Financial Reporting Council

September 2015

Enhancing Confidence in Audit: Proposed Revisions to the Ethical Standard, Auditing Standards, UK Corporate Governance Code and Guidance on Audit Committees

The FRC is responsible for promoting high quality corporate governance and reporting to foster investment. We set the UK Corporate Governance and Stewardship Codes as well as UK standards for accounting, auditing and actuarial work. We represent UK interests in international standard-setting. We also monitor and take action to promote the quality of corporate reporting and auditing. We operate independent disciplinary arrangements for accountants and actuaries, and oversee the regulatory activities of the accountancy and actuarial professional bodies.

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Introduction

As published in its Regulatory Strategy,[1] the Financial Reporting Council (FRC) is committed to a proportionate approach to the use of its powers, making effective use of impact assessments and having regard to the impact of regulation on small enterprises.

The FRC follows three guiding principles in producing impact assessments:

- the work that goes into the production of an impact assessment should be proportionate to the importance of the proposal that it covers;
- where a standard is being introduced as a direct response to legislation or regulation, or as part of an agreed policy commitment to adopt international standards of accounting or auditing, the impact assessment should explain the rationale for introducing the standard and should focus on any aspects of the proposed standard which augment the relevant legislation or augment or diverge from the relevant international standard; and
- where appropriate, we are particularly alert to the impact of proposals on small businesses.

The FRC has decided to prepare a single impact assessment to cover revisions to the Ethical and Auditing Standards, and revisions to the UK Corporate Governance Code (the Code) and Guidance on Audit Committees (the Guidance) resulting from the implementation of the European Union (EU) Audit Regulation and Directive. This is explained in the 'Background to the Impact Assessment' section.

This impact assessment also provides, through Section 4 and Appendix 1, feedback on the December 2014 consultation: '*Auditing and ethical standards implementation of the EU Audit Directive and Audit Regulation*.'

1 www.frc.org.uk/FRC-Documents/FRC/Regulatory-Strategy-Our-Role-and-Approach-%28Version.aspx

Section 1: Executive Summary

In April 2014, the European Parliament and the Council of the EU issued Directive 2014/56/EU (the Directive) covering the statutory audit of annual accounts and consolidated accounts, and Regulation EU/537/2014 (the Regulation) covering specific requirements regarding statutory audit of public interest entities. Both apply with effect from 17 June 2016. The Directive and Regulation taken together require revisions to both the Ethical and Auditing Standards.

The implementation of the Regulation and Directive, and the revision of International Standards on Auditing (ISAs) by the IAASB require a significant change to the FRC's extant Ethical and Auditing Standards. There are also changes proposed to the Code and associated Guidance.

The 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.

The requirements of the Regulation and Directive are set out in UK or EU law, and the costs associated with them have already been included in the impact assessment carried out by the Department of Business, Innovation and Skills (BIS), which has been subject to review by the Regulatory Policy Committee. This impact assessment does not duplicate costs already covered in the BIS impact assessment, but instead focuses on any incremental costs and benefits arising from decisions taken by the FRC in those areas where it has discretion. As a result, for instance, changes made to standards or to the Code to ensure compliance with the law are not included within this assessment.

While this assessment includes quantifiable costs and benefits, there are much greater benefits arising from high-quality audit, and stakeholder confidence, however, these are impossible for us to quantify and include in this assessment although we know them to be valued by investors and other stakeholders. The Competition and Markets Authority noted in its market review of the statutory audit market in FTSE 350 firms that:

"The purpose of audit is to provide assurance to shareholders regarding the financial reports produced by the management of the companies in which they hold shares. However, other stakeholders such as lenders, suppliers and customers, as well as ratings agencies, also benefit from the assurance audit firms provide".

The FRC strongly believes that the changes to the Ethical and Auditing Standards proposed in this consultation will contribute significantly to increasing those benefits.

We are aware of the fact that additional costs arising from decisions we take will ultimately be paid for by UK business through higher audit fees. In implementing the requirements of the Regulation and Directive we have, therefore, looked to minimise any additional requirements and identify off-setting benefits to cover additional costs. As a result, we estimate that the total net cost arising from decisions taken by the FRC to implement the Regulation and Directive is £0.253 million. Once the requirements have been adopted, any ongoing annual cost arising from decisions taken will be part of the normal process of audit firms keeping their methodologies and staff up to date, and the incremental cost is, therefore, considered to be de minimis.

In preparing this impact assessment, our estimate of costs and benefits is based on a number of assumptions set out in the tables in the appendices, and using data drawn from a number of sources. As the values are comparatively small, we have rounded them to the nearest thousand. Although this produces values that may seem spuriously accurate, we have reported at this level of precision to support any future reporting requirement that the FRC may have to comply with to track the costs and benefits of regulation on business. We also recognise that the values reported are best estimates, but that these may be subject to change as we monitor them in subsequent periods.

Our proposals are set out in the following sections of this document:

Section 3A: Explains quantifiable costs and benefits associated with actions proposed by the FRC to implement the Regulation and Directive, and to adopt revisions to the ISAs issued by the IAASB.

Section 4: Explains quantifiable costs and benefits associated with decisions proposed by the FRC, and which were subject to the public consultation issued in December 2014.

Section 5: Explains quantifiable costs and benefits arising from FRC proposals which augment either the requirements of the Regulation and Directive or the ISAs issued by the IAASB.

Section 6: Sets out our approach to estimating and attributing quantifiable costs and benefits.

Section	**Cost/ (Benefit) (£ million)**[2]
Section 3A – implementation changes proposed to the Standards (*Appendix 3, Table 1*)	(£4.492)
Section 3A – changes arising from Member State Options exercised by the FRC (*Appendix 3, Table 3*)	(£1.210)
Section 4 – changes included in December 2014 consultation (*Appendix 3, Table 2*)	£3.567
Section 5 – Augmentations proposed by the FRC (*Appendix 3, Table 4*)	£2.388
Net Total Cost	**£0.253**

Detailed calculations are included in Appendix 3.

[2] The values contained in this impact assessment and the attached tables are derived from assumptions made by the FRC and BIS and FRC data. As the values are small, we have not rounded the numbers, to avoid many of the assumptions being rendered de minimis

Section 2: Background to the Impact Assessment

The FRC is issuing, for consultation, a revised Ethical Standard for audit and other public interest assurance engagements (in place of APB Ethical Standards 1 to 5 and the Ethical Standard for Reporting Accountants) which incorporates changes required by the Regulation and Directive.

In April 2014, the FRC set out its work to give justifiable confidence in the quality of audit.[3] A key element of that work was a review of the ethical framework for auditors, including the ethical standards, the results of which are included in our consultation, and are covered by this impact assessment. A small number of other revisions to the ethical standards are proposed as a result of that review, including to emphasise the ethical principles in the standard that should be complied with and to further clarify some requirements.

The FRC is also issuing, for consultation, revised ISAs (UK and Ireland) which incorporate changes required by the Directive, along with changes required to comply with our policy commitment to adopt ISAs issued by the IAASB. The revised ISAs also reflect necessary conforming amendments.

FRC guiding principles require the impact assessment to explain the rationale for introducing the revised Ethical and Auditing Standards, and focus on aspects of the standards that augment the relevant framework.

Many of the revisions made to the Standards issued for consultation along with this impact assessment, are to meet the requirements set out in EU or national legislation. It also includes proposed revisions to ensure that the UK and Ireland continue to base auditing standards on ISAs issued by the IAASB. Use of international standards on auditing is widely and consistently supported by stakeholders.

In developing the Standards for consultation, the FRC seeks to ensure that they provide a single, comprehensive source of requirements and guidance to support auditors and providers of other public interest assurance engagements in carrying out their responsibilities.

The FRC has already undertaken a public consultation exercise on the implementation of the Directive. This impact assessment explains how we have responded to this consultation.

Small businesses that are not '*public interest entities*' are not affected by the revised Ethical Standards – we are proposing to retain the Ethical Standard – Provisions Available for Smaller Entities, which provides alternative provisions for auditors of Small Entities (as defined in the introduction to that Standard) to apply in respect of the threats arising from economic dependence and where tax or accounting services are provided and allows the option of taking advantage of exemptions from certain of the requirements in the revised Ethical Standard for a Small Entity audit engagement.

This impact assessment covers the following elements:

a) the rationale for the changes to the (i) Ethical and (ii) Auditing Standards;
b) aspects of the Standards that augment or diverge from either (i) applicable EU or national legislation or (ii) the ISAs issued by the IAASB; and
c) evidence of costs and benefits of the Standards.

[3] https://www.frc.org.uk/News-and-Events/FRC-Press/Press/2014/April/FRCs-work-to-enhance-justifiable-confidence-in-au.aspx

Section 3A: Rationale for the revisions to the Ethical and Auditing Standards

The IAASB has recently issued revised auditor reporting standards,[4] a revised Standard on 'The Auditor's Responsibility Relating to Other Information' (ISA 720), and revised standards on 'Communication with Those Charged with Governance' (ISA 260) and 'Going Concern' (ISA 570). The IAASB has also issued the results of its project on 'Addressing Disclosures in the Audit of Financial Statements'.

The requirements of the Directive must be transposed into UK law. It is a minimum harmonisation directive, so UK law may exceed the Directive's requirements. As well as certain mandatory requirements, the Directive sets out some areas of flexibility where Member States may exercise derogations and options.

The requirements of the Regulation do not need to be transposed into UK law (they have 'direct effect'). It is a maximum harmonisation regulation, so UK law may not exceed the terms of the Regulation. Unusually, however, the Regulation also includes some Member State options.

The options in the Regulation and Directive which require decisions by the FRC relating to Codes and Standards are set out in Appendix 4 of this document.

The FRC has a policy commitment to base its auditing standards on ISAs issued by the IAASB[5]. The consultation proposes the adoption of the revised ISA 700 'Forming an opinion and reporting on financial statements'. The UK has previously not based its reporting standard on the international ISA 700, instead issuing a UK Standard which allowed auditors to demonstrate their compliance with international standards, and which better supported auditor reporting in the UK and Ireland context. The revised Standard issued by the IAASB in January 2015 'Forming an Opinion and Reporting on Financial Statements' incorporates many of the requirements previously included in ISA 700 (UK and Ireland) and allows even closer alignment between UK and Ireland standards, and those issued by the IAASB.

The FRC's current Ethical Standards for Auditors and Reporting Accountants were developed with the intent that they should adhere to the relevant principles of the IESBA Code and not be less stringent.

Options Considered

The FRC is a principles-based regulator, and is committed to issuing proportionate Codes, Standards and Guidance that comply with all legal requirements, and demonstrate compliance with international standards. Our Standards support the provision of high-quality, independent audit.

The FRC has previously consulted publicly on additional, more stringent requirements currently contained in existing Ethical and Auditing Standards. These requirements have been developed in response to particular issues or concerns, or to address UK and Ireland specific requirements, such as those contained in the Code. Where Member State options permit the retention of these more stringent requirements that have been subject to consultation and supported by stakeholders, this is not considered to be an additional cost in this impact assessment as any costs are already included in the current baseline cost of delivering statutory audits. The FRC,

4 ISAs 700, 701, 705, 706

5 Where necessary, the international standards have been augmented with additional requirements to address specific UK and Irish legal and regulatory requirements; and additional guidance that is appropriate in the UK and Irish national legislative, cultural and business context

supported by previous consultations considers retention of these requirements to be important in supporting the delivery of high-quality audit in the public interest.

In developing our consultation document, the FRC considered the following options:

For the Regulation and Directive (applicable to both Ethical and Auditing Standards)

- whether to exercise Member State options where the Regulation and Directive give a Member State the option to do so (see Appendix 4). The FRC's response to each of those is detailed in Section 6 of this document;
- whether to include the requirements of the Regulation in the text of the Standards, given that the Regulation has direct effect in law;
- whether relevant requirements applicable to the audit of public interest entities (as defined by the EU) should be applicable to other statutory audits (such as audits of other listed companies as defined by the FRC and the international standard setting bodies, that are not covered by the EU definition of a public interest entity;
- whether to provide reliefs in respect of the application of certain requirements for the audit of smaller listed firms.

For IAASB Revisions to International Standards on Auditing (applicable to Auditing Standards)

- to do nothing (not incorporate the changes);
- whether recent revisions made by the IAASB obviate existing FRC requirements (referred to as FRC pluses);
- whether recent revisions made by the IAASB require the addition of further UK and Ireland specific requirements by the FRC to reflect the UK and Ireland context and should be applicable to the audit of public interest entities; and
- whether to delay the effective date for the IAASB revisions so that it aligns with the application date of the Directive.

In our earlier consultation: 'Auditing and Ethical Standards – Implementing the EU Audit Directive and Audit Regulation' we stated that decisions about whether to propose new additional requirements in the future that exercise any Member State options within the FRC's remit would be made with regard to the FRC's 'Principles for the development of Codes, Standards and Guidance'[6] which include:

- there is a clearly defined issue relevant to the FRC's mission and responsibilities;
- the change is the most appropriate way to address the issue;
- one or more of the following conditions is met:
  - a change is necessary to comply or align with a legal requirement; or
  - a change is required in the light of developments in international standards or in UK or EU regulation; or
  - the risks to the public interest of not acting are significant, for example, a risk of systemic and/or market failure; or
  - it is possible to eliminate or significantly simplify a current requirement; or
  - it is necessary to clarify a current requirement; or
  - it is possible to create significant additional benefits in the public interest; or
  - a change is necessary to underpin the effectiveness of the FRC's enforcement and disciplinary activities;
- the anticipated benefits of the change outweigh the costs.

[6] https://www.frc.org.uk/FRC-Documents/FRC/About-the-FRC/Principles-for-the-development-of-Codes.pdf

FRC Conclusions

With reference to the FRC's Principles for the development of Codes, Standards and Guidance, in respect of the Regulation and Directive, the FRC concluded that:

- Member State options should only be exercised where they either provide (i) a transitional arrangement to support the implementation of the Regulation and Directive in a proportionate and cost-effective way; or (ii) maintain an existing FRC requirement which has already been subject to public consultation, and which is intended to support the delivery of high-quality audit;
- requirements should be included in the text of the Standards, to allow them to be a single source of authoritative information to support practitioners, although in places this makes the text of some of the Standards duplicative, it includes all of the requirements in a single place;
- more stringent requirements applicable to the audit of public interest entities should be applicable to the audit of other listed entities as defined by the FRC and international standard setters, subject to those requirements supporting high-quality audit, and not being unduly burdensome to audited entities;
- that smaller-listed entities that are not public interest entities should be eligible for reliefs in respect of certain more stringent requirements in the Ethical Standards, where this is proportionate and will not detract from high quality corporate reporting.

In respect of the IAASB revisions to Standards, the FRC concluded that:

- doing nothing is not an option for the FRC. We have a policy commitment to base our auditing standards on ISAs (supporting international harmonisation), and will reflect the latest IAASB revisions to the ISAs (UK and Ireland);
- FRC pluses should be removed where the issues that they relate to have been addressed in the revised IAASB standards;
- FRC pluses should only be added where they will enhance the quality of audit, and maintain requirements already subject to public consultation; and
- the implementation date for the IAASB revisions to standards should be aligned with the implementation date for the Regulation and Directive, to co-ordinate all revisions at a single point in time, thus reducing the burden on audit firms and business.

The costs and benefits arising from each of the conclusions drawn by the FRC have been calculated and are included in Section 5 of this impact assessment, with further detail set out in Appendix 3, Table 2.

The **net quantifiable benefit** as a result of these proposals is estimated to be **£4.492 million** based on the audit type and cost data in Appendix 2. A further **net quantifiable benefit** of **£1.210 million** arises from decisions taken by the FRC in respect of Member State options set out in Appendix 3, Table 3.

Section 3B: Rationale for revisions to the Corporate Governance Code and Guidance on Audit Committees

EU Audit Directive and Regulation

The Regulation and Directive apply with effect from 17 June 2016. Taken together they require revisions to both the Ethical and Auditing Standards as well as changes to the Code. The FRC has also taken the opportunity to review the Guidance, last published September 2012.

The Directive requires minimum harmonisation of requirements at the European level and these are being transposed into UK law. The Directive also gives the opportunity for Member States to exercise derogations and options. The requirements of the Regulation have a direct effect in law. Unusually for a regulation, it also includes some Member State options. The Regulation requires maximum harmonisation at the European level.

Competition and Markets Authority Report

In its original report on the market for audit services in FTSE 350 companies from October 2013, the Competition Commission – now the Competition and Markets Authority (CMA) – made a number of recommendations addressed to the FRC. However, its final Orders were only published in September 2014 after they were deferred to assess the implications of the Regulation and Directive on the audit of public interest entities, as there is some overlap with the Orders.

Following the decision of the CMA to delay finalising its proposed Orders, the FRC deferred consideration of whether to make any changes to the section of the Code dealing with the audit committee and appointment of the external auditor until the Code was next reviewed. More detail on what impact of the CMA's Orders and recommendations is covered in Sections 3 and 4 of the consultation.

Options considered

The 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 committee work and reporting, to maintain investor and wider stakeholder confidence in audit.

The FRC has therefore considered carefully the extent to which the new requirements of the Regulation and Directive, and the CMA report, require revisions to the Code. We have concluded that the current implementation of the requirement of Listed Companies to have an audit committee, through the Financial Conduct Authority's Listing and Disclosure and Transparency Rules is appropriate and the Code does not need to be changed.

We consider that changes to the Code should be kept to a minimum to limit the impact on all stakeholders – in particular companies, which are required to establish an audit committee and report on their application of and compliance with the Code, and investors, who monitor and evaluate companies' adherence to the Code and their explanations. Only three minor changes to the Code are therefore recommended, which are described in more detail in the consultation. The only one of these which potentially requires a change to the way in which the audit committee is established or reports, is that which requires the committee as a whole to have relevant competence to the sector in which the company operates. In the FRC's view, this requirement will already be met by virtually all those companies which are required to report on the Code and the cost implications are zero or negligible.

Section 4: Issues subject to consultation by the FRC in December 2014

The FRC issued a public consultation in December 2014,[7] to support our work on the measures required to implement the Regulation and Directive, including how Member State options should be addressed. The consultation included the questions reported in the table at Appendix 1, along with the FRC's proposed response. The purpose of that consultation exercise was not to set out an FRC position in respect of any of the questions, but rather to openly seek information from stakeholders to support the development of the FRC's approach to implementation.

The FRC has reflected the results of the December 2014 consultation in its proposals for implementing the requirements of the Regulation and Directive. Areas where the FRC proposes to implement additional requirements that go beyond those proposed by the EU or the IAASB are set out later in this impact assessment, along with the rationale for that proposal.

Our estimation of the net cost resulting from these proposals is estimated to be **£3.567 million** based on the audit type and cost data in Appendix 2. The specific costs associated with these proposals are set out in Appendix 3, Table 2.

7 Consultation: Auditing and Ethical Standards implementation of the EU Audit Directive and Audit Regulation

Section 5: Aspects of the Standards that augment the Regulation and Directive, or augment International Standards issued by the IAASB

Our December 2014 consultation set out a series of principles which support the FRC's aims for audit. These include:

- roles and responsibilities of auditors and audit committees are clear, and aligned with the interests and needs of investors;
- audit and auditors are trustworthy, act with integrity, serve the public interest and consistently meet the objectives of audit and audit standards;
- audit innovates to meet changing business and economic circumstances to improve audit quality;
- audit is a sustainable business with adequate capacity, and sufficient levels of competition and choice;
- global audits are effectively managed and overseen and quality is consistent across international work; and
- audit is subject to appropriate oversight within a clear regulatory regime.

Having considered these principles, the FRC proposes a small number of new additional requirements to the Ethical and Auditing Standards which augments either the Regulation and Directive or International Standards issued by the IAASB.

Existing requirements in Ethical and Auditing Standards issued by the FRC which have already been subject to public consultation, and which are being retained, are not included in this assessment.

Ethical Standards

The FRC proposes to:

- extend the more stringent EU PIE ethical and independence requirements to 'other listed companies' (this will affect companies listed on 'recognised markets', such as AIM, that are not EU regulated). These companies are already subject to these requirements through the Standards, and therefore, the impact of this change affects non-premium listed PIEs;
- extend the more stringent FRC ethical and independence requirements to EU PIEs (this will impact non-listed credit institutions and insurance undertakings);
- offer exemptions or limited reliefs from more stringent requirements in respect of certain EU non-audit services prohibitions, where these affect entities which are not EU PIEs, and whose securities are not freely transferable or cannot be traded freely by the public (such entities arguably therefore not being in the public interest);
- maintain FRC more stringent conditions on: (a) partner rotation; (b) limits on proportion of total firm fee income; (c) prohibition on providing non-audit services to 'significant affiliates' and extend to EU PIEs that are not listed (as defined by the FRC for consistency); and (d) requiring the group auditor to only use the work of other firms who are independent by the same requirements applied to the group auditor, so that independence requirements are applied consistently for a group audit; and
- consider the application of more stringent requirements to 'other public interest assurance engagements' (specifically SIRs and CASS engagements). In so doing, we have proposed amendments to the Ethical Standards to cover SIRs engagements allowing the Ethical Standard for Reporting Accountants to be withdrawn.
- consult on prohibiting the provision of all tax services by auditors on a contingent fee basis. The FRC believes this will address risks posed by conflicts of interest, and thereby contribute to our objective to deliver confidence in audit.

Auditing Standards

The FRC proposes that:

- **Professional scepticism** (ISA 200, ISA 540 and ISA 570) – The requirement in the Directive to maintain professional scepticism throughout the audit (and in certain areas in particular) is extended to all audits. This affects the audit of management estimates (ISA 540) and going concern (ISA 570). The FRC anticipates that the additional audit effort required should be minimal as professional scepticism is already required throughout the audit.
- **Going concern reporting requirements** (ISA 700) – We extend the extant requirement for the auditor to report by exception on the going concern basis of accounting and material uncertainties thereto from Code entities to all entities. The FRC considers that the effect of this will be limited as it is only required by exception.
- **Communicating key audit matters** (ISA 701) – We include a small number of additional UK requirements (UK pluses) based on the extant UK extended auditor reporting requirements for Code entities. These requirements, to communicate risks, scope and materiality, have been added to ISA 701 to extend the communication requirements to all entities that apply the ISA (i.e. listed entities as defined in the IAASB Standards which would include AIM, and any other entities either required to apply ISA 701, or choosing to apply it voluntarily). The FRC anticipates that the additional audit effort will be marginal as these are reporting requirements only, and not considered to be a significant burden.
- **Documentation of auditor's experts** (ISA 620) – The documentation requirements for external experts in the Directive be extended to all auditor's experts, including internal (audit firm) experts. This should not require additional audit effort as internal experts are defined as part of the engagement team by the ISAs and therefore are subject to all ISA documentation requirements.

The **net cost** as a result of these proposals is estimated to be **£2.388 million** based on the audit type and cost data in Appendix 2. The specific costs associated with these proposals are set out later in this report, and in Appendix 3, Table 4.

Section 6: Evidence of the costs and quantifiable benefits of the Standards

We have broken down the estimated costs and quantifiable benefits arising from the proposed changes to the Ethical and Auditing Standards as follows:

- Costs and benefits arising from mandatory requirements in the Regulation and Directive being incorporated in the revised Ethical and Auditing Standards;
- Costs and benefits arising from revisions to the Ethical Standards to address issues identified in the FRC's review of the Standards as part of its work to give justifiable confidence in the quality of audit;
- Costs and benefits arising from revisions to the UK and Ireland Auditing Standards required to adopt changes to ISAs issued by the IAASB;
- Costs and benefits arising from the proposal to offer certain reliefs applicable for the audit of smaller listed entities that are not public interest entities; and
- Costs and benefits arising from decisions taken by the FRC e.g. to make use of a derogation or member state option, or as a result of additional requirements being included in the Standards, or as a result of widening the applicability of any of the requirements contained within the Regulation and Directive.

As explained earlier in this impact assessment, requirements contained in the existing Ethical and Auditing Standards, which have been incorporated following prior public consultation, and which the FRC proposes to retain are not included within the calculations of costs and benefits, as they are already determined to be supported by a majority of stakeholders and included in the current baseline audit cost.

We have gathered evidence to support our assessment of costs and quantifiable benefits by drawing on data used by the BIS in its own impact assessment and data provided by a range of audit firms. To ensure that our evidence base includes small and medium sized audit firms, as well as larger audit firms, we have worked with a range of practitioners to provide a broad assessment of costs and benefits.

Where the information to support this assessment is qualitative rather than quantitative, we have indicated the relative significance of the measures.

BIS has separately prepared an impact assessment presented to the Regulatory Policy Committee which assesses the costs and benefits arising from:

- The implementation of the Directive on statutory audits of annual accounts and consolidated accounts; and
- The implementation of the Regulation on specific requirements regarding statutory audit of public interest entities.

The costs and quantifiable benefits contained in the department's impact assessment relate to activities undertaken by the department to implement the Regulation and Directive. The costs and quantifiable benefits included in this impact assessment relate to additional actions taken by the FRC to implement the requirements of the Regulation and Directive, and continue to support the provision of high-quality audit. For example: familiarisation costs for audit firms to understand their obligations in respect of non-audit services are included in the departmental impact assessment. The cost of complying with the revised ethical standards is included in this FRC assessment.

Table 1: Decisions taken by the FRC over the implementation of the Regulation and Directive, and the adoption of IAASB revisions to ISAs (see Section 3 of this assessment)

The FRC considered several options which are set out in Section 3 of this assessment to implement the requirements of the Regulation and Directive, and revised ISAs issued by the IAASB. The impact of our proposed approach to those issues is assessed in the table below, where they have not already been covered by our assessment of the impact of the implementation of requirements subject to consultation in December 2014.

Requirement	Estimate of change in work effort	Cost or benefit of proposed change	Attribution of cost or benefit of proposed change
(a) Member state options should only be exercised where they either provide (i) a transitional arrangement to support the implementation of the Regulation and Directive in a proportionate and cost-effective way; or (ii) maintain an existing FRC requirement which has already been subject to public consultation, and which is intended to support the delivery of high-quality audit.	Either covered in Table 4, with no further quantification to avoid double counting of costs or benefits. Maintaining existing FRC requirements have been subject to prior consultation, and are already included in baseline audit costs. No additional work required.		
(b) Requirements should be included in the text of the Standards, to allow them to be a single source of authoritative information to support practitioners, although in places this makes the text of some of the Standards duplicative, it includes all of the requirements in a single place.	Auditors have access to a single source of information to support their work – benefits from not having to consult multiple sources of information and guidance.	Estimated benefits to practitioners of 2 hours per year, based on providing guidance in one place. Numbers of practitioners drawn from FRC's Key Facts and Trends 2015.	(e) FRC
(c) More stringent requirements applicable to the audit of public interest entities should be applicable to the audit of other listed entities as defined by the FRC and international standard setters, subject to those requirements supporting high-quality audit, and not being unduly burdensome to audited entities.	Changes covered in questions 4a/4b and 5 in Table 2 – no further quantification to avoid duplication of costs or benefits.		
(d) That smaller-listed entities that are not public interest entities should be eligible for reliefs in respect of certain more stringent requirements in the Ethical Standards, where this is proportionate and will support higher-quality corporate reporting.	Proposed reliefs covered in question (5) in Table 2 – no further quantification to avoid duplication of costs or benefits.		

Requirement	Estimate of change in work effort	Cost or benefit of proposed change	Attribution of cost or benefit of proposed change
(e) Policy commitment to base our auditing standards on ISAs (supporting international harmonisation), and will reflect the latest IAASB revisions to the ISAs (UK and Ireland).	Firms will be required to update guidance for practitioners, and auditors will require familiarisation.	Updating guidance by technical managers/ partners. Familiarisation IAASB changes – mainly on reporting standards – 2 hours per practitioner. Numbers of practitioners drawn from FRC's Key Facts and Trends 2015.	(c) IAASB
(f) FRC pluses should be removed where the issues that they relate to have been addressed in the revised IAASB standards.	No changes – FRC pluses have been retained where required.	Nil cost – no change in requirements.	(e) FRC
(g) FRC pluses should only be added where they will enhance the quality of audit, and maintain requirements already subject to public consultation.	Changes covered in Table 3 – no further quantification to avoid duplication of costs or benefits.		
(h) Implementation of changes arising from the Regulation and Directive and IAASB in a single revision to standards.	Removes requirement for an additional update to firm's methodology and guidance, and familiarisation for audit staff.	Saving of technical manager, and partner time updating guidance. Saving of familiarisation training time – 3 hours per practitioner	(e) FRC

Table 2: Costs and quantifiable benefits arising from decisions taken by the FRC subsequent to the December 2014 Consultation

The FRC included several consultation questions, the results of which have been reflected in the revised Ethical Standards. The way in which the FRC proposes to respond to the December 2014 consultation, and our assessment of the impact is set out in the table below. The questions and the proposed response can be found in Appendix 1 to this assessment.

Requirement (question references from December 2014 consultation)	**Estimate of change in work effort**	**Cost or benefit of proposed change**	**Attribution of cost or benefit of proposed change**
4a/4b: Proposal: (a) to apply to all PIEs for consistency purposes; and (b) to apply to other listed to maintain existing requirements and provide consistency.	None required	Nil cost – maintaining existing requirement that has been subjected to prior consultation. Benefit from maintaining consistent requirement for all audits. Offsetting benefit as practitioners will need to monitor fewer prohibitions, and audit committees will need to approve fewer non-audit services requests, calculated at 2 partner hours per PIE (average rate) and 12 person hours of audit committee time (3 committee members) per PIE calculated per BIS principal rate.	(e) FRC
5: Proposal: maintain for other listed entities subject to consultation on reliefs for (a) entities with non-tradable shares; and (b) smaller listed entities with market capitalisation below a threshold.	Application of consistent approach will increase audit work effort for non-PIE entities.	Additional cost, mitigated by savings proposed by reliefs for entities which do not have freely tradeable securities, and those with market capitalisation below £100 million.	(d/e) FRC
6: Proposal: No extension of requirements.	None required	Nil cost – unquantified benefit of additional work not required.	(e) FRC
7: Proposal: proceed with black list per regulation.	None required	Nil cost – unquantified benefit of additional work not required.	(e) FRC
8: Not applicable – black list applied	None required	Nil cost – unquantified benefit of additional work not required.	(e) FRC
9: Proposal: No expansion of black list.	None required	Nil cost – unquantified benefit of additional work not required.	(e) FRC
10: Proposal: Permit derogations but where 'clearly trivial' rather than immaterial.	None required	Benefit to smaller entities from derogations.	(e) FRC

Requirement (question references from December 2014 consultation)	**Estimate of change in work effort**	**Cost or benefit of proposed change**	**Attribution of cost or benefit of proposed change**
11: Proposal: To also consult where issues are subjectively important in the context of the engagement.	None required	May marginally reduce benefit in (10) subject to consultation.	(e) FRC
12: Proposal: Implement per Regulation.	None required	Nil cost, additional audit committee costs covered in BIS impact assessment – unquantified benefit of additional work not required.	(e) FRC
13/14: Proposal: Obligation sits with group auditor to satisfy themselves that other auditors, whose work they propose to use meet the independence requirements.	Additional work by group auditor.	Additional costs, mitigated by savings by not applying requirement to other network and non-network firms.	(e) FRC
15: Proposal: No lower cap – apply per Regulation.	None required	Nil cost – benefit to business from reduced tendering requirement.	(e) FRC
17: Proposal: Extend requirement to network firms for non-audit services provided by PIEs.	Administrative monitoring on firms; potential tendering requirement for business.	Additional costs on business and audit firms.	(e) FRC
19: Proposal: No requirement to go further, but propose to get rid of a ‘gap’ year being used to reset the three year period.	None required	Nil cost - no additional burden – just a variation in measurement methodology.	(e) FRC
20/25: Proposal: To maintain requirements.	None required	Nil cost – maintaining existing requirement that has been subjected to prior consultation. Benefit from maintaining consistent requirement for all audits.	(e) FRC

Table 3: Costs and quantifiable benefits arising from decisions taken by the FRC in respect of Member State options included in Appendix 4, and not covered elsewhere in this assessment

Included within the Regulation and Directive are a small number of Member State options to be decided on by the FRC – the impact of the FRC's proposal are set out in the table below.

Requirement	Estimate of change in work effort	Cost or benefit of proposed change	Attribution of cost or benefit of proposed change
2 year exemption for non-audit services cap requirements.	Delays impact of work required for up to 2 years	No direct cost, but benefit from delaying implementation for 2 years and costs associated.	(e) FRC
Non-audit services – more stringent requirements.	None. The FRC does not propose more stringent requirements in respect of the non-audit services fee cap. Other audit fee requirements are covered by existing FRC requirements to be maintained.	Benefits from no additional requirements being applied. Costs avoided, but unquantifiable.	(e) FRC
Non-audit services – prohibition of additional services where they pose a threat to independence.	See question 6 in Table 2 – no further quantification to avoid duplication of costs or benefits.		
Non-audit services – de minimis exemption.	See question 10 in Table 2 – no further quantification to avoid duplication of costs or benefits.		
Non-audit services – stricter rules for non-audit services nor prohibited by Article 5.	See questions 13, 14 and 17 in Table 2 - no further quantification to avoid duplication of costs or benefits.		
Audit report – additional requirements.	See Table 3, items 7 and 8 – no further quantification to avoid duplication of costs or benefits.		
Additional report to audit committee – additional requirements on content.	No additional requirements added by FRC.	Benefits from no additional requirements being applied. Costs avoided, but unquantifiable.	(e) FRC
Delegation of Tasks – requirement for key audit partners to rotate before 7 years.	Proposal to retain existing FRC requirements to the extent permissible under the regulation – FRC aim to secure consistency of approach.	No additional costs to current baseline – if amendments are required, FRC will ensure consistency. Costs avoided, but unquantifiable.	(e) FRC

Requirement	Estimate of change in work effort	Cost or benefit of proposed change	Attribution of cost or benefit of proposed change
Definitions – wider application of certain requirements to non-PIEs.	The FRC does not propose to expand PIE requirements to non-PIEs.	Costs avoided, but unquantifiable.	(e) FRC
Preparation of statutory audit – simplified requirements for certain small undertakings.	FRC consulting on retaining ES PASE for smaller entities.	Costs avoided, but unquantifiable.	(e) FRC
Internal organisation - simplified requirements for certain small undertakings.			
Organisation of work – exemption from obligation to keep records of any breaches of the Directive.	FRC proposes to exercise option – removing requirement to record minor breaches.	Costs avoided, but unquantifiable.	(e) FRC
Organisation of work – exemption from obligation for audits of small undertakings to keep records of any breaches of the Directive.	FRC proposes to exercise option – removing requirement to record minor breaches.	Costs avoided, but unquantifiable.	(e) FRC

Table 4: Costs and quantifiable benefits arising from actions proposed by the FRC which augment the requirements in the Regulation and Directive, or those in International Standards included in Section 5 of this assessment.

In revising the Ethical and Auditing Standards, the FRC has identified a small number of proposals which either augment or diverge from the requirements of the Regulation and Directive. The costs and benefits associated with those decisions are set out below.

Requirement	Estimate of change in work effort	Cost or benefit of proposed change	Attribution of cost or benefit of proposed change
1. Extension of ethical and independence requirements to other listed entities	Changes covered in questions 4a/4b and 5 in Table 2 – no further quantification to avoid duplication of costs or benefits.		
2. Extend FRC ethical and independence requirements to PIEs	None – arrangements already apply, and thus are included in the baseline cost.	Nil cost. Unquantifiable benefit from retaining measures to uphold justifiable confidence in audit	(e) FRC
3. Reliefs for non-public interest entities from certain non-audit services provisions	Proposed reliefs covered in question (5) in Table 2 – no further quantification to avoid duplication of costs or benefits.		
4. Maintain certain FRC conditions on independence	No change in work effort required, as this relates to retaining existing requirements which have been subject to previous public consultation.	Nil cost. Unquantifiable benefit from retaining measures to uphold justifiable confidence in audit. Quantifiable benefits by reducing admin burden of dealing with non-audit services approvals.	(e) FRC
5. Application of ethical standards to other public interest assurance engagements	No change to CASS engagements (covered by recent FRC consultation), some additional effort required for SIRs work, relieved by the reduction of the ESRA.	Familiarisation costs for reporting accountants based on 2 hours per practitioner. Firm costs based on updating guidance.	(e) FRC
6. Prohibiting the provision of all tax services on a contingent fee basis.	Some additional costs for entities which make use of such arrangements.	This clarifies an existing prohibition, and therefore the number of engagements affected will be small, this will also have a limited impact on cost as fixed fees replace contingent fees. Provision based on 0.05% of UK non-audit services work value per Key Facts and Trends	(e) FRC

Requirement	Estimate of change in work effort	Cost or benefit of proposed change	Attribution of cost or benefit of proposed change
7. Professional scepticism (ISA 200, 540 and 570)	Minimal expansion of additional requirements	Nil	(e) FRC
8. Going concern reporting requirements (ISA 700)	Marginal expansion, but on a by exception basis estimated to affect 2.5% of cases.	0.5 hour, Principal per affected engagements	(e) FRC
9. Communicating key audit matters (ISA 701)	Marginal expansion of existing reporting requirements	1 hour, Principal per affected engagements	(e) FRC
10. Documentation of auditor’s experts (ISA 620)	None	Nil	(e) FRC

Appendix 1 – Questions consulted on by the FRC in the December 2014 consultation

Question	Matter	Outcome and Response
4a/4b	Application of current more stringent requirements in the FRC's Standards to (a) all PIEs and (b) some or all other listed entities.	Outcome: Mixed views, but majority considered that no additional entities other than current 'FRC Listed' and other PIEs should be subject to more stringent requirements. Proposal: (a) to apply to all PIEs for consistency purposes; and (b) to apply to other listed to maintain existing requirements and provide consistency.
5	Application of stringent new requirements on PIEs to other listed entities (other recognised markets and EU regulated markets).	Outcome: Mixed support for the extension of requirements where this will ensure consistency of approach for entities of public interest. Proposal: maintain for other listed entities subject to consultation on reliefs for (a) entities with non-tradable shares; and (b) smaller listed entities with market capitalisation below a threshold.
6	Application of the requirements of the Regulation to other types of entity or listed entity.	Outcome: Majority expressed concerns about disproportionate effects of applying more stringent requirements to listed entities that are not PIEs. Proposal: No extension of requirements.
7	Prohibited non-audit services – how to best reduce perceived threats to auditor independence (black list 'v' white list).	Outcome: Strong support for a 'black' list. Proposal: proceed with black list per regulation.
8	Possible 'white list' services if a decision were taken to adopt such a list.	Not applicable – black list applied
9	Other non-audit services that should be subject to prohibition.	Outcome: Little support to increase 'black' list beyond that set out in the Regulation. Proposal: No expansion of black list.
10	Derogations to allow certain prohibited non-audit services if immaterial.	Outcome: Strong support to take up derogations to maintain flexibility and choice for audit committees. Proposal: Permit derogations but where 'clearly trivial' rather than immaterial.
11	If the derogation in Q10 is taken up, should additional conditions other than materiality apply?	See response to Q10. Proposal: To also consult where issues are subjectively important in the context of the engagement.
12	Should the provision of non-audited services be subject to audit committee approval, or should other conditions be established.	Outcome: Strong support that audit committee approval is appropriate for approval. Proposal: Implement per Regulation.

Question	Matter	Outcome and Response
13/14	Should group auditors of PIEs ensure that the principles of independence apply (a) to all members of the network whose work they use; and (b) by other non-network firms whose work they use?	Outcome: Mixed views – support for consistency but not extending requirement to other auditors to avoid 'gold-plating'. Challenge over monitoring compliance. Proposal: Obligation sits with group auditor to satisfy themselves that other auditors, whose work they propose to use meet the independence requirements.
15	Should a lower cap of fees for non-audit services be provided for some or all types of non-audit service?	Outcome: Strong support for the 70% cap. Proposal: No lower cap – apply per Regulation.
17	Should the cap for non-audit services apply to the auditor of the PIE, or should it be applicable to non-audit services provided by network firms.	Outcome: Mixed views – support for a consistent approach, but not extending requirement to network firms to avoid 'gold-plating' and challenge over monitoring compliance. Support for consistent approach. Proposal: Extend requirement to network firms for non-audit services provided by PIEs.
19	Should the calculation of the cap by reference to three preceding years for the provision of non-audit services go further than the basis set out in the Regulation?	Outcome: Clear support for the three year rolling base period as set out in the Regulation. Proposal: No requirement to go further, but propose to get rid of a 'gap' year being used to reset the three year period.
20/25	Should the more stringent requirements in Ethical Standards 4 (fees earned from an audited entity) and Ethical Standards 3 (rotation for the engagement and other key audit partners) be maintained.	Outcome: Mixed views, but majority support to maintain existing requirements for both ES4 and ES3. Proposal: To maintain requirements.

Appendix 2 – Audit fee planning assumptions for the impact assessment

Entity Type	Details	Aggregate audit fees (current baseline)
PIE, UK Premium Listed PIE, unlisted credit institutions and insurance undertakings 1,665 entities	756 UK Premium Listed entities[8] and 909[9] other PIEs categorised using EU size definitions:[10] 15 very large (average annual audit fee £19.6 million); 174 large (average annual audit fee £3.4 million); 599 medium (average annual audit fee £0.46 million); and 877 small (average annual audit fee (£0.04 million).	 £294,000,000 £591,600,000 £275,540,000 £35,080,000
Total PIEs		**£1,196,220,000**
UK non-premium listed on recognised exchanges 818 entities	818 entities[11] split out between: 4 very large (over £1 billion market cap. average audit fee £200,000); 59 large (market cap. £250-£1,000 million, average audit fee £140,000); 266 medium (market cap. £50-£250 million, average audit fee £85,000); and 489 small (market cap. less than £50 million, average audit fee £40,000).	 £800,000 £8,260,000 £22,610,000 £19,560,000
Total Other Listed		**£51,230,000**
Other statutory audits – large	1,200 – average audit fee £125,000	£150,000,000
Other statutory audits – medium	10,000 – average audit fee £30,000	£300,000,000
Other statutory audits – small	85,000 – average audit fee £12,000	£1,020,000,000
Total Other Statutory		**£1,470,000,000**
Total		**£2,717,450,000**

Average audit fee and information on numbers of audits has been reconciled to BIS data.

[8] LSE as at 31 March 2015
[9] EBA and PRA data as at April 2015 and July 2014
[10] Plus further entities listed on EU Markets, totalling 1,665 per BIS data
[11] AIM 741 and ISDX 77

Auditor costs

Audit fee costs have been derived from the impact assessment prepared by BIS, and indicative data for audit firms that has been subject to confirmation.

Large Audit Firms	**Cost per hour**
Partner	£700.00
Manager	£400.00
Principal	£45.90
Team Member (weighted average)	£25.52

Other Audit Firms	**Cost per hour**
Partner	£375.00
Manager	£225.00
Principal	£45.90
Team Member (weighted average)	£25.52

Appendix 3 – Cost and quantifiable benefit estimate calculations

Table 1 – Net quantifiable benefits of £4.492 million arising from decisions taken by the FRC over the implementation of the EU Audit Regulation and Directive, and the adoption of IAASB revisions to ISAs

Requirement	Work impact	Assumptions	Net cost (benefit) (£million)
(b)	Requirements should be included in the text of the Standards, to allow them to be a single source of authoritative information to support practitioners, although in places this makes the text of some of the Standards duplicative, it includes all of the requirements in a single place.	Estimated benefits to practitioners of 2 hours per year, based on providing guidance in one place. Numbers of practitioners drawn from FRC's Key Facts and Trends 2015, assumption that 75% of the holders of the AQ are actively in practice. Benefit at weighted average team rate per BIS data, and discounted by 50%.	(£2.682)
(e)	Policy commitment to base our auditing standards on ISAs (supporting international harmonisation), and will reflect the latest IAASB revisions to the ISAs (UK and Ireland).	Updating guidance by technical managers/ partners (90%/10%) 1,200 hours for large firms (6), 100 hours in medium firms (30) and 20 hours in small firms (64) – using BIS assumptions for PIEs familiarisation discounted by 50% as these are revisions to existing requirements. Familiarisation IAASB changes – mainly on reporting standards – 2 hours per practitioner. Numbers of practitioners drawn from FRC's Key Facts and Trends 2015, assumption that 75% of the holders of the AQ are actively in practice. Benefit at weighted average team rate per BIS data, and discounted by 50%.	£2.314 £2.689
(f)	FRC pluses should be removed where the issues that they relate to have been addressed in the revised IAASB standards.	No impact on cost or benefits.	£0.000
(h)	Implementation of changes arising from the Regulation and Directive and IAASB in a single revision to standards.	Removes requirement for an additional update to firm's methodology and guidance, and familiarisation for audit staff. Saving of technical manager, and partner time updating guidance. Updating guidance by technical managers/ partners (90%/10%) 1,200 hours for large firms (6), 100 hours in medium firms (30) and 20 hours in small firms (64) – using BIS assumptions for PIEs familiarisation. Saving of familiarisation training time – 2 hours per practitioner. Numbers of practitioners drawn from FRC's Key Facts and Trends 2015, assumption that 75% of the holders of the AQ are actively in practice. Benefit at weighted average team rate per BIS data, and discounted by 50%.	(£4.131) (£2.682)
Total			**(£4.492)**

Table 2 – Net costs of £3.567 million arising from decisions taken by the FRC subsequent to the December 2014 Consultation

Requirement	Work impact	Assumptions	Net cost (benefit) (£million)
4a/4b	Application of FRC more stringent requirements to ‘other’ PIEs (non-listed credit institutions and insurance undertakings) and other listed entities will require a small amount of additional work effort to ensure compliance with ethical standards.	909 other PIE audits, based on average of medium and small fee cost of £0.25 million increasing by 1.75%; 818 other listed audits increasing by 1%. Offsetting benefit as practitioners will need to monitor fewer prohibitions, and audit committees will need to approve fewer non-audit services requests, calculated at 2 partner hours per PIE (average rate) and 12 person hours of audit committee time (3 committee members) per PIE calculated per BIS principal rate.	£4.489 (£2.707)
5	Application of stringent new requirements on PIEs to other listed entities – marginal addition to requirements already set out in 4a/4b. To be offset by reliefs for smaller other listed entities, for the purpose of this exercise, those with a market capitalisation of under £100 million, or those with shares that are not freely tradeable by members of the public.	818 other listed audits increasing in cost by 0.5%, net of reliefs for 489 small audits and 123 medium audits resulting in savings of 2% of audit fees.	£0.256 (£0.600)
6	Application of Regulation to other listed entities – FRC decision not to apply.	No additional cost to business.	£0.000
7	Prohibited non-audit services – avoiding threats to auditor independence. FRC decision to keep to requirements set out in Regulation.	No additional cost to business. [Note that base cost of applying the Regulation is covered in the BIS impact assessment].	£0.000
8	‘White list’ option.	No additional cost to business. [Note that base cost of applying the Regulation is covered in the BIS impact assessment].	£0.000
9	Adding additional non-audit services to prohibited services list.	No additional cost to business. [Note that base cost of applying the Regulation is covered in the BIS impact assessment].	£0.000
10	Derogations for immaterial non-audit services (where clearly trivial)	Allows flexibility which is taken up by 1.75% of (97,000) audited entities, saving on average 10 hours of staff time at £23.26/ hour (per ASHE 2014) per entity.	(£0.395)
11	Additional conditions for derogation to apply for trivial non-audit services.	Recognition that subjective issues apply in 25% of cases in Q10, reducing benefit claimed.	£0.099
12	Should approval of non-audit services require conditions other than audit committee approval?	FRC proposes no additional conditions – audit committee time and cost already included in BIS impact assessment.	£0.000
13/14	Should group auditors of PIEs ensure that principles of independence apply (a) to all members of the network whose work they use; and (b) by other non-network firms whose work they use?	Requirement on group auditors of PIEs means average additional cost of 5 partner hours per group audit – assumption that 40% of 1,665 PIEs are group audits, and 80% of auditors are large firms.	£2.115
15	Should a lower fee cap apply for some or all types of non-audit services? FRC proposes to adhere to the cap in the Regulation.	No additional cost to business.	£0.000

Requirement	Work impact	Assumptions	Net cost (benefit) (£million)
17	Should the cap for non-audit services apply to the auditor of the PIE or should it be applicable to non-audit services provided by network firms? FRC proposes to extend requirements to network firms.	Requires tendering action in 10% of PIEs which requires 80 hours of staff time per entity at ASHE rates per Q10.	£0.310
19	Calculation basis for the cap on non-audit services to get rid of the gap year when calculating the rolling three year basis.	Methodological only - no additional cost to business.	£0.000
20/25	Maintaining the more stringent current requirements in Ethical Standard 4 (fees earned from an audited entity) and Ethical Standard 3 (rotation of key partners).	Maintains existing requirement so no addition to baseline cost – if these were limited in any way this would result in a net benefit against the baseline.	£0.000
Total			**£3.567**

Table 3 – Net costs of £2.388 million arising from decisions taken by the FRC to augment the requirements of the Regulation and Directive, and the ISAs issued by the IAASB

Requirement	Work impact	Assumptions	Net cost (benefit) (£million)
2.	Extend FRC ethical and independence requirements to PIEs. Assumed no work impact as requirements are already included in the current baseline cost.	Nil cost – unquantifiable benefit from retaining measures to uphold justifiable confidence in audit.	£0.000
4.	Maintain certain FRC conditions on independence. No change in work requirement as this relates to existing requirements which have already been subject to public consultation.	Nil cost – unquantifiable benefit from retaining measures to uphold justifiable confidence in audit.	£0.000
5.	Application of Ethical Standards to other public interest assurance engagements. Impact on SIRS work and other PI work, updating of guidance, relieved by removal of ESRA.	Increase in familiarisation effort of 2 practitioner hours (principal) and 2 hours (partner) for 50% of PIEs and other listed entities. Split 67/33 between large and smaller firms.	£1.586
6.	Prohibiting the provision of all tax services on a contingent fee basis will require alternative provider of services to be used, and changes the balance of risk and reward in these assignments.	This clarifies an existing prohibition, and therefore the number of engagements affected will be small, this will also have a limited impact on cost as fixed fees replace contingent fees. Provision based on 0.05% of UK non-audit services work value per Key Facts and Trends.	£0.631
7.	Professional scepticism (ISA 200, 540 and 570). Minimal expansion of additional requirements.	Nil cost.	£0.000
8.	Going concern reporting requirements (ISA 700). Small impact in a minority of cases (planning assumption 1.25%)	Using 97,000 engagements with 1.25% affected – additional requirement 0.5 hours of effort at manager rate average of £312.50.	£0.189
9.	Communicating key audit matters (ISA 701). Marginal expansion of reporting requirements.	Calculated using PIEs, other listed and large statutory audits, 1 hour per assignment, principal rate. Offset by savings as firms are no longer required to provide specific guidance – 2 hours partner + 2 hours manager for 100 firms split 67/33 large and small.	£0.169 (£0.187)
10.	Documentation of auditor's experts (ISA 620). No additional work effort required.	Nil cost.	£0.000
Total			**£2.388**

Table 4 – Net quantifiable benefits of £1.210 million arising from decisions taken by the FRC in respect of Member State options included in Appendix 4

Requirement	Work impact	Assumptions	Net cost (benefit) (£million)
2 year exemption for non-audit services cap requirements.	Delays impact of work required for up to 2 years, to be permitted by FRC as competent authority.	No direct cost, but benefit from delaying implementation for 2 years and costs associated. Opportunity cost 'benefit' set at 10% of BIS best estimate of additional tendering costs for non-audit services of £12.1 million.	(£1.210)
Non-audit services – more stringent requirements.	None. The FRC does not propose more stringent requirements in respect of the non-audit services fee cap. Other audit fee requirements are covered by existing FRC requirements to be maintained.	Benefits from no additional requirements being applied. Costs avoided, but unquantifiable.	£0.000
Additional report to audit committee – additional requirements on content.	No additional requirements added by FRC.	Benefits from no additional requirements being applied. Costs avoided, but unquantifiable.	£0.000
Delegation of Tasks – requirement for key audit partners to rotate before 7 years.	Proposal to retain existing FRC requirements to the extent permissible under the regulation – FRC aim to secure consistency of approach.	No additional costs to current baseline – if amendments are required, FRC will ensure consistency. Costs avoided, but unquantifiable.	£0.000
Definitions – wider application of certain requirements to non-PIEs.	The FRC does not propose to expand PIE requirements to non-PIEs.	Costs avoided, but unquantifiable.	£0.000
Preparation of statutory audit – simplified requirements for certain small undertakings.	FRC consulting on retaining ES PASE for smaller entities.	Costs avoided, but unquantifiable.	£0.000
Internal organisation - simplified requirements for certain small undertakings.	FRC consulting on retaining ES PASE for smaller entities.	Costs avoided, but unquantifiable.	£0.000
Organisation of work – exemption from obligation to keep records of any breaches of the Directive.	FRC proposes to exercise option – removing requirement to record minor breaches.	Costs avoided, but unquantifiable.	£0.000
Organisation of work – exemption from obligation for audits of small undertakings to keep records of any breaches of the Directive.	FRC proposes to exercise option – removing requirement to record minor breaches.	Costs avoided, but unquantifiable.	£0.000
Total			**(£1.210)**

Appendix 4 – List of Member State options

Member State options for both the Regulation and Directive are included on the BIS website, and can be found using the attached links:

Audit Regulation

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/388846/member-state-options-table-for-regulation-537-2014.pdf

BIS published a list of 22 Member State options included in the Regulation along with its discussion document, of which 8 concern areas within FRC consultations on the Regulation and Directive:

- Non-audit services – exemption from requirements for a period not exceeding two years (Art 4, Para 2, sub 3);
- Non-audit services – may choose to apply more stringent requirements (Art 4, Para 4);
- Non-audit services – prohibition of additional services where they represent a threat to independence (Art 5, Para 2);
- Non-audit services – de minimis exemption (Art 5, Para 3);
- Non-audit services – stricter rules for non-audit services not prohibited by Article 5 (Art 5, Para 4, sub 2);
- Audit Report – additional requirements in relation to the content of the audit report (Art 10, Para 2, sub 2);
- Additional Report to Audit Committee – additional requirements on content (Art 11, para 2, sub 2); and
- Delegation of Tasks – requirement for key audit partners to rotate before 7 years (Art 24, Para 7, sub 2).

Audit Directive

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/388777/member-state-options-table-for-directive-2014-56-eu.pdf

BIS published a list of 30 Member State options included within the Directive along with its discussion document, of which 5 concern areas within FRC consultations on the Regulation and Directive:

- Definitions – article allows wider application of certain requirements to non-PIEs (Art 1, Para 2(f));
- Preparation of statutory audit – provides for simplified requirements for certain small undertakings (Art 1, Para 16);
- Internal organisation – simplified requirements for audits of small undertakings (Art 1, Para 18);
- Organisation of work – exemption from obligation to keep records of any breaches of the Directive (Art 1, Para 19); and
- Organisation of work – simplified requirements for audits of small undertakings with regard to recording breaches of the Directive (Art 1, Para 19).

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