

# PARLIAMENTARY DEBATES

HOUSE OF COMMONS  
OFFICIAL REPORT

First Delegated Legislation Committee

## DRAFT STATUTORY AUDITORS, THIRD COUNTRY AUDITORS AND INTERNATIONAL ACCOUNTING STANDARDS (AMENDMENT) (EU EXIT) REGULATIONS 2019

*Monday 9 September 2019*

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**Friday 13 September 2019**

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**The Committee consisted of the following Members:**

*Chair:* MR VIRENDRA SHARMA

- |   |  |
|---|--|
| † Beckett, Margaret ( <i>Derby South</i> ) (Lab)              | † Murray, Mrs Sheryll ( <i>South East Cornwall</i> ) (Con)   |
| † Crabb, Stephen ( <i>Preseli Pembrokeshire</i> ) (Con)       | † Selous, Andrew ( <i>South West Bedfordshire</i> ) (Con)  |
| † Duguid, David ( <i>Banff and Buchan</i> ) (Con)             | † Smith, Nick ( <i>Blaenau Gwent</i> ) (Lab)   |
| † Esterson, Bill ( <i>Sefton Central</i> ) (Lab)              | † Stevens, Jo ( <i>Cardiff Central</i> ) (Lab)   |
| † Farrelly, Paul ( <i>Newcastle-under-Lyme</i> ) (Lab)        | † Stewart, Iain ( <i>Milton Keynes South</i> ) (Con)   |
| † Graham, Luke ( <i>Ochil and South Perthshire</i> ) (Con)    | † Tolhurst, Kelly ( <i>Parliamentary Under-Secretary of State for Business, Energy and Industrial Strategy</i> ) |
| † Grant, Peter ( <i>Glenrothes</i> ) (SNP)                    |  |
| † Heald, Sir Oliver ( <i>North East Hertfordshire</i> ) (Con) | Brad Albrow, <i>Committee Clerk</i>  |
| † Hollingbery, George ( <i>Meon Valley</i> ) (Con)            |  |
| † Jones, Susan Elan ( <i>Clwyd South</i> ) (Lab)              |  |
| † Murray, Ian ( <i>Edinburgh South</i> ) (Lab)                | † <b>attended the Committee</b>  |

# First Delegated Legislation Committee

Monday 9 September 2019

[MR VIRENDRA SHARMA *in the Chair*]

## Draft Statutory Auditors, Third Country Auditors and International Accounting Standards (Amendment) (EU Exit) Regulations 2019

4.30 pm

**The Parliamentary Under-Secretary of State for Business, Energy and Industrial Strategy (Kelly Tolhurst):** I beg to move,

That the Committee has considered the draft Statutory Auditors, Third Country Auditors and International Accounting Standards (Amendment) (EU Exit) Regulations 2019.

It is a pleasure to serve under your chairmanship, Mr Sharma. Since the UK's 2016 referendum decision to leave the EU, the Department for Business, Energy and Industrial Strategy has undertaken a significant amount of work preparing for a range of potential outcomes. The best outcome is for the UK to leave with a deal, and we continue to put forward serious and credible proposals for that. Although we remain confident, we must and will continue the work of preparing for no deal.

The Committee may be aware that around the turn of the year I laid regulations before Parliament to address deficiencies arising from the withdrawal of the United Kingdom from the European Union in the fields of accounting and audit. They did not implement new policy but did grant new powers and responsibilities to the Secretary of State and the Financial Reporting Council. Continuing that process requires further regulations now. Although the fundamental elements of current UK accounting and audit regulation will remain the same after exit, legislation has had to be amended to ensure its effective working once the UK has left the EU.

The accounting and audit directives set out the requirements on the accounts and audit of most incorporated businesses, as well as a framework of standards. The directives also set out the responsibilities of the competent authorities for accounting and audit. Meanwhile, under the EU's international financial reporting standards regulation, standards are set for accounting by parent companies of groups, which apply if those companies issue shares that are admitted to trading on regulated markets. Another regulation—the audit regulation—sets additional requirements on the statutory audit of those businesses defined as public interest entities: banks, building societies, insurers and issuers of shares or debt securities on regulated markets.

To the extent that those EU regulations are not repealed, they form part of retained EU law under the European Union (Withdrawal) Act 2018. Our aim is to ensure that the framework for accounting and audit

regulation works effectively following the UK's withdrawal from the EU, and the regulations take further steps to help facilitate that.

Under the audit directive, the European Commission has powers to grant equivalence to third countries for their audit regulatory framework, and adequacy to third countries' competent authorities for their framework on audit regulatory co-operation. These measures facilitate international trade and investment. The Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2019 transferred those powers to the Secretary of State and provided powers to set out the criteria and procedure for assessment, equivalence or adequacy status decisions in the future, which will be granted by regulations under the negative procedure. These regulations ensure that, irrespective of whether a withdrawal agreement is reached, the Secretary of State can make regulations after our exit from the EU to set out the framework for future assessment of equivalence and adequacy by the UK regulator. They will also enable us to grant equivalence and adequacy status to some third countries that have had their applications under consideration in the EU since March of this year.

The regulations also complete the process of extending powers to the Financial Reporting Council—the UK's competent authority—making the final consequential amendments needed to extend the FRC's ability to regulate third-country auditors to include European economic area auditors and Gibraltar auditors. They also put beyond doubt that those EEA auditors who have already registered as statutory auditors in the UK will retain their status after exit.

The regulations also make an important change to the audit exemption framework. In common with the exemptions in the accounting framework for subsidiaries, the subsidiary audit exemption will not be available unless a subsidiary has a UK parent. This instrument corrects an error in the previous audit SI affecting the frequency of audit inspections required for auditors of public interest entities.

On accounting standards, the instrument revokes some EU regulations relating to the adoption or amendment of the IFRS within the EU. Without revocation, the regulations would be brought into domestic law by the EU (Withdrawal) Act. However, the International Accounting Standards and European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2019 have already made provision for what will be the international accounting standards for the UK at exit day. The revocations remove any duplication and potential confusion. They also reflect changes in EU adopted international accounting standards issued or identified since the earlier accounting SIs were made.

The Government have carried out a de minimis impact assessment of the instruments as the overall costs to business are expected to be small. It confirmed that the additional impact on business of the changes in the SI is a cost of approximately £930,000, which derives from the amendment to the subsidiaries audit exemption. Only limited sectors are affected by each of the changes. Such limited impact is counterbalanced by what was actually an overall beneficial effect of the changes in the first audit EU exit SI, which was assessed as saving businesses approximately £2.96 million per year.

In conclusion, the regulations aim, wherever possible, to provide continuity for businesses operating in the audit sector and to ensure that UK companies continue

to benefit from global trade and investment. If the UK leaves the EU without an agreement, the measures contained within the regulations will be critical in ensuring that the audit regulatory framework in the UK works effectively. I therefore commend the draft regulations to the Committee.

4.37 pm

**Bill Esterson** (Sefton Central) (Lab): It is a pleasure to serve under your chairmanship, Mr Sharma, and to make the most of this limited opportunity to sit in Parliament. Before I go into the SI, I could not help noticing that the Government still have a majority on this Committee. The Government have nine Members, and the Opposition only eight. I wonder why that is, because the Government have lost their majority in the House of Commons over the past few weeks. Will you confer with the Clerks, Mr Sharma, as to whether the Government should still have a majority on the Committee?

**The Chair:** I am advised that it is not up to this Committee; it is up to the Selection Committee. I am sure the message will go back to it for future consideration if the situation is the same.

**Bill Esterson:** Thank you for taking that point on board, Mr Sharma. I realise it was not a decision you could adjudicate on, but it is an important point because this is yet another example of how the Government operate and ignore the democracy of the House of Commons at every available turn. They should have arranged not to have a majority in this Committee. *[Interruption.]* The hon. Member for South East Cornwall can intervene and challenge me on that point if she does not agree, or if she thinks that a party that is 43 or 45 seats short of a majority—

**The Chair:** Order. I think the point is noted.

**Bill Esterson:** Thank you, Mr Sharma.

Now, to the matter at hand. We are faced with regulations and, as ever, the Minister did her best to make them appear to be a matter of minor change, but the House of Lords Secondary Legislation Scrutiny Committee said the

“range and magnitude of the changes are significant: the Regulations make changes to 15 items of legislation and include a sub-delegation of powers to UK regulators and extend a ministerial power of direction.”

The Minister did mention that.

**Kelly Tolhurst:** I did.

**Bill Esterson:** Well, the Minister mentioned the ministerial power of direction; I am not sure that she spoke about just how far reaching the changes are. The Lords Committee expressed its

“concern about the scale of the challenge facing financial services firms in adjusting to these changes.”

Yet when we turn to paragraph 10 of the explanatory memorandum, we find that no consultation was carried out with the financial services sector on these far-reaching changes, which will affect financial services firms. Sadly, that problem has bedevilled such statutory instruments, more than a few of which the Minister and I have considered, including the one she mentioned.

There is also a link to the 2013 report from the Parliamentary Commission on Banking Standards, which was chaired by members of the Minister’s own party. It was jointly chaired by a Member of the House of Commons—the then chair of the Treasury Committee, Andrew Tyrie—and a Member of the House of Lords. They found great concerns about the robustness of our audit regulations and called for wide-ranging changes. Those changes have not happened. The relevance of those points centres on the scandals surrounding companies the collapse of which related to a lack of audit, such as British Home Stores, Patisserie Valerie and Carillion.

The link to the regulations is important, because the Government are proposing to adopt the IFRS system, which is run by a private entity in Delaware in the United States and overseen by the European Commission. I wonder how the Government propose to accept arrangements whereby, once we have left the European Union, the European Commission will have oversight of our financial reporting standards. The Government are making a major change to those standards, tacked on to the regulations. Such a significant change clearly should be fully scrutinised, should have been the subject of consultation, and is very difficult for us to support.

I did some consultation of my own. I asked the Institute of Chartered Accountants in England and Wales for its assessment of the regulations. It confirmed the concerns I have just outlined regarding the Government’s proposed elimination of the exemption for EU companies with a UK-based subsidiary. It wants the Government to say what the timescales will be, because it is not clear from the regulations.

Beyond those concerns from the ICAEW, the proposed amendment is not just minor or technical. The controversies that I mentioned regarding audit mean that if such changes are to be made, they should be subject to much wider consideration. The consideration recommended by the 2013 report from the Parliamentary Commission on Banking Standards gives us a good place to start.

There are some significant concerns about the proposed changes, which are significant changes. It is simply not the case, as far as I can see from the commentary that I have received, that there will be no significant impact on the private, voluntary or public sectors. The lack of an impact assessment yet again is concerning. The Minister will no doubt say that the Government are preparing responsibly for Brexit, with or without a deal, but I am afraid that the lack of an impact assessment, the lack of consultation and the way in which standards have been tacked on to a set of regulations that are actually of a very different nature show that today’s statutory instrument should not have been introduced in its present form. For those reasons, we will oppose the regulations.

4.45 pm

**Peter Grant** (Glenrothes) (SNP): I am pleased to make a brief contribution. In the Chamber, several hon. Members are still paying tribute to the Speaker; shortly, there will be an application for an emergency debate to force the Government to come clean about what on earth is going on with Prorogation and much else; later, there will be another attempt to force a general election. In Westminster Hall, our colleagues are debating a petition that was possibly the quickest ever to reach more than 1 million signatures. We—the lucky few—are

[Peter Grant]

here talking about the Statutory Auditors, Third Country Auditors and International Accounting Standards (Amendment) (EU Exit) Regulations 2019. These regulations will not be the news headlines tonight, but perhaps they should be.

If we get this wrong—I think the Government are still getting it wrong on their second attempt—the consequences will be catastrophic for businesses, homes, jobs and the suppliers of big companies. That is why it is important for us to get it right this time. Part of the reason that we are discussing these regulations is that we did not get them right last time, because everything had to be done in such a panic-stricken rush that they were not as watertight as legislation needs to be. We should have been out of the European Union five months ago. We would have been out six months ago without a deal, if some hon. Members on the Government Benches had had their way. Even on such fundamental questions as who regulates those who regulate the conduct and misconduct of multinational businesses, however, we have still not got it right.

As the hon. Member for Sefton Central mentioned, auditors tend to be anonymous most of the time, but when we look at the causes of almost all the huge corporate failures, of which Carillion is perhaps the most recent mega-failure, there are always big questions to be asked about why the auditors did not do something and how they could not have noticed. I should mention that although I am a qualified member of the Chartered Institute of Public Finance and Accountancy, which may be why I was given the privilege of coming here this afternoon, I am not qualified to conduct statutory company audits, so I do not have an interest to declare.

As well as the questions that always come up about what the auditors were doing, the inquiry almost always concludes, although it is not inevitable, that the auditors did not break any rules at the time. We have had to completely review—realign, reset and turn inside out—the structure of the institutions that regulate statutory auditors and their profession a number of times. Try as we might, we will always struggle to keep up with the multinational chancers who look for every minor loophole in any regulation to allow their misconduct to go undetected for as long as possible—and often unpunished forever.

It is therefore important to get it right this time. The hon. Member for Sefton Central highlighted some of the concerns. When there are a lot of statutory instruments to get through, there is a danger that among some relatively minor consequential technical stuff that nobody could object to, significant changes to Government policy and to legislation are slipped in, in terms that should be brought as specific items for the whole House to consider, rather than in Committee on the upper corridors of the House of Commons on a wet Monday afternoon. I understand that quite a lot of what is in the regulations needed to be put in there, but the Committee needs to say to the Government that it cannot accept the regulations as they are.

**Luke Graham** (Ochil and South Perthshire) (Con): I am a member of the Chartered Institute of Management Accountants. I am on the Committee and I am happy to dig into the detail, but I am not getting detail from Opposition Members, although I am hearing opposition

from them. The hon. Gentleman says that there are things in the regulations to be worried about; perhaps he could outline them for us, as is the purpose of the Committee, point by point and subsection by subsection. I am happy to sit here and go through it. We have other business in the House of Commons, but as he rightly points out, this is an enormously important issue for the whole United Kingdom—it applies to the whole United Kingdom—for my constituents and for the businesses they are in. I ask him to please outline the details, so we can go through them together in a cross-party way.

**Peter Grant:** The hon. Gentleman agrees with some of the points I am making. As he helpfully points out, if Government Members were all that interested in going through the regulations in fine detail, perhaps they should have asked professionals in the various accounting and auditing institutions before the Committee. I have no doubt that Government Members will rise to speak in support of the regulations. When they do so, perhaps they will tell the Committee what could have gone disastrously wrong if they had taken the time to get the policy right on their third attempt, and asked the statutory accounting and audit bodies what the regulations would do.

**Mrs Sheryll Murray** (South East Cornwall) (Con): Perhaps the hon. Gentleman could help me by telling us, as my hon. Friend the Member for Ochil and South Perthshire asked him to do, which specific parts of the regulations he objects to.

**Peter Grant:** It has already been pointed out. As I said, if there has not been consultation with the bodies whose purpose it is to regulate the profession, why would the Government ask a group of lay people to agree the regulations?

**Mrs Murray:** Will the hon. Gentleman give way?

**Peter Grant:** No, I will not give way again. The hon. Lady will get a chance to speak if she wishes. I would be interested to know why the Government did not have that consultation. Why are they making significant changes to policy during a process that the House agreed could be used to make technical, consequential, minor and non-controversial changes, of which there would need to be millions to get us even vaguely ready for 31 October? Why are they trying to put in much more significant and substantive changes that should have been tested on the Floor of the House before they passed into law?

**Sir Oliver Heald** (North East Hertfordshire) (Con): Will the hon. Gentleman give way?

**Peter Grant:** I can see that lots of Members want to speak, so perhaps the best thing is for me to sit down and give them a chance to do so.

4.51 pm

**Kelly Tolhurst:** I thank the hon. Member for Sefton Central for his comments, but I must pick him up on one point. He questioned whether the Government respect democracy. We have sat across from each other

numerous times in Committees this year, and I point out to him that respecting democracy is exactly what we are doing. The regulations ensure we are fit and ready for when we exit the European Union. That is respecting democracy and the 2016 democratic vote. I need to point that out, and it is exactly why my Department has been doing the work that is required for us to ensure that we are fit and ready to leave with or without a deal.

I remind the Committee that the regulations are part of what will enable us to ensure that the EU retained law that comes into UK law is fit and proper for when we leave the European Union. We are ensuring that we can communicate that to business, and that the current laws will continue to operate correctly in the UK. As the hon. Member for Glenrothes pointed out, the limitations in the withdrawal agreement set out what the Government can do when bringing secondary legislation through the House. He will note that the only change in the regulations is to ensure the smooth and effective running of regulatory systems when we leave.

Members also commented on the quality of audit and on their concerns about the performance of some UK companies. As the hon. Member for Sefton Central will know, we had the Sir John Kingman review of the Financial Reporting Council, and the Government are working through that and consulting where possible to make modifications and changes within the FRC. That ongoing piece of work by Government is not necessarily completely related to these regulations.

The hon. Gentleman will know that the IFRS is a high-quality, internationally accepted and supported set of financial reporting standards that is regarded as a benchmark throughout the world by listed companies.

**Peter Grant:** The Minister seems, rightly, to be recognising the importance of that organisation of experts. Why will the Government not listen to other organisations of experts in their consideration of the Brexit proposals?

**Kelly Tolhurst:** I am here to speak to the regulations that are in front of us. I assure the hon. Gentleman that the experts in the Department for Business, Energy and Industrial Strategy, as well as our stakeholders and partners across the sectors, have been spoken to. I challenge him to name the organisations that I have ignored or chosen not to speak to.

**Peter Grant:** The Minister will be aware that there are six recognised chartered accounting bodies in the United Kingdom. Can she name the ones that were consulted over these regulations, or is she saying that those organisations are not experts?

**Kelly Tolhurst:** As part of our ongoing engagement with stakeholders across all the Department's responsibilities, we have regular dialogue with those organisations, whether it be on this statutory instrument or on any of the Department's other business.

**Sir Oliver Heald:** Is it not correct to say that the hon. Member for Glenrothes has not pointed in detail to a single complaint about these regulations, and his speech is just a general waffle? Does my hon. Friend agree that

as the Scottish National party receives £1.2 million in Short money to do research on things like this, we should have a rebate?

**Kelly Tolhurst:** My right hon. and learned Friend is quite right. The hon. Member for Glenrothes has not mentioned the particular point that we have made more expressive, as the ICAEW asked us to do, in these amended regulations. That is a clear example of where we have listened to the professionals in the industry and chosen to respond to their requests as clearly as we can.

**Luke Graham:** I will perhaps try to articulate some of the points that the hon. Member for Glenrothes was trying to make. The regulations are designed to ensure that international accounting standards are still operational in the UK on EU exit day, incorporating the aspects of EU law that we are meant to incorporate. Essentially, the regulations fill in the gaps.

I ask my hon. Friend two things. First, if she does not have it with her today, will she make available the gap analysis that the Department undertook—between the IFRS, the IAS and the UK generally accepted accounting practice—to make sure that there are no gaps, and that the regulations are sufficient to satisfy all the professional bodies around the UK?

Secondly, has there been consultation with the International Accounting Standards Board, which is the governing body for IFRS? My hon. Friend is quite right to say that bodies in the UK have been consulted; it has been made explicit that the ICAEW has been consulted. It would be good to know whether the Institute of Chartered Accountants of Scotland has also been consulted, because, as a United Kingdom, we have a united internal market.

I would be quite happy to receive the answers to those questions as a follow-up, because I know that there is a lot of detail in the regulations. Opposition Members have completely failed to raise specific points that constitute a substantive opposition to this statutory instrument.

**Kelly Tolhurst:** I will happily provide my hon. Friend with any advice that we have available. I point out to hon. Members that these regulations constitute an amendment to, and an extension of, the statutory instrument that was laid before and passed by this House at the beginning of the year. They particularly focus, as I outlined in my opening speech, on aspects to do with subsidiaries. They also correct an omission of three words, which it was important to do to ensure that the regulations expressed the true intention behind the original statutory instrument.

I emphasise that as part of the Department's role in preparing for EU exit and making sure that we are in the best possible place to leave the European Union, with or without a deal, we have engaged continuously with stakeholders. Quite rightly, as Ministers, we have challenged our officials within the Department and our stakeholders, when we have had the opportunity to do so.

**Bill Esterson:** That is interesting, because I have a briefing note from the ICAEW here. It raises concerns, which I went through earlier, about regulation 4, on the loss of EEA subsidiary exemption, and regulation 6, on

[Bill Esterson]

EEA qualification for auditors; I did not spend as long on that earlier. I mentioned some other concerns that had been raised with me by professional bodies. It does not seem, from anything that the Minister has said, as though she has had those discussions with the ICAEW. It does not seem to me as though she has had that note from the ICAEW, or those concerns have been raised with her. Perhaps she could clarify the situation for me. Did she receive those concerns from the ICAEW before this meeting?

**Kelly Tolhurst:** I can confirm that officials in the Department have been speaking to the ICAEW. As I outlined in my response to my hon. Friend the Member for Ochil and South Perthshire, we have made something explicit in these regulations on the back of our conversations with the ICAEW. Those conversations are ongoing and will continue, as I laid out in my opening speech, because we are to bring forward the assessment framework in a further statutory instrument.

The hon. Member for Sefton Central asked how we would cope with the fact that the European Commission was no longer making these opinions or decisions. The statutory instruments that we have made give these powers to the Secretary of State, thereby enabling parliamentary scrutiny of decisions and the ability to delegate responsibilities.

The hon. Gentleman is quite right that we have had many conversations about impact assessments in our debates on statutory instruments as part of the EU exit programme. He will notice that a de minimis assessment took place, because the level of impact was below £5 million. As I outlined in my opening remarks, the overall benefit from the statutory instruments will be a reduction of £2 million per year.

The hon. Member for Glenrothes asked why we are bringing this forward now, and why we did not do it in the original statutory instrument earlier in the year. The regulations before us were not needed for exit day, but because we have had the opportunity to extend our leaving date to 31 October, we have been able to consider them prior to exit day.

As the UK exits the EU, we are committed to maintaining the integrity of the UK system for regulatory oversight of audit. The regulations contribute to that by clarifying

and building on the approach to oversight of the audit profession following our withdrawal from the EU that we began to set out in the original regulations at the start of the year. Like those regulations, this statutory instrument does not introduce a change in policy, as I have explained. The fundamental elements of the current statutory audit legislation will remain the same after exit. These regulations make only a small number of further amendments that are necessary to ensure that audit legislation remains operable in the UK following our withdrawal from the EU.

The regulations will mean that the UK system for regulatory oversight remains coherent and understandable, and they will enable us to do more on this over the coming months, irrespective of the outcome of the EU exit negotiations. I regret that the Opposition have decided that they are not prepared to support the regulations, which would give business and stakeholders consistency and clarity about how the market will work as we leave the European Union. I commend the regulations to the Committee.

*Question put.*

*The Committee divided: Ayes 9, Noes 8.*

#### **Division No. 1]**

#### **AYES**

Crabb, rh Stephen  
Duguid, David  
Graham, Luke  
Heald, rh Sir Oliver  
Hollingbery, George

Murray, Mrs Sheryll  
Selous, Andrew  
Stewart, Iain  
Tolhurst, Kelly

#### **NOES**

Beckett, rh Margaret  
Esterson, Bill  
Farrelly, Paul  
Grant, Peter

Jones, Susan Elan  
Murray, Ian  
Smith, Nick  
Stevens, Jo

*Question accordingly agreed to.*

*Resolved,*

That the Committee has considered the draft Statutory Auditors, Third Country Auditors and International Accounting Standards (Amendment) (EU Exit) Regulations 2019.

5.6 pm

*Committee rose.*