



Financial Reporting Council

Feedback Statement and Impact Assessment

Revised Ethical Standard

January 2024

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1. Introduction and Executive Summary

1. The Financial Reporting Council (FRC) is committed to acting as a proportionate and principles-based regulator and balances the need to minimise the impact of regulatory requirements on business, while working to support the delivery of high-quality audit and assurance work, to maintain investor and wider stakeholder confidence in audit and assurance.
2. In August 2023 the FRC issued a public consultation on proposed revisions to the Ethical Standard (ES). Our objectives were:
 - To take account of changes to the International Ethics Standards Board for Accountants (IESBA) Code of Ethics (including a significant expansion of the Code’s definition of a Public Interest Entity (PIE));
 - To respond to issues identified through audit inspection and enforcement cases;
 - To provide greater clarity in respect of specific prohibitions and requirements;
 - To allow the FRC to consult on whether to withdraw the Other Entities of Public Interest (OEPI) category introduced in 2019.
3. We received 24 responses to our exposure draft, including 12 from audit firms, 7 from professional bodies, and 3 from national audit agencies. We are extremely grateful for the volume and quality of the responses we have received.
4. In the table below we set out a summary of the feedback received and our responses. These fall into two categories:
 - (i) answers to the 8 specific questions in our call for feedback, and
 - (ii) significant other matters raised by practitioners.
5. We would further note that many of the comments we received related to defined terms and suggestions for improving these. We will take these forward immediately as part of an ongoing project to revise the FRC’s Glossary of Terms. We also commit below to dealing with specific issues through the FRC’s Technical Advisory Group (TAG).
6. Many of the high-level audit market policy issues that were raised by respondents in our consultation feedback (and set out in the table below) fall outside the FRC’s statutory remit, and are decisions for government. Nevertheless, we will communicate this feedback to the Department for Business and Trade.

Summary of Key Revisions, Consultation Feedback and FRC Responses

7. The consultation feedback received is set out below alongside the FRCs response:

Consultation question	ES reference	Consultation Feedback	Response
Q1: Do you agree with the proposal to remove the category of Other Entity of Public Interest (OEPI) from the Ethical Standard once the government's revised statutory definition of a UK Public Interest Entity (PIE) becomes effective?	5.43	<p>There were 21 responses to this question (11 firms/practitioners, 7 professional bodies and 3 national audit agencies). Respondents unanimously supported the removal of the OEPI category, but only once a final statutory definition becomes effective.</p> <p>The responses also overwhelming focussed on 4 critical issues:</p> <ul style="list-style-type: none"> • The need for any new definition of a UK PIE to be as simple and understandable as possible; • The need for alignment (again as far as is possible) between the various definitions of a UK PIE 	<p>For the sake of clarity, the FRC does not have the statutory powers to revise the definition of a UK PIE. That is a decision for government.</p> <p>However, the FRC does have the power to amend or withdraw the OEPI category, and given the unanimous nature of this consultation feedback it is highly likely that we will do so once details of any new statutory definition are known. We believe this will be an effective de-regulatory action, reducing complexity and helping the competitiveness of the UK economy.</p> <p>The FRC entirely agrees with the objective to have a simple and straightforward definition of a UK PIE, including one that is as closely aligned as possible to the IESBA Code.</p>

		<p>including the statutory definition, the FRC’s ES and the IESBA Code;</p> <ul style="list-style-type: none"> • The need for carefully thought through transitional measures when any new definition is finalised; and • The need to consider whether the new definition of PIEs should reflect the current relief for Private Equity fund management companies within the OEPI category. 	<p>The FRC also notes the multiple references in our feedback to potential issues for private equity fund management companies once the OEPI category is withdrawn. We will draw the government’s attention to these consultation responses.</p>
<p>Q2: Do you agree the revisions in respect of breach reporting by firms? Could they be further enhanced?</p>	<p>1.21-1.25 5.42</p>	<p>20 respondents commented on proposed changes to the ES relating to ethical breach reporting by the firms to the regulator (11 firms/practitioners, 6 professional bodies and 3 national audit agencies).</p> <p>3 of the 20 were supportive, but the remaining 17 were either against the changes or indicated that significant additional guidance might be need to</p>	<p>Ethical breach reporting by the firms to the FRC is now an established process which we believe helps drive better ethical behaviours, actions and outcomes.</p> <p>We propose to retain those changes to the ES which better align it to published policies and procedures.</p> <p>We recognise however (based on consultation feedback) that our proposed revisions in respect of inadvertent breaches are more likely to cause</p>

implement them effectively and consistently.

Comments focussed on changes which were made:

- To align the text of the ES to our published policies and procedures in relation to breach reporting; and
- On our attempt to provide additional definition of what might represent an 'inadvertent' breach of the standard.

confusion and distract from the focus on professional ethics by practitioners. We have therefore deleted the relevant text from paragraphs 1.25 and 5.42 of the exposure draft of the ES.

Q3: Does the revised paragraph 1.46 enhance the accessibility of the ES? Are there other areas where similar enhancements could be made?

1.46

18 respondents commented on enhancements to the accessibility of the ES (11 firms/practitioners, 5 professional bodies and 2 national audit agencies).

All respondents welcomed the changes, with some suggesting some additional minor drafting changes.

Minor drafting changes have been made to make the tables at paragraph 1.46 clearer.

Q4: Do you agree that the changes made to paragraphs 2.3 & 2.4, and 2.5 to 2.10; and the addition of additional guidance in paragraphs 3.22 to 3.23 enhance the clarity of ES?

2.3-2.10; 3.22-3.23

22 respondents commented on the proposed enhancements to sections 2 and 3 (13 firms, 7 professional bodies and 2 national audit agencies). 15 of these supported the revisions, with 6 neutral responses that offered comments on drafting, and 1 response that believes the extant requirements are clearer.

The significant majority believed the revisions enhance the clarity of paragraphs 2.3 and 2.4, but some noted that the requirements are now slightly more stringent in certain narrow cases, and queried if this was intentional.

Many respondents requested that the FRC define certain terms in section 2, in particular diversified collective investment schemes.

Many responses suggested drafting amendments to enhance the clarity of various provisions in section 3.

We have reworked the revisions to paragraphs 2.3 and 2.4 slightly, to remove an unintentional extension to the prohibitions for partners who are not covered persons.

The FRC notes that the concept of a diversified collective investment scheme is not new to the Ethical Standard, and no definition is present in the extant version. The FRC will consult with its Technical Advisory Group about a potential definition of this and other terms.

We have accepted some of the suggested drafting additional amendments to enhance clarity across sections 2 and 3.

Q5: Do you agree with the changes made to section 4 on fees?

4.6, 4.8, 4.21-4.29

18 respondents commented on the revisions to section 4 (12 audit firms, 4 professional bodies and 2 national audit agencies). 8 supported the revisions, 5 thought they introduced ambiguity in some areas and 5 offered comments on the drafting but gave no overall statement of support or opposition.

See the section below on Other Matters for general comments on the fee cap.

Many responses believed the new requirements to look at fees receivable from collections of entities with the same beneficial owner or controlling party (which is not a corporate holding entity) could be clarified to remove any ambiguities.

The FRC will consult with its Technical Advisory Group to ascertain whether the requirements are clearly and consistently understood.

Q6: Do you agree with the changes made to section 5 which extend some existing restrictions on the provision

19 respondents commented on the detailed changes we proposed to Section 5 of the ES on non-audit services (11 firms/practitioners, 6

As a general principle, where feedback has identified further areas where the ES could be seen to be less stringent than the IESBA Code

of non-audit or additional services?

professional bodies and 2 national audit agencies). Additional comments on the 70% non-audit services fee cap for PIE auditors, and its interaction with the permitted services list for PIEs at paragraph 5.40 are set out in the 'Other Matters' section below.

then we have amended Section 5 accordingly. An example would be where IESBA Code prohibitions extend to network firms. We have also considered the significance of any specific differences and the proportionality of any extensions.

Responses specifically focussed on:

- Proposed extensions to UK prohibitions (including tax services);
- Alignment with ISEBA Code changes;
- The potential need for supplementary guidance in some areas.

Q7: Are there any implications for the work of Reporting Accountants or

18-18-5

There were 11 responses to this question which included specific commentary (8 from firms/practitioners and 3 from

The FRC accepts the recommendation of some respondents that it should develop a 'roadmap' for the future development of ethical and assurance standards.

CASS assurance providers that should be considered alongside these revisions?

professional bodies). None of the other respondents identified any potential issues.

Many respondents stated that the Ethical Standard has become increasingly difficult for non-audit assurance providers to apply to the circumstances of their engagements. This includes where Reporting Accountants or CASS assurance providers are involved in engagements where their firm is not the statutory auditor.

Respondents also made reference to the FCA's review of UK Listing Rules and potential impacts for Reporting Accountants. These include the extent to which some Investment Circular Reporting Engagements (ICRE's) will continue to be required by law or regulation, and therefore how this will impact the permissible services list at paragraph 5.40 of the ES, and the 70% non-audit services fee cap.

In respect of the Ethical Standard this will include consideration of developments in the wider regulatory environment, the assurance market and international standards (IESBA Code). We will consider the need to expand elements of the Ethical Standard, or to address specific parts of the market through the issuance of separate standards. However, it would not be appropriate for the FRC to pre-empt the outcome of other consultations – for example in respect of the UK Listing Rules – in this current iteration of the ES.

We are also not currently of the view that there is a clear case for the development of separate ethical standards for Reporting Accountant or CASS assurance work. We do recognise that there are some circumstances where it is more difficult for practitioners. This is particularly the case when the Reporting Accountant or CASS assurance provider is not also the statutory auditor of the financial statements. Expanding the ES to address the specific examples given by respondents would risk making the ES even more complex and undermine the primarily principles based nature of the standard.

There was further commentary on future ESG assurance, and the extent to which similar problems may arise in the application of the ES.

As an alternative we will collate the various points raised in this consultation and address them directly in a meeting of the audit and assurance Technical Advisory Group (TAG).

Some respondents also suggested some specific drafting amendments which they believe would add clarity for Reporting Accountants in particular.

Minor editorial changes have been made to paragraph I8 in response to feedback. Further changes have been made at various paragraphs in Section 5 of the ES to make the use of language more consistent.

Q8: Do you agree with the proposed effective date of the revised ES? Are additional transitional reliefs required?

1.73-1.75

There were 19 responses to this question which included specific commentary (11 from firms/practitioners, 6 from professional bodies and 2 from national audit agencies).

The FRC notes that respondents were nearly unanimous in their support for the 15th December 2024 effective date, particularly as it aligns with the effective dates of elements of the revised IESBA Code.

Only 1 respondent suggested that a later effective date would be needed. None of the other respondents identified any potential issues.

The FRC agrees with the proposal for Implementation Guidance, which will be published in due course.

Respondents also suggested that it would be helpful for the FRC to issue

Additional paragraphs have been added (new paragraphs 1.32 and 1.33) which cover how the ethical standard applies to entities transitioning in and out of PIE status. This new material is an

implementation guidance (as was the case with the 2019 ES revision), and for additional explicit clarity to be included within the ES relating to transitional arrangements when an entity becomes, or ceases to become, a PIE.

amended version of published FRC guidance from the December 2016 Technical Advisory Group.

The FRC also accepts the need to respond at pace to any future changes in the UK statutory definition of a PIE.

A further issue raised was the need to respond to any future change in the UK statutory definition of a PIE.

Other Matters	ES reference	Consultation Feedback	Response
The 70% Non-audit services fee cap for PIE auditors	4.13	<p>11 out of the 20 respondents raised issues around the statutory non-audit services fee cap (9 audit firms and 2 Professional Bodies).</p> <p>All respondents recognised that the FRC has no powers to amend the cap (that is a decision for government), nor did any of the respondents argue in favour of removing it.</p>	<p>The FRC has no powers to amend the 70% non-audit services fee cap for PIE auditors.</p> <p>At the same time we acknowledge the large volume of feedback we have received, which we will share with our colleagues in the Department for Business and Trade.</p>

However, they wanted to highlight potential future issues, including:

- Whether the cap could potentially limit choice for entities seeking emerging forms of assurance. These included assurance over environmental, social and governance reporting (ESG). Unless this assurance is mandated by law or regulation it falls under the 70% non-audit services fee cap.
- Potential revisions to the UK Listing Rules by the FCA. Respondents wanted to highlight the impact on the fee cap of changes which could result in certain reporting accountant services being no longer mandatory, and therefore falling within the fee cap.

- The application of the fee cap to new PIEs after any revision of the statutory definition of UK PIEs by the government.

Public Sector Secondments (loan staff) 2.36

2 of the 3 national audit agencies who responded to the consultation raised the issue of public sector secondments (loan staff). Firms are generally prohibited from providing such services to the entities that they audit, although an exemption applies to public sector audit agencies where loan staff arrangements are for 3 months or less.

Both national audit agencies consider this exemption to be too restrictive, because of the way that it limits staff professional development in public sector audit. National audit agencies are keen to give their staff relevant more direct experience and knowledge of the sector they audit, with the aim to drive up the quality of

The FRC has carefully considered the arguments put forward by the national audit agencies. For the purposes of the public sector exemption to the loan staff prohibition, the FRC will now use language similar to that used in the IESBA Code.

Loan staff arrangements for national audit agencies will be limited to a 'short period of time', which we define as being no more than 12 months. The National Audit Office has identified further mitigations to manage any increased risk to auditor objectivity and independence.

work across their financial audit and VFM portfolios.

The way in which the current prohibition applies – to the entire audit portfolio of a firm – significantly limits the national audit agencies, where non-public sector firms can potentially provide loan staff to entities in the relevant market sector who they do not audit.

'Hardship' relief

n/a

1 audit firm suggested that it would be helpful for the FRC and DBT to agree to a policy for 'hardship' relief in an audit tender process. This would allow for audit firms to participate in audit tenders where they, or a network firm, have provided trivial non-audit services in the relevant period. Under current regulations there is no de-minimis level. This could potentially enhance competition and choice in the market.

The FRC does not have the statutory powers to make any such amendment to the current regulations. We will, however, raise this observation with colleagues in DBT.

Impact Assessment

8. As a matter of policy, the FRC's Ethical Standard is closely aligned to auditing standards the corresponding international IESBA Code. As we noted in our August 2023 Consultation document very many UK Audit firms already voluntarily comply with the IESBA Code. In that respect we do not anticipate significant additional costs to arise as a result of our revisions to the ES.
9. We believe that the Revised Ethical Standard 2023 introduces changes that are appropriate and proportionate to address issues that have been identified since the current standard was issued. We believe that benefits in the public interest, enhancing the quality of group audit engagements, will outweigh the costs of changes that may be necessary to audit firms' methodologies.

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