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19 September 2012

Dear Ms Colban

Disciplinary Schemes Proposed Changes

We refer to our accompanying letter and now enclose our detailed responses to the above consultation paper. Before turning to them, however, we make some initial observations to set our submissions in context. It was time for a mature look at how the Scheme has operated in the past, to learn necessary lessons, and to revise it accordingly (though arguably the better course might have been to cause a wholly new re-draft to be written, so as to avoid the often unforeseen consequences of incremental re-drafting).

The stimulus and timeliness of revision are appropriate and we urge those reading the consultation responses to follow the profession's best suggestions through to implementation, either immediately or through further consultation: this chance for root and branch appraisal may not come again.

Initial observations:

There may always be questions around the interpretation of given provisions of the Accountancy Scheme but we sense an opportunity being extended through and in the wake of the consultation to the practising profession, in particular, so that the operation of the Scheme may be much more inclusive of representations the profession makes to the FRC, both generally and in terms of how cases are to be handled in the future.

We advocate a much more inclusive dialogue between the FRC as regulator (specifically, going forward, its Conduct Committee), the Participating Bodies which license the regulated population, and the regulated population itself. We believe that there would be benefits from every party's perspective were that to be the case.

We appreciate that the Accountancy Scheme is predicated on an adversarial model but we think that, when cases arise or are about to, there would be much to be gained from an early dialogue between the Conduct Committee, the Participating Bodies,

and the firms concerned. A more inclusive and real-time dialogue is virtually bound to identify any areas of real concern quite quickly, and cause time and cost-consuming blind alleys to be avoided.

Whereas we recognise that each stakeholder will have its own priorities and emphases in relation to any given case, all stakeholders will have an interest in contributing to a well-rounded - and swiftly arrived at - set of conclusions about the matter under the microscope. That objective is best served by the facilitation of good and purposeful communication among them at an early stage.

It is in the public interest for that communication to take place and the best medium for securing it as early as possible is private discussion, untrammelled by the expectations and presumptions that flow from premature publicity. One of our principal submissions to you is therefore about the use of 'Preliminary Enquiries'.

We make principal points too about the division of operation between the Participating Bodies and the Conduct Committee, about 'Interim Orders', and about the test for misconduct. These seem to us to be the most fundamentally important aspects of the consultation.

Above all, however, the success of the revised Scheme will depend on good sense, discretion and the capacity to put the Hampton Principle of Proportionality into three-dimensional practice when new cases come along. That represents a heavy onus on the FRC, the Conduct Committee, and the Executive Counsel but it is one that must be discharged if the difficulties which we all recognise have attached to the operation of the Scheme throughout much of its history are to be avoided for the future: it is the way the Scheme is now to be run, as opposed to the text of its Rules and Regulations, that will make the most telling difference going forward.

These preliminary observations made, we now turn to our detailed responses to the consultation questions;

1. Should the Schemes be amended as set out in paragraphs 3.3 to 3.11 above so as to enhance the independence of the disciplinary arrangements?
2. Are the proposals to conclude cases without the need for a tribunal hearing appropriate (paragraphs 3.12 to 3.13)?
3. Do you agree with the role envisaged for the Case Management Committee (paragraph 3.15)?
4. Are the proposals to facilitate the timely completion of investigations and disciplinary proceedings appropriate (paragraphs 3.16 to 3.18)?
5. Should the Executive Counsel be able to seek an interim order against a member or member firm? If so, are the proposed provisions (paragraph 3.19) appropriate?
6. Do you have any comments on the proposals to amend the investigation test (paragraphs 3.24 to 3.29)?
7. Do you have any other comments on the proposed Schemes or the points raised in this paper?

1. Should the Schemes be amended as set out in paragraphs 3.3 to 3.11 above so as to enhance the independence of the disciplinary arrangements?

Swiftness of response to circumstances is, of course, an important principle for professional disciplinary schemes to observe but it is not a surrogate for surefootedness of action: the launch of an investigation should be predicated on other factors – precision around an allegation in the public domain, an assessment as to whether what is in the public *domain* amounts to an issue of legitimate public *interest*, the availability of evidence underpinning an irresistible inference that an investigation needs to be commenced, and generally, an examination of all of the circumstances at the time the Board's attention is drawn to an event.

Although there may be *some* circumstances where there is an irresistible inference that an investigation needs to be launched straightaway, in most it is better to come to a qualitative view on necessity before announcing it.

We believe that the FRC is of that view too, in that the consultation paper itself says, at paragraph 3.4, that "*[T]he proposed amendment will enable the FRC to act more swiftly in launching an investigation in appropriate circumstances*". It does not seem to us that a period of three months during which it is debated between a Participant and the FRC which of them should have jurisdiction over a particular case, is wasted, or a disproportionally long, time, especially given the gestation time of the average case in the Scheme's hands historically.

We also feel that the compulsion around publication by the FRC of cases that it either begins itself or begins following debate with a Participant, should be removed. We have more to say on this in answer to Question 6 but there is much common sense, in our opinion, in the FRC retaining discretion not to leap to publication when it has not had the chance to come to a reasoned set of conclusions on the circumstances it is looking at. If we are correct in this assumption, though, we would not support the wording that accompanies the change: what both paras 5(2)(ii) and 5(7) say is that the FRC retains a discretion not to publish unless failing to publish *would not...be in the public interest*".

Issues in the public domain are not synonymous with public interest issues, though we imagine the difference is already well known to the Board – otherwise it would not have set such store by the introduction of Preliminary Enquiries (which are intended to fathom out whether there is a case, ahead of the glare of publicity).

With regard to paragraphs 3.6 to 3.8 of the consultation paper, we are much less concerned with who conducts Preliminary Enquiries than with the fact that there are proper grounds for beginning one and that it is carried out in confidence, for the reasons we have mentioned.

We think that the Participating Bodies' views ought to be taken into account when any amendments to the Scheme are in contemplation, though we take your point about the necessity of operational independence of it.

Lastly, in relation to this Section, although you make it clear in paragraph 3.8 that there is a distinction to be made between a Preliminary Enquiry, on the one hand, and a Supervisory Enquiry, on the other (we take it to mean that a PE is for operational cases and an SE is for regulatory phenomena, like the profession's role in relation to banking supervision, for example), that distinction is not clear.

2. Are the proposals to conclude cases without the need for a tribunal hearing appropriate (paragraphs 3.12 to 3.13)?

The need for the suggested new power is based almost solely, as we see it, on the convenience of the Scheme and the desire to effect a quick determination of investigations "in appropriate cases" (para 3.12). Its success will depend on the clear and early identification of facts that support a conclusion that the Member or Member Firm has a case to answer. Where that conclusion is clear from the evidence, and not merely arguable, then there may be instances where it would be appropriate to use such a power but we caution against unbridled usage.

Our concern is that straightforward cases – where the facts and the conclusions to be drawn from them are clear at an early stage in process – will be few and far between; cases will be far more typically decided on the basis of a reconstruction of professional judgement applied to the engagement by the Member or Member Firm at the material time rather than on clear acts or omissions on the part of the Member or Member Firm being established. The determination of cases will far more often depend on the application of expert evidence than the discovery of a smoking gun.

The danger, in our view, is that the power will be used rather less to conclude cases where the arguments against the Member or Member Firm are clearly made out, and rather more to bring about a forced settlement to a case the Executive Counsel may not be able to prove if tested. The cost and resource implications facing a Member or Member Firm under investigation are, on any view, substantial, and it may feel impelled along the avenue of compromise with the FRC, simply because it is offered a settlement which it knows it can live with, and thereby avoid an outcome at Tribunal that it might not be able to.

Our concern, therefore, is that the power is used not merely to coerce a settlement but to drive a *compromise* settlement; one that impels the member or Member Firm to abandon its defence of allegations in favour of accepting a position which it does not wholly agree with but is driven to, through fear of the costs and other consequences it might ultimately face, were it to insist on its right to a whole airing of the case at a Tribunal hearing.

The use of this power of early settlement will militate far more heavily against the smaller firms than the largest ones. There is a clear 'equality of arms' concern about the unbridled use of paras 6(12) to 6(18) which we fear might be readily resorted to by the Conduct Committee. The FRC's motivation in introducing the power is self-evidently to reduce the length of time that cases take and the costs the Scheme has to bear along the way, but its implementation would come at the cost of the capacity of some Members and Firms to defend themselves adequately.

It must be clear, surely, that the likelihood of less well-resourced Members and Firms being driven into the Executive Counsel's arms is far higher than for the largest firms. The power is objectionable because it is *capable* of being deployed capriciously – to achieve a 'win' through stronger bargaining position rather than force of argument.

Having stated our strong reservations in principle about the uses to which such a power could be put, we turn our attention to the proposed workings of it. We have several comments in this regard.

First, paragraphs 6(12) to 6(18) do not make any reference to the sanctions set out in Appendix 1 (the FRC Scheme Schedule) and it is therefore not clear what the scope of settlement is (would the Member or Firm be able, for example, to agree a settlement that did not involve the application of a formal sanction competent to a Tribunal?).

Second, the entitlement to settle is intended to apply only to the 'window' between the Executive Counsel serving a notice under paragraph 6(10) that he intends to serve a Formal Complaint and a Formal Complaint actually being served – in our opinion, any power to settle ought to be capable of application at any time following service of a Formal Complaint, including in the course of a Tribunal hearing.

Third, in the event that a Member or Firm has offered terms for settlement that were turned down by the Executive Counsel and the Tribunal returns conclusions that reflect the reasonableness of the terms offered, how is that to be reflected in the sanctions awarded against the Defendant?

Our overall concern, though, is about the potential restriction of a Member's or Member Firm's right to a fair and independent hearing: whereas, on the face of it, the intended new power does not remove that right, in practical terms it might well have the effect of doing so and is therefore objectionable: it is not a surrogate for justice.

3. Do you agree with the role envisaged for the Case Management Committee (paragraph 3.15)?

The Case Management Committee is, according to paragraph 3.15, to be given a number of roles, all to be exercised prior to the service of any Formal Complaint (assessment of the adequacy of the evidence the Executive Counsel is relying on, and whether the case should proceed to a Tribunal hearing or cause 'settlement discussions' to take place). We think that it should have an additional, explicit, purpose – to be satisfied that the investigation has been carried out as swiftly and expeditiously as possible, and that there have been no inexcusable delays on the part of the Executive Counsel or the Conduct Committee of the FRC. Inexcusable delay ought to cause the CMC to consider recommending that the investigation be abandoned.

4. Are the proposals to facilitate the timely completion of investigations and disciplinary proceedings appropriate (paragraphs 3.16 to 3.18)?

We support the addition to paragraph 6(10) as currently expressed of a requirement on the Executive Counsel to give the Member or Member Firm notice that he intends to serve a Formal Complaint and the grounds supporting it. (We point out that, in contrast with what the consultation paper says at paragraph 3.16, we do not see that there is any such obligation on the Executive Counsel at present.) However, it seems to us that giving a Member or Member Firm only eight weeks (as paragraph 6(10)(ii)(b) suggests) to respond to such a notice, when the investigation may have lasted for years, is inherently unfair. The Case Management Committee's opinion should be sought in relation to any such time-limit within which the Member's or Member Firm's response should be received.

5. Should the Executive Counsel be able to seek an interim order against a member or member firm? If so, are the proposed provisions (paragraph 3.19) appropriate?

This is a substantial new power, intended to be brought in under a wholly new paragraph (13) of the Scheme, and once granted, can impose on the Member or Member Firm a suspensive order under Appendix 2 that is equal to the severest of sanctions available to a Tribunal at the conclusion of a case, never mind at or near its start.

The power, as drafted, of the Executive Counsel to seek an Interim Order would subsist at any time in the course of an investigation, even when it is at an inchoate stage and when little evidence may be in his hands. Such a power needs to be accompanied by adequate checks and balances. Whereas we appreciate that the Executive Counsel must first justify his intention by having it endorsed by the Conduct Committee of the FRC and that the application must then be subject to scrutiny by a Tribunal, we do not consider these to be adequate checks on the exercise of this, highly substantial, new power, which could be fatal to the career of a Member and to the survival of a Member Firm.

The Executive Counsel's entitlement to seek an Interim Order is left entirely unfettered by the Rules: paragraph 13(1) would allow him to present an application where he is "of the opinion that a Disciplinary Tribunal should consider making [one].". We strongly suggest that it is not appropriate to repose that degree of discretion in one set of hands, especially when there are no criteria guiding when that entitlement should be invoked.

It is our opinion, based on the jurisprudence of other regulatory and disciplinary schemes and case-law decided under them, that this is an extreme interdictory power that ought only be exercised in the starkest of circumstances – involving conduct that is highly suggestive of *criminal or wholly reckless* conduct, not merely conduct that, if proved at Tribunal, might lead to a disciplinary finding against a Member or Member Firm. The text of paragraph 13 makes no such stipulation and in our view is objectionable at law.

In fact, it would be inadvisable from the FRC's point of view, never mind a Member's or Member Firm's for the power, as currently expressed in paragraph 13, to be implemented. Apart from being objectionable in its terms, it is, in a practical sense, likely to be next to useless as, absent the starkest evidence of the kinds we have suggested, it is near-inconceivable that a Tribunal, properly directed, would grant such an Order.

We do not say that the Rules of the Accountancy Scheme should not contain *any* provision for Interim Orders but we do say that the factual circumstances and the degree of evidence that should have to be demonstrated before one is invoked should be heavily circumscribed and it should be made clear (i) that the Member or Member firm has a right of representation at any hearing by a Tribunal of an application for Interim Order (paragraph 13 gives no such right; it merely says opaquely in paragraph 13(4) that, "...[T]he procedure adopted by a Disciplinary Tribunal to deal with an application for Interim Order shall be in accordance with the Regulations [of the Scheme]."; (ii) that the power can only be invoked in exceptional circumstances, where the evidence or supportable indications are that there may have been misconduct of the grossest kind, and that (iii) the test for proof is towards the criminal one, not merely the standard that would be required to sustain an adverse finding at the conclusion of the hearing of a Formal Complaint.

6. Do you have any comments on the proposals to amend the investigation test (paragraphs 3.24 to 3.29)?

We welcome discussion around this topic, as it has bedevilled the Scheme since inception. It was, as we understand it, argued cogently by the Participants even prior to inception that the present test was set at a level that was and remains inappropriate. In our opinion, that is a major reason why the Scheme has been unable to secure adverse findings in the numbers that it would probably have anticipated when its earliest cases were being adjudicated.

We recognise in the 'reasonable grounds for suspecting' test an intention to draw from other statutes and forms of regulation. The intention underlying the 'reasonable grounds' test is that the evidence available to a prosecutor must throw up an irresistible inference that a case needs to be investigated before one should be sanctioned and initiated. We support that intention.

However, the difficulty we see is that the Executive Counsel is unlikely to be in a position to apply the new test at the much more premature stage at which the Scheme's Rules (paragraph 4(1)(i) and (ii)) fall to be applied. To make the point clear, it is worth looking at these two provisions in detail.

Paraphrasing them, they say that the liability of a Member or Member Firm to disciplinary action is predicated on (i) whether a matter raises important issues in the public interest in the UK (or appears to); and (ii) if so, that matter needs to be looked at so a view can be taken as to whether that Member or Firm has been guilty of misconduct.

Condition (i) is likely to be satisfied by anything by the mere fact that something is in the public domain about a failure in the governance and/or the financial statements of a company or large charity. If Condition (i) is met, then Condition (ii) is entirely self-fulfilling. Investigations can, as things currently stand, routinely be initiated without more than a partly formed bank of information (even none) being known that links the causes of the issue with a Member of Member Firm.

It is a trite observation but the mere *known fact of the existence of* an enquiry can create presumptions adverse to the interests of the Member or Firm in itself.

We support the 'reasonable grounds for suspecting that misconduct has occurred' test because it is so closely related to an interpretation of misconduct that is moving closer to where it should be. If, as seems likely from the consultation, it is the intention of the Conduct Committee to be closer to being able to make *informed* conclusions about professional conduct before causing an investigation to be triggered and publicised, then we would support that. However, we reiterate the point we made in answer to Question 1, that proposed Rule 5(2) (decision to investigate) should be conjoined with a discretion on the Conduct Committee to publish the fact of preliminary enquiry *only where* there are compelling reasons to do so.

We believe that one of the primary reasons why cases were lost by the AADB at Disciplinary Tribunal was because Formal Complaints were 'over-charged': that allegations of misconduct amounted to no more than allegations of negligence: actions, and failures to act, will all feature to one extent or another in the chain of causation of an event but the jurisdiction of the revised Scheme should only be invoked where a professional's acts or omissions are, as lawyers say, *causa sine qua non* of that event. It is relatively easy to find on any retrospective examination of the conduct of an engagement one or more aspects that were deficient or sub-optimally performed. There is a temptation for any disciplinary scheme under pressure to project failures like that as worthy of prosecution in themselves and it is our submission that Formal Complaints have been found not proved by Tribunals for that reason - they do not find the prosecutor's thought-process seductive.

The revised Scheme should be looking to uncover instances where there has been a *substantial* departure from the degree of professional conduct reasonably to be expected in the circumstances. It is our further submission that allegations which are not proved to that degree will fail. The proposed test for invocation of an investigation goes part-way to deal with this point but it would be helpful if it were to be made clear, perhaps through guidance from the Conduct Committee to the Executive Counsel, or a Protocol between the Participants and the FRC, that Formal Complaints will only proceed in instances where there has been that substantial degree of departure from the standards reasonably to be expected, and it is well-evidenced.

7. Do you have any other comments on the proposed Schemes or the points raised in this paper?

None, other than to emphasise the point we made at the start of this submission, that the success of the revised Scheme will depend largely on the good sense with which it is run, and that the principle of Proportionality is the most important in this regard. The Conduct Committee, Case Management Committee, and the Executive Counsel need to exercise discretion in a way that best supports the principle for the revised Scheme to be a success.

Yours sincerely

T M McMorrow

T M McMorrow
Secretary to the Group A firms