EXPLANATORY MEMORANDUM TO

THE STATUTORY AUDITORS AND THIRD COUNTRY AUDITORS (AMENDMENT) REGULATIONS 2026

2026 No. 431

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.

2. Declaration

2.1 Blair McDougall, the Minister for Small Business and Economic Transformation 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 can be contacted by email at the following address with any queries regarding this instrument: pauld.smith@businessandtrade.gov.uk. Alternatively, the department can be contacted by telephone: 020 4 551 0011.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 This instrument amends legislation originally made to prepare the audit regulatory framework in the United Kingdom (UK) for the UK's exit from the European Union (EU). The amendments are made to provisions in the Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2019 (SI 2019 No. 177 - 'the 2019 regulations') on the competent authorities of countries outside the United Kingdom ('third countries'), which are 'approved third country competent authorities' on the basis of the adequacy of their arrangements for the handling of audit working papers and investigation reports transferred to them from the UK.

4.2 The amendments to the 2019 regulations made by this instrument concern the approvals or provisional approvals of the competent authorities in two third countries: Most significantly, this instrument grants full indefinite approval, as an approved third country competent authority, to the New Zealand Financial Markets Authority (FMA), by inserting a reference to the FMA into the 2019 regulations. In addition, this instrument addresses the provisional approvals previously granted to two competent authorities of the Peoples' Republic of China, which have now expired. As these provisional approvals are no longer legally effective, the Government has taken the opportunity to remove references to those competent authorities, and the expiry dates, from the 2019 regulations.

4.3 The full indefinite approval of the FMA is granted by the Secretary of State on the basis of an assessment and recommendation provided by the Financial Reporting Council (FRC) as the audit regulatory authority for the UK. These assessments and determinations, of the adequacy of the arrangements of third country competent authorities for the handling of audit working papers and investigation reports transferred from the UK, accord with the framework in Part 4 of the Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2020 (SI 202 No. 108 - 'the 2020 regulations'). The Department for Business and Trade (DBT) commissioned the assessment of the FMA in the 2023/24 financial year.

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 that are part of 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 Schedule 2 to the 2019 regulations, to make two changes to the approvals granted to third country competent authorities based on the adequacy of their arrangements for the handling of audit working papers and investigation reports transferred to them from the UK. Almost all the approvals currently granted in Schedule 2 are the result of determinations made by the European Commission during the UK's membership of the EU, and during the transition period that applied as part of the UK's exit from the EU. Those determinations were set out in EU law by the European Commission in the form of Commission Decisions and implemented in a framework in the Companies Act 2006 that was then amended by the 2019 regulations to prepare for the UK's exit from the EU. With those amendments, all the approvals in UK law were set out in in Schedule 2 to the 2019 regulations.

5.2 While most of the EU determinations granted full approval to third country competent authorities, some granted provisional approval, which was on a time-limited basis. As a result, Schedule 2 to the 2019 regulations includes expiry dates alongside the approvals of certain third country competent authorities.

5.3 The 2019 regulations provided new powers for the Secretary of State to grant and revoke approvals of third country competent authorities by inserting section 1240B into the Companies Act 2006. Those powers also enabled the Secretary of State to put in place a framework setting out the basis on which future approvals would be granted or revoked. This was put in place in Part 4 of the 2020 regulations. It provides that determinations must be made by the Secretary of State of the adequacy of the arrangements in third countries for the handling of audit working papers and investigation reports transferred from the UK, via the making of regulations approving the relevant third country competent authorities. These determinations may be based on assessments by the FRC as the UK's audit regulatory authority. Under this

framework, a determination of adequacy and the resulting grant of approval may result in the grant of full or provisional approval; ie in the determination of the full indefinite adequacy of the arrangements or of their time-limited provisional adequacy.

What was the previous policy, how is this different?

5.4 The framework on the transfer of audit working papers and investigation reports from the UK is set out in sections 1253D to 1253F of the Companies Act 2006, and paragraphs 16A to 16AB of Schedule 10 to that Act ("the framework on audit transfers from the UK"). It provides that, where a third country competent authority has been granted approval or provisional approval, a transfer can then be made, which must be in accordance working arrangements agreed between the FRC and the relevant third country competent authority. The requirements as to the content of the working arrangements are set out in section 1253E, while the remainder of framework for transfers from the UK sets out other restrictions depending on the different circumstances in which transfers might be made. This includes transfers made by UK statutory auditors to the relevant third country competent authority, usually with the approval of the FRC, in addition to transfers by the FRC. It also includes transfers made via inspections by the relevant third country competent authority of the relevant audit working papers and / or audit investigation reports. Usually these must take the form of inspections conducted jointly by the relevant third country competent authority and the FRC. While section 1253E requires that the working arrangements must be reciprocal in several respects, the remainder of the framework makes their application a precondition to the transfer of audit working papers and inspection reports from the UK.

5.5 Among the other applicable requirements is that transfers must be made in accordance with requirements on the protection of personal data. The FRC's usual approach to compliance with this is only to put in place arrangements with countries that, in addition the determination of the adequacy of their arrangements under the audit regulatory framework, are also subject to a determination of the adequacy of their arrangements for the transfer of personal data under the UK's personal data protection framework. At present New Zealand is determined as having adequate arrangements under this framework.

5.6 In the case of the authorities of the People's Republic of China, no reassessment of the of the competent authorities has been conducted under the 2020 regulations, and the period of provisional approval has been allowed to expire. The expiry date of 14 November 2024 was specified in Schedule 2 to the 2019 regulations reflecting the expiry date in EU law. This instrument therefore now removes references from the 2019 regulations to each of the competent authorities of the People's Republic of China, and to the applicable expiry date for each one.

5.7 For the FMA, as the competent authority in New Zealand, the FRC will keep under review whether it might be appropriate to enter into working arrangements on the transfer of audit working papers and investigations reports. The adequacy of New Zealand under the UK's personal data protection framework means that it would be relatively straightforward to put these in place. Working arrangements are usually considered appropriate where UK companies trade securities on the markets of the relevant third country or where multinational groups with parent undertakings there, that prepare audited consolidated accounts, have UK subsidiary companies that are audited here. In both these cases, it may be necessary for the FRC to be ready to transfer audit working papers or investigation reports to the relevant third country competent authority.

6. Legislative and Legal Context

How has the law changed?

6.1 The insertion of the reference to the FMA in New Zealand into Schedule 2 to the 2019 regulations, as an approved third country competent authority, by regulation 2(2)(c) of this instrument, enables the FRC to enter into working arrangements with it indefinitely for the transfer, between the UK and New Zealand, of audit working papers and investigation reports. Following the making of working arrangements, and in accordance with them and the framework on audit transfers from the UK, it will be possible for transfers of audit working papers and investigation reports to be made from the UK to the FMA in New Zealand.

6.2 The removal of references to the competent authorities of the People's Republic of China from Schedule 2 to the 2019 regulations by regulation 2(2)(a) and (b) of this instrument does not represent a change in the law because the approval of those third country competent authorities has already expired. Instead, these amendments merely remove references from Schedule 2, which it already makes clear are of no continuing legal effect.

Why was this approach taken to change the law?

6.3 The amendments made to Schedule 2 to the 2019 regulations by this instrument are necessary because the framework on audit transfers from the UK, which is assimilated law originating from when the UK was an EU member state, only permits the transfer of audit working papers and investigation reports in accordance with the requirements of that framework, including the requirements of working arrangements, which may only be put in place with an approved third county competent authority.

6.4 The amendments to the 2019 regulations in this instrument are made in a way that is comparable to amendments made for similar purposes previously. This is illustrated by the following previous examples.

6.5 Regulation 2(3)(b) of the Statutory Auditors and Third Country Auditors (Amendment) Regulations 2022 (SI 2022 No. 762 - 'the 2022 regulations') revoked the expiry date relating the approvals of the two competent authorities in the United States of America referred to in Schedule 2 to the 2019 regulations. That amendment was made before the relevant expiry date took effect. It had the effect of granting those two third country competent authorities full approval in place of the previous time limited provisional approval that applied. The decision by the Secretary of State to grant full approval was based on an assessment by the FRC, which was commissioned by the Secretary of State in the 2021/22 financial year.

6.6 Before that, regulation 3 of the 2020 regulations made three amendments to Schedule 2, two of which are relevant. First, regulation 3(a) inserted the references to the competent authorities of the People's Republic of China into Schedule 2 that are now being removed. In that case, this reflected the determination of the provisional time limited adequacy of China in EU law relating to those authorities' arrangements for handling relevant transfers from the EU. The previous approach taken there is consistent with the insertion of the reference to the FMA in New Zealand, which is made by regulation 2(2)(b) of this instrument. In this case no expiry date is inserted however, because the FMA is being granted full indefinite approval, and in this case approval is granted based on an assessment by the FRC. Second, regulation 3(b) removed the reference from Schedule 2 to the 2019 regulations to the competent authority of Indonesia following the expiry of its period of provisional adequacy in EU law on 31 July 2019. Originally reference had been included both to the

competent authority of Indonesia and to the expiry date in EU law in readiness for the framework in Schedule 2 to take effect at the completion of the UK's exit from the EU. That process then took until after the expiry date in EU law had taken effect. The reference in the 2019 regulations referring to a competent authority remained, while making clear its period of provisional approval had expired. The 2020 regulations were then also made before the completion of the UK's exit from the EU. They removed the reference to the competent authority of Indonesia and the applicable expiry date, as those references were no longer necessary. This approach is consistent with that taken in regulation 2(2)(a) and (b) of this instrument relating to the competent authorities of the People's Republic of China.

7. Consultation

Summary of consultation outcome and methodology

7.1 The Department for Business and Trade consulted with the FRC before commissioning the assessment of the FMA in New Zealand in respect of the adequacy of its arrangements for the handling of audit working papers and investigation reports transferred from the UK. It also consulted with the FRC on the decision not to commission reassessments of the competent authorities of the People's Republic of China.

7.2 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 instrument.

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 small number of companies and audit firms affected. The main types of UK company for whom audit working papers and investigation reports might need to be transferred to New Zealand under these regulations are those that either trade securities on capital markets there, or that are audited UK subsidiaries of parent undertakings incorporated there. The numbers of these companies in the UK are thought to be small.

9.2 Although the agreement of working arrangements may also facilitate some transfers of audit working papers and investigation reports to the UK from New Zealand, these transfers are likely to be possible in any case already. Furthermore, to the extent that companies incorporated in New Zealand, and their auditors there, are affected by these regulations, they are overseas businesses and therefore any impact on them is not required to be assessed as part of an impact assessment relating to burdens on UK businesses.

Impact on businesses, charities and voluntary bodies

9.3 There is no, or no significant, impact on business, charities or voluntary bodies because most of these do not trade securities on capital markets in New Zealand and are not audited UK subsidiaries of parent undertakings incorporated there.

9.4 There is no, or no significant, impact on the public sector because most audited companies in the public sector do not trade securities on capital markets and are not UK subsidiaries of parent undertakings incorporated in New Zealand as they are owned within the UK public sector. Public sector companies that are part of central government are also often able to take advantage of exemption from statutory audit under the Companies Act 2006.

9.5 There is no, or no significant, impact on the small or micro businesses as most of these in the UK will take advantage of exemption from statutory audit under the Companies Act 2006. Those whose accounts undergo statutory audit voluntarily, or that are excluded from audit exemption, are unlikely to trade securities on markets, particularly those outside the UK, due to their small size. If they are part of multinational groups with parent undertakings in New Zealand that prepare consolidated accounts and are audited, paragraph 9(2) of Schedule 1 to the Statutory Auditors and Third Country Auditors Regulations 2016 already permits the transfer of audit working papers for the purpose of the audit of those parents' consolidated accounts, so this instrument is of only marginal impact.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 This instrument does not include a statutory review clause and, in line with the Small Business, Enterprise and Employment Act 2015 (c. 26), the Minister for Small Business and Economic Transformation at the Department for Business and Trade, Blair McDougall, has made the following statement: "A review provision is not included in respect of the provisions of the Statutory Auditors and Third Country Auditors (Amendment) Regulations 2026 or the amendments made by those regulations to the Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2019, because these provisions and amendments have no, or no significant, impact on business, charities or voluntary bodies".

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 None.

12. European Convention on Human Rights

12.1 As this instrument is subject to the negative resolution procedure and does not amend primary legislation, no statement is required.

13. The Relevant European Union Acts

13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 ("relevant European Union Acts"). However, it is made under section 1240B of the Companies Act 2006, which was inserted into that Act by the 2019 regulations using powers provided in the European Union (Withdrawal) Act 2018. It also amends Schedule 2 to the 2019 regulations, which itself was made under powers in that Act.

13.2 The new powers in section 1240B of the Companies Act 2006 enabled provisions to be made on the approval or provisional approval of third country competent authorities based upon the adequacy of their arrangements for the handling of audit working papers and investigation reports transferred to them from the UK. Prior to the UK's exit from the EU, similar powers of approval were granted to the European Commission in EU law and were exercised in Commission Decisions whose effect then had to be reflected in UK law. Following the UK's exit from the EU, these approvals must now be granted by the Secretary of State in accordance with section 1240B of the Companies Act 2006 and provisions in the 2020 regulations, which themselves were made using the section 1240B powers.

13.3 Consistent with the above approach, this instrument amends the framework of approvals and provisional approvals of third country competent authorities in Schedule 2 to the 2019 regulations. That Schedule took effect with the completion of the UK's exit from the EU. In so far as it relates to third countries beyond the EU, in large part, that Schedule has continued, up to now, to reflect the framework that applied in EU law at that point. The amendments in this instrument however, relating to the FMA in New Zealand, change the effect of that Schedule. They do this by enabling the FRC to enter indefinite working arrangements with the FMA, so that audit working papers and investigation reports can be transferred to it.