

The Financial Reporting Council refuses to bite the bul...

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The Financial Reporting Council is still the regulator of UK auditors. Plans for change have been announced, but nothing has happened as yet. So, we continue with an authority that has persistently been proven to act in the best interests of the accounting profession rather than those of the public.

The pattern is being repeated this morning. The Financial Reporting Council has issued a demand to the Big 4 accounting firms. It [has said that its objectives are:](#)

Objective 1: Improve audit quality by ensuring that people in the audit practice are focused above all on delivery of high-quality audits in the public interest.

Objective 2: Improve audit market resilience by ensuring that no material, structural cross subsidy persists between the audit practice and the rest of the firm.

As explanation it has said:

In pursuing these objectives, we will seek to ensure that audit remains an attractive and reputable profession and increase deserved confidence in audit.

But there are massive problems inherent in the principles it has laid out. They have said that their objectives are:

- * Audit practice governance prioritises audit quality and protects auditors from influences from the rest of the firm that could divert their focus away from audit quality.
- * The total amount of profits distributed to the partners in the audit practice should not persistently exceed the contribution to profits of the audit practice.
- * Individual audit partner remuneration is determined above all by contribution to audit quality, taking account of the degree of difficulty and risk of the audits.
- * Audit practice financial reporting is transparent to the regulator and public, allowing effective monitoring of audit practice performance and financial resilience.
- * The culture of the audit practice supports audit quality and the public interest by

encouraging ethical behaviour, openness, teamwork, challenge and professional scepticism/judgement.

* Auditors should act in the public interest and work for the benefit of shareholders of audited entities and wider society; they are not accountable to audited entities' executive management and are not (nor viewed as or considered to be) consultants.

In other words, they are saying that audit must be separated from the other parts of the Big 4 firms but are not asking that in practice the firms be split. And that makes no sense at all.

If you are going to separate, as the FRC demands, then it makes sense that the activities be entirely separate.

If you are going to remove cross-subsidy, do so beyond any doubt.

And if you are going to have proper governance structures then make sure they are wholly independent of a consulting firm.

In other words, create a wholly new and separate audit market where the price will undoubtedly be considerably higher than it is now.

This is what is very obviously necessary but still the FRC will not say it. And as a result they over-arching question over the newly announced process is 'why is it that the FRC is holding back, and in whose interests is it still really acting?'

Whilst that doubt persists the FRC can say what it wants, but it remains an ineffective regulator. We cannot afford such a regulator now. Three things follow.

First, the FRC has to, finally, be replaced.

Second, audit, and not just in the Big 4, has to be split from other activity.

Third, companies have to be told to be prepared to pay the proper force for an audit. The days of subsidy at the cost of quality have to be over, and what the FRC is doing is not enough to prove that as yet.