

Private and Confidential

General Counsel's Team
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By email:
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6 October 2021

Your ref:

Our ref: [REDACTED]

Please ask for [REDACTED]

Email: [REDACTED]

Dear Sirs

Comments on proposed amendments to The Audit Enforcement Procedure ("AEP") Rules

Thank you for seeking comments on the proposed amendments to the AEP Rules. BDO LLP welcomes the opportunity to review and comment on them before they come into force, which we understand is likely to be on 1 January 2022.

We note that you are seeking comments on both:

- (a) The proposed specific changes (including an indication whether we support the changes); and
- (b) The amended AEP as a whole.

We have carefully considered the amendments, in particular in the context of the two questions above, and set out below some positive areas of improvement and also some areas where, in our view, further additions, clarifications or explanations could be given.

Positive changes

Given that the AEP Rules have now been in force for over 5 years, we entirely support an update to them to reflect how the Rules have been working in practice. In particular, we welcome the following amendments:

- Greater clarity regarding the Case Examiner's role, the investigative steps which could be taken at this early case examination stage and, in particular, the determination of the scope of the investigation at this point (Part 2).
- The introduction of more timescales for certain steps (in particular in Part 4 relating to The Tribunal), which should assist matters to progress at a reasonable speed.
- The codification of the FRC's approach to settlement (Part 6), which gives greater transparency in this area to Respondents.
- The ability for the FRC to amend the scope of an existing investigation (Part 3, paragraphs 12 and 13). In our view this ought to avoid two investigations into the same PIE / firm being opened, often duplicating time, effort and costs.
- The provisions allowing for Joint Tribunals (Part 11, paragraph 153-160). Again, these should also save time, effort and costs as firms will not have to respond to a FRC investigation separately from investigations under the Accountancy or Actuarial Schemes.

Additional broad points for consideration**1. Further amendments at the case examination stage**

Whilst we welcome the additional clarity provided regarding this stage, we consider the new Rules could be amended further to take into account the following points.

First, we note from paragraph 3(d), that going forward the Case Examiner could ask for information in respect of PIE entities / audits from the audited entity itself or its subsidiary as well as the firm. If this power were exercised, it would mean that audited entities may be learning of investigations into their auditor at a far earlier stage than is the case under the existing Rules, which could give rise to a reputational risk which does not currently exist at the case examination stage.

Secondly, it is disappointing that the FRC has not taken the opportunity to amend the Rules such that an audit firm is informed that a matter is being referred to the Conduct Committee, so that the firm can give representations at this point and provide, if applicable, other relevant information which the Case Examiner may not have knowledge about (particularly if the matter has been referred very quickly to the Conduct Committee without a detailed review of the facts and audit file).

Thirdly, given the welcome inclusion of additional detail surrounding the Case Examination process in the Amended Rules, we also recommend that the Guidance for the Case Examiner (in particular the guidance regarding Constructive Engagement set out at paragraphs 13-15 of that Guidance) is updated to reflect the way Constructive Engagement operates in practice and also to reflect the amended AEP Rules.

2. Inclusion of additional set time periods for certain steps

As noted above, we welcome the inclusion of time directions for certain steps, which should ensure that investigations proceed within a more reasonable time frame than previously (for instance, the 14 day period for appointing a Tribunal Panel set down at paragraph 32 and the 56 day period for Executive Counsel to serve the Allegation and factual evidence relied upon recorded at paragraph 34).

However, we also think it would be helpful for time directions to be given in some further areas. For instance, the Executive Counsel could commit to providing the Investigation Report within 28 days of completing the investigation. We note that under the current AEP, the Executive Counsel has 14 days to deliver the initial investigation report and yet under the new AEP there is no time period prescribed at all for delivering the Investigation Report. This means that the Investigation Report could follow some considerable time after the investigation has concluded, adding additional stress to the Respondent(s) involved. Further, if clear time limits were to be set, cases could be kept moving at a reasonable pace.

In making this suggestion, we are mindful that each case is different and some are larger and/or more complex than others. However, to protect the ability to flex the timetable, the AEP Rules could reserve the right for the parties to agree an alternative timetable in certain cases. This has worked well in the Pre-Action Protocol for Professional Negligence claims set by the Courts and the Civil Procedure Rules themselves, a regime which also has to cater for all different types of cases.

Bearing in mind the emotional and mental stress of an investigation, it would also be helpful if the AEP Rules could indicate the likely time period in which a) the Tribunal Hearing decision will be delivered (at paragraph 75) and b) the Sanctions and Costs Hearing will be listed (at paragraph 76). This is particularly so as this latter hearing is now an entirely

separate stage which follows the liability hearing. Time directions such as this would, in our view, give some welcome clarity for the individuals involved who will undoubtedly be anxious about both these aspects.

In addition, again to reduce the pressures on those involved, we also recommend that publication of any decision is delayed until after both the liability and sanction hearings have taken place so that a lay reader can understand the full position. If a decision is published after the liability hearing only, it may well be that a lay reader of that decision does not appreciate the seriousness of the breaches found and jumps to conclusions which could unduly prejudice the firm and the individuals involved.

3. Role of the Independent Reviewer

We understand that the Independent Reviewer has been introduced to ensure that all parties act fairly, particularly given the Enforcement Committee stage has now been removed from the process.

However, we are concerned that, under the current draft amended AEP Rules, a considerable degree of responsibility will rest on one individual with their own biases and, depending on the number of Reviewers appointed, this individual could become fixed in their views over time. Indeed this individual will have ultimate responsibility for confirming which matters should proceed to Tribunal (per paragraphs 23-28) and the terms of any settlement notice (paragraphs 106-110). We would like to understand how the FRC will ensure complete objectivity on an ongoing basis (and thus far this is not clear from the amended rules).

We recommend that the FRC prepare and publish comprehensive guidance for Independent Reviewers to help ensure consistency in decision making and transparency for stakeholders.

In our view, to avoid these concerns (or even the perception of them), it may have been better to have kept the concept of the Enforcement Committee and provided that Committee with clear Terms of Reference to carry out the role it is now envisaged the individual Independent Reviewer will perform. The responsibility for decisions over the direction and settlement of matters would then have been spread across a number of individuals.

We also note that the Independent Reviewer will also always be a lawyer (per the definitions of "Independent Reviewer"). This may not be appropriate in every case, particularly some of the more technical ones, where an auditor may be better skilled for the role. This is again where a Committee (which could comprise both lawyers and auditors) may be more appropriate. At the very least, we consider the "Independent Reviewer" definition should be expanded to include auditors as well as lawyers so that the most appropriate individual can be chosen for each case.

4. Removal of the Enforcement Committee stage

We note that the amended AEP no longer includes the Enforcement Committee stage and we understand that the rationale for this is that this Committee stage has never been used in practice. This means, of course, that there will now be no choice but for every matter to proceed to a Tribunal hearing (at least currently there is the option of referring the matter to the Enforcement Committee). Given how long it currently takes for a matter to proceed to a Tribunal hearing and also bearing in mind the increasing volume of cases being referred to be considered under the AEP, this is likely to mean that more and more matters are slowed down at the Tribunal stage.

Rather than removing the Enforcement Committee stage, it seems to us that it may be better to have considered how the Committee could be better utilised. In the section above, for instance, we highlight that the Committee could have been used to act in the role currently envisaged for the Independent Reviewer. In the alternative, such a Committee could be used to hear and consider some cases and/or aspects of cases in the first instance, perhaps in a similar manner to the ICAEW's Investigation Committee, thus keeping cases moving and preventing the Tribunals from being overwhelmed.

5. Procedural detail regarding witness and expert evidence

As noted at the outset, we welcome the fact that additional procedural detail is now included in the AEP. This will enable affected individuals and firms to better understand the process and what is expected from them at each stage.

However, we note that there is a complete lack of information regarding factual witness and expert evidence. We appreciate that case management directions will be agreed on a case by case basis (paragraphs 37-44) and these are likely to deal with the timetable for provision of this evidence. However, we consider it would also be useful to codify some general expectations such as the format for both the factual and expert evidence, whether the evidence will be exchanged simultaneously or sequentially in each case, whether it may be open for experts to meet and discuss issues in advance of the Tribunal hearing etc. All such matters are covered in the Civil Procedure Rules for Court cases (which have recently been updated) and this has led to increased streamlining of the evidence gathering process.

6. Provisions relating to Interim Order hearings heard without notice

There is considerable emphasis in the amended AEP Rules on the fact that hearings relating to Interim Orders may proceed without notice to the Respondent firm / individuals (see paragraphs 85, 88(a) and 91). We are surprised by this given such hearings would be a fundamental restriction on the Respondent's right to a fair hearing and, as such, we assumed that they would occur in very rare circumstances (as they are in the courts of England and Wales). This is particularly so given that all matters falling under the AEP are likely to be professional matters involving professional people. That said, the number of paragraphs devoted to them suggests that such hearings may be more commonplace. If that is the case, additional guidance (such as that contained in Practice Direction 23A.3 in the Civil Procedure Rules as to exactly when without notice hearings are likely to be considered appropriate would, in our view, be helpful.

7. Appeals to an outside body

We note that the Appeals section (Part 7) has been expanded and there is greater clarity over the appeals process. It is, however, disappointing that the FRC has not taken the opportunity to establish a process whereby an appeal is made to an entirely independent body outside the regulatory regime. For instance, when Solicitors are disciplined by the SRA, their right of appeal is to the Court of Appeal (which clearly has complete independence from the regulator). This has worked well in practice to date and is a very good precedent for the FRC to consider for auditors.

Specific observations relating to particular parts / paragraphs

We set out below some more minor observations in relation to particular sections of the amended AEP.

1. Postponement and adjournment (paragraphs 60-67). We assume that these provisions apply to both Case Management hearings and Tribunal hearings. Certainly under the current AEP

they do. However, the definition of "Hearing" which is used throughout this section does not expressly refer to "Case Management hearings" and, as such, you may wish to expressly refer to this in the definition.

2. Appeals (Part 7). We note that there is no longer provision for the Appeal Tribunal to remit a matter back to the Tribunal. We appreciate that you may consider this right is covered by the Reconsideration section (Part 8). However, in the current AEP there is both a right to remit granted to the Appeal Tribunal and also a Reconsideration section and, in our view, it would still be right to include the right to remit as an option available to the Appeal Tribunal within the Appeals section.
3. Sanctions (Part 9). We note that the list of sanctions no longer includes the ability to impose conditions or the ability for a Respondent to provide written undertakings. In our view these were both useful options available in the Sanctions armoury and we would submit that they should still be included under the amended AEP Rules.
4. Costs (Part 10). We note that costs are now either summarily assessed by the Chair of the Tribunal or agreed between the parties and provision for costs to be independently assessed is no longer given (paragraph 93(c) in the current AEP Rules). Given costs in Tribunal cases are often high, we consider such a provision should still be included, if only to avoid any perception that the issue of costs is not being fairly and fully considered.
5. Confidentiality (paragraphs 165 and 166). These paragraphs appear to be new and, on their face, it is not very clear whether they are designed to cover both the Respondent's confidential information and also the FRC's confidential information or just the latter. We assume they are meant to cover all confidential information no matter its genesis, but this could be drafted more clearly.

I hope these comments help you with finalising the amended AEP Rules. Should you wish to discuss any of the points raised in this letter or if you would like us to expand on any of our comments, please do not hesitate to contact me.

Yours faithfully

