

APPENDIX A

ICAEW'S INTERNAL GOVERNANCE RULES COMPLIANCE ARRANGEMENTS

INTRODUCTION

1. ICAEW is an accountancy body that regulates a number of reserved and unreserved professional services activities in the UK, The discharge of those activities is delegated by ICAEW Council to the Professional Standards department, and in turn the oversight of the delivery of Professional Standards is overseen by the ICAEW Regulatory Board.
2. The voluntary regulation dates back to the Charter in 1880 whilst statutory regulated activities commenced with the Insolvency Act 1986 and were augmented by the Companies Acts for audit in the UK in 1989 and Ireland in 1990.
3. ICAEW has always been mindful of its public interest responsibilities as a regulator, and reviews its regulatory arrangements every few years to ensure that it follows best practice and increasingly is seen as being independent from the membership body.
4. In 2013 an independent review was undertaken by Sir Christopher Kelly of the regulatory arrangements and governance of ICAEW at that time, which resulted in a number of changes to the regulatory structure in 2015 (including formation of the ICAEW Regulatory Board (IRB)) that met the expectations of the different oversight bodies to which Professional Standards were behoven at that time.
5. Following reviews by a number of oversight bodies in the last couple of years ICAEW at the request of the IRB has considered it timely to implement further elements of the Kelly recommendations that enable Professional Standards to continue to deliver a quality regulatory process with the appropriate degrees of independence expected from the different oversight bodies.
6. The relevant bodies and legislation involved may be summarised as follows;
 - The FRC for audit under the Companies Act 2006 and SATCAR 2016 implementing article 32 of the 2014 EU Directive on Audit
 - IAASA for audit in the Irish Republic according to Statutory Guidelines issued by that body pursuant to the Companies Act 2014 (as amended in 2018) also implementing article 32 of the EU Directive.
 - The Insolvency Service under the clauses contained in the Small Business and Enterprise Employment Act 2015
 - The Financial Conduct Authority under requirements contained in the Financial Services and Markets Act 2000 as amended by the Financial Services Act 2012.
 - The Legal Services Board by virtue of Internal Governance Rules issued under section 30 of the Legal Services Act 2007

- The Office for Professional Body Ant-Money Laundering Supervision (OPBAS) supervising regulators' compliance with the Money Laundering Regulations 2017
7. Each of these oversight bodies need to be consulted in making any changes to the governance arrangements of ICAEW's regulatory function. In the case of the Legal Services Board the requirement is to submit an application for rule changes that would permit the IRB and ICAEW to implement the improvements they consider appropriate at this time, which would also serve to meet the revised internal governance rules issued by the LSB in July 2019. This document is part of that process.
 8. In making these changes the IRB are conscious of their responsibilities under the Legislative and Regulatory Reform Act 2006 in applying the better regulation principles which are also captured in section 28 of the Legal Services Act 2007. In particular in acting as a regulator for over 10,000 accountancy firms and 2,500 audit firms it has to be mindful of the relatively small part that the 325 firms licensed for probate activity play in the overall regulatory governance responsibilities of the IRB.

Legal Services Board Internal Governance Rules

9. ICAEW is an Approved Regulator (AR) and Licensing Authority for legal Services under the Legal Services Act 2007 (the Act) and therefore, being a unitary body, has both representative and regulatory functions
10. On 24 July 2019 the Legal Services Board (LSB) published new Internal Governance Rules (IGRs) which have been a factor in the alterations to be made to ICAEW's current regulatory arrangements..
11. Following various meetings and discussions with the LSB, and provision of two compliance reports, ICAEW's proposed changes have been given provisional approval by the LSB for compliance with all the IGRs with the exception of Rules 4 and 8. For this reason this document outlines the changes ICAEW is proposing to make in order to comply with rules 4 and 8 and, as it deals with matters relevant to these rules, also rule 7, before outlining other changes that affect the compliance with the other rules. However firstly this document addresses the most significant change it is proposed to make to ICAEW's regulatory structure.

THE REGULATORY BOARD AND REGULATORY BODY

12. It is proposed that the ICAEW Regulatory Board (IRB) will replace the Probate Committee as the apex of ICAEW's legal services regulatory function and be the body referred to as the "*Regulatory Board*" in the Rules. The IRB will then together with the N Department ("PSD") be the "*Regulatory Body*" under the Rules which will be required to have control over various aspects of legal services regulatory work. The IRB approved this proposed change, not just to comply with the IGRs, but because it believes that legal services regulatory policy and strategy decisions should be made by ICAEW's most senior regulatory committee.

RULE 8 - APPOINTMENTS TO THE REGULATORY BOARD

13. Rule 8 provides that the Regulatory Body (PSD / IRB) must independently determine and carry out its procedures for appointing, re-appointing and terminating members of its board or equivalent decision-making body including the Chair, assessing their remuneration and carrying out appraisals.
14. The AR (ICAEW Council and Board) may only seek to influence these determinations in the exercise of its representative functions and must not prejudice the independent judgement of the Regulatory Body.
15. In order to comply with rule 8 we propose to make the following changes to the current appointments processes:
- (a) The IRB establishes a standing *Regulatory Board Nomination Committee* (reporting formally to it) for the: Appointment of IRB members (including the Chair) as and when vacancies arise; to conduct their appraisals; to set their terms and conditions; and to decide their remuneration. The Regulatory Board Nomination Committee will comprise the following four members:
- An independent Chair (who will be lay for all matters including legal services) to be selected through an independent process and the appointment approved by the IRB Chair and ICAEW President).
 - IRB Chair
 - Alternate IRB Chair
 - The ICAEW President or an office-holder nominated by him / her.
- (b) For each duty of the Committee the Chair of the Committee will convene a panel to carry out the duty and this panel will always consist of the following three members:
- The Chair of Regulatory Board Nomination Committee
 - The ICAEW President or an office-holder nominated by him / her
 - The IRB Chair or the Alternate IRB Chair (which chair will sit on the panel will depend on the nature of the duty being discharged)
- (c) The Chair of the Regulatory Board Nomination Committee will be provided with guidance on which IRB Chair to appoint to the panel.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B Section 3 – new Terms of Reference of the Regulatory Board Nomination Committee]

- (d) The IRB establishes a Panel to appoint the Chair of the Regulatory Board Nomination Committee which will formally report to the IRB. The Panel will comprise the following members:
- IRB Chair
 - IRB Alternate Chair
 - The ICAEW President

- (e) In order to ensure that there is the right majority of lay / non-lay and representative / regulatory members of each panel which might be convened by the Regulatory Board Nominating Committee and the proposed panel for the Appointment of the Chair of the Regulatory Board Nominating Committee, the Alternative Chair will be neither a lawyer nor an accountant.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B Section 4 – new Terms of Reference of the Panel to appoint the Chair of the Regulatory Nomination Committee]

- (f) It is proposed that the current Professional Standards Appointments Committee (PROSAC) will continue to be responsible for appointing members of all the quasi-disciplinary committees but PROSAC should report to the new Regulatory Board Nomination Committee rather than the ICAEW Nominating Committee.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B section 5 – changes to the Terms of Reference of the Professional Standards Appointments Committee and section 6 – the changes to the Terms of Reference of the ICAEW Nominating Committee]

- (g) The Terms of Reference of the ICAEW Nominating Committee will be amended to reflect the fact that it will no longer be involved in the processes for appointing members of the IRB and the Executive Director, Professional Standards Department (PSD)

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B section 6 – changes to the Terms of Reference of the ICAEW Nominating Committee]

RULE 7 - GOVERNANCE – LAY COMPOSITION

16. It is proposed that the Terms of Reference of both the Probate Committee and the IRB will be changed to allow the IRB to become the Regulatory Board for legal services regulation and to take over the responsibility for setting strategy and policy for legal services from the Probate Committee; to give it supervisory responsibility for the Probate Committee (whose direct reporting line to the LSB will be removed); and to provide the IRB with a direct reporting line to the LSB in relation to any concern it had about the independence of the legal services regulatory function (which the Probate Committee has at the moment). In addition, the constitution of the IRB will be refined so as to ensure that it has a lay majority at all times for legal services purposes. This would mean a majority of non-legally qualified members and also that, for legal services purposes, it would need to have a non-legally qualified alternative Chair. Once the amended Terms of Reference have been formally approved, the necessary appointments will be made under the new appointments processes outlined below for compliance with rule 8.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B Sections 1 and 2 – changes to the Terms of Reference of the IRB and Probate Committee]

RULE 4 - REGULATORY AUTONOMY

17. This Rule requires a legal services regulator, in particular, to determine its own governance, structure, priorities and strategy.
18. The Rule also states that the AR may only seek to influence these determinations in the exercise of its representative functions and provided it does not prejudice the independent judgement of the Regulatory Body.
19. ICAEW is of the opinion that it will be compliant with Rule 4 by making the following changes to its regulatory arrangements:

- (a) Representatives of the IRB will be involved in the appointment of any future PSD Executive Director and will have a veto against any candidate it considers unsuitable being given responsibility for legal services regulatory work.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B Section 8 - changes to the Terms of Reference of the Senior Staff Appointments Committee Terms of Reference]

- (b) A Protocol will be put in place between the AR and Regulatory Body confirming that the provision of information regarding legal services regulatory work (including information provided by the PSD Executive Director to the ICAEW Chief Executive Officer (CEO)) would be for the purposes of compliance with Rule 3 [the entitlement of the AR (ICAEW Council and Board) to be assured as to the compliance of the 'Regulatory Body' with its obligation under the Legal Services Act] and to confirm that no information will be passed on regarding general legal services regulatory developments before they are publicly announced.

[For changes to ICAEW's regulatory arrangements documents to comply with this rule – see Appendix B section 11 – new Protocol]

- (c) The PSD Executive Director's employment contract will be amended to confirm that the PSD Executive Director will report only to the IRB for all legal services regulatory matters.
- (d) The IRB Chair / the IRB Alternate Chair to have input into the setting of objectives for the PSD Executive Director in relation to legal services regulatory work and to have input into remuneration decisions in respect of the PSD Executive Director in relation to legal services regulatory work (in addition to other regulatory work).

20. ICAEW's remaining compliance proposals are as follows:

RULE 1 – OVERARCHING RULE

21. ICAEW's compliance arrangements take account of the overarching Rule 1. They therefore ensure that the exercise of its regulatory functions is not prejudiced by any representative functions and, if and where necessary, arrangements are in place to separate regulatory functions from any representative functions.

RULE 2 – DUTY TO DELEGATE

22. Arrangements to comply with Rule 2 are already generally in place as outlined below:

- (a) Under ICAEW's current structure the AR (ICAEW Board and Council) delegates all its regulatory functions to the IRB. The IRB delegates, in turn, those regulatory functions relating to legal services to the Probate Committee (the current Regulatory Body for legal services).
- (b) The AR only retains a role to the extent that it is reasonably necessary to be assured that its regulatory functions are being discharged in compliance with section 28 of the Legal Services Act. This limits ICAEW Council's role to receiving reports and assurances about the proper discharge of the regulatory functions from the Regulatory Body.

23. It is however proposed that the IRB will now be the Regulatory Board for all regulated services including legal service and, as such, will report directly to the LSB. The Terms of Reference of the IRB and Probate Committee will therefore be amended to reflect this change. On implementation of these proposed changes the Probate Committee's delegated powers will be limited to dealing with legal services applications and compliance with legal services regulations only and it will report in to the IRB.

24. To be fully compliant with Rule 2 however, certain changes required to comply with Rules 4 and 8 also need to be implemented (as outlined above). Subject to those, we consider that our regulatory operations are compliant with Rule 2 and will continue to be once the proposed changes have been implemented.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B sections 1 and 2 – changes to the Terms of Reference of the IRB and Probate Committee]

RULE 3 - ASSURANCE TO APPROVED REGULATOR

25. We consider that ICAEW is compliant with Rule 3 as the AR is already provided with sufficient information to be assured of the Regulatory Body's compliance with section 28 of the Act, through the annual reports (which ICAEW Council receives from the IRB and include the regulatory processes for legal services), and from the attendance of the PSD Executive Director at ICAEW board meetings to answer questions about issues relating to ICAEW's regulatory functions. In addition, the PSD Executive Director has monthly meetings with the ICAEW CEO to update the CEO on general developments in relation PSD's regulatory work.

26. While, as a result of compliance with Rule 5, the PSD Executive Director will be resigning as a member of the ICAEW Board, assurance will continue to be provided through (1) the IRB's annual report, (2) the monthly updates to the CEO and (3) the PSD Executive Director's continued attendance at the start of ICAEW board meetings (as an observer / presenter but not a member).

27. Furthermore, as recommended in the guidance to this Rule, the current arrangements will be formalised with the Regulatory Body agreeing a formal Protocol with the AR for provision of assurance information. The Protocol will also cover who has access to the assurance information; restrictions on its use and on the dissemination of the

information more widely within ICAEW or outside of it; and will set out the safeguards that have been put in place to prevent the misuse of information received for assurance purposes.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B section 7 – changes to the Terms of Reference of the ICAEW Board and section 11 – New Protocol]

RULE 5 - PROHIBITION ON DUAL ROLES

28. The only person currently with a “Dual Role” as defined by Rule 5 is the PSD Executive Director who has been a member of ICAEW Board since June 2016.
29. The PSD Executive Director will resign as a member of the ICAEW Board but will continue to attend parts of Board meetings which are relevant to the regulatory functions in order to update and answer questions in relation to the regulatory functions in accordance with obligations under Rule 3 and the obligations that relate to the discharge of statutory regulation of other reserved services such as audit and insolvency and voluntary regulation of the accountancy sector.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B Sections 7 – changes to the Terms of Reference of the ICAEW Board]

RULE 6 - INDIVIDUAL CONDUCT

30. PSD / IRB have determined which individuals have “*a role in*” either the exercise of regulatory functions, or in representative functions which interact with those in the regulatory functions and these individuals already have a basic understanding of their independence obligations. However, all such individuals will be given training on standards expected for independent regulatory operations (including the current Rules and any future amendments). Steps will also include
 - (a) Ensuring such knowledge is part of an ‘identified individual’s’ role profile and objectives for appraisals
 - (b) Ensuring the delivery of such training is logged
 - (c) Putting mechanisms in place to monitor and be notified of issues with compliance and to enforce relevant individual’s compliance when necessary
 - (d) Putting arrangements in place for individuals to internally report any such issues which come to their attention
 - (e) Revisiting the compliance and enforcement mechanisms in the Terms of Reference of Boards and Committees and committee member contracts.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B Sections 11 – new Protocol]

RULES 9 & 10 - REGULATORY RESOURCES / REGULATORY BODY BUDGET

31. ICAEW considers that it is already in compliance with Rules 9 and 10 and has not received any feedback in the late 2019 meetings with the LSB to the contrary.
32. With regard to Rule 10, whilst we consider that we are also in compliance with this rule, PSD will however introduce a formal signing-off process by the IRB of the PSD budget and the legal services part of the PSD Budget.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B section 12 – new Terms of Reference of the Shared Services Committee]

RULE 11 - SHARED SERVICES

33. ICAEW is proposing to comply with this Rule by;
- (i) continue the carrying out of regular assessments by the PSD Director of Finance, Operations & Projects on the level of risk created by the sharing of existing services and the value for money of the Regulatory Body's use of the shared services;
 - (ii) the establishment of a Shared Services Committee which will meet quarterly to review the existing shared services and to discuss any new proposed shared service, steps which could be taken to eliminate or mitigate any risk to the independence of the Regulatory Body arising out of the sharing of any new service and an evaluation of the proposed cost to the Regulatory Body of sharing in any new service.

[For changes to regulatory arrangements documents to comply with this rule – see Appendix B section 12 – new Terms of Reference of the Shared Services Committee]

RULE 12 - COMMUNICATION BY PERSONS INVOLVED IN REGULATION –

34. ICAEW considers that it is already compliant with this Rule as PSD already has in place steps for persons involved in the exercise of the regulatory functions to have direct access to the LSB. This not only includes its senior staff but also the Chair and members of the Probate Committee. Once the above changes are in place, this power will also be available to all members of the IRB.