EXPLANATORY MEMORANDUM TO

THE STATUTORY AUDITORS AND THIRD COUNTRY AUDITORS (AMENDMENT) (EU EXIT) REGULATIONS 2019

2019 No. 177

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Business, Energy and Industrial Strategy and is laid before Parliament by Act.

1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

2.1 This instrument is primarily being made using various powers in the European Union (Withdrawal) Act 2018 as well as other domestic powers in the Companies Act 2006, the Companies (Audit Investigations and Community Enterprise) Act 2004, the Limited Liability Partnerships Act 2000 and the European Communities Act 1972. It addresses failures of retained EU law to operate effectively and other deficiencies arising from the withdrawal of the United Kingdom (UK) from the European Union (EU). It will ensure that the framework for the regulatory oversight and professional recognition of statutory auditors and third country auditors in the UK works effectively following the UK's withdrawal from the EU.

Explanations

What did any relevant EU law do before exit day?

2.2 Directive 2006/43/EC of the European Parliament and of the Council on statutory audits of annual accounts and consolidated accounts ("the Audit Directive", as amended by Directive 2014/56/EU) set out requirements on the statutory audit of certain businesses that are required to be audited under EU law (see section 1210 of the Companies Act 2006 for how this was transposed in the UK). It also set out the responsibilities of the competent authorities of Member States for regulation of statutory audit, including audit inspections, investigations and enforcement, and requirements as to the registration of auditors. It includes a framework on standards for the conduct of auditors in relation to professional ethics and professional competence. In the UK the competent authority is the Financial Reporting Council (FRC), which has ultimate responsibility for monitoring and inspections, investigations and sanctioning of auditors

2.3 Regulation (EU) No. 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities ("the Audit Regulation") applies only to audits of "public interest entities" ("PIEs"), including banks, building societies, insurers and undertakings with securities that are admitted to trading on a regulated market. The Audit Regulation includes enhanced requirements because of the extent of the public interest in those audits.

Why is it being changed?

2.4 As a result of the UK's withdrawal from the EU, references to arrangements with the EU, its institutions and those of Member States, to EU institutions, EU law and concepts under EU law are no longer workable in legislation implementing the Audit Directive. The Audit Regulation forms part of retained EU law under the European Union (Withdrawal) Act 2018 and will therefore continue to apply in the UK as a domestic instrument.

2.5 This instrument makes amendments to the legislation that implements the Audit Directive and to the retained UK version of the Audit Regulation. It also grants powers previously held by the European Commission, to the Secretary of State and to the FRC. The new statutory functions that are therefore provided for in this instrument are summarised in section 2 and described in section 7 below.

2.6 This instrument amends references to non-retained EU law, EU institutions and functions exercised by EU institutions contained in UK law (see paragraph 6.3 for the full list of amended UK law) so that those references instead refer to legislation, institutions and functions that are provided for in UK law.

What will it now do?

2.7 Under the audit regulatory framework that applies prior to the UK's exit from the EU, EEA auditors are afforded preferential treatment over third country auditors in some areas (and UK auditors are afforded preferential treatment in similar ways in EEA States). This preferential treatment is inappropriate after exit. Both EEA auditors and auditors from other countries outside the EEA ("third countries") will be treated in the same way in most respects. In fact this instrument amends the definitions in the UK's audit regulatory framework so that a "third country auditor" will be one from any country outside of the UK. Similarly, EEA audited businesses and third country audited businesses will also be treated largely on the same basis. The EEA States and other third countries will all be subject to the same assessment framework for the equivalence of their audit regulatory frameworks and the adequacy of their competent authorities.

2.8 This instrument provides for the following new, expanded or amended statutory functions to be fulfilled as part of the UK's audit regulatory framework (further details on all these are provided in section 7):

- the FRC as the UK's audit competent authority will continue to be able to put in place "Mutual Recognition Agreements" on audit qualifications with the competent authorities of third countries (but following the UK's exit from the EU this will include the competent authorities of EEA States and Gibraltar).
- the FRC will continue to be able to register third country auditors, that are not eligible for appointment as statutory auditors in the UK, to enable them to audit businesses from outside the UK that have securities admitted to trading on the UK's regulated financial markets (but following exit this will include EEA auditors and auditors from Gibraltar and auditors of businesses incorporated in the EEA States and Gibraltar);
- once further regulations on the applicable process have been made by the Secretary of State, the FRC will be able to assess the equivalence of the audit regulatory frameworks of third countries (which will include the audit regulatory frameworks of EEA States and Gibraltar), and to make

recommendations to the Secretary of State on the use of new powers for the determination of equivalence;

- the FRC will then, as it does now, direct which registration and regulatory frameworks should not apply to auditors of businesses from equivalent third countries or those third countries granted a transitional period;
- once further regulations on the applicable process have been made by the Secretary of State, the FRC will be able to assess the adequacy of the competent authorities of third countries (which will include EEA States and Gibraltar) and make recommendations to the Secretary of State on the use of new powers for the determination of adequacy;
- the FRC will be able to cooperate with all competent authorities from outside the UK under the same framework, which for the exchange of audit working papers and investigation reports, will be based on agreeing working arrangements with those competent authorities that have been determined as adequate;
- the FRC will be able to formally adopt international standards on auditing (ISAs) for application in the UK if they consider this appropriate;
- where the FRC proposes to adopt ISAs that contain provisions that conflict with certain provisions in UK law on auditing standards, the Secretary of State will have new powers to amend those provisions by regulations under the affirmative resolution procedure.

2.9 This instrument includes provisions on the recognition of EEA auditors and EEA audit firms as being eligible for appointment as statutory auditors after the UK's exit from the EU. It includes provisions on the recognition of EEA auditors and EEA audit firms that own or part own a UK audit firm, or are part of the management body of a UK audit firm, as part of the required majorities of qualified owners and managers of UK audit firms. Transitional arrangements are provided for the recognition of EEA auditors' qualifications for them to practice in the UK. Prior to the UK's exit from the EU, approval of individual EEA auditors was subject to passing an aptitude test or adaptation period. This instrument provides a transition period until the 31 December 2020 to continue to allow EEA auditors to have their qualifications recognised in this way. Similarly, the required majority of owners of an audit firm may not include EEA audit firms after 31December 2020. Audit firm registrations, where instead the majority ownership only includes individual EEA auditors, will not be affected.

2.10 This instrument also provides for transitional arrangements on the equivalence of audit regulatory frameworks and the adequacy of audit competent authorities in the EEA States and Gibraltar for a transitional period ending 31 December 2020.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 This instrument uses powers under section 2(2) of the European Communities Act 1972 to complete the implementation of Article 32 of the Audit Directive (paragraphs 3, 4a and 5) that is necessary for the UK's audit regulatory framework to be assessed by the European Commission to be equivalent to that required by the Audit Directive in the EEA States. The relevant provisions in the Audit Directive were applicable to the FRC before exit day, but as Directives are not retained EU law, they are now

inserted by Part 5 of this instrument into the Statutory Auditors and Third Country Auditors Regulations 2016.

3.2 This instrument provides the Secretary of State with new powers to determine third countries' equivalence, and the adequacy of their competent authorities, as well as to set out the framework for future determinations of equivalence and adequacy. These powers can be exercised by regulations made under the negative resolution procedure. It is not thought necessary to require debates of these regulations in the future through the affirmative procedure for the following reasons:

- Regulations determining the equivalence of third countries only affect reliance upon the regulation of audits of businesses incorporated in that third country that trade securities on the UK's markets. Incidence of cross border trading of securities is relatively low.
- Regulations determining the adequacy of competent authorities from third countries only affect cooperation on the regulation of audits of businesses incorporated in that third country that trade securities on the UK's markets, or of subsidiaries of UK corporate groups incorporated in that third country. There is only limited need for the cross border cooperation provided for and only a small number of third country competent authorities have so far agreed working arrangements on regulatory cooperation.

3.3 This instrument also brings the effects of the existing Decisions and Implementing Acts of the European Commission on the equivalence of third countries, and the adequacy of their competent authorities, into UK law. Equivalence status is granted to any third countries that were granted equivalence in relation to the EU by the European Commission before exit day. In the same way adequacy status is granted to any third country competent authorities that were granted adequacy by the European Commission. The relevant provisions, which are in Schedules 1 and 2 to the instrument, also grant transitional status to the EEA States and Gibraltar and provisional adequacy to their competent authorities.

3.4 Schedules 1 and 2 therefore provide a single standard implementation of all determinations of equivalence and adequacy in UK law. They also provide for the EEA States and Gibraltar to have an appropriate status as from exit day, and for each of their competent authorities to also have an appropriate status. This replaces previous different approaches for implementing equivalence and adequacy determinations by the European Commission in UK law:

- Determinations of equivalence were previously given effect in directions issued by the Financial Reporting Council on behalf of the Secretary of State under sections 1239(7) and 1242(4) of the Companies Act 2006.
- Determinations of adequacy were included in section 1253D of the Companies Act 2006 via repeated amendments using powers in the section 2(2) of the European Communities Act 1972.

3.5 For these determinations UK law has not therefore relied upon the direct applicability of the EU Decisions on equivalence and adequacy. Schedule 3 to this instrument repeals the current applicable Decisions to make sure they have no continuing effect as retained EU law after exit day.

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

3.6 The territorial application of this instrument includes Scotland and Northern Ireland.

3.7 The powers under which this instrument is made cover the entire United Kingdom (see the European Communities Act 1972, section 19(4) of the Limited Liability Partnerships Act 2000, section 66(2) of the Companies (Audit, Investigations and Community Enterprise) Act 2004, sections 1284, 1286 and 1299 of the Companies Act 2006 and section 24 of the European Union (Withdrawal) Act 2018). The territorial application of this instrument is not limited either by these Acts or by this instrument.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is the United Kingdom.

4.2 The territorial application of this instrument is the United Kingdom.

5. European Convention on Human Rights

5.1 The Minister for Small Business, Consumers and Corporate Responsibility at the Department for Business, Energy and Industrial Strategy, Kelly Tolhurst, has made the following statement regarding Human Rights:

"In my view the provisions of the Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2019 are compatible with the Convention rights."

6. Legislative Context

6.1 The Audit Regulation is retained EU law under the European Union (Withdrawal) Act 2018. It applies to those businesses that are subject to statutory audit and are defined by the Audit Directive as being Public Interest Entities (PIEs). It includes an enhanced framework on further assurance of auditor independence and a framework of mandatory retendering of auditor appointments. As well as retendering their auditor appointments at least once every ten years, a PIE must rotate its auditor off from its audit at least once every twenty years. Finally, the Audit Regulation includes further provisions on the competent authority for statutory audit including limitations on its ability to delegate functions to accountancy professional bodies for regulation of the statutory audit of PIEs. For the purpose of effective audit regulation across the EU, this includes a framework for regulatory cooperation with other Member State competent authorities.

6.2 To reflect the fact that the UK will no longer be an EU Member State this instrument makes amendments to:

- Part 16 of the Companies Act 2006 on a company's obligations in respect of the audit of its annual accounts;
- Part 42 of the Companies Act 2006 to make a number of changes to the framework for the regulation of statutory audit. This framework applies to the audit of any business whether a company or other undertaking whose auditor is required by section 1210 of that Act to be subject to the framework in that Part. The amendments to Part 42 are extensive and are explained further in the following paragraphs;

- Schedules 10 and 11 to the Companies Act 2006 to make changes to the rules to be applied by professional accountancy bodies on the recognition of individuals and firms as eligible for appointment as statutory auditors, as well as certain other changes to their rules and practices for the qualifications of statutory auditors and the regulation of statutory audit work;
- Schedules 11A and 12 to the Companies Act 2006 which cover the scope for regulatory cooperation on statutory audit work and the arrangements for the regulation of registered "third country auditors" - most of the amendments to these Schedules are made as a consequence of the amendments to Part 42 of the Companies Act 2006;
- the Building Societies Act 1986 and the Friendly Societies Act 1992, which provide for the statutory audit of building societies and friendly societies and include provisions that correspond with those in Part 16 of the Companies Act 2006;
- the Companies (Audit, Investigations and Community Enterprise) Act 2004 and the Companies (Bodies Concerned with Auditing Standards etc.) (Exemption from Liability) Regulations 2016 include provisions on the regulatory responsibilities and powers of the FRC - these are amended as a consequence of the amendments to Part 42 of the Companies Act 2006;
- the Local Audit and Accountability Act 2014 is amended to make sure that the amendments made by this instrument to Part 42 of the Companies Act 2006 and Schedule 10 to that Act do not apply for the purpose of their application to "local auditors" (who audit local authorities in England);
- the Statutory Auditors and Third Country Auditors Regulations 2016 which make provision alongside Part 42 of the Companies Act 2006 on the powers of the FRC in respect of the regulation of statutory auditors - in particular the amendments to these Regulations introduce new powers for the FRC and the Secretary of State in respect of auditing standards, which are explained further in section 7;
- the Statutory Auditors and Third Country Auditors Regulations 2013, which provide for the maintenance of the register of third country auditors in the UK - after the UK's exit from the EU the register will include EEA auditors where appropriate in the same way that it already includes other third country auditors, so amendments are made to these regulations as a result and as a consequence of other amendments to Part 42 of the Companies Act 2006 and the Statutory Auditors and Third Country Auditors Regulations 2016;
- the Statutory Auditors (Amendment of Companies Act 2006 and Delegation of Functions etc) Order 2012, which delegates certain functions of the Secretary of State under Part 42 of the Companies Act 2006 to the FRC - amendments are also needed to these regulations as a consequence of the amendments made to Part 42 of the Companies Act 2006;
- the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008 and the Limited Liability Partnerships (Accounts and Audit) (Application of the Companies Act 2006) Regulations 2008, which provide for the statutory audit of miscellaneous insurance undertakings and LLPs and apply provisions of Part 16 of the Companies Act 2006 for this purpose.

6.3 Finally, this instrument makes amendments to the Audit Regulation for its application as a part of UK law. While many of these amendments are simply to make sure the terms and language used in the Regulation are consistent with that in UK law some amendments are made as a direct consequence of the UK's exit from the EU. These include similar amendments to those made to the legislation listed above to make sure that the Regulation no longer gives special treatment to EEA auditors and businesses incorporated in the EEA but instead applies any frameworks affecting trade by businesses outside of the UK on a consistent and objective basis.

7. Policy background

What is being done and why?

7.1 The instrument amends Part 42 of the Companies Act 2006 to introduce a number of important changes associated with the UK's exit from the European Union:

- It expands the power in section 1221 of the Companies Act 2006 for the Secretary of State to enter into Mutual Recognition Agreements ("MRAs") with the EU Member States and the other EEA States on audit qualifications. This is an expansion of the power previously provided to the Secretary of State under section 1221 as it already existed for other "third countries" outside of the EEA. This power has previously been delegated by the Secretary of State to the FRC by Order under section 1252 of the Companies Act 2006 so that, in the future, the FRC will be able to enter into MRAs with EEA competent authorities on audit qualifications.
- For the purposes of the amendment of section 1221 described above and other amendments made by this instrument the EEA States and Gibraltar will all be included within references to "third countries" in the framework in Part 42 in future. This change is made via amendments to the various definitions in Part 42 of the Companies Act 2006 and Schedule 10 to that Act including that of "third country".
- After the UK's exit from the EU, the equivalence of third countries' audit regulatory frameworks and the adequacy of their competent authorities for the exchange of audit working papers and investigation reports will be determined as part of UK law, rather than as part of EU law. Determinations of the equivalence of third country audit regulatory frameworks were made previously by the European Commission. Determinations of the adequacy of their competent authorities were also made by the European Commission. The effects of all the necessary changes to achieve this, both for existing third countries and for the EEA States and Gibraltar now that they are brought into this framework are set out in the next paragraph.

7.2 The changes being made to the frameworks in Part 42 of the Companies Act 2006 on the equivalence of third countries and the adequacy of their competent authorities are:

- From exit day this instrument grants transitional status under the equivalence framework to the EEA states and Gibraltar for a period ending on 31 December 2020. For the first time EEA and Gibraltarian auditors will be required to register as third country auditors if they audit a business that has securities admitted to trading on the UK's regulated financial markets. During this period the FRC will establish and take forward a programme in which the EEA states, Gibraltar and other third countries will be able to be assessed on

the equivalence of their regulatory framework, for the purposes of the FRC making a recommendation to the Secretary of State. Where a business is incorporated in an equivalent or transitional third country and issues securities on the UK's regulated markets, the FRC already applies fewer registration requirements to its auditor and does not subject them to regular inspections of their work.

- This instrument also includes further provision on the FRC's power to disapply registration and regulatory requirements which would otherwise apply to a third country auditor on the basis of the equivalent or transitional status of the country in which their client business is incorporated. For equivalent third countries or those granted a transitional period under the equivalence framework, including the EEA States and Gibraltar, the FRC will be able to continue with the approach in its existing direction issued under section 1239(7) and 1242(4) of the Companies Act 2006. The FRC's direction disapplies certain registration and regulatory requirements to auditors of companies incorporated in those countries that issue securities admitted to trade on the UK's regulated markets. During the transitional period provided for the EEA States and Gibraltar this will also apply to them.
- From exit day, this instrument also grants provisional adequacy status to the competent authorities of the EEA States and Gibraltar for the period ending on 31 December 2020. During this period, and once regulations on the applicable procedure have been made by the Secretary of State, the FRC will establish and take forward a programme in which the EEA States, Gibraltar and other third countries will be able to be assessed for the purposes of FRC making a recommendation to the Secretary of State on whether they should be granted full adequacy status. The FRC will also agree bilateral working arrangements in accordance with the Companies Act 2006 with EEA competent authorities and those in Gibraltar based on their provisional adequacy. These arrangements will apply for the purposes of exchanging audit working papers and investigation reports. These documents are subject to special controls on their transfer under Part 42 of the Companies Act 2006.
- This instrument also amends provisions on regulatory cooperation so that the framework that previously applied for cooperation with the EEA States will apply in future to cooperation with any third country competent authority. This is provided where the third country previously has been approved as adequate, and has transitional or equivalence status. This means that, during the transitional period, subject to the agreement of working arrangements, it will be possible for the FRC to cooperate with EEA competent authorities and those of Gibraltar in the same way as for other equivalent third countries that have adequate competent authorities. Requirements for compulsory cooperation have been removed.

7.3 The amendments to the Statutory Auditors and Third Country Auditors Regulations 2016 in this instrument provide the FRC with powers to adopt International Standards on Auditing ("ISAs"). Previously the European Commission had these powers under the Audit Directive and Regulation. The new FRC powers supplement their existing powers to set standards in the UK under the Statutory Auditors and Third Country Auditors Regulations 2016. As the FRC already sets auditing standards that are largely in line with international auditing standards this power is unlikely to lead to any considerable practical change in auditing in the UK. However, if the FRC

proposes to adopt ISAs that conflict with Articles 7, 8 and 18 of the Audit Regulation as it applies in the UK, or paragraphs 1 to 15 of Schedule 1 to the Statutory Auditors and Third Country Auditors Regulations 2016, the Secretary of State is granted a new power in those regulations to amend these Articles and paragraphs if the Secretary of State considers it appropriate. Again, this is consistent with powers granted to the European Commission under EU law.

7.4 Wherever possible this instrument provides for continuity and consistency with the framework that applied prior to the UK's exit from the EU. One exception to this is where a UK company has securities admitted to trading on an EU regulated market but does not have securities admitted to trading on a UK regulated market. These companies will not be treated as PIEs following the commencement of this instrument. This is due to amendments to Part 16 of the Companies Act 2006, Schedule 10 to that Act and to the Statutory Auditors and Third Country Auditors 2016. As a result, the relevant companies and their auditors will not be subject to the provisions of the Audit Regulation (or to certain other provisions in the Companies Act 2006 and the regulations themselves that apply only to PIEs and their auditors). This is done to ensure there is equal treatment as far as possible between listings on EEA regulated markets and listings on other third country regulated markets. Transitional provisions are included in Schedule 4 to this instrument to make sure that, for financial years or audit investigations beginning before exit day, those entities affected by this change in status will continue to be treated as PIEs for the purposes of the completion of ongoing processes.

7.5 This instrument applies to company law which is a transferred matter for Northern Ireland under section 4 of the Northern Ireland Act 1998. The UK Government remains committed to restoring devolution in Northern Ireland. This is particularly important in the context of EU Exit where we want devolved Ministers to take the necessary actions to prepare Northern Ireland for exit. We have been considering how to ensure a functioning statute book across the UK including in Northern Ireland for exit day absent a Northern Ireland Executive. With exit day less than one year away, and in the continued absence of a Northern Ireland Executive, the window to prepare Northern Ireland's statute book for exit is narrowing.UK Government Ministers have therefore decided that in the interest of legal certainty in Northern Ireland, the UK Government will take through the necessary secondary legislation at Westminster for Northern Ireland, in close consultation with the Northern Ireland departments. This is one such instrument.

Dependencies with instruments being made by HM Treasury

7.6 There are some amendments made by this instrument which have dependencies with EU Exit instruments made by HM Treasury. These are as follows.

- The definition of "CRR firm" (relevant to the definition of "credit institution") cross-refers to provisions inserted into Regulation (EU) No. 575/2013 by HM Treasury's instrument the Capital Requirements (Amendment) (EU Exit) Regulations 2018 (SI 2018/1401). The instrument can be found here: http://www.legislation.gov.uk/uksi/2018/1401/contents/made
- The definitions of "MiFID investment firm", "regulated market" and "UK regulated market" cross-refer to provisions inserted into Regulation (EU) No. 600/2014 by HM Treasury's instrument the Markets in Financial Instruments

(Amendment) (EU Exit) Regulations 2018 (SI 2018/1403). The instrument can be found here: http://www.legislation.gov.uk/uksi/2018/1403/contents/made

8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union

8.1 This instrument is being made using the power in section 8(1) of the European Union (Withdrawal) Act 2018 in order to address failures of retained EU law to operate effectively or other deficiencies arising from the withdrawal of the United Kingdom from the European Union. The instrument is also being made using the powers in section 23(1) and paragraph 21 of Schedule 7 of the European Union (Withdrawal) Act 2018. In accordance with the requirements of that Act the Minister has made the relevant statements as detailed in Part 2 of the Annex to this Explanatory Memorandum.

8.2 Alongside the European Union (Withdrawal) Act 2018 powers, this instrument is also being made under section 2(2) of the European Communities Act 1972, sections 15 and 17 of the Limited Liability Partnerships Act 2000, section 18A of the Companies (Audit, Investigations and Community Enterprise) Act 2004 and sections 484(1), 519A(5), 1239(1)(b), (2) and (5)(d), 1241(2)(c), 1246(1), 1252(1), (4)(a) and (8), 1292(1) and (2) and 1294(1) of the Companies Act 2006.

9. Consolidation

9.1 This is not a consolidation.

10. Consultation outcome

10.1 We have not been able to publicly consult in order to minimise sensitivities in advance of negotiations with the EU. This instrument was developed in the Department for Business, Energy and Industrial Strategy on the basis of informal consultation with representatives of various groups with an interest in the regulation of statutory auditors. Consultees included representatives of the audit profession, of the larger audit firms, of investors in companies who must make investment decisions on the basis of the audited accounts and reports of businesses, and with the FRC. BEIS officials met regularly with a group of representatives to discuss legislative options and potential impacts on auditing.

11. Guidance

11.1 The practical implementation of the changes in this instrument will primarily be a matter for the audit profession with the support of the professional accountancy bodies and oversight by the FRC. Guidance on the audit requirements of the Companies Act 2006 from Companies House will also be updated in due course to reflect the framework that will apply following the coming into force of this instrument.

11.2 This instrument refers to the Rulebook made by the Prudential Regulation Authority under the Financial Services and Markets Act 2000 (c.8). The Rulebook is available on http://www.prarulebook.co.uk and copies of the rules referred to can be obtained from the Prudential Regulation Authority, 20 Moorgate, London EC2R 6DA, where they are also available for inspection.

11.3 This instrument also refers to a sourcebook made by the Financial Conduct Authority under the Financial Services and Markets Act 2000. Sourcebooks made by the Financial Conduct Authority are available on

https://www.handbook.fca.org.uk/handbook and copies of the rules referred to can be obtained from the Financial Conduct Authority, 12 Endeavour Square, London E20 1JN, where they are also available for inspection.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

12.3 An Impact Assessment has not been prepared for this instrument because of the low level of impact on business (less than £5 million). However, a De Minimis assessment has been carried out and has concluded that only a limited sector is affected by most of the substantial changes. Comparatively few EU companies issue securities that are admitted to trading on UK regulated markets. In any case we are granting their auditors some transitional relief. Also, a comparatively small number of UK companies issue securities that are admitted to trading on EU regulated markets and even fewer of these do so without also issuing securities on the UK's own regulated markets.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses.

13.2 To minimise the impact of the requirements on small businesses (employing up to 50 people), as these would mostly be audit firms, the approach taken is to only make very necessary changes outside of those that are required in the context of sophisticated cross border transactions between companies and financial markets. We would not expect these audits to be undertaken by smaller firms. Meanwhile most small companies are audit exempt and will be unaffected by these changes. Many larger companies, if they are subsidiaries included in the accounts of a group, also have access to audit exemption. However, further possible amendments to this audit exemption as a result of the UK's exit from the EU will be considered in due course.

14. Monitoring & review

14.1 For those amendments made by this instrument under the European Union (Withdrawal) Act 2018, no review clause is required.

14.2 The instrument does not include a statutory review clause and, in line with sections 28(2)(b) and 31(2)(b) of the Small Business, Enterprise and Employment Act 2015 (c. 26), the Minister for Small Business, Consumers and Corporate Responsibility at the Department for Business, Energy and Industrial Strategy, Kelly Tolhurst, has made the following statement:

"I consider that it is not appropriate to make provision for review of the amendments to Chapter 1 and section 519A of Part 16 of the Companies Act 2006, made by the Statutory Auditors and Third Country Auditors (EU Exit) (Amendment) Regulations 2019, as the Regulations are amending regulatory provision that is contained in primary legislation, which is outside the scope of the policy objectives as set out in the statutory guidance. It is also not appropriate to make provision for review of the amendments made to the Statutory Auditors and Third Country Auditors Regulations 2016 using powers under the European Communities Act 1972, as those Regulations are themselves already subject to review, and the amendment will be considered as part of that review.

"The amendments to the Statutory Auditors (Amendment of Companies Act 2006 and Delegation of Functions etc) Order 2012, the Statutory Auditors and Third Country Auditors Regulations 2013 and the Companies (Bodies Concerned with Auditing Standards etc.) (Exemption from Liability) Regulations 2016 are also not made subject to review, because the activities affected by these Regulations are not "qualifying activities" under section 29(2) of the Small Business, Enterprise and Employment Act 2015 and so do not constitute regulatory provision under that Act.

"A review provision is not included in respect of the amendments made to the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008 because these amendments have no, or no significant, impact on business, charities or voluntary bodies".

15. Contact

15.1 Paul Smith at the Department for Business, Energy and Industrial Strategy Telephone: 0207 215 4164 or email: pauld.smith@beis.gov.uk can be contacted with any queries regarding the instrument.

15.2 Andrew Death, Deputy Director, at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.

15.3 Kelly Tolhurst, Minister for Small Business, Consumers and Corporate Responsibility at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.

Annex

Statements under the European Union (Withdrawal) Act 2018

Part 1

Table of Statements under the 2018 Act

This table sets out the statements that may be required under the 2018 Act.

Statement	Where the requirement sits	To whom it applies	What it requires
Sifting	Paragraphs 3(3), 3(7) and 17(3) and 17(7) of Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) to make a Negative SI	Explain why the instrument should be subject to the negative procedure and, if applicable, why they disagree with the recommendation(s) of the SLSC/Sifting Committees
Appropriate-ness	Sub-paragraph (2) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	A statement that the SI does no more than is appropriate.
Good Reasons	Sub-paragraph (3) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	Explain the good reasons for making the instrument and that what is being done is a reasonable course of action.
Equalities	Sub-paragraphs (4) and (5) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	Explain what, if any, amendment, repeals or revocations are being made to the Equalities Acts 2006 and 2010 and legislation made under them. State that the Minister has had due regard to the need to eliminate discrimination and other conduct prohibited under the Equality Act 2010.
Explanations	Sub-paragraph (6) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2 In addition to the statutory obligation the Government has made a political commitment to include these statements alongside all EUWA SIs	Explain the instrument, identify the relevant law before exit day, explain the instrument's effect on retained EU law and give information about the purpose of the instrument, e.g., whether minor or technical changes only are intended to the EU retained law.
Criminal offences	Sub-paragraphs (3) and (7) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9, and	Set out the 'good reasons' for creating a criminal offence, and the penalty attached.

		23(1) or jointly exercising powers in Schedule 2 to create a criminal offence	
Sub-delegation	Paragraph 30, Schedule 7	Ministers of the Crown exercising sections 10(1), 12 and part 1 of Schedule 4 to create a legislative power exercisable not by a Minister of the Crown or a Devolved Authority by Statutory Instrument.	State why it is appropriate to create such a sub-delegated power.
Urgency	Paragraph 34, Schedule 7	Ministers of the Crown using the urgent procedure in paragraphs 4 or 14, Schedule 7.	Statement of the reasons for the Minister's opinion that the SI is urgent.
Explanations where amending regulations under 2(2) ECA 1972	Paragraph 13, Schedule 8	Anybody making an SI after exit day under powers outside the European Union (Withdrawal) Act 2018 which modifies subordinate legislation made under s. 2(2) ECA	Statement explaining the good reasons for modifying the instrument made under s. 2(2) ECA, identifying the relevant law before exit day, and explaining the instrument's effect on retained EU law.
Scrutiny statement where amending regulations under 2(2) ECA 1972	Paragraph 16, Schedule 8	Anybody making an SI after exit day under powers outside the European Union (Withdrawal) Act 2018 which modifies subordinate legislation made under s. 2(2) ECA	Statement setting out: a) the steps which the relevant authority has taken to make the draft instrument published in accordance with paragraph 16(2), Schedule 8 available to each House of Parliament, b) containing information about the relevant authority's response to— (i) any recommendations made by a committee of either House of Parliament about the published draft instrument, and (ii) any other representations made to the relevant authority about the published draft instrument, and, c) containing any other information that the relevant authority considers appropriate in relation to the scrutiny of the instrument or draft instrument which is to be laid.

Part 2

Statements required when using enabling powers under the European Union (Withdrawal) 2018 Act

1. **Appropriateness statement**

1.1 The Minister for Small Business, Consumers and Corporate Responsibility at the Department for Business, Energy and Industrial Strategy, Kelly Tolhurst, has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In my view the Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2019 do no more than is appropriate".

1.2 This is because this instrument merely remedies deficiencies in retained EU law. Where new powers have been taken this is because there would also be insufficient powers following the UK's exit from the EU for the operation of the regulatory framework. Further details are provided in sections 2 and 7 of the explanatory memorandum.

2. **Good reasons**

2.1 The Minister for Small Business, Consumers and Corporate Responsibility at the Department for Business, Energy and Industrial Strategy, Kelly Tolhurst, has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In my view there are good reasons for the provisions in this instrument, and I have concluded they are a reasonable course of action".

2.2 These are that it will be important to enable a smooth transition to a framework where the UK's relationship to the EU Member States in the field of audit regulation is comparable to its relationship to existing third countries. This involves the provision of a transitional period in which EU audit qualifications and firm registrations will continue to be recognised as they are now for all existing purposes. For further details see section 2 of this explanatory memorandum.

2.3 The EEA states will also be granted transitional status in respect of the equivalence of their audit regulatory frameworks and their audit regulatory bodies will be granted provisional adequacy status for the purposes of regulatory cooperation. This is intended to avoid any consequences of "cliff edge" effects applying on timeframes in which auditors, their client businesses and the financial markets and regulators will not be able to adapt in a planned and organised way.

3. **Equalities**

3.1 The Minister for Small Business, Consumers and Corporate Responsibility at the Department for Business, Energy and Industrial Strategy, Kelly Tolhurst, has made the following statement(s):

"The instrument does not amend, repeal or revoke a provision or provisions in the Equality Act 2006 or the Equality Act 2010 or subordinate legislation made under those Acts.

3.2 The Minister for Small Business, Consumers and Corporate Responsibility the Department for Business, Energy and Industrial Strategy, Kelly Tolhurst, has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In relation to the instrument, I, Kelly Tolhurst, Minister for Small Business, Consumers and Corporate Responsibility at the Department for Business, Energy and Industrial Strategy, have had due regard to the need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010.".

4. Explanations

4.1 The explanations statement has been made in section 2 of the main body of this explanatory memorandum.