



FRC DRAFT 3 YEAR PLAN CONSULTATION

Issued 27 January 2023

ICAEW welcomes the consultation by the Financial Reporting Council (FRC) on its **Draft 3 Year Plan**, published on 16 December 2022.

In ICAEW's submission to the **FRC's consultation on the principles for funding ARGA**, we set out the four pillars we believe are necessary to construct a stable, sustainable and independent ARGAs – and through which we have approached the FRC's draft three-year plan:

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

Bringing forward consultation on the draft plan and budget has provided a valuable opportunity for dialogue with stakeholders. We hope the FRC will continue to engage proactively with stakeholders, finding opportunities for collaboration to advance progress on its priorities for 2023.

The draft 2023/24 budget heralds a significant increase in the contribution that ICAEW is required to make to the Consultative Committee of Accountancy Bodies (CCAB) to fund the FRC's activities. The CCAB contribution increases by £2.9m (25%). It is essential that this increased funding is accompanied by increased transparency about what the FRC will be using these funds to achieve.

The draft plan is also an important document for ICAEW, both as we forecast our future financial contributions to the FRC and as we plan our activities for the period. To help us do that we would like to see:

- greater clarity about the FRC's priorities and more detail on the activities and deliverables its plans will entail for the next three years;
- greater transparency on progress against the FRC's deliverables. At the budget stage it would be useful to see disclosure of milestones for each priority; and
- activities aligned with the strategic objectives that stakeholders most need to see effective action on. From our perspective, we have identified seven priority areas we believe are particularly important:
 - tangible progress in restoring trust in corporate reporting, governance and audit;

- the FRC completing the elements of its transformation programme that it is able to implement ahead of legislation;
- supporting companies as they prepare to implement the four major new areas of reporting promised in the feedback statement (Resilience Statement, Material Fraud Statement, Audit and Assurance Policy (AAP) and Distribution Statements);
- supporting the government's ESG priorities by properly preparing companies for new carbon and other reporting requirements;
- entities, directors and auditors all playing their part in enhancing the quality of reporting, governance and audit, with the FRC calibrating its activities across the whole ecosystem, directing its attention based on evidence of risk;
- the FRC acting as an effective shadow system leader for local audit and financial reporting in preparation for assuming full system leader powers once the Audit, Reporting and Governance Authority is established; and
- convening UK stakeholders to set and pursue clear objectives in the major International Auditing and Assurance Standards Board (IAASB) and International Ethics Standards Board for Accountants (IESBA) standard setting projects;

- it is appropriately attributed, replicated accurately and is not used in a misleading context;
- the source of the extract or document is acknowledged and the title and ICAEW reference number are quoted.

KEY POINTS

1. ICAEW welcomes the opportunity to comment earlier in the cycle on the FRC's draft three-year plan for 2023-26. We believe the FRC's decision to bring forward the publication of this plan allows for a wider opportunity for stakeholders to feed in their views on the FRC's priorities and plans, and for the FRC to consider these before adopting its budget.
2. The budget shows an increase of £2.9m (25%) in the contribution the CCAB makes to the FRC. This reflects increased expectations on the FRC as it transitions to ARGA and several strategic areas where it is essential the FRC makes a strong impact in 2023. It is essential with this increased funding that the FRC is more transparent about how it intends to address these strategic areas and shows that it is making effective use of the additional funds.
3. The FRC's draft three-year plan provides a helpful indication for what it will be focusing on over the period 2023-26. At ICAEW we will be developing our own workplans for this period, which will be informed by FRC activity – updating our members, adjusting our approach to supervision, and providing our own input into the FRC as the organisation seeks to deliver policy outcomes. Unfortunately, the current level of detail in the plan is insufficient to properly support this – a better understanding of the FRC's deliverables and their phasing, in particular for the year ahead is important for our own planning.

Engagement and transparency

4. ICAEW welcomes the FRC's suggestion of engagement with current and future funders. Short and long-term insight will be helpful to all funders, not least in order to help facilitate their own plans and budgets. The FRC's levy payers, including the professional bodies via their CCAB contribution, will be seeing significant increases in how much funding they provide to the FRC.
5. We are concerned, however, that the plan itself does not currently provide the level of detail to assure stakeholders that there is justification for the increased spend, or articulate the systemic risks which the FRC is seeking to address with the activities it has selected. There should be a clearer link between key risks/priorities, activities to address those areas and value delivered.
6. This is important because many of the key areas the FRC is working on are shared priorities. Stakeholders need to invest and develop plans in these areas, where the timing and nature of activities will depend on outputs from the FRC. Knowing what the FRC will be doing, and when, will help with better planning and more robust and timely responses to these shared priorities. As the FRC grows and its touch points with stakeholders increase, that coordination becomes more important. We have listed some key areas in paragraph 13.
7. ICAEW recognises that the FRC needs to strike a balance in its three-year plan between providing a broader strategy for its work, and a more in-depth plan for each priority. However, we do not believe the proposed plan provides sufficient granularity on the priorities listed. Indeed, without outlining how they will be scheduled and resourced, the number of priorities that the FRC is seeking to pursue risks not providing stakeholders with confidence that they will be delivered.
8. One important example is how the FRC ensures that it takes a 'joined-up' approach to improving competition and choice in the audit market. The regulatory approach of the FRC and the activities it undertakes can have the effect of either reinforcing or restricting the effectiveness of measures designed to improve competition and choice – for example, changes to the PIE definition and PIE auditor registration. It is important for the FRC to always approach the complex issues of competition, quality and capacity in the market in a holistic manner, rather than dealing with issues piecemeal.
9. This 'joined-up' approach must also be applied to the FRC's work restoring trust in the UK's corporate reporting, governance and audit regime – reforms on all aspects of this package must be considered together to ensure they are well aligned. A failure to do so will lead to lop-sided reform, and demonstrate a failure to learn the lessons from Carillion and other

recent company failures – that there needs to be a strong emphasis on tightening internal controls and modernising corporate governance.

10. In outlining its prioritisation of the supervisory oversight strategy for professional bodies, the FRC hasn't provided an explanation for the increase in expenditure for Professional Oversight. In the absence of serious issues in performance of any of the Recognised Supervisory Bodies (RSBs), we question the rationale for increased funding to recruit and deploy more Oversight staff – especially considering growing evidence that the enlargement of this team is leading to additional workload for RSBs which will require the audit registration fee to increase, potentially causing smaller audit registered firms to consider giving up their registrations.

Priorities

11. The FRC should provide greater clarity on those activities which it believes contribute to strategic priorities, and those which are more 'business as usual'. While business as usual activities might be expected to be spaced evenly over the year, strategic or transformational projects will have specific milestones, and it would be helpful for these to be disclosed as stakeholders themselves need to plan for actions at these points.
12. It would be helpful for the FRC in its forward plan to frame its priorities within the context of the wider UK economic and business landscape. Looking at 2023, and across the three-year period this plan covers, it is expected that the UK economy will be entering recession. This brings with it sustained pressure on businesses and a renewed emphasis on investor and societal confidence in the resilience and reporting of companies. It may also require a greater focus on going concern, and risks of fraud.
13. We welcome the opportunity this consultation presents for proactive dialogue with stakeholders, which we hope will be helpful to the FRC in focusing on those issues which require sustained attention this year. ICAEW believes that over the next twelve months, the FRC will need to demonstrate to stakeholders progress on, and appropriate resourcing of, the following issues:
 1. tangible progress in restoring trust in corporate reporting, governance and audit;
 2. the FRC completing the elements of its transformation programme that it is able to implement ahead of legislation;
 3. supporting companies as they prepare to implement the four major new areas of reporting promised in the feedback statement (Resilience Statement, Material Fraud Statement, AAP, and Distribution Statements);
 4. supporting the government's ESG priorities by properly preparing companies for new carbon and other reporting requirements;
 5. entities, directors and auditors all playing their part in enhancing the quality of reporting, governance and audit, with the FRC calibrating its activities across the whole ecosystem, directing its attention based on evidence of risk;
 6. the FRC acting as an effective shadow system leader for local audit and financial reporting in preparation for assuming full system leader powers once ARGAs is established; and
 7. convening UK stakeholders to set and pursue clear objectives in the major IAASB and IESBA standard setting projects.
14. Alongside the provision of greater detail on priorities and their phasing across the coming year, we would like to see the FRC be transparent about the problem it is seeking to fix in each area. This will allow stakeholders to understand what activity the FRC will be undertaking, including any workstreams they will likely be involved in. It will also enhance transparency and accountability by allowing stakeholders to scrutinise the success of the FRC's activity.
15. Following the consultation we would encourage the FRC to explore opportunities to convene stakeholders to discuss those areas they will be prioritising in 2023. We believe it would be mutually beneficial to share information about plans and expectations in the areas above and other priorities identified.

DETAILED COMMENTS ON THE 2023 PLAN

Regulatory Standards

Development and maintenance of standards and codes, including completion of the periodic review of FRS 102, adoption of a revised International Standard on Auditing (ISA) (UK) 500 Audit Evidence, post-implementation reviews of UK auditing standards (in particular ISA (UK) 540 Accounting Estimates and Related Disclosures), review of the UK Corporate Governance Code, and post-implementation review and revision of technical actuarial standards (TAS)

16. We welcome the FRC indicating which regulatory standards it will be prioritising development on and maintenance of within its three-year plan. However, we believe stakeholders would benefit from detail on the work being done in different fields of standards, distinguishing between corporate reporting, audit and assurance, corporate governance etc. The International Accounting Standards Board (IASB), IAASB and IESBA publish detailed workplans by standard showing a timeline of activities, with further details outlined in the board minutes, which are made public; a similar approach by the FRC would benefit stakeholders.

International influencing of auditing, assurance and ethical standards, and significant contribution to non-financial reporting developments in the UK and internationally (especially sustainability reporting)

17. It is good to see the FRC participating actively in the IAASB and IESBA through its board representation and leadership of key projects. This provides a good opportunity to project a UK voice internationally. Last year the UKEB established broad ranging advisory groups to support it in its projection with the IASB and this approach is one the FRC might replicate with its international standard setting work.
18. The FRC's priority of influencing international standards does not make clear the role of the UK Endorsement Board, which have similar objectives for their activities which are much more specific to the UK adoption of IFRS and IASB-influencing. The FRC should provide greater detail on how the work of the UK Endorsement Board interacts with this priority and ensure there is no duplication of activity.

Policy support for ARGAs local audit systems leader role

19. We set out our views on local audit in paragraphs 37 – 42.

Activities focused on improvements and innovation to support high-quality reporting and audit including Lab publications and use of the new 'Audit Sandbox'

20. These are important activities for the FRC, particularly in preparation for the four new reports promised in the feedback statement and the increasing focus on ESG and statutory carbon disclosures. The Lab has been very successful in bringing together companies and investors to discuss ways to improve corporate reporting. It produces high quality guidance based on those discussions. ICAEW is pleased to have had the opportunity to contribute actively to the work of the Lab over many years, including as a member of its steering group. We believe that the new Audit and Assurance Sandbox could similarly provide a valuable space for innovation, drawing on relevant aspects of the Lab's approach. With this in mind, we encourage the FRC to adopt a collaborative and transparent to the activities of the Sandbox, and would welcome more information on the scale of investment, timeline and milestone deliverables.

Promoting the use of technology throughout our policy areas through digital reporting and the implications for data and data governance

21. ICAEW welcomes the FRC's three-year plan referencing digital reporting and data, and the related ethical implications. However, we believe the FRC should provide stakeholders with

further detail of their activity as it relates to areas of emerging tech such as AI, and Blockchain. These are topics ICAEW will be looking at in 2023. On digital reporting, we would welcome clarity about how the FRC will measure their successful achievement of this objective.

Supporting FRC's objectives and activities through increased stakeholder engagement with impact and influence, including website improvements, connected and systematic development of publications, webinars, and podcasts, focused on collective impact

22. We strongly support increased stakeholder engagement and the investment implied in this area. It would be helpful to understand more about what is planned and the budget allocated for this area.

Supervision

Deliver a full programme of high-quality AQR inspections, CRR reviews and the FRC's statutory professional oversight functions and publish associated reporting, including thematic reviews

23. These appear to be 'business as usual' activities. The FRC have not given an indication that the AQR will be reformed or altered, and it would be welcome to see potential improvements in the AQR process being investigated in 2023, with indication of funding investment to achieve the objective of improved quality.
24. The plan does not refer to actuaries. As a regulator of both actuaries and auditors, FRC should prioritise ensuring that the regulatory expectations of auditors in auditing defined benefit pension figures in sponsor company financial statements are mutually consistent with the requirements of actuaries in providing the valuations.
25. We have heard from pension scheme trustees that increasing regulatory expectations of sponsor auditors are leading in some cases to trustees and scheme management making decisions with the aim of smoothing audit interactions, rather than decisions solely for the benefit of the scheme and its members. In some cases, the scheme actuaries are being asked to carry out additional work only as a result of the sponsor audit, rather than for the purposes of the scheme valuation or scheme audit.
26. Increased costs for auditors, or costs passed on to the sponsor entity in pursuance of achieving higher audit quality are in most cases understandable. However, where requests made as part of the statutory audit lead to increased costs for the scheme trustees, who are independent of the sponsor entity, and where the scheme also has its own independent audit, these are difficult to justify.
27. One issue highlighted to ICAEW in particular is around the allocation of assets between employers in the Local Government Pension Scheme, where regulatory expectations are for sponsor auditors to obtain information beyond that which the scheme, the employers or the actuaries hold.
28. ICAEW would be keen to facilitate a roundtable discussion with the FRC involving audit firms, pension funds and actuaries to understand the issues and determine an approach that is not onerous on pension scheme trustees.

Increase activities focused on improvements and innovation to support improved audit quality and resilience in the market, including implementation of the FRC Scalebox

29. During 2023 fresh insights should be provided into competition and choice in the audit market from the many PIE audits that come up for tender as the ten-year anniversary nears of the 2016 EU audit reforms. Gathering a robust evidence base about competition and choice is important, to ensure that policy actions are rooted in evidence which may rapidly evolve over this period. It is also important that actions on competition and choice are 'joined-up' as several FRC projects and papers affect this area and would benefit from being considered holistically.

Approval and registration of audit firms and responsible individuals who undertake PIE audit work

30. The FRC is prioritising the approval and registration of audit firms and responsible individuals who undertake PIE work. A substantial amount of work was completed in 2022, resulting in the FRC approving all firms that currently audit PIEs. We therefore expect the focus on the work in the three-year plan will be maintenance and monitoring of the firms' registrations, plus any new applications that may arise with a change in the PIE definition. Professional Supervisory Bodies, such as ICAEW and its Audit Registration Committee, have a role in this process. The FRC should provide further information on how it will be working with these stakeholders on delivering this priority.

Assess the effectiveness of the firms' implementation of new auditing and quality management standards

31. This is an important area of focus, given the new standards, and the need to make sure these are properly embedded within the firms monitored. We expect this assessment will be undertaken alongside the AQR inspections that the FRC delivers. However, it is not disclosed how much incremental investment is planned – we have highlighted this issue previously in paragraph 23.

Develop a supervisory approach for audit committees

32. We are responding to the FRC's consultation on a new audit committee standard and look forward to exploring this in more detail with the FRC.

Develop the supervisory oversight strategy for the professional bodies

33. In ICAEW's response to the ARGAs Funding Consultation, we stated the benefits of ARGAs being a proportionate regulator with a reasonable balance struck in terms of inspections between cost of compliance and the risk of undetected deficiencies. The same principles apply to the FRC's three-year plan.
34. The suggested increase in expenditure for Professional Oversight from £4.6m in 2022/23 to £6m in 2023/24 comes with no explanation in the consultation document as to why such a significant increase (over 30%) in funding is required. The published inspection report on the performance of the RSBs in 2022 does not indicate that there are any serious issues in the performance of any of the RSBs in their front-line regulatory tasks. In the absence of serious issues in performance, it is difficult to understand the rationale for the increased funding to recruit and deploy more Oversight staff. Increased staffing levels have already led to increased data requests and increased amounts of time being spent by Professional Oversight staff in reviewing in even greater detail work being carried out by RSB staff creating a real and increasing risk of there being a disproportionate number of overseers compared to front-line regulators.
35. The other consequence of the unexplained increase in the number of Oversight staff is that this is starting to create significant, additional work for staff at the RSBs in responding to data requests, increasing number of cases being reviewed, increased meetings etc. This increased workload will require the RSBs to make significant increases to audit registration fees to fund the recruitment of additional staff to respond to the Oversight team's requirements. Such increases are likely to cause more smaller audit registered firms, or firms not carrying out a significant amount of audit work, to consider giving up their registrations at a time when the FRC is concerned at the significant drop in audit registered firms over the past 5 years.
36. We would urge strongly that these worrying, perhaps unintended, consequences of increasing the number of staff in Oversight are taken into account when determining the appropriate ratio of oversight staff to the number of staff carrying out front-line regulatory work. Indeed, there are a number of factors which indicate that Oversight activities should be contracting, not increasing due to:

- a) The extension of PIE audits which will see more audits come under the jurisdiction of AQR and fewer high-risk, high-profile audits continue to be monitored by the RSBs
- b) The launch of the FRC's PIE audit registration scheme which will remove the review of AQR's reports on the largest firms from the RSBs' audit registration committees
- c) The continuing (and accelerating) reduction in the number of firms registered to carry out audit by the RSBs
- d) The continuing reduction in the number of audit registered firms which hold the registration but are not carrying out any statutory audit work

Develop the local audit system leader role and team in shadow form ahead of ARGA implementation

37. ICAEW believes that one of the FRC's priorities for the next three years should be playing its part in resolving the delays to local audit and financial reporting. Local audit is vital for providing transparency and accountability to taxpayers and for strengthening public financial management.
38. We welcome that the plan sets out the FRC's intention to develop the local audit system leader role in shadow form and has allocated a budget of £2.2m for this directorate in 2023/24.
39. However, we believe that FRC's strategic objectives for the next three years should include a specific objective relating to local audit. In May 2022, the government announced plans for ARGA to have an overarching statutory objective relating to local audit. For the FRC to carry out the role effectively in shadow form and fully prepare for its transition to ARGA, we believe it would be helpful if the FRC had a similar specific overarching objective relating to local audit.
40. We also believe the plan would benefit from more detail about how FRC intends to undertake its role as shadow system leader. ICAEW believes that a 'whole-system' approach is required to tackle the crisis in local audit, including improvements to local authority financial reporting and action to make the local audit profession more attractive.
41. ICAEW recommends that the plan sets out how the local audit directorate of the FRC will interact with the FRC's regulatory function. It is important that a balance is struck between close alignment between the different FRC functions and sufficient separation that auditors feel confident raising issues with the system leader that are currently raised through the National Audit Office's technical network. One of the immediate priorities for the shadow system leader should be to help resolve the disconnect between what audit regulators perceive as the priority areas for local audit and the perceptions of local authority or NHS finance teams. A key role for the FRC as shadow system leader will be to determine what statutory powers ARGA requires to be an effective system leader for local audit and ensure those are reflected in the legislation. ICAEW believes that in order to achieve the planned objective of ensuring local audit operates effectively, the system leader needs statutory powers to improve local authority financial reporting.
42. As we stated in our [response](#) to the Department for Levelling Up, Housing and Communities (DLUHC)'s [consultation](#) on the local audit framework, we believe that the system leader should be funded by DLUHC. We are pleased to see in the plan that the FRC's local audit directorate will be funded directly through grant-in-aid.

Reporting on implementation of operational separation

43. The strategy and plan document provides little detail about activities planned to support operational separation and what reporting the FRC will be doing on this. Given its significance it is clear that this should be a priority but more information on the nature, scale and timing of activities would be helpful.

Develop market monitoring function

44. The plan refers to this as a new team the FRC will be setting up, which we assume will be to look at resilience and associated issues. This is also mentioned in the 'corporate services' section, alongside references to data analytics. It is important that this complements and coordinates with the existing supervision structure

Deliver projects on developing AQR and Improving the Quality of Auditor Education and Training

45. The FRC will be taking steps over the next three years to reform and restore trust in the UK's audit and corporate governance regimes. It has rightly highlighted the delivery of projects on developing AQR and improving the quality of auditor education and training as priorities. ICAEW strongly encourages the FRC to maintain a collaborative approach with the professional bodies, to ensure no inefficiencies and duplication with projects they are in the process of developing – particularly on developments with professional qualifications, auditor education, training and continuing professional development.

Enforcement

Fair, robust, and timely case closures, or conclusion through focus of investigations, prioritisation, training, and recruitment

46. We agree the FRC should strive to achieve this objective, and would be keen to see greater transparency from the FRC regarding their approach to enforcement as all future cases will likely fall within the Audit Enforcement Procedure (AEP). Given the infrequency of disputed issues coming before tribunals under the AEP compared to the Accountancy Scheme, we have been 'surprised' to see the FRC's Enforcement Costs increasing given how weighted time spent and costs are to the tribunal end of disciplinary proceedings. The FRC should engage further with stakeholders over the medium-to-long term on how its investigation costs and resource requirements change as it takes forward cases under the AEP.

Upskilling and training to respond to changes in AEP from January 2022 and to intended changes to procedural published guidance

47. The FRC makes reference to 'upskilling' its staff as part of its priorities of responding to changes in AEP and procedural published guidance, and to enable full implementation of future powers arising from regulatory reform. However, it has not made clear what skills are required by its staff to deliver these priorities. To ensure stakeholders can better understand the FRC's plans, and where appropriate support the FRC in ensuring its teams have the skills to deliver its new responsibilities, the FRC should provide further information on how this will be delivered.

Collaboration with the Department for Business, Energy, and Industrial Strategy (BEIS) on planned legislative change to reach the best achievable outcomes as they pertain to enforcement and the FRC's stated purpose and objectives

48. We agree this is an important area of focus, but it would be helpful to have more information about the nature and phasing of activities to support our own planning and to ensure stakeholders can meet regulatory requirements.

Upskilling to enable full implementation of future powers arising from proposed regulatory reform in 2024 onwards

49. See comments above on upskilling.

Publication of the Annual Enforcement Review, delivering transparency and driving improved behaviours through messaging case outcomes

50. It is not clear from this objective what incremental activity is planned for 2023.

ABOUT ICAEW

The response of 27 January 2023 has been prepared by ICAEW's Reputation & Influence Department.

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.

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.

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.