



Financial Reporting Council

The Rt Hon. Liam Byrne MP

Chair, Business and Trade Select Committee
House of Commons
London
SW1A 0AA

29 April 2024

Select Committee Appearance

Dear Mr Byrne,

Thank you for the opportunity to provide evidence to your Committee on 26 March 2024 regarding the progress made by the FRC in recent years and the continued support for reform.

As I explained during the session, the FRC has a critical role to play in supporting the UK as a great place for business growth and investment. High standards of audit, governance and reporting underpins investor confidence resulting in UK companies more readily accessing capital to grow which is good for the economy. These standards also reduce the likelihood of disorderly corporate failures which impact communities, livelihoods, and the taxpayer.

We are resolutely focused on ensuring our current regulatory toolkit is used to best effect for this purpose, working closely with our stakeholders. I outlined five particular areas where our effectiveness can be strengthened in line with other regulators. Alongside this letter is a follow up note which provides further comment on these priorities, including our regulatory viewpoint on legislating for these proposals, something we remain ready to support.

The note also includes data responding to Mark Pawsey's question during the session on the number of accountants which have been disbarred in recent years.

I look forward to a constructive relationship with you and your Committee as we restore trust in the UK's corporate governance, reporting and audit frameworks.

Yours sincerely

Richard Moriarty
Chief Executive

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FRC Follow Up Note

**Delivering Audit Reform: follow-up
to Business and Trade Committee
session on 26 March 2024**

April 2024

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1. The FRC welcomes the opportunity to provide further information to the Business and Trade Committee following its hearing, Delivering Audit Reform: follow-up; and on options for reforming the UK's corporate governance, reporting and audit regimes.
 2. The FRC's work is central to the UK's reputation for high-quality corporate governance, reporting and audit, which underpins investor confidence and results in UK companies more readily accessing capital to grow, supporting our economy. High standards also reduce the likelihood of disorderly corporate failures which disrupt communities, cost jobs and livelihoods, and impact the taxpayer.
 3. We have included information in response to Mark Pawsey MP's question regarding the disbarment of accountants. We have also provided comments on three areas that were of follow up interest to the Committee: scrutiny of proposals, measures to regularise the FRC as regulator, and longer-term reforms.

Disbarment of accountants

4. Since 2016, 29 accountants have been excluded from their membership bodies following cases investigated by the FRC. A further 3 accountants have been prohibited from conducting audit work or signing audit opinions. Of these 32 accountants, 12 were auditors.
5. In the most recent year (2023), there were 10,432 Responsible Individuals (an individual who undertakes regulated audit work) registered with the UK's Recognised Supervisory Bodies.
6. The Recognised Supervisory Bodies also remove Responsible Individual registrations following outcomes of their own relevant registration or disciplinary committees. They will be able to provide further information on their own removals.

Scrutiny of proposals

7. Since the publication of the 2018 Kingman Review, the FRC has transformed into a more assertive and effective regulator and taken steps to restore trust in the UK's corporate governance, reporting, and audit regimes. We have implemented 47 of the 50 recommendations that were directed at the FRC and within our control, with the other 3 underway. We welcomed that Sir John Kingman, himself, recognised our significant progress in his evidence to the Committee.
8. The remaining 28 recommendations require legislation. The case for change is as compelling today, if not more so, than it was in 2018. There is strong support across stakeholders for these measures, however, there has not been parliamentary time available to legislate.
9. In the Queen's Speech delivered to Parliament in May 2022, the Government announced its intention to bring forward the draft Audit Reform Bill which would implement these recommendations, as well as take forward other policy areas such as insolvency reform.

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10. The production of a draft Bill provides Parliament the opportunity to provide pre-legislative scrutiny, for example by a Select Committee. This would allow government to address any concerns in the drafting ahead of its passage through both Houses of Parliament.

Priorities for regularising the FRC as a regulator

11. As outlined by Richard Moriarty, the FRC's Chief Executive, in his evidence to the Committee, there are serious gaps in the FRC's current regulatory toolkit which need modernising so it is equivalent to those other regulators overseeing the well-running of the UK's capital markets.
12. We consider there to be two immediate priorities for regularisation that should be urgently corrected:
13. **Statutory funding:** An effective regulator must have a means to adequately fund its activities. The FRC is currently dependent on voluntary contributions from those we regulate for nearly 40% of our income. As Sir John Kingman outlined in his evidence to the Committee, this is inappropriate and we are not aware of any other UK regulator which operates on this basis. Putting the FRC's funding on a statutory footing like other regulators would address this issue.
14. **Information powers:** An effective regulator must have powers to obtain information relevant to its work. The FRC is, however, reliant on the goodwill of corporate entities to provide information and documents concerning private or AIM listed companies regarding auditors, and the conduct of accountants or actuaries working for any corporate entities. It is most irregular in regulation that the FRC does not have the powers to require information as part of its investigations.
15. These two measures are separate from wider consideration on the scope of reforming the UK's corporate governance, reporting and audit regimes. Instead, these two measures would simply bring the FRC's powers into line with other regulators. As such, these proposals could be considered as regulator-specific reforms for a separate legislative vehicle. They don't need to await the establishment of ARGAs and broader reform.

Priorities for broader reform

16. The Government's response to its White Paper, Restoring trust in audit and corporate governance, identified further areas of reform which would serve to restore investor and public confidence in the UK's corporate governance, reporting and audit regimes. There are two proposals that would modernise our powers to recognise how corporate UK has changed over the many years since our powers were established. Without these two changes, the FRC will continue to have serious gaps in its regulatory perimeter, which is why Richard Moriarty described the situation to the Committee as like being "sheriff for only half the county".
17. **Modernising the definition of Public Interest Entities:** The FRC's regulatory perimeter only applies mainly to publicly listed companies, which does not reflect how corporate structures have evolved in recent years. Recent cases which the Committee has taken an

interest in have involved privately held businesses rather than publicly listed companies and so outside the scope of the current definition of Public Interest Entity. The definition of 'Public Interest Entity' which define the scope of our authority should, as recognised by the government's White Paper, be modernised to cover large private sector industries and those other businesses which are in the public interest.

18. **Accountability of company directors:** The FRC can currently only take enforcement action against those company directors who are members of the accountancy profession, creating a two-tier approach to the accountability of those involved in financial wrongdoing and serious failures. This should be equalised so all directors of large businesses which are classed as Public Interest Entities are held to the same consistent standards. It is perverse that there is no regulatory accountability if you happen not to be a member of the accountancy profession.
19. The prospect of legislative reform to modernise the FRC's regulatory perimeter for these two important issues also offers Government and Parliament a chance to review and take forward another proposal that featured in the government's White Paper.
20. **Competition powers:** Improving audit committees' choice of and access to auditors is important to driving competition which lowers costs and strengthens resilience of the statutory audit market. The FRC has taken steps to support firms to compete for statutory audit tenders by working with them to share best practice and enhance their capabilities, however, we lack any competition related powers unlike many other sector regulators.
21. While not within the responsibility of the Department for Business and Trade, the Audit, Reporting and Governance Authority has been identified as the **local audit system leader**, addressing fragmentation seen in the regulation of the local audit system. This requires primary legislation owing to the transfer of responsibility for the Code of Audit Practice from the NAO. The FRC is currently supporting DLUHC in performing this role, but without legislation there is not a statutory basis for DLUHC to transfer this role to the FRC.

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