



## ARGA FUNDING CONSULTATION

Issued 21 October 2022

ICAEW welcomes the opportunity to comment on the **principles for funding ARGA** the FRC published on 29 July 2022. The funding model is a critical precursor for a strengthened regulator.

Stakeholders need ARGA to have stable, sustainable and independent funding to enable the strengthened regulator envisaged by Sir John Kingman to be achieved. They need ARGA to have reliable funding so it can consistently deliver on its mandate.

We appreciate being invited to contribute to the principles aimed to achieve this at the design stage, before detailed plans and budgets are set. We recognise the contribution stakeholders like ICAEW can make to help demonstrate how ARGA has calibrated its activities and resources through consultation.

As a statutory body, ARGA will be accountable to parliament for what it achieves, to what standards and with what effect. It will be subject to parliamentary scrutiny for the use of public funds and for the value for money it has provided. New approaches will be needed to budgeting, outcomes appraisal and reporting, supported by robust stakeholder dialogue.

The principles set out in the consultation document are a good starting point, but they are inadequate to address the considerations above. To do that we believe the Framework Document must have its foundation in four crucial pillars, to construct an ARGA that is:

1. **strong** – through a funding model that supports stability, sustainability and independence;
2. **proportionate** – by focusing on risk and minimising unnecessary costs;
3. **constructive** – with funding based on efficient, targeted and well-developed plans; and
4. **accountable** – as transparency and consultation secure strong stakeholder support.

We believe it is these pillars that will ensure ARGA is stable, sustainable and independent. These considerations go some way beyond what is set out in the consultation paper, but we believe they are essential components of the Framework Document and that they must be addressed now to give ARGA a firm foundation.

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# Key points

## A FRAMEWORK FOR SUSTAINABLE AND INDEPENDENT FUNDING

1. The funding of the FRC has historically been a combination of statutory requirements, contractual arrangements and a voluntary basis, paid for by preparers of accounts and the audit profession. As Sir John Kingman rightly observed in his independent review of the FRC, such an arrangement was ‘very unusual and is clearly inappropriate’.
2. Sir John recommended replacing that arrangement with a statutory levy. He envisaged ‘BEIS agreeing a new budget, consistent with the Review’s recommendations, working with the new regulator and consulting stakeholders’. In its Feedback Statement BEIS concluded that ‘the Government intends to give ARGA statutory powers to raise a levy so that it has a sustainable and independent basis to carry out its regulatory activities’.
3. **We strongly agree that ARGA should have statutory powers to raise a levy.** The *Statutory Auditors and Third Country Auditors Regulations* have since 2016 given the FRC a statutory basis to recover certain costs from the Recognised Supervisory Bodies. The new legislation would replace this with wider powers to raise public monies through a levy – which naturally creates a wider base to bear the costs of regulation. That should provide certainty and stability, not only for the regulator to carry out its activities in an effective manner, but also to the stakeholders within the audit, assurance, governance and reporting ecosystem.
4. The three principles on which the Consultation Document states ARGA’s funding model will be based – fair, transparent and proportionate – are at a high level appropriate and ones with which we agree. However, at such a high level, more detail will be needed to demonstrate that such principles are applied satisfactorily and in full accordance with relevant government guidance such as the Regulators’ Code and Managing Public Monies (MPM).
5. The Framework Document will require significant development from the principles set out in the Consultation Document. To help do that, this response is therefore structured around expectations which we believe could form sound principles for that framework. We believe a consultation on the contents of the Framework Document should follow in due course.
6. We strongly agree that, in order to secure a successful regulator, tasked with protecting and promoting the interests of investors, other users of corporate reporting and the wider public interest, ARGA will need a funding model that is stable, sustainable and independent. To achieve that, we believe the Framework Document should lay the foundation for a regulator that is: **Strong; Proportionate; Constructive; and Accountable**:

### 1. A STRONG REGULATOR

7. ICAEW firmly believes a statutory levy is essential for a strong regulator. Such a levy was a crucial part of Sir John Kingman’s recommendations and needs careful as well as rapid development to put ARGA in a secure and predictable position right from the start.
8. It is critical that ARGA can plan ahead reliably and provide consistency in the delivery of its functions. Levy payers, of which ICAEW is included, also require clarity and certainty in terms of the monies paid to deliver a strong regulator. To achieve this, we appreciate the important contribution that stakeholders can play through engaging with the regulator and helping demonstrate that ARGA has carefully calibrated its activities and funding in delivering on its remit. In reporting annually to parliament on its work, performance and value for money we hope that the contributions of ICAEW and other levy payers to ARGA’s consultations on its budget and planned activities can be useful in helping evidence efficiency and value for money.
  - **Recommendation 1. A statutory levy should be introduced as soon as parliamentary time allows to provide ARGA and relevant market participants with resilience in funding and certainty in expectations to establish a strong regulator.**

## 2. A PROPORTIONATE REGULATOR

### Base regulatory activities on risk

9. The **Regulators' Code** requires regulators to 'base their regulatory activities on risk' and 'take an evidence-based approach to determining priority risks'. The Code is clear in stating that risk should be considered at every stage of a regulator's decision-making process
10. It is therefore surprising that the consultation refers to risk only in the context of Corporate Reporting Review. We strongly believe a risk-based approach should guide all ARGA's regulatory work. Not only would that target scrutiny where it can have the most effect; a risk-based approach would also ensure efficiency and enable ARGA to fulfil one of the principles of its funding model, that of being proportionate.
11. For example, the cost of monitoring will largely be linked to the frequency and coverage of monitoring inspections. A constructive regulator should be resourced to conduct monitoring visits robustly and focus resources on identified risks; strong intelligence, review and reporting enables inspections to be directed to where they can be most effective. Decisions need to be made however about the extent of coverage and a reasonable balance struck between the cost of compliance and the risk of undetected deficiencies. We believe this balance can be informed by transparent dialogue with stakeholders.
  - **Recommendation 2. ARGA should make explicit reference to the risk-based approach in its guiding principle of proportionality.**

### Minimise unnecessary costs

12. BEIS's **statutory guidance on the Growth Duty** requires regulators to take 'steps to minimise unnecessary costs and maximise the benefits of interventions'. MPM expects public bodies to 'control their costs so that public money is used efficiently and effectively'. There are a number of examples that demonstrate choices that could be made to improve value for money. For example:
  - a. 'recognising where a business has established its own compliance system or participates in a wider compliance scheme such as those operated by, or potentially operated by, professional bodies and having regard to this in conducting its interventions' - duplication is clearly undesirable;
  - b. 'using digital delivery';
  - c. 'making effective use of networks that already exist in the business community';
  - d. having regard to proportionality in the design and stratification of interventions, in the conduct of individual interventions and cumulatively across interventions;
  - e. setting and meeting response targets.
13. The Regulators' Code requires regulators to 'minimise the costs of compliance for those they regulate'. This provision goes beyond ARGA minimising its own costs and expects that its interventions are designed in a way that also minimises the costs of complying with them. The FRC's draft plan and budget is insufficiently granular to enable stakeholders to assess choices the regulator has made in how it conducts its interventions.
  - **Recommendation 3. ARGA should establish regular and ongoing dialogue with levy-payers about efficiencies and networks and systems it can utilise.**

### Make effective use of existing compliance systems and networks

14. The Growth Duty statutory guidance requires regulators to have regard to compliance schemes already established and to existing networks in minimising unnecessary costs and maximising the benefits of interventions. Such a principle is reinforced by the Regulators' Code, which asserts that, in making a risk assessment decision, regulators should recognise the compliance record of those they regulate, including evidence of relevant external verification.
  - **Recommendation 4. To provide an efficient regulatory service and be proportionate in a risk-based approach, ARGA should evaluate compliance systems of entities being regulated in determining the nature and volume of its activity. It may be able to rely on them in making its own activities more efficient.**

## Understand the economic impacts of regulatory activities

15. The Regulators' Code requires regulators to 'understand and minimise negative economic impacts of regulatory activities'. To do so requires transparency and dialogue with stakeholders so that choices can be understood, and sufficient input given during consultation to enable options to be properly assessed. The regulatory approach that ARGA selects will have wider implications for stakeholders and entail certain costs which could have an economic impact.
16. For example, although the 2022-25 strategy, plan and budget does not disclose headcount for Professional Oversight, it shows ARGA significantly increasing expenditure on overseeing professional bodies and implies an increase in the volume of monitoring visits performed. This is despite (1) the decision to widen the PIE definition in the Feedback Statement, which will move more high risk audits into the jurisdiction of AQR; (2) the launch of the FRC's PIE audit registration scheme, transferring the review of AQR reports to a FRC committee; (3) the continuing decrease in the number of firms who are registered with the professional bodies to carry out audit work; (4) the continuing decrease in the number of those registered firms who carry out statutory audit work; and (5) the lack of any significant concern being raised in any recent inspection report about the quality of the work and the evaluation of audits by any of the professional bodies. So, the proposed increased expenditure on oversight appears to run contrary to that landscape and does not appear to be risk-based. The funding consultation provides no check and balance on how, and by much, the oversight functions of ARGA might increase and no requirement for any additional resources to be justified.
17. It is also important that any increased funding for the expansion of ARGA's activities takes into account, not only the additional direct costs of ARGA's operation which will be passed through as levies, but also the significant indirect costs which would be created by a significant expansion of ARGA's oversight functions. Additional costs will be incurred by all professional bodies in dealing with a larger oversight team. This would be due to more frequent and broader requests for information and more extensive inspection work (resulting in more time being spent answering queries, commenting on draft reports). An increase in work has already been seen through the recent expansion of the FRC's oversight team. This will force an increase in headcount at the professional bodies which, in turn, will have to be passed onto audit registered firms through increases in audit registration fees. This may result, in turn, to more audit registered firms deciding to give up their registrations, given how little audit work is carried out by many firms at the moment. The FRC is already undertaking an investigation into the sharp drop in the number of audit registered firms over the past 5 years. The additional costs falling onto those firms as a result of the professional bodies having to respond to increased oversight activity may exacerbate this issue and could lead to competition issues in parts of the country. We are concerned that the potential consequences of the ripple effect of increasing costs in this area will pose a serious risk of damage to the important eco-structure of smaller audit firms who are engaged by the UK's important SME sector. It would also run contrary to ARGA's second operational objective "to promote effective competition in the market for statutory audit work".
18. Equally, ICAEW will need to be in a position to be able to inform those it registers about the rationale for fees it charges, particularly where those increase significantly from year to year. Without adequate explanation and disclosure, ICAEW may face delays or even shortfalls in collecting fees. For this reason, it is important that there are clear and reliable mechanisms for dialogue with ARGA and that the regulator provides a high level of transparency about its activities.
19. In any regulated area a sensible balance needs to be struck between the degree of oversight and the risks observed and this should also take into account not only the performance levels of the professional bodies in discharging their audit regulatory tasks but also the extent and robustness of the governance and internal checks already in place at the professional bodies. For example, the FRC oversight team currently carries out its own annual independent inspection of all key elements of ICAEW's audit regulatory work and places little reliance on the checks which are already made by independent committees and the degree of supervision of those committees and staff by the ICAEW Regulatory Board. Greater efficiencies could be achieved by leveraging off the work already done to provide assurances

that ICAEW is fulfilling its regulatory responsibilities and acting in the public interest. We believe that any future funding of ARGA's oversight functions should take into account, and put greater leverage on, all of this work before any conclusion is reached that more oversight, and more funding, is required for oversight activity.

20. To augment and extend the current consultation exercise, ARGA could continue to develop the feedback statements that the FRC has recently instigated, and post implementation reviews of changes, after a certain period has elapsed. Together these could help explain how a regulatory development has resulted in a positive change. In this reporting ARGA could also consider diversity and inclusion outcomes – as regulatory changes may particularly impact certain sections of the regulated community or their stakeholders.
- **Recommendation 5. The legislation establishing ARGA should contain a duty that it will assess and report on the economic impact of the activities it is proposing to undertake and then consult on this as part of the annual budget exercise.**

### 3. A CONSTRUCTIVE REGULATOR

21. We agree with the proposed approach set out in the Consultation Document that, in accordance with *Managing Public Money*, ARGA's funding requirement will be split into 'activity blocks' and allocated to market participants, or 'funding groups'. This high-level approach should provide certainty and transparency.
22. We also believe that a constructive regulator could usefully provide transparency around the activity blocks. The blocks could be broken down into a series of programmes and projects, each with clearly defined outputs and outcomes – but crucially as a whole giving assurance that ARGA has a robust strategy to achieve restored trust in audit and corporate governance.
23. To enable this needed transparency and accountability – and generally to make the levy process more efficient – the FRC could simplify the levy categories as far as possible. Where a single entity is being assessed for levies under multiple categories, it would make sense for it be simplified such that there is only one category for that type of entity. That would make the segmentation of reporting less complex, among other benefits.
24. The HM Treasury *Magenta Book* sets out a framework for Value for Money evaluation, this includes 'whether the benefits of the policy are outweighed by the costs, and whether the intervention remains the most effective use of resources'. We believe that such an approach would enhance transparency and make ARGA more accountable to stakeholders.
- **Recommendation 6. Through its public reporting and open dialogue with levy payers, ARGA should disclose its planned programmes and projects, report on how they are keeping to their critical paths and spending envelope and explain how they are making effective use of resources.**

**ARGA should simplify its levy structure so that a single entity only falls into one levy category – as far as possible.**

#### Match levies to the cost of provision

25. The consultation envisages that different levies would be charged to different kinds of licensee. *MPM* anticipates such a situation and stipulates that charges should reflect the cost of provision to that category of licensee. The consultation document makes reference to different activities pertaining to each levy category, but as set out above, further transparency is needed to be able to conclude that the levy amount does indeed represent the cost of provision.
26. For example, for accountancy bodies it is suggested that an allocation would be made according to the number of members. This is an over-simplification. The CCAB uses member numbers for a minority of the recharge, a larger portion is funded by a levy on registered audit firms. In general, the basis used expects those that benefit from regulatory coverage to pay rateably for it. Conversely, no evidence has been presented that the FRC's proposed

basis will actually reflect ARGA's cost of provision, and we believe further analysis is necessary to support such a conclusion.

27. A sensible solution to this would be to build in mechanisms for constructive dialogue with levy payers, or groupings of levy payers, supported by appropriate transparency.
- **Recommendation 7. Under the principle of proportionality ARGA should stipulate that the levy charged to each category licensee reflect the costs of provision to that category.**

#### 4. ACCOUNTABLE REGULATOR

28. The consultation document identifies transparency as one of the three guiding principles for the funding model. We agree that this is important. MPM expects public bodies to publish information 'in sufficient detail to enable users to hold the organisation to account'. It expects also that they provide adequate controls and reporting on 'what is being achieved, to what standards and with what effect'.
29. It is welcome that the Consultation Document pledges ARGA will 'explain how its funding requirement has been set for each regulatory activity' and publish its 'annual work programme and key performance indicators'. However, in so doing, the granularity the FRC has previously provided in its reporting falls short of expectations for a statutory body and is insufficient to enable stakeholders, including Parliament and the general public, to hold ARGA to account.
30. In our response to this year's draft plan and budget we said that 'regardless of funding, the principle should be transparency and value for money. There are some areas where further elaboration would help stakeholders better understand the FRC's plan and strategy during this critical period – including some aspects that need to be developed with urgency'. We requested 'metrics to enable assessment of value for money' and information sufficient for 'a clear understanding of what the regulator is delivering'.
31. MPM requires public bodies to 'make available timely information about their services, standards and performance', publish 'regular information about their plans, performance and use of public resources', and give 'sufficient detail, and be sufficiently regular, to enable users and other stakeholders to hold the organisation and its ministers to account'.
32. Specifically, it states 'it is important that parliament is fully informed about use of charges. Each year the annual report of the charging organisation should give:
- the amounts charged;
  - full costs and unit costs;
  - total income received;
  - the nature and extent of any subsidies and/or overcharging; and,
  - the financial objectives and how far they have been met'.
- To this might also be added reporting on the benefits achieved from the regulator's work.
33. The FRC's Annual Report runs to 160 pages, but it does not provide sufficient information to enable the cost of providing services at the unit level to be reconciled to the contributions levied on the different groups benefiting from those services. We appreciate the effort the FRC has gone into in the current consultation to analyse its activities into different areas. To provide the transparency envisaged by MPM we believe the FRC should disaggregate the reporting of its costs into these categories, as appears to be envisaged in the consultation document. That would give visibility of unit costs and provide transparency of subsidies and overcharging between areas of activity.
34. We are concerned that the proposals have considerable flexibility to enable ARGA to expand its scope of work, employ additional staff and accordingly raise levies to fund such activities without sufficient explanation to, or effective challenge from, stakeholders.

### Role-model high standards of transparency

35. We staunchly endorse a strong regulator, focused on achieving higher standards and quality in audit, governance and corporate reporting. However, there is a clear absence of processes and controls to place a downward restraint on the regulator's rising budget. Such increased costs will ultimately be borne by companies. At a time when costs of doing business are growing, this will have an additional impact on the ability of the UK corporate base to power economic growth and enhance this country's international competitiveness.
36. Given these concerns, proper, informed public debate is vital, as is timely dialogue with levy-payers. That requires transparency, and here we look to ARGA to role-model high standards.
37. G20/OECD **Principles of Corporate Governance** recognise 'a strong disclosure regime that promotes real transparency is a pivotal feature of market-based monitoring of companies'. They acknowledge that cost and commercial sensitivity affect granularity – with materiality defining disclosure – that is, the level of information necessary to inform users' decisions.
38. Levy payers are interested in what materially affects the levy they are required to pay. To do that, they need disclosure of costs for each levy category. Otherwise, it is impossible to assess what contributes to the levy that must be paid.
- **Recommendation 8. Under the principle of transparency, and as envisaged by MPM, ARGA should disaggregate reporting of its costs into the separate activity areas assessed for levies. This information should be disclosed in its annual report.**
39. We appreciate that even though material to levy-payers, full disaggregation may still be considered undesirable in public reporting; MPM acknowledges the need to 'strike a careful balance between protecting confidentiality and open disclosure in the public interest'. ARGA should be a role model in considering and solving this challenge.
40. Thought is needed of who will carry out ARGA's audit. We assume that will be the NAO.

### Role-model high standards of governance

41. ICAEW has **consistently provided input** to the FRC's annual budget exercise and the Consultation Document envisages this process continuing. While we are pleased that stakeholders have been consulted on the FRC's activity plan and its resourcing, it has not always been clear how this feedback has been received. That is despite an expectation in the Growth Duty that "the regulator draws on all relevant information that is available to it to improve the targeting and focus of interventions".
42. To become a truly accountable and transparent regulator, greater clarity is needed as to how ARGA has amended its funding envelope or mix of activities in response to the budget consultation. One route through which greater transparency could be achieved is by opening parts of ARGA's board meetings to public observation.
- **Recommendation 9. ARGA should open part of its board meetings to the public. For example, the PCAOB broadcasts board meetings that discuss its budget.**
43. We support the Government's and FRC's ambitions to make ARGA help set high standards in audit, reporting and corporate governance. A key element of good governance, particularly in respect of accountability, is the holding of an annual general meeting. As the FRC has itself stated in its Corporate Governance AGM guidance, published in October 2020, 'The Annual General Meeting is an essential governance event for companies and their shareholders. It should provide transparency, accountability and integrity'. We believe, that as regulator of high governance standards, an Annual General Meeting, in which the board could present the regulator's strategy, performance and budgetary plans, and stakeholders could hold the board to account, would be welcome.
- **Recommendation 10. To help get this input and enable points of difference to be raised ARGA should hold an Annual General Meeting. Ideally the cycle would be timed to allow for the AGM to be held during the period of the budget consultation.**

44. In evidencing good governance ARGAs board – and its Independent Non-Executives - will play a crucial role. ARGAs INEs should be given a role in giving an opinion on the effectiveness with which ARGAs has met its funding principles. This could be done as part of the process for reviewing the annual accounts.



# Answers to specific questions

## OVERALL APPROACH TO ARGA'S FUNDING

### **Question 1. Do you have any comments on the proposed guiding principles for ARGA's overall funding arrangements?**

45. Yes. We agree that ARGA's funding model should reflect the principles BEIS has consulted on and be fair, transparent and proportionate. However, in developing the Framework Document these principles in isolation are inadequate and need further development. There are a range of considerations in government rules and guidance that are relevant to ARGA's funding model and which we believe will be expected to be reflected in the Framework Document. In the Key Points to this response therefore we set out four pillars that we believe will help build on and draw out what is intended by fairness, transparency and proportionality. We believe the Framework Document should be built around these four pillars to construct a regulator that is **Strong, Proportionate, Constructive and Accountable**.

### **Question 2. Do you have any comments on the proposals for setting ARGA's annual funding requirement?**

46. Yes. We agree ARGA should establish a Framework Document and consult annually on its business plan, budget, annual work plan and key indicators. This will need to be much more granular than the exercise currently undertaken by the FRC – enabling analysis both of expenditure and the activity planned by levy area and would benefit from proactive dialogue with stakeholders. There should be meaningful and granular feedback on the actions resulting from consultation.
47. In terms of the annual funding requirement, we do not believe it will be sufficient for ARGA to set out only 'the resources it requires'. As referenced in paragraph 14, BEIS expects regulators to avoid unnecessary costs. Therefore, we believe that published information should go further and provide assurance that the activities selected also provide value for money when assessed against other options.
48. Paragraph 4.7 of the Consultation Document suggests that a similar approach may be envisaged for each of the four enforcement regimes – we do not believe that such an approach would be proportionate. We agree that ARGA needs to have statutory powers in relation to PIE Directors duties for reporting and audit and for Accountants involved in PIEs, but our expectation was that these powers would be directed by risk and would be expected to be used in exceptional cases only. The AQR and the CRR need to have coverage over the regulated population and should be the primary means of monitoring audit and reporting quality. We assume that ARGA is not seeking to replicate the monitoring approach of AQR or CRR in its new powers over PIE Directors and Accountants.
49. Paragraph 4.11 suggests that there should be provision for top-up levies in the event of underbudgeted enforcement costs. We have serious concerns about this proposal. Firstly, we believe that the future funding of ARGA's enforcement activity needs to explicitly recognise that money is already flowing into public funds from financial sanctions which are levied on the firms when allegations are proved. Financial sanctions imposed on firms in enforcement cases brought under the Audit Enforcement Procedure are already remitted to HM Treasury. The advent of ARGA and a new funding model should consider how those financial sanctions can be reinvested by ARGA to ensure adequate funding for all enforcement activity. It is positive that HM Treasury acts as an intermediary – to reduce the potential incentives to ARGA of maximising fines to increase its own funding. But these monies need to be available for reinvestment in enforcement and ideally a buffer would be created within ARGA which would be topped up, whenever necessary, to an appropriate level by levies on firms. All of the professional bodies are currently obliged by the Delegation Agreements to ensure that all financial sanctions imposed on audit firms through disciplinary proceedings are re-invested in future audit investigations and disciplinary proceedings so,

ensuring the FRC's own financial sanctions are similarly reinvested will create much needed consistency.

50. The ability to seek top up levies during a funding year also provides no incentive within an organisation for effective and efficient financial management if the organisation is able to find additional funds if it going to exceed its budget. If such levies are to be imposed at all, there should be strict criteria to be fulfilled including the need for the Executive Counsel to set out good reasons why such additional levies are necessary by pointing, for instance, to the opening up of a new significant investigation which was not foreseen at the time when the original levies were collected or to explain why costs on existing cases are now likely to exceed original budgets. While elements of such matters will be confidential, we consider that there is a compelling need to explain why the position has changed so significantly in such a short space of time to justify calls for additional funding mid-year.
51. We are also concerned that there is no reference to what would happen in the event that enforcement costs are overestimated. This could happen in circumstances where the estimated costs include the heavy costs of contested tribunals, but those costs are not incurred due to settlement agreements with the firms facing complaints. In such circumstances, it would only be fair and appropriate for any excess funding to be carried forward into the next financial year (rather than being used for any other activity) and set off against the levies which would otherwise be collected for the estimated costs of the following year's enforcement activities.
52. The annual reporting cycle would benefit from an additional step of an AGM, giving an opportunity for pre-active dialogue and greater accountability between ARGAs and levy payers as part of the consultation. In addition, parts of ARGAs's board meetings could be made open to public observation.

**Question 3. Do you have any comments on the proposed approach to setting ARGAs's annual levies?**

53. Yes. It is not clear how the Funding Principles and Funding Rule Book will relate to the Framework Document. We suggest that the Framework Document make reference to the four pillars above (strong, proportionate, constructive and accountable) and that ARGAs's implementing documents then elaborate these in more detail.

## ALLOCATION OF THE LEVY

**Question 4. Do you have any comments on the proposed approach to setting ARGAs's annual levies for its responsibilities in relation to audit?**

54. Yes. We agree that a direct levy on PIE audit firms is appropriate for the items set out in the table. The PIE audit firms benefit directly from ARGAs's oversight in these areas and should contribute to that. Conceptually the principle of allocating PIE audit fees based on the firm's overall fees from PIE audits has some logic, but the FRC should do further analysis to disclose and explain how far this reflects the distribution of expected activity. However, as elsewhere in the consultation it does not seem adequate as a conclusion without further disclosure and dialogue to provide assurance that it does indeed result in a fair allocation. The core principle should be that the levy is based on the cost of provision – although that may vary by size of firm, it is not possible to conclude that it is directly linear without more information about ARGAs's activities. We agree that it is preferable to use an 'input' measure such as audit fees rather than an 'output' measure such as the volume of regulatory interventions, which could incentivise adverse behaviour. However, the costs recovered through the levy should only be those of provision. We suggest that greater transparency and dialogue are the way to address this.
55. Equally, it does not stand up to scrutiny that the professional body contribution be based solely on the number of members. That the CCAB has hitherto used this method is not necessarily relevant as ARGAs will be operating under government guidelines, whereas the CCAB operates in agreement with its members. MPM requires that levies recover the cost of

provision. The number of members is unlikely to correlate with ARGA's core costs around audit supervision and standards, indeed it is an over-simplification of the methods currently used by the CCAB, which more closely link costs to those services are provided to.

56. The solution here, as above, is to implement incremental transparency and dialogue so that levy-payers, or groupings of levy-payers, can see the basis is fair and have an opportunity to raise any concerns with ARGA.
57. 6.25 suggests that ARGA will be able to recover all of the costs of pursuing Mutual Recognition Agreements from the professional bodies. ARGA needs to play a strong role in this area. However, from our experience it can be easy to invest significant time in unproductive negotiations. There needs to be transparency about the nature and success of ARGA's MRA work and a pro-active opportunity to raise any concerns.
58. We object to the proposal that professional bodies be levied for the costs of third country audit registration, except where there is reasonable grounds for doing so, for example in the case of the Crown Dependencies. In the case of the Crown Dependencies we would like to see greater transparency around the nature of ARGA's activities there.

***Question 5. Do you have any comments on our proposals for funding ARGA's responsibilities in relation to accountants and their professional bodies?***

59. We argued strongly in our response to the BEIS White Paper that the proposals had failed to put forward any good evidential basis to introduce statutory regulation on accountants who are affiliated to professional bodies. The ICAEW Regulatory Board's initial and supplemental responses set out the comprehensive system of independent oversight already in place at ICAEW to oversee the activities of ICAEW chartered accountants which fall outside of any statutory regime. It is very disappointing that such a comprehensive analysis was dismissed in the Feedback Statement by inaccurate references to the regulatory boards being funded by the professional bodies (they are not – the activities of the ICAEW Regulatory Board are funded by regulatory fees which it imposes on firms carrying out regulated work – hence our claim to have independent oversight in place which could not be influenced by ICAEW's representative side).
60. Our response to these proposals in the White Paper – particularly the IRB's detailed supplemental response setting out just how much independent oversight is already in place – needs to be the starting point for any consideration of funding for any additional oversight. We do not oppose the proposal that the costs of this additional oversight if it is implemented through legislation should be imposed on the professional bodies (as it is difficult to see where else it could be imposed) but we would want to ensure again – in common with the theme of many of our responses within this document – that the costs of this oversight are limited due to ARGA leveraging off the independent oversight which is already in place rather than carrying out its own independent assessment. Such oversight should, in the case of ICAEW, take into account the constitution of the independent disciplinary and regulatory committees, the extent of the delegated powers' reviews which they carry out every year of the work carried out by PSD staff on their behalf and the quality assurance programme carried out by the IRB over the effectiveness of the committees. It should also reflect the fact that certain aspects of the work carried out to ensure ICAEW chartered accountants are acting appropriately (e.g. the ICAEW Practice Assurance Scheme) are already evaluated by other oversight regulators.
61. We believe this is important because ICAEW, like other professional bodies who will bear this cost, will have no alternative but to pass the costs of this oversight onto ICAEW members through an additional levy on top of membership fees and/or practising certificate fees. This will, in turn, be an additional cost on businesses and firms in public practice which, in turn, will be passed onto their clients which, for smaller firms, will be individuals and small businesses. Alternatively, an additional significant levy on accountants who are affiliated to professional bodies may be the 'straw which breaks the camel's back' in respect of the value they see in maintaining that affiliation. The passing on of this additional cost may have the effect of making them even less competitive against fees charged by the significant number of accountants who will continue to operate in the UK without any regulation at all. We do not

believe that any further movement of accountants to the unregulated sector would be in the public interest.

62. In relation to the work envisaged at B2, we do not understand the current proposal which appears to suggest that the costs of any enforcement action against an accountant in relation to a public interest matter will be borne by the professional bodies generally. If this is the case, we do not understand why there would be no continuation of the current situation under the Accountancy Scheme (through which those complaints could be taken currently) where the professional body of the member in question would fund the costs of those enforcement actions by ARGA on the basis and understanding that such costs would be remitted to the professional body if the investigation leads to the upholding of a complaint and the imposition of a costs order on the member concerned. There is no mention in Section 7 of costs being recovered by the professional bodies in this way which seems both unfair and inconsistent with what is in place currently. Presumably, there will still be costs orders imposed? And, if so, there would seem to be no reason why the current process should not continue to operate. If it is, however, being proposed that such actions are funded without any costs order being imposed or without the proceeds of any costs order being remitted, such a regime will lead to all well-behaving members of professional bodies paying for the costs of ARGA investigating and prosecuting an enforcement case against a member who is believed to have acting in breach of their fundamental principles. This would be a very unfair outcome. As it is, well-behaving members would appear to be liable in any event for the costs of any investigation carried out by ARGA's enforcement team which did not lead to a complaint being upheld and a costs order being made.
63. Given the potentially inequitable funding arrangements examined above, we would also stress the need for ARGA to ensure, as was proposed in the Feedback Statement, that any such enforcement actions are limited to members who are accused of poor conduct or work in respect of work carried out with the financial reporting process of PIE entities where there will be a public interest concern.

**Question 6. Do you have any comments on the proposed approach to setting ARGA's annual levies for its responsibilities in relation to corporate reporting?**

64. No, apart from the principles above, which also apply to this section. A new preparers' levy is an important part of ARGA's funding and it is crucial that this is adequate to support the incremental work required in this area.

**Question 7. Do you have any comments on the proposed approach to setting ARGA's annual levies for its responsibilities in relation to corporate governance?**

65. Yes. We believe that ARGA's objectives in this regard needs to be further developed. In our response to the BEIS consultation on audit reform and corporate governance, we suggested that ARGA's remit be specifically targeted at directors' duties in relation to reporting and audit. This would naturally extend to the corporate governance around reporting and audit, and to reporting on corporate governance. However, the feedback statement suggests that ARGA will have much wider responsibilities for 'good corporate governance' – this is so open ended as to be impractical. It is questioned what actions ARGA's powers will enable it to take to identify and address corporate governance concerns.
66. To take one, more objective, example – one principle of the Corporate Governance Code is that the roles of Chair and CEO be separated. The control over this is to explain in reporting where this is not the case, such as stakeholders can take this code contravention into account in their decisions. Our suggestion of an ARGA objective linked to audit and reporting would cover this. We assume that it is not intended that ARGA would have powers to forcibly separate the roles of Chair and CEO. It is therefore unclear what it is envisaged that ARGA will do in relation to enforcing good corporate governance.
67. If is not at all clear what the regulator will do in this area, there is not a sound basis for generating a levy. It needs to be clear exactly what ARGA is setting out to achieve, with KPIs and then detailed disclosure of the activities deemed necessary to achieve this to enable informed input through consultation.

**Question 9. Do you have any comments on the proposed approach to setting ARGAs' annual levies for its responsibilities in relation to public interest actuarial work?**

**Question 10. Do you have any initial comments on the metrics that should be applied to determine the appropriate share of the costs of actuarial regulation between the proposed funding groups?**

68. No. We believe the recommendations set out in this response should be applied equally to ARGAs' regulation of actuarial work. However, as we are not a qualifying or supervisory body for actuaries we do not have any specific observations in this regard.

## ABOUT ICAEW

Since our Royal Charter was granted in 1880, ICAEW has been responsible for maintaining the highest professional standards as well as delivering technical excellence in the public interest.

### Our role as a world-leading improvement regulator

We protect the public interest by making sure ICAEW firms, members, students and affiliates maintain the highest standards of professional competency and conduct.

ICAEW's regulatory and disciplinary roles are separated from ICAEW's other activities so that we can monitor, support or take steps to ensure change if standards are not met. These roles are carried out by the Professional Standards Department (PSD) and overseen by the independent ICAEW Regulatory Board (IRB).

Our role is to:

- **authorise** ICAEW firms, members and affiliates to undertake work regulated by law: audit, local audit, investment business, insolvency and probate;
- **support** the highest professional standards in general accountancy practice through our Practice Assurance scheme;
- **provide** robust anti-money laundering supervision and monitoring;
- **monitor** ICAEW firms and insolvency practitioners to ensure they operate correctly and to the highest standards;
- **investigate** complaints and hold ICAEW firms and members to account where they fall short of standards;
- **respond** and comment on proposed changes to the law and regulation; and
- **educate** through guidance and advice to help stakeholders comply with laws, regulations and professional standards.

The PSD's regulatory, disciplinary and Practice Assurance functions are self-financing. ICAEW membership and practising certificate fees are not used for these functions. Income is mainly funded by the fees paid by the firms or individuals regulated and supervised by ICAEW. These fees are set by the IRB. Fees are also generated from outsourcing contracts carried out by the Quality Assurance team and from award-winning training films.

ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision of a world of strong economies, ICAEW works with governments, regulators and businesses and it leads, connects, supports and regulates more than 157,000 chartered accountant members in over 147 countries. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical and ethical standards.

## BACKGROUND TO THE CONSULTATION

For the reference of our members and others who may be reading this response in the public domain, we have set out here some background to the consultation to give context to the comments in this response.

BEIS published its Feedback Statement to the White Paper Restoring Trust in Audit and Corporate Governance on 1 June 2022. The Feedback statement says ‘the government intends to give ARGAs statutory powers to raise a levy so that it has a sustainable and independent basis to carry out its regulatory activities. It said it intends the levy to be:

- **‘Fair**, funded by market participants, that is persons or bodies for which ARGAs’ activities directly relate or which otherwise benefit from those activities;
- **Transparent**, with information made publicly available on the costs and activities being funded by levy payers, and the basis for the apportionment model; and
- **Proportionate**, to avoid any significant adverse impact on growth and competition, the levy contributions should consider factors such as the size and type of body being levied.

BEIS says it intends ‘that the regulator will be given the power to make rules requiring that market participants pay a levy to meet the regulator’s costs of carrying out its regulatory functions. Those rules would specify the market participants who will be required to pay the levy, and the amounts payable by them. ARGAs will consult publicly on those rules before they are made’.

In setting those rules BEIS suggested these parameters:

- that the levy is transparent, predictable and sustainable;
- the levy will be cost reflective and will comply with Treasury guide [Managing Public Money](#);
- the regulator group its activities into “activity blocks” similar to the FCA and PRA;
- ARGAs would then estimate the costs of carrying out the activities which fall into each block, and apportion those costs between the relevant persons or bodies within that block. In making allocations ARGAs would consider the size and nature of the market participant;
- firms responsible for PIE audits will contribute to ARGAs’ funding on the basis that those firms will be directly regulated by ARGAs;
- RSBs, in performing their delegated responsibilities, will contribute on the basis that those bodies will continue to be supervised by ARGAs;
- ARGAs’ levy-raising power is flexible enough to cope with unforeseen circumstances.

We published an analysis of the FRC consultation to inform our members about it and encourage them to share their views with us [FRC launches consultation on ARGAs funding](#).

We will be following further developments, including the publication of the draft legislation to establish ARGAs and the FRC’s feedback statement on this consultation. Developments will be published in [ICAEW Insights](#) which is free to the public to subscribe to.

Comments and enquiries can be sent to ICAEW at [john.boulton@icaew.com](mailto:john.boulton@icaew.com).