



PROPOSED INTERNAL GOVERNANCE RULES

Issued 18 January 2019

ICAEW welcomes the opportunity to comment on the Proposed Internal Governance Rules (IGRs) issued by the Legal Services Board (LSB) in October 2018.

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 152,000 chartered accountant members in over 160 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.

This response dated 21 January 2019 reflects the views of ICAEW as a regulator. ICAEW Professional Standards is the regulatory arm of ICAEW. Over the past 25 years, ICAEW has undertaken responsibilities as a regulator under statute in the areas of audit, insolvency, investment business and most recently Legal Services. In discharging our regulatory duties it is subject to oversight by the FRC's Conduct Committee, the Irish Auditing and Accounting Supervisory Authority (IAASA), the Insolvency Service, the FCA and the Legal Services Board.

Amongst ICAEW's regulatory responsibilities;

- It is the largest Recognised Supervisory Body (RSB) and Recognised Qualifying Body (RQB) for statutory audit in the UK, registering approximately 2,800 firms and 7,500 responsible individuals under the Companies Act 2006.
- It is the largest Prescribed Accountancy Body (PAB) and Recognised Accountancy Body (RAB) for statutory audit in Ireland, registering approximately 2,800 firms and 7,500 responsible individuals under the Republic of Ireland's Companies Act 2014.
- It is the largest single insolvency regulator in the UK licensing some 800 of the UK's 1,700 insolvency practitioners as a Recognised Professional Body (RPB).
- It is a Designated Professional Body (DPB) under the Financial Services and Markets Act 2000 (and previously a Recognised Professional Body under the Financial Services Act 1986) currently licensing approximately 2,200 firms to undertake exempt regulated activities under that Act.
- [It is a Supervisory Body recognised by OPBAS for the purposes of the Money Laundering Regulations 2007 dealing with approximately 13,000 member firms.]

It is designated an Approved Regulator and Licensing Authority for probate under the Legal Services Act 2007 (the Act) currently accrediting approximately 300 firms to undertake this reserved legal activity.

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INTRODUCTION

GENERAL

1. ICAEW welcomes the LSB's initiative to improve the existing IGRs. While at the time of responding to this consultation, ICAEW is still unaware of the outcome of its application for judicial review of the Lord Chancellor's decision on ICAEW's application to broaden its regulatory role, it is fair to say that ICAEW has suffered more than any other legal service regulator in recent times from the belief or perception of others, including the Lord Chancellor, that compliance with the existing IGRs is not of itself sufficient assurance in relation to a regulator's governance arrangements.
2. ICAEW has always believed in the importance of the independence of its regulatory function; not only from a statutory perspective where it is authorised by statute to act as a regulator of a number of regulated services but also in the conduct of its members in the unregulated services they provide to the public including accountancy and tax services through the imposition of obligations and disciplinary rules through the membership contract. This approach has been reinforced in recent years through a restructuring of the governance around ICAEW's regulatory functions as a result of implementing the recommendations made in an independent review.
3. ICAEW is proud of its record so far since being authorised to regulate the provision of probate services in 2014. As the LSB knows, over 300 ICAEW firms have chosen to obtain probate licences to start offering probate services to their clients. This is considered to have been an important development for consumers as it has provided them with the opportunity to obtain seamless assistance at a time of great sensitivity and vulnerability from one regulated professional who can deal with the obtaining of probate and then move seamlessly into the work involved in estate administration. It was pleasing to see that LSB's own research¹ noted that consumers are keen to obtain advice from their accountants on key issues concerning them.
4. ICAEW believes that, in light of all of the regulatory objectives in section 30 of the Act, it is important that ICAEW and other professional accountancy bodies remain part of the regulatory framework for legal services. This is because many of the firms regulated by us for probate are relatively small and many would give up this line of work rather than take on the additional compliance costs of dealing with two regulators if ICAEW were to withdraw from its regulatory role as a result of any difficulties in complying with the final version of the new rules. For the reasons set out below, ICAEW does not believe that this will be the case. However, ICAEW does have concerns about the overall approach which has been taken in producing the Rules and Guidance and in the lack of clarity in some of the key terminology used.

APPROACH

OUTCOMES-FOCUSED / PRINCIPLES-BASED?

5. ICAEW is disappointed at the decision taken by the LSB to produce prescriptive rules, and even more prescriptive guidance, which seems to run directly contrary to the outcome of the initial consultation on changes to the IGRs and the expressed intent for the LSB to ensure that the new Rules would be principles-based and outcomes-focused. The clear focus would appear to be on the 'inputs' to the governance arrangements of the legal service regulators and on prescribed ways of ensuring the independence of their governance arrangements rather than defining key principles and allowing the regulators to adjust their existing arrangements in whichever way works most practically and efficiently for them in order to be able to demonstrate to the LSB that it complies fully with that principle.

¹ The Legal Needs of Small Businesses 2013 – 2017 <https://research.legalservicesboard.org.uk/wp-content/media/FINAL-Summary-Small-Business-FEB-18.pdf>

6. In ICAEW's dealings with its other oversight bodies, ICAEW has found that an 'outcomes-based' approach enables the oversight body to direct the bodies in the preferred direction of travel, but gives the regulatory body flexibility in how the ultimate outcomes are achieved. Good examples of outcomes-focused / principles-based oversight can be seen in the operation of IAASA and OPBAS, two of ICAEW's other oversight regulators. Those oversight regulators recognised that their authorised regulators all had vastly different structures which had been developed over time and in accordance with the wishes of those bodies' other oversight regulators and that a focus on inputs and the imposition of prescribed rules could potentially render as suddenly inadequate, a structure or mode of operation in the regulatory function which had operated successfully and without concern from other oversight regulators for many years.
7. ICAEW believes that the level of prescription does not just cause problems in compliance for it but that difficulties will be caused to other regulators too. For this reason, ICAEW would request the LSB to re-consider the overall approach and whether it should re-formulate some of the Rules and Guidance into principles with the onus on the regulators to demonstrate that they comply. Another issue with the prescriptive approach is that some of the key terms in the Rules and Guidance, for example, "regulatory body" will mean different things to different bodies and, depending on what part of an AR in a unitary body is determined to be the "regulatory body" will depend on the degree to which compliance with the Rules will be possible or desirable.
8. The LSB itself has issued some practical required outcomes in some of its section 55 and section 162 reporting and the diversity obligations, where ICAEW have approached the objectives from a different expected angle yet satisfied the LSB that it had achieved its key objectives. The more detailed approach applied to the IGRs is therefore slightly at odds with the LSB's previous regulatory stance, and in our view has been to their detriment as an effective practical document.
9. There is also the management of reputational risk to consider; under the framework to date the risk if anything goes wrong lies with the relevant AR, and the Ministry of Justice (MoJ) and the LSB can as supervisors indicate where key outcomes have not been achieved by the body and censure it accordingly. If the supervisory rules are over prescriptive, there is a danger that the failing would be seen as lying with the LSB and the MoJ as it could be interpreted as indicating weaknesses in their guidance rather than the performance of an AR. A less prescriptive framework allows the LSB to determine direction of travel but gives the ARs options in approach, allows scope for innovation and keeps the reputational risk away from government.

COMPLIANCE WITH THE ACT?

10. ICAEW is concerned that the requirements imposed by many of the Rules do not reflect either the requirements of Section 30 of the Act or the clear intention of Parliament. Section 30 states that [emphasis added]:

*"The Board must make rules ("internal governance rules") setting out requirements to be met by approved regulators for the purpose of ensuring (a) that the exercise of an approved regulator's regulatory functions is not **prejudiced** by its representative functions, and (b) that decisions relating to the exercise of an approved regulator's regulatory functions are so far as reasonably practicable taken independently from decisions relating to the exercise of its representative functions."*
11. The section does not include any prohibition against "influence" from the representative functions in a unitary body. Despite this, Rules 1, 4, 8 and 10 all contain a prohibition against influence. A particular concern is that "influence" is the focus of Rule 1 which is clearly the most important Rule as it contains the overarching duty. In contrast, and inconsistently with the rest of the Rules but consistent with section 30, Rule 12 refers to "prejudice".

12. The importance of the distinction between “prejudice” and “influence” and the degree of consideration of this specific issue at the time the Act was introduced can be seen by the fact that it was the focus of two debates in Parliament on the wording of this section of the Act when the original choice of “prejudice” was challenged with a suggestion that the Government change it to “influence”. In the Public Bill Committee’s examination of the Bill for this Act the Parliamentary Under-Secretary of State for Justice (Bridget Prentice) dealt with this point specifically²:

“A lot of consideration has gone into the use of the word ‘prejudiced’ in the clause. It has been argued that it would not be unusual for representative bodies to seek to influence regulatory decisions, if it is in the interests of their members to do so. As the approved regulator is the body recognised in the Bill as responsible for both representative and regulatory functions, I would argue that it should accept certain responsibilities as part of that role. It might be reasonable for the representative arm to try to influence regulatory decisions, but it is important that the board is able to take appropriate action where it considers that the approved regulator is allowing representational interests to prejudice the exercise of regulatory functions. It is important to ensure that the board is able to act where, for example, the actions of the representative side discredit the regulatory arm, resulting in damage to consumer confidence. Clause 29(2) is necessarily and deliberately wide in definition to ensure that the board is not prevented from taking such appropriate action. Therefore the use of the word ‘prejudiced’ is correct in the context. ...I understand that these are often very fine definitions, but ‘prejudiced’ is more appropriate than ‘improperly constrained or influenced’, because the latter wording would narrow the definition just a little bit too much.”

13. During an earlier debate in the House of Lords on 22 January 2007 the use of the test of “prejudice” was also discussed.³ During this debate the then Under-Secretary of State for Justice (Baroness Ashton of Upholland) said the following:

“The word “prejudiced” is an appropriate word. We seek to ensure that the regulatory arm is aware of the influence placed on it; in other words, the representative arm will not necessarily do anything other than quite reasonably and quite rightly lobby on particular issues and do things that are designed to take forward the representative functions. I have no difficulty with that at all.

The issue for me is how the regulatory arm knows that it has been influenced. I suggest that the onus is on those who are being influenced to know that they have been influenced. We have chosen that word because it is not about improper behaviour at all; it is about asking, “Do you know that you have been influenced and are you aware of the fact that, with two arms, one is operating on the other?” that is why “prejudiced” is used; it does not suggest that something untoward has happened.

Members of the Committee will recognise that on occasions one is lobbied by people one knows well on issues with which one is familiar. When looking at regulation, you have to be clear that you know you have been influenced and can justify its nature. That is the way I have approached the matter.”

14. ICAEW is concerned from its reading of section 30 that Rules 1, 4, 8 and 10, as presently drafted, would be ultra vires of the Act. It is also concerned that the LSB should be seen to be introducing prohibitions which are clearly contrary to the intentions of Parliament at the time the Act was introduced. ICAEW believes that careful consideration should be given to the final wording of Rules 1, 4, 8 and 10 before they are introduced.

² Hansard, Public Bill Committee, 6th Sitting, col. 222 19 June 2017

³ <https://publications.parliament.uk/pa/ld200607/ldhansrd/text/70122-0013.htm>

15. Aside from the legal issues thrown up by the prohibitions on “influence”, ICAEW are disappointed that the LSB considers that any “influence” from the representative functions should be avoided. The measured and controlled interaction which aids ICAEW in the performance of its regulatory function could be significantly compromised by following the Rules as they stand. As was recognised by the Ministers in the quotes above, influence, by way of lobbying or otherwise, can have a beneficial impact. Indeed, the imposition of regulations and rules without properly taking into account any practical issues which would be thrown up, or without first understanding possible unintended consequences for those working in practice, is neither efficient nor the way to introduce effective regulation.
16. By preventing the regulatory body from interacting with the representative functions (which, for ICAEW, include a well-respected Technical Strategy Department), the Rules will deny the regulatory body from access to technical expertise and know-how which could result in poorer quality decision-making. It will also increase the costs of operation of the regulatory body as it would either have to employ more in-house experts or pay for the expertise from a third party rather than tap into the expertise present within the technical departments of representative functions. The success ICAEW has had in meeting the LSB’s objectives on, for example, diversity and CMA recommendations has been through engaging with relevant experts within the representative functions. Indeed, the LSB’s Diversity outcome number 3 requires the regulatory body, among other things, to “*collaborate with... the representative body*” and the new Rules would seem to prevent such interaction and collaboration.
17. A major difficulty with the current IGRs has been that the legal status to act as a regulator has been granted not directly to the regulatory body but to the whole professional body where the applicant is a unitary body. In the case of ICAEW, the legal status of regulator for probate has been conferred on ICAEW which is governed by ICAEW Council and where, in accordance with the arrangements set out in ICAEW’s application, the responsibility for the discharge of the regulatory functions was immediately delegated to the Probate Committee supported by ICAEW’s Professional Standards Department. However, the responsibility and legal risk has remained with ICAEW’s Council which, operating through the ICAEW Board, has the responsibility to ensure that regulatory tasks are being carried out in accordance with the legislation. It does not, therefore, appear to be practicable or logical for the new Rules to limit the degree of interaction.

COMPLIANCE WITH THE REGULATORY OBJECTIVES?

18. While ICAEW does not disagree with the focus in Rule 1 on the importance of the independence of the regulatory functions, and notes the reference to the eight regulatory objectives in section 28 of the Act, it is concerned that, the Rules as a whole appear to strive for independence above everything else, including the objectives and the application of the five Hampton Principles. For example, the introduction of prescriptive rules impacting the governance structures of bodies whose governance structures have been deemed by other statutory oversight regulators as being fit for the regulation of (arguably) riskier regulated services (in ICAEW’s case, audit, insolvency and investment business) could potentially risk a diminution in competition if a regulator were to give up its legal services regulator role and those it regulates were to choose to give up rather than deal with the additional compliance cost of dealing with two regulators.

REMOVAL OF DISTINCTION BETWEEN AR AND AAR

19. ICAEW welcomes the decision to remove the two tier system presented by the AR and AAR classifications. ICAEW believes that this was an artificial and unnecessary complication in the existing IGRs and that, with one tweak (converting our Probate Committee to lay majority rather than lay parity where the lay Chair has a casting vote) our governance complied with the requirements for both an AR and an AAR. ICAEW has been concerned to note that some media reporting has sought to portray the categorisation of the professional accountancy bodies as AARs to be providing bodies like ICAEW with an advantage and allowing it to have more relaxed governance arrangements. The abolition of the distinction will remove this perception and ICAEW welcomes this.

LACK OF CLARITY RE NEW TERMINOLOGY

20. ICAEW is also concerned at the lack of clarity around the new terminology used in the Rules and Guidance. A consequence of the decision to produce prescriptive rules is that the Rules seek to impose obligations on various parties, particularly the “regulatory body”.
21. The lack of clarity as to which part of ICAEW would be deemed to be the “regulatory body” in the application of the Rules has led to various meetings during the consultation period between directors and senior managers in ICAEW’s Professional Standards Department and LSB staff to gain a greater understanding as to how the Rules would apply in practice to ICAEW, in particular what would be considered to be the ‘regulatory body’ in ICAEW’s current structure. ICAEW has concluded from its analysis of the Rules and from the discussions at the recent meetings that the ‘regulatory body’ would be regarded as PSD and the Probate Committee (as the regulatory board for legal services) collectively.
22. While greater clarity in the Rules would have been helpful, the difficulty in applying in identifying what is a regulator’s ‘regulatory body’ will not be a problem unique to ICAEW and this is the unfortunate consequence of producing prescriptive rules rather than providing a set of principles and expected outputs which the bodies would have to demonstrate however they were organised
23. Another area where ICAEW would like to see greater clarity in terminology is in relation to what is meant by “involved in a material way” in Rule 5 particularly in light of the Guidance; *“there will be cases in which the materiality of the role is clear, such as a member of a decision-making committee or an individual elected to represent a particular group of regulated persons”*. It is not clear to ICAEW whether the fact that the PSD Executive Director is a member of the main ICAEW board, like all other Executive Directors with operational responsibility for the divisions of ICAEW, would infringe this Rule. The PSD Executive Director is clearly involved in a material way in the operations of PSD and, therefore, this Rule may be breached if the ICAEW board were to be regarded as a “decision-making committee” for the representative functions rather than recognised as the board of the unitary body and if the PSD Executive Director’s role were to be considered “material”. At the most recent meeting with LSB staff, this particular concern was raised and a distinction appeared to be drawn by LSB staff between merely sitting on a board of a unitary body and acting in a material way to promote the interests of the representative functions which has provided some assurance.
24. While ICAEW agrees that a Rule preventing a person who is materially involved in the representative functions from being a member of the governing body of the regulatory body, would enhance the independence of the regulatory functions (and ICAEW’s own internal governance rules prevent this), it would appear to be contrary to the interests of the regulatory body to be deprived of the insight provided by the current arrangements through the PSD Executive Director being provided with information regarding future plans of the institute and having the ability at an early, formative stage to indicate potential concerns about the way in which any future plans may undermine or impact the regulatory body and its functions. If this was intended to be prohibited, ICAEW would request the LSB to re-consider this and, if it was not intended to be prohibited, the LSB is asked to provide clearer guidance with the final Rules.

FINANCIAL INDEPENDENCE

25. ICAEW is surprised to see that the new Rules are not as robust on the sensitive issue relating to the independence of the funding for the regulatory functions. ICAEW understands from the attendance of senior PSD staff at meetings of the various regulators that this is a significant source of friction and undue influence in other bodies where all income is received by the Approved Regulator and has to be allocated separately to the regulatory functions.

26. One of the central tenets of ICAEW's belief that it has independence around its regulatory functions is that PSD's operations are not funded in any way by either the membership or the practising certificate fees which fund the representative functions. PSD's operations are funded by regulatory fees charged to those members and firms who are authorised to carry out regulated services in addition to fines and costs from the disciplinary scheme. The ICAEW Regulatory Board sets the level of regulatory fees for the following year after reviewing the budget drawn up by the PSD Finance Director to ensure that there is sufficient funding to carry out all functions. In the same way, for ICAEW's regulatory functions in relation to probate, the Probate Committee sets the probate licence fees charged to firms after reviewing budgets for the cost of the regulatory functions as they relate to probate. There is, therefore, no question of disputes in relation to the allocation of funding where leverage could be used to influence matters.
27. It seems to ICAEW that, if the LSB was looking to strive for as much independence as was permissible under the Act between representative and regulatory functions, one of the key issues would be the establishment of an independent source of funding and this is not included within the Rules despite the fact that this might increase the independence of operation much more than some of the other Rules which are proposed. Conversely, no recognition appears to be given to the fact that some regulators can demonstrate financial independence as part of their own arrangements to show independence in the conduct of their regulatory functions. While Rule 1 and the saving provisions in Rule 16 seem to suggest some form of flexibility, ICAEW considers that the Rules should expressly make provision for the LSB to take into account arrangements which are in place at one or more regulators which go above and beyond what the Rules are requiring when deciding whether to provide a waiver to a regulator which is unable to comply with the provisions or one or more of the other Rules. Alternatively provision should be made to ensure that such factors can be taken into account and given weight in any future assessment by the LSB of those regulators' compliance with the Rules.

CONCLUSION

28. As a result of the concerns expressed above on the approach which has been taken, ICAEW believes that a less detailed and more flexible approach should be taken in the finalisation of the Rules and a re-consideration as to whether it would be easier and more effective to formulate principles with attendant guidance and put the onus on the regulators to demonstrate that they comply with the principle howsoever they are structured and operate. The final document should continue to remind the bodies of the "what" but not get over-involved in the "how".
29. In the paragraphs below ICAEW set out their overview response to the questions and then address them at an individual level.

RESPONSES TO SPECIFIC QUESTIONS

Q1: Do you agree that the proposed rules would enhance the independence of regulatory functions and improve clarity leading to fewer disputes and more straightforward compliance/enforcement? If not why not?

30. As explained in our introductory comments ICAEW believe that the framework is a sensible one. However the lack of definitions in certain areas creates some confusion and doubt. In addition some tendency to over engage in detail results in the outcomes becoming outputs and compromising the statutory objectives and Hampton principles. With tighter drafting and definitions it is believe the IGRs will meet the objectives sought by the LSB.

31. It is noted in paragraph 25 above that the principal source of disputes appears to be the funding of the regulatory body; given the opaque nature of rule 10 ICAEW are not sure this rule cuts to the chase and that therefore the aim of fewer disputes may not be readily achieved.
32. Set out below the individual observations ICAEW have with respect to each of the rules.

Rule 1 – Overarching Duty

33. ICAEW is of the opinion that the wording of this rule will cause uncertainty. Paragraphs 21 - 22 of the consultation document states: “*The overarching duty reflects section 30 of the Act and sets the context for the rest of the IGR.....Whilst the current IGR simply repeat the wording of section 30, the rule sets out the requirements for achieving the outcomes specified in section 30*”
34. Rule 1 does not however accurately reflect the requirements of section 30. As has been noted in the opening paragraphs above, the intent of Parliament and the act was to apply a test that was less rigid and allow a carefully guarded degree of interaction. The tests accordingly should be focused on the undesirable elements of influence (**eg**, prejudicial) rather than the whole of influence. Otherwise the structure of the rule inhibits the effectiveness of other regulatory activity.

Rule 2 – Duty to delegate

Rule 3 – Provision of assurance

35. As the term “Regulatory Body” has not been defined in these proposed rules, for the purposes of responding to this consultation, ICAEW has interpreted it as having the same definition as that used in the current IGRs ie, a body (whether a separate legal entity or not) without any representative functions which must have a regulatory board.
36. ICAEW does however feel that it is important to define the term “Regulatory Body” for the reasons set out in paragraphs below (in response to rule 4) and therefore recommends that the LSB adds this definition to these proposed rules.

Rule 4 – Regulatory autonomy

37. As mentioned above, as the term “Regulatory Body” is central to these rules it needs to be defined. Furthermore, the rules do not appear to distinguish between the roles of the executive and regulatory board of the Regulatory Body and compliance with the rules appears to be assured provided the Regulatory Body carries out its regulatory functions independently without interference or undue influence from the Approved Regulator
38. Whilst ICAEW will have no difficulty in complying with this rule, as its Regulatory Body independently determines the most appropriate and effective way of discharging its functions to meet the regulatory objectives in accordance with the better regulation principles; it is somewhat surprising that the rules do not ensure more independence of the regulatory board within a Regulatory Body from the body’s executive.
39. By way of explanation, whilst ICAEW’s Regulatory Body’s executive determines its own structure and the most appropriate governance arrangements to put in place to ensure independence from its representative arm (Approved Regulator), it has also ensured that its regulatory board is independently appointed (independent of the Regulatory Body as well as the Approved Regulator) and operates independently, determining issues such as governance, priorities, strategy and regulatory arrangements. It is our opinion that such matters should not be for the executive to determine but the independently appointed regulatory board.

40. As the wording of and/or guidance for Rule 4 does not distinguish between the roles of the executive and the regulatory board in a Regulatory Body it is felt this rule is currently unclear which could lead to uncertainty. This point is illustrated below in relation to comments on the guidance to this rule.

Rule 5 – Prohibition on dual roles

41. ICAEW agrees that a rule preventing a person who is materially involved in representative functions from being a member of the board, council or committee which makes decisions about how to exercise regulatory functions would enhance the independence of regulatory functions (Rule 5(2)).
42. However this rule and its guidance is unclear as to whether a person who is materially involved in regulatory functions is considered to be materially involved in representative functions if that person sits on the Board of an Approved Regulator in order to represent the Regulatory Body on that board (Rule 5(1))

Rule 6 – Individual Conduct

43. This is standard procedure for any regulatory body and therefore no further comment is required

Rule 7 – Governance lay majority

44. Whilst the value of lay input is recognised especially for the purposes of external perception, it is equally important that those regulated have confidence in the competence as well as independence of any regulatory body that directs their activity. As was noted in ICAEW's January 2018 representation, the GMC and the Dental Council in 2012 indicated that lay parity achieved the necessary balances for both objectives.
45. It has been noted earlier the difficulties around what constitutes the regulatory body and where the key functions are exercised. The view of ICAEW having taken account of the observations of the LSB, is that the Probate Committee is the key functional area requiring the lay majority and a move to a lay majority can be done should it be necessary.
46. However the IRB which oversees the regulatory function overall, also oversees audit, insolvency and other reserved activity where the oversight bodies are satisfied with existing arrangements. This board is formed of a parity of lay and non-lay members.
47. In practice the lay members (being paid whereas members are not) are more likely to be present and therefore lay majorities apply most of the time. In addition the lay chair of the Probate Committee has a casting vote which is tantamount to a lay majority. If the LSB remains insistent however ICAEW can apply this rule as drafted to the Probate Committee with no significant additional cost

Rule 8 - Appointments and terminations

48. No specific comment on the rule itself

Rule 9 – Regulatory resources

Rule 10 – Regulatory body budget

49. It has been noted above the light touch element of rules 9 and 10 as they pertain to the funding model of the regulatory body. In ICAEW's view this rule does not address the fundamental problems that lie at the heart of the current tensions between the representative and regulatory arms within a unitary body. As a consequence it is believed this weakens attainment of the objectives of the new IGRs as a whole.

Rule 11 – Shared services

50. As ICAEW operates a ‘self-financing’ model it is free to assess the services and resources it needs and to consider whether the cost of those services is appropriate. As mentioned above, resource considerations, free from outside influence and with particular emphasis placed on meeting statutory and regulatory objectives and requirements, are carefully reviewed and calculated, and form a key cost component of the ‘self-financing’ model to achieve an appropriate level of annual registration fee.
51. ICAEW’s Regulatory Body therefore only shares services where this is appropriate, necessary and efficient, creating synergies and a cost effective delivery model through shared resource, functions and technology such as those related to IT, property etc. This does not undermine or infringe the separation of functions or impede our Regulatory Body’s ability to discharge its regulatory functions. Where services are shared there is no difference to the basis as provided to the Regulatory Body or to the Approved Regulator.
52. ICAEW believes that such a ‘self-financing’ model is an important factor in ensuring there is no interference with or undue influence leading to prejudice on the exercise of regulatory functions by Approved Regulators with a residual role. ICAEW are therefore of the opinion that the proposed IGRs should encourage such a model for other unitary regulators as it would enhance regulatory independence and reduce the risk of disputes.

Rule 12 – Communication by persons involved in regulation

53. ICAEW already has such arrangements in place and therefore has no comment to make on this proposed rule save for the comment made in paragraph x (Rule X) relating to the notification requirements in Rule 12(2)

Rule 13 – Candour about compliance

54. ICAEW has no issues with this rule and therefore no comment to make.

Rule 14 – Disputes and referrals for clarification

55. ICAEW has no issues with this rule and therefore no comment to make.

Rule 15 – Guidance

56. In the issuance of guidance care is required in the wording that it itself does not become prescriptive. The use for example of the words “must” and “should” can be equivalent to law, and “due regard” has an interesting legal series of interpretations. The rules themselves are of course law by virtue of the LSB’s powers under section 30. However provided that some of the wording is tightened up and the guidance is not prescriptive ICAEW do not have difficulty with rule 15.

Rule 16 – Saving provisions

57. This is a sensible provision that facilitates the recognition of regulatory process that achieves the overarching objectives whilst in itself not meeting the specific IGR rule. However, this should be only used by exception rather than on a regular basis. This is why the accurate and high level outcomes expressed in the rules themselves should not be too prescriptive and the ARs and the LSB have the ability to recognise effective alternative regulatory models.

Rule 17 – Exemptions

58. ICAEW has no comment to make on this rule.

Q2: Does the proposed guidance provide sufficient detail to help you to interpret and comply with the proposed IGR? Please provide specific comments on any areas of the guidance where further information would improve clarity.

59. In the main the guidance to the rules provides sufficient detail to interpret the rules and ascertain whether ICAEW is able to comply with them. The guidance to some rules does however lack clarity in specific areas and is also overly prescriptive in others possibly leading to disproportionate cost inefficiency.
60. For example, as outlined above, with regard to the guidance to Rule 4 - regulatory autonomy, this requires clarity regarding the definition of a "Regulatory Body" and the roles and powers of the executive and regulatory board of this body; and with regard to Rule 6 – prohibition on dual roles, the guidance on "material involvement" needs to be clarified to ensure executive representation of a Regulatory Body on an Approved Regulator's Board is not prohibited.
61. Finally, the guidance to rule 11 – share services is overly prescriptive and should be more outcomes focused. The detailed examples in the guidance appear to exacerbate this.
62. Some of the comments made above on the rules themselves also have covered the guidance. However set out below are additional observations held with respect to the guidance for each certain of the rules where applicable.

Rule 3 – Provision of assurance

63. The guidance provides sufficient detail to interpret these rules and ascertain whether ICAEW can comply.

Rule 4 – Regulatory autonomy

64. The guidance on this Rule 4 is also unclear with regard to the definition of a Regulatory Body. The wording of the guidance under the sub-heading *Governance & Structure* states [emphasis added]:

*"Determining its own governance and structure, essentially requires that the **regulatory body** has control over its constitution including:*

- *Its hierarchy,*
- ***Its decision-making processes,***
- *the make-up of its board(s) and committee(s),*
- *election of members,*
- ***the division of power between those bodies and its executive***
- *its conduct rules, and*
- *terms of reference for its bodies*

65. It is unclear where the control lies. For example who decides on the division of power between the regulatory board and the executive and on the processes for decision-making? ICAEW is of the opinion that the guidance needs to be much clearer on these issues.

Rule 5 – Prohibition on dual roles

66. The guidance on 'material involvement' states: *"There will be cases in which the materiality of the role is clear, such as a member of a decision-making committee or an individual elected to represent a particular group of regulated person."*
67. ICAEW is of the opinion that it is good regulation to have executive representation of the Regulatory Body on its Approved Regulator's Board as such an executive is more able to assess whether a decision, plan or other arrangement being considered by such a Board is likely to undermine the discharge of regulatory functions and/or prejudice the independence or effectiveness of regulatory functions. Such representation assists with compliance of section 28 and rules 2(3) and 12(2).

68. Membership of an Approved Regulator's Board by an executive of the Regulatory Board should not therefore be considered 'material involvement' in representative functions but the guidance to this rule does not make this clear. The guidance therefore needs amending to add this clarity

Rule 8 - Appointments and terminations

69. For the guidance on this rule ICAEW repeats its concerns about the definition of a Regulatory Body and the need for the guidance to make clear that appointments and terminations should not just be made independently from the Approved Regulator with a residual role but should also be made independently from the executive of the Regulatory Body as outlined in paragraph 64 for rule 4 above. .

Rule 11 – Shared services

70. ICAEW is of the opinion that the guidance on this rule is overly prescriptive and should be more outcomes focused. Giving detailed examples appears to exacerbate this. Such over-prescription does not take into account the different structures of current legal regulators.

Q3: Is there any reason that your organisation would not be able to comply with the proposed IGR within six months? Please explain your reasons.

71. ICAEW currently sees no difficulties in complying with these rules provided the definition of the Regulatory Body is as assumed in this response (see paragraphs 37 - 40). Our regulatory structure and procedures would already comply with the majority of these rules and, where they don't, compliance should be relatively straightforward.
72. With regard to the time required to effect implementation this should be straight forward with the exception of rule 11 – shared services. It is difficult, at this stage, to judge how long a review of shared services will take, particularly as the guidance on this rule is so prescriptive in its requirements. It is noted below that infra-structure changes could take between 18 months to two years to implement. As it is also cost burdensome for a number of reasons and affecting our other areas of regulation it is something that would need a careful application.
73. Some of the comments made above on the rules themselves also have covered implementation issues. However set out below are additional observations with respect to the implementation for each certain of the rules where applicable.

Rule 3 – Provision of assurance

74. ICAEW as an Approved Regulator already delegates its regulatory functions to its regulatory body and only retains a residual role as an Approved Regulator requiring only assurance of compliance with the rules and the Act. Furthermore, mechanisms are already in place within ICAEW's regulatory structure to ensure that ICAEW's Regulatory Body is able to provide sufficient information to ICAEW as an Approved Regulator to give this assurance. Implementation of this rule is therefore not an issue as ICAEW is already compliant

Rule 9 – Regulatory resources

Rule 10 – Regulatory body budget

75. ICAEW's Regulatory Body independently formulates its own strategy, operational plan and resulting budget. The principles of its self-financing model includes income generation and compensation schemes funded largely by levy. Due regard is given to oversight, strategic and market priorities when formulating its operational plan and supporting budget. Resource considerations, free from outside influence and with particular emphasis placed on meeting statutory and regulatory objectives and requirements, are carefully reviewed and calculated, and form a key cost component of the 'self-financing' model to achieve an appropriate level of annual registration fee.

76. Any increase in annual registration fees is discussed and agreed with the Regulatory Board, with the LSB and finally approved by their Chief Executive. Under the transparency initiative, the financial results (in respect of the probate services) are published on the ICAEW.com website each year.
77. The 'self-financing model' of ICAEW's Regulatory Body therefore ensures that there is no interference or undue influence leading to prejudice from the Approve Regulator.
78. However, as the Approved Regulator with a residual role is entitled to assurance of compliance with the Act, the Regulatory Body's budget and resource plans are reviewed by the Approved Regulator.
79. ICAEW therefore in itself has no operational issues with this rule.

Rule 11 – Shared services

80. Concerns on the implementation challenges of this rule are set out in the paragraphs below in response to question 4.

Q4: Beyond the usual resources allocated to compliance with the IGR what, if any, additional resource do you anticipate you will need: (i) to assess compliance with the proposed IGR and then to make changes to come into compliance, if any are required; and (ii) to comply with the IGR on an ongoing basis

81. Overall, as ICAEW's current regulatory arrangement would already appear to comply with the majority of these rules and, where they don't, compliance should be relatively straightforward, there are not any significant resourcing issues anticipated relating to their implementation. This is based on the interpretation that has been made of "regulatory body" and other areas where the drafting is uncertain.
82. However, it is difficult at this stage to assess the additional resources that will be needed to undertake a review of shared services and, where changes are needed, if at all, what resources would be needed to implement them and the cost of such sources and implementation.
83. The potential requirements set out in the rule and supporting guidelines, such as for example, obtaining quotes for comparable services individually in order to make an informed assessment of whether the provision of such services continue to meet the requirements in the IGRs, are excessive and causes problems under red tape legislation in other regulatory areas. They may also not bear successful scrutiny by the Better Regulation Executive.
84. The LSB should note that such requirements will inevitably increase the regulatory fees which will not be consistent with an Approved Regulator's duty under Section 28 of the Act to promote the regulatory principle of 'protecting and promoting the interests of consumers' (onto whom the cost would be passed) and to have regard to the better regulation principle of proportionality. For these reasons it is likely that Approved Regulators will be unable to comply with a number of the ongoing review requirements prescribed in the guidance on this rule as it is likely to result in them breaching their overarching duty to comply with Section 28 of the Act.

Q4(b): Do you agree with our assessment that the cost of compliance (which includes the costs of dealing with disputes and disagreements) will reduce under the proposed IGR ? Please provide details of your assessment of the costs and actions associated with the initial assessment of compliance under the transition period and your estimation of the difference in the ongoing cost of compliance with the proposed IGR compared to the existing IGR

85. ICAEW do not agree with the LSB's assessment that the cost of compliance (which includes the costs of dealing with disputes and disagreements) will reduce under the proposed IGR.

86. ICAEW can see that the proposed rules could lead to a reduction in the cost of compliance for those unitary regulators which have been in numerous disputes with their representative arm (approved regulator) on the interpretation of the IGR and their respective roles under them.
87. However, these rules would not enhance the independence of ICAEW's regulatory functions any more than they currently are as ICAEW's internal governance structure ensures separation of ICAEW's regulatory functions from its representative functions and therefore independence of its regulatory functions. This makes for minimum of dispute and none have been encountered since reorganisation in January 2016. Furthermore, ICAEW's Regulatory Body independently determines the most appropriate and effective way of discharging its functions to meet the regulatory objectives in accordance with the better regulation principles.
88. In addition it is considered that ICAEW's Professional Standards "self-financing" model is an important factor in ensuring there is no interference or undue influence leading to prejudice in the exercise of its regulatory functions by its representative arm (Approved Regulator).
89. As a consequence ICAEW do not feel that the current IGRs required clarity in these areas as the Approved Regulator and Regulatory Body of ICAEW have always been in agreement on what their respective roles are within the current IGRs, that is to say the residual role of the Approved Regulator to be assured of compliance with the Act by the Regulatory Body and the Regulatory Body's role to discharge the regulatory functions that have been delegated to it by the Approved Regulator.
90. ICAEW has therefore never had any disputes or difficulties with compliance with the IGRs and so there will be no cost saving in this respect. Conversely the implementation of these rules as drafted will therefore increase costs for ICAEW which is likely to be, most particularly, in the areas of shared services.
91. The LSB should not underestimate the additional resources that will be required and therefore costs incurred in its requirement for regular IGR reviews and commitment to ongoing compliance. The IGRs are not as straightforward as an initial assessment and then move on. Approved Regulators will need to understand, pre-review each year, manage the LSB annual returns and questions and potentially resource further visits and other compliance related reporting. Not to mention the requirements in relation to shared services to, for example, obtain quotes for comparable services individually in order to make an informed assessment of whether the provision of such services continue to meet the requirements in the IGRs.
92. The LSB is accordingly urged to note that such requirements will inevitably increase the regulatory fees which will not be consistent with an Approved Regulator's duty under Section 28 of the Act to promote the regulatory principle of 'protecting and promoting the interests of consumers' (onto whom the cost would be passed) and to have regard to the better regulation principles of proportionality. For these reasons it is likely that Approved Regulators will be unable to comply with a number of the ongoing review requirements prescribed in the guidance on this rule as it would mean breaching their overarching duty to comply with Section 28 of the Act and section 21 of the Legislative and Regulatory Reform Act 2006.
93. In terms of evaluating the financial impact overall this is difficult to attempt when the overall framework and intent is unclear. ICAEW applies other statutory regulation to the firms it regulates (for example over two thirds of the firms it regulates for probate are also regulated for audit) and mechanisms required by the LSB which are not appropriate under the FRC governance guidelines may duplicate costs of licensing and monitoring in these respective areas, potentially involving annual additional costs in excess of £50,000 for those regulatory tasks alone.

94. Separately at a support level an estimate of an assessment of compliance rests largely with a more detailed in depth review of shared services provided to support the effective operation of Professional Standards. This ranges, for example, from managing the supply of coffee, office space and web presence through to pension management, finance, HR, IT and cyber-security. An estimate of effort to review this set-up and consider alternatives, in addition to internal staff time and expertise, is £50,000. The up-front cost of change is difficult to estimate but far in excess of a £50,000 one-off assessment. As there are a number of beneficial consolidated arrangements, and these operating across differing contractual timeframes, ongoing annual compliance cost is estimated at £25,000 pa.

Q5: Please provide comments regarding equality issues which, in your view/experience, may arise from implementation of the proposed IGR.

95. For the most part ICAEW agree with the LSB's assessment on equality that there appear to be no material impacts from an equality perspective.