these procedures in addition to receiving the reports and reconciling these with underlying records.
- The audit team obtained, from its two key customers, written confirmations of the total amount of product purchased by them during the year. This provided additional evidence in relation to both the revenue recognised and the quantity data provided by the entity.

Bespoke procedures

- There was evidence of robust challenge of the methodology and key management assumptions used in the calculation of deferred revenue. This included consideration of diverse possible outcomes under an extensive range of plausible scenarios.
- The audit team's challenge of the deferred consideration resulted in a revision to management's original estimate. The work performed demonstrated a comprehensive understanding of the operations of the entity. By utilising evidence obtained in other areas of the audit, the audit team were able to challenge management's assumption of continuing to achieve historic results after the loss of a major customer and, therefore, the achievability of the EBITDA target included in the estimate.
- The audit team's technical analysis and critical assessment of management's approach to licence revenue was thorough. This included revisiting previous consultations with the firm's central technical team on the more complex aspects to support the continuing applicability of the judgements made.
- The audit team performed comprehensive testing over the cash to revenue reconciliation, with appropriate corroboration of reconciling items. This 'proof in total' test provided assurance over the completeness and accuracy of the high-volume, low-value revenue transactions in an efficient and effective way.
- In response to the entity being unable to provide a complete listing of premium transactions for the year, the audit team performed a series of alternative audit procedures to confirm the completeness of the revenue population and the accuracy of the entity's reported insurance revenue. This included consulting the firm's technical team on its sampling approach.

4. Valuation of assets and liabilities

Challenge the assumptions for unquoted investments

The valuation of unquoted investments is inherently subjective and may be susceptible to management bias or error. Auditors should challenge and corroborate the key judgements in management's valuation models.

Background	Issue
The audit team obtained the year-end net asset value statements prepared by X. For certain investments, the audit team also benchmarked the average EBITDA multiples of comparable companies to those used in the relevant valuation report to determine the premium or discount applied. In assessing the reasonableness of the premium or discount, the audit team determined an expected range of 0–30% based on the responsible individual's (RI's) judgement and experience auditing other similar entities.	The audit team did not obtain sufficient, appropriate audit evidence to conclude that the valuation of level 3 investments was free from material misstatement. In particular, insufficient procedures were performed to challenge the valuation of the co-investments as the audit team did not: • Assess the comparability of the benchmark data provided by management for a material investment. • Sufficiently challenge the specific level of discount or premium applied, including where X's management's valuation was within the expected range. • Justify the suitability and characteristics of the expected range given the anonymisation of comparable investments used.
As at year-end, the group held unquoted investments at fair value through profit and loss. The largest investment was in X. X was valued using an earnings multiple valuation technique. The actual earnings were adjusted to annualised expected earnings for new units opened called the 'run-rate adjustment'.	The audit team did not sufficiently evaluate, corroborate, or challenge certain assumptions used in the valuation models for unquoted investments. In addition, it did not perform adequate sensitivity analyses to determine whether reasonably possible changes to key valuation assumptions would be unlikely to materially change the valuation. For the valuation of X, the audit team did not sufficiently: • Corroborate and evaluate the data supporting the run-rate adjustment. • Challenge and assess with sufficient precision the reliability of the EBITDA for year-end.

Challenge pension assumptions

The existence and valuation of pension assets can be complex and subject to significant judgement and estimation. Auditors should obtain sufficient and appropriate evidence to support whether the pension scheme assets exist, and whether the valuation appropriately reflects the fair value of those assets.

Background	Issue
The Fund was a direct lending fund investing in unquoted loans to overseas entities. The asset was designated as harder-to-value by the audit team. The valuation of the fund used the net asset value (NAV) based on the audited financial statements. The audit team confirmed that the loans were valued at the lower of amortised cost and impaired value, rather than fair value.	The audit team performed inadequate procedures over the valuation of the Fund. Specifically, the audit team did not challenge the use of the NAV and how it represented the fair value of the Fund, particularly in the absence of fair valuation of the underlying loans, which were accounted for at amortised cost.

Recognition of capitalised costs

Determining the cost of internally generated development assets is judgemental and may be subject to management bias. Auditors should challenge the reasonableness of capitalising these costs and the key assumptions used by management, which support their carrying value.

Background	Issue
The audit team performed an assessment of the capitalisation criteria for all products in aggregate. The audit team primarily focused on inquiries with management to verify assumptions such as the capitalisation rate for a product. The audit team also relied on time allocation summaries prepared by development managers.	The audit team's challenge of a number of key judgements made by management regarding the capitalisation of development costs was inadequate, including the following: • Whether individual enhancements to products should be capitalised. • Whether any costs capitalised superseded existing development costs. • The capitalisation rate for the product. • The accuracy of the time allocation summaries provided by the development managers. In addition, the audit team did not accurately describe the procedures undertaken in this area in the auditor's report and the report to the Audit Committee.

Background	Issue
Management determined that a very high percentage of the total costs incurred as part of a revenue contract could be capitalised to intangibles considering the developed intellectual property would be used to deliver services for other revenue contracts in the future. The audit team confirmed the time allocated in management's project plan to development activities was at that percentage level of the total project time.	The audit team did not obtain sufficient audit evidence to conclude that the existence and valuation of capitalised internally generated labour development costs was free from material misstatement. The audit team did not sufficiently challenge or corroborate the key judgements made in capitalising costs generated from the contract.

Recoverability of deferred tax

Accounting Standards state that deferred tax assets shall be recognised for unused tax losses only to the extent that it is probable that such losses can be utilised against future taxable profits. Audit teams should robustly evaluate and challenge the appropriateness of management's forecasts.

Background	Issue
The group recorded a significant deferred tax asset (DTA) relating to the UK operations, which had been loss-making since FY2X. Management's 'base case' for the UK operations assumed significant year-on-year growth and forecast that historic tax losses would be fully utilised within 15 years. The assessment was highly sensitive to changes to key assumptions in the cash flow forecasts. If management's 'reasonable worst case' forecast had been applied, the tax recovery period would have been significantly extended.	The audit team did not obtain sufficient, appropriate audit evidence to support its conclusion over the recoverability of DTAs against future profits. In particular, the audit team did not perform sufficient procedures to evaluate and challenge whether the taxable profits in management's forecasts were probable and the appropriateness of the extended period over which tax losses were forecast to be recovered.

Background	Issue
The group recognised a net DTA of over £100 million at the year-end, of which a significant proportion related to non-trade and trade losses. The group had been making significant losses for four years. The group was originally forecast to first make an annual taxable profit in the year following the audit, but that was revised to three years' time. Budgeted EBITDA in the current year was missed due to operational timing issues and additional costs, partly due to supply chain disruption. The utilisation of the non-trade losses DTA was based on the expectation that the group would generate ongoing taxable profits from 203X.	The audit team obtained insufficient audit evidence to challenge the recoverability of the DTA against future profits. In particular, the audit team did not: • Obtain details of the forecast taxable profits over an eight-year period from 203X to support the utilisation of the non-trade losses DTA. • Perform sensitivity analysis on the volume forecasts to assess and challenge how a reasonable change in the forecasts could impact the trade losses DTA recognition.

Business combination accounting

Acquisition accounting often involves significant judgement and may be subject to management bias. Auditors should obtain sufficient, appropriate audit evidence to ensure the methodology and assumptions applied by management for acquisition accounting are reasonable.

Background	Issue
In the financial year, the group completed its purchase price allocation (PPA) for the prior year acquisition of X and recognised material adjustments to the fair values of assets acquired and related goodwill. The group accounted for the majority of its current year acquisitions on a provisional basis. No fair value adjustments were recognised in relation to the assets and liabilities acquired, pending completion of the acquisition purchase price allocations.	The audit team did not obtain sufficient, appropriate audit evidence to support management's accounting for business combinations. In particular: • The audit team did not perform sufficient procedures to evaluate and challenge the cash flow forecasts provided by management used in the X PPA. • The audit team did not adequately evaluate or challenge the appropriateness of management's approach to recording provisional amounts for items where the current year acquisition accounting was incomplete.

Background	Issue
In the acquisition of X, the first year of the EBITDA forecast used in estimating the fair value of the contingent consideration differed to that used in the acquired intangibles fair value model. In response to our queries, the audit team determined the book value of previously capitalised costs had been incorrectly added to the fair value of acquired intangible assets. We were informed by the audit team that management confirmed that the value of acquired assets was misstated as a result of the incorrect addition. Prior to the announcement of the proceeding years group's results, management performed a further review of intangible asset valuations resulting in balance sheet reclassification adjustments in the current year.	The audit team did not obtain sufficient audit evidence to support the fair value of the acquired assets. In particular, the audit team did not identify discrepancies that led to a balance sheet reclassification above materiality.

Share-based payments

Accounting for management bonus arrangements may be subject to manipulation and carries an increased risk of error. Auditors should ensure that appropriate procedures are performed.

Background	Issue
The group operated several long-term incentive plans that are equity settled. The charge for the year included new plan awards/bonuses and ongoing charges for awards from earlier years.	There was insufficient evidence to support the equity settled bonus accrual. In particular, the audit team did not evidence or agree: • The bonus calculation to the underlying bonus scheme and the Remuneration Committee minutes approving the award. • That the financial/personal performance conditions had been met or agreed to in supporting documentation. • The mathematical accuracy of the bonus calculation or whether the salaries used as a basis for this were consistent with other audit work on Directors' Remuneration.

Valuation of assets and liabilities: good practice points

Risk assessment

- The qualitative risk assessment was extensive and precise with respect to accounting for complex transactions, the valuation of financial derivatives and the risk of unauthorised trading activity. This resulted in the audit procedures performed being responsive to the specific risks identified in these areas.
- The audit team undertook a thorough assessment of the design and implementation of the key controls over the entity's holdings of private investments. It also performed extensive testing on a range of factors, such as credit ratings and spreads, to assist in their valuation.
- The assessment of the operating effectiveness of the cost meeting control was robust and well-evidenced. A large sample of meetings were attended, and the audit team evidenced its challenge, key considerations and conclusions clearly.

Use of specialists

- A panel, which included the firm's relevant partners and the Engagement Quality Review Partner, met on several occasions during the audit to assess and challenge the audit team's approach and conclusions. The panel discussions, which demonstrated a robust evaluation of the audit procedures, resulted in additional evidence being obtained and a consensus being reached on the final conclusions.
- The independent revaluation procedures performed by the firm's financial instrument experts, including the testing of models over a complex portfolio, were comprehensive. The quality of evidence to support the work of specialists demonstrated that they were part of a well-integrated audit team.
- The group completed the acquisition of the entire share capital of X during the period. The audit team, with the aid of internal specialists, robustly assessed the valuation of land and buildings. This work reflected the specific circumstances of abnormal land conditions, planning issues and demolition costs and resulted in a significant amendment to the valuation.
- The audit team instructed its valuation specialists to independently remodel the impact of a higher attrition rate used in a sample of valuations of acquired businesses. The procedure was performed to challenge management's assertion that differences identified in attrition rate expectations would not materially impact the valuation.
- The audit team identified properties with unusual fluctuations in valuation from its opening balance review. It included these properties in its testing and requested the internal specialist to conclude on the reasonableness of such movements; this also informed the current year valuation conclusions.
- Based on the advice of its internal actuarial expert, the audit team challenged management to obtain an external legal opinion to support the entity's unconditional right to surplus in two pension schemes.

Use of specialists

- The group audit team used tax specialists to assist in the complex areas of taxation. The specialists' work was comprehensive and included a detailed analysis of the impact of different tax matters on current and deferred tax. The group audit team also used the firm's specialist to assess discount rates in impairment assessment. There was clear evidence of the group audit team's discussions with and challenge of, the specialists' work.
- Management used a sector-wide model for the pension provision, which may be subject to extensive third-party scrutiny. The audit team and its experts performed extensive integrity, and logic checks on the model. This work identified an imprecision in the model, resulting in an audit adjustment.
- The audit team's analysis of the key assumptions relating to the defined benefit pension obligation was well-structured, clear and concise. For each assumption, the audit team outlined the requirements of the relevant accounting standard, management's determination of the point estimate, the auditor's expert's analysis and the core audit team's review and conclusion.
- The auditor's actuarial expert's report referred to their challenge of management's actuaries and application of judgement in specific areas. For example, the assumption used for the constructive obligation to provide pre-retirement increases in a particular scheme and the lack of specific allowance for Covid-19. Clear evidence of this enabled effective supervision of the actuarial work by the audit team.
- The firm's data analytics specialists assisted the audit team in obtaining and testing the completeness of data used in the substantive testing. This included reconciliations between primary trading systems and the general ledger. Furthermore, there was evidence of effective integration between the audit team and their data analytics specialists, including translation of complex IT code into plain English.
- The audit team, in addition to using an internal valuation specialist to independently obtain external prices, compared management's valuation of the quoted investments to the external custodian's report, which provided further secondary evidence over the fair value of quoted investments.
- There was appropriate involvement of specialists in relation to the valuation of unlisted investments. This enhanced the level of audit challenge around certain assumptions used (such as the discount rate).
- The audit team's use of internal valuation specialists was of a good standard. In particular, their involvement in the assessment of obsolescence rates in the valuation of acquired intangible assets and in the calculation of the discount rates used in the goodwill impairment assessment.
- There was effective involvement of the firm's pensions experts in assessing the key assumptions used in the valuation of the defined benefit pension obligation. This included performing a detailed benchmarking analysis across a number of entities to challenge the appropriateness of management's assumptions.

Challenge of management

- The audit team's procedures for the various categories of investments were comprehensive in nature. There was clear evidence of challenge and scepticism being applied, with a thorough assessment of assumptions and key inputs. The audit team's report to the Audit Committee also included details of challenges raised on individual samples of investments in spinouts.
- The audit team's extensive procedures over natural resource reserves included an element of unpredictability, resulting in the testing of certain territories that would not otherwise have been covered (due to movements during the period being below the testing threshold).
- For the new projects sampled, the audit team made inquiries with the project owners in addition to inspecting supporting evidence to better understand the nature of the projects. This demonstrated increased scrutiny in response to the identified risk of fraud.
- The audit team performed a range of procedures to challenge the valuation of the entity's deferred acquisition costs. These included substantive testing, sensitivity analyses and an assessment of the reasonableness of the amount the entity deferred on the basis of expected policy renewals.
- There was evidence of robust challenge of management's property valuation model, including independently identifying underperforming properties to challenge management's forecast assumptions.
- The models that supported the valuation of assets were subjected to robust evaluation and challenge by the audit team. Particular attention was paid to possible management bias through, for example, the model inputs, assumptions and related judgements.
- There was a well-executed integrated approach to the audit of deferred tax, involving members of the group audit team, component audit teams and tax specialists. This included detailed and timely audit partner involvement, meetings with management to understand the forward-looking assumptions, and extensive evaluation and challenge of those assumptions. The relevant component audit teams also verified the consistency of the long-term profit forecasts used in the deferred tax calculations with the information audited in other areas.
- The audit team's procedures in relation to the valuation of the deferred tax assets were thorough and clearly evidenced. There was robust challenge, which resulted in changes to management's model and the final recognised asset.
- The audit team performed a thorough assessment of the frequency of trading of the entire portfolio of investments throughout the year. This was performed to ensure appropriate classification and disclosure within the fair value hierarchy and demonstrated the application of professional scepticism.

Reporting

- The audit team's reporting to the Audit Committee included an evaluation of management's discount rates for each asset class using a 'heatmap' to set out where each rate fell in a range of 'conservative' to 'optimistic'. This visualisation presented the full population of discount rates in an easily understandable format that would clearly highlight any significant trend.

5. Inventory

Inventory cost

Auditors should perform sufficient and appropriate audit procedures over the cost of inventory to assess whether the period-end balances are materially correct.

Background	Issue
To test the accuracy of the cost of inventory, the audit team selected a sample of stock lines and compared the costs per unit – using the latest supplier invoice where available – to the weighted average cost per the system. Differences were identified for most of the items tested, some of which were large.	The audit team did not perform sufficient procedures to obtain adequate assurance over the accuracy of the weighted average cost of inventory. In particular, the audit team did not: • Adequately evaluate or follow up the differences identified in the sample tested. • Set a threshold to evaluate the differences. • Sufficiently review the audit procedures performed.
Inventory included an adjustment to capitalise purchase price variances (PPV). For finished goods, the audit team tested the standard cost for a sample of items, as well as overhead absorption for the components where it was material. The cost of inventories, recognised in cost of sales as an expense in the notes to the financial statements, was significantly lower than the total cost of sales. The difference predominantly related to direct labour and energy costs. The audit team's testing of raw material inventory identified a number of differences between the audit team's calculation of the expected PPV, using the year-end standard cost, and the actual PPV expensed to the P&L as at the purchase date. These were not all evaluated for the purpose of the capitalised PPV testing.	The audit team did not perform sufficient procedures over the cost of inventory. In particular, it did not adequately: • Assess whether the standard cost of finished goods materially represented actual costs, for example, evaluate for finished goods whether direct labour and energy costs were appropriately absorbed into year-end inventory and evaluate the appropriateness of the year-end PPV adjustment. • Evaluate all the differences identified in the raw material inventory testing for the purpose of the capitalised PPV testing.

Background	Issue
The audit team identified a fraud risk in respect of manipulation of inventory system data. The response to this risk included reconciling opening and closing inventory quantities to movement reports and verifying a sample of individual movements to supporting evidence. An elevated risk was identified over the accuracy of inventory costing. The team's response included agreeing purchase costs to invoices and recalculating the application of the first-in first-out (FIFO) approach. The audit team identified variances across several sampled items.	The audit team did not obtain sufficient, appropriate audit evidence to conclude that the inventory balance was free from material misstatement. In particular, the audit team did not: • Perform sufficient procedures to address the identified fraud risk over manipulation of the inventory system data. • Appropriately test the other inventory movements or adjustments. • Evidence any testing of the freight and import duty costs allocated to inventory. • Test the application of the FIFO policy sufficiently. • Sufficiently evaluate or corroborate the variances identified.

Inventory existence

Inventory is significant to the group's balance sheet. Auditors should perform sufficient procedures to obtain evidence in relation to inventory counts to verify that the year-end balance is not materially misstated.

Background	Issue
Management's internal control for verifying the existence of inventory at the group's two main warehouses was to perform weekly cycle counts and investigate any net differences that exceeded 1% of the total stock quantity counted on that date. The audit team identified certain stock variances, which on a gross basis were significantly higher than 1%. Furthermore, for the counts closer to the year-end date, certain variances were not followed up by audit team.	The audit team did not adequately test the design, implementation and operating effectiveness of the inventory count controls and, therefore, did not obtain sufficient evidence to conclude that inventory existence was free from material misstatement. The audit team's evaluation of the differences identified during the perpetual inventory counting was insufficient to conclude that the control was designed to an appropriate precision level and was operating effectively.

Background	Issue
For retail stores, the audit team tested the operating effectiveness of management's annual count controls. These counts were performed on a rolling basis, with some stores subject to this control in the first week of the financial year and not again for the remainder of the year. To evaluate the total inventory cost, the audit team performed substantive procedures that included tracing a sample of inventory costs to the latest invoice. Variances were identified within this procedure that were not appropriately followed up by the audit team.	The audit team did not obtain sufficient, appropriate audit evidence to conclude that the existence and valuation of inventory was free from material misstatement. In particular, the audit team did not: • Evaluate the operating effectiveness of sufficient inventory count controls to place reliance on controls over the existence of inventory. • Perform procedures to corroborate the variances identified within the inventory cost testing, nor evaluate their impact on total inventory. • Perform sufficient testing over the accuracy of the inventory provision calculation.

Inventory valuation

Auditors should perform sufficient procedures in relation to inventory valuation and undertake sufficient review procedures to ensure appropriate audit evidence has been obtained.

Background	Issue
To audit the accuracy of the cost of inventory, the audit team tested a sample of stock lines. For the X testing, nearly half of the samples were incorrectly selected as they had nil values. There were also variances on some individual samples, which exceeded the audit team's threshold so were not tested. The Y testing workpaper had a formula error and therefore the relevant variances were incorrectly calculated.	There was insufficient audit evidence obtained for the valuation of inventory, in particular from the inventory cost testing. This was not detected by the review of the relevant audit working papers undertaken.

Background	Issue
After year-end, the group recognised a significant loss from the disposal of a division. The loss was generated from the write-off of the division's net assets, the majority of which was inventory. The recoverability of the inventory at year-end was tested by vouching the latest sales invoices for selected items (based on a moderate risk level) to ensure they were sold at a profit and by performing a high-level comparison of the inventory provision to the prior year.	The audit team did not sufficiently assess the impairment risks arising from the sale of the business and, consequently, did not design and execute an appropriate audit response to address the risks over the valuation and recoverability of inventory. Specifically, it did not obtain appropriate audit evidence over the recoverability of inventory, including the identification and analysis of slow-moving and aged balances in inventory.
Management's valuation model for its stock included production information sourced from a report, which was prepared and assessed by management's experts. Members of the audit team attended management's year-end survey of the stock.	The audit team did not perform adequate audit procedures over the stock inventory valuation. In particular, it did not adequately understand and evaluate the work of management's experts (in relation to their report) and did not perform all of the audit procedures set out in the inventory instructions for the year-end survey of the stock.
The group held material non-current stock. Management prepared a net realisable value (NRV) assessment to support the carrying value of the inventory. No discounting was included in the assessment to account for the expected timing of the processing. The audit team prepared an analysis of NRV on an individual stock basis. The audit team's analysis identified certain long-term stock, which showed an NRV below recoverable amount. The NRV assessment was very sensitive to changes in each of the key assumptions, particularly the impact of discounting.	The audit team did not perform adequate procedures to assess and challenge the assumptions in management's NRV assessment for long-term stock. In particular, the audit team did not: • Perform any evaluation of why discounting for the long-term effects of realising inventories would not have had a material impact on the valuation. • Assess and challenge the impact of changes in the key assumptions in the NRV model at an individual stock level.

Inventory: good practice points

Inventory cost

- The audit team effectively addressed the risk of incorrect application of the first-in, first-out inventory costing method by manually recalculating the closing balances of all selected inventories and testing the underlying data.

Inventory existence

- The audit team's approach to testing the existence of inventory was robust and reflected the significant amount of inventory held across its large unit network and a number of warehouses. A significant number of sites were attended and a larger sample size used for inventory counts.
- The audit team's approach to testing the existence of inventory was robust and reflected certain increased risks arising. Senior members of the audit team, including the engagement partner, attended the year-end inventory counts at key locations.
- As part of the stock count procedures, the audit team members were provided with a detailed and comprehensive set of instructions. This included an overview of management's stock count process, nature of the expected stock, physical access rights and additional procedures to perform in case of a stock count variance. This enhanced the effectiveness of the procedures performed by the audit team across all the count locations throughout the financial period.

Inventory valuation

- The use of the engagement team's data analytics tool over the inventory transactions and balances provided substantial coverage over calculations performed by management including standard to actual costing, inventory aging and net realisable value. This ensured the audit team's testing in these areas focused on those items that were not consistent with its expectations.

6. Quality management

Background	Issue
Effective quality reviews should be performed to enable the audit team to conclude that it has performed an appropriate level of audit work to support its conclusions. An Engagement Quality Reviewer (EQR) should provide an objective assessment and challenge of the work performed and conclusions reached for audit areas with significant risks.	On six inspections, the separate firm audit teams did not perform sufficient quality control challenge and rigour in relation to the significant risk areas of those audits.
A clear and detailed quality review should be performed to enable the audit team to conclude that they have performed appropriate audit work to support their conclusions. The audit team should clearly evidence the audit procedures performed, the key judgements made, and conclusions reached.	The audit team's review procedures, including the audit partner and EQR, failed to identify the significant risk X and Y issues and did not provide sufficient challenge over several other risk areas.
Auditing Standards require firms to establish policies and procedures for the timely completion of the assembly of audit files that must be completed within 60 days of signing their auditor's report. Archiving the audit file is important to ensure the integrity of the record of the audit work performed and audit evidence obtained.	The overseas component file was not archived on a timely basis alongside the group audit file, and the overseas component file assembly process was not completed within the 60-day period required by Auditing Standards.
The archived audit files contained several deficiencies relating to file assembly, omitted working papers and the archiving process. These included working papers being amended after the date the auditor's report was signed, with no record of the specific reasons for this (and when and by whom they were amended and reviewed).	The firm's quality control and review procedures were ineffective on this engagement. In particular, reviews by the audit partner and EQR failed to identify the significant issues identified in our inspection, including instances where additional audit procedures should have been performed. In addition: • There were numerous instances of working papers being omitted from – and incomplete working papers being retained within – the archived version of the audit file. • The audit team did not retain evidence of the changes made to certain working papers after the date of signing its auditor's report.

Quality management: good practice points

Engagement quality review

- The Engagement Quality Review provided strong challenge over the significant risk areas, which clearly enhanced the quality of the audit. The audit team responded to the challenge by performing additional testing procedures and corroboration.

7. Financial services excluding expected credit losses

Banking payments process

The payments process is a core area for a banking and financial services audit. The audit team should therefore understand the process and perform sufficient testing over it.

Background	Issue
The settlement/clearing area and the resulting reconciliations represent a core area for a banking audit. The audit team should, therefore, sufficiently understand the process and, where necessary, appropriately engage IT specialists to assess the adequacy and operating effectiveness of matching rules and IT-dependent manual controls, as well as perform sufficient substantive procedures.	On two inspections, the separate firm audit teams did not perform adequate procedures to test the cash, settlement and payments process and consequently failed to obtain sufficient, appropriate evidence that the relevant balances were free from material misstatement.
The main banking activities (deposits, withdrawals, anti-money laundering checks, interest computation etc.) of the group were fully managed by a service organisation. A third-party assurance report for the service organisation noted that certain control objectives, including those related to IT and payment processes, could only be achieved if complementary user entity controls (CUECs) were suitably designed and operating effectively at the group, alongside related controls at the service organisation.	The audit team did not adequately assess and respond to matters within the third-party service organisation assurance report. Specifically, it did not perform any procedures to assess, identify and test relevant CUECs.

Financial services excluding ECL: good practice points

Risk assessment
- For key judgemental areas, the audit team performed detailed risk assessments, analysing each underlying assumption. This resulted in a clear and well-justified identification of significant and higher risk assumptions. The audit team used underwriting solvency capital requirements to provide an indication of the significance of each assumption used in the valuation of actuarial liabilities and communicated these sensitivities to the Audit Committee. - The audit team's understanding of the loan book enabled it to identify the risks associated with the recognition of interest and associated provision for loan losses at an appropriately disaggregated level. This resulted in focused testing of those areas subject to significant management estimation.

Use of specialists

- The actuarial specialists involved in the audit performed independent re-projections of the majority of the incurred, but not reported, reserve. They also reviewed the methodology and assumptions and undertook a movements analysis. These procedures enhanced the audit team's challenge of the entity's gross claims reserves.
- The actuarial specialists demonstrated a depth of understanding of the business, performing a range of procedures to assess the reasonableness of different elements of the technical provisions. These included independent projections for a significant proportion of the portfolio, a methodology and assumptions review, benchmarking and diagnostics checks. These procedures enabled the actuaries to demonstrate appropriate challenge of the managing agent's assumptions.
- The audit team engaged an external actuarial expert to assist with the audit of the valuation of long-term business provisions and carried out a thorough assessment of the sufficiency of the expert's report. It also prepared its own Analysis of Movement to ensure it had a proper understanding of the reasons for the key movements and that they were sufficiently addressed by the actuarial expert.
- The audit team engaged actuarial specialists to perform procedures to assess the reasonableness of the valuation of the group's insurance contracts provisions. These procedures included an independent reprojection of certain injury claims, which provided both a point estimate of the claims and an estimate of the variability surrounding that point estimate. The work here encompassed uncertainties within the data in the past without the need to have explicit scenarios for scenario testing addressing the heightened risk identified in this area.
- The actuarial specialists' procedures were comprehensive and included independent projections for a high proportion of the entity's insurance liabilities, as well as a methodology and assumptions review. This resulted in two levels of review and challenge. The independent projections included specific consideration of the impacts of inflation and an estimation of claim amounts. The actuarial specialists' work included a range analysis, which was further enhanced by consideration of alternative inflation scenarios.
- The firm's actuarial specialists provided comprehensive evidence of their consideration and challenge of the entity's key judgements and the risk of management bias. This included careful consideration of the firm's Insurance Benchmarking Survey in the assessment of the entity's key assumptions.
- The actuarial specialists placed no reliance on the previous auditors' evidence relating to the entity's models and baselined (or tested management's own baselining) all models. They assessed the entity's methodology on a line-by-line basis against the requirements of the Accounting Standards. There was comprehensive evidence of their consideration and challenge of the entity's key judgements, including the risk of management bias.

Insurance – challenge of management

- The actuarial team performed a range of procedures, with comprehensive evidence of its consideration and challenge of the entity's key judgements. This included a replication of the entity's experience study results applied to the base mortality assumptions, as well as detailed testing over inputs to the illiquidity premium calculation.
- In addition to independent projections, the actuarial specialists undertook a methodology and assumptions review, movements analysis and diagnostics checks to challenge the entity's technical provisions. The specialists also used two different inflation measures to challenge the appropriateness of the entity's assumptions.
- The audit team, including the actuarial specialists, performed a range of procedures to assess the valuation of claims outstanding. This included challenging management's methodology and assumptions and developing a range of projections (despite the data limitations for an entity in its first year of underwriting). Furthermore, there was explicit consideration for the entity of uncertainties, including emerging risks.
- The engagement partner drew up an extensive audit completion summary. This demonstrated their stand-back assessment of the assessed audit risks, including the transition to IFRS 17, and the range of procedures carried out to obtain sufficient appropriate audit evidence. It also demonstrated the depth of the engagement partner's understanding of the entity and its environment.
- The audit team provided comprehensive evidence of its challenge of the valuation of the entity's insurance contract liabilities. This included a granular assessment of the entity's base mortality and mortality improvement assumptions, as well as extensive testing to assess the entity's inflation model and related assumptions. Its testing demonstrated a deep understanding of the entity's business and modelling.
- The audit team, including the actuarial specialists, performed a range of procedures to assess the valuation of claims outstanding. This included independent projections over all classes of business. The use of diagnostics within the projection work brought further depth and breadth to this approach. In addition to the independent projections, the audit team's procedures included a methodology and assumptions review, and consideration of inflation assumptions.
- The audit team, including the actuarial specialists, provided comprehensive evidence of its evaluation of the risk of management bias in the valuation of insurance contract assets. This included procedures to challenge the entity's mortality improvement assumptions and the appropriateness of its expense allocations. The audit team also challenged whether the results of an overseas study on the mortality differentials for different categories of policyholder were appropriate to apply in the UK.
- The actuarial specialists and core audit team carried out careful scoping, which enabled their procedures to focus on the higher-risk classes of business. In addition, their procedures on the IFRS 17 Risk Adjustment challenged local management oversight and evaluated its reasonableness by reference to group and local considerations, external comparators and the prior year.

Insurance – challenge of management

- The audit team performed a variety of procedures to assess the reasonableness of the valuation of the group's insurance liabilities and engaged actuarial specialists to perform specific procedures on classes of business assessed as higher risk. The actuaries performed additional procedures on the group's claims handling costs and assessed the potential impact of claims inflation on the group's future claims cash flows, reflecting uncertainty at the time of the audit.
- The audit team included comprehensive material to evidence its procedures in connection with the entity's actuarial data, key actuarial assumptions and the modelling of its insurance liabilities. In addition, the benchmarking of the entity's margins for adverse deviation was thorough and insightful.
- The audit team recorded clear evidence of its valuation challenges and the basis on which issues were resolved. For the entity's mortgage portfolio, the audit team evidenced thorough consideration of the methodology and assumptions and baselined the relevant models.
- The audit team robustly challenged management's key assumptions used in the calculation of claims due from insurance companies and self-insuring organisations. This included developing its own model to corroborate management's outcomes, in what was a complex process.
- The audit team challenged the entity's accounting policy for the recognition of income. As a result of this challenge, the entity's financial statements included a prior period restatement that was marginally greater than audit materiality.

Use of data analytics for insurance liabilities

- The audit team supplemented its testing of the completeness and accuracy of data by using analytic tools to identify movements from previous periods and testing these movements on a sample basis. This additional testing incorporated an understanding of the business and the underlying products owned or underwritten. In particular, the audit team analysed data changes for in-force policies (for data related to technical provisions) and movements in loans and personal details (for data related to equity release mortgages).

IFRS 17

- The audit team's work on the adoption of IFRS 17, including on the opening balance sheet and prior year comparatives, was thorough and demonstrated its challenge of management's key transition judgements. In addition, the audit team issued a special transition report to the Audit Committee, which set out the range of procedures it performed.
- The audit team engaged extensively with other group and audit firms in the UK and overseas to support its conclusions on the IAS 8 disclosures relating to the adoption of IFRS 17 Insurance Contracts.
- The audit team performed extensive procedures on the implementation of IFRS 17, the opening balance sheet, prior year comparatives and challenged management's key transition judgements. It also undertook thorough testing to confirm the completeness and accuracy of data and the dataflows for the purposes of the valuation of the entity's insurance contract liabilities.

8. Planning and risk assessment

Risk assessment process

Auditors are required to identify and assess the risks of material misstatement at both the financial statement and assertion level. This should include a clear rationale of how the auditor has concluded on the significance of such risks and the impact on their audit approach.

Background	Issue
The audit team performed its risk assessment at both the financial statement level and for individual financial statement line items.	The audit team did not perform sufficient and appropriate risk assessment procedures. The risk assessment conclusions, including the risk of fraud, were not supported by robust qualitative and quantitative assessments.

Ethics and independence

Auditor independence is key to ensuring confidence in the auditor's report on the financial statements. Auditors need to assess independence threats and safeguards in accordance with the Ethical Standard.

Background	Issue
The firm engaged X from Y Limited as an external regulatory expert to provide certain services on audit engagements, including on this entity. During the year, X was appointed as a non-executive director of the entity. To respond to potential threats to independence, X was removed as the regulatory expert by the audit team and their work was reperformed by another independent consultant. They continued to provide similar services for other audits at the firm. The audit team should have assessed at the time of the audit whether X should be identified as staff, as defined by the FRC Ethical Standard. This states that a member of staff shall not accept appointment to a role as a member of the board of directors of an audited entity.	The audit team did not adequately assess or respond to the threats to independence resulting from X joining the entity's board of directors. In particular, the audit team did not adequately consider whether X met the definition of staff, and therefore whether them joining the entity's board of directors could have resulted in a breach of the FRC Ethical Standard.
The group was newly listed on the London Stock Exchange, and the audit was subject to the requirements of the FRC Ethical Standard 2019.	The engagement partner's involvement in the audit of the entity was in breach of the Ethical Standard. This should have resulted in the partner rotating off as the Senior Statutory Auditor for the audit.

Planning and risk assessment: good practice points

Risk assessment

- The audit team's approach to risk assessment allowed for a bespoke targeted response to the testing of individual assets. The disaggregated understanding of expected cash flows led to clear communication with management over specific asset risks and concise reporting to the Audit Committee.
- The audit team responded appropriately to the group's evolving circumstances, which included inflation shocks, profit warnings and a change in senior management. The audit team responded by increasing the internal risk rating and the scope of the audit, reducing materiality levels and the reliance on controls, and engaging fraud and regulatory specialists. In addition, the engagement partner delayed signing the auditor's report to enable the required level of work to be completed. Taken together, these steps demonstrated an appropriate response to the heightened audit risk.
- Internal audit findings were considered in detail by the audit team as part of its risk assessment. This resulted in a more targeted audit plan for the nature and extent of substantive procedures and desktop reviews for out-of-scope components.
- The previous auditors allowed the audit team significant time to review their files. Following this, the audit team identified nine significant risks relating to the audit of the group financial statements and, for each one, it drew up an 'audit approach paper'. These papers summarised the audit team's planned procedures and formed the basis of its response to the significant risks identified.
- The audit team used the output of an exercise in which fraud cases and compliance cases were considered to assist in its risk assessment process. This analysis provided insight into both the compliance risk for each entity and the Corruption Perceptions Index score of entities operating in certain countries. This assisted in identifying high-risk entities during the scoping exercise.
- The group audit team performed a comprehensive stand back assessment over the identified IT control privileged access issues, including a thorough analysis of the impact on the overall risk assessment and the audit approach.
- The audit team performed a clear impact assessment over the errors and adjustments identified on lease accounting from the prior year audit. The assessment clearly considered the impact these items might have on the current year audit approach, including where recurring audit differences might arise; this demonstrated appropriate professional scepticism.
- The audit team clearly set out the procedures it performed to understand and assess the varying level of risks across the audit, how the changes in the revised ISA 315 had been complied with and the conclusions it reached through this process.
- Two audit teams involved the firm's specialists in climate workshops with management to inform the design of audit procedures to address climate related risks. The use of in-house tools, with the help of the specialists, led to an independent climate risk assessment being undertaken, including identification of assets with specific climate change risks.

Risk assessment

- The audit team performed a robust risk assessment of the impact of climate change for both accounting purposes and financial statement disclosures. This included:
 - Issuing detailed instructions over climate risk considerations to component audit teams.
 - Involving a sustainability specialist for the assessment of climate risks throughout the group and evaluation of impairment triggers arising relating to CO2 emissions.
 - Performing a detailed evaluation of the internal controls for the identification and monitoring of climate risks.
- When determining the make-up of the audit team, it was decided to include a second audit partner specialising in the valuation of properties held. This allowed for a greater degree of focus at partner level on the key audit matters and demonstrated a robust approach to the complexities of a large audit.

Fraud

- The audit team involved its forensic specialists as part of its fraud risk assessment at the planning stage, which provided deeper insight on potential fraud risk factors and enhanced the audit approach over the areas impacted by the risks identified.
- The audit team held a separate discussion at planning stage focused on fraud risks. The discussion was clearly evidenced on the file and covered a very broad range of matters at a granular level, and the attendees demonstrated a high-level of professional scepticism.
- The audit team engaged a fraud specialist to assist with the fraud risk assessment at the planning stage. For the fraud risks identified by the specialist, the audit team evidenced its assessment of the potential impact for the entity and how the audit plan addressed them.

Ethics and independence

- During the audit, the audit team consulted promptly with the firm's ethics function when a perceived independence threat arose. The agreed responses and actions were clearly communicated to the Audit Committee.
- The audit team identified a matter relating to the potential lack of independence of the predecessor auditor. To address this risk, the audit team delayed signing the audit opinion to allow for further audit procedures to be performed over the opening balance sheet.
- The audit team involved bribery and corruption specialists as part of its risk assessment procedures. This provided additional insights into the potential risk factors and supported the audit team's planning process and audit strategy for those areas impacted by laws and regulations.
- The audit work in response to the risk of bribery and corruption was performed to a good standard. This included:
 - Performing a comprehensive risk assessment for bribery and corruption risks across the group, considering the subsidiaries' inherent risk from geographical locations and nature of operations.
 - Involving a forensic specialist, which enhanced the audit procedures performed that responded to the specific risks identified.

9. IT testing

Where an audit approach relies on IT systems, data and associated controls, it is important that related General IT Controls (GITCs) are tested to an appropriate level to support this reliance. Inadequate testing and assessment of these GITCs increases the risk that inappropriate changes made to IT systems are not identified, including the integrity of data and functioning of automated controls.

Background	Issue
X's ABC system infrastructure, including the underlying database, is hosted and managed externally by a third-party, Y. The audit team obtained and reviewed Y's third-party Service Organisation Controls (SOC) report, which covered the first three months of the audit period. The audit team did not place reliance on the SOC report and assessed the report for risk assessment purposes only. We were informed by the audit team that the SOC report indicated that controls were in place to ensure Y and X IT users are unable to bypass segregation of duty controls over change management.	The audit team did not justify how it could obtain sufficient assurance from the procedures performed without relying on the SOC report, nor perform sufficient procedures to confirm that segregation of duty controls over ABC change management were operating effectively for the entire audit period.
Where audit risks are identified as a result of IT control deficiencies, the audit team should ensure these are appropriately mitigated by compensating controls or perform additional substantive procedures to address these risks. In the prior year audit, the audit team identified that certain administrators had access to both the development and production environments in the two systems. During the audit, management implemented a new tool, which the audit team concluded satisfactorily remediated the historic privileged user access issues identified.	The audit team and IT specialists did not adequately consider or respond to issues of privileged user access. In particular the IT audit team did not perform sufficient procedures to test that segregation of duties conflicts had been satisfactorily resolved, and that management's new tool appropriately mitigated the historic issues.

Background	Issue
The audit team engaged IT specialists (the 'IT audit team') to test GITCs for three IT systems managed and hosted in the UK. This testing identified certain roles with privileged user access. The IT audit team did not perform any procedures to identify which roles grant deployer and developer access for these systems. The IT audit team confirmed that management were unable to obtain the listing of one IT system database of privileged access accounts. The audit team concluded that this database of privileged access accounts could therefore not be tested.	The audit team, including the IT audit team, performed insufficient procedures to conclude on the appropriateness of segregation of duties and privileged user access within key IT systems. Furthermore, the audit team did not sufficiently demonstrate how any risks arising from the results of these procedures were considered and addressed through its audit approach.

IT testing: good practice points

Planning/use of specialists
• The audit team ensured the planned and executed audit procedures relating to the IT system were appropriate by comparing them against internal inspection findings on a comparable audit. • As part of the audit team's risk assessment, it performed a thorough assessment of the prior year GIRC deficiencies and their impact on the audit approach. The related risks, including the risk of fraud for individual financial statement line items, were reassessed following the current year GIRC testing. • The audit team's approach to GIRC testing was supported by a thorough and well-evidenced understanding of the entity's IT processes and controls. This included a comprehensive assessment of the homogeneity of these controls across in-scope IT applications. • The procedures performed by the IT specialists to assess the completeness of IT systems (and related user accounts) covered by the entity's privileged access management and activity monitoring tools, were thorough and well evidenced. The testing was complex and spanned multiple working papers. However, the various procedures were clearly linked together to demonstrate the IT specialists' understanding of the entity's IT environment and controls and support their conclusions. • Specialists were well integrated into the audit team. This was particularly evident in the case of the IT specialists, who were closely involved in the audit planning, and whose workpapers were retained on the audit file and reviewed by the core audit team. This approach improved knowledge sharing between the specialists and the core audit team. • The evidence of the audit procedures conducted around the data migration was clear, detailed and responsive to the specific risks presented by the approach to migration undertaken by the entity.

10. Group audit oversight

Oversight

The group auditor is responsible for the direction, supervision and performance of the group audit, including work at a component level. The group auditor should design an appropriate audit strategy and approach for components, and review and evaluate the appropriateness of the work performed, audit evidence obtained and conclusions reached by component auditors.

Background	Issue
The overseas component was identified as a significant component that required a full-scope audit. The group auditor's approach for this component was to issue agreed-upon procedures to the overseas component auditor. The group auditor took responsibility for the full-scope audit of the overseas component.	The audit strategy and approach to the overseas component audit contained several deficiencies, and the group auditor was not sufficiently involved in the work of the overseas component auditor. Overall, given the deficiencies in the overseas component audit, the group auditor failed to obtain sufficient, appropriate audit evidence over this financially significant component of the group.
The audit team placed reliance on work performed by the joint auditors of the parent entity (the 'group joint auditors') in respect of ECL and other centralised processes including GITCs. Several of the required group reporting deliverables were not obtained, and there was limited evidence of the group audit team's oversight of aspects of the work performed by the group joint auditors.	The audit team did not adequately direct, supervise and evaluate the work performed by the group joint auditors, which supported the audit of GITCs and ECL.

Group audit oversight: good practice points

Scoping and risk assessment

- The group audit team issued comprehensive group audit instructions, including minimum audit procedures for each component auditor. It held an extensive planning workshop with all in-scope component auditors and made site visits to component management and audit teams. The group audit team also performed detailed reviews of component auditors' work and reperformed certain controls and substantive testing for significant risk areas.
- The group engagement team identified the differences between UK and international versions of the auditing and ethical standards and incorporated these into the group instructions. It performed specific component oversight procedures to ensure the component teams had performed adequate procedures over the resulting differences.
- Certain aspects of the group audit were particularly well-planned and executed. This included:
 - Template revenue workpapers designed by the group team for use at the component level.
 - A stand-back assessment of the consolidation journal entries, focused on the aggregate impact by individual financial statement line item.
- The group planning and risk assessment procedures were thorough. For example, the group audit team held detailed planning workshops for component auditors and involved the group Audit Committee Chair. The workshops covered the use of audit technology, the business environment and key risks faced by the group. The sessions helped the wider audit team to broaden their knowledge of the group's strategy and to consider its impact on the audit.

Oversight

- The evidence of the group audit team's involvement in, and oversight of, the work of component auditors was of a high standard. In particular, the group team:
 - Performed a high-level of engagement throughout the audit process, with frequent calls and meetings with component teams.
 - Prepared detailed evidence covering the review of component auditors' working papers and the group audit team's site visits.
- The audit team held both virtual and in-person audit planning workshops for component auditors, with the Audit Committee Chair and a senior finance executive. The workshops covered the use of audit technology, the business environment and what challenges the company faced. The sessions helped the wider audit team to broaden their knowledge of the group's strategy and to consider its impact on the audit.
- The audit team's oversight of, and involvement with, component auditors was of a high standard. This included a comprehensive scoping assessment, high-quality reporting from component teams and extensive evidence of the audit team's interactions and discussions with component teams throughout the audit.

Oversight

- In response to challenges raised externally regarding the quality of audit work performed by the non-network component audit firm, the audit team designed and executed enhanced oversight and review procedures where reliance was placed on the component auditor's work.
- The group audit team provided their risk assessment results to the component audit teams. This included considerable detail at a financial statement line-item level and contained clear explanations for the inherent risk factor assessments. Component audit teams were asked to provide explanations in cases where their risk assessment differed.
- The audit team issued supplemental appendices to their group audit instructions to the component auditor of a newly acquired group, which included minimum and suggested audit procedures to be performed. This detailed up-front planning, coupled with effective supervision and review, mitigating the risk of insufficient work being performed by the component auditor.
- The level of reporting over the significant risk areas received from the component audit teams, was comprehensive and the group audit team's assessment of this work was well-evidenced. There were detailed notes and minutes by senior members of the audit team on what they reviewed, what they challenged (including specialists of the component audits) and who they met from management and component audit teams. The EQR also visited the overseas component audit team in person during the finalisation to review and evidence his challenge of that team.
- The staged approach to reviewing the component auditor's workpapers allowed the group audit team time to evaluate and respond to matters arising on a timely basis. This enabled the group audit team to identify that the component auditor had wrongly evaluated a non-audit service and ensured that this non-audit service was ceased in the timeframe permitted by the Revised Ethical Standard 2019.
- The audit team performed extensive oversight procedures in respect of the work performed by the component audit team. These were well-executed throughout the audit and clearly evidenced on the file.
- The group audit team performed an extensive review of the working papers for the overseas component and required the component audit team to provide more detailed reporting in response to travel restrictions at the time.
- The group audit team issued clear instructions to component audit teams and interacted with them throughout the audit, including through site visits. They also compared on a granular level the group risk assessment with those at component level to identify, assess and evaluate any significant differences.
- The group audit team demonstrated effective oversight and challenge of the component auditors. A detailed tracking document was prepared to evidence issues raised with the component audit team arising from its review of the working papers, the responses received and how matters had been resolved.
- There was extensive review of certain component audit work by the group audit team. In particular, there was a stand-back analysis of inventory balances by overseas components to ensure any unusual movements had been evaluated by the relevant component auditor.

Oversight

- The audit team's oversight of, and involvement with, component auditors included robust challenge of both local management and the component audit teams during in person visits by senior group audit team members to both overseas locations.
- The group audit team evidenced its involvement and oversight of the work of component auditors through a detailed working paper that analysed the responses within the component audit teams' reporting and the potential impact on the group audit.
- The audit team's oversight of, and involvement with, the component auditors included a comprehensive scoping assessment; high quality reporting from the component team; and engaging a London-based specific foreign language speaker to perform and evidence an extensive review of the working papers that covered significant risks and other areas of audit focus.
- The group audit team demonstrated effective integration and direction of the component audit teams in the audit process. This involved:
 - Using 'risk workshops' with component auditors during the planning and execution stages of the audit.
 - Issuing clear instructions to component audit teams, setting out minimum and suggested audit procedures to be performed.
- This detailed up-front planning, coupled with effective supervision and review, mitigated the risk of insufficient work being performed by the component auditors.
- The evidence of the group audit team's involvement in, and oversight of, the work of component auditors was of a high standard. In particular, the group team:
 - Issued high-quality group audit instructions that included a range of specifically tailored deliverables designed to enhance and aid the oversight and supervision of work performed by component auditors.
 - Prepared detailed evidence covering its review of component auditors' working papers and the group audit team's site visits.
- The group audit team's involvement with, and oversight of, the work performed by overseas component auditors, being a key manufacturing site and fundamental to the overall operations to the entity, was of a high standard. The group audit team evidenced its involvement and site visit through a detailed working paper, which analysed the responses within the component audit teams' reporting and the potential impact on the group audit.
- The group audit oversight work was enhanced by performing an aggregated stand-back review of the revenue and accrued customer marketing costs correlation results for all the in-scope components. The group team compared the differences that arose in the flows of transactions in the different components, and these were considered and challenged by them as appropriate.
- The group audit team's oversight of, and involvement with, the significant component auditor was of a high standard, with a high level of engagement throughout the audit process. This included regular attendance by members of the group audit team at meetings between the component auditor and management and a detailed review of underlying audit working papers of the component auditor, covering both significant risk and other audit areas.

Oversight

- The group engagement team engaged its own specialists to challenge and oversee the work performed by the component audit team's credit modelling specialists.
- The group audit team demonstrated effective oversight of the component audit teams through the use of data analytics tools. This included identifying higher-risk journal entries across all components and enhanced direction and oversight of the testing by the component audit teams. The group audit team also instructed the component audit teams on using the inventory data analytics tool, which allowed the identification of unusual changes in inventory and further directed the testing by the component audit teams.
- Extensive oversight procedures were performed by the group audit team over a component audit. In particular, the group audit team involved an industry specialist (separate to the component audit team) to assist and review the underlying work papers for the component. There was also extensive evidence of the group audit partner's involvement in the significant audit matters relating to the component.
- The shared service centre audit work was mainly performed by employees from an overseas network firm, who were part of the group audit team. A log was maintained which demonstrated comprehensive and detailed interactions with the UK group audit team, component auditors worldwide and management.

11. Journal testing

Journal testing is performed to address the risk of management override of controls. Auditors should test the appropriateness of journal entries, including examining the supporting evidence for the items selected.

Background	Issue
Only a small number of journals entries across the group were agreed to supporting evidence.	The audit team did not perform adequate journal testing and therefore obtained insufficient evidence to mitigate the risk of management override of controls. In particular, the audit team did not adequately demonstrate: • The basis on which it stratified the population of journals into 'higher-risk' and 'lower-risk' journals. • How it assessed the underlying support for the journals identified using risk-based criteria. • How it concluded that there was sufficient supporting evidence for higher-risk journals.
In response to the significant risk of management override, the audit team tested certain journal entries. Consolidation and other elimination manual entries for final accounts preparation purposes were excluded from this testing. The following significant and individually material, manual adjustments impacted the group's financial statements: • Unrealised profit on inventory elimination. • Cumulative translation reserve movement. • Acquired intangible asset amortisation.	The audit team did not perform sufficient, appropriate procedures over material consolidation and elimination journals. Specifically, the audit team did not adequately test the: • Unrealised profit on inventory elimination, including both the value of inter-group inventory and the margin applied in its calculation. • Cumulative translation reserve movement. • Acquired intangible assets amortisation charge.

Journal testing: good practice points

Management override and journal entry testing

- The audit team performed an additional risk assessment, using the results from a data analytic tool, to identify high-risk journals. Analytical reviews were used to evaluate the impact of untested journals and to refine the high-risk criteria for further testing.
- The audit team's risk assessment and strategy for journal entry testing were enhanced by the firm's general ledger analyser tool. This was applied to the entire audit period to identify unusual movements, and the audit team responded appropriately through its audit approach.
- The audit team's risk assessment and strategy for journal entry testing was enhanced by designing appropriately tailored risk criteria, which enabled it to identify high-risk journals for testing.
- The group audit team assigned a risk rating to each of the group's components, based on a number of internal and external factors (including the number of manual journals). For components with a high-risk , which were out of scope for audit procedures due to their size, the group audit team performed journal testing in line with that performed for in-scope components.
- The group audit team assessed in detail the completeness of the historic consolidation adjustments, including whether they were appropriately rolled-forward into the current year's consolidation or appropriately excluded.

12. Going concern

The going concern assumption is a fundamental principle in the preparation of financial statements. Auditors should assess the appropriateness of management's use of the going concern basis of accounting and whether there are any material uncertainties that should be disclosed to the users of the financial statements and included within their auditor's report.

Background	Issue
Management prepared their going concern assessment paper, which the audit team assessed and concluded that the going concern basis of accounting was appropriate.	The audit team did not perform sufficient procedures over management's going concern assessment. The audit team did not corroborate or challenge the forecast assumptions in management's going concern assessment or demonstrate how it independently evaluated and tested management's stress scenarios.
The financial statements disclosed a material uncertainty around going concern. This related to the group's debt service obligations and the exposure to, and potential volatility in, future prices.	The audit team did not perform sufficient procedures to evaluate, corroborate and challenge the cash flow forecasts used in management's going concern assessment.

Going concern: good practice points

Challenge of management's forecast assumptions
• The audit team performed a robust evaluation of management's going concern assessment. The procedures performed included developing a more severe downside scenario based on the risks it believed management had not sufficiently reflected in the initial assessment. • The audit team performed a robust evaluation of management's going concern assessment. The procedures performed included challenging management on loan covenants, convening two audit technical panels and delaying the signing of the audit opinion. • The audit team robustly challenged the disclosures relating to the going concern assumption and included additional detail in the key audit matter to enhance transparency for users of the Annual Report. • The audit team challenged and performed extensive procedures over management's going concern assessment and the adequacy of the related disclosures in the financial statements. The procedures performed included reviewing the impact of previously disclosed material uncertainties on trading performance against forecasts including analysing working capital trends during those periods.

Involvement of specialists and consultations

- The interaction between the core audit team and the firm's specialists was of a high standard. In particular, the audit team used the firm's industry specialist to assist its evaluation of the entity's market position and to challenge management's forecasts used in the going concern assessment.
- The audit team performed extensive procedures over management's going concern assessment. These included holding discussions with the firm's industry lead and reviewing external publications to identify specific risks. Detailed procedures to mitigate the identified risks were designed and executed.
- The audit team obtained detailed input from multiple internal experts, including valuation experts and debt advisory teams from across the firm's international network. This facilitated a better understanding of going concern and viability risks.
- The audit evidence obtained demonstrated heightened professional scepticism, as reflected in the extent of internal debt advisory specialist involvement, the use of various external sources, and the consideration of operator concentration and potential financial distress faced by the industry.
- The audit team challenged and performed extensive procedures over management's going concern assessment and the adequacy of the related disclosures in the financial statements. The work performed included holding two going concern panels to independently challenge the judgements made by the audit team and holding discussions with prospective investors to understand the quantum and timing of the external funding. Enhanced disclosures were made.

13. Disclosures and reporting

Disclosures and reporting: good practice points

Challenge of disclosures

- The incoming RI and the audit team demonstrated professional scepticism by robustly challenging the financial statements, which resulted in a number of separate prior period adjustments across a range of financial statement line items (most of which were reclassification). The audit team clearly evidenced its stand-back of the errors identified over revenue, the related accounting guidance and the actions it took to ensure no further procedures were required in response to the prior period errors.
- The audit team performed extensive procedures to corroborate the key financial and non-financial disclosures in the front half of the Annual Report.
- The audit team provided suggested improvements to the Task Force on Climate-related Financial Disclosures, which included illustrative examples for each of the improvement points from annual reports of peer companies.
- In assessing management's climate-related disclosures, the audit team took into consideration its interactions with third parties and external publications. This included an assessment of critical external comments over the group's prior year climate disclosures, leading to improvements being proposed relating to risks, sensitivity disclosures and other qualitative aspects.
- The audit team reviewed and robustly challenged the accounting policies of the group, identifying the following presentation and disclosure matters:
 - Freight charges on product sales were not appropriately reflected in cost of sales (a prior year adjustment was made to correct this).
 - The property dilapidation provision was presented within accruals (this was reclassified to provisions).
- Procedures were performed to recompute and check the vesting periods for each share-based payment award (including awards from the previous year). As a result, errors totalling approximately one and a half times materiality were identified and corrected.

Reporting

- The audit team's reports to the group Audit Committee included an explanation of the challenges it encountered in the audit, the alternative procedures undertaken and how it addressed key findings in the FRC's public reports.
- The quality of the audit team's reporting to the Audit Committee promoted effective two-way communication. The use of graphics in the Audit Committee reports, notably in relation to revenue and journals analytics, aided the communication of specific insights achieved from the audit work performed. The audit team also included an extensive summary of control observations identified, along with the firm's recommendations and management's responses in all cases.
- The group audit team provided relevant component audit teams with access to the draft Audit Committee report, so that information on key matters could be drafted by them (and reviewed by the group audit team). This approach enabled the group audit team to remain abreast of key issues and judgements and helped facilitate achieving the reporting deadline.



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