



Financial Reporting Council

# **The FRC's Future Audit Supervision**

Discussion paper on the  
future approach

August 2025

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## Introduction

1. The FRC has welcomed the rich feedback from our stakeholders throughout our early engagement on our Future Audit Supervision Strategy (FASS). This is one of the FRC's major programmes of work as set out in our 3 year Strategy published in March 2025.<sup>1</sup> We have been pleased with the open dialogue and the willingness stakeholders have shown to support this review of our supervisory activities. From the outset of this review, it has been good to see shared support from all stakeholders for a supervisory environment that promotes a resilient audit market and enables firms of all sizes to deliver high-quality audit.
2. In our early engagement, all stakeholders expressed clear support for a proportionate supervisory model that increases focus on the firms' systems of quality management (SoQMs), as well as recognising the importance of continuing file inspections. We also heard initial views from both the firms and users of auditor's reports on FRC's reporting and how it could develop under an evolved supervisory approach.
3. The FRC would also like to thank the Recognised Supervisory Bodies (RSBs) for their continued support as part of this review. It is essential that we continue to work together to deliver consistent supervisory outcomes and tackle key challenges experienced across the whole audit market.
4. As we progress into our second phase of engagement, the FRC is keen to continue the dialogue we have established with our stakeholders, including those who use and rely on audits (investors, lenders, and others), and hear further feedback on the proposed developments to our supervisory model.
5. Reflecting the early feedback, the FRC's proposed approach to FAASS is outlined below, with some specific questions on which we would welcome your views.

## Supervisory Approach

6. The introduction of the new standard of quality management provides a platform for a paradigm shift. As the FRC's confidence in the quality and effectiveness of firms' systems of quality management builds, we will place increasing reliance on them, backed up by file inspections. We will be able to place a much greater emphasis on the role of leadership and governance in embedding a quality-oriented culture within the firm. In this approach, while individuals (RIs) of course retain responsibility for quality at the engagement level, firms' leaders are explicitly tasked with promoting an environment in which quality is foundational. This can broaden our supervisory approach to drive quality in the non-Public Interest Entity (PIE) portfolios of PIE audit firms, reflecting our ambition to improve the whole market for the benefit of those who use and rely on audits.
7. This approach will drive more targeted supervision activity in graded file inspections, supervisors' focus, and firm-wide work, as well as greater consistency of approach between

<sup>1</sup> [FRC 3 Year Strategy 2025-2028](#)

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the FRC and the Professional Bodies. It will provide a platform to explicitly incorporate wider system learning and improvement across both PIE and non-PIE audit firms.

8. We are proposing a future supervisory approach which balances our current approach with firms' SoQMs, which are required by the International Standard on Quality Management (UK) 1 (ISQM (UK) 1). We believe this is the best way to ensure sustained improvement to audit quality which is important for all stakeholders, in particular investors, users of financial statements (such as pensioners, employees, and creditors), businesses, and providers of capital to UK corporates to support their growth and scale. This is because ISQM (UK) 1 promotes a culture of quality by embedding proactive, risk-based thinking into every aspect of a firm's operations. It enhances audit quality through tailored systems that address specific risks, while fostering accountability, continuous improvement, and a shared commitment to high standards. This will create a learning environment and system accountability, and place a focus on behaviours. Please see the diagram below.
9. SoQMs should be tailored to the firm and the engagements it performs, and therefore should be proportionate, and we also want our supervision to be proportionate. We do not believe that this necessarily means doing *less* work – it means doing the *correct* work to respond to the risks arising from a particular firm's impact on the market, the specifics of its portfolio, and assessed risk.

# Future Audit Supervision Framework

## Consistent yet bespoke

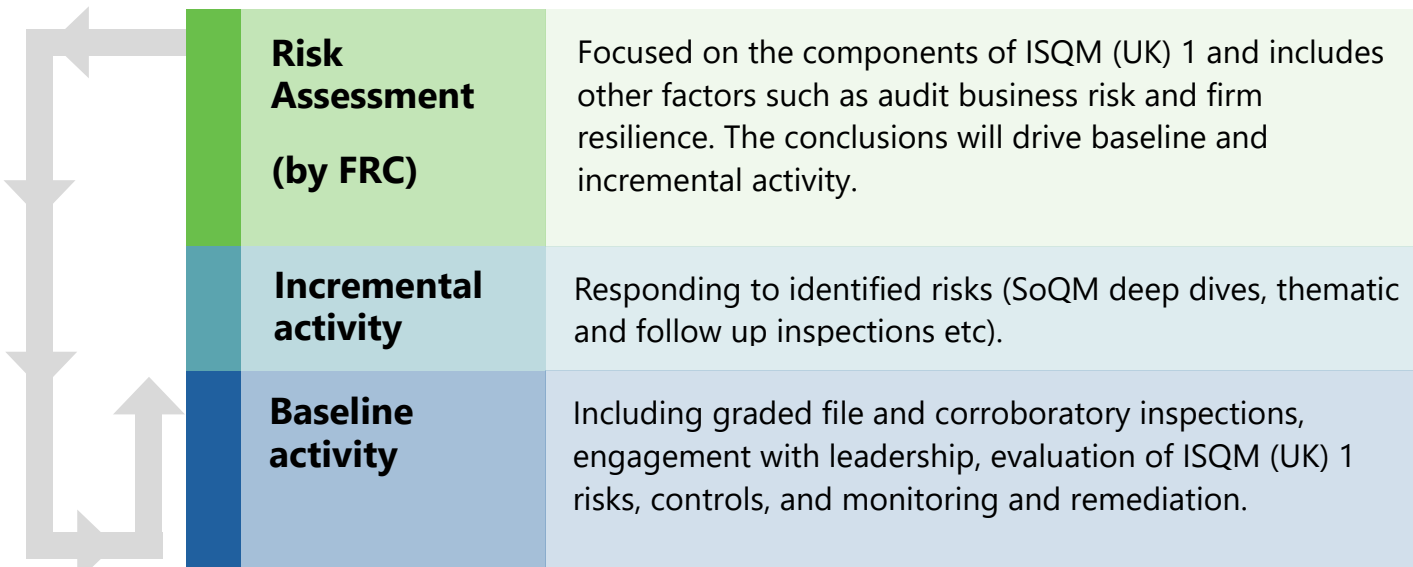
### Grounded in systems of quality management (ISQM (UK) 1)

ISQM (UK) 1 requires a firm to establish a system of quality management that includes these components

- Risk assessment
- Monitoring and remediation
- Governance and Leadership
- Relevant Ethical Requirements
- Acceptance & Continuance
- Engagement Performance (EP)
- Resources
- Information & Communication

The firm must also undertake an annual evaluation (AE) of the system.

The FRC’s approach will assess the firms’ AE and risk assessment. Work over ISQM (UK) 1 components will be driven by changes in a firm’s system and any new risk factors identified (as shown below).



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10. In addition to the components of the SoQM and related file inspections, we propose that the FRC's risk assessment takes account of a firm's **audit business risk** and its **operational and financial resilience**. This is important because the portfolio of entities that a firm audits affects the approach that the firm should take to its work; and weaknesses in the operational and financial resilience of the firm as a whole may negatively affect the audit practice.
  11. Obtaining confidence in an audit firm's SoQM will provide a more holistic view of its audit quality (across both PIE and non-PIE audits) compared to solely via a small sample of inspections.
    - Q1: Do you agree that SoQMs should be a key focus of our supervision approach? If not, please explain why.
  12. Graded inspections of audit engagements (i.e. file inspections, sometimes referred to as "AQR file reviews") will remain important, as they provide evidence of how firms deliver audit quality in practice, with a focus on the exercise of scepticism and the quality of firm judgements. We will actively consider how our approach to file inspections and its impact will develop to remain proportionate and reflect a firm's audit portfolio and role in the market. In addition, one of the components in ISQM (UK) 1 is Engagement Performance, and FRC graded file inspections play a key role in many of the firms' controls for this (in conjunction with RSB inspections and their own internal inspections) and in our testing of this component.
  13. We intend to supplement graded file inspections with three other types of file inspection, namely corroboratory inspections (to obtain confidence on the effectiveness of the firm's own internal quality monitoring programme), follow up inspections (where there are specific areas or entities with specific quality findings), and thematic inspections (where there appears to be an issue with a particular element of audits).
    - Q2: Do you agree that these would be useful additions to our future supervision approach? If not, please explain why.
  14. Smaller firms are already subject to relatively small numbers of graded file inspections.<sup>2</sup> Under the supervision approach being proposed, those larger firms which are currently subject to a greater number of such file inspections may well receive fewer in future (in line with improved audit quality inspection results as reported by the FRC). This will allow for the new types of inspection mentioned above.
    - Q3: Should the FRC reduce the number of graded file inspections at larger firms as the other types of inspection are introduced?
  15. There is a historic expectation that we cover all the FTSE 350 in a five-year cycle. This comes from a Competition Commission (predecessor of the CMA) recommendation, the objective of which was to support enhanced information for companies on audit quality, to help improve how the audit market functioned. The recommendation was based on a supervisory

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<sup>2</sup> Inspection numbers vary from one per firm over a six-year cycle for the smallest PIE firms, up to 20 each year for the largest firms.

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approach that was grounded in individual file inspections. However, since then we have developed our approach and reporting so there is already much more information publicly available than previously. With the development of our risk-based approach to selecting inspections, we no longer focus on a five-year cycle for the FTSE 350.

16. We believe that moving to a supervisory model grounded in SoQM renders this expectation less relevant, although we will ensure that FTSE 350 companies continue to be appropriately included in our file selection approach. (In addition, FRC's Corporate Reporting Review will continue to aim for one full-scope and at least one limited-scope review of a FTSE 350 company's annual report and accounts every five years.<sup>3</sup>) We expect that our approach will further enhance the information available on a broader view of factors affecting audit quality which would further benefit the market.
- Q4: Do you agree that, given the other information the FRC publishes, the five-year cycle of inspections of the FTSE 350 is no longer necessary? If not, please explain why.
17. We propose to allow a transition period before implementing our new approach. This will give firms the opportunity to ensure that their systems and staff are well prepared to embed any changes to their SoQMs that result from our feedback over recent years. It will also allow the FRC time to evolve our supervisory assurance framework on ISQM (UK) 1 to ensure it is proportionate, and refine our own related processes. During this transition, we will reduce the FRC's formal inspection work that we perform on SoQMs for the 12 largest PIE audit firms (currently Tier 1 and Tier 2), compared to the current or future approach. We will also reduce the total number of graded file inspections of audits of corporates at the 12 largest audit firms. We are considering the impact of a transition period for the smaller firms based on where they are in the regulatory cycle, and will share details with these firms in the autumn. We will continue to work closely with firms during this period and our overall engagement will not reduce.
- Q5: Do you agree with the FRC's proposal to have a transition period? If not, please explain why. Do you have any other suggestions for the FRC's initial year of implementing FASS?

## Segmentation

18. We have listened to feedback on the unintended consequences of our current approach to segmentation ("tiering") of audit firms. Our "tiering" approach was originally intended to guide our supervisory response and internal resource allocation but it has been perceived as a form of "league table" externally, which has impacted the market. This was never our intention. Therefore, in future we will not use any labels for groups of firms externally.
- Q6: Do you agree that "tiering" should be removed. If not, please explain why. If you do agree, what consequences do you think this might have, including for:

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<sup>3</sup> <https://www.frc.org.uk/library/supervision/corporate-reporting-review/selection-and-review/>

- Market dynamics; and would these consequences be affected by any names of groupings of firms developed by the market itself;
- The information that the FRC makes public, and hence transparency about what the FRC does; and
- Users of FRC information – which users might find this proposed approach helpful or less helpful?

## Supervisory approach across the whole audit market

19. The FRC is responsible for the whole audit market, not just audits of PIEs. However, we generally delegate responsibility for regulation of the non-PIE audit market to the RSBs; all PIE auditors audit non-PIEs, and are therefore also within the RSBs' scope. As a result, there is an overlap of supervision for firms operating near the PIE/non-PIE boundary. Therefore we intend to work closely with the RSBs to evolve the supervisory approach so that it can be applied proportionately across the whole market, by both the FRC and the RSBs.
- Q7: How can the supervisory approach be adapted to ensure a smoother alignment between FRC and RSB oversight, particularly for firms operating near the PIE/non-PIE boundary?
  - Q8: What practical steps can the FRC and professional bodies take to support a proportionate supervisory approach that reflects the varying risk profiles across the market, including taking account of the size and complexity of the entities being audited?
  - Q9: In what ways can collaboration between the FRC and RSBs be strengthened to improve consistency in audit quality across all market segments?

## Reporting

20. The FRC publishes annual reports which provide an overview of audit quality across the PIE market, most recently the [Annual Review of Audit Quality \(ARAQ\)](#), in July 2025. Our objectives for public reporting are:
- To improve transparency, especially for users of audit;
  - To foster improvements in audit quality; and
  - To provide our perspective on issues facing the UK audit market.
- Q10: Does the ARAQ achieve this objective? Are there alternative ways to achieve this objective?
    - How do you currently use the ARAQ, and how could it be developed to improve usability?
21. We currently also publish reports about six individual firms (BDO LLP, Deloitte LLP, EY LLP, Forvis Mazars LLP, KPMG LLP, and PwC LLP). We understand that the audit firms find these firm-specific reports useful.

- Q11: Do other stakeholders find firm-specific reports useful? If so, for which firms in particular? If not, please explain why.
- Q12: Would it be more useful if firm-specific reports continue to be published at the same time as each other (and the ARAQ), or in “real time” as soon as the FRC finishes annual work on a particular firm?

22. Currently, both the ARAQ and firm-specific reports contain quantitative information such as AQR grades, alongside more qualitative narrative, including responses from the firms to the points raised. This year, for the first time, the FRC has also published a suite of ten Audit Firm Metrics comparable across the twelve largest firms.<sup>4</sup> We intend to publish this data annually, alongside the ARAQ. The FRC’s Strategy also discusses a wider suite of Market Health Indicators.<sup>5</sup>

- Q13: How much of the FRC’s assessment of audit firms should be published and how much should remain private to the firm and FRC?
- For the published material:
  - Should it focus more on quantitative data or more on qualitative narrative, or are they equally useful and support each other?
  - If you find quantitative information useful, given our decision to increase our focus on SoQMs, what kind of data would be most valuable? AQR grades, and/or a Red/Amber/Green rating for a firm’s SoQM either overall or by component, or something else?
  - Is the level of qualitative detail in these reports useful or could any of it be more streamlined or focused (e.g. the level of detail on the findings and good practices)?
  - Do you find the firm’s responses to be a useful aspect of the reporting?

## Next steps:

This phase of engagement invites responses to the questions set out in this document **by 30 September 2025**, and the FRC will be holding a series of roundtables online and in-person on the following dates:

- **11 September** for Auditors
- **15 September** for Auditors
- **17 September** for Independent and Audit Non-Executives
- **18 September** for users of audit
- **22 September** for Recognised Supervisory Bodies

<sup>4</sup> <https://www.frc.org.uk/library/supervision/audit-market-supervision/firm-metrics/>

<sup>5</sup> See page 12 of the [FRC 3 Year Strategy 2025-2028](#)

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- **25 September** for Auditors
  - **29 September** for Auditors

If you are interested in attending these events, please register your interest by emailing: [stakeholderengagement@frc.org.uk](mailto:stakeholderengagement@frc.org.uk). Please submit any written responses to: [fass@frc.org.uk](mailto:fass@frc.org.uk).



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