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Dear Sir

#### **FRC Draft Plan and Budget 2013/14**

KPMG welcomes the opportunity to comment on the FRC Draft Plan and Budget 2013/14. We note that in the last couple of years the FRC has not published any feedback on such consultations (nor indeed the responses themselves). In order to encourage stakeholders to respond, we believe it is important that you do so - either separately or as part of the final plan and budget - so that they can see how any comments are duly taken into account.

Our detailed responses to the questions in the draft plan are in the appendix. In this covering letter we have made some more general observations. Unless otherwise stated, all references are to pages or sections of the draft plan.

It is helpful for the FRC to set out its plans in a three year context. This makes it clear how many of its activities are actually expected to continue for a considerable time, rather than being discrete projects that will be concluded, for example, when a pronouncement is finalised. It will also be helpful if the FRC's future plans can explain where they have not turned out as expected and have had to be changed.

The scope of the plan is inevitably very broad, covering as it does monitoring, disciplinary and standard-setting activities as well as promoting the concept of stewardship, improving the accessibility of accounts, seeking to influence UK and EU legislation and international standard-setting and gathering evidence to support the FRC's contributions to thought leadership. In this context whilst we support the general sentiments expressed in section 1 of the draft plan (and in particular the need to influence developments in Europe and internationally), we are also disappointed that there is a lack of any clear indication of how success is to be measured and as a consequence how the FRC might be held to account for its achievements or lack thereof. This might be assisted if the FRC clearly identified a smaller number of discrete activities and projects which it will focus on. We believe this is important for any organisation, but particularly one where those providing the funding (corporates and the professions) have

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(appropriately) less influence on the activities undertaken than other key stakeholders (investors and government).

There is some work that we are not convinced that the FRC needs to be doing, certainly by itself. In particular we believe the FRC should carefully consider the evidence obtained from its own monitoring and consultation activities or from work carried out elsewhere before carrying out its own research or commissioning studies. We would also encourage collaborative working with, for example, stakeholders, academics or other standard setting bodies in order to minimise costs. This would help the FRC to be seen more as a body that is keen to work with and learn from others and whose initiatives are clearly supported by its stakeholders.

We are concerned at the proposed cost increases. In the current economic climate the FRC should distinguish between those activities and projects that are essential and those which, while desirable, are either not so urgent or as noted above can be pursued in cooperation with other bodies. In this regard we are also disappointed that the savings projected at the time of the FRC reorganisation (from streamlining the organisation) are not yet evident from the proposed budget. Whilst we accept the need to increase resources in some areas (the audit of financial institutions and IT audit spring immediately to mind although these do not of course affect core costs) we believe that some of this additional cost should be offset by savings elsewhere, particularly in the FRC's general administration/internal governance roles.

At a time when corporate budgets are shrinking and industry profits are falling, the net increase in the budget therefore needs clearer justification in terms of enhanced performance and the achievement of identifiable milestones. However the lack of detail in the budget either by type of cost (no staffing details at all are provided although we presume it is mainly payroll related) or activity (over half the total cost is simply characterised as "Corporate governance, reporting and auditing) makes it difficult to comment further. You have given in section 3 some indication of where activity might increase and we comment on aspects of these in the Appendix. As a general point we would observe however that nearly all of these increases relate to conduct activities and hence primarily only to priority 1 (Regulatory activities) and part of priority 4 (Audit quality and value) set out in section 1.

We hope you find these comments helpful and would be happy to discuss them in more detail with you.

Yours faithfully

Tony Cates  
*Head of Audit*  
KPMG LLP

## **Appendix**

### **Response to consultation questions**

#### **1 Do you have any comments on the proposed priorities and engagement strategy outlined in section 1?**

We support the FRC's intention to enhance its influence by focusing on quality and relevance and by obtaining supporting evidence through studies and enquiries, etc. However, while there may in some circumstances be a place for the FRC to carry out its own studies, we consider that the FRC should find most of the information it needs from its regular communications with stakeholders and from feedback from its own ongoing review and monitoring activities.

The FRC's "priority projects" are introduced in this section before being set out in more detail in section 2. As we explain in our covering letter, we consider the term "projects" for the broad areas of the FRC's activities to be somewhat misleading. Within these broad areas, we would expect the FRC to analyse what it does in terms of continuing activities and specific – and normally time-bound – projects.

#### **2. Do you have any comments on the activities outlined in section 2?**

We consider that a number of the activities listed in this section will continue up to 2015/2016 and beyond, including influencing developments such as UK and EU legislation and the work of the international standard setting bodies and potentially addressing any ultimate concerns of the Competition Commission.

A number of the activities refer to carrying out studies, enquiries and research. Bearing in mind our comments above, if this proves necessary, then wherever possible the FRC should seek to collaborate with others in this work, particularly as people like academics are likely to be more accustomed to carrying out research to the required standards.

As markets become increasingly global, it is important that the FRC should work closely with international standard setters and regulators. While such cooperation is high on the FRC's Corporate Reporting and Stewardship lists, working with the IAASB and the IESBA should similarly be high on the Audit Quality and Value list. It is important for the sake of international consistency and the credibility of financial statements and audit worldwide that differences between international and UK requirements should be kept to a minimum. We would hope that higher positions on the FRC's lists will mean that the FRC will channel its efforts into achieving solutions internationally and not seek to develop its own unilaterally.

In the Audit Quality and Value list, as well as considering the assurance model generally, consideration should be given to incorporating the IAASB's pronouncements on "other

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assurance” engagements into UK requirements. The preferred option for pronouncements on narrative reporting, forward-looking information, governance and controls, etc, should be to develop them at the international level. If the UK develops its own versions, it should be clearly stated that these are only in force until the international pronouncement is in place and adopted for use in the UK.

On the Actuarial Oversight and Standards list, it is not clear what will be involved in “establishing the most effective way for the profession to build public trust in the ethical standards of actuarial work”, nor is it clear that public trust is currently lacking?

### **3. Do you have any comments on our draft Budget 2013/14?**

As noted in the covering letter, there might be some justification for the proposed increases in costs and levies if it were clearer what the FRC aims to do and how it has sought to achieve savings either from the reorganisation or otherwise. In relation to the areas identified in section 3 as necessitating the increased resource we have the following observations.

*Respond to the increasing demands from EU, international and other national regulators and standard setters for evidence from our conduct work.*

We are pleased that the FRC recognises up front the need to strengthen the role played by evidence and analysis in its work and to be clear when points of view are based on judgement. If it does this then the provision of such evidence to others should not add greatly to costs. It is not however evident that this principle (and the suggested clarity) is always followed through in practice – for example in reports of the AQRT.

*Conduct thematic studies in response to emerging corporate reporting and audit issues.*

We appreciate that such studies may be helpful in highlighting pervasive issues that need to be addressed. However we would not wish this intention to lead to a demand to perform such studies irrespective of their merits. We would therefore encourage the FRC to be disciplined in its approach and to be clear upfront about both the issue and the objectives it believes would be met by such a study. In some circumstances it may be appropriate to consult on carrying out such a study in advance and/or work with others in order to defray the costs.

*Conduct supervisory inquiries into events such as corporate failures or near-failures to better determine what action might be required.*

In our response to the FRC’s reorganisation proposals we urged that care be taken not to duplicate the work of other bodies such as Inspectors appointed under the Companies Acts. We would reiterate that request and also as above encourage the FRC to be clear in advance

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as to what it aims to achieve both launching full scale (and potentially expensive) enquiries of this nature.

*Discharge our new auditor sanctioning powers and proportionate powers in relation to the accountancy regulatory bodies we regulate.*

The comment implies that the FRC believes these new powers will lead to a significant extension of the sanctions that it seeks to impose as a result of routine inspections. We are both surprised and concerned at this given its previous ability to recommend sanctions in the past to the Audit Regulatory Committee. Given the criteria in the proposed sanctioning procedures and the need to act proportionately it is not evident that any increase would be merited.

*Manage a step increase in the speed and effectiveness of our disciplinary processes whilst at the same time clearing the back-log of cases.*

We also note the intention to undertake more aspects of disciplinary investigations in-house rather than through external suppliers. Provided that the FRC continues to improve its determination of which cases should be pursued is not clear to us why this should lead to any significant increase in core costs given the separate funding of the disciplinary schemes and the ability to recover costs from those who are successfully prosecuted. We are also concerned that “clearing the back-log of cases” should not lead to any permanent increase in core costs.

*Regulate third country auditors*

We continue to be willing to work with the FRC and others as to how its mandate in this area might be best satisfied at least cost. We would hope therefore that any increases would be marginal. It is also unclear to us whether such activities are funded via the core levy or through the separate funding of the AQRT by the professional bodies.

*Plan for the regulation of local authority audit*

Clearly this is one development that leads to some increase in costs. It is not clear to us that the existing funding arrangements (which rely heavily on corporate levies) are altogether satisfactory for dealing with this and we believe this is something that should be explored further.

*Enhance the FRC’s strategic, analytical and research capacity*

Whilst we support such efforts we would again stress the importance of carrying out a few clearly targeted projects well rather than spreading the resource too thinly. As such whilst it

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will always be important to react to specific developments if and when they occur we believe that you should set out a clear plan of which projects you have in mind.

*Increase our work in setting codes and standards for corporate governance and reporting*

Similarly we suggest you clarify exactly which areas you have in mind – particularly given the recent changes in such areas as the governance and stewardship codes which should be allowed time to bed down before considering further changes

**4. Do you have any comments on our proposed preparers' levy rates for 2012/14?**

No comments.

**5. Do you have any comments on our proposal to align the FRC levy arrangements with the current UK Listing regime?**

No comments.

**6. Do you have any comments on our proposals in relation to the insurance and pension levy rates for 2013/14?**

No comments.