

Independent Review of the Financial Reporting Council (FRC)

Initial consultation on the recommendations by the Department for Business, Energy & Industrial Strategy (BEIS)

Comments from ACCA

June 2019

Ref: TECH-CDR-1830

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management.

Founded in 1904, ACCA has consistently held unique core values: opportunity, diversity, innovation, integrity and accountability. We believe that accountants bring value to economies in all stages of development. We aim to develop capacity in the profession and encourage the adoption of consistent global standards. Our values are aligned to the needs of employers in all sectors and we ensure that, through our qualifications, we prepare accountants for business. We work to open up the profession to people of all backgrounds and remove artificial barriers to entry, ensuring that our qualifications and their delivery meet the diverse needs of trainee professionals and their employers.

ACCA supports its 219,000 members and 527,000 students (including affiliates) in 179 countries, helping them to develop successful careers in accounting and business, with the skills required by employers. ACCA works through a network of 110 offices and centres and 7,571 Approved Employers world-wide and 328 approved learning providers who provide high standards of learning and development.

Through its public interest remit, ACCA promotes appropriate regulation of accounting and conducts relevant research to ensure accountancy continues to grow in reputation and influence.

ACCA is a Recognised Supervisory Body (RSB) for audit under Schedule 10 of the Companies Act 2006. The FRC, as the audit competent authority, delegates certain audit regulatory tasks to ACCA as an RSB under a Delegation Agreement. This places an obligation on ACCA as an RSB to fund the FRC's performance of any tasks that have not been delegated where these relate to the regulation of auditors registered with ACCA. This funding covers the costs of the FRC's audit review activities, audit enforcement activities and standard-setting procedures.

Further information about ACCA's views of the matters discussed here may be requested from:

Maggie McGhee
Executive Director – Governance
maggie.mcghee@accaglobal.com

Sundeep Takwani
Director - Governance
sundeep.takwani@accaglobal.com

www.accaglobal.com

GENERAL COMMENTS

1. ACCA welcomes BEIS's initial consultation on the recommendations made by the independent review of the FRC to create a new regulator responsible for audit, corporate reporting and corporate governance.
2. ACCA's views are framed through a public interest lens and we support the development of a regulatory system that is proportionate, effective and credible and which operates to uphold the public interest.
3. ACCA is supportive of the proposed reforms which strengthen trust and public confidence in the audit and corporate reporting regulatory framework. ACCA also agrees that the regulatory framework needs to achieve robust oversight based on a proportionate, fit for purpose governance regime which supports the UK economy and an efficient and effective capital market. ACCA therefore welcomes the principles of the Kingman proposals contained in the 83 recommendations.
4. ACCA supports the proposal to establish the new regulator as a statutory body, accountable to Parliament, with a full range of powers defined in legislation and internal governance arrangements that not only comply with the UK corporate governance code but also with best international practice. It follows that the regulator should be expected to comply with the Regulators Code.
5. It is vital that the UK economy has efficient and effective capital markets and there is confidence in the corporate framework through greater transparency.

AREAS FOR SPECIFIC COMMENT

In this section, we respond to the specific questions asked by the BEIS in its consultation paper.

Question 1: What comments do you have on the proposed objective set out in Recommendation 4?

6. ACCA supports the proposed objective set out in Recommendation 4.
7. ACCA believes that clearly stating the strategic objective for the new regulator should enable it to focus its activities on businesses that pose a systemic risk to the economy.

Question 2: What comments do you have on the duties and functions set out in Recommendations 5 & 6?

8. ACCA supports the proposed set of duties and functions set out in Recommendations 5 & 6. In particular, ACCA welcomes, among other things, the clear obligation on the new regulator to:
 - be proportionate, ie balance the costs and benefits of regulation
 - prioritise regulatory activity on the basis of risk
 - work collaboratively with regulators both in the UK and Internationally.
9. ACCA believes that by clearly setting out the duties and functions, it will allow the new regulator to prioritise its role as the competent authority for PIE audits and PIE audit firms. ACCA therefore supports the registration of PIE audit firms by the new regulator (Recommendation 15) instead of by the professional accountancy bodies at present as this would allow for a more joined up approach for the regulation of PIE audit firms.
10. By focusing the attention of the new regulator on statutory audit, corporate reporting and corporate governance in order to protect the interests of users of financial information and the wider public interest, should allow it to be a more effective regulator.

Question 3: How do other regulators mitigate the potential for conflict between their standard setting roles and enforcement roles as set out in Recommendation 14?

11. ACCA has some reservations in regard to Recommendation 14, in particular the proposal to enable the board of the new regulator to launch audit investigations in cases it regards as of particular significance or public interest. In general, cases considered by the new regulator would involve audit of entities that pose a systemic risk to the economy and therefore by their very nature are of particular significance or public interest.
12. ACCA agrees that the board of the new regulator should play a key role in

overseeing the effective and efficient functioning of the regulatory and disciplinary process. ACCA would, however, caution against the board's involvement in individual cases as it may hinder fairness and impartiality and could be seen as prejudicial.

13. In ACCA's case, the Regulatory Board provides oversight over ACCA's regulatory arrangement, including our disciplinary process. As part of its oversight role, the Regulatory Board is provided with key performance information at each meeting, including data on investigation times and case progression. The role of the Regulatory Board is to assess whether ACCA has a robust process in place to provide confidence that ACCA's regulatory arrangements operate in the public interest while ensuring the fairness and impartiality of the regulatory and disciplinary process.

Question 4: Are there specific considerations you think we should bear in mind in taking forward the recommendations in this chapter? Are there other ideas we should consider?

14. ACCA supports the proposed thrust of Recommendations 7 to 14 in that regulatory structures need to not only be effective in the current circumstances but need to be sufficiently agile to accommodate for the future. It is important for the UK economy and the capital markets that the new regulator is a beacon for best practice in governance, transparency and independence.
15. ACCA believes the membership of the new regulator should include stronger links with other UK regulatory bodies, including the Financial Conduct Authority and The Pensions Regulator, as it is critically important that the interactions between key regulators are effective and allows for co-ordinated action when warning signs emerge.

Question 5: How will the change in focus of CRR [Corporate Reporting Review] work to PIEs [Public Interest Entities] affect corporate reporting for non-PIE entities?

16. ACCA supports Recommendations 24 to 27 in regard to CRR. ACCA nevertheless believes the experience to date of CRR has been positive and these reviews have acted as a deterrent. This has been driven by FRC's approach which is to focus on issues of significance as opposed to mere tick-box compliance.
17. ACCA similarly supports the focus of CRR on PIEs given that such entities pose a systemic risk to the economy. This has, quite rightly, been the focus of FRC's activity to date. ACCA nevertheless believes that there should be provision within the new regulator's arrangements to accommodate reviews of non-PIEs where concerns about the quality of the accounts are brought to its attention. This accords with the risk-based approach promoted by Recommendation 24.

Question 6: What are your views on how the pre-clearance of accounts proposed in Recommendation 28 could work?

18. ACCA's primary concern with the proposals set out in Recommendation 28 is that it

may diminish the responsibility of directors and hinder good corporate governance.

19. In addition, it is not clear whether there is a demand or need for pre-clearance of accounts. Similarly, it is not clear how pre-clearance would assist the new regulator in the event of issues which subsequently arise or indeed who carries the risk.

Question 7: Are there specific considerations you think we should bear in mind in taking forward the recommendations in this chapter? Are there other ideas we should consider?

20. Recommendation 17 – This concerns issues arising from the audit expectations gap, which, as the consultation paper acknowledges, is a matter to be addressed by Sir Donald Brydon's review.
21. Public confidence in audit is decreasing and large corporate failures have led to a lack of confidence in the audit profession and the regulator by Parliament and by the wider public. ACCA has undertaken a global research initiative entitled 'Closing the expectation gap in audit', which was published on 9 May 2019 (<https://www.accaglobal.com/uk/en/professional-insights/global-profession/expectation-gap.html>). The research involved an open dialogue involving auditors, company management directors, the broader accountancy profession, stakeholders and the public to explore what kind of audit future the public expects. All play a role. Our findings demonstrate that importantly the public sees audit as part (but not all) of the solution to unacceptable corporate behaviour, making sure financial statements give a holistic 'true and fair view', and ensuring fraud is addressed and appropriate levels of professional scepticism are applied.
22. The research surveyed 11,000 people across 11 countries (including 1,000 in the UK), weighted evenly by sample size, gender and spread across age, education level and household income. The Countries included in the initiative are; Greece, Czech Republic, New Zealand, South Africa, Australia, Netherlands, Singapore, Canada, UAE, Malaysia and the UK.
23. ACCA support the recommendations in regard to audit quality reviews (Recommendations 20 to 22) as the proposals should promote greater transparency and confidence in relation to the audit firm inspection process.
24. ACCA supports Recommendation 35 to replace the voluntary accountancy scheme with a statutory scheme for investigating apparent wrongdoings by accountants in PIEs in relation to financial reporting or corporate governance matters. It should be noted that the current scheme applies only to members of the participating bodies – ACCA, ICAEW, ICAS, ICAI, CIMA and CIPFA; it does not extend to all accountants nor does it extend others involved in financial reporting or corporate governance matters.
25. While ACCA supports the thrust of Recommendation 36, the proposals appear to run counter to the collective responsibility of the board of directors to prepare and approve true and fair accounts and compliant corporate reports, and to deal openly and honestly with auditors.

26. ACCA broadly supports Recommendation 37 and 38 and agrees that there should be regulation of directors of PIEs, but we are not entirely in agreement with the proposal that the FRC / the new regulator should be given the power to regulate the conduct of company directors in corporate reporting and corporate governance matters. ACCA believes that consideration should be given as to whether this responsibility could be more effectively undertaken by the FCA.
27. ACCA believes Recommendations 39 to 41 in regard to the oversight of regulation of non-audit activities undertaken by members of professional accountancy bodies require further consideration and discussion.
28. As the report recognises, this is a voluntary arrangement in which some (but not all) accountancy bodies have chosen to participate. Therefore if the new regulator is to oversee the accountancy bodies' regulation of their members' non-audit activities on a more formal basis, consideration should be given to including all professional accountancy bodies into the arrangements and protecting the use of the title "accountant".
29. By way of background, the governance arrangements for the oversight of ACCA's (and those of other bodies subject to FRC oversight) regulatory functions in 2003 when the voluntary arrangements were put in place were very different to those in place today. ACCA Regulatory Board, which was launched in 2008, brings together all of ACCA's public interest oversight arrangements into a single entity. The Board's public interest role sits at the heart of ACCA's oversight structure and it provides oversight of all of ACCA's public interest functions – setting qualifications and assuring their delivery, setting professional standards, and the licensing and disciplinary system. The Board comprises a lay chairman (ie a non-accountant), further five lay members and two members of Council and it has a clear programme of work, directed at strengthening the public interest elements of ACCA's activities. Further information on the Regulatory Board can be viewed at <https://www.accaglobal.com/an/en/about-us/regulation/regulatory-board.html>.
30. The remit of the Regulatory Board is to provide independent oversight of ACCA's regulatory arrangements, including over ACCA's complaints and discipline arrangements, and to report to ACCA's Council on the fairness and impartiality of these activities. ACCA believes its public interest oversight arrangements, ie the Regulatory Board and its sub-Boards – Appointments, Qualifications and Standards Boards - provide the necessary safeguards to protect the public interest. Further, ACCA's public interest oversight mechanisms help to reassure stakeholders that ACCA's regulatory arrangements are operated impartially, with integrity and in the public interest.
31. In addition, the recommendations' proposals that the regulator identify any emerging concerns of public interest on non-audit matters and that a backstop power requiring a professional body to take action if there was a need in the public interest on such matters does not appear to acknowledge that there may be other regulators having locus on such matters. Examples include the Insolvency Service on insolvency matters, the Legal Services Board on legal services matters, the Office for Professional Body Anti-Money Laundering Supervision on AML matters

and HMRC on tax matters. There is therefore a danger that the new regulator may encroach on matters which are within the purview of another regulator.

Question 8: Are there specific considerations you think we should bear in mind in taking forward the recommendations in this chapter? Are there other ideas we should consider?

- 32. ACCA is broadly supportive of the recommendations set out at Chapter 3, Corporate failure.
- 33. Specifically in regard to the proposed interventions and the 'skilled person' review, ACCA agrees careful consideration needs to be given to any framework that is put in place and the market implications - for example, will there be time for such interventions, what will the market consequences be, etc. ACCA welcomes therefore BEIS's intention to consult on these proposals.
- 34. In regard to Recommendation 53, Enhanced grading of inspected audits, ACCA believes the grading of key audit matters in the auditor's report warrant further discussion and deliberation.

Question 9: Are there specific considerations you think we should bear in mind in taking forward the recommendations in this chapter? Are there other ideas we should consider?

- 35. ACCA supports the recommendations set out at Chapter 4, The new regulator: oversight and accountability.

Question 10: Are there specific considerations you think we should bear in mind in taking forward the recommendations in this chapter? Are there other ideas we should consider?

- 36. ACCA broadly supports the recommendations set out at Chapter 5, Staffing and resources, but we believe the proposals on the cooling-off period to ensure the independence of FRC staff require further consideration and discussion.

Question 11: Are there specific considerations you think should be borne in mind in taking forward the recommendations in this chapter? Are there other ideas we should consider?

- 37. ACCA broadly supports the recommendations set out at Chapter 6, Other matters.
- 38. ACCA supports the recommendations in regard to the competition role of the new regulator (Recommendations 71 to 73). ACCA also agrees that these recommendations are reviewed after the completion of the Competition and Markets Authority's (CMA) market study on competition in the audit market study and the BEIS Secretary of State's recent announcement to consult on the remedies proposed by CMA.
- 39. ACCA agrees with the proposal to reallocate oversight of the actuarial profession to another regulator (Recommendations 74 and 75). This should allow FRC / the new regulator to focus on its core activities and not be distracted by other activities.

40. ACCA supports the recommendations in regard to local audit arrangements (Recommendations 76 to 78 and 82). ACCA believes, as with oversight of the actuarial profession, for the regulation of local government audits should be reallocated elsewhere, for example in a body similar to the former Audit Commission.
41. ACCA supports the broad thrust of the recommendations regarding independent supervision of the National Audit Office (NAO) (Recommendations 79 to 81). ACCA, however, believes, as with the regulation of local government audit, that supervision of NAO should be by a separate body (ie not the new regulator or FRC). Such a separate body could have responsibility for both the regulation of local government audit and supervision of NAO.

Question 12: Are there specific considerations you think we should bear in mind in taking forward the recommendations in this chapter? Are there other ideas we should consider?

42. ACCA supports Recommendation 83 on the proposed interim steps. ACCA would nevertheless caution against interim measures limiting the new regulator's ability to make changes to the regulatory system.

Question 13: What evidence or information do you have on the costs and benefits of these reforms?

43. The Kingman review acknowledges that there will be considerable increase in the activities of the new regulator compared with the FRC, which will inevitably cost more; this is supported by the increase in FRC's budget for 2019 / 20.
44. ACCA believes that more careful consideration should be given as to how the activities of the new regulator will be funded: expecting PIEs and the professional accountancy bodies to meet all costs is unrealistic. ACCA is therefore disappointed that the proposals did not take up the suggestion that the Government should make a contribution to these increased costs since the benefits will be enjoyed by the wider public.
45. In addition, Recommendation 5 recognises that the activities of the new regulator should be proportionate and take into account the resources of those being regulated. ACCA believes reserves held by FRC (accumulated through annual levies) should be used to fund not only the transition to the new regulator but also more generally to implement the reforms.

Question 14: What further comments do you wish to make?

46. There are no other matters that ACCA wishes to raise at this stage.

CONCLUSION

47. ACCA supports the development of a regulatory system that is proportionate, effective and credible and which operates to uphold the public interest.
48. ACCA welcomes the proposed reforms to strengthen trust and public confidence in the audit and corporate reporting regulatory framework. We welcome opportunities to share our views on proposals to implement the Kingman recommendations.