



19 September 2012

Our ref: ICAEW Rep 137/12

Your ref:

Anna Colban  
Secretary to the AADB  
Financial Reporting Council  
5<sup>th</sup> Floor, Aldwych House  
71-91 Aldwych  
London WC2B 4HN

Dear Anna,

**Proposed changes to the Disciplinary Schemes**

ICAEW is pleased to respond to your request for comments on the FRC consultation on proposed changes to the Disciplinary Schemes.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

**Vernon Soare**  
Executive Director

**T** +44 (0)20 7920 8787  
**E** [Vernon.soare@icaew.com](mailto:Vernon.soare@icaew.com)





## ICAEW REPRESENTATION

### CONSULTATION ON PROPOSED CHANGES TO THE DISCIPLINARY SCHEMES

**Memorandum of comment submitted in September 2012 by ICAEW, in response to the Financial Reporting Council's consultation paper Disciplinary Schemes Proposed Changes published in June 2012**

| <b>Contents</b>                 | <b>Paragraph</b> |
|---------------------------------|------------------|
| Introduction                    | 1                |
| Who we are                      | 3                |
| Major points                    | 9                |
| Responses to specific questions | 18               |

## INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the consultation paper Disciplinary Schemes Proposed Changes published by the Financial Reporting Council (FRC) in June 2012, a copy of which is available from this [link](#).
2. All comments in this response constitute the ICAEW's response to the consultation paper and not just those responses to the specific questions. Responses relate only to the Accountancy Scheme.

## WHO WE ARE

3. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 140,000 ICAEW Chartered Accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
4. ICAEW Chartered Accountants operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.
5. ICAEW is a Recognised Supervisory Body (RSB) under the provisions of Schedule 10 of the Companies Act 2006 (Schedule 10). ICAEW is the largest of the UK's RSBs, regulating some 3,800 registered audit firms. Under the Schedule 10 provisions, inter alia, the rules and practice of the RSB relating to the discipline it exercises over its members must be fair and reasonable and include adequate provision for appeals. The RSB must also have effective arrangements for the investigation of complaints against persons eligible under its rules for appointment as a statutory auditor. The RSB may make provision for the whole or part of the function of these arrangements to be the responsibility of an independent body or person.
6. Under Schedule 10, the RSB must participate in appropriate arrangements that ensure that the carrying out of investigations, the holding of disciplinary hearings and the taking of disciplinary action in relation to public interest cases in connection with the performance of statutory audit functions by the RSB's members and /or member firms are done independently of the RSB. Public interest cases means matters which raise or appear to raise important issues affecting the public interest.
7. The Accountancy and Actuarial Discipline Board (AADB), a subsidiary of the FRC, is the independent body that investigates public interest statutory audit cases and, where appropriate, takes disciplinary action against the RSB's members in relation to such cases. Following a recent reorganisation of the FRC this independent function will transfer from the AADB to the FRC's Conduct Committee, which will assume day to day responsibility for the oversight and maintenance of the disciplinary arrangements.
8. The AADB Accountancy disciplinary scheme (the Scheme) has operated since 2004. With the agreement of the participating professional accountancy bodies (the professional bodies), the Scheme provides for the investigation of public interest statutory audit matters and other non-statutory audit matters in relation to professional, business and financial activities. Consequently, the Scheme has wider scope than that strictly required by the provisions of Schedule 10.

## MAJOR POINTS

9. The consultation paper proposes a number of changes to the scheme many of which are sensible and straightforward. However, we highlight the following proposals as requiring specific comment:-

### 10. Independence

10.1 We have previously put on record in our response to the joint BIS/FRC consultation on the reform of the FRC (October 2011) our concerns regarding the ultimate accountability of the FRC. These concerns extend to the new governance arrangements for oversight of the Accountancy Scheme. The new Conduct Committee combines several roles previously separated between the former Professional Oversight Board, AADB, the Independent Convenor and Executive Counsel. Combined with proposed Scheme changes which reduce or remove the requirement for consultation with or the consent of the Recognised Supervisory Bodies (which retain significant statutory responsibilities), there is a risk that conduct matters will be determined without effective accountability and with exposure to judicial review.

10.2 Regarding the following proposals in the current consultation:

- (1) Launching an investigation (paragraph 5 (8))
- (2) Preliminary enquiries (Paragraph 5 (10))
- (3) Scope Extensions (Paragraph 6 (8))
- (4) Amending the Scheme (Paragraph 18)

10.3 The common theme of these proposals is the removal of the requirement on the FRC to either obtain the consent of the professional bodies before taking certain steps (amending the Scheme) or to consult with them (launching an investigation, preliminary enquiries and scope extensions).

10.4 In relation to the launching of an investigation on the FRC's own initiative, the proposal is that the current requirement to first consult with the professional bodies is removed. It is said that consultation can add up to three months to the process of starting an investigation. The first point we would make is that the paper does not provide any example or examples of when consultation has resulted in delay. Certainly, it is our experience that any consultation is generally straightforward and not prone to delay. Secondly, we think it important that the professional bodies continue to play a role in the investigation of individual complaints. Indeed, the paper recognises that this involvement can add value to the process and may lead to a more informed decision. Whilst we fully support the continuation of close liaison at an operational level between FRC staff and those of the professional bodies, we currently fail to understand the need for the consultation requirement to be removed. The risk must be that the lack of any formal requirement results increasingly in decisions being taken by the FRC in isolation.

10.5 In relation to preliminary enquiries, these are currently carried out by the AADB following consultation with the relevant RSB(s). Efforts were made two years ago by the RSBs to formalise these arrangements with the AADB via a protocol. We do not know why the protocol previously drafted by the FRC on which we commented has not materialised and why the FRC failed to conclude the matter with any final correspondence. But we do not think that the fact that the protocol has not materialised justifies the launching of preliminary enquiries arbitrarily. We support the concept of a protocol and it should extend beyond simply preliminary enquiries. Rather it should do two things. Firstly, set out the criteria on which the FRC will call in and investigate cases. This already exists in the FRC's publication "*What cases will be dealt with by the AADB*". However, there is an opportunity

for a protocol to formalise these criteria and so clarify that the liability test in paragraph 4 (1) of the Scheme applies to the investigation of serious acts and omissions where in the public interest to do so. Secondly, the protocol should clearly set out those steps to be taken under the Scheme following consultation with the relevant professional body or bodies. ICAEW remains willing to sign and operate such a protocol.

- 10.6 Scope extensions currently require the FRC to consult with the professional bodies. The ICAEW has never resisted such a request and, again, we question the basis on which the need to consult should be removed. The premise is that consultation can lead to delays of 1-2 months. But no examples are provided as to when such delays have occurred. Whilst we fully support the FRC's desire to progress cases as quickly as possible we do not think it wise to potentially remove the involvement of the professional bodies in this respect without there being evidence that this is actively hampering the investigation of actual cases.
- 10.7 Amendments to the Scheme. The proposal is to replace the requirement to obtain the consent of the professional bodies to changes to the Scheme with a requirement for the FRC to instead consult with the professional bodies on changes to the Scheme. It is proposed that there would be a mechanism for resolving disputes about whether a change or changes should be made following consultation; for example, by referring the dispute to a retired senior judge. To remove the requirement to obtain consent is clearly a significant step. Yet, the consultation paper sets out no basis or bases for such a radical departure from the current position. As the paper says, the professional bodies have a legitimate interest in the operation and funding of the scheme, and, we would add, its scope. Consequently, we do not think that changes to the Scheme should be made without the agreement of the professional bodies that fund it. No matter how robust any dispute resolution mechanism is, it is a fundamental principle of the Scheme, in our view, that it should only be amended where the professional bodies and the FRC agree. Consultation is not a legitimate substitute for agreement in this context.
- 10.8 In summary, we stress that we have no wish to hamper the FRC in the speedy and effective operation of the Scheme generally and the investigation and resolution of individual cases. Nevertheless we consider that the FRC's proposals here are not sufficiently evidenced. Proposals to remove or restrict the involvement of the professional bodies in certain respects must be based on clear evidence that that involvement actively limits and restricts the effective operation of the scheme. No such evidence is provided.
11. Concluding cases without a Tribunal hearing (Paragraphs 6 (12) to 6 (18)). It appears to us sensible to provide for appropriate matters to be resolved without a full disciplinary hearing not least as this may avoid unnecessary expense. Historically, where complaints of misconduct have been admitted, this has been achieved through the 'Carecraft'<sup>1</sup> process. The proposal is now that the Executive Counsel and the Member or Member Firm may enter into settlement discussions in appropriate cases with any proposed settlement being subject to approval by two Settlement Approvers drawn from the Case Management Committee of the FRC.
12. The mechanism set out in the consultation paper envisages that the Executive Counsel may decide, having regard to the public interest, that a matter is appropriate for settlement discussions. He may decide this at any point after he serves a notice informing the Member or Member Firm of his intention to deliver a Formal Complaint and setting out the substance of the allegations and inviting written representations, and prior to delivery of the Formal Complaint. Consequently, any settlement discussions will take place prior to delivery of a Formal Complaint. It is not clear, therefore, that any settlement will involve an admission or admissions by the Member or Member Firm of a specified complaint. In our view, in any transparent settlement process, it must be clear what admissions are being made in relation to

<sup>1</sup> So called after the case of *Re: Carecraft Construction Co Limited* [1994] 1 WLR 172

which specific complaints. Otherwise, there is the risk of matters being settled on a vague basis without any admissions at all.

13. As is recognised in the consultation paper, it is vitally important that any settlement is transparent and that decisions to settle cases are taken by those with objectivity who are separate from the investigation process and settlement discussions. We think this would be better achieved without any additional cost or delay by convening an independent tribunal to consider, approve or reject proposals for settlement. In our view, this would better safeguard the need for an independent and transparent process. Should a settlement not be approved by the tribunal and the matter proceed to a full disciplinary hearing, a fresh tribunal panel would be convened. Subject to this, the potential for settlement should be available up to the full disciplinary hearing.
14. Further, insofar as it is not made clear in the consultation paper, the Executive Counsel should be subject to a requirement to provide the tribunal convened to consider settlement with representations detailing the proposed terms of settlement and why any settlement is in the public interest. The tribunal should be required to publicise its reasons for approving or rejecting a settlement. The terms of any settlement should be publicised.
15. Interim Orders (Paragraph 13)). The consultation paper does not evidence why these orders are necessary in the operation of the Scheme. The paper refers to circumstances where an interim order could be in the public interest without setting out what those circumstances may be. It should be borne in mind that the professional bodies have a regulatory jurisdiction and will often have considered whether to make an interim order under their own powers before a disciplinary matter is referred to, or is taken up by, the FRC. Consequently, it should be clear that any powers to make interim orders under the Scheme are expressly without prejudice to the professional bodies' own powers to make such orders. Otherwise there is likely to be scope for different regulators to be played off one against the other.
16. We also query the need for interim orders under the Scheme given the recently enhanced powers of the Audit Quality Review team (formerly the Audit Inspection Unit) of the FRC.
17. It is envisaged that the Executive Counsel can apply for an interim order at any stage after it has been decided to investigate a matter and prior to a full Disciplinary Tribunal hearing. In this context and in the context in which the Scheme operates, the proposed interim order to suspend a practising certificate for a period prior to a full Tribunal hearing appears draconian as no Adverse Finding on the merits will have been made when suspension is ordered. Indeed, no Formal Complaint may have been delivered. Further, although suspension is subject to review, it is not subject to any long stop and is, effectively, unlimited. Further, it is proposed that an order suspending membership may be made. ICAEW has no such power.

## RESPONSES TO SPECIFIC QUESTIONS/POINTS

**Q1: Should the Schemes be amended as set out in paragraphs 3.3 to 3.11 so as to enhance the independence of the disciplinary arrangements?**

18. Please see our response at paragraph 10 of this paper.

**Q2: Are the proposals to conclude cases without the need for a tribunal hearing appropriate? (paragraphs 3.12 to 3.13)**

**19.** We have already commented on this proposal. Please see paragraphs 11 to 14 of this response. We do not oppose the proposal in principle but have some concerns about the transparency of the proposed mechanism which we suggest could be improved.

**Q3: Do you agree with the role envisaged for the Case Management Committee? (paragraph 3.15)**

**20.** We agree the proposals in relation to the Case Management Committee.

**Q4: Are the proposals to facilitate the timely completion of investigations and disciplinary proceedings appropriate? (paragraphs 3.16 to 3.18)**

**21.** The proposal to introduce time limits (which can be extended) within which Members and Member Firms must respond with any representations to a proposed complaint appears reasonable to us.

**Q5: Should the Executive Counsel be able to seek an interim order against a member or member firm? If so, are the proposed provisions in paragraph 3.19 appropriate?**

**22.** We have set out at paragraphs 15 to 17 of this response our comments on the proposal. We suggest that greater explanation is required as to why such orders are necessary and the circumstances in which they might be relevant. The specific proposals regarding the suspension of practising certificates and membership currently appear to us to be unnecessary and onerous.

**Q6: Do you have any proposals to amend the investigation test? (paragraphs 3.24 to 3.29)**

**23.** Whilst we note what is said in the consultation paper we are not aware that any specific amendments have been proposed to paragraph 4 (1) of the Scheme to give effect to any such change. Generally, it is important to make clear that the Scheme is only concerned to investigate and make Adverse Findings, where appropriate, in relation to serious matters in the public interest. Insofar as there is any doubt that that is the case, the FRC and the Scheme should make this entirely clear in the underpinning principles and Scheme wording. In relation to, specifically, misconduct sufficient to found an investigation and, potentially, an Adverse Finding, it should, of course, be clear that this is concerned with serious acts and omissions that have serious impact and repercussions. We have suggested that a protocol would be helpful in this respect (see paragraph 10.5 above).

**24.** Within this context, where the FRC decides to investigate, we would expect that investigation to encompass all matters arising out of the particular case and not leave any relatively less serious issues to be dealt with by the participating professional bodies. Otherwise there are risks in not dealing with all related issues in one forum.

**Q7: Do you have any other comments on the proposed Schemes or the points raised in the paper?**

**25.** Paragraph 9 (1) Tribunal appointments. The proposal is that the responsibility for appointing members of the Tribunal Panel is transferred from an independent Convener to the Conduct Committee. The Convener will continue to appoint individual Tribunals from the Panel. This is different from ICAEW disciplinary procedures under which individual panel members are nominated by an independent nominating committee and individual tribunal panels are appointed by the Chairmen of the disciplinary committees. We consider that panel members should be appointed by an independent committee and be subject to independent scrutiny.

**26.** Paragraphs 2 (1) and 4 (7) Successor Member Firms. The intention appears to be to make successor firms responsible for acts/omissions of predecessor firms in circumstances where the successor entity may bear no legal responsibility. In principle, we have no difficulty with a



suggestion that a successor firm which is substantially the same entity should continue to be responsible for the failures of a firm which it has acquired. Nor do we have any difficulty with individual owners of accountancy firms having personal responsibility to meet fines and costs that might be imposed. But the consultation paper does not explain why this change is required nor spell out its potential effect. We are, for example, unclear as to how this concept will read across to the imposition of fines under sanctions guidance, given that the proposal is to link fines, where appropriate, to group turnover.

E paul.bentall@icaew.com

Copyright © ICAEW 2012  
All rights reserved.

This document may be reproduced without specific permission, in whole or part, free of charge and in any format or medium, subject to the conditions that:

- it is appropriately attributed, replicated accurately and is not used in a misleading context;
- the source of the extract or document is acknowledged and the title and ICAEW reference number are quoted.

Where third-party copyright material has been identified application for permission must be made to the copyright holder.

[icaew.com](http://icaew.com)