EXPLANATORY MEMORANDUM TO

THE COMPANIES ACT 2006 (RECOGNITION OF THIRD COUNTRY QUALIFICATIONS AND PRACTICAL TRAINING) (AMENDMENT) REGULATIONS 2025

2025 No. 444

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Business and Trade and is laid before Parliament by Command of his Majesty.

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

2. Declaration

2.1 Justin Madders, the Minister for Employment Rights, Competition and Markets at the Department for Business and Trade confirms that this Explanatory Memorandum meets the required standard.

2.2 Andrew Death, Deputy Director for Corporate Reporting and Audit, at the Department for Business and Trade confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Paul Smith at the Department for Business and Trade, Telephone: 07826 874 384 or email: pauld.smith@businessandtrade.gov.uk can be contacted with any queries regarding this instrument.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 This instrument makes amendments to provisions in the Companies Act 2006 ("the Act") on overseas qualifications of auditors that may be recognised in different ways for the purpose of enabling a holder of a qualification to obtain eligibility for appointment as a statutory auditor in the United Kingdom. The Act provides for both individuals and firms to obtain eligibility for appointment in the UK but requires that only an individual who is eligible for appointment may sign an audit report on the accounts of an audited business on behalf of an appointed audit firm. Eligibility must be based on that individual holding an appropriate qualification.

4.2 The first set of amendments is made to section 1221 of the Act, which enables the Secretary of State to approve overseas qualifications by entering into Mutual Recognition Arrangements (MRAs) on the UK's recognised professional qualifications for statutory audit. The amendments clarify that the applicable requirement for recognition of an overseas qualification is that the subjects and skills covered by it must be substantially the same as those covered by a UK qualification, and the overseas qualification must demonstrate those subjects and skills to substantially the same standard.

4.3 The second set of amendments is made to paragraph 9 of Schedule 11 to the Act, which sets out the procedure and criteria for the recognition by the Secretary of State of a UK professional qualification for statutory auditors. Paragraph 9 sets the criteria for recognition of a qualifying body's arrangements for the required period of practical training to be undergone by a trainee auditor. The amendment to paragraph 9 enables practical training in audit to be provided by an approved overseas auditor in any country, including those outside of the UK and European Economic Area (EEA), under appropriate arrangements. This amendment broadens the ability of the UK qualifying bodies to include practical training provided, in effect beyond the UK and EEA, so as to include any country or territory outside the UK, which has similar laws and practices on the audit of accounts to those in the UK.

Where does the legislation extend to, and apply?

4.4 The extent of this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is England and Wales and Scotland and Northern Ireland.

4.5 The territorial application of this instrument (that is, where the instrument produces a practical effect) is England and Wales and Scotland and Northern Ireland. The Northern Ireland Executive has agreed that, while the operation and regulation of business associations remains a transferred matter within the legislative competence of the Northern Ireland Assembly, amendments to the Companies Act 2006 and related legislation regulating business associations and the audit of their annual accounts and reports by individuals and firms in the audit profession should be made in the same terms for the whole of the United Kingdom.

5. Policy Context

What is being done and why?

5.1 This instrument amends section 1221 of the Act, to clarify the requirements that apply to reciprocal arrangements on the mutual recognition of audit qualifications in line with the approach taken in the Professional Qualifications Act 2022. Section 1221 provides for MRAs as the main way in which overseas audit qualifications may be recognised in the UK. Under the Act, these MRAs must be put in place by the Financial Reporting Council (FRC) on behalf of the Secretary of State, using the powers in section 1221, which the Secretary of State has delegated to the FRC for the purpose of enabling UK audit qualifications to be recognised overseas while also making sure that overseas auditors may only be granted eligibility for appointment in the UK if their qualifications are of a suitable standard.

5.2 The amendments to section 1221 align with the approach to mutual recognition in the Professional Qualifications Act 2022, which provides a new power, for the putting in place where not yet available, powers to make MRAs for a statutorily regulated profession. Although the powers in section 1221 are already in place and have been for many years in some form, the amendments in this instrument clarify what it means for an overseas audit qualification to cover all of the subjects that are covered by a UK audit qualification. This requirement has always been a part of the framework, where knowledge of those subjects is essential for the pursuit of the profession.

5.3 The amendments to section 1221(1A) recognise firstly that, given the practical training element of a UK recognised qualification, it covers both subjects *and skills*. Secondly the amendments recognise that, if it is to be considered to cover all of those subjects and skills, an overseas qualification will cover *substantially the same* subjects and skills, but also *demonstrate knowledge of those subject and skills to substantially*

the same standard. This clearer articulation of the existing conditions for recognition of an overseas audit qualification is intended to aid the FRC and the other organisations supporting its efforts, as well as overseas audit regulatory authorities, in putting in place MRAs in the UK. Similar clarificatory amendments are also made to section 1221(7A), with the insertion of a new subsection (7AA), so that the required content of an aptitude test, if one is put in place to compensate for any gaps in the content of the overseas qualification, is articulated in the same way.

5.4 This instrument also amends the requirements on practical training of trainee auditors in paragraph 9 of Schedule 11 to the Act. The amendments enable qualified auditors, who are approved as being eligible for appointment in other countries beyond the EEA, to provide practical audit training which can contribute to the trainee obtaining a UK recognised professional qualification as a statutory auditor.

5.5 Part 2 of Schedule 11 to the Act requires that, for an individual to obtain a UK professional qualification in statutory audit, they must: undergo a course of theoretical instruction in certain required subjects; sit a recognised examination; and undertake a required period of recognised practical training in the audit of accounts. The FRC, as the UK's independent regulator for accounting, reporting, audit and corporate governance, approves audit qualifications in the UK, on behalf of the Secretary of State, having also been statutorily delegated these functions, and oversees the development of any changes to the qualifications once they are approved. Under other delegated powers it also assesses the similarity of an overseas country's law and practice on the audit of accounts to that in the UK, and therefore of the practical experience in audit gained in that country, so that practical training based on that experience can contribute to obtaining a UK qualification.

5.6 This amendment will enable practical training in audit to be provided by an approved overseas auditor in any overseas country, including those outside the EEA, under appropriate arrangements. Prior to this amendment, only auditors granted eligibility for appointment in the UK or the EEA could provide at least two thirds of the training that could be recognised by the UK qualifying bodies and contribute to a UK audit qualification. In future, an auditor who is eligible for appointment in any jurisdiction may be approved as a training provider, if the law and practice in the jurisdiction has been assessed by the FRC, under the existing power in paragraph 9(2) of Schedule 11 to the Act, as being sufficiently similar to that in the UK.

5.7 The previous exclusion of an auditor from a jurisdiction beyond the EEA has presented a barrier to other non-EEA auditors becoming UK qualified auditors because at least two thirds of the practical training they could obtain in their home country had to be provided by an individual in that country carrying the necessary eligibility in the UK or an EEA state.

5.8 Overall, this instrument will provide potential benefits to the UK skills base in audit, and the ability for UK and overseas audit firms to transfer specialist skilled personnel between their respective jurisdictions, so UK auditors and their firms can take advantage of new commercial opportunities and maintain and improve audit quality.

What was the previous policy, how is this different?

5.9 Prior to the making of the amendments in this instrument, only individuals who have been eligible for appointment as statutory auditors in the UK, or who have a comparable eligibility in an EEA state, have been able to provide at least two thirds of the practical training for a UK audit qualification. Other overseas auditors have effectively been excluded.

5.10 Although the Act grants powers only for the FRC to enter into MRAs, recognition overseas of the various components of a UK audit qualification can also be facilitated by MRAs between the Recognised Qualifying Bodies (RQBs) in the UK and their overseas counterparts on components of qualifications. For instance, an RQB and overseas qualifying body can agree the mutual recognition of certain examination credit. In theory, the framework also allows an agreement so that practical training obtained overseas will be recognised in the UK. However, this is only where the training has been provided by a person who is eligible for appointment as a statutory auditor in the UK or who has a comparable approval an EEA State. The effect of this instrument, however, is that it will now also be possible for the bodies to agree the mutual recognition of periods of practical training provided by an individual with a comparable approval in any jurisdiction, subject to certain conditions being met.

5.11 Prior to the making of this instrument, trainee EEA auditors have had greater access to the UK's audit profession than trainee auditors in other overseas jurisdictions. In overseas countries outside of the EEA it is very unlikely that a UK or EEA state approved auditor would be available to provide practical training. This requirement was introduced when the UK was a part of the European Union (EU) in compliance with the EU Audit Directive, under which the other EU Member States and the EEA EFTA states were required to implement reciprocal legal requirements. The effect was that UK auditors could provide practical training in other EEA states. However, this is no longer possible for UK auditors since the UK's exit from the EU.

5.12 This instrument therefore removes the previous preferential treatment of EEA auditors, which is no longer reciprocated, and instead puts in place arrangements where all overseas auditors are all treated on a comparable basis. To do this it takes advantage of the FRC's existing powers to determine the similarity of law and practice on audit in an overseas country, so that auditors approved as eligible for appointment in those countries may also be approved to provide the required practical training. EEA auditors approved previously may continue to provide the required practical training even if the law and practice on audit in the relevant EEA state has not been determined as being similar to that in the UK. The instrument achieves this via a saving provision.

6. Legislative and Legal Context

How has the law changed?

6.1 The amendments in these Regulations, revoke and replace provisions in section 1221 of, and paragraph 9(4) and (5) of Schedule 11 to, the Act, which relate to the approval of overseas audit qualifications and the requirement for a minimum level of practical training for recognition of a professional qualification for UK auditors under appropriate arrangements.

Why was this approach taken to change the law?

6.2 The amendments made by this instrument are minor amendments to legislation that will broaden the potential jurisdictions, and further clarify the requirements that must be met, where an auditor there wishes to become a qualified auditor in the UK. The requirements to become a qualified auditor remain largely the same as before, with modest changes described above made for the reasons given.

7. Consultation

Summary of consultation outcome and methodology

7.1 The Department for Business and Trade conducted a targeted consultation with the regulatory body FRC and chartered accountancy bodies between August 2023 – January 2024. Stakeholders were identified due to their status as both RQBs (that offer UK recognised professional qualifications in statutory audit and oversee the practical training of individuals seeking qualification), and as Recognised Supervisory Bodies (RSBs, that approve individuals as being eligible for appointment as statutory auditors so that they may sign audit reports on behalf of appointed audit firms).

7.2 The Department for Business and Trade met stakeholders through a series of meetings to test the proposals to amend section 1221 of, and paragraph 9 of Schedule 11 to, the Act. A questionnaire was also sent to stakeholders to gather feedback on the impact and opportunities that would result from the amendments. Regular discussions have continued with the regulatory bodies on the amendments and their application. Reception from stakeholders has been positive and they have welcomed this instrument.

7.3 The Department has also consulted with the Department of the Economy in Northern Ireland as company law is formally a transferred matter in Northern Ireland and this legislation extends to Northern Ireland by agreement of the Northern Ireland Executive.

8. Applicable Guidance

8.1 No guidance is being published with this legislation.

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A full Impact Assessment has not been prepared for this instrument because of the likelihood of a small and only gradual response by the accountancy regulatory and qualifying bodies affected and by those providing and undergoing practical training, The main objective of this instrument is to increase the supply of specialist audit expertise in the UK. This instrument is intended to provide clarity in the making of MRAs and remove legislative barriers to the recognition of equivalent practical training carried out overseas. These barriers reduce the attractiveness of the UK to overseas auditors. The benefits are likely to be indirect and hard to predict and our judgement is that the direct benefits to business are likely to be marginal and below the de minimis threshold.

Impact on businesses, charities and voluntary bodies

9.2 There is no significant impact on business, charities or voluntary bodies because the effects of the legislation are likely to be small and gradual across all businesses.

9.3 This instrument does not impact small or micro businesses as most of these will take advantage of the audit exemption offered in the Act. Those whose accounts undergo audit voluntarily, or who are excluded from audit exemption will only experience marginal effects resulting from the amendments in this instrument because most trainee auditors train in, and then continue to work on, the audits of larger businesses.

9.4 There is no significant impact on the public sector because the changes made by this instrument affect the qualifications of auditors of incorporated businesses very largely in the private sector.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 As this instrument is made under the relevant European Union Acts (as defined at 13.1), no review is required. The Department for Business and Trade intends to carry out engagement with the FRC to monitor progress and impact of the legislative changes.

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 This instrument was laid before Parliament on 12 March 2025 for sifting by the Sifting Committees as it includes changes made under the Retained EU Law (Revocation and Reform) Act 2023 and it was proposed it should be subject to approval under the negative resolution procedure. The relevant Sifting Committees of the House of Commons and the House of Lords confirmed they were content with that proposal on Wednesday 19 March and Wednesday 26 March respectively.

12. European Convention on Human Rights

12.1 The Minister for Employment Rights, Competition and Markets, Justin Madders, has made the following statement regarding Human Rights:

"In my view the provisions of the Companies Act 2006 (Recognition of Third Country Qualifications and Practical Training) (Amendment) Regulations 2025 are compatible with the Convention rights."

13. The Relevant European Union Acts

13.1 This instrument is made, under sections 14(2) and 20(1)(b) of the Retained EU Law (Revocation and Reform) Act 2023 and therefore relates to the reform of assimilated law. It revokes and replaces provisions of retained EU law on audit qualifications and practical training in the Companies Act 2006 to provide clearer grounds on which mutual recognition arrangements may be put in place and to enable practical training providers to be approved where they are eligible for appointment as auditors in any jurisdiction, subject to certain requirements.

Sifting statement

13.2 The Minister for Employment Rights, Competition and Markets at the Department for Business and Trade has made the following statement regarding use of legislative powers in the Retained EU Law (Revocation and Reform) Act 2023:

"In my view Companies Act 2006 (Recognition of Third Country Qualifications and Practical Training) (Amendment) Regulations 2025 should be subject to annulment in pursuance of a resolution of either House of Parliament (i.e. the negative resolution procedure). This is because the changes made by this instrument are intended simply to make sure the framework meets its existing objectives more effectively than at present following the UK's exit from the European Union. The specific amendments made using powers in the Retained EU Law (Revocation and Reform) Act 2023 are intended to continue to enable the Financial Reporting Council and the UK's audit qualifying bodies to make sure that audit personnel are appropriately qualified, while also facilitating the recognition of qualifications and training of an appropriate standard provided overseas, without arbitrarily preferring the recognition of qualifications and training provided in some jurisdictions over that in others."