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Guidance note on the eligibility requirements in Audit Regulation 2.03



Purpose

This guidance is published by ICAS to assist firms in understanding the eligibility requirements in Regulation 2.03 of [ICAS' Audit Regulations](#) ("the Regulations") which are shared with the Institute of Chartered Accountants in England & Wales, and the Institute of Chartered Accountants of Ireland.

As Regulation 2.03 does not apply to sole practitioners who are not incorporated, any questions on their eligibility are not covered in this guidance and should be directed to ICAS.

This guidance must be read alongside the Regulations, as it is the Regulations which provide full details of the auditor eligibility requirements.

This guidance is written for firms which are registered by ICAS. While the eligibility requirements are applied consistently by the professional bodies, firms registered by ICAEW, ICAI, and ACCA should consult their registering body wherever assistance is required.

Firms which have a separate registration with the Financial Reporting Council (FRC) for auditing Public Interest Entities (PIEs) should contact the FRC to discuss PIE auditor eligibility compliance.

Importance of auditor eligibility

All firms must ensure that they satisfy the eligibility requirements to be auditors; not only at the point of applying for audit registration, but for the full duration of the licence.

Any failure to meet the eligibility requirements could invalidate any audit reports signed by the firm and may lead to regulatory and / or disciplinary action being taken by ICAS against the firms and its principals.

Basis of requirements

As the Competent Authority for audit in the UK, the Financial Reporting Council (FRC) has ultimate responsibility for the performance and oversight of the audit regulation tasks, including setting the eligibility criteria.

The FRC publishes [Eligibility Criteria](#), which are then replicated by the professional bodies in the Regulations. Through ongoing supervisory activities, the FRC ensures that the professional bodies are taking robust action to ensure that firms continue to satisfy the eligibility requirements.

Changes in requirements

Firms should ensure that they pay proper attention to changes in the eligibility criteria, as these may require pro-active steps to be taken to maintain compliance. Changes will always be communicated to firms by ICAS, with sufficient time being given to allow for remedial action.

Key requirements

This sections provides a high-level summary of the key eligibility requirements, with firms reminded that full information can be found in the Audit Regulations.

Principals

Each of the firm's principals – whether or not they are involved in audit work – must fall into one of the stated categories. This covers partners, directors, and members, depending on the firm's corporate structure.

- Principals who are individuals must be either be a member of ICAS, ICAEW, ICAI, or ACCA, or registered as an audit affiliate.
- There are allowances made for auditors qualified in European Economic Area (EEA), which should always be discussed directly with ICAS.

Some firms have corporate principals – i.e. limited companies or LLPs which are listed as directors or members of the firm. The Regulations require such principals to be registered as corporate affiliates or audit firms in their own right.

Firms should ensure that all principals meet the eligibility requirements in the Regulations.

Directing the firm's policy and altering its constitution

Individuals with the audit qualification (whether issued by ICAS or one of the other professional bodies), and corporate principals registered as auditors (i.e. registered audit firms), must hold at least a majority of the following voting rights in the firm:

- Voting rights under the firm's constitution to enable them to direct its overall policy or alter its constitution.
- Voting rights on the firm's management board – if one exists – to enable them to direct its overall policy or alter its constitution. The Audit Regulations define a management board as “*The committee, board or other body which administers or manages the firm*”. It may be called various things by firms.

Neither the FRC nor the professional bodies take a prescriptive approach to exactly what is covered by 'directing the firm's overall policy'. Firms are encouraged to apply common sense, with the following factors likely to be relevant:

- The significance of the impact of the decision in terms of the firm, its employees, its clients, and the public interest. To what extent would a decision change the firm's current practice?
- The extent to which the decision impacts the firm's audit functions (as opposed to other commercial workstreams).
- Any likely or potential impact on audit quality and / or regulatory compliance.

While firms may contact ICAS to discuss such matters as and when they arise, as the ultimate decision rests with the firm, it may be better to take external legal advice on whether a certain decision does direct its overall policy.

It should be easier to identify whether a decision will alter a firm's constitution. This could include changes to the firm's name, its corporate structure, or voting rights. As the Regulations do not set a *de minimis* limit here, all changes to a firm's constitution are covered by the requirement.

'Super majorities'

Whilst the normal meaning of majority is greater than 50%, firms should be mindful that there may be occasions where a higher threshold is applied. For example, the Companies Act specifies matters which require approval through a Special Resolution, which means a majority of not less than 75% (e.g. changes to the company name or Articles of Association). Firms may also decide to include higher voting thresholds for other decisions in their governance documents (sometimes referred to as 'reserved matters'). This issue does not only affect incorporated firms, with partnership agreements also commonly having reserved matters which may require consideration.

To the extent that any such decisions direct the firm's policy or alter its constitution, the firm must ensure that individuals with the audit qualification hold at least a majority of the following voting rights.

Firms must understand and comply with the requirements for certain decisions to be taken by individuals with the audit qualification or corporate principals registered as auditors.

Requirements for Articles of Association

Regulation 2.03(d) sets out six required inclusions for a corporate practice's Articles of Association, relating to the interactions between the firm's principals and its shareholders.

Actions to ensure eligibility

If a firm considers that its corporate structure may not comply with the eligibility requirements, it is important that two steps are taken without delay: (i) notification to ICAS, and (ii) identifying steps which could be taken to achieve compliance.

In terms of (ii), firms should consider taking legal advice, given the important impact which such action could have on the firm, its principals and shareholders. Common steps include changes to the wording of governance documents and transfers of shareholdings.

Dispensation

Where a firm ceases to meet one of more of the eligibility requirements, ICAS' Authorisation Committee may grant a 90-day dispensation from the requirement to comply with the relevant provision in the Regulations. This will only be appropriate where the Committee considers that the firm is taking all practical steps and that these will remedy the position, and there are no grounds to believe that granting the dispensation will adversely affect an audit client or any other person.

Full information on the dispensation process is contained in Regulations 2.17 to 2.20. If a firm fails to appropriately remedy matters within the 90-day period, it is likely that the Committee will remove the firm's audit registration.

Changes within firms

Firms need to carefully consider their compliance with the eligibility requirements whenever they are considering changes to the firm's structure or composition.

Regulation 2.11 ('change in circumstances') lists various matters which must be reported to ICAS *"in writing as soon as practicable, but not later than 10 business days after the event"*. This includes matters which could impact the firm's audit eligibility, including changes in the firm's principals, and changes in shareholders / shareholdings.

Firms contemplating a change in corporate structure are strongly encouraged to contact ICAS at the earliest opportunity to discuss the impact of possible changes on audit eligibility.

As significant work might be required for ICAS to fully assess a new corporate structure, auditors should not delay in reporting proposed changes.

Firms which have a separate registration with the FRC for audits of Public Interest Entities (PIEs) must also ensure that they also meet the FRC's notification requirements.

Further information

Further information in respect of the issues set out in this guidance can be requested by contacting the Authorisations Team at ICAS: regulatoryauthorisations@icas.com

As noted above, while ICAS will assist firms in understanding the eligibility criteria, decisions over corporate structures, governance, shareholdings etc will always rest with firms. Careful consideration should be given to obtaining appropriate external legal advice.