



Need to Know

Accounting, auditing and corporate governance – legal and regulatory changes arising from Brexit

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Under the *European Union (Withdrawal) Act 2018*, the UK ceased to be a member of the EU on 31 January 2020 ('Exit day'). Under the withdrawal agreement, enacted in UK law by the *European Union (Withdrawal Agreement) Act 2020* (WAA 2020), there is an implementation period, which ends on 'IP completion day', defined as 31 December 2020 at 11.00 p.m. UK time. UK reporting continues to be subject to the EU legislative framework until IP completion day. However, for financial periods commencing on or after IP completion day, a number of changes will come into effect in order to incorporate EU concepts into UK law and hence maintain continuity of treatment (and, ultimately, allow for the possibility of divergence in the fullness of time). Whilst many of these changes are highly technical amendments to fix definitions and references in the law, several will affect the requirements around company reporting, auditing and governance.

- The government has enacted several Statutory Instruments (SIs) addressing the UK accounting, corporate reporting, auditing and corporate governance regimes which largely take effect for periods beginning on or after IP completion day.
- After IP completion day, UK companies will continue to have the choice, or be required, to adopt IFRS, as relevant to their circumstances. However, the version of IFRS will be IFRS as adopted by the UK rather than IFRS as adopted by the EU, with a UK endorsement mechanism to be introduced, which will be overseen by the Secretary of State.
- The Companies Act 2006 will be amended to change references to the European Economic Area (EEA) to refer instead to the UK, affecting a variety of provisions including eligibility for the small companies regime and the availability of audit exemption for subsidiaries.
- These changes are generally effective for financial periods beginning on or after IP completion day, defined as 31 December 2020 at 11.00 p.m. UK time, but some changes may require thought or action on or soon after IP completion day.

For more information please see the following websites:

www.ukaccountingplus.co.uk

www.deloitte.co.uk

Background

The UK's accounting, corporate reporting, auditing and, to a lesser extent, corporate governance regimes have their roots in European law. In many cases these laws have been implemented by the Companies Act 2006 and related Statutory Instruments (SIs); in some cases they are directly binding EU law.

Under WAA 2020, the relevant EU laws continue to have direct application until IP completion day. By the end of that period a future economic partnership may be in place, which will set the degree to which the UK and EU remain converged; as yet, there is little detail as to how that will work. If, however, IP completion day is reached with no further developments, then a number of inconsistencies and issues arise which will need to be addressed.

This Need to Know summarises the effect of the complex changes made to the Companies Act 2006, Financial Services and Markets Act 2000, retained EU law and related regulations and FCA rules. It does not focus on the broader accounting and reporting implications of Brexit which are covered in our publication [Closing Out 2019](#).

The extent to which UK companies are affected by these changes will depend on the extent of their relationships with European parents and subsidiaries, where (if anywhere) their securities are traded, and the choices they have made previously.

Choice of accounting framework

Under the Companies Act 2006, companies have a choice of preparing 'Companies Act' accounts (i.e. under UK Financial Reporting Standards (FRSs)) or 'International Accounting Standards' accounts (i.e. those under IFRS as adopted by the EU). Those companies with securities admitted to trading on an EEA regulated market must prepare their consolidated accounts under IFRS as adopted by the EU. 'IFRS as adopted by the EU' are those international standards adopted after an endorsement mechanism under the European IAS Regulation EC 1606/2002.

The International Accounting Standards and European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2019 (SI 2019/685):

- Repeal the IAS Regulation so that it will no longer apply to the UK.
- Introduce a new legal term 'UK-adopted international accounting standards' for IFRS as adopted by the UK. This will apply to UK companies that choose this framework, or which are required to use this framework for accounting periods commencing on or after IP completion day.
- Preserve IFRS as adopted by the EU immediately before IP completion day as the initial set of IFRS as adopted by the UK on IP completion day.
- Provide for a UK mechanism for the adoption of IFRS – this provides that endorsement will be by the Secretary of State but allows for delegation of this function. The government has indicated that it intends to exercise this delegation option to a UK Endorsement Board, which is currently in the process of being established. The UK endorsement mechanism envisages:
 - Consultation as to whether a standard should be adopted – including with users and preparers of accounts, based on certain principles (not being contrary to the requirement to give a true and fair view; conducive to the long term public good; understandability, relevance, reliability and comparability of the financial information).
 - The possibility of adopting a standard in part, although only in exceptional circumstances.
 - A requirement to publish a decision as to whether to adopt a standard in whole, in part, to extend the scope of undertakings eligible to use an option in the standard or not to adopt the standard.
 - A requirement to publish a consolidated text of IFRS as adopted by the UK on a website.
 - A requirement to carry out a post-implementation review of any standard which is likely to lead to a significant change in accounting practice within five years of that standard first being applied.

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- Incorporate into the Companies Act 2006 the requirement for UK companies with securities admitted to trading on a UK regulated market to prepare their consolidated financial statements under IFRS as adopted by the UK.
- Provide a transitional provision for companies that adopt IFRS as adopted by the UK. The law as amended by the regulations (s395, s403 Companies Act 2006) provides that, once a company has started to use IFRS as adopted by the UK, it may only revert to 'Companies Act accounts' (e.g. FRS 101, FRS 102 or FRS 105) once in any five year period, unless there is a 'relevant change of circumstances' (typically delisting or a change of control). Under the transitional provision, if a company is using IFRS as adopted by the EU prior to the adoption of the new regulations, this is treated as equivalent to applying IFRS as adopted by the UK for the purpose of this requirement.

Similar changes are made to the Building Societies Act 1986, the Friendly Societies Act 1992 and related regulations, and to the regulations which apply the Companies Act requirements to Limited Liability Partnerships (LLPs).

The *International Accounting Standards, Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2020 (SI 2020/335)* introduce a further provision allowing entities that prepare financial statements for a period commencing before and ending after IP completion day, or a period which finishes before but where the accounts are filed after IP completion day, the option to apply IFRS as adopted by the UK in those financial statements.

Changes to accounting and audit exemptions available to UK companies after Brexit

The Companies Act 2006 (and the equivalent provisions applicable to LLPs) contain a number of optional exemptions. In some cases these are not available to certain classes of entity. Many of these will change (but without any substantive effect) because the underlying definitions refer to EU law but will now need to refer to UK law. These changes are made by the *Accounts and Reports (EU Exit) Regulations 2019 (SI 2019/145)*, the *Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2019 (SI 2019/177)* and the *Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2020 (SI 2020/108)*.

Several of these changes may have a real effect for a number of companies -- all of which are applicable for the first accounting period commencing on or after IP completion day:

- The exemption from audit (and, if also a dormant company, from preparing and filing accounts) for subsidiaries whose liabilities are guaranteed by an EEA incorporated parent will only be available where the guarantee is given by a UK incorporated parent.
- The exemption from preparation of group accounts on the grounds of consolidation into a larger group changes. The exemption in s400 of the Companies Act 2006 is narrowed to situations where the larger group is headed by a UK parent, and that in s401 is broadened to include all non-UK parents. In practice this is likely to have little initial effect; however, if in future IFRS as adopted in the EU diverges from IFRS as adopted in the UK, the availability of this exemption may change.
- Some exemptions (adoption of the small companies regime (s384 of the Companies Act 2006), small groups not required to prepare consolidated financial statements (s399), medium-sized companies (s467)) rule out companies that are members of an ineligible group. Groups will no longer be ineligible if this had been solely because they contained a company with securities admitted to trading on a non-UK EEA regulated market. This means that small subsidiaries of a parent listed in the EEA may now be able to take these exemptions.

In the directors' report, the requirements to disclose information in respect of political donations and expenditure will change for accounting periods commencing on or after IP completion day. The detailed disclosures of individual donations and expenditure will be restricted to the UK (previously it applied throughout the EEA). Political donations and expenditure in the EEA will be included in a single worldwide aggregate figure.

Large public interest entities must include a 'non-financial information statement' within their strategic report (s414CA) unless they are included within a consolidated non-financial information statement prepared by an EEA parent undertaking. For accounting periods commencing on or after IP completion day, this exemption will only be available to those entities with a UK parent that prepares a consolidated non-financial information statement.

Other changes

Impacts on EEA incorporated subsidiaries of UK incorporated parent undertakings

There may be indirect effects of the UK ceasing to be a 'member state' which will apply immediately on IP completion day to companies incorporated elsewhere in the EEA (unless these matters are addressed in any future economic agreement or through concessions made by individual member states):

- Subsidiaries that wish to rely on the audit, preparation and filing exemptions (if available in their member state) on the grounds of being consolidated into an EEA parent which guarantees their liabilities will no longer be able to rely on the UK parent to give such a guarantee. This may necessitate additional audits in those countries unless another holding company can be found to give such a guarantee.
- Subsidiaries which are in turn parent entities that rely on being included in a UK consolidation for their own exemption from preparation of consolidated financial statements will only be able to do so if their member state has taken the option to exempt subsidiaries of non-EEA parents – not all member states have.
- Subsidiaries which cannot take certain exemptions in their national law solely because they are included in a group with a UK financial institution may now be entitled to exemptions as those UK entities will no longer be EEA regulated entities.
- Large public interest entities reliant on a UK parent's non-financial information statement to exempt them from preparing their own will lose that exemption.

Changes to the accounting requirements for qualifying partnerships after Brexit

The *Partnerships (Accounts) Regulations 2008* require certain partnerships, known as qualifying partnerships, to prepare accounts unless they are exempt on the grounds that they are dealt with on a consolidated basis in the financial statements of an entity incorporated under the laws of a member state. For financial years commencing on or after IP completion day, the exemption will only be available if the qualifying partnership is dealt with on a consolidated basis in the financial statements of a UK parent.

Impact on UK companies with a branch or place of business elsewhere within the EEA

UK companies with a branch or place of business in another EEA country will now count as a non-EEA company in that country. Under that EEA country's law there may be additional overseas companies filing requirements which cannot be met by simply filing the UK annual report and accounts.

Changes to the accounting requirements for overseas companies and those Societas Europaea with a registered office outside the UK which have a branch or place of business in the UK

The *Overseas Companies Regulations 2009* require overseas companies with a branch or place of business in the UK to file accounts in the UK. These regulations have two regimes:

- One for entities required to prepare, have audited and disclose accounts under their national law, who can simply file their national law accounts in the UK.
- One for entities that have no such requirement – for which more detailed requirements apply.

Previously entities incorporated elsewhere in the EEA but which were exempt from audit could use the first regime; they will not be able to in future. This will have little effect for many such companies; but for small EEA companies with a UK branch additional disclosures may be required, and a profit and loss account will need to be filed even if it is not needed in the home state.

A Societas Europaea is a company treated as incorporated 'in Europe' – it adopts the company law requirements of the member state in which its registered office is located. Currently, if the registered office is not in the UK then no accounts need to be filed in the UK, even if it has a place of business or branch here. For financial years commencing on or after IP completion day, they will be treated like any other overseas company – requiring accounts to be filed in the UK if there is a branch or place of business here.

Changes relating to Societas Europaea with a registered office in the UK

The *European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2018* (SI 2018/1298) provide that a Societas Europaea with a registered office in the UK will become a UK Societas on IP completion day. It will be subject to the normal UK Companies Act accounting, reporting and audit requirements applicable to a public limited company (PLC).

Changes for mining, quarrying and logging undertakings

The *Reports on Payments to Governments Regulations 2014* (SI 2014/3209) require large or public interest entities that are mining, quarrying and logging undertakings to prepare a report covering payments to governments. The regulations exempt such entities if they are included in a consolidated report prepared under the law of an EEA state; for accounting periods commencing on or after IP completion day the exemption will be available to those entities with a UK parent, but the regulations allow the Secretary of State to determine that requirements in other countries are 'equivalent' – which will include other EEA countries. In practice, this means that in due course such entities with non-EEA parents may be newly exempt once the Secretary of State has carried out an equivalence exercise – for example, those which are subsidiaries of SEC registrants caught by the similar Dodd-Frank Act requirements.

Changes to audit committee and corporate governance exemptions

In the UK the statutory requirement to have an audit committee contained in Article 39 of the Audit Directive is dealt with in two places.

Section 7.1 of the Disclosure Guidelines and Transparency Rules (DTR) issued by the Financial Conduct Authority (FCA) requires most issuers of securities admitted to trading on an EEA regulated market with the UK as their 'home state' to have an audit committee or equivalent body. This requirement will change in two ways for periods commencing on or after IP completion day:

- Firstly, issuers that are subsidiaries of a parent undertaking that is in turn subject to Article 39 are currently exempt. This will be narrowed to those with a parent subject to DTR 7.1 – i.e. with securities admitted to trading on a UK regulated market. This means that, for example, a UK listed debt issuer of a parent listed in the Netherlands will need a UK audit committee or equivalent body.
- Secondly, the rules will apply to all entities admitted to trading on a UK regulated market; previously, if an entity was listed on more than one EEA regulated market, it may have designated another country as its 'home state' – and comply with that country's rules instead.

The Prudential Regulation Authority (PRA) implements the Article 39 audit committee requirements for banks, building societies, Solvency II insurance undertakings, the Society of Lloyd's and Lloyd's managing agents in their Handbook. The PRA has proposed that after IP completion day:

- The existing exemption for non-significant regulated firms with an EEA parent that complies with Article 39 will be narrowed to those with a UK parent. This may require UK incorporated subsidiaries currently reliant on a non-UK parent's audit committee to establish their own.
- The existing exemptions for financial years commencing prior to 17 June 2018 which refer to EEA parents will also be amended to apply to all third country parents. This will now be a small number of entities so no further details are given here.

The PRA has not as yet made the instrument which will effect these changes; this is now expected to be made at the end of the implementation period.

DTR 7.2 also requires most issuers of securities admitted to trading on an EEA regulated market with the UK as their home state to make certain corporate governance disclosures. For financial years commencing on or after IP completion day, these will apply to all entities listed on a UK regulated market, regardless of their current 'home state'.

Cross-border listings

Impact on UK incorporated companies listed on a regulated market in another EEA country

The UK will no longer be treated as a 'member state' after IP completion day. This means that, with immediate effect:

- Companies will need to adopt a GAAP that is 'equivalent' to IFRS as adopted by the EU. IFRS as adopted by the UK has not yet been determined to be equivalent. Until such time as it is, companies will (as long as it remains true) wish to state compliance with IFRS as adopted by the EU (for financial years commencing prior to IP completion day – when this is acceptable under both UK and EU law) and with both IFRS as adopted by the UK and either IFRS as issued by the IASB and/or as adopted by the EU (for financial years commencing on or after IP completion day).
- UK auditors will no longer be EEA auditors, and so will need to register in the relevant EEA country as a Third Country Auditor.
- The UK will no longer count as a "home state" under EU law, and so the annual report will need to be filed in both the UK and the new "home state" within the EEA. UK companies may wish to contact the relevant state's regulator to tell them of their new "home state".

These are not specific rule changes – they are a consequence of applying existing EU legislation to the UK as a third country.

Impact on EU incorporated companies listed on a UK regulated market

The UK changes for EU companies listed on a regulated market will have little immediate impact:

- Companies will need to adopt a GAAP that is 'equivalent' to IFRS as adopted by the UK. The *Prospectus (Amendment etc.) (EU Exit) Regulations 2019 (SI 2019/1234)* clarify that, for non-UK issuers, IFRS as adopted by the EU will continue to be allowed (as well as IFRS as issued by the IASB and the GAAPs of the US, Japan, Peoples' Republic of China, Canada and South Korea). The *Official Listing of Securities, Prospectus and Transparency (Amendment etc.) (EU Exit) Regulations 2019 (SI 2019/707)* provide that IFRS as adopted by the EU is equivalent to IFRS as adopted by the UK. The law will extend the existing UK 'third country auditor' regime to EEA auditors, and so EEA auditors of entities with equities or retail debt securities admitted to trading on a UK regulated market will need to register in the UK. However, the FCA's rules will provide that such a registration is only needed in respect of financial years commencing on or after IP completion day; for earlier periods an EEA auditor is qualified under DTR 4.1.7.
- The DTR will apply in all cases even if there is also a listing elsewhere in the EEA. This means that the annual report will need to be filed in the UK and comply with the FCA's rules, rather than just relying on a non-UK "home state" regulator.

Further information

The Regulations discussed above are available from legislation.gov.uk:

- [The Accounts and Reports \(Amendment\) \(EU Exit\) Regulations 2019 \(SI 2019/145\)](#)
- [The Statutory Auditors and Third Country Auditors \(Amendment\) \(EU Exit\) Regulations 2019 \(SI 2019/177\)](#)
- [The Statutory Auditors, Third Country Auditors and International Accounting Standards \(Amendment\) \(EU Exit\) Regulations 2019 \(SI 2019/1392\)](#)
- [The Statutory Auditors and Third Country Auditors \(Amendment\) \(EU Exit\) Regulations 2020 \(SI 2020/108\)](#)
- [The International Accounting Standards and European Public Limited-Liability Company \(Amendment etc.\) \(EU Exit\) Regulations 2019 \(SI 2019/685\)](#)

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- [The International Accounting Standards, Statutory Auditors and Third Country Auditors \(Amendment\) \(EU Exit\) Regulations 2020 \(SI 2020/335\)](#)
- [The Companies, Limited Liability Partnerships and Partnerships \(Amendment etc.\) \(EU Exit\) Regulations 2019 \(SI 2019/348\)](#)
- [The European Public Limited-Liability Company \(Amendment etc.\) \(EU Exit\) Regulations 2018 \(SI 2018/1298\)](#)
- [The Official Listing of Securities, Prospectus and Transparency \(Amendment etc.\) \(EU Exit\) Regulations 2019 \(SI 2019/707\)](#)
- [The Prospectus \(Amendment etc.\) \(EU Exit\) Regulations 2019 \(SI 2019/1234\)](#)

The Financial Reporting Council and the Department for Business, Energy and Industrial Strategy (BEIS) have also published letters for auditors and accountants with information regarding auditing, accounting and corporate reporting standards during the transition period. These are available [here](#).

If you have any questions about the proposals, please speak to your usual Deloitte contact.



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