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# Guidelines on Enforcement Measures against Recognised Supervisory Bodies and Recognised Qualifying Bodies

for breach of the statutory requirements and  
obligations in relation to the regulation of  
statutory audit set out in Part 42 Companies Act  
2006

Feedback Statement

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## 1. Introduction

1.1. The purpose of this feedback statement is to summarise the responses to our consultation document: Guidelines on Enforcement Measures against Recognised Supervisory Bodies and Recognised Qualifying Bodies for breach of the statutory requirements and obligations in relation to the regulation of statutory audit set out in Part 42 Companies Act 2006 (November 2014) and provide our feedback on the consultation responses.

## 2. Responses received

2.1. **We received six responses to the Consultation document. Five respondents were Recognised Bodies. The respondents were:**

| Respondent | Organisation type |
|------------|-------------------|
| AAT        | Professional Body |
| ACCA       | Recognised Body   |
| CARB       | Recognised Body   |
| ICAS       | Recognised Body   |
| ICAEW      | Recognised Body   |
| AIA        | Recognised Body   |

2.2. **The individual responses to the Consultation Paper can be found on the FRC website.**

## 3. Summary of responses

3.1. **In general, respondents were not opposed to the principle of having Guidelines, but made a number of suggestions to improve proportionality and transparency. Key concerns and themes included:**

- emphasising the need for productive dialogue with the Recognised Bodies before the FRC considers imposing Enforcement Measures so as to avoid unnecessary or disproportionate regulation;
- Financial Penalties should be exceptional and, if considered at all, should be considered from the starting point of UK audit-related fees;
- there should be a right to challenge a Direction Decision Notice;
- timeframes should be expanded to a minimum of 28 days to better reflect Recognised Bodies' internal governance requirements;
- the FRC's governance and decision making in relation to Enforcement Measures should be clarified in the Guidelines.

**3.2. The consultation document asked five questions. These are set out below together with a summary of the responses received:**

**Q1: Do you consider that the proposed Guidelines provide a clear framework to guide the Board's decision making when imposing Enforcement Measures?**

- *Deterrence*: Five respondents considered that the Guidelines risked leaning disproportionately towards deterrence. Four respondents commented either that they were not aware of any circumstances in which a Recognised Body had refused to comply with an FRC request or that it was not clear what types of non-compliance the Guidelines sought to address.
- *Remedy of last resort*: Four respondents responded that the Guidelines should be framed around the presumption that Enforcement Measures should be imposed as a last resort. This was a consistent theme throughout the responses to all the questions.

**Q2: Do the proposed Guidelines include the factors that you would expect the Board should take into account when deciding which enforcement measures to impose?**

- *Deterrent effect*: One respondent considered there should be more focus on the deterrent effect. Two respondents considered that the deterrent objective was overstated.
- *Aggravating and Mitigating Factors*: Four respondents suggested the addition of aggravating and mitigating factors in the main body of the Guidelines (and not just Appendix 2) to assist the Board to consider which Enforcement Measures to impose.

**Q3: What is your view of the starting point proposed (a percentage of the Recognised Body's total UK fee income) for calculating the amount of a financial penalty?**

- *Exclusion of non-audit fees*: Five of the six respondents were strongly opposed to non-audit fee income being included in the starting point for calculating the amount of a financial penalty.

**Q4: Do you consider there is anything missing from the proposed guidelines that would improve their effectiveness?**

- *Independent review and appeal*: All six respondents considered variously or in combination that an independent review of subject elements of the FRC's decision making and a right of appeal or challenge to a Direction Decision Notice were missing. Two respondents considered that there was insufficient clarification on publication in the Guidelines.
- *Remedy of last resort*: All six respondents considered variously or in combination that the option of taking no enforcement action or the presumption that the FRC and the Recognised Bodies will engage in voluntary dialogue was missing.
- *Practicable timescales*: Four respondents considered that the Guidelines were missing realistic timescales to reflect the internal governance processes of the Recognised Bodies.
- *Clarity on costs*: Two respondents considered that there was insufficient clarity on costs.
- *Cap on penalties*: One respondent responded that there should be a cap on penalties.

**Q5: Do you have any other comments about the proposed enforcement measures?**

Other than the points identified above, the following comments were made:

- **Proportionality:** A number of responses highlighted concern that imposing Enforcement Measures at all ran contrary to the public interest because this calls into question the integrity of the Recognised Bodies, some of which operate under Royal Charter and none of which are profit-focused organisations. One respondent concluded that goodwill and public interest pursuits would be compromised by a sanctions regime. Some respondents considered that the Guidelines were too heavy handed and/or focused on principles more appropriate for sanctioning commercial enterprises.
- **Financial penalties:** if retained at all, these should only be applied in the most extreme circumstances as they will tend towards being punitive rather than simply a deterrent and will have a potentially adverse effect on Recognised Bodies' activities.
- **Publicity as deterrent:** three respondents considered that publication of Enforcement Measures would be a sufficient deterrent.

## 4. FRC response

### 4.1. We have accepted a number of suggestions and a revised set of Guidelines is attached. In particular:

- **Voluntary dialogue:** The FRC's intention was always that Enforcement Measures should normally only be considered after dialogue with the Recognised Body had been exhausted. We have amended the Guidelines to reflect this.
- **Financial penalties:** we have removed non-audit fees received from the calculation processes at Appendix 2 and replaced the five levels of seriousness with three levels of seriousness, the most serious attracting a starting point of 10% of audit related UK fee income subject to a deemed minimum audit-related income of £300,000.
- **Governance:** we have clarified the decision making bodies in relation to Enforcement Measures.
- **Timescales:** where deadlines are not governed by other processes (for example the Civil Procedure Rules) we have amended them to 28 days.
- **The Guidelines do not address what will happen to recovered fines:** We have clarified that, as set out in s1225D(3), penalties are payable to the Secretary of State.

### 4.2. Where we have not carried through proposed amendments or comments, we respond as follows:

- **Subjective elements in the FRC's approach:** Various responses outlined a concern about subjective application of the Guidelines by the FRC. Regulation requires the exercise of reasonable judgement. At each stage of the recommended procedure the Recognised Body will have an opportunity to make representations and the FRC takes seriously its obligation as a regulator to give due and proper consideration to such representations and provide reasoning to support transparent and consistent decision making.
- **Use of a third party reference:** (e.g. at the Direction Decision Notice stage): A third party reference is not contemplated by the legislative arrangements save as expressly provided and it is not considered appropriate for the FRC to overwrite Parliamentary

will. The arrangements as drafted are considered to protect the Recognised Bodies sufficiently, as follows:

- The Recognised Body will already have had in most cases ample opportunity to consult with and explain its position to the FRC outside the Enforcement Measures regime by the FRC's stated commitment to participating in a preliminary, voluntary dialogue stage.
  - At the Direction Decision Notice process the Recognised Body has the opportunity to make formal representations to the Board in response to a Notice of Proposed Direction. The Board is obliged to take these representations into consideration in order to reach a reasonable and procedurally compliant decision. (It should be noted that the power to issue a Direction is given to the Secretary of State and delegated to the FRC without provision for a further layer of independent/third party assessment at this stage). If the FRC were to seek to pass on the final decision regarding directions to another party, the FRC would risk breaching the principles against unauthorised sub-delegation.
  - At the Compliance Order or Financial Penalty Notice stages, the Act already provides for third party assessment by reference to the Court.
  - Adding any further (interim) references to an independent third party, unless specifically contemplated by statute will add an unnecessary further layer and make the processes longer and more unwieldy.
- ***Fundamental right to attend and take part in any hearing regarding an application for a Compliance Order should not be conditional on the Recognised Body having submitted supporting evidence within the timeframe set out in Appendix 1:*** As a matter of civil procedure, the Recognised Body's right to be heard by the Court is contingent upon filing an acknowledgement of service within 14 days or otherwise seeking the Court's permission. The Guidelines simply reflect the procedural position. This is not within the FRC's power to alter. We have nonetheless removed the reference to the procedural position in the Guidelines, but would draw the Recognised Body's attention to the Civil Procedure Rules in force at the applicable time.
- ***The Guidelines do not address costs:*** Where the Recognised Body has not complied with the Requirements and the FRC has applied successfully to the Court for a Compliance Order or successfully defended a challenge in the Court to a Financial Penalty Decision Notice, the FRC is likely to ask the Court to award its costs. This is considered to fall outside the scope of the Guidelines.
- ***Interest should not be payable on Financial Penalties;*** ss 1225G(1)(3) make clear that if the whole or any part of a penalty is not paid, the unpaid balance carries interest at the rate set out in the Judgments Act 1878 unless otherwise determined by the Court and that interest may accrue throughout an appeal period – also at the discretion of the Court. It is not appropriate for the FRC to re-write legislative provisions and we consider that the interests of the Recognised Bodies are sufficiently protected in this regard by the Court's clear discretion to award a different (or no) rate of interest in relation to a Financial Penalty upon the successful application of a Recognised Body.



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