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Dear Sirs

The Accountancy & Actuarial Discipline Board (the "AADB"): Sanctions Guidance to Tribunals

RPC act for a number of the UK's top 20 accountancy firms and/or their PI insurers. We have canvassed our clients in relation to the AADB consultation paper of April 2012, and set out below a representative response on behalf of our clients. A list of the firms and organisations who wish to be expressly named is set out at the end of this response. Unless it is expressly stated otherwise, this representative response represents both our and our clients' views.

We respond below to each of the invitations for comment:

1. ***Do you agree with the AADB's objective and approach to sanctions guidance?***

1.1 We agree with the policy objectives that sanctions guidance should promote consistency, clarity, accessibility and fairness for Tribunals to determine sanction, both for the Tribunal and respondent. It should be available to all parties from the outset so that respondents may reasonably predict and react to a consistent sanctions approach.

2. ***Do you agree that Tribunals need a clear framework for sanctions which reflect the nature of its cases and the wider context in which the accountancy profession operates today?***

2.1 We agree. We comment however, that sanctions guidance should be advisory, rather than binding and applied rigidly in every case. There will be exceptional cases where a Tribunal may not wish to slavishly follow guidance, although in cases where this is appropriate, we agree that any departure should be explained, and that this should remain the exception rather than the norm.

3. ***Do you agree that the sanctions imposed by Tribunals should act as a credible deterrent and be proportionate to the seriousness of the misconduct and to all the circumstances of the case, including the financial resources of Members and the size and financial resources of Member Firms?***

3.1 We agree, that where misconduct is established by a Tribunal, sanctions should act as a credible deterrent and be both proportionate to the seriousness of misconduct and to all the circumstances of the case. However, the proposals for the levy of a fine based on the financial resources of Members and Member Firms raise a number of issues of concern requiring clarification, which we highlight below.

4. ***Have we included the sorts of factors in the sanctions guidance that you would expect to see taken into account by Tribunals?***

4.1 Yes.

5. ***Are there any factors you believe Tribunals should take into account when deciding sanctions we have overlooked?***

5.1 Please see our comments below at paragraph 7.4.

5.2 In addition, we believe greater consideration should be placed upon the length and delay of an investigation, which may be wholly outside the control of the firm or individual in question. An investigation lasting a number of years can (and does) have an extremely detrimental impact on an individual, not least from a professional perspective (with investigations being publicly announced), but also on a personal level. Delay can extremely exacerbate the stress of being under investigation, and this alone can serve as a credible sanction as far as individual members are concerned.

The Consultation proposes that it will normally be appropriate to take action against both the Member Firm and individual Members. However, it should be queried whether it is reasonable to take action against a Member Firm for the actions of "rogue partners". A Member Firm may have in place the utmost quality systems and controls, monitoring and implementation, and it is questionable whether a Member Firm should be the subject of sanctions in a situation where an individual Member has acted beyond the bounds of all authority and gone his/her own way. It is difficult to see sanctioning a Member Firm in such circumstances can act as a credible deterrent.

6. ***Do you agree that there needs to be an adjustment in the level of fines imposed in AADB cases?***

6.1 We question whether there is a disproportionate emphasis upon a fine as the only sanction to act as a credible deterrent. There does not seem to be enough consideration of the deterrent value of publicity surrounding an investigation in any event. Of itself, the public announcement of an investigation (even if later unproven) can and does lead to damage to an individual and firm's reputation, together with loss of business and goodwill. In this internet age of immediate publicity, public announcements can curtail (and end) a professional's career and reputation, which is often gained at great expense. The desire to avoid adverse publicity is a very powerful deterrent in itself for professionals subject to AADB jurisdiction. We query whether an upward adjustment in the level of fines is based more upon a public perception need to have "teeth", as opposed to the legitimate aim of acting as a credible deterrent.

6.2 We believe there is a risk that an adjustment towards significantly increased fines could result in substantive, entrenched litigation of AADB investigations. Faced with the prospect of substantially increased fines, Member Firms will have a far greater interest in defending both their reputations and financial resources.

6.3 In addition, we do not agree with the sweeping comment and observation that "there has been a significant change in the accountancy profession over the past decade". Even if

there has been a change, we are not convinced that there has been such a significant shift in the context of which Member Firms operate so as to require an increased level of fines payable for misconduct. Member Firms continue to operate in a very competitive market. Member Firms have to increasingly adopt the highest standards of care, not only to attract new work, but simply to maintain existing work and clients. The Audit Quality Control Team, part of the FRC's Conduct Division itself, encourages a strong compliance regime for Member Firms, and reports publicly on the performance of auditors, in itself acting as a strong incentive to continue to invest in quality. A number of Member Firms are also subject to other regulatory regimes, eg the FSA for corporate finance advisory work, and already take compliance very seriously, having significantly invested over the years in risk management systems and controls. We are not persuaded that the levy of significantly increased fines (as a public policy objective to protect the public) will increase corporate governance and standards of care, or result in greater investment in risk and compliance functions within Member Firms.

7. ***What is your view of the alternative mechanisms proposed for calculating fines?***

7.1 Each mechanism is predicated on an assessment of the seriousness of the misconduct and calculates fines with reference to the financial means of the Member or Member Firm concerned. At its core, the proposal is that group turnover is referenced as the basis for calculating fines on Member Firms.

7.2 We question how it is appropriate and proportionate to base fines upon Member Firms' group turnover. Why has group turnover been chosen as opposed to some other metric such as profit, or fees received for the work done? Please see our further comments below at 8.2.

7.3 The second proposed mechanism links the fine to a staged level of misconduct on a 1-5 level. Levels 1-3 (the least serious) include where a Member Firm takes steps to address the misconduct and report it to the AADB, of its own volition. The reporting thresholds, however, appear ill-defined. If a Member Firm does not think that its conduct is reportable, it could be prejudiced if a Tribunal later decides otherwise.

7.4 The guidance proposes that Tribunals should follow a six step process to determine the right category and level of sanction to impose in any particular case. However, within the process there is no express reference to whether loss has been suffered as a result of the alleged misconduct. As one of the AADB's core aims and objectives is to protect the public, an analysis of whether actual loss has been suffered should, in our view, be incorporated expressly into the six step process.

7.5 It is proposed that tribunals allow a four stage reduction for admissions or early settlement, similar to the FSA regime. However, the FSA regime allows for greater flexibility and the opportunity to discuss on a without prejudice basis. In contrast, the guidance proposes that this discount scheme will "only apply automatically if the Member or Member Firm admits all the heads of complaint of the Formal Complaint". Is that fair? What if incorrect allegations are included in the Formal Complaint? Should a Member or Member Firm be penalised for not admitting all heads of complaint in such circumstances?

7.6 Finally, there is no express mechanism for how and the extent to which fines may be reduced for serious financial hardship caused to an individual Member.

8. ***What level of turnover/income do you consider would be appropriate in respect of each mechanism?***

8.1 Please see our comments above at 7.2.

8.2 We question whether it is fair for a Member Firm's annual group turnover to be the marker for calculating the level of a fine. The proposed guidance states that the term group *"should normally include all entities effectively subject to control by the same management team and with the same beneficial ownership"*. We can see considerable problems, and potential satellite litigation, arising in the absence of a more precise definition.

8.3 As an alternative to referencing annual group turnover, it would appear far more equitable and fair for any fines to be referenced and restricted to the entity which is the subject of the investigation.

8.4 In addition, the proposal is to fine a Member Firm based upon its latest financial statements (i.e. as at the date of the fine). If a Member Firm's profits have grown since the date of breach, which may be many years previously, the Member Firm will be facing a much larger fine than may otherwise have been the case. Furthermore, within a partnership structure, issues may arise as to whether the liability properly falls upon the partners at the time the investigation was commenced or at the time the fine is levied. Would it be more equitable to assess the fine based on a Member Firm's profits as at the date of breach, or afford greater flexibility based on the circumstances?

8.5 It is proposed that an individual Member could be fined a percentage of their total assets. It appears that these are not restricted to a Member's professional income or assets they have derived from their professional activities. Is it fair that a Member/Partner's independent means should be taken into account and, if so, will this act as a deterrent from those with significant independent means from entering the profession?

9. ***Do you agree that a tribunal should not take account of the costs that it is considering awarding against a Member or Member Firm when determining the appropriate level for a fine?***

9.1 We do not agree. It does not appear to be fair for costs not to be taken into account given that the proposed mechanisms for setting the level of fine appears to be tied to the affordability of that fine by the Member Firm. Given the significant level of costs that may apply, there is a danger that a Member Firm will be fined on the basis of what it can afford and then be exposed to a further significant financial penalty of costs.

9.2 Indeed, with the intended significant increase of level of fines, we would expect a greater number of cases to be contested by Member Firms. This will lead to greater expense and a far greater cost exposure. In addition, the current trend of AADB outsourcing its work to commercial law firms is likely to result in profit costs being applied (and subsequently claimed from Member Firms), as opposed to what appears to have been AADB's past practice of charging at cost.

10. ***Do you have any other comments about the proposed structure or content of the sanctions guidance?***

10.1 It is proposed that the new sanctions regime will have retrospective effects that may be highly prejudicial to Member Firms who currently have open investigations with the AADB. In particular, Member Firms may lose the intended opportunity of fixed early settlement discounts, or face much more severe sanctions as a result of the AADB's own failure to pursue investigations promptly. We note that some AADB investigations have been open for a number of years.

We welcome the opportunity to submit this response, and invite the AADB to contact us for further discussion and clarification. We are content for this response to be published.

Yours faithfully

Simon Perkins
for RPC

RPC

List of firms/organisations subscribing to this representative response:

RSM Tenon

Haines Watts

Mazars