

Insights

WHAT DOES THE BEIS WHITE PAPER MEAN FOR AUDIT ENFORCEMENT?

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SUMMARY

The Government has published its long-awaited [White Paper](#) on the reform of the UK's audit and corporate governance framework including a package of measures aimed at improving controls in the wake of the recent accounting and corporate governance scandals.

Under the proposals, there will be operational separation between large audit and non-audit practices, and a new audit regulator will be created with powers to hold directors personally to account.

The new regulator - ARGA

Sir John Kingman's Independent Review of the Financial Reporting Council (the "**Kingman Review**") previously recommended that the Financial Reporting Council (the "**FRC**") be replaced by a new regulator called the Audit, Reporting and Governance Authority ("**ARGA**"). The Government intends to introduce legislation to create ARGA, and fund it with a statutory levy.

ARGA will be subject to the following statutory objectives and regulatory principles:

- The General Objective: *"To protect and promote the interests of investors, other users of corporate reporting and the wider public interest."*
- The Quality Objective: *"To promote high quality audit, corporate reporting, corporate governance, accounting and actuarial work."*
- The Competition Objective: *"To promote effective competition in the market for statutory audit work."*

In contrast with the Kingman Review, the White Paper places the Quality Objective and the Competition Objective on equal footing (whilst the Kingman Review recommended the Competition Objective be prioritised).

Enforcement by ARGA

The Government intends to provide ARGA with the power to investigate, gather information and take enforcement action against directors of public interest entities for breaches of their corporate reporting and audit-related responsibilities. This represents a significant step change as the FRC is not able to bring enforcement action against directors who are not chartered accountants. Additionally, ARGA will have the power to impose requirements on FTSE 350 audit committees in relation to the appointment and oversight of auditors, and take enforcement action if these requirements are breached.

ARGA's new powers will create some overlap with the powers of the Financial Conduct Authority ("**FCA**") and the Insolvency Service, which is recognised by the Government. A memorandum of understanding between the FCA and ARGA will be published setting out how the two bodies will work together. One area to watch will be the amount of resource provided to ARGA and whether it is comparable to that of the FCA. The statutory levy should at least provide ARGA with a reasonable revenue stream.

The White Paper proposes a "graduated range of civil sanctions" that ARGA could apply when a breach by a director is proven (according to the civil standard of proof). The proposed sanctions are similar to those the FCA can impose and include: reprimands; fines; orders to take action to mitigate the effect of a breach (or the recurrence of a breach) or to make declarations as to non-compliance; and, in the most serious of cases, temporary prohibition on acting as a director of a public interest entity.

The White Paper also provides for ARGA to be given new powers to take enforcement action in relation to accountants who are members of a professional accountancy body. The White Paper notes that there have been several comments that the FRC's enforcement process seemed slow (a common issue in the context of complex regulatory investigations). As part of its reporting and transparency obligations ARGA will be required to report the time it takes to conclude investigations in its annual report and in appearances before the BEIS Select Committee.

Conclusion

This sea change in audit regulation should not come as a surprise to the market. With a new regulator on the horizon, and the potential for draconian penalties being imposed, firms will need to focus efforts on strengthening audit practices to ensure that their directors do not become the targets of enforcement action.

To learn more about the White Paper and in particular the proposed far-reaching reforms to the UK's corporate governance framework, please read our linked article [here](#).

Katerina Hemalova, Trainee Solicitor, assisted with the drafting of this blog.

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