FINANCIAL REPORTING COUNCIL

REPORT AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

HC 2421

ANNUAL REPORT AND FINANCIAL STATEMENTS OF THE FINANCIAL REPORTING COUNCIL LIMITED

– INCLUDING THE REPORT OF THE INDEPENDENT SUPERVISOR YEAR TO 31 MARCH 2019

The Report of The Financial Reporting Council Limited (‘FRC’ or ‘Company’) as the body designated by a delegation order under section 1252 of the Companies Act 2006 and the Report of the Independent Supervisor is presented to Parliament pursuant to sections 1231(3) and 1252(10) of, and paragraph 10(3) of Schedule 13 to, the Companies Act 2006.

The Report of the Independent Supervisor is also presented, pursuant to section 1231(2), to:

— The First Minister in Scotland;

— The First Minister and Deputy First Minister in Northern Ireland; and,

— The First Minister for Wales and is laid before the National Assembly for Wales pursuant to section 1231(3A) of the Companies Act 2006.

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OUR MISSION AND REMIT ARE TO PROMOTE TRANSPARENCY AND INTEGRITY IN BUSINESS

HIGH QUALITY AUDIT, CORPORATE GOVERNANCE AND FINANCIAL REPORTING ARE VITAL TO THE SUCCESS AND CONTINUED GROWTH OF OUR ECONOMY

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FRC AT A GLANCE

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OUR MISSION AND REMIT ARE TO PROMOTE TRANSPARENCY AND INTEGRITY IN BUSINESS

Our Role

Competent Authority for statutory audit in the UK setting auditing and ethical standards and monitoring and enforcing audit quality.

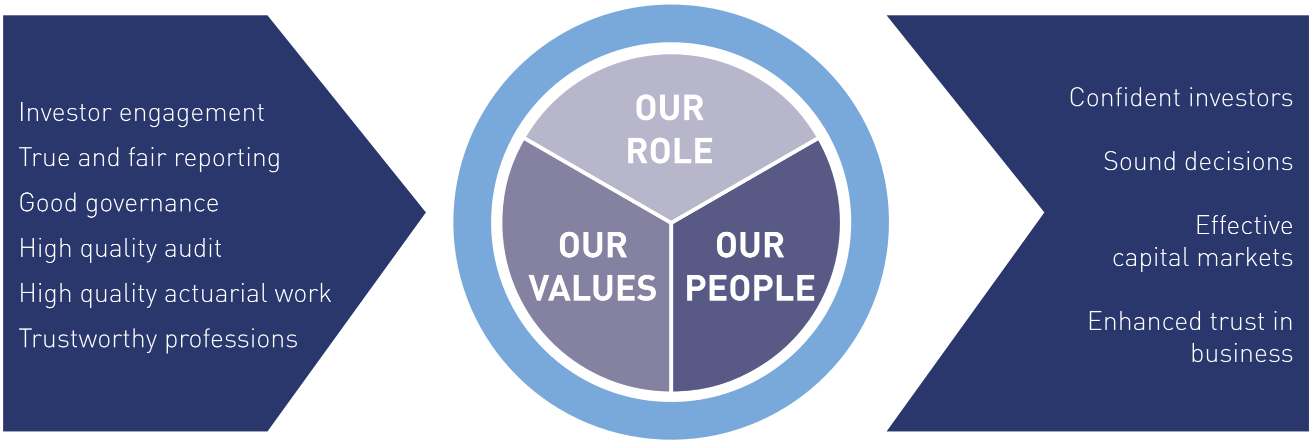
Sets UK and Ireland accounting standards.

Sets the UK Corporate Governance Code, the UK Stewardship Code and standards for actuarial work.

Monitors and takes action to promote the quality of corporate reporting.

Operates some independent disciplinary arrangements for accountants and actuaries, and oversight.

WHAT WE PROMOTE | HOW WE DO IT | OUTCOME



Our Values

Effective – timely, decisive, innovative and relevant

Fair – consistent and proportionate

Independent – taking decisions based on evidence

Influential – in the UK and internationally, demonstrating thought leadership

Our People

Attract, inspire, develop and reward high calibre people

High levels of employee engagement

Promoting equality and diversity in all areas of our work

More details about our role can be found at https://www.frc.org.uk/Role-and-Responsibilities.

2018/19 AT A GLANCE

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Throughout the year the FRC has been delivering against its planned projects and initiatives, including regular monitoring work, enforcement cases and innovative policy developments, intended to promote transparency and integrity in business.

April 2018

We updated our sanctions guidance following an independent review.

Greater use of non-financial sanctions applied to enforcement cases closed during the year.

May 2018

We issued the first of our updates on our investigations in relation to Carillion plc.

June 2018

Big Four audit inspection results for 2017/18 were published, showing 73% of audits of FTSE 350 companies requiring no more that limited improvements, compared to 81% the year before.

Results for 2018/19 are 75%. Audit quality remains a significant concern.

July 2018

The FRC's new Investor Advisory Group met for the first time.

August 2018

The *UK Corporate Governance Code* (July 2018) was issued.

September 2018

Board Diversity Reporting was issued showing that companies should do more to treat diversity as part of business strategy.

October 2018

We set out a new strategic programme of work on audit, intended to ensure it better meets the public interest.

November 2018

A Financial Reporting Lab report on performance metrics and a thematic review of reporting by smaller listed and AIM quoted companies seek improvements in corporate reporting.

December 2018

The *Independent Review of the Financial Reporting Council* is published.

The FRC welcomed the recommendations.

January 2019

A consultation on a new Stewardship Code was launched.

February 2019

Over the year the Enforcement team has grown by 25%, helping to deliver more timely and effective enforcement activity.

March 2019

A consultation on increasing the work required of auditors in relation to going concern was launched.

Enforcement · Audit · Governance & Stewardship · Reporting · Independent Review

CHAIRMAN'S STATEMENT

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SIR WINFRIED BISCHOFF CHAIRMAN

This will be my sixth and final annual report as Chairman, having been appointed in May 2014. Following the *Independent Review of the Financial Reporting Council* by Sir John Kingman, it is proposed that the FRC will transition into the new Audit, Reporting and Governance Authority (ARGA) under a new mandate, new powers and new leadership to implement its new mission. The Board and I were pleased that Sir John's recommendations included many which we had made over the years, and that his Review added valuable independent credibility to our views. We are working with the Government, as a matter of urgency, to take forward those aspects of the transition that can be undertaken or initiated in advance of legislation. This includes measures already in hand to strengthen our supervisory and enforcement work.

I strongly share the Government's view that high quality audit, corporate governance and financial reporting are vital to the success of our market economy, and that the FRC and ARGA have an important role in maintaining the UK as a great place to do business. Our *Plan & Budget 2019/20* sets out our strategic priorities, including supporting the transition to the ARGA.

Businesses, as major generators of economic activity, provide employment and are a source of dividends and returns for shareholders including pension schemes that provide retirement benefits for many. However, at present there is debate about the wider purpose of business and the role of audit and auditors. In that context we welcome that the future of audit and the audit market are being reviewed by Sir Donald Brydon and through the *Statutory Audit Services Market Study* by the Competition and Markets Authority (CMA).

There continue to be challenges and risks to our mission and ultimately to that of the ARGA. In no particular order: the work and recommendations of the CMA and of Sir Donald Brydon may not address all stakeholders' expectations; a focus on the future must not divert attention from business-as-usual and the imperative of quality in audit; the delay in, and nature of, the UK's exit from the EU continue to give rise to uncertainty; challenging economic conditions in certain sectors of the economy may result in corporate failures despite good corporate governance and reporting; and a sound audit framework.

CHAIRMAN'S STATEMENT

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Activities of the last year included the development of some important initiatives.

A key area was corporate governance and stewardship. We revised the *UK Corporate Governance Code* in July 2018 and participated in the Coalition Group that issued the *Wates Corporate Governance Principles for Large Private Companies* in December 2018. The revised *UK Corporate Governance Code* was well received, and we will extend our monitoring of corporate governance practice and reporting and consider how effectively the new Code is being applied. However, that effectiveness depends on investors holding companies to account. We have consulted on a revised *UK Stewardship Code* which demands more effective stewardship and critically improved reporting requirements. We are committed to engagement with stakeholders and in this area have continued our outreach in the UK, as well as in Europe and globally.

The number of referrals to enforcement increased but, due to greater staff numbers, we improved the speed of investigations. We also significantly reduced the backlog of legacy cases, largely through settlement with respondents without the need for a full Tribunal process.

It was very disappointing that the results of this year's AQR reviews have once again fallen short, in aggregate, of the target we set for the industry, and we have not seen a significant increase in audit quality. Although the quality of audit of the FTSE 350 (as assessed by our monitoring programme) has stabilised since last year at 75% requiring no more than limited improvements (2017/18: 73%, 2016/17: 81%) we are not seeing more immediate improvements from the firms and there is undesirable inconsistency across the market. There are many good audits, but too many fall short of the 90% target of requiring no more than limited improvements. We are continuing to challenge and call out the firms to improve.

During the year there have been some changes to the Board. In October 2018, at the end of his term, Roger Marshall left the Board and Paul Druckman stepped down at the end of March 2019. Since the year end our Deputy Chairman, Gay Huey Evans OBE, stepped down on 30 April 2019, as did Mark Armour on 30 June 2019, as both had concluded their terms of appointment. Mark Zinkula also left the Board with effect from 30 June 2019 on his retirement as Chief Executive of Legal and General Investment. Therefore, since the last Annual Report the Board has been reduced from 15 members to ten, which is in line with the conclusion of our own 2017/18 Board Effectiveness Review for a smaller Board, a recommendation which was also made by Sir John Kingman. Going forward all Board appointments will be made by the Secretary of State for Business, Energy and Industrial Strategy, and the new Chair will be accountable to Parliament as befits a public body. I thank all past and present members of our Board for their valuable contributions over the years.

On behalf of the Board I would like to also thank our staff for their continued commitment and contribution in challenging circumstances and at a time of considerable uncertainty regarding their own position, and that of the FRC as it transitions to the ARGA.

SIR WINFRIED BISCHOFF
CHAIRMAN
4 July 2019

CHIEF EXECUTIVE'S REPORT

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STEPHEN HADDRILL CHIEF EXECUTIVE

This report discusses progress against the priorities set out for 2018/19 and then looks forward to 2019/20. This is my final Chief Executive's Report for the FRC, with a new Chief Executive expected to be recruited during the autumn.

The FRC has always evolved and will continue to change as it transitions into the ARGA. It has substantially increased its monitoring of corporate reports and audit quality, issued new accounting, auditing and actuarial standards, significantly enhanced its enforcement activities, revised the UK Corporate Governance Code and introduced the UK Stewardship Code.

We have been innovative and at the forefront of international developments, such as auditor rotation, the enhanced audit report and limiting the period of Chairmans' appointments at listed companies. Some of the actions we have taken are in areas where statutory powers do not exist. This is an approach that can push the best to achieve more, and advances best practice, but ultimately a lack of statutory powers limits what can be achieved across the whole market. Some of the changes we have made, should have had and should now get statutory backing.

Public, or societal, expectations of corporate behaviour, audit and regulators have changed. There has also been a significant change in Government policy, from one of deregulation to the current launching of reviews to strengthen regulation of audit. The FRC remains committed to continuous improvement and transitioning into the new ARGA.

REGULATION DURING 2018/19

Whilst it is important that the FRC responds to the changing environment to serve the public interest effectively, the FRC has also had a full programme of business-as-usual work during 2018/19 and will continue to deliver it in the future. This includes our corporate reporting review work, our audit quality review programme and enforcement casework, as well as policy work and standards development. In carrying out our regulatory work we comply with the Regulators' Code and follow the principles of good regulation set out in the *Legislative and Regulatory Reform Act 2006*. We seek to be proportionate, accountable, consistent, transparent and targeted in the way we discharge our responsibilities and operate in the public interest. We keep our regulatory approach under review to ensure that we are meeting best practice.

Much of our work is reported on in more detail through individual reports and our *Developments in Audit 2018* and *Annual Review of Corporate Governance and Reporting 2017/18* reports, both

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of which were issued in October 2018. During 2019 we will also be issuing, for the first time, an Enforcement Annual Review.

TRANSITION TO THE NEW ARGA

On 11 March 2019 the Government issued its response to the *Independent Review of the Financial Reporting Council* confirming that it is taking forward the review's recommendations and that the FRC will transition into the new ARGA, once established by legislation. Many of the recommendations of the review can be actioned in advance of the establishment of the ARGA and work has commenced on these overseen by a Joint Project Board with BEIS.

The first recommendation to be implemented was the issue of a remit letter from the Secretary of State on 11 March 2019. This confirmed the FRC's mission to promote transparency and integrity in business and established the creation of the ARGA as a top priority. Taking forward this programme of change is reflected in our *Plan & Budget 2019/20*.

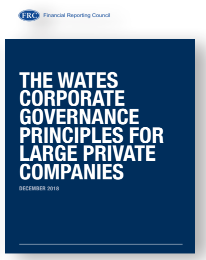
We will support BEIS in considering the policy and practical aspects of the proposed new powers. Without legislative changes, the vision of the *Independent Review of the Financial Reporting Council* cannot be fully realised. Change needs to be carefully managed. The benefits are great but there are also risks, including in terms of damage to the UK as a place to invest, to the operation of markets, and to the strength of the accounting and audit professions.

As well as working with BEIS on the overall programme of change, we have been working with HM Treasury on its work implementing the recommendations in respect of the FRC's actuarial responsibilities.

CORPORATE GOVERNANCE AND STEWARDSHIP

As part of our contribution to restoring public trust in business we have been working on a number of corporate governance projects.

We revised the *UK Corporate Governance Code* in July 2018 and supported the Coalition Group that issued the *Wates Corporate Governance Principles for Large Private Companies* in December 2018. The revised *UK Corporate Governance Code* was well received and we will extend our monitoring of corporate governance practice and reporting and consider how effectively the new Code is being applied.



Other major activities during the year included:

- we have consulted on a revised UK Stewardship Code which aims to increase demand for more effective stewardship and improved reporting requirements;
- our report on *Board Diversity Reporting* and the associated event, which was attended by almost 300 people; and
- the establishment of our Investor Advisory Panel, which complements our existing stakeholder outreach activities including those with investors.

CORPORATE REPORTING

In our *Annual Review of Corporate Governance and Reporting 2017/18* we found a higher number of basic errors or mistakes in the financial statements we reviewed during 2017/18. We have addressed these with the companies concerned. The overall results of our 2018/19 reviews will be reported later in the year.

We have focused more on thematic reviews this year, which can have a significant influence over improving corporate reporting in targeted areas, including those looking forward to the introduction of major new IFRSs. We issued three thematic reviews this year. Two focused on the implementation of IFRS 9 *Financial Instruments* and IFRS 15 *Revenue from Contracts with Customers*, by looking at disclosures provided in interims, and the third was targeted at small listed and AIM quoted companies.

We have been more transparent about our Corporate Reporting Review work with quarterly reporting of the names of the companies that have been reviewed. With the Government we will be taking forward recommendations to strengthen our corporate reporting review work, including extending the process to the entire annual report.

We continue to work to influence the IASB in setting IFRS and with EFRAG on European views on standard setting, and in supporting the endorsement of standards for use in Europe. A focus for this year has been IFRS 17 *Insurance Contracts*, on which the

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IASB is now considering limited amendments. We have also been working with the Government to set up the new UK Endorsement Board, which will determine whether IFRS should be endorsed for use in the UK after the UK's exit from the EU.

We set up an advisory group for our Future of Corporate Reporting project with representatives from a wide range of stakeholder groups. The project aims to influence changes in the form and content of company reports.

AUDIT

The FRC's role as Competent Authority includes setting auditing and ethical standards, monitoring audit quality, taking enforcement action and delegating, under the direction of the Secretary of State, various oversight tasks to the Recognised Supervisory Bodies (RSBs).

We continue to innovate in the way we monitor firms and encourage continuous improvement. In April 2018 we announced innovative plans to enhance our monitoring of the six largest audit firms, the Audit Firm Monitoring and Supervision approach (AFMAS). This complements our continuing work in reviewing audit quality by seeking evidence about leadership and governance, firm values and behaviour, business models and financial soundness, and risk management. AFMAS aims to reduce the likelihood of systemic deficiencies that could impact on audit quality and ultimately the stability of the financial markets. We do not have specific powers in this area, but it contributes to our work on audit quality. *The Independent Review of the Financial Reporting Council* supported this new monitoring approach, and recommended that it become a statutory role of the ARGA. We are recruiting staff for this function and expect it to make a greater impact in 2019/20.

We report on our activities as Competent Authority through this report and our annual *Developments in Audit* report. Inevitably that report reflects on our activity in the previous year and therefore, although issued during 2018/19 reflects our audit quality reviews from 2017/18. We report on matters affecting the audit market as a whole, as well as our casework reviewing individual firms and our thematic reviews.

In 2015 we set the auditors of FTSE 350 companies a target that, by 2018/19, at least 90% of those audits inspected should require no more than limited improvements. After a number of years of increasing audit quality, our assessment in 2017/18 was that 73% of audits achieved this standard, leaving a significant amount of progress required in the final year to meet the target. One firm in particular, KPMG, had shown an unacceptable deterioration in quality, and this year we have carried out additional reviews of its audits.

The 90% target has not been met this year, audit quality is not as high as it should be, and in some quarters confidence in audit has fallen. Our assessment of the reviews we carried out this year is that 75% (2017/18: 73%) achieved the standard. This shows only a very limited improvement on last year, and performance at individual firm level was mixed.

As a result, we will, for 2019/20:

- Continue to measure firms audit quality against the 90% FTSE 350 target and expect all firms to meet that target.
- Extend the 90% target to all other audits within the scope of our inspection.

We will, for 2020/21 onwards, set a new target for audit firms, that 100% of audits should require no more than limited improvement.

At one firm, Grant Thornton, the quality of the audits inspected in the year, and indeed the overall lack of improvement in quality over the past five years, is a matter of deep concern. We have therefore required the firm to prepare and implement a detailed action plan to improve quality.

We are taking forward recommendations relating to greater transparency over our inspections, to respond to the *Statutory Audit Services Market Study* from the CMA. We are enhancing our programme of work on auditing standards. High quality auditing and ethical standards contribute to overall audit quality. During the year we consulted on revisions to the auditing standard on going concern and a post-implementation review of the 2016 ethical and auditing standards. Our position paper, issued in March 2019, sets out the next steps in further strengthening these standards.

ENFORCEMENT

A number of cases have been concluded this year with significant fines and other non-financial penalties, reflecting the implementation of the review of our sanctions that was carried out in 2017. Significant fines imposed this year include:

- £3.15 million for KPMG in relation to Quindell plc (discounted from £4.5 million for settlement);
- £6.5 million for PwC in relation to BHS Limited (discounted from £10.0 million for early settlement);
- £2.1 million for KPMG in relation to Ted Baker plc (discounted from £3.0 million for settlement); and

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	2018/19 £m	2017/18 £m	2016/17 £m
Total financial penalties imposed	32.0	13.1	9.3

	2018/19 Number	2017/18 Number	2016/17 Number
Number of financial penalties imposed	27	11	13
Number of non-financial penalties imposed	38	11	16
Of which:			
exclusions	6	2	7

- £3.0 million for Grant Thornton in relation to Nichols Plc and the University of Salford (discounted from £4.0 million for settlement).

Since the year end we have announced further closed cases with significant fines, including:

- £6.0 million for KPMG in relation to Equity Red Star;
- £4.0 million for KPMG in relation to The Co-operative Bank plc (discounted from £5.0 million for settlement); and
- £4.2 million for Deloitte in relation to Serco Geografix (discounted from £6.5 million for settlement).

The FRC's investigations in relation to Carillion plc are ongoing. Due to the significant public interest in the matter we have issued two updates this year, in relation to the progress of the investigations, but are unable to comment in detail in order to protect the integrity of the investigations. We continue to progress our investigations in conjunction with other regulators.

A key area of focus has been the financial performance of Carillion's major contracts in both the construction and services divisions, and whether Carillion management and its auditors ensured that this was appropriately reported in its financial statements. The investigations are also considering conduct relating to pension liabilities, goodwill, cash disclosures and going concern.

Cases opened and closed during the year	2018/19	2017/18	2016/17
Open as at 1 April	39	34	32
Opened	15	14	11
Closed	(13)	(9)	(9)
Open as at 31 March	41	39	34

In addition to Carillion, our Enforcement Division has 40 other cases[1] in progress, with more cases being opened each year than in the previous year.

During the year the Conduct Committee opened 15 new investigations: 12 audit investigations under the Audit Enforcement Procedure (AEP) and three investigations into accountants under the Accountancy Scheme. The increase in the number of investigations opened, compared to two years ago (2016/17) is partly a result of the lower threshold for opening cases under the AEP, compared to the previous Misconduct test. No investigations have been opened during this period under the Actuarial Scheme.

The 12 AEP investigations concern a wide range of audit issues including the audit of cash, supplier rebates, provisions and pensions; revenue recognition; oversight of component auditors and compliance with laws and regulations.

Constructive engagement is a process introduced by the AEP for resolving cases where the audit quality concerns can be appropriately and satisfactorily addressed without full enforcement action. We used constructive engagement to resolve 16 cases during the year.

UK EXIT FROM THE EU

During the year we have continued to work with BEIS on preparations for the UK's exit from the EU. This has included work to establish a new UK Endorsement Board that will endorse IFRS for use in the UK, and work relating to the registration of auditors once the UK becomes a 'third country' in the context of EU legislation, and EU countries become 'third countries' in the context of UK legislation.

1 A 'case' is deemed to be an investigation into either the auditors at a company (one case covering the audit firm and individual auditors) or Members in Business at a company (one case covering one or multiple members). A case is only deemed closed once the investigations into all subjects have been concluded.

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PROFESSIONAL OVERSIGHT

Appendix 1 is our report on our oversight activities for the year. It includes an executive summary that sets out the key matters to note.

ACTUARIAL

As part of the Joint Forum on Actuarial Regulation (JFAR), we have completed the *Risk Perspective: 2019 Update*, which was published after the year end in April 2019. We also took the lead for JFAR on a series of roundtable discussions with chief actuaries and Non-Executive Directors of general insurance companies to discuss the Actuarial Function Holders Report considering how to ensure an effective report.

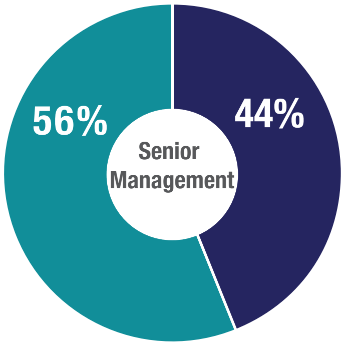
As part of our ongoing work on technical actuarial standards, we undertook a review of the *Actuarial Standard Technical Memorandum 1: Statutory Money Purchase Illustrations* and concluded that no change was required for illustrations prepared from April 2019. We also consulted on a new *Actuarial Statement of Recommended Practice 1: Financial Analysis of Social Security Programmes*, which is in effect adopting an international model actuarial standard. This Actuarial Statement of Recommended Practice will be the first issued by the FRC.

PEOPLE

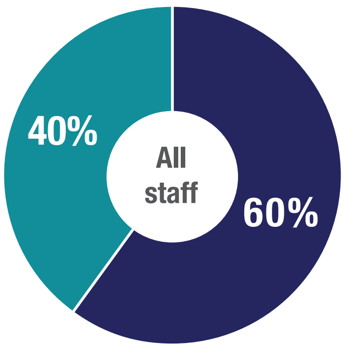
Over the past year we have expanded our workforce, particularly as part of strengthening the enforcement function. At 31 March 2019 the FRC had 210 employees (2018: 192). During 2019/20 we expect to recruit 80 additional staff to pursue a step change in audit quality, continue to strengthen enforcement and promote the quality of corporate reporting, governance and investor stewardship.

In terms of gender balance:

- 50% (2018: 67%[2]) of the members of the Executive Committee are female;
- 44% (2018: 48%) of the senior managers (including the Executive Committee) are female (there are 24 female and 30 male senior managers as at 31 March 2019 (2018: 25 female and 27 male)); and
- 60% (2018: 64%) of all staff are female.



■ 24 Women ■ 30 Men



■ 127 Women ■ 83 Men

Last year, for the first time, we disclosed data on the ethnic diversity of our staff, which had been voluntarily provided. This year we carried out some work on a pilot exercise to calculate our ethnicity pay gap.

Going forward, we will be conducting our annual staff survey in conjunction with BEIS as one of its partner bodies. This means a change of timing from January/February to the autumn and as a result no full staff survey has been carried our during 2018/19. In addition to the annual staff survey we also carry out a number of 'pulse surveys' each year, often of topical interest. We engage actively with staff, for example through the People Forum (for which a Non-Executive Director provides liaison with the Board) and our active Diversity and Inclusion Committee that has championed a number of initiatives throughout the year.

During the year the FRC gained accreditation from the Government as Disability Confident Committed, which evidences our commitment to improving opportunities for disabled people by ensuring that our recruitment processes do not discriminate; we consider reasonable adjustments; and we continue to support our current staff to remain at work who come under the Equality Act 2010.

The FRC is committed to supporting the physical and mental health of its people and fostering employee wellbeing and has run a number of related training events this year. We have in place an employee assistance provider to offer additional support to our people. The average working days lost to sickness absence for the 12 months to 31 March 2019 was 4.3 days.

This year the FRC has been adjusting to some of the requirements of being a public body. One that has a particular impact on our people has been the way in which pay reviews are carried out, which now requires approval from BEIS. This year approval from HM Treasury and the Cabinet Office was also required.

2 The comparative has been revised to include Acting members of the Executive Committee.

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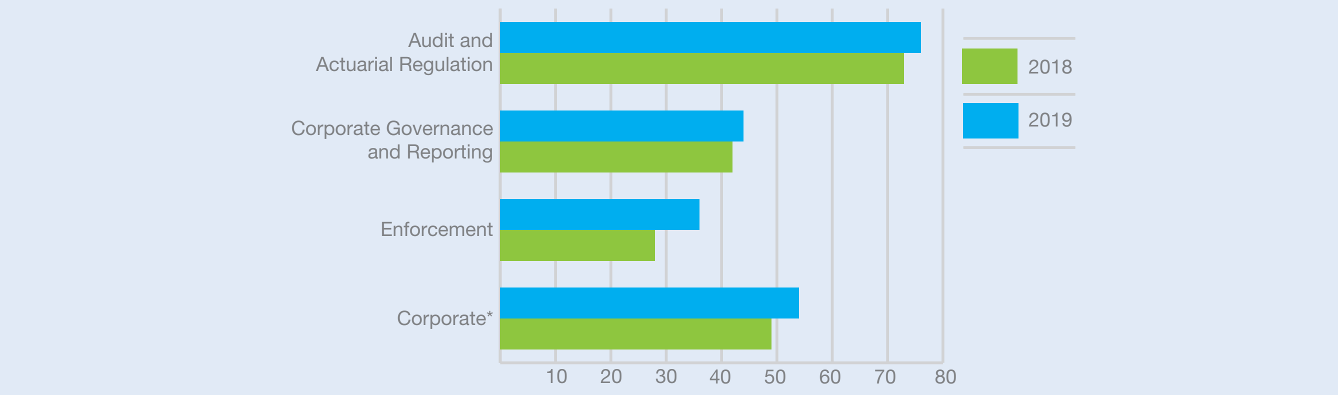
OUR PEOPLE BY DIVISION



* Corporate includes the CEO's office, Governance and Legal and Strategy and Resources.

The FRC's proposals for the year commencing 1 April 2018 were submitted to BEIS in July 2018, once the Public Sector Pay Guidelines were available, and a further business case was required for HM Treasury and the Cabinet Office. The Secretary of State set out his conclusions in March 2019. Final approval was provided in July 2019. This delay has had a major impact on morale at a time when more and more is being asked of all in relation to delivering existing, and planning for future, activities.

Recruitment of 80 new roles represents nearly a 40% increase in staff. A recruitment programme of this size inevitably represents a challenge for the FRC, which would be increased if voluntary staff turnover rises significantly above its current level of 11%.

To mitigate this we are reviewing our recruitment processes to ensure they continue to support effective and timely recruitment, and integration of new employees into the FRC. We are also actively encouraging internal applications for the new roles and focusing on employee development as part of a new performance management system that is being developed.

EXECUTIVE COMMITTEE

In delivering the FRC's strategic plan and meeting my responsibilities as Accounting Officer I am supported by my colleagues on the Executive Committee. The Executive Committee currently[3] consists of:

Stephen Haddrill	Chief Executive Officer and Accounting Officer
Elizabeth Barrett	Executive Counsel and Director of Enforcement (from 1 August 2018)
Paul George	Executive Director, Corporate Governance & Reporting
Anne McArthur	General Counsel and Company Secretary
Mike Suffield	Acting Executive Director, Audit & Actuarial Regulation (from 1 August 2018)
Tracy Vegro	Executive Director, Strategy & Resources

Looking forward David Rule the new Director of Supervision joins us on 1 September 2019. I would like to echo the Chairman's thanks to all my FRC colleagues, including those on the Executive Committee, for their hard work over the last year.

STEPHEN HADDRILL
CHIEF EXECUTIVE OFFICER AND ACCOUNTING OFFICER
4 July 2019

3 Executive Committee members that stepped down from the Committee during the year are:
Melanie Hind Executive Director, Audit and Actuarial Regulation (to 31 July 2018); and
Claudia Mortimore Acting Executive Counsel and Director of Enforcement (to 31 July 2018).

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Each year we develop a series of priorities that support our remit and strategy. Our remit letter is set out below. Our priorities for each year evolve over time to respond to changes in the external environment and to reflect the impact of actions taken in earlier years. These are set out in our *Strategy 2018/21, Budget and Levies 2018/19* document and our *Plan & Budget 2019/20*. The *Plan & Budget 2019/20* shows how our strategic priorities have been focused to address both the transition of the FRC into the ARGA and our ongoing regulatory activities.

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Business, Energy
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Stephen Haddrill
Chief Executive, Financial Reporting Council
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11 March 2019

Dear Mr Haddrill

As the Government publishes its response to Sir John Kingman's Independent Review of the Financial Reporting Council, I wish to act straight away on Sir John's second recommendation: to issue a 'remit letter' setting out policies to which the FRC should have regard when pursuing its objectives and duties over this financial year. I expect to send a further letter to you after we have completed our consultation on the regulator's proposed objective and duties.

High quality audit, corporate governance and financial reporting are vital to the success and continued growth of our economy. The confidence that shareholders, employees, investors and the wider public can place in company reports and audited accounts is dependent in part on the effectiveness of the regulatory framework.

I have accepted Sir John's recommendations to create a new independent statutory regulator, and the Government has published a consultation document which seeks views on several aspects of its operation and remit. It will require a programme of transformation for the FRC to transition into the new statutory regulator. While some of the changes will require legislation, many aspects of transformation can and should be undertaken or initiated in advance of legislation.

Taking forward those transitional steps should therefore be a priority for the FRC over this year. I welcome the commitment that the FRC has already made to work with my Department to deliver those changes over the coming months.

Trust in the sector has been damaged by recent failures. Whilst these reflect a minority of companies and audits, it is important that when standards and requirements are not met, specific and thematic concerns must be dealt with, including through continued cooperation with other regulators. Action may also be needed to ensure that auditors understand the expectations on them. Inspection and enforcement should therefore remain clear priorities for the FRC. Following recent evidence given to the BEIS Select Committee by audit firms, I would encourage the FRC to take steps to ensure that audit firms are correctly applying audit standards in relation to fraud.

STRATEGIC PRIORITIES

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In relation to the FRC's existing areas of work, I expect the FRC to continue to discharge its existing statutory and non-statutory functions which together serve to promote transparency and integrity in business.

- As the competent authority for Statutory Audit in the UK, the FRC should continue to set auditing and ethical standards and to monitor and enforce audit quality.
- The FRC should also continue with its work relating to the UK Corporate Governance and Stewardship Codes and UK standards for accounting and actuarial work.
- It should continue to monitor and take action to promote the quality of corporate reporting.
- The FRC should continue to operate independent enforcement arrangements for accountants and actuaries as well as providing some oversight, by arrangement, of those professions' membership bodies' regulation of their members.

Where these matters overlap with recommendations of the FRC Review, the CMA's study, and Sir Donald Brydon's Review of audit quality and effectiveness, my expectation is that the FRC will work closely with the review teams and with my Department in order to consider the timing and ensure the coherence of any action taken. Naturally, such a commitment to engagement extends to the direction of the FRC's work, and not to individual matters of its regulatory operation.

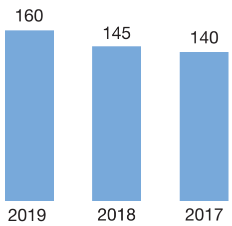
I am grateful to the hard-working staff of the FRC for their continued commitment, and to the FRC's leadership for its engagement in the programme of change we are embarking on.

Yours sincerely

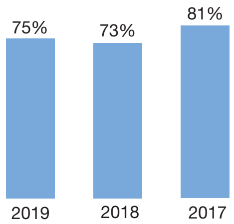
THE RT HON GREG CLARK MP
Secretary of State for Business, Energy & Industrial Strategy

Promoting high quality audit and assurance

KPIs



Total number of reviews



Proportion of Audits of FTSE 350 reviewed as requiring no more than limited improvements (assessed by our monitoring programme)

Key priority 2018/19

Drive improvements in audit quality, including through implementing a new approach to the monitoring and supervision of the six largest audit firms, reviews of firm-wide audit quality processes, thematic reviews, and reviews of audit engagements, focusing on areas of high risk.

Performance in 2018/19

The results of our audit quality reviews show that, whilst at some firms there has been an improvement in audit quality, this is not seen consistently, the overall level of audit quality has only marginally improved and has not met our target of 90% requiring no more than limited improvements.

We announced our plans for AFMAS in April 2018, we are recruiting staff for this function and expect it to make a greater impact in 2019/20.

We issued two thematic reviews this year on Audit Culture and Other Information in the Annual Report. The report on culture looks at firms' actions to establish, promote and embed a culture committed to delivering high quality audits. It identified elements of good practice and areas that required greater attention from the firms.

Key priority 2019/20

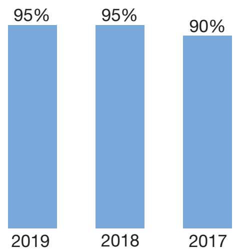
Use our powers to set auditing standards and monitor and supervise auditors to drive a step change in audit quality. This will include a focus, alongside our audit inspections, on the audit improvement programmes put in place by firms, further development of our AFMAS supervision work, and a continuing programme of work to enhance auditing and ethical standards. We are revising our target for audit quality reviews.

Link to our remit

As the competent authority for Statutory Audit in the UK, the FRC should continue to set auditing and ethical standards and to monitor [...] audit quality.

Promoting corporate governance and investor stewardship with a long-term focus

KPIs



Proportion of FTSE 350 companies reporting compliance with all, or all but one or two of the Code's provisions

Key priority 2018/19

Finalise the revised UK Corporate Governance Code and consult on a revised UK Stewardship Code.

Performance in 2018/19

The revised UK Corporate Governance Code was issued in July 2018, to be effective for accounting periods beginning on or after 1 January 2019. It places greater emphasis on relationships between companies, shareholders and stakeholders.

In January 2019 we issued a consultation on a revised UK Stewardship Code, which aims to increase demand for more effective stewardship and proposes more rigorous reporting of outcomes.

Key priority 2019/20

Promote corporate governance and investor stewardship that contribute to trust in business. This will include extending our monitoring of practice and reporting on corporate governance and our update to the UK Stewardship Code.

Link to our remit

The FRC should continue with its work relating to the UK Corporate Governance and Stewardship Codes.

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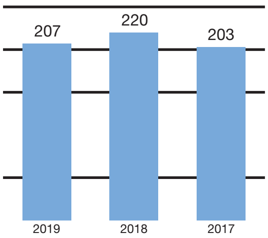
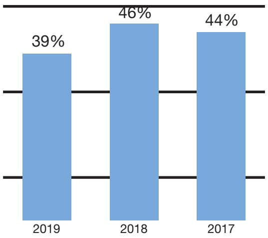
Promoting true and fair reporting

KPIs



Total number of reviews



Proportion of companies additional explanation and information was sought from

Note: the comparative for 2018 has been revised as reviews were completed after the annual report was issued.

Key priority 2018/19

Continuous improvement in corporate reporting through our monitoring of annual reports and accounts (with a focus on how companies are implementing the new IFRS on revenue, financial instruments and leases), the use of thematic reviews and Financial Reporting Lab projects.

Performance in 2018/19

Our Annual Review of Corporate Governance and Reporting 2017/18 issued in October 2018 highlighted areas for improvement in corporate reporting.

We undertook 207 reviews this year, including those forming part of our thematic reviews, and we have started, on a quarterly basis, publishing the names of companies reviewed.

Further explanation and information was sought from 39% of companies reviewed. This year we issued no Press Notices and 3 FRC references were required by companies (2018: 1 and 15 – the comparatives have been revised as reviews were completed after the annual report was issued). A number of 2018/19 reviews are still ongoing and these numbers could rise. Virtually all of our queries led to some degree of change or improvement in companies' reporting.

Our Financial Reporting Lab issued reports this year on business model and risk and viability reporting, performance metrics and digital developments.

Key priority 2019/20

Monitor and take action to promote the quality and usefulness of corporate reporting. This will include increasing the planned number of corporate reporting reviews we undertake and our major project on the future of corporate reporting.

Link to our remit

[The FRC] should continue to monitor and take action to promote the quality of corporate reporting.

Effective enforcement

KPIs

Complete investigations within two years (from the date on which our Conduct Committee decides to investigate until a Proposed Formal Complaint or Initial Investigation Report is made, or the case is closed).

Increasing the speed of our investigations continues to be a key priority, and we are improving our performance in this area. Factors beyond our control may impact upon the speed at which we can act. Further reporting on timeliness will be included in our Enforcement Annual Review.

Key priority 2018/19

Ensure that our enforcement action continues to be robust, proportionate and timely.

Performance in 2018/19

We have invested significantly in our enforcement work, partly in response to an increased case load, and will continue to do so.

We have concluded a number of cases this year with significant sanctions levied, including fines and non-financial penalties. In concluding the case against PwC in relation to BHS Limited the largest fine ever awarded by the FRC was levied, at £10.0m, reduced to £6.5m for early settlement, in addition to a suite of non-financial sanctions.

Key priority 2019/20

Use our enforcement powers effectively. This will include continuing to expand our Enforcement team to provide timely and effective enforcement action to encourage improvements in the quality of audit and financial reporting.

Link to our remit

As the competent authority for Statutory Audit in the UK, the FRC should continue to […] enforce audit quality.

The FRC should continue to operate independent enforcement arrangements for accountants and actuaries.

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Promoting high quality actuarial work

Key priority 2018/19

Continue to influence effective monitoring of actuarial work by the actuarial profession.

Performance in 2018/19

The FRC has no statutory powers in this area. We have continued to work with the Institute and Faculty of Actuaries (IFoA) on its monitoring programme. After a public consultation on its proposals the IFoA has announced next steps including proceeding with thematic reviews.

As the IFoA is still considering aspects of its monitoring programme it is taking time to become operational.

Not a key priority in 2019/20

We will continue to oversee the IFoA's planned approach to monitoring the quality of actuarial work.

Operating effectively and efficiently

KPIs

Financial

Operate within resources, breaking even after planned contributions to reserves

	2018/19 £'000	2017/18 £'000	2016/17 £'000
Surplus for the year	1,787	3,852	2,525
Planned contribution to reserves	–	(700)	(1,100)
Surplus after planned contribution to reserves	1,787	3,152	1,425

We have revisited our target for holding reserves representing six months operating costs, and we will not plan to allocate additional resources to general reserves. As a public body, cash representing our existing reserves can only be deployed with Government consent.

Employee engagement and view of FRC leadership

We are not able to report on this KPI this year as our annual staff survey was not carried out. Going forward we will carry out our survey in the autumn with BEIS and its partner bodies.

Key priority 2018/19

Further develop our culture of high performance, in which we develop people to be decisive, speedy, firm and fair, as well as engaged with a broad set of stakeholders.

Performance in 2018/19

These principles have remained key aspects of our culture throughout the year. However, specific FRC-wide action to further develop our culture has been limited this year in the light of the *Independent Review of the Financial Reporting Council*. Nevertheless our regulatory work has aimed to be speedy, firm and fair and we have engaged with a broad set of stakeholders on various project such as the UK Corporate Governance Code and the Future of Corporate Reporting.

Key priority 2019/20

Support the transition to the ARGA. This will include investing in the staff and supporting IT and other systems necessary to deliver our regulatory responsibilities effectively.

Link to our remit

Taking forward those transitional steps [to the new statutory regulator].

STRATEGIC PRIORITIES

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UK's exit from the EU

Key priority 2018/19

Help ensure the UK is positioned to maintain high standards of accounting by contributing to the development of the framework for any UK endorsement process for international accounting standards.

Performance in 2018/19

We have been working with BEIS on the establishment of the UK IFRS Endorsement Board. The Secretary of State will appoint the chair of the Board. The Board will be accountable to the Secretary of State for its decisions, and the FRC Board will monitor the due process.

Key priority 2019/20

Ensure an effective regulatory framework following EU exit. This will include our role in relation to the UK IFRS Endorsement Board and adding capacity to assess and register EU auditors of entities listed in the UK.

Link to our remit

No explicit link, but this forms part of our role as Competent Authority. In addition, the role of the FRC in relation to the UK IFRS Endorsement Board will be set out in legislation.

International influence

Key priority 2018/19

Work closely with international organisations and regulators in other jurisdictions (including through IFIAR) to promote high quality IFRSs and auditing standards.

Performance in 2018/19

This year we have continued to work with a number of international organisations and regulators to influence developments in corporate reporting and auditing. For example, one of our staff is a Board member of the IAASB, where we encourage improvements in auditing standards. We are also on the Board of IFIAR.

In relation to IFRS we actively participate in EFRAG at Board and TEG level and have recently been appointed to the IASB's Accounting Standards Advisory Forum.

We have also expanded our outreach with overseas investors.

Not a key priority in 2019/20

We will continue to aim to work effectively with fellow regulatory authorities and standard-setters around the world.

ENGAGING WITH STAKEHOLDERS

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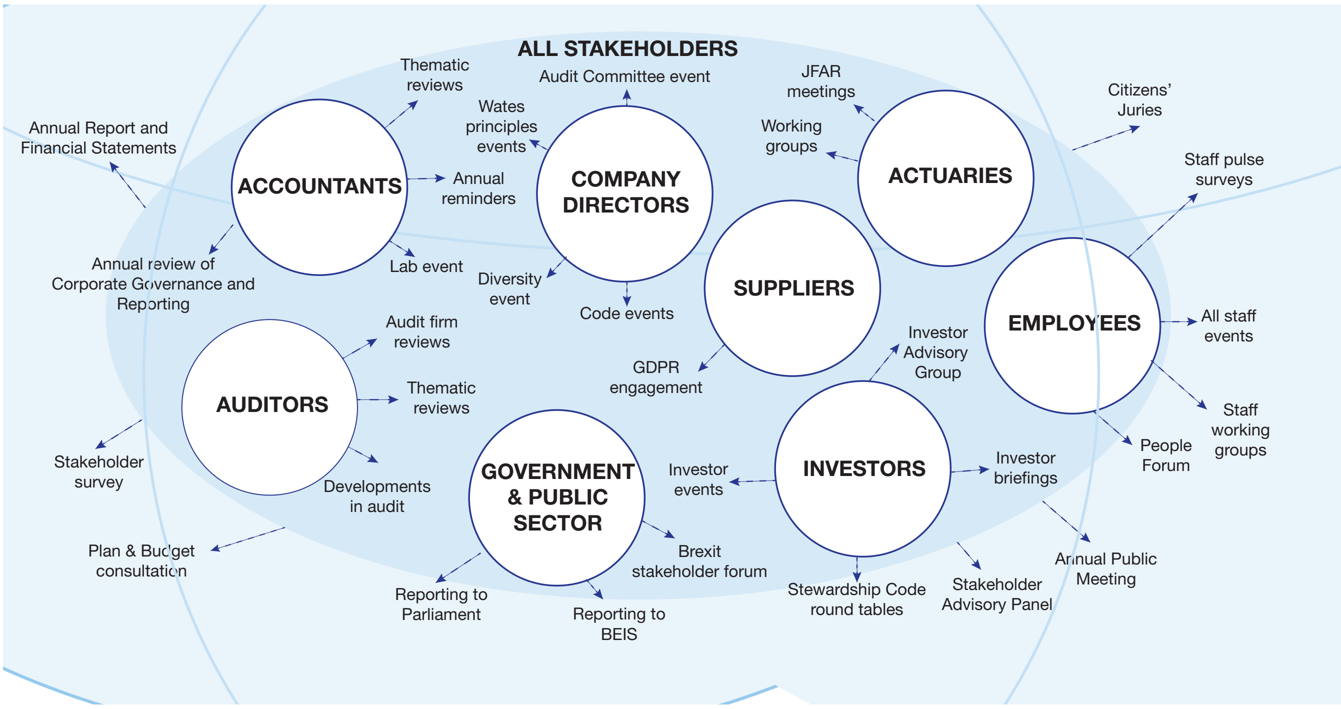
Working with a wide range of stakeholders and listening to their views is very important to us and is a crucial part of ensuring that we are properly acting in the public interest. It provides us with evidence to inform our decision-making in developing and maintaining Codes, Standards and guidance, and information about risks, concerns and challenges relevant to our regulatory frameworks.

The ways in which we listen to stakeholders include public events, our Stakeholder Advisory Panel, our Investor Advisory Group, meetings with individual or smaller groups of stakeholders and formal and informal consultations on our activities and proposals. As well as events in London, we have held, or participated in, more regional events throughout the UK this year as well as webinars and podcasts, which can be accessed anywhere.

We consult formally on our Plan & Budget each year, and hold a Public Meeting about our priorities. We also consult formally on new, or amendments to, Codes, accounting, auditing and actuarial standards and aspects of our procedures. Informal consultation enables us to obtain wider views on various topics that will inform current and future policy development. This year we have also held a series of three Citizens' Juries (one of which took place after the year end), to provide greater insight into the views of members of the public regarding our work and our areas of regulatory responsibility. We will publish a report of the outcomes during 2019/20, but the citizens were aligned with the *Independent Review of the Financial Reporting Council* in calling for enhanced powers to hold companies to account whilst also working with them to promote best practice, in the public interest.

When analysing consultation responses we categorise respondents by type, for example, users, preparers, professional bodies, accounting firms, etc, which enables us to consider whether the views of all stakeholders are aligned, or whether certain types of respondent hold alternative views and we can consider the impact on different stakeholders as part of our decision-making. Feedback statements provide stakeholders with information about how their views have been taken into account in finalising requirements.

We would like to thank all stakeholders that have been involved in our work and engagement activities, including members of our Committees, Councils, Advisory Groups and other forms of engagement, for their contributions.



RISK MANAGEMENT

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The Chief Executive and the Board have responsibilities for managing risk. The Chief Executive is responsible for ensuring risk is managed effectively and, as the Accounting Officer, in accordance with the requirements set out for public bodies in *Managing Public Money* issued by HM Treasury. The Board's responsibilities include setting the risk appetite and the risk tolerance boundaries in which it is managed, and, supported by the Audit Committee, in ensuring the effectiveness of risk management. The focus is on managing risks to the FRC achieving its mission and remit of promoting transparency and integrity in business.

Over the last year, the risk environment has changed considerably. The collapse of a number of companies, corporate scandals, and major concerns over audit quality and the independence of auditors have seriously challenged the credibility of the UK corporate governance regime, including the 'comply or explain' approach, and the FRC's regulatory framework, two of our principal risks. This and heightened societal concern over corporate behaviour and audit prompted the Government to commission the *Independent Review of the Financial Reporting Council*. The Review has recommended inter alia that the FRC be replaced by a new ARGA founded on a much firmer statutory basis and with much more wide-ranging powers than the FRC has, and staffed and funded accordingly. The Government has proposed to adopt this and other recommendations of the review and is currently consulting on these. The recommendations of the review and their implementation impact on the FRC's risk environment and mitigations.

Additionally, the CMA has reviewed the structure of the audit market and has proposed significant change to its operation; the BEIS Select Committee has issued a report on The *Future of Audit*; and the *Independent Review into the Quality and Effectiveness of Audit* by Sir Donald Brydon (the Brydon review) is ongoing.

The changes being developed in the regulatory regime present considerable opportunity for the FRC and its successor to serve the public interest more effectively, in particular to create better informed markets for investors and boards that are better equipped to drive long-term growth. Risks include the challenge of recruiting for a significant number of new posts in a tight labour market, whilst retaining existing staff when morale is being impacted by a variety of changes and uncertainties, and the uncertainties about the timing of legislation to bring about the proposed new body. The risks from poor management of change are potentially significant, including in terms of damage to the UK as a place to invest, to the operation of markets, and to the strength of the accounting and audit professions.

Notwithstanding the prospective changes referred to above, the FRC continues to use its powers and its influence to improve corporate governance, stewardship, corporate reporting and audit as set out elsewhere in this Annual Report. This includes the revisions to the UK Corporate Governance Code and the Stewardship Code to increase the focus by boards and investors on outcomes; the more intrusive Audit Firm Monitoring and Supervision regime; expanded audit quality reviews and a systemic review of one firm; the increased number of investigations into audits which follows the changes to the misconduct test in 2016/17 and the pursuit of failings identified through our audit quality reviews; and the application of tougher sanctions for poor work. We are also consulting on revised standards for auditors on Ethics and on Going Concern work.

The Directors (including the Chief Executive as Accounting Officer) have carried out a robust assessment of the principal risks and these developments in the risk environment are reflected in the FRC's principal risks and mitigation.

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PRINCIPAL RISK	MITIGATION	DIRECTION OF RISK TREND
The framework in which we operate fails sufficiently to deter or address misconduct or inadequate diligence by directors, professionals and professional bodies, leading to a loss of public confidence in the regulatory regime.	Our monitoring of audit and financial reporting, together with our oversight of the professional bodies' regulation of their members, is a tool for both identification and deterrence. During 2018/19 we have expanded the number of audit quality reviews that we undertake. We operate enforcement procedures that enable us to investigate and take enforcement action against audit firms and members of the accountancy and actuarial professions. During 2018/19 we have taken on more cases and imposed tougher sanctions and fines through tribunals. We are also consulting on revised standards for auditors on going concern work. On Ethics we have issued a position paper as part of a post implementation review. The FRC has limited powers in relation to directors, but our enforcement powers do extend to company directors who are chartered accountants or actuaries.	↓ Significant company failures, major concerns over the quality of audits and the independence of auditors, and 2017/18's deteriorating results from our audit quality reviews have shaken confidence in the efficacy of the regulatory framework. The establishment and timing of a more powerful regulatory structure as recommended by the *Independent Review of the Financial Reporting Council* is subject to legislative and political uncertainty.
FRC fails to retain, recruit and motivate high quality people to pursue its mission and deliver its regulatory responsibilities.	We have developed a long-term reward strategy as well as formal appraisal, career development and training programmes. We are communicating the roles and career opportunities that should be available within the proposed more powerful regulator, and on the importance of the regulatory activities currently undertaken and in transition. We are reviewing our well-established recruitment processes to ensure they continue to support effective and timely recruitment, and integration of new employees into the FRC.	↓ The FRC's status as a public body means the Public Sector Pay Guidelines now apply, which may impact our ability to recruit and retain high quality people, including professional technical staff at a time when the firms are also increasing recruitment in similar areas. The challenges of transitioning to the ARGA may also affect retention and recruitment.

KEY

N New Principal Risk — ↑ Improving

↓ Worsening — → Static

RISK MANAGEMENT

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PRINCIPAL RISK	MITIGATION	DIRECTION OF RISK TREND
Credibility of the UK Corporate Governance regime, including the 'comply or explain' approach, is compromised by poor or ineffective governance or reporting thereon by directors and insufficient engagement and stewardship by investors.	During 2018/19 we introduced a revised *UK Corporate Governance Code* and its associated guidance, which is effective from 1 January 2019. It is shorter, sharper and takes account of the needs of wider stakeholders including the workforce. In 2019/20 we are expanding our corporate reporting reviews to include practice and reporting on corporate governance. We also publish the *UK Stewardship Code*, to which many investors are signatories, which sets standards for investor engagement with companies to promote challenge and to hold directors to account. We scrutinise and report on the quality of reporting against the Stewardship Code and de-list signatories that fall short of the standard required. During 2018/19 the FRC consulted on a revised Stewardship Code that focuses inter alia on more rigorous reporting on stewardship activities and the outcomes achieved. We participated in the Coalition Group that issued the *Wates Corporate Governance Principles for Large Private Companies*. New legislation requires large private companies to provide a statement on corporate governance arrangements. It remains to be seen how effective the Wates Principles will be in improving corporate governance in large private companies.	Significant company failures and scandals and high executive remuneration have shaken public confidence in the ability of investors and the 'comply or explain' regime to deliver the trustworthy behaviours expected of companies.

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PRINCIPAL RISK	MITIGATION	DIRECTION OF RISK TREND
The quality of audit work by major audit firms falls below the high standards expected because of a failure to comply with auditing standards, shortcomings in firms' governance or culture, or a failure to invest in their audit function.	We have powers as UK Competent Authority for audit. We set UK auditing standards and help develop and adopt international auditing standards, and we publish the Audit Firm Governance Code. We select each year a number of audits and review aspects of them, including particular themes across audits. We report publicly each year on our findings individually in respect of the more significant audit firms and in aggregate. We also promote continuous improvement in standards of auditing through our role in overseeing the audit professional bodies. We have introduced a voluntary supervisory regime in the form of the Audit Firm Monitoring and Supervisory Approach, which enables us to assess firms' controls against systematic deficiencies within a major audit firm. We work with auditors, audit committees and investors to highlight good practice and advocate continuous improvement in the effectiveness and quality of audit, including through the use of data analytics and technology. After the disappointing results of our 2017/18 audit quality reviews, which we published in June 2018, and some significant corporate collapses, we have expanded the number of reviews undertaken and have commenced a more detailed evaluation of the auditing quality of one firm in particular. We have also issued proposed revisions to the standard on auditing the going concern assumption. We take enforcement action against individuals and firms when it is believed that audit work may breach the required standards. Following the change in 2016/17 of the serious misconduct test to a lesser test of breach of relevant requirements, together with the corporate collapses and deterioration in audit quality noted above, we are investigating significantly more cases and are applying tougher sanctions.	→ The most recent results of our audit quality reviews, published in July 2019, show that in 2018/19 the overall quality of audits has yet to improve. There is considerable focus on raising audit quality and pressure on the firms to do so, not only from the step up in our monitoring and enforcement activities but in the recommendations from the *Independent Review of the Financial Reporting Council* on the regulatory framework and the recent study by the CMA into the audit market and the BEIS Select Committee on *The Future of Audit*.

RISK MANAGEMENT

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PRINCIPAL RISK	MITIGATION	DIRECTION OF RISK TREND
Audit market is severely disrupted by the failure of an audit firm or their withdrawal from all or part of the market.	Our oversight regime is designed to promote high quality audit work, strong ethical standards and effective risk management, and to address shortcomings. During 2018/19, this oversight was enhanced by the introduction of the more extensive AFMAS regime. We require each of the major firms to have contingency plans in place that would minimise the impact on the quality of audit in the event of a failure, and we work with firms and other regulators on scenario testing. As a problem might not originate in the UK, our work in this area includes consideration of network risk. However, we have no locus in relation to the international networks, although firms are required to notify us of major risks arising elsewhere in their network. Through the IFIAR international regulators forum, we are expanding considerations of wider audit firm network risk. We have conducted detailed reviews of the UK firms' contingency planning and made recommendations. We are considering the CMA's recommendations in relation to mitigating the effects of the distress or failure of a Big 4 firm.	↓ There is greater uncertainty given the pressures on the industry from recent audit failings and the regulatory and governmental response, including proposals for structural changes to the market from the CMA and from what may emerge from Brydon review. Political uncertainty could also significantly alter the timing and content of the proposed regulatory structure in the UK.
FRC policy and standards, including those designed to replace current EU regulation, are misguided or ineffective.	We base our overall regulatory approach on the principles of good regulation – including rigorous impact assessment. We consult widely and publicly on both our strategic priorities and our regulatory proposals and publish the feedback and how this has been taken into account in our decision-making. Our Codes and Standards are subject to detailed review and consultation at least every five years and each year improvements in some areas are proposed/made. Our Financial Reporting Lab helps promote understanding of investors' views and develop best practice in reporting. We maintain close relationships with BEIS in order to understand the Government's priorities and enable us to respond accordingly, including preparation for EU exit. We engage through our existing networks of international standard-setters and regulators to maintain our influence internationally and learn from experience elsewhere.	→ The consensus built around the FRC's regulatory approach has been superseded by the proposed move to the new regulatory authority. Policies and standards will be subject to review by the new authority. These and changes made to replace EU regulations are subject to political uncertainty.

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PRINCIPAL RISK	MITIGATION	DIRECTION OF RISK TREND
Decisions based on the work of actuaries are ill-founded due to a failure of such work to meet the professional standards expected.	Together with the IFoA, Prudential Regulation Authority, Financial Conduct Authority and The Pensions Regulator we are members of the Joint Forum on Actuarial Regulation, which is a unique collaboration between regulators to coordinate, within the context of its members' objectives, the identification of and response to public interest risks to which actuarial work is relevant. The FRC issues technical actuarial standards which the IFoA requires its members to follow in carrying out their actuarial work. We oversee the IFoA's regulation of its members. The IFoA is developing a monitoring framework for actuaries' work.	↓ The IFoA's monitoring regime is taking time to become operational and the FRC has no statutory powers in this area. *The Independent Review of the Financial Reporting Council* recommended that the FRC's oversight role in relation to the work of actuaries be transferred to a public body more directly involved with such work. There is uncertainty as to whether, how or when this recommendation will be implemented.
FRC fails to maintain data privacy and to prevent unauthorised access to confidential information, including through cyber-attack.	We have information security policies and procedures in place, and we provide regular training to all staff. We regularly test the effectiveness of our network security and data handling and continue to invest when needed. The FRC's information security policies were updated ahead of the new General Data Protection Regulation (GDPR) in May 2018.	→ Obtained Cyber Essentials Plus accreditation, which provides independent verification of our systems and processes.
The FRC's directors and/or staff are, or are perceived to be, too close to those we regulate or to be otherwise conflicted, or to be insufficiently diverse.	Our consitutional requirements, Codes of Conduct, policies for registering interests and gifts and other working practices are designed to avoid real and perceived conflicts. There are specific requirements for Board members, Conduct Committee members and staff to ensure their independence from the entities they regulate. Our Board, the Committees and Councils, are drawn from a range of backgrounds and bring diverse experience to our deliberations and decision-making. This is an area of continuing focus.	↑ The FRC's Articles of Association have been amended and the Secretary of State will now make Board appointments. New appointments are in progress.

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PRINCIPAL RISK	MITIGATION	DIRECTION OF RISK TREND	
The establishment of ARGA is subject to legislative delays or recommendations of the *Independent Review of the Financial Reporting Council* are not implemented such that the proposed step up in regulatory powers and effectiveness is delayed or diminished.	We are working closely with BEIS to support the creation of the new authority and the implementation of the Review's recommendations, including the early adoption of those recommendations that do not require legislation. We and BEIS will closely monitor and manage implementation through a Joint Project Board. A communications plan is being developed to ensure that our stakeholders are kept informed of direction and progress.	N	The changes flowing from the recommendations of the *Independent Review of the Financial Reporting Council* are profound, are subject to political uncertainties and represent a significant implementation challenge.

MANAGING COMPLAINTS

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The FRC undertakes several functions to ensure confidence in the integrity and conduct of professional accountants and actuaries, the quality of corporate reporting and the quality of auditing in the UK, and to support the FRC's mission of promoting transparency and integrity in business. Evidence available outside the FRC may be relevant to our work and we welcome such information from the public either through a formal complaint or an informal enquiry.

Complaints that fall within our regulatory remit are considered by our:

- **Corporate Reporting Review Team**, which is responsible for reviewing accounts of listed companies, UK AIM quoted companies, large private companies and limited liability partnerships, to determine whether they have complied with relevant accounting and reporting requirements, as set out in the Companies Act 2006 (the Act);
- **Enforcement Division**, which conducts investigations and will bring prosecutions, if appropriate, against auditors, accountants, accountancy firms, and actuaries where there appears to be misconduct or a breach of the relevant professional standards; or
- **Professional Oversight Team**, which provides independent oversight of the professional accountancy and actuarial bodies and can consider the way a body has handled a complaint that was made to it.

In summary the action taken in respect of the complaints considered by the FRC during 2018/19 was:

CORPORATE REPORTING REVIEW

Corporate Reporting Review received 28 complaints related to corporate reporting matters during the year of which:

- 15 related to financial statements reporting matters. These were in respect of a wide range of issues including impairment, the accounting related to particular transactions, measurement and valuation issues, and disclosures. Of these 15, improvements to future reporting have been made (or agreed to) in five cases (and in one case explicit reference to the FRC involvement was required to be made by the company in its subsequent accounts). Seven cases are still in progress.
- Eight related to information provided in the Strategic Report (four on climate risk reporting), all of which have now been closed. Improvements to future reporting have been secured (or agreed to) in respect of five of these cases.
- Five were not followed up as there was insufficient merit to pursue or they were otherwise outside our scope.

The complaints came from a diverse range of parties (including investors, fund managers, journalists and academics) and have involved companies that have ranged from private and small AIM companies to very large FTSE 100 groups.

ENFORCEMENT

Enforcement opened eight complaint cases this year (one of which was a whistleblowing disclosure).

The following is a summary of 11 complaint cases closed during the year:

- one case resulted in action by the FRC, in terms of making enquiries, and this case was resolved through constructive engagement (without finding any breaches by the audit firm);
- seven cases were closed with no further action taken, where there was no basis to support the complaint; and
- three matters were referred on to an RSB or other regulator (including two to the Insolvency Service).

PROFESSIONAL OVERSIGHT

This year Professional Oversight received 56 complaints about the professional accountancy and actuarial bodies we oversee, of which:

- 19 complaints were within our remit, of which two matters are still currently under review, and of the 17 complaints no recommendations were made to the professional accountancy and actuarial bodies in relation to their enforcement and complaints procedures; and
- 37 matters were outside our complaints handling remit and/or the complainant had not first exhausted the professional accountancy body's or actuarial body's complaints procedure.

This year the FRC has seen an increase in the volume of complaints being received from student members in relation to examination procedures at the accountancy bodies, although no trends have been identified across the range of complaints received.

Additional information on our oversight activities can be found at Appendix 1 of this report.

MANAGING COMPLAINTS

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WHISTLEBLOWING TO THE FRC AS A PRESCRIBED PERSON

Public Interest Disclosures
Whistleblowing is the term used when a worker passes on information concerning suspected or known wrongdoing by their employer (it is also known as 'making a disclosure'). The Employment Rights Act 1996, as amended by the Public Interest Disclosure Act 1998 provides the legal framework for protecting workers from harm if they blow the whistle. The purpose of a prescribed person is to provide workers with a way of whistleblowing to an independent body that may be able to act on those concerns.

The FRC is a prescribed person and as such, individuals working outside the FRC, but in the accounting or actuarial professions, may get in touch with the FRC if they want to make a disclosure about their employer in relation to matters which are with the scope of the FRC's regulatory duties.

During 2018/19 the FRC received 16 disclosures in its capacity as a prescribed person. In respect of the disclosures made, the following action was taken:

- four were referred to the relevant professional accountancy body for consideration;
- seven were referred to another regulator or organisation for consideration;
- four were of direct relevance to the FRC's responsibilities and were addressed or are being considered by the relevant team(s); and
- one did not respond to requests for further information.

The FRC's whistleblowing policy can be found here: https://www.frc.org.uk/about-the-frc/whistleblowing

COMPLAINTS ABOUT THE FRC

During 2018/19 we received new complaints under the FRC Complaints Procedure (which deals with complaints from those who are unhappy or dissatisfied about the way the FRC has exercised its functions) from seven complainants, some of which raised multiple complaints.

Concerns were raised regarding:

- the efficacy of FRC's oversight in relation to the IFoA, the ICAEW and the ACCA;
- the time taken or the lack of communication provided to individuals referring matters to our Corporate Reporting Review Team; and
- the FRC's response to references in published material regarding the potential subjects of an enforcement investigation.

Of the complaints received this year, full responses have been provided to six of the complainants and correspondence with the seventh complainant is under consideration. In two cases, relating to our handling of complaints in relation to the professional bodies, the complaints were partially upheld, and in one case it was accepted that the complaints outcome letter was not as clear as it might have been. The other complaints were not upheld. One case has been referred to the Independent Complaints Reviewer.

During the year we also concluded correspondence with five complaints from the previous year. The complaints were not upheld but improvements for the future were identified including giving complainants sufficient information on how their complaint will be considered from the outset so that they can be satisfied that the process is fair and appropriate. In two instances, referrals were made to the Independent Complaints Reviewer but the complainants subsequently decided not to pursue their referral.

This year, as in previous years, the majority of complaints received under the FRC Complaints Procedure, concern the Professional Oversight Team's review of complaints regarding the professional bodies and in particular, dissatisfaction with the FRC's inability to undo or overturn a substantive finding by a professional body. Our complaints processes make clear that our present arrangements with the professional bodies in question do not allow us to act as a route of appeal against their substantive decisions and that the scope of oversight reviews is limited to reviewing those bodies' complaints-handling.

A significant review of the FRC's complaints handling is underway, which also addresses specific recommendations made in the *Independent Review of the Financial Reporting Council* and steps are being taken to centralise and better resource complaints handling within the FRC with the aim of providing consistent complaints handling practices as appropriate, timely and effective outcomes and to facilitate transparent and regular reporting of trends, outcomes and turnaround.

FINANCIAL REVIEW

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Each year we consult publicly on our budget and funding requirements. We aim to operate efficiently and effectively and make sure we follow the principles of *Managing Public Money*. In setting our budget, we seek to recover the costs we expect to incur in carrying out our role and responsibilities and achieving our strategic objectives. Our target for 2018/19 was to break even so that our funders are contributing no more than what is required, although in recent years we have sometimes budgeted to increase reserves in order to mitigate possible detrimental scenarios.

SURPLUS FOR THE YEAR

	2018/19 £'000	2017/18 £'000
Surplus for the year	1,787	3,852
Planned contribution to reserves	–	(700)
Surplus after planned contribution to reserves	1,787	3,152

During 2018/19, the FRC generated a £1.8 million (2017/18: £3.2 million after planned contribution to reserves) surplus primarily resulting from an underspend in core operating costs.

EXPENDITURE

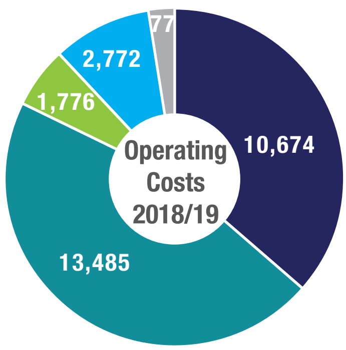
Overall expenditure for the year was £28.8 million (2017/18: £31.7 million) of which £28.7 million (2017/18: £28.2 million) relates to core operating costs, the costs of Corporate Governance & Reporting, Audit & Accountancy Regulation, Actuarial Standards & Regulation and Enforcement Core, as set out in the pie charts below. The remainder relates to case costs.

The budgeted enforcement case costs of £5.0 million was based on an estimate of the expected cost of accountancy cases after considering any costs awards. During 2018/19 the FRC recovered substantial costs for cases arising in earlier years. As a result the net cost was only £0.1 million after incurring case costs of £6.2 million and receiving costs awards of £6.1 million, part of which have been passed back to the relevant professional bodies.

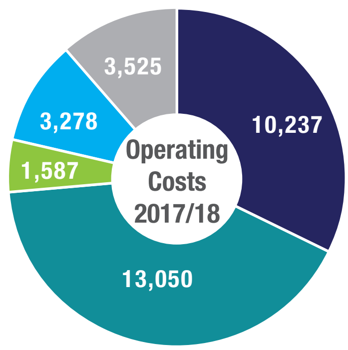
The budgeted core operating costs were £30.8 million and the actual underspend of £2.0 million in comparison to budget arose from factors including:

1. During 2018/19 a large proportion of the underspend was in staff costs. This was largely due to the difficulty of recruitment for our AFMAS team as well as delays in comparison to expected timelines for recruitment in our Corporate Reporting Review and actuarial teams. In addition, we started to implement a new pay structure, which included replacing our previous bonus scheme with the Values in Practice (VIP) recognition scheme, which is a more modest in-year award scheme.

Expenditure across our main areas of responsibility is shown below.



- Corporate Governance & Reporting
- Audit & Accountancy Regulation
- Actuarial Standards & Regulation
- Enforcement Core
- Accounting Case Costs



- Corporate Governance & Reporting
- Audit & Accountancy Regulation
- Actuarial Standards & Regulation
- Enforcement Core
- Accounting Case Costs

FINANCIAL REVIEW

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2. Value for money has been our primary focus and we have been able to achieve a reduction in spending of £0.2 million on travel and expenses. The implementation of a new Travel and Expenses policy follows the *Managing Public Money* principles and we have made sure everyone across the FRC adapted to those principles.

3. We have a long-term lease on our office building and we are in the final stages of planned rent review negotiations. Indications are that the rent agreement will be lower than budgeted and this has resulted in a further £0.2 million underspend.

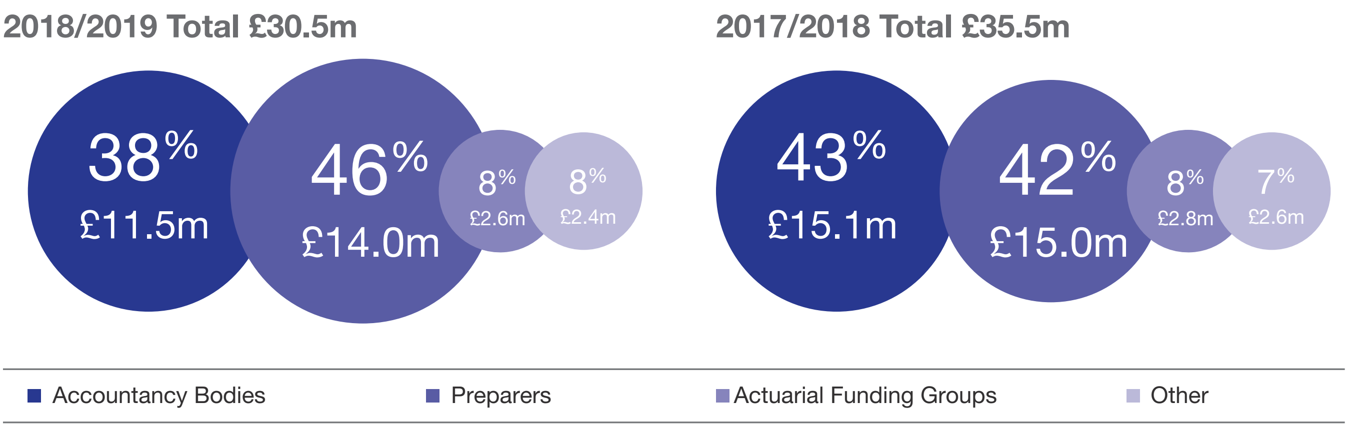
FUNDING

The FRC does not receive funding from the UK government. We are funded mostly by the accountancy and actuarial professions and from voluntary contributions from accounts preparers, insurance companies and pension schemes.

Other Income includes income from publications and electronic rights, and registration fees of Third Country Auditors.

During the 2018/19 year, the FRC received total funding of £30.5m from the following categories:

Funding



The decrease in funding from Accountancy Bodies is because of the recovery of substantial case costs arising in earlier years. As noted above, the budget for enforcement case costs was £5.0 million and the net cost after recoveries, requiring funding, was £0.1 million.

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FINANCIAL POSITION

The conclusion of a number of enforcement cases prior to the year end has had a significant impact on our reported financial position. When a case is concluded, and a fine is agreed and case costs are awarded, we recognise the amount due to the FRC as a debtor, and simultaneously recognise the amount payable to the relevant professional body as a creditor. Fines and costs awards are not paid over to the relevant professional body until they have been received by the FRC.

Towards the end of the financial year, there were around £1.4 million of fines and £1.0 million of costs awards that had already been finalised but had not yet reached our bank account and therefore appear in our Balance Sheet as at 31 March 2019 as debtors. There are £5.5 million of fines and £2.6 million of costs awards in creditors (£8.1 million in total) and, as a number of fines and costs awards were paid shortly before the year end, this includes £5.6 million cash received in March 2019 and paid to the relevant professional bodies in April 2019.

Reserves

The reserves of £15.8 million are mainly driven by a policy to build reserves as part of our risk management strategy and recent underspends, including £1.8m in 2018/19. As a public body, operating under a remit letter from BEIS, the potential impact of this risk has changed, as well as the controls over our spending; our existing reserves can only be deployed with Government consent. If funding is necessary for additional costs relating to the UK's exit from the EU and the implementation of the *Independent Review of the Financial Reporting Council*, it will be agreed with BEIS including the extent to which there is a contribution from the cash represented by General Reserves.

In compliance with *Managing Public Money* guidance, we have now opened a Government Banking Service (GBS) bank account. We transferred cash representing most of the Reserves into the GBS account post year end. The remainder is currently held as secured deposits and upon maturity, will be transferred over to the GBS account.

The Directors consider that the Strategic Report set out in pages 1 to 29 is fair, balanced and understandable and that it is comprehensive and contains the information necessary for the user to assess the position, performance, regulatory model and strategy of the FRC. It was approved by the Board of Directors on 4 July 2019 and signed on its behalf by:

STEPHEN HADDRILL
CHIEF EXECUTIVE OFFICER AND ACCOUNTING OFFICER

GOVERNANCE AND TRANSPARENCY

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THE BOARD IS COMMITTED TO HIGH STANDARDS OF GOVERNANCE AND CONSIDERS THAT THE PRINCIPLES OF THE UK CORPORATE GOVERNANCE CODE (APRIL 2016) PROVIDE AN APPROPRIATE FRAMEWORK ON WHICH THE FRC'S GOVERNANCE ARRANGEMENTS ARE BASED.

GOVERNANCE STATEMENT

The FRC is a public body, with a central government classification. The Chief Executive, as the Accounting Officer, is personally responsible for safeguarding the public funds under his control, for ensuring propriety and value for money in the handling of those public funds, and for the day-to-day operations and management of the FRC. The Board is responsible for the FRC's strategy and monitoring the implementation of that strategy. The FRC reports to the Secretary of State for Business, Energy and Industrial Strategy and Parliament on the discharge of its functions, and as a company, conforms to the requirements of the Companies Act 2006.

As the body responsible for the UK Corporate Governance Code (the Code) the FRC seeks to comply with the principles of the Code to the greatest extent possible and the Code provides the framework on which the FRC's governance arrangements are based. The FRC considers that it generally complies with the overall principles of the Code, as a public body and a company which is limited by guarantee and of which its Directors are its members, but this status drives the main areas of non-compliance.

Section B: Effectiveness

The Board has put in place mechanisms to assess the effectiveness of the Board and its Directors, including careful consideration of any proposed reappointments by the Nominations Committee and the Board (page 34 provides further detail). However, this year, as set out on page 37, a Board effectiveness review has not been carried out.

Directors are appointed for fixed terms, which may be renewed, rather than being submitted for re-election at regular intervals.

Section C: Accountability

The FRC's principal risks are set out on pages 19 to 24, and the Board has considered the FRC's risk appetite. However, as a public body with its remit and 'licence to operate' set by the Government, the FRC has not provided a viability statement assessing the FRC's prospects over the longer-term.

Section D: Remuneration

As a public body the role of the Remuneration Committee has changed, with the application of the Public Sector Pay Guidelines and greater oversight from BEIS, HM Treasury and the Cabinet Office in relation to remuneration decisions. As a result the Remuneration Committee has reduced responsibility for setting remuneration.

Section E: Relations with shareholders

As there are no additional requirements for engagement with shareholders, the FRC does not appoint a Senior Independent Director. However, the Deputy Chairman fulfils a similar role to a Senior Independent Director[4], the FRC undertakes an extensive engagement programme to ensure the views of its stakeholders are heard (page 17) and consults annually on its Plan & Budget.

Looking forward, all appointments to the Board will be made by the Secretary of State. The FRC is in transition to the ARGA and, in future years, expects to report compliance against public sector governance provisions eg *Corporate Governance in Central Government Departments: Code of Good Practice* issued by HM Treasury and the Cabinet Office, which should be suitably adapted for other parts of central government.

STEPHEN HADDRILL
CHIEF EXECUTIVE OFFICER AND ACCOUNTING OFFICER

4 When the new Deputy Chair is appointed, part of their role will be to act as the Senior Independent Director of the FRC.

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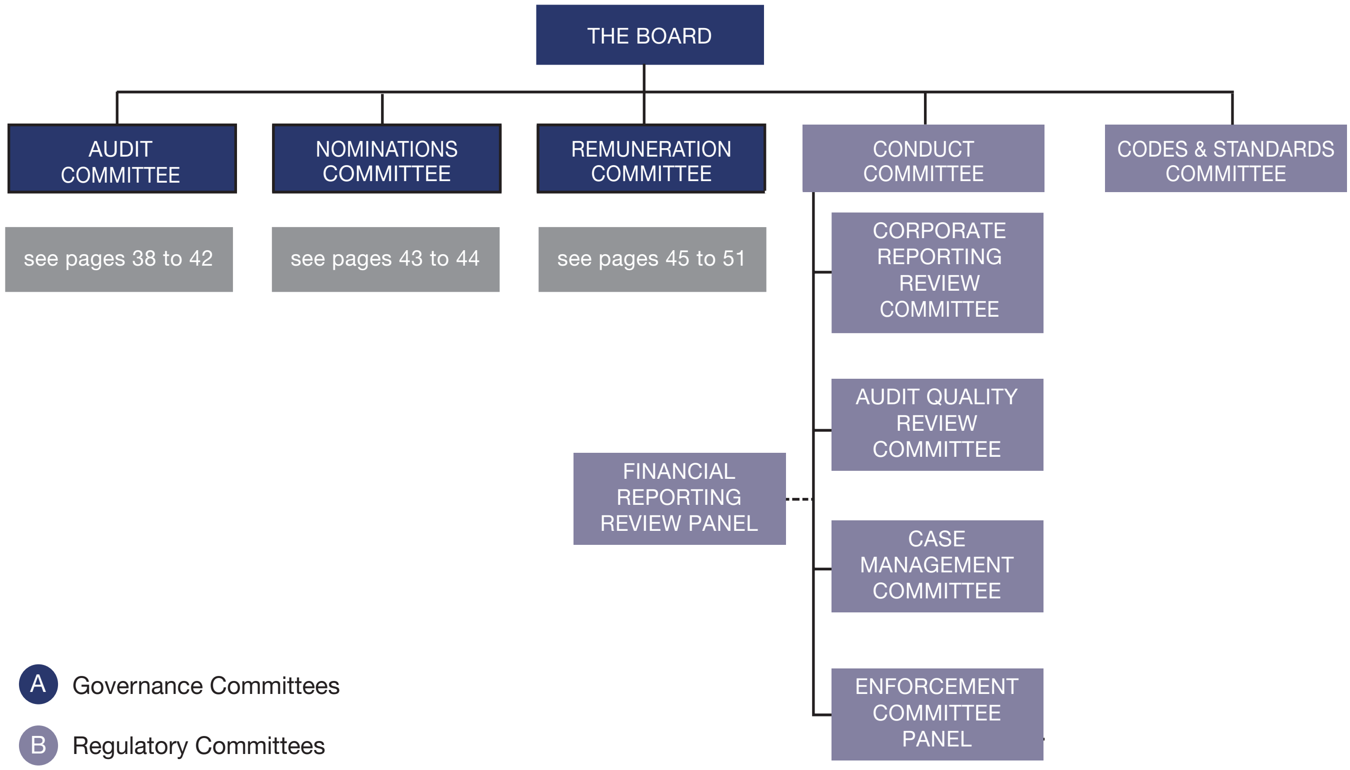
HOW WE ARE GOVERNED

Consistent with the Code, the FRC is headed by a Board which has collective responsibility for the strategic leadership of the organisation. The Board also sets the FRC values and culture, and ensures the FRC has the necessary financial, human and other resources to meet its objectives.

The Board is responsible for setting accounting, auditing and actuarial standards. It is not responsible for making enforcement decisions, but receives quarterly reports on progress with enforcement cases.



To support the efficient discharge of its functions and facilitate effective decision-making, the Board is supported by three governance committees and two regulatory committees. Sub-committees, panels and advisory councils are in place to support and ensure relevant information flow.

During 2018/19, the Board implemented a number of the recommendations relating to speed and agility of decision-making from a governance review carried out in the previous year; a key change was to limit the remit of the Codes & Standards Committee in relation to standard setting. The Committee's terms of reference were narrowed to advising the FRC Board on corporate governance matters, including proposed changes to the UK Corporate Governance Code and Stewardship Code.

The remainder of the 2017 recommendations were put on hold pending the outcome of the *Independent Review of the Financial Reporting Council* and, in the event, anticipated a number of its conclusions. When the new Chair joins the FRC later this year, one of their key priorities will be to review governance arrangements and to determine the changes to be made ahead of the transition into the new ARGA. The new regulator will have a smaller board and to this end, the FRC's Articles of Association have already been amended to remove the requirement that the minimum number of directors shall be 11.

GOVERNANCE AND TRANSPARENCY

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OUR BOARD MEMBERS

Sir Winfried Bischoff (N) (R)
Chairman

Appointed 1 May 2014

Experience:
Sir Winfried brings experience of leading international committees and boards, drawn from a range of sectors, including banking and capital markets, finance and government regulation and public policy.

Stephen Haddrill
Chief Executive

Appointed 16 November 2009

Experience.
Stephen brings experience in government and regulation. Prior to joining the FRC, he was Director General of the Association of British Insurers and before that Director General of the Department of Trade and Industry (DTI) fair markets group.

Sir Brian Bender (R) (N) (CC)

Independent Non-Executive Director

Appointed 1 March 2014

Experience:
Sir Brian brings experience of UK government, European policy and regulation and regulatory policy. His former roles include Head of the European Secretariat and Permanent Secretary in the Business Department and the Department for Environment, Food and Rural Affairs.

David Childs (N) **(CC)**

Independent Non-Executive Director

Appointed 1 May 2014

Experience:
As a former Global Managing Partner at Clifford Chance, David brings strong expertise in corporate law and regulation.

John Coomber (A) (R) (CSC) **(AC)**

Independent Non-Executive Director

Appointed 23 July 2015

Experience:
John brings insurance industry experience, in particular global reinsurance and UK pensions insurance. His previous roles include CEO and Non-Executive Director at Swiss Re. He was also a Director and CEO at Pensions Insurance Corporation. John is a member of the actuarial profession.

Olivia Dickson (CSC)

Independent Non-Executive Director

Appointed 2 July 2012

Experience:
Olivia brings non-executive remuneration, risk and audit committee experience from a variety of roles in the private sector. She also has experience in regulation, both financial services and pensions, and particular expertise in sustainability reporting and impact investing.

Key to Committees / Councils
(A) Audit (N) Nominations (R) Remuneration (CC) Conduct (CSC) Codes & Standards
(AAC) Audit & Assurance Council (CRC) Corporate Reporting Council (AC) Actuarial Council
Bold denotes Chair of the Committee/Council

Full biographical details of each Director, including current appointments, are available at www.frc.org.uk/FRC-Board/Members.

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Nick Land (A) (CSC) (N) (R)
Independent Non-Executive Director

Appointed 1 April 2011

Experience:
As a former Executive Chairman of Ernst & Young and an experienced Non-Executive Director of major public companies, Nick brings experience of audit, finance and governance, both in the UK and internationally.

Keith Skeoch (CSC)
Independent Non-Executive Director

Appointed 1 March 2012

Experience:
Keith is the CEO of Standard Life Aberdeen. He brings economic and financial expertise, including best practice in stewardship and governance, as well as asset management and audit committee experience.

Julia Unwin CBE (A) (CSC)

Independent Non-Executive Director

Appointed 1 April 2018

Experience:
Julia brings experience of broader civil society, having been the Chief Executive of the Joseph Rowntree Foundation for ten years. Her expertise also includes the role of public regulatory bodies.

Jenny Watson CBE (R)

Independent Non-Executive Director

Appointed 1 April 2018

Experience:
Jenny brings experience of public interest, social and consumer issues. Her career includes board and chair roles in the public and not for profit sectors.

Gay Huey Evans OBE (N) (CC)
Former Deputy Chairman

Appointed 1 April 2012 – Retired 30 April 2019

Experience:
Gay brought experience of corporate plc, financial services and regulation, both in the UK and the US.

Mark Armour (A)
Former Independent Non-Executive Director

Appointed 2 July 2012 – Retired 30 June 2019

Experience:
Mark brought extensive experience of company and financial management, including corporate reporting, investor engagement and audit committee work, and of audit gained through a number of executive and non-executive roles.

Paul Druckman (CSC) **(CRC)**
Former Independent Non-Executive Director

Appointed 1 January 2017 – Retired 29 March 2019

Experience:
Paul brought global expertise in capital market reform, from corporate governance to reporting, accounting and sustainability. He also has extensive entrepreneurial business experience.

Roger Marshall (CSC) **(CRC)**
Former Independent Non-Executive Director

Appointed 1 November 2010 – Retired 31 October 2018

Experience:
As a former PwC audit partner, Roger brought significant experience of policy development at an international level and experience as a board member and audit committee chair.

Mark Zinkula
Former Independent Non-Executive Director

Appointed 1 April 2017 – Retired 30 June 2019

Experience:
Mark is the CEO of Legal & General Investment Management and a board member of the Legal & General Group Plc. Mark brought broader experience of asset management and operating at listed company board level.

GOVERNANCE AND TRANSPARENCY

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BOARD COMPOSITION AND DIVERSITY

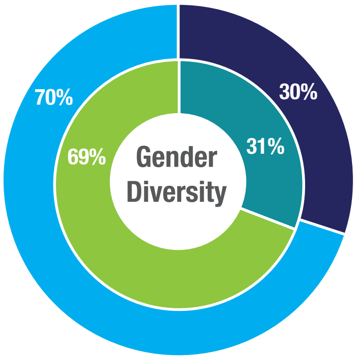
The Board adopted a diversity policy in 2017, which can be found on the FRC website at https://www.frc.org.uk/Board-Diversity-Policy. It had targets of:

(a) one third of Board members being women by the end of 2019; and

(b) at least one member being from a Black and Minority Ethnic (BAME) background by the end of 2021.

The Board aims to include members that have a wide range of experience reflecting the breadth of the FRC's stakeholder base. At the time of writing the Board comprises nine independent Non-Executive Directors and the Chief Executive.

The FRC's diversity policy was relevant to appointments made by the FRC. Going forward all appointments to the Board will be made by the Secretary of State (rather than just the Chairman and Deputy Chairman, as has previously been the case). The Chair's appointment will be subject to a pre-appointment hearing with the BEIS Select Committee, and the Chair will be accountable to Parliament as befits a public body. We anticipate all appointments made by the Secretary of State will reflect the diversity of wider society and a balance of skills and backgrounds, with high-quality candidates, drawn from a strong and diverse field, whose skills, experience and attributes have been judged to best meet the needs of the FRC.

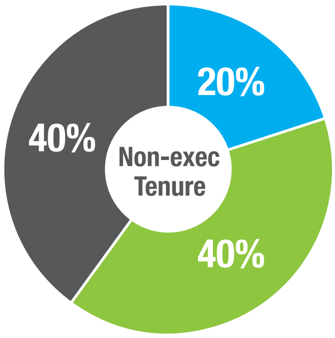


As at 4 July 2019

3 Women 7 Men

As at 31 March 2019

4 Women 9 Men



0-3 years

3-6 years

6+ years

SUCCESSION AND INDUCTION

No new Non-Executive Directors were appointed during 2018/19. During 2019/20, the FRC will work with BEIS to align current succession and induction plans with the new process following the *Independent Review of the Financial Reporting Council*.

The 2017 internal governance review included several recommendations, including that the Chief Executive should be the only Executive Director that is a member of the Board. This was implemented when Paul George and Melanie Hind stepped down from the Board on 31 March 2018. In order to be consistent with this position the FRC introduced a policy that Executives shall not be members of Board Committees. As a result Paul George also stood down as a member of the Codes & Standards Committee, and Melanie Hind as a member of the Conduct Committee, in July 2018.

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THE ACTIVITIES OF THE BOARD

In addition to the eight scheduled business meetings, additional meetings were held to consider the *Independent Review of the Financial Reporting Council* (May 2018) and the organisation's response to the CMA's *Statutory Audit Market Study* (January 2019), as well as a strategy awayday in March 2019.

A number of matters were considered by email outside formal business meetings. Details of attendance at scheduled meetings can be found at page 51.

At business meetings, the Board considers a number of standard agenda items including a report from the Chief Executive, management accounts and a report on the progress of priority projects and activities. The Non-Executive Directors provide strategic input and advice, actively and robustly challenging management and the Executive on key issues to ensure proposals and issues for decision are aligned to the FRC's strategy and mission.

The Board is responsible for the FRC's risk management and internal control systems, and for reviewing their effectiveness. In this it is supported by the Audit Committee. An annual review of the effectiveness of the FRC's risk management and internal control systems is carried out. This has been informed by the work of the Government Internal Audit Agency (GIAA) as internal auditor. More information on the Audit Committee's role and internal audit can be found on pages 38 to 42.

Minutes of Board meetings can be found on the FRC website: https://www.frc.org.uk/frc-minutes.

Key areas of activity included:

AREA OF FOCUS	ACTION TAKEN	WITH INPUT OR ADVICE/OR ON THE RECOMMENDATION OF:
Audit and actuarial	Approving the 2017/18 Audit Quality Review Inspections Report publication.	CC
	Considering the Institute and Faculty of Actuaries' (IFoA) public consultation on monitoring actuarial work.	CC
	Considering the FRC's approach to monitoring work with regards to systematic data gathering and working with other regulators.	AQRC / CC
	Approving *Developments in Audit 2018*.	
	Considering the bi-annual reports on the FRC as a designated competent authority.	
	Considering the Audit Firms Contingency Planning Review.	
	Approving any standards and exposure drafts related to the FRC's standard-setting role.	
	Approving the FRC's Annual Report to the Crown Dependencies 2017/18.	CC
	Considering bi-annual reports on Professional Oversight activities against the Professional Oversight activity plan for 2018/19.	CC
Corporate governance and reporting	Approving the revised UK Corporate Governance Code and supporting guidance.	CSC
	Approving consultation for the new Stewardship Code, and a joint discussion paper (*Building a regulatory framework for effective stewardship*).	CSC
	Considering the draft consultation paper on the *Wates Corporate Governance Principles for Large Private Companies*.	CSC
	Approving the updated Strategic Report Guidance and Feedback Statement.	CSC
	Considering a draft plan for the FRC project on the future of corporate reporting.	CSC
	Considering the *Annual Review of Corporate Governance and Reporting*.	CC, CRRC, CSC
	Approving any standards and exposure drafts related to the FRC's standard-setting role.	

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GOVERNANCE
DIRECTORS' REPORT
FINANCIAL STATEMENTS
APPENDICES

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AREA OF FOCUS	ACTION TAKEN	WITH INPUT OR ADVICE/OR ON THE RECOMMENDATION OF:
Enforcement	Considering quarterly reports on the activities of the Enforcement Division and the status of investigations.	CC
Strategy and culture	Monitoring progress against the *2018/19 Plan & Budget* and of objectives within the 2018/21 Strategy.	A / CSC
	Approving the draft 2019/20 plan, budget and levies for consultation.	
	Considering the *Independent Review of the Financial Reporting Council* and the implementation of its recommendations.	N
Other FRC matters	Approving the *2017/18 FRC Annual Report and Financial Statements*.	A / CC / N / R
	Considering the FRC's classification as a public body and consequent responsibilities.	
	Approving the FRC Risk documents, including the risk register, risk management report, risk management policy and risk appetite statement.	N
	Approving the *Unreasonable Complaints and Communications Policy* and revisions to the FRC Complaints Procedure.	
	Reviewing the results of the 2018 Employee Survey.	
	Approving revisions to the Schedule of Matters Reserved for the Board and amendments to the Terms of Reference for the Nominations Committee, Conduct Committee and Codes & Standards Committee, Advisory Councils and AQRC effective from 1 July 2018.	N, CC / CSC / AQRC
	Approving one Board reappointment and a number of Board Committee appointments and reappointments.	N
	Considering regular updates on the FRC's 2018/19 pay award awaiting final Ministerial approval.	R / A

Planning ahead	In 2019/20 the Board's focus will be on:
	• considering updates to the FRC's international influencing strategy in light of the UK's withdrawal from the EU including:
	  • legislative changes to the Third Country Auditor (TCA) regime;
	  • the establishment of an IFRS UK Endorsement Board; and
	  • consultation with BEIS on draft legislation for withdrawal from the EU.
	• the Future of Audit Project.
	• implementation of the *Independent Review of the Financial Reporting Council* recommendations.	

Key to Committees / Councils
(A) Audit (N) Nominations (R) Remuneration (CC) Conduct (CSC) Codes & Standards
(AAC) Audit & Assurance Council (CRC) Corporate Reporting Council (AC) Actuarial Council

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BOARD EFFECTIVENESS

In accordance with the UK Corporate Governance Code, Board effectiveness is usually reviewed annually, with an externally led review every three years. The most recent externally facilitated review was in 2015/16, and an external review was initially scheduled for 2018/19. However, the *Independent Review of the Financial Reporting Council* included a recommendation for a change in the composition of the Board.

The current Board members will remain on the Board, or end their terms of appointment early if necessary, in order to ensure an orderly transition to the new Board. This will commence with the appointment of the new Chair and Deputy Chair. We believe it is more appropriate for the new Chair, once appointed, to commission an externally facilitated review.

The *Independent Review of the Financial Reporting Council* also recommended that the Government, working with the Chair of the new Board, should review the existing FRC governance structure with a view to achieving a significant simplification in the architecture.

Despite the lack of formal effectiveness review this year, the Board's way of working has evolved during 2018/19. This has included working more agilely with ad hoc meetings and sub-groups convened to address emerging issues.

REGULATORY COMMITTEE REPORTS

To ensure independence, no member of the Conduct Committee shall also be a member of the Codes & Standards Committee. However, to facilitate effective, informed and evidenced decision-making, the two Committees consider and respond to requests from one another, taking advice from the sub-committees as appropriate.

CONDUCT COMMITTEE

The Conduct Committee exercises specified delegated functions of the Secretary of State under Companies Act legislation. In addition, it oversees the FRC's supervisory, monitoring and enforcement work with the objective of promoting high quality corporate governance and reporting. The Committee appoints members of the following sub-committees: Audit Quality Review, Corporate Reporting Review, Case Management and the Enforcement Committee Panel and receives updates on the work of those committees.

In addition to the matters reported to the Board on pages 35 and 36, during 2018/19 the Committee:

- took a number of decisions required under the FRC's disciplinary schemes and Audit Enforcement Procedure including 15 decisions to start investigations and one to widen the scope of an investigation;
- agreed to the publication of decisions to open a number of enforcement investigations;
- oversaw the Executive's monitoring of compliance with the conditions of the delegation arrangements with each RSB;
- approved proposals in relation to matters to be the subject of thematic review findings;
- approved the *Developments in Audit 2018*;
- approved the *Professional Oversight Key Facts and Trends* report; and
- approved a number of appointment and reappointments to its various sub-committees.

CODES & STANDARDS COMMMITTEE

Following on from the 2017 review of the FRC's governance arrangements, with effect from 1 July 2018 the Codes & Standards Committee's (CSC) role was narrowed to advising the Board on corporate governance matters, including proposed changes to the UK Corporate Governance Code and Stewardship Code. This also includes identifying the current, emerging and potential risks to the quality of corporate governance and stewardship in the UK and approving the adequacy of actions to mitigate those risks. The CSC also approves the issue and maintenance of FRC taxonomies, including for consultation.

During the 2018/19 the Committee:

- provided its views on the consultations on corporate governance principles for large private companies and the Stewardship Code;
- considered the proposals resulting from analysis of the UK Corporate Governance Code consultation;
- approved the issue of the FRC's Statement on the Pensions SORP and the FEHE SORP;
- agreed the assumptions made to AS TM1 v4.2;
- approved the FRC 2019 Taxonomies suite relating to IFRS 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers*, IFRS 16 Leases and annual improvements; and
- approved a number of appointments and reappointments to the advisory councils.

Since 1 July 2018 some of these activities are no longer part of the Committee's role.

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AUDIT COMMITTEE

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NICK LAND COMMITTEE CHAIRMAN

The Audit Committee:

- monitors the integrity of the FRC's Financial Statements including its Annual Report, formal announcements relating to the FRC's financial performance, and management accounts on behalf of the Board;
- advises the Board on whether the Annual Report and Financial Statements are fair, balanced and understandable;
- advises the Board on the appointment, re-appointment and removal of the FRC's internal and external auditors, as well as their effectiveness;
- monitors the integrity, adequacy and effectiveness of the FRC's system of risk management and internal controls, including the internal audit function; and
- reviews progress, on behalf of the Board, in managing the FRC's resources within the published budget and funding requirement.

During the year, the Committee's focus was on:

- the requirements of the FRC's public body status, particularly with respect to *Managing Public Money* requirements and its relationship with BEIS as its sponsor Department, including the treatment of its reserves;
- embedding the new internal audit arrangements following the appointment of the GIAA as internal auditors in the previous financial year; and
- information security, including cyber-security and data protection.

2018/19 was something of a transitional year for the Audit Committee. The FRC is now subject to the requirements of *Managing Public Money* and during the year much of the Committee's focus was on how the FRC should comply with these requirements and ensure that systems and processes are aligned with *Managing Public Money* guidelines. Awareness training sessions were provided (and will continue) for staff, and the FRC continues to draw on specialist HR and finance support available from BEIS and the GIAA during the transition to full public body status.

The FRC is also an active participant of the BEIS Partner Bodies Audit and Risk Assurance Committee (ARAC) Chairs group.

COMMITTEE OPERATION AND PERFORMANCE

All members of the Committee are independent Non-Executive Directors and three of the four members have relevant and recent financial experience. The Committee has competence relevant to the sectors in which the

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FRC operates: auditing, accounting and actuarial matters and corporate governance and reporting.

The Committee met six times during the year and members' attendance can be found on page 51. In addition to the members, the external auditor, haysmacintyre, and the internal auditor from the GIAA are invited to each meeting together with the Chief Executive, Finance Director, Executive Director of Strategy and Resources and General Counsel and Company Secretary. The Committee meets the external auditor in private at least once a year and the Chair meets the external auditor outside the formal committee process during the year. To protect the objectivity and independence of the external auditor, it is the FRC's policy that they are not contracted to carry out any non-audit services.

How the Committee discharged its responsibilities.

AREA OF FOCUS	CONSIDERATION	ACTION TAKEN/PROGRESS UPDATE
Financial and narrative reporting	In relation to the Annual Report and Financial Statements for the year ended 31 March 2018: • monitored and reviewed the integrity of the financial statements including the quality and acceptability of accounting policies and practices. • monitored material areas in which significant judgements had been applied. • assessed whether the Annual Report, taken as a whole, is fair, balanced and understandable and advised the Board accordingly. Considered draft outline plan for the Annual Report and Financial Statements for the year ended 31 March 2019.	Additional disclosures on the FRC's enforcement work were added following the June meeting. No significant issues requiring additional disclosures were identified. The assessment was reported to the Board.
Financial reporting	Monitored financial performance, in terms of both income and expenditure, against the published 2018/19 budget and subsequent reforecasts.	Throughout the year, the Committee paid close attention to income and expenditure. It encouraged continued efficiency savings as well as the ongoing development of a tighter budgeting process in line with *Managing Public Money*.
	Reviewed the reserves policy.	In line with *Managing Public Money* cash representing the FRC's reserves is now held in an FRC bank account within the Government Bank Account and can only be deployed with consent of BEIS as sponsor Department.
	Reviewed the Counter Fraud Policy and Plan.	The Committee suggested amendments to clarify that as well as staff, the policy applies to all Non-Executive Directors and that it covers data fraud.

AUDIT COMMITTEE

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How the Committee discharged its responsibilities.

AREA OF FOCUS	CONSIDERATION	ACTION TAKEN/PROGRESS UPDATE
	Reviewed and approved for recommendation to the Board the draft 2019/20 budget and, following the consultation process, approved the final budget for recommendation to the Board.	The Committee reviewed the draft plan and budget and the allocation of the funding requirement to FRC funding groups.
	Received regular updates on discussions with the ICAEW in respect of case cost agreements.	The Committee was satisfied that case costs had been accounted for appropriately.
External audit	Assessed the effectiveness, independence and objectivity of the external auditor, haysmacintyre. Based on that assessment, the Committee recommended to the Board the reappointment of the external auditor, the auditor's engagement letter and the auditor's remuneration.	The Committee was satisfied that appropriate safeguards were in place in respect of the fact that the external auditor also audits the accounts of the ICAEW; this matter is kept under review.
	Reviewed the external audit plan for recommendation to the Board.	The Committee identified areas of additional focus to be considered as part of the external audit. The audit plan was updated and subsequently approved.
Internal audit	In 2018 the Committee recommended to the Board the appointment of the GIAA for the next reporting period.	The Board approved the appointment of the GIAA at its March 2018 meeting.
	Approved the 2018/19 internal audit plan.	The internal auditor attended the Audit Committee during the year and conducted audits on the following areas: • Payroll and HR systems. • Budgeting and *Managing Public Money*. • HR follow up and contract management[5]. • FRC Operations - Enforcement. The Committee considered management responses and progress to address identified actions.
Risk management and internal control	Monitored the implementation of the FRC's risk management framework.	Risk management continues to become embedded in the FRC's activities.

5 This audit was finalised before 31 March 2019, with the management responses and actions considered at the May Audit Committee meeting.

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How the Committee discharged its responsibilities.

AREA OF FOCUS	CONSIDERATION	ACTION TAKEN/PROGRESS UPDATE
Risk management and internal control	Reviewed management's assessment of the risks to the FRC's mission, including new risks, revision to existing risks, 'deep-dives' into principal risks and the adequacy of the mitigations.	The Committee advised management and the Board on its assessment of the identified principal risks and mitigations to those risks.
	Reviewed a revised risk appetite statement.	The revised risk appetite statement was subsequently approved by the Board.
	Reviewed a risk assurance map.	The risk assurance map was considered by the Committee as part of enhancements to the FRC's risk control environment. A plan for further enhancements to the assurance map through 2019 was approved by the Committee.
	Reviewed the FRC's internal controls, including the findings of the internal audit on budgeting and *Managing Public Money* and Payroll and HR systems.	The internal audit report was considered by the Committee at its May meeting.
Other matters	Maintained close focus on robustness of FRC funding streams.	Ongoing
	Received regular reports on: • IT and information security; • management accounts; and • physical security. In addition, the Committee received an annual report on compliance and whistleblowing.	The Committee welcomed the fact that the FRC was awarded advanced level accreditation Cyber Essentials Plus as assurance that appropriate systems and processes are in place to protect the organisation against this threat.

In 2019/20 the Committee's focus will be on:

- responding to the requirements of public body status;
- changes to processes stemming from the *Independent Review of the Financial Reporting Council* recommendations; and
- reviewing possible additional security controls to safeguard against unauthorised disclosure of information.

AUDIT COMMITTEE

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OTHER AUDIT MATTERS

Internal Audit

In March 2018 the Board approved the Audit Committee's recommendation that the GIAA should conduct the FRC's internal audits.

The GIAA undertook an initial review of areas to be addressed in ensuring, and documenting, compliance with *Managing Public Money*. All these areas were addressed during the year in line with the GIAA's advice.

External Audit

As the body responsible for regulating statutory auditors in the UK, the FRC has to consider threats to auditor independence, which in particular may arise from our monitoring and review of Public Interest Entity (PIE) audits. This risk is addressed by appointing an engagement partner for the audit of the FRC's financial statements who has no PIE clients, and is therefore not subject to direct monitoring and review by the FRC. Similarly, as the Independent Supervisor and Comptroller and Auditor General, it is not considered appropriate to appoint the National Audit Office as the FRC's external auditor.

Haysmacintyre LLP was appointed as the FRC's statutory auditor by the Board in 2013 following a formal tender process. The external audit contract will be put out to tender at least once every ten years. The effectiveness of the auditor is assessed by the Audit Committee based on its own interaction with the auditor and input from the FRC Executive. The Committee concluded that the auditor provided a sufficiently challenging and sceptical view of management's key judgements and remained appropriately qualified and experienced. Consideration of independence included a review of the safeguards that had been put in place at Haysmacintyre LLP to ensure complete separation in relation to the audit of the FRC and the audit of the ICAEW, which is a recognised supervisory body for statutory audit and acts as a delegate of the FRC; it was concluded that appropriate safeguards were in place but that this would be kept under review. On the basis of the Audit Committee's assessment, the Board approved the reappointment of Haysmacintyre LLP for 2018/19.

NOMINATIONS COMMITTEE REPORT

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SIR WINFRIED BISCHOFF
COMMITTEE CHAIRMAN

The Nominations Committee:

- regularly reviews the size, structure and composition of the governance structure;
- in respect of Board appointments appoints independent search consultants and the Independent Assessor, and presents the nomination of the Independent Assessor to the Board;
- recommends to the Board reappointments to the Board and appointments and reappointments to Board Committees and of Council Chairs; and
- monitors succession planning for the Board, its Committees and Senior Executives.

The Committee's focus during 2018/19 was on achieving the diversity target, and on succession planning for the Board, Committees and Senior Executives. In addition, the Committee reviewed its terms of reference to respond to the FRC's public sector classification. In the latter part of the year, additional meetings were scheduled to consider and progress the recommendations on the leadership of the FRC, Non-Executives and succession from the *Independent Review of the Financial Reporting Council*.

COMMITTEE OPERATIONS AND PERFORMANCE

All Members of the Committee are independent Non-Executive Directors; biographies can be found on the FRC website: https://www.frc.org.uk/FRC-Board/Members. The Committee met seven times during the year, and members' attendance at meetings can be found on page 51. In addition to the members, meetings are attended by the Chief Executive and the General Counsel and Company Secretary. Although the Committee has the authority to appoint external advisers, none were engaged during the reporting year.

NOMINATIONS COMMITTEE REPORT

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How the Committee discharged its responsibilities.

AREA OF FOCUS	ACTION TAKEN	PROGRESS UPDATE
Board size and composition	Reviewed the structure, size and composition of the Board throughout the year having regard to the *Independent Review* recommendations, FRC strategy, the external environment, the UK's withdrawal from the EU, and the FRC's published diversity targets.	
	Recommended to the Board that Keith Skeoch's term of office as a Non-Executive Director be extended to July 2020. In taking this decision, the Committee considered the importance of retaining a Board member with investor experience.	The Board approved the extension of Keith Skeoch's term of office. Prior to this, the FRC secured BEIS support for this approach.
Non-Executive, committee, council and panel member appoint-ments and reappoint-ments	Considered and approved various recruitment exercises in relation to Board and Committee member vacancies. Appointed the Appointments Committee to deal with Tribunal Panel member vacancies. Appointed an Independent Assessor to assist with appointment process for a member of the Conduct Committee. Considered and recommended to the Board the reappointment of a number of Committee members.	Where appropriate recommendations were approved by the Board and by further Committees.
Executive succession planning	Reviewed succession arrangements for Board members and Senior Executives and the interaction of succession plans for Senior Executives and Board members and received notifications of resignations as appropriate.	Succession arrangements updated.
Register of interests	Approved, for recommendation to the Board, amendments to the Code of Conduct and revisions to the form of the published register to ensure greater transparency of financial and other interests.	Code of Conduct reviewed by the Board and updated register published on the website.
Gifts and hospitality	Approved, for recommendation to the Board, amendments to the Code of Conduct and the form of the register for publication to ensure greater transparency of gifts and hospitality offered, accepted and/or declined.	Code of Conduct reviewed by the Board and register published on the website.

The Deputy Chairman's term of office expired on 30 April 2019 and Sir Winfried Bischoff has announced his intention to step down as Chairman once a new Chair's appointment becomes effective later in 2019. The appointments of the new Chair and Deputy Chair are made by the Secretary of State and the recruitment process to identify a successor is being led by BEIS. During the year the FRC amended its Articles of Association, including a change in order to provide that all appointments to the Board are made by the Secretary of State. This implemented one of the recommendations of the *Independent Review of the Financial Reporting Council* and took effect on 1 April 2019.

In 2019/20, the focus of the Committee will be working with BEIS to review board size, composition and succession to enable the Secretary of State working with the new Chair on the implementation of the recommendations of the *Independent Review of the Financial Reporting Council.* This will include the governance review with BEIS, and a Board effectiveness review. As future appointments to the Board will be made by the Secretary of State, the Committee's role will inevitably change over the course of the year, with the precise delineation of responsibilities to be determined as part of the governance review.

REMUNERATION COMMITTEE REPORT

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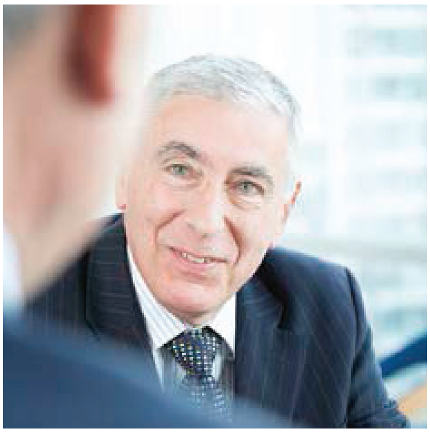

SIR BRIAN BENDER
COMMITTEE CHAIRMAN

2018/19 has been a year of transition for the FRC as it has adjusted to its status as a public body with a central government classification. Following the *Independent Review of the Financial Reporting Council,* and as the recommendations are implemented and the FRC transitions to the ARGA, the extent to which the FRC will have flexibility to determine its pay arrangements will be settled. During this interim period, staff pay will be subject to compliance with Public Sector Pay Guidelines and Rules. This has meant that reward policy has not been solely determined by the Remuneration Committee, particularly in relation to its previous responsibilities to:

- set the long-term pay strategy for FRC staff;
- annually determine the framework and broad policy for the remuneration of FRC staff, the Chief Executive, Executive Committee members and the Chairman; and
- recommend to the Board the total remuneration package of the Chief Executive and Executive Committee members.

During 2018/19, the Committee has continued to advise the Executive on these matters and its remit and terms of reference will be revisited once the FRC's exact classification is finalised.

The most significant remuneration issue during the year was the 2018/19 Pay Award. Following delays in the issuing of the Public Sector Pay Guidance, the FRC's proposals were submitted to BEIS in July 2018 and partial funding was approved by the Secretary of State in March 2019. However, HM Treasury and Cabinet Office approval is also required, and was provided in July 2019. Separately, discussions with BEIS, the Cabinet Office and HM Treasury have commenced regarding the FRC's long-term pay strategy and the extent to which greater flexibility over pay arrangements, as recommended by the *Independent Review of the Financial Reporting Council*, may be granted.

COMMITTEE PERFORMANCE AND OPERATION

All members of the Committee are independent Non-Executive Directors. The Committee held four meetings during the year, including one to consider the leaving arrangements for Stephen Haddrill, who announced his decision to step down as Chief Executive in late 2018 and is due to leave the FRC in autumn 2019.

Meetings are attended by the Chief Executive, the Executive Director, Strategy and Resources, General Counsel and Company Secretary and the Head of Human Resources, by invitation, except where agenda items would present a conflict of interest.

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AREA OF FOCUS	ACTION TAKEN	PROGRESS UPDATE
NED remuneration	Considered whether fees to be paid to Board, Committee and Council members remained appropriate having regard to fees paid at comparator bodies, time commitments and workloads.	The Committee considered the fees for FRC Board members remained appropriate for 2018/19.
Pay and performance review	Received routine updates on the progress of the review and impact on staff retention, providing input and advice as appropriate.	Approved by HM Treasury and Cabinet Office in July 2019.
	The Committee reviewed proposed salary adjustments in line with the work undertaken by the independent Beamans Management Consultants in 2017/18.	
	Considered the FRC's long-term pay strategy.	Proposals are currently with BEIS.
Bonus awards for 2018/19 and salary awards for 2019/20	It was agreed that the company and individual bonus awards would be discontinued for all staff including the Chief Executive and Executive Committee members.	
	A new Values in Practice (VIP) recognition scheme for staff excluding Executive Committee members was introduced on a pilot basis for 2018/19.	
Equal pay	When determining salary proposals for 2018/19, due attention was given to equal pay considerations.	Although the FRC is under the threshold for compulsory reporting of its gender pay data, data was published in both March 2018 and March 2019 alongside analysis. In addition, there is a detailed plan to address any identified gender pay gap issues.
Diversity and inclusion	Received reports in relation to the activities of the FRC Staff Committee.	
	Considered reports on the FRC's gender pay gap reporting.	

In 2019/20, the Committee's focus will be on:

- working with BEIS, the Cabinet Office and HM Treasury to agree the FRC's long-term pay strategy;
- the development of new performance management arrangements; and
- a review of the new Values in Practice (VIP) recognition scheme.

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REMUNERATION FRAMEWORK

The Chief Executive is the only executive member of the Board[6]. The performance of the Chief Executive and other Executive Committee members is assessed against both collective objectives set in line with the FRC business plan and individual objectives, including employee survey results for the areas under their control and a citizenship rating relating to living the FRC Values.

An overview of the remuneration framework that applied to all staff during 2018/19 is set out below. The main components of the Chief Executive and other Executive Committee members' remuneration are consistent with this framework unless indicated otherwise:

ELEMENT AND PURPOSE	OPERATION	OPPORTUNITY/OUTPUT
BASE SALARY *To provide core remuneration for the role recognising the responsibility for setting and delivering the annual FRC Plan & Budget*	Salaries are reviewed annually by the Committee who consider the Chief Executive and other Executive Committee members' responsibilities, performance and experience alongside market trends and relevant comparator organisations, where available. Salaries for new Chief Executive and other Executive Committee member appointments are now subject to HM Treasury approval in line with Senior Civil Service Pay Guidance.	Any annual increase awarded reflects movement in market rates and increasing competency within role. Work to benchmark some Executive Director roles was undertaken by the independent consulting group Korn Ferry. The Chief Executive and Executive Committee members are required to achieve higher ratings for performance and citizenship than other members of staff in order to qualify for a potential salary increase. Individual adjustments in excess of general market movements may be made in appropriate circumstances (e.g. where the role scope has changed or as a reflection of a significant development in the role).
BENEFITS *To provide a competitive and cost effective benefits package in line with public sector norms*	All staff who were offered employment prior to 1 June 2018 are eligible to receive benefits which may include: • dental insurance; • private health insurance; • income protection insurance; and • life insurance. In aligning the FRC's remuneration policy more closely with the public sector, new joiners who started from 1 June 2018 are no longer eligible for dental or private health insurance.	

6 Prior to April 2018, the Executive Director, Audit & Actuarial Regulation and the Executive Director, Corporate Governance & Reporting were also members of the Board.

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ELEMENT AND PURPOSE	OPERATION	OPPORTUNITY/OUTPUT
PENSION BENEFITS *To provide competitive retirement benefits in line with relevant market comparators*	All staff are eligible to participate in the group personal pension scheme which is a defined contribution scheme. Staff offered employment prior to 1 June were able to elect to take pay in lieu of pension contributions less an amount equivalent to Employer's National Insurance contributions but this has been discontinued for staff offered employment after 1 June 2018.	A maximum of 10 percent of base salary.
VALUES IN PRACTICE RECOGNITION SCHEME	It has been agreed that the Chief Executive and other Executive Committee members are not eligible to receive a VIP award which is a modest in-year award scheme for specific examples of strong performance in relation to the FRC's values and behaviours.	

Pay multiples
The remuneration of the highest paid Director in 2018/19 was £389,879* (2017/18: £389,902). This was 4.54 times (2017/18: 4.38) the median remuneration of the workforce, which was £85,949 (2017/18 £89,111). The Chief Executive chose not to be considered for a bonus for 2017/18 and bonuses were replaced with the VIP scheme in 2018/19, for which the Chief Executive, as an Executive Director, is not eligible.

Total remuneration includes salary and benefits in kind. It does not include severance payments, or any employers pension allowance or payments in lieu of pension payments. In 2018/19 no employees received remuneration in excess of the highest paid director.

*The difference between the total remuneration of the highest paid director for the purposes of this disclosure and the total remuneration set out in the Directors' remuneration table (page 50) is that the salary in the remuneration table includes payments of £33,789 (2017/18 £33,789) received in lieu of pension and £7,394 (2017/18 to) received as a result of the voluntary sale of annual leave.

DIRECTORS' REMUNERATION

Chief Executive
Employment contracts and policy on payment for loss of office.

Notice period
The Chief Executive has a notice period of 12 months, although he will be leaving the FRC at the end of October 2019. The notice period for his replacement is expected to be six months.

Payments for loss of office
No payments or compensation for loss of office have been made in the current year.

Non-Executive Appointments
The FRC Remuneration Committee agreed that where the Chief Executive serves as a Non-Executive Director elsewhere, they may retain those earnings. Stephen Haddrill is a Non-Executive Director of the Royal Institute of Chartered Surveyors (RICS) for which he receives an annual fee of £26,000 (2017/18: £25,000).

Non-Executive Directors
The remuneration of Non-Executive Directors, including the Chairman and Deputy Chairman, is determined by the Board on the recommendation of the Remuneration Committee and is now subject to Senior Civil Service Pay Guidance and rules. The Board, with the Committee, determines the remuneration of current Non-Executive Directors by assessing the responsibility, workload and time commitment to the role and by calculating a daily rate of fees comparable to those paid by other regulators and in relation to comparable roles in the public sector. Future appointments to the Board will be made by the Secretary of State, who will also determine the appropriate remuneration.

A Non-Executive Director who is the chair of any Committee is not involved in any decision relating to their remuneration. The total remuneration and benefits received are shown in the Directors'

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remuneration table (page 50) and have been subject to audit (see also note 4 to the Financial Statements).

Non-Executive Directors
Remuneration levels are based on the time commitment required, which may include preparation, scheduled meetings and any additional meetings required during the course of the year.

Non-Executive Director remuneration can be broken into the following elements:

Board membership
Eight scheduled meetings a year and one strategy day[7]

Chairman	£120,000
Deputy Chairman	£35,000
Membership	£25,000

Audit Committee
Four scheduled meetings a year

Chairman	£5,000
Membership	No additional

Remuneration Committee
Three scheduled meetings a year

Chairman	£5,000
Membership	No additional

Nominations Committee
Three scheduled meetings a year

Chairman	No additional
Membership	No additional

Codes & Standards Committee
Nine scheduled meetings a year and one strategy day

Chairman	£45,000
Membership	£10,000

Conduct Committee
11 scheduled meetings per year

Chairman	£65,000
Membership	£10,000

Non-Executive Director fees were reviewed by the Committee in 2018. Whilst it was agreed that they would be reassessed as part of the wider governance review, this was superseded by the *Independent Review of the Financial Reporting Council.* Instead, Non-Executive Director fees for continuing Directors will be revisited with BEIS as the FRC transitions to the ARGA. Revised fees for the Chair and Deputy Chair have been published as part of the advertisements for those roles.

7 In addition to these meetings, several ad hoc meetings were convened during 2018/19 to discuss the Independent Review and CMA's Statutory Audit Market Study

REMUNERATION COMMITTEE REPORT

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DIRECTORS REMUNERATION

	2018/19 Fees/ salary	2018/19 GHI[1]	2018/19 Total £	2017/18 Total £
Non-Executive Directors				
Sir Winfried Bischoff	120,000	–	120,000	120,000
Gay Huey Evans	45,000	–	45,000	45,000
Mark Armour	25,000	–	25,000	25,000
Sir Brian Bender	40,000	–	40,000	40,000
David Childs	90,000	–	90,000	90,000
John Coomber	46,250	–	46,250	35,000
Olivia Dickson	38,750	–	38,750	50,000
Paul Druckman (until 29 March 2019)	50,000	–	50,000	50,000
Ray King (until 5 July 2017)	–	–	–	13,077
Nick Land	75,000	–	75,000	75,000
Roger Marshall	37,917	–	37,917	65,000
Keith Skeoch [2]	35,000	–	35,000	35,000
Julia Unwin (from 1 April 2018)	30,833	-	30,833	–
Jenny Watson (from 1 April 2018)	25,000	-	25,000	–
Mark Zinkula	25,000	–	25,000	25,000
Sub-total	**683,750**	**–**	**683,750**	**668,077**
Executive Directors				
Stephen Haddrill [3][4][5]	425,697	5,365	431,062	423,691
Paul George [3][5] (until 31 March 2018)	–	–	–	367,284
Melanie Hind (formerly McLaren) [3][5] (until 31 March 2018)	–	–	–	342,574
Sub-total	425,697	5,365	431,062	1,133,549
Grand total	1,109,447	5,365	1,114,812	1,801,626

Notes:
When Directors have served for part of a year, the amounts shown are for the relevant proportion of the year.
(1) This is Life Assurance and Group Income Protection Insurance.
(2) From 1 April 2012 Keith Skeoch waived his fees in favour of charity.
(3) Executive Directors are entitled to receive pension contributions and other benefits. The figures shown are the cash equivalent of their full pay and benefits.
(4) As the pay review for 2018/19 had not yet been approved by HM Treasury and the Cabinet Office, the average salary and reward increase for the year was 0.0% for all staff including Executive Directors (2017/18:1.0%). In accordance with the FRC's policy for all staff, the CEO chose to sell some of his holiday entitlement, which has resulted in a non-consolidated increase in salary paid in 2018/19.
(5) Total Directors' remuneration in 2018/19 amounted to 5.8% (2017/18: 9.3%) of total company remuneration.

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ATTENDANCE AT SCHEDULED MEETINGS HELD DURING THE YEAR

	FRC Board	Remuneration Committee	Nominations Committee	Audit Committee	Codes & Standards Committee	Conduct Committee
Sir Winfried Bischoff	10/10	3/4	7/7			
Gay Huey Evans	10/10		5/7			9/12
Stephen Haddrill	9/10					
Mark Armour	9/10			5/6		
Sir Brian Bender	9/10	4/4	7/7			9/12
David Childs	10/10		7/7			11/12
John Coomber	6/10	4/4		6/6	4/5	
Olivia Dickson	10/10				4/5	
Paul Druckman	9/10				5/5	
Nick Land	10/10	4/4	7/7	6/6	5/5	
Roger Marshall[(1)]	6/6				2/3	
Keith Skeoch	7/10				4/5	
Julia Unwin[(2)]	6/10			4/4	2/3	
Jenny Watson[(3)]	8/10	1/2				
Mark Zinkula	9/10					
Paul George[(4)]					2/2	
Ashok Gupta[(5)]					2/2	
Sue Harris					4/5	
Liz Murrall					5/5	
David Cannon						9/12
Sean Collins[(6)]						10/12
Geoffrey Green						12/12
Philippa Hardwick						11/12
Melanie Hind[(7)]						4/4
John Hitchins						11/12
Helen Jones						11/12
Emmy Labovitch						12/12
Malcolm Nicholson[(8)]						4/4
Martin Slack						11/12

Notes:
(1) Roger Marshall stood down from the Board and Codes & Standards Committee on 31 October 2018.
(2) Julia Unwin was appointed to the Audit Committee and Codes & Standards Committee with effect from 1 September 2018.
(3) Jenny Watson was appointed to the Remuneration Committee with effect from 1 September 2018.
(4) The requirement for the Executive Director Corporate Governance & Reporting to sit on the Codes & Standards Committee was removed in July 2018. Consequently Paul George stepped down from Codes & Standards Committee on 31 July 2018.
(5) Ashok Gupta stood down from the Codes & Standards Committee on 31 August 2018.
(6) Due to a declared conflict of interest, Sean Collins did not attend the Conduct Committee meeting held on 25 November 2018.
(7) The requirement for the Executive Director Audit & Actuarial Regulation to sit on the Conduct Committee was removed in July 2018. Consequently Melanie Hind stepped down from the Conduct Committee on 31 July 2018.
(8) Malcolm Nicholson stood down from the Conduct Committee on 31 July 2018.
The attendance figures represent attendance at formal and strategy meetings.

DIRECTORS' REPORT

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The Directors of the FRC (Registered number: 02486368) present their report for the year ended 31 March 2019.

We have included information on the names of the individuals, who, at any time during the financial year, were Directors of the FRC on pages 32 and 33. The attendance of the Directors at the meetings held during the year is in also on page 51.

DIRECTORS AND DIRECTORS' INSURANCE AND INDEMNITIES

Under the terms of the FRC's Articles of Association, all Directors are members of the FRC and each has undertaken to guarantee the liability of the FRC up to an amount not exceeding £1. There are no other members and no dividend is payable.

The FRC purchased and maintained throughout the financial year Directors' and Officers' liability insurance in respect of itself and for its Directors and Officers. This gives appropriate cover for any legal action brought against the FRC or its Directors or Officers.

DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT & FINANCIAL STATEMENTS

Directors' Responsibilities Statement

The Directors (including the Chief Executive as Accounting Officer) are responsible for preparing the Annual Report and Financial Statements in accordance with applicable laws and regulations. Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*. Under company law the Directors must not approve the financial statements unless satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for the period.

In preparing these financial statements the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the FRC will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the FRC's transactions and disclose with reasonable accuracy at any time the financial position of the FRC and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the FRC and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Strategic Report

The Directors use the Strategic Report to explain how they have performed their duty to promote the success of the FRC. The Strategic Report, which can be found at pages 1 to 29, contains information on the following matters:

- the FRC's financial risk management policy;
- important events affecting the FRC since the end of the financial year; and
- likely future developments in the business of the FRC.

DISCLOSURE TO THE AUDITOR

The Directors, including the Chief Executive as Accounting Officer, at the date of this report, confirm that, as far as he/she is aware, there is no relevant audit information of which the FRC's auditor is unaware. Each Director has taken all steps that they ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the FRC's auditor is aware of that information.

AUDITORS

The auditors, Haymacintyre LLP, have expressed their willingness to remain in office and the Audit Committee has recommended their reappointment to the Board. A resolution to reappoint the auditors and to authorise the Directors to determine their remuneration will be proposed at the Annual General Meeting of the Company.

Approved by the Board of Directors on 4 July 2019 and signed on its behalf by:

Anne McArthur
Company Secretary

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TO THE MEMBERS OF THE FINANCIAL REPORTING COUNCIL LIMITED

Opinion
We have audited the financial statements of The Financial Reporting Council Limited (the FRC) for the year ended 31 March 2019 which comprise the profit and loss account, the balance sheet, the statement of changes in equity, the cash flow statement and the notes to the financial statements, including its significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 102, the Financial Reporting Standard applicable in the United Kingdom (UK) and Ireland.

In our opinion, the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2019 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion
We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern
We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the Directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Key audit matters
Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) we identified, including those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

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KEY AUDIT MATTER	OUR RESPONSE
Fraud and error in revenue recognition	We reviewed all material income streams to consider whether revenue is recognised appropriately in line with the FRC's stated accounting policies and ensured the treatment is reasonable, reflects the nature of the activity and the FRC's obligations, and is recognised in accordance with FRS 102. Our review included an assessment of accounting policies and those systems relevant to our audit, detailed controls testing and substantive verification procedures. Our work included visiting and reviewing the work a service organisation responsible for a significant proportion of levy invoicing and collection. In addition to our review of income recognised during the year we reviewed the recognition and recoverability of trade receivables, and the recognition and calculation of accrued and deferred income at the year-end to assess the appropriateness of their recognition and carrying values as at 31 March 2019.
Enforcement case costs and provisions	We reviewed the controls and procedures used to monitor and record case costs, including the allocation of both external and internal costs to each case and considered the operating effectiveness of these systems. We reviewed a sample of significant cases ensuring that the FRC's stated protocols, controls and procedures have been followed. As part of our review of a sample of significant cases we considered the effectiveness of the procedures that have been implemented to ensure that the risk of damages or other claims against the FRC are mitigated.
Possible impacts of the Kingman review on the financial statements	We reviewed the proposals and discussed the Kingman review and the implementation process with members of the Executive Committee, representatives from BEIS and other Board/Committee members. We used these procedures to seek to gain an understanding of the process to date and in the future to help us assess the potential impact of the review and the implementation process on the financial statements for the year ended 31 March 2019.

Our application of materiality
The scope and focus of our audit was influenced by our assessment and application of materiality. We define materiality as the magnitude of misstatement that could reasonably be expected to influence the readers and the economic decisions of the users of the financial statements. We use materiality to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the financial statements as a whole.

Due to the nature of the company and its status as regulator we considered expenditure and associated funding to be the main focus for the readers of the financial statements, accordingly this influenced our judgement of materiality. Based on our professional judgement, we determined materiality for the company to be £150,000, based on 0.5% of budgeted expenditure (before case costs).

Based on our risk assessments and our assessment of the overall control environment, our judgement was that performance materiality (i.e. our tolerance for misstatement in an individual account or balance) for the company was 75% of materiality, namely £112,500.

We agreed to report to the Audit Committee all audit differences more than £7,500, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also reported to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit
As the FRC is a standalone corporate entity based in London the scope of our work was the audit of the financial statements of the company. The scope of the audit and our audit strategy was developed by using our audit planning process to obtain and update our understanding of the company, its activities, its control environment, and likely future developments. Our audit testing was informed by this understanding of the company and accordingly was designed to focus on areas where we assessed there to be the most significant risks of material misstatement.

During our audit planning process, we also obtained an understanding of how the company uses service organisations in its operations. We then evaluated the design and implementation of relevant controls at the company that relate to the services provided by service organisations and assessed draft financial data for the financial year to build an understanding of the operation and effectiveness of these service organisations. We considered it appropriate to visit a service organisation engaged by the FRC to collect a significant element of its levy income.

To maintain and reinforce our knowledge of the FRC and the risks it faces we attend Audit Committee meetings during the year and during the audit planning process, the senior statutory auditor and senior audit manager met the senior members of the company's finance team and members of the Executive Committee. This dialogue continued throughout the audit process, as we reassessed and re-evaluated audit risks where necessary and amended our approach accordingly.

Other information
The Directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006
In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception
In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the Strategic Report or the Directors' Report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Responsibilities of directors
As explained more fully in the Directors' responsibilities statement set out on page 52, the Directors

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are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report
This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an Auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Bernadette King (Senior Statutory Auditor)

For and on behalf of
Haysmacintyre LLP,
Statutory Auditors

10 Queen Street Place
London
EC4R 1AG

9 July 2019

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THE FINANCIAL REPORTING COUNCIL LIMITED

Profit and Loss account for the year ended 31 March 2019

	Note	2018/19 £'000	2017/18 £'000
Revenue		**30,505**	35,488
Operating expenses	2	**(28,784)**	(31,677)
Operating profit		**1,721**	3,811
Interest receivable		**81**	51
Profit on ordinary activities before taxation		**1,802**	3,862
Tax on profit on ordinary activities	3	**(15)**	(10)
Profit for the financial year		**1,787**	3,852

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THE FINANCIAL REPORTING COUNCIL LIMITED

Balance Sheet at 31 March 2019

	Note	31 March 2019 £'000	31 March 2018 £'000
Fixed assets			
Intangible assets	6	**87**	121
Tangible assets	7	**1,923**	2,175
		2,010	2,296
Current assets			
Debtors	8	**5,842**	3,237
Current asset investments	9	**5,530**	6,972
Cash at bank and in hand	9	**17,822**	8,826
		29,194	19,035
Creditors – amounts falling due within one year	10	**(13,514)**	(5,112)
Net current assets		**15,680**	13,923
Total assets less current liabilities		**17,690**	16,219
Creditors – amounts falling due after more than one year	11	**(1,704)**	(2,051)
Provisions for liabilities	13	**(231)**	(200)
Net Assets		**15,755**	13,968
Capital and reserves			
Accounting, auditing and corporate governance:			
– General reserve		**6,928**	6,016
– Corporate reporting review legal costs fund		**2,000**	2,000
Actuarial standards and regulation:			
– General reserve		**4,827**	3,952
– Actuarial case costs fund		**2,000**	2,000
		15,755	13,968

The financial statements and notes on pages 57 to 69 were approved by the Board of Directors on 4 July 2019 and signed on its behalf by:

Sir Winfried Bischoff
Chairman

Stephen Haddrill
Chief Executive and Accounting Officer

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Statement of Changes in Equity for the year ended 31 March 2019

	Accounting, auditing and corporate governance		Actuarial standards and regulation		
	General reserve	Corporate reporting review legal cost fund	General reserve	Actuarial Case cost fund	Total
	£'000	£'000	£'000	£'000	£'000
At 31 March 2017	3,912	2,000	2,204	2,000	10,116
Profit for the year	2,104	–	1,748	–	3,852
At 31 March 2018	6,016	2,000	3,952	2,000	13,968
Profit for the year	912	–	875	–	1,787
At 31 March 2019	6,928	2,000	4,827	2,000	15,755

As the FRC is a public body the use of cash represented by General Reserves is subject to approval by the Government.

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THE FINANCIAL REPORTING COUNCIL LIMITED

Cash Flow Statement for the year ended 31 March 2019

	Note	2018/19 £'000	2017/18 £'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Operating Profit		**1,721**	3,811
Adjustments for:			
– Depreciation and amortisation		**464**	422
– Increase in dilapidation provision		**31**	110
– (Increase)/Decrease in trade and other debtors	8	**(2,605)**	82
– Increase/(Decrease) in trade and other creditors	10	**8,055**	(613)
Net cash inflow from operations		**7,666**	3,812
Corporation tax paid		**(10)**	(14)
Total cash inflow from operating activities		**7,656**	3,798
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of tangible & intangible assets		**(171)**	(327)
Current asset investments sold		**1,442**	47
Interest received		**64**	55
Foreign exchange translation adjustment		**5**	–
Total cash outflow from investing activities		**1,340**	(225)
NET INCREASE IN CASH AND CASH EQUIVALENTS		**8,996**	3,573
Cash and cash equivalents at 1 April	9	**8,826**	5,253
CASH AND CASH EQUIVALENTS AT 31 MARCH	9	**17,822**	8,826

NOTES TO THE FINANCIAL STATEMENTS

1. PRINCIPAL ACCOUNTING POLICIES

The Financial Reporting Council Limited (the FRC) is a company limited by guarantee, incorporated in the United Kingdom, and its registered office is 8th floor, 125 London Wall, London, EC2Y 5AS. The company's registered number is 02486368.

The following principal accounting policies are those policies which have been applied consistently in dealing with transactions and balances that are considered material to the FRC.

The financial statements are prepared on the going concern basis of accounting. The Directors took into account the publication of the *Independent Review of the Financial Reporting Council* in December 2018, and the Government's response to, and initial consultation on the recommendations of, that review which was issued in March 2019. In time, the Directors expect the FRC to be wound up and replaced by a new statutory regulator, the ARGA. The ARGA will assume the existing functions of the FRC, but will have a wider range of powers and functions, and there will be a programme of transformation for the FRC to transition into the new statutory regulator. However, in assessing what might happen in the next twelve months, the Directors consider that the FRC will not cease operating and will continue to meet its debts as they fall due.

a) Basis of Preparation

These financial statements for the year ended 31 March 2019 are prepared in compliance with FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*. The Triennial review 2017 amendments to FRS 102 were applied for the first time in the FRC's financial statements for the year ended 31 March 2018 and continue to be applied in these financial statements, which is prior to their effective date; they have not had an impact on the reported results or financial position of the FRC, but some changes to disclosure were made.

These financial statements are prepared on an historical cost basis.

The preparation of financial statements requires the use of estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. Although these estimates and associated assumptions are based on historical experience and management's best knowledge of current events and actions, the actual results may ultimately differ from those estimates.

The estimates and underlying assumptions are reviewed on an on-going basis.

Provisions for dilapidations
Provisions for dilapidations is the area involving estimates and judgements where there is the greatest potential risk of a material adjustment in future years. The provision is expected to be utilised at the end of the lease.

Accounting estimate – The current provision is based on management's current best estimate of the future obligation. This year the estimate draws upon a prior valuation report provided by a third party surveyor.

Accounting judgement – In making the estimate management has exercised judgement about the likely future outcomes, including factors such as building and material costs. However various factors and changes in circumstances could affect any amount payable in the future.

Presentation of Financial Statements
The presentational and functional currency is the British Pound Sterling.

b) Revenue Recognition

Revenue is measured at the fair value of the consideration received or receivable. The FRC has predominantly the following sources of revenue:

- Revenue in respect of voluntary contributions is recognised on a cash basis.
- The following revenue is received from participants to fund specific activities:
  - Revenue receivable from RSBs for the FRC's activities as the competent authority for Audit in the UK is recognised on an accruals basis. Specifically, revenue receivable from RSBs in respect of Audit Quality Review and Audit Supervision costs is recognised as the costs to be recovered are incurred in each financial year.
  - Revenue receivable from various professional accounting bodies in respect of Accountancy disciplinary case costs and from RSB's in respect of Enforcement case costs is recognised as the

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costs to be reimbursed are incurred in each financial year.

- In addition there are some other smaller sources of revenue as listed below;
  - Revenue in respect of publications of books, guidance and standards is recognised on sale of goods or delivery of services.
  - Revenue in respect of inspection income for third country audit, the National Audit Office, the Public Sector Audit Appointments and Crown Dependencies is recognised as the work is delivered and the other party is required to pay.
  - Revenue in respect of XBRL taxonomy development activity is recognised as cost is incurred and the other party agrees that the project requirements have been met.

c) Tangible and Intangible assets

Depreciation is provided on all property, plant and equipment and amortisation is provided on all software at rates calculated to write off the cost, less estimated residual value (intangibles are assumed to have nil residual value), over their estimated expected useful lives on a straight line basis, as follows:

Tangible assets	
Office equipment	3 Years
Fixtures, fittings & furniture	10 years
Leasehold improvements	Lease term
Intangible assets	
Capitalised software	3 Years

Although the expected useful lives of some of these assets extend beyond the possible life of the FRC, as it will be replaced by ARGA, the timing of this is currently uncertain. BEIS has indicated that the existing assets (and liabilities) of the FRC will transfer to ARGA as part of the transition. Therefore in reviewing the estimates of the useful lives and residual values of the tangible and intangible assets the Directors do not expect a significant change in the consumption of the assets and the useful lives and residual values have not been revised.

d) Financial Instruments

Financial assets and financial liabilities are recognised when the FRC becomes a party to the contractual provisions of the financial instrument.

Cash and cash equivalents

These comprise cash at bank and other short-term highly liquid bank deposits with an original maturity of three months or less.

Current asset investments

These comprise bank deposits with an original maturity of more than three months but less than one year.

Debtors

Debtors do not carry any interest and are stated at their nominal value. Appropriate allowances for estimated irrecoverable amounts are recognised in the Profit and Loss account when there is objective evidence that the asset is impaired.

Trade creditors

Trade creditors are not interest bearing and are stated at their nominal value.

e) Case Costs and Fines

Case costs

The legal and professional costs of accountancy and actuarial disciplinary cases and Corporate Reporting Review cases incurred in the period are included in the financial statements on an accruals basis. Provision is made for the future costs of any disciplinary cases only where the contract is onerous, the costs are unavoidable and they represent a present obligation at the Balance Sheet date.

Fines and Cost Awards Receivable

Case costs awards receivable in respect of accountancy disciplinary cases, which are due to the relevant participant body under the Accountancy Scheme, are included in the income statement of the FRC, as a reduction to case costs incurred and associated revenue receivable. Fines received are not included in the profit and loss account as the FRC acts only as a mechanism whereby the fines are transferred from one party to another. When a fine is agreed and case costs are awarded, we recognise the amount due to the FRC as a debtor, and simultaneously recognise the amount payable to the relevant professional body as a creditor. Fines and costs awards are not paid over to the relevant professional body until they have been received by the FRC.

Fines receivable and case costs awards in respect of actuarial disciplinary cases are retained and included within revenue in the period in which the fines and case costs become due and collectable.

f) Components of Equity

As set out in the Statement of Changes in Equity, equity comprises the General Reserves of the FRC and two Costs Funds. As the FRC is a public body the use of cash represented by General Reserves is subject to approval by the Government.

Costs Funds

The costs funds are the Corporate Reporting Review Legal Costs Fund and the Actuarial Case Costs Fund.

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Contributions have been received to enable the Conduct Committee to take steps to pursue compliance with certain requirements of the Companies Act 2006 and applicable accounting standards and to investigate departures from those requirements and standards. Those funds may be used only for this purpose and may not be used to meet other costs incurred by the FRC. The FRC may be liable to repay the balance on the Legal Costs Fund to the contributors if it ceases to be authorised by the Secretary of State for the Department for Business, Energy and Industrial Strategy (BEIS) for the purposes of section 456 of the Companies Act 2006.

The Legal Costs Fund is currently maintained at £2m. Where use is made of these funds in the year, the funds are replenished the following year. BEIS has confirmed that if the legal costs fund falls below £1m in any one year, it will make a grant to cover legal costs subsequently incurred in that year.

The Actuarial Case Costs Fund consists of contributions received from the Actuarial Profession and through levies on pension schemes and insurance companies. The fund is used to fund investigations into potential misconduct by actuaries and any subsequent prosecutions.

g) Deferred lease Incentive

Deferred lease incentives are released on a straight line basis over the term of the lease.

h) Provision for dilapidations

A provision for dilapidations in respect of leased property is recognised based on the estimated amount required to settle obligations under the lease as at the Balance Sheet date.

i) Contingent liabilities

On 11 March 2019 the Government agreed that a new statutory regulator should replace the FRC. A programme of transformation for the FRC to transition into the new statutory regulator will take place. Despite the fact that BEIS has indicated that the existing assets and liabilities of the FRC will transfer to the ARGA as part of the transition, it is possible that additional obligations associated with the winding up of the FRC will arise. At present it is not probable that the FRC has incurred any relevant obligations and the amount of any possible obligations cannot be estimated reliably. The timing of any possible obligations will be dependent on the time taken for transition.

j) Taxation

The FRC is subject to Corporation Tax only on its interest receivable income. There are no temporary differences between the recognition of that income in the financial statements and the tax computation. Accordingly, there is no provision for deferred tax.

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2. OPERATING EXPENSES

	2018/19 £'000	2017/18 £'000
Core staff and related people costs (note 4)	**21,697**	21,677
IT and facility costs	**2,459**	2,499
Lease expense	**855**	766
Depreciation and amortisation costs	**464**	422
Auditor's remuneration:		
– audit	**52**	53
– non-audit services	**–**	–
XBRL taxonomy development costs	**271**	206
Accountancy and actuarial case costs – gross	**6,220**	6,619
– Less cost awards recovered	**(6,086)**	(3,336)
Accountancy and actuarial case costs – net	**134**	3,283
Other operating expenses		
– Travel and conferences	**485**	566
– Legal and professional fees	**986**	1,122
– Contribution to EFRAG	**309**	304
– All other costs	**1,072**	779
Total operating expenses	**28,784**	31,677

3. TAXATION

Corporation Tax at an effective rate of 19% (2017/18: 19%) on interest income of £81,000 (2017/18: £51,000).

As the FRC is subject to Corporation Tax only on its interest receivable income, no reconciliation between tax expense and profit on ordinary activities before taxation is presented.

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4. STAFF AND RELATED PEOPLE COSTS (INCLUDING DIRECTORS)

	2018/19 £'000	2017/18 £'000
Permanent staff:		
Salaries	**17,339**	16,721
Social security costs	**2,157**	2,042
Pension costs	**1,504**	1,408
Total permanent staff costs	**21,000**	20,171
Other people related costs:		
Seconded staff and contractors	**391**	338
Fees paid to Board, Committee and Council members	**1,433**	1,490
Other costs	**544**	510
Total staff and related people costs	**23,368**	22,509
Staff costs transferred to cases	**(1,671)**	(832)
Total core staff and related people costs	**21,697**	21,677

	2018/19	2017/18
Average no of permanent staff employed	**198**	184
Accounting, auditing and corporate governance including audit quality review and accountancy disciplinary cases	**193**	180
Actuarial standards and regulation	**5**	4

Directors' emoluments

	2018/19 £'000	2017/18 £'000
Fees and salaries (included in staff costs)	**1,115**	1,770
Other pension costs	**–**	31
Total directors emoluments (see page 50)	**1,115**	1,801
Social security costs	**134**	221
	1,249	2,022

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5. FINANCIAL RISK MANAGEMENT

The FRC's operations expose it to some financial risks. Management continuously monitors these risks with a view to protecting the FRC against the potential adverse effects of these financial risks. There has been no significant change in these financial risks since the prior year.

Financial instruments

The FRC's basic financial instruments in both years comprise cash in hand, current investments, loans, debtors and creditors that arise directly from its operations. A Government bank account has been opened for the FRC and from May 2019 money from the commercial bank account and matured deposits have been transferred.

The FRC has no long term borrowings or other financial liabilities apart from creditors.

Credit Risk

It is the FRC's policy to assess its debtors for recoverability on an individual basis and to make provisions when considered necessary. In assessing recoverability management takes into account any indicators of impairment up until the reporting date.

Depositing funds with commercial banks exposes the FRC to counter-party credit risk. The amounts held at banks at the year end were with banks with solid investment grade credit ratings. To reduce the risk of loss, the bank deposits are spread across a range of major UK banks. As these deposits mature, they will be invested with the Government Banking Service (GBS) which has minimal risk concerns.

Interest rate risk

The FRC invests the majority of its surplus funds in highly liquid short term deposits. The average interest rate on short term deposits for 2018/19 is 0.7% (2017/18: 0.7%) and none of the deposits has an original maturity of more than one year at the balance sheet date.

Liquidity risk

The FRC maintains sufficient levels of cash and cash equivalents and manages its working capital by carefully reviewing forecasts on a regular basis to meet the requirements for its day-to-day operations.

6. INTANGIBLE ASSETS

	Software £'000
Cost at 1 April 2018	465
Additions	21
Disposals	–
Cost at 31 March 2019	486
Amortisation at 1 April 2018	344
Disposals	–
Charge for year	55
Amortisation at 31 March 2019	399
Net book value at 31 March 2019	**87**
Net book value at 31 March 2018	121

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7. TANGIBLE ASSETS

	Leasehold improvements £'000	Office equipment £'000	Fixtures, fittings and furniture £'000	Total £'000
Cost at 1 April 2018	2,515	544	391	3,450
Additions	–	149	8	157
Disposals	–	(4)	(3)	(7)
Cost at 31 March 2019	2,515	689	396	3,600
Depreciation at 1 April 2018	875	254	146	1,275
Charge for year	234	134	41	409
Disposals	–	(4)	(3)	(7)
Depreciation at 31 March 2019	1,109	384	184	1,677
Net book value at 31 March 2019	**1,406**	**305**	**212**	**1,923**
Net book value at 31 March 2018	1,640	290	245	2,175

8. DEBTORS

	2018/19 £'000	2017/18 £'000
Trade debtors	**415**	292
Prepayments	**991**	745
Accrued income	**1,919**	2,031
Enforcement fines and cost awards	**2,439**	–
Other debtors	**78**	169
	5,842	3,237

9. CASH AND INVESTMENTS HELD

	Cash 2019 £'000	**Deposits 2019 £'000**	**Total 2019 £'000**	Cash 2018 £'000	Deposits 2018 £'000	Total 2018 £'000
Actuarial Case Costs Fund	–	2,000	2,000	–	2,000	2,000
Corporate Reporting Review Legal Costs Fund	–	2,000	2,000	–	2,000	2,000
General Accounts (1)	17,822	1,530	19,352	8,826	2,972	11,798
Totals at 31st March 2019	**17,822**	**5,530**	**23,352**	**8,826**	**6,972**	**15,798**

Note:
(1) Includes fines and cost awards of £5,645,000 received in March 2019 and paid to professional bodies in April 2019.

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10. CREDITORS – AMOUNTS FALLING DUE WITHIN ONE YEAR

	2018/19 £'000	2017/18 £'000
Trade creditors	**1,286**	323
Other taxation and social security	**751**	1,031
Accruals	**2,061**	1,812
Deferred income	**939**	1,080
Deferred lease incentive	**345**	344
Enforcement fines and cost awards payable to professional bodies	**8,083**	–
Corporation Tax	**15**	10
Other payables	**34**	512
	13,514	5,112

11. CREDITORS – AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	2018/19 £'000	2017/18 £'000
Deferred lease incentive	**1,704**	2,051
	1,704	2,051

12. SIGNIFICANT TRANSACTIONS WITH OTHER STANDARD SETTERS

With the agreement of HM Treasury, BEIS and the FCA, the FRC has, since 2008, taken the responsibility for collecting the UK contribution to the International Accounting Standards Board (IASB) alongside its preparers' levy. The FRC makes a small charge for providing this service. The amount of monies collected during the year was £849,000 (2017/18: £914,000), of which £27,000 (2017/18: £15,000) remained in creditors to be paid over by the FRC to the IASB as at 31 March 2019.

13. PROVISIONS FOR LIABILITIES

Leasehold improvements and dilapidations	2018/19 £'000	2017/18 £'000
Balance at 01 April 2018	**200**	90
Amount charged to Profit and Loss account	**31**	110
Balance at 31 March 2019	**231**	200

14. COMMITMENTS

Total commitments for the FRC under operating leases relating to the leasehold property were as follows:

	2018/19 Total £'000	2017/18 Total £'000
Payments due within one year	**824**	746
Payments due within two to five years	**3,294**	2,963
Payments due after more than five years	**846**	1,497
	4,964	5,206

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Total commitments for the FRC under operating leases for office equipment were as follows:

	2018/19 £'000	2017/18 £'000
Payments due within one year	9	14
Payments due within two to five years	5	11
Payments due after more than five years	–	–
	14	25

15. RELATED PARTY TRANSACTIONS

Transactions with related parties

Any related party transactions arise in the normal course of business and are not material.

Total key management personnel compensation

	2018/19 £'000	2017/18 £'000
Fees and staff costs	2,321	1,770
Other pension costs	73	31
	2,394	1,801
Social security costs	290	221
	2,684	2,022

The Executive Director Audit & Actuarial Regulation and the Executive Director Corporate Governance & Reporting stepped down from the Board on 31 March 2018. Until this date key management personnel had been deemed to be the Directors.

From 1 April 2018, as only one Executive Director (the Chief Executive Officer) is a member of the Board, key management personnel is deemed to be the Directors and the members of the Executive Committee (including any Acting members).

When members of key management personnel have served for part of a year, the amounts shown are for the relevant proportion of the year.

16. SUBSIDIARY UNDERTAKING

The FRC established a new subsidiary during the year. UK Accounting Standards Enforcement Board Limited (at 31 March 2019 its name was UK Endorsement Board Limited) is a company limited by guarantee of which the FRC is the sole member. Its registered office is 8th Floor 125 London Wall, London, United Kingdom, EC2Y 5AS. It did not trade during the period to 31 March 2019, and has not been consolidated because it is not material.

17. LIABILITY OF MEMBERS

The members of the FRC have undertaken to contribute a sum not exceeding £1 each to meet the liabilities of the Company if it should be wound up.

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FRC'S OVERSIGHT RESPONSIBILITIES 2018/19 - AUDIT, ACTUARIAL AND ACCOUNTANCY PROFESSIONS

1. **Executive Summary**
2. **Oversight of statutory audit: as the Competent Authority for statutory audit in the UK of the regulatory tasks delegated to the recognised supervisory bodies (RSBs) and its statutory oversight of recognised qualifying bodies (RQBs)**
3. **Oversight of local audit**
4. **Oversight responsibilities as the Independent Supervisor of Auditors General**
5. **Regulation of Third Country Auditors (TCAs)**
6. **Oversight of the Institute and Faculty of Actuaries (IFoA)**
7. **Governance review of the RSBs and IFoA**
8. **Oversight of accountancy professional bodies**

1 Executive Summary

1.1 This Appendix provides an overview of the findings in 2018/19 arising from, and the legal basis for, all our professional oversight responsibilities, as listed above. The key matters to note are set out below.

Oversight of statutory audit

1.2 The FRC is concerned about the risk to audit quality of including in the Joint Audit Register (the Register), without specific clarification, audit firms and responsible individuals with no recent statutory audit work, as they would lack recent audit experience. This needs to be immediately apparent to those using the Register to identify an auditor for statutory audit purposes. The FRC and the RSBs will set up a working group to design and implement a system to highlight those firms and individuals which have insufficient or no recent statutory audit experience. This system will be subject to FRC oversight.

1.3 The RSBs acknowledged the issues raised by the FRC in relation to audit quality monitoring in its 2017/18 RSB reports. One RSB worked with the FRC to improve how it evidences its risk analysis and judgements in key audit areas, particularly in relation to large and complex audits. However, as a result of our work this year, that RSB is required to provide better evidence of how it plans its reviews and assesses the risks associated with firms which have complex audits. We will review how all the RSBs have evidenced their work during our monitoring in 2019/20.

1.4 During 2018/19 we concluded that the RSBs and RQBs fulfilled their obligations as required in the 2016 Delegation Agreements with one exception. During the year the RSBs had still not agreed an audit quality key performance indicator (KPI) with the FRC as required by the Delegation Agreements. This matter has now been addressed and an audit quality KPI has been agreed. From 2019/20, the FRC will monitor performance against this KPI as well as the annual review activity indicators which were agreed last year.

Oversight of local audit

1.5 The FRC is responsible for overseeing the RSBs and RQBs for local audit, but because of the transition to implementation, some of the functions of the RSBs for local audit are not yet in operation. The ICAEW[8] is the only RSB, at the time of writing, that has firms registered with it for local audit. The first full financial year for the phase I local audit bodies ended on 31 March 2018. The audits of the financial statements were reviewed by the ICAEW on a sample basis during 2019. We will monitor these reviews as part of our 2019/20 oversight activity. We continue to work with the Ministry of Housing, Communities and Local Government (MHCLG) and other independent bodies responsible for the regulation and oversight of aspects of the local audit regime, to identify and manage the risks in this audit sector.

Oversight responsibilities as the Independent Supervisor of Auditors General

1.6 The overall results of our reviews of the NAO's Companies Act audits have declined since last year. This assessment is, however, based on reviewing only a small sample of Companies Act (the Act) audits. These may not be representative, so we intend to follow up on the NAO's root cause analysis in 2019/20 to ensure that appropriate and timely actions are taken to improve audit quality.

8 Institute of Chartered Accountants in England and Wales

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Regulation of Third Country Auditors (TCAs)

1.7 Of the five firms inspected by the FRC's audit quality monitoring (AQR) team, four required limited improvements and one required significant improvement. We will take action during 2019/20 to ensure the relevant third country audit firms address the quality issues raised.

1.8 The UK's TCA regime is ready to register European Economic Area (EEA) audit firms from the date of exit from the European Union (EU). The FRC has worked alongside the Department for Business, Energy and Industrial Strategy (BEIS) to prepare for exit from the EU (EU Exit), including for a scenario where there are no transitional arrangements.

Oversight of the IFoA

1.9 The IFoA is planning to implement a regime for monitoring the quality of actuarial work from September 2019. A significant amount of work is still required to achieve this outcome. We remain concerned about the ongoing lack of evidence to demonstrate the quality of actuaries' work in the UK.

Governance review of the RSBs and the IFoA

1.10 Our recent desktop review of governance of the RSBs and the IFoA highlighted the complexity of their regulatory governance arrangements. In 2019/20 we will follow up with each of the bodies through interviews with members of councils, boards and committees (including lay members), observation of behaviour at meetings and direct engagement with the bodies' relevant executive teams. We will focus particularly on evidence of the effectiveness of each body's governance of its regulatory activities, including evidence of how the public interest is represented in matters which are also of interest to its members. We will also engage with the bodies to identify actions to increase the transparency of the governance arrangements over their regulated activities.

Oversight of accountancy professional bodies

1.11 This year the FRC has seen an increase in the number of complaints about the bodies, particularly in complaints received from student members about the examination procedures. No trends were identified across the range of complaints received and there was no increase in the number of complaints upheld.

2 Oversight of statutory audit

2.1 We report annually:

- As the Competent Authority

  As the Competent Authority for statutory audit in the UK on our activities under the EU Audit Regulation (Audit Regulation) and under the Statutory Auditor and Third Country Auditor Regulations 2016 (SATCAR 2016). Since 2016, audit regulation tasks under this legislation are carried out by the FRC in its capacity as Competent Authority and by RSBs as delegates of the FRC, under terms set out in Delegation Agreements. The FRC reports in its annual report and accounts on the activities undertaken by it as the Competent Authority and in this appendix on the oversight of the tasks delegated to the RSBs; and

- As the Secretary of State delegate

  As the Secretary of State delegate under Part 42 of the Act we report on the accountancy bodies that are responsible for:

  (i) supervising the work of statutory auditors as set out in Schedule 10 to the Act;

  (ii) offering an audit qualification as set out in Schedule 11 to the Act, and

  (iii) the enforcement of statutory requirements under Part 42 of the Act.

2.2 Section 1252(10) of, and paragraph 10(3) of Schedule 13 to the Act, require the FRC to report annually to the Secretary of State on the discharge of these delegated powers and responsibilities.

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Recognised bodies and recognition criteria

2.3 To be an RSB, the body must satisfy the recognition criteria as set out in Schedule 10 of the Act; similarly, to be an RQB, the body must satisfy the recognition criteria as set out in Schedule 11 of the Act.

2.4 Individuals and audit firms that wish to be appointed as a statutory auditor in the UK must be registered with an RSB and individuals responsible for audit at registered firms must hold the appropriate audit qualification from an RQB.

2.5 The following are both RSBs and RQBs:

- Association of Chartered Certified Accountants (ACCA);
- Institute of Chartered Accountants in England and Wales (ICAEW);
- Institute of Chartered Accountants in Ireland (CAI); and
- Institute of Chartered Accountants of Scotland (ICAS).

In addition:

- Association of International Accountants (AIA) is an RQB; and
- There is a separate regime for local audit. Local audit RSBs and RQBs are discussed in Section (3) below.

Our enforcement powers against the Recognised bodies

2.6 As the Competent Authority, and under the terms agreed with the RSBs in the Delegation Agreements, where the FRC finds issue with an RSB's performance of a Delegated Task, the FRC may:

- Direct the RSB to do or refrain from doing a particular action;
- Reclaim a case or Delegated Task;
- Terminate the Delegation Agreement with that RSB; or
- Take such other measure(s) as the FRC deems reasonable and appropriate.

2.7 As Secretary of State delegate, the FRC also has the following range of statutory enforcement powers in relation to the recognised bodies' compliance with the required statutory criteria for their continued recognition under the Act as RSBs and RQBs:

- Direct an RSB or RQB to take specific steps to meet its statutory requirements or obligations;
- Seek a High Court order requiring an RSB or RQB to take specific steps to secure compliance with all statutory requirements or obligations;
- Impose a financial penalty on an RSB or RQB where it has not met a statutory requirement or obligation on it; and
- Revoke the recognition of an RSB or RQB where it appears to us that requirements for continued recognition have not been met.

FRC's oversight and monitoring procedures

2.8 The FRC follows a risk-based approach to determine the regulatory activities that we should focus on each year in addition to the monitoring activities of the different bodies. To help us plan and carry out our oversight role, each RSB and RQB provides an annual regulatory return, which includes information on their regulatory activities during the previous year. The regulatory plans are broad, forward-looking documents covering all significant work in progress. Each body is expected to inform the FRC immediately of any significant issues relevant to its role as an RSB/RQB to ensure that the FRC's views are considered before decisions are made.

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2.9 To discharge the FRC's responsibilities as the Competent Authority and the Secretary of State delegate, the FRC undertakes oversight activities throughout the year as follows:

- Understanding and documenting how each body meets all the statutory requirements for continued recognition, including information on how it complies with relevant legislation;
- Annual compliance testing of the way in which each body's regulatory systems operate in practice during monitoring visits and evaluating the effectiveness of specific aspects of the regulatory system;
- Reviewing and discussing the information in returns and regulatory plans submitted by the bodies;
- Keeping in regular contact with each body to discuss current issues, trends and future developments;
- Ensuring that the RSBs are compliant with the Delegation Agreement;
- Requiring specific actions or making recommendations arising from the activities above; and
- Ensuring our requirements and recommendations made in prior years have been implemented and have effectively addressed the issues raised.

Delegation by FRC to the RSBs

2.10 Under regulation 3(12), the Secretary of State may give Directions to the FRC in connection with the delegation of tasks to the RSBs. In the Direction issued pursuant to this provision, the Parliamentary Under-Secretary of State, Baroness Neville Rolfe, stated that: "The Government intend that the FRC should be the UK Competent Authority for the regulation of auditors, but that legislation will require it to delegate regulatory tasks so far as is possible to RSBs that meet criteria set out in the legislation".

FRC's oversight and monitoring of RSBs and RQBs in 2018/19

2.11 During 2018/19 we assessed each RSB's performance of its Delegated Tasks in relation to (i) audit registration, (ii) audit monitoring, (iii) enforcement and (iv) continued professional development (CPD), as well as its compliance with conditions in the Delegation Agreements for the delegation of tasks and with the general criteria for continued recognition as an RSB. We performed an in-depth review of audit registration at the RSBs, including de-registration procedures and the appropriateness of conditions and restrictions attached to initial and continued registration. In addition to this work, we changed the emphasis of our audit quality monitoring inspections from desktop reviews every two to three years, to annual on-site shadowing of the RSBs' monitoring visits to the firms.

2.12 Having implemented the FRCs' annual review activity KPIs[9] in 2017/18, the RSBs agreed an audit quality KPI[10] with the FRC, as required by the Delegation Agreement, during the first half of 2019. We will monitor the RSBs against these measures from 2019/20 to ensure audit quality is maintained or improved wherever necessary. See the "**RSB section**" for further details.

2.13 The FRC also carried out oversight monitoring of the RQBs. We assessed whether the RQBs' qualifications continued to meet the requirements of the Act, which include the requirements of Article 10 of the EU Audit Directive 2006/43/EC. We also completed (i) a review of the policies and procedures used by each RQB to authorise and monitor Authorised Training Offices (Training Offices), and (ii) a programme of accompanying the RQBs' inspectors performing monitoring visits at these firms. We found no significant issues with the policies and procedures of the RQBs and the monitoring visits were performed to a satisfactory standard. See the "**RQB section**" for further details.

9 a) 100% of Registered Auditors subject to an accelerated audit monitoring visit ordered by the relevant RSB Committee receive that visit within the timeframe specified by the relevant RSB Committee.

b) In cases where the audit monitoring visit report is submitted to the relevant RSB Committee for a decision, 100% of reports are issued by the registering RSB to Registered Auditors within 180 days from the date the audit monitoring visit is concluded.

10 75% of completed audit file reviews by the registering RSB on a Registered Auditor should require not more than limited improvements, i.e. should be grade 1 (ACCA: A) or 2A (ACCA: B). Where completed audit file reviews by the registering RSB on a registered auditor require more than limited improvements i.e. grade 2B or 3 (ACCA: C), the RSB will apply guidance agreed with the FRC to determine whether a root cause analysis should be conducted by the firm and, where appropriate, should ensure that such analysis is then submitted and considered as part of the relevant visit closedown process, which includes both initial and follow up regulatory action determined by the RSB as appropriate.

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Conclusions from oversight and monitoring 2018/19

2.14 Our principal conclusions are:

- The RSBs' complied with the terms and conditions of the Delegation Agreement;
- The RSBs and RQBs continue to meet the requirements of the recognition criteria of Schedule 10 and 11 of the Act;
- We were satisfied that the RQBs meet the requirements of the Act in relation to approving and monitoring of Training Offices, apart from AIA, which currently has no audit trainees; and
- The RSBs and RQBs continue to monitor the sufficiency of their staff and other resources in respect of their regulatory responsibilities and take their regulatory responsibilities seriously.

RSB Section

Key findings from oversight and monitoring of RSBs 2018/19

2.15 The following section summarises the findings from each of the RSBs in relation to:

- audit registration;
- audit monitoring;
- reviewing prior year requirements and recommendations; and
- compliance with the Delegation Agreement.

Audit registration

2.16 As the Competent Authority with the ultimate responsibility for audit regulation pursuant to SATCAR 2016, the FRC delegates to the RSBs certain of the regulatory tasks (audit registration, audit monitoring, enforcement and CPD) where it is satisfied that these bodies meet the criteria set out in Schedule 10 of the Act, as amended.

2.17 The FRC's audit registration monitoring work was carried out at the RSBs in 2018/19. We assessed the RSBs registration and de-registration procedures in respect of registering firms and their members and the appropriateness of conditions and restrictions attached to initial and continued registration. During the visits we tested a sample of applications for compliance with RSBs' rules and regulations and reviewed all supporting documentation. We assessed how the RSBs carried out their registration process, from collating the relevant documents, to following up queries and processing applications. We did not identify any systemic issues that raised concerns about the compliance by each of the RSBs with the delegation conditions and with the requirements of the Act.

2.18 We did, however, identify areas where we required or recommended actions, some within a specific timeframe, to improve the performance of the Delegated Tasks. We highlight below the key findings from our monitoring, some of which resulted in generic requirements and recommendations across all the RSBs. These actions will be tracked by the FRC throughout the course of 2019/20 and assessed during future monitoring visits:

- The RSBs were applying an inconsistent approach to assessing statutory auditor applications as there is no standard audit experience template;
- Statutory audit firms may remain on the register of statutory auditors despite not carrying out any statutory audit work for several years;
- Some audit firms apply to be registered statutory auditors to enable an accountant within the firm, who is a member of a chartered accountancy body, to carry out non-statutory audit work. Certain organisations, such as the Solicitors Regulatory Authority require certain types of non-statutory audit and accountancy work to be performed by a registered audit firm. However, some of these audit firms register solely for this purpose and do not perform any statutory audit work. There is a risk that such registered audit firms do not have sufficient recent relevant audit experience to carry out statutory audits to an acceptable standard. While the RSBs take steps to mitigate risks of this happening by imposing conditions on registration, and through monitoring, the lack of sufficient audit experience is not currently flagged on the Register, so any business or individual seeking a statutory auditor may be unaware of the risk. The FRC and RSBs will set up a working group in 2019/20 to consider both registration and transparency issues;

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- There was insufficient communication between ACCA, ICAEW and ICAS where there were changes in registration of their respective members which impacted on their continued status as statutory auditors with another RSB. Failure to notify another RSB of such changes could potentially lead to an individual signing audit reports whilst ineligible to do so; and
- It became apparent to the FRC that CAI, ICAS and ICAEW do not have formal policies in relation to medical disclosures. The risk is that their members may use medical conditions as a mitigation to reduce the sanction for a breach.

2.19 In addition to the generic requirements and recommendations listed above, we found the following specific areas where improvements are required or recommended:

ACCA

2.20 ACCA has the necessary arrangements in place to carry out its registration function. However, the high volume of annual returns it receives at 31 December each year makes processing inefficient at that time. We have recommended that ACCA stagger the due dates for some of its returns for audit firms and audit practitioners. ACCA's current practice could lead to errors being made in registering and de-registering audit firms and individuals if the volume of returns continues to increase at the end of each year.

CAI

2.21 Based on evidence from our sample, we found that although CAI was using the audit experience template previously recommended by the FRC, it was not requiring applicants to provide sufficient details of their previous audit experience to enable it to assess the applicant for the necessary competencies. The FRC's expectations have evolved over time to require more detail of an applicant's audit experience. To mitigate the risk that the Audit Qualification is awarded to those that are not sufficiently competent, we now require the RSBs to work with the FRC to agree a new template for assessing the audit experience of applicants.

ICAS

2.22 We were informed of two cases, one of which was a legacy case, where firms had notified ICAS of structural changes to their ownership that were not acted upon in a timely manner by ICAS. ICAS is currently developing a new IT system which will enable its staff to monitor notification activity more efficiently.

Audit monitoring

2.23 We have enhanced our approach to inspecting the RSBs' audit quality monitoring framework and procedures as a result of our 2017/18 findings. Since 2018, we performed inspection work in this area on an annual basis rather than once every two to three years. We also changed the basis of our work in this area from desktop reviews to on-site shadowing of the RSB audit quality monitoring teams through accompanied visits. The focus is on larger audits and we will report on findings annually. This approach allows the FRC to observe interactions between RSB and audit firm staff which was not previously possible through desktop reviews. It also means that RSB staff can demonstrate to the FRC how they respond to concerns on a real time basis. We set out below areas for improvement at each RSB.

ACCA

2.24 We did not identify any systemic issues where new requirements were raised with ACCA's audit quality monitoring processes, however, we found some areas for improvement. To ensure that the audit of financial reporting is conducted appropriately, we recommended ACCA perform a comprehensive review of disclosures in financial statements during audit monitoring visits and report all inconsistencies or errors identified to the audit firm.

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ICAEW

2.25 ICAEW is the registering RSB of the largest audit firms in the UK and consequently monitors audits of significant non-public interest entities (PIEs) with a public interest profile. During our 2017 inspection we raised concerns in relation to the lack of evidence recorded by ICAEW during audit monitoring visits. Our findings revealed that the level of documentation retained on ICAEW file reviews did not provide sufficient evidence of key elements of the review. These were: the rationale for selection of areas to review; the assessment of risk; the work performed; and the judgements applied in concluding whether the audit work was adequate. ICAEW has since updated its documentation template and has tested it on the large firm visits in autumn 2018. However, given the timing of the visits we shadowed in 2018/19, this requirement continues to remain open until we have concluded our audit monitoring work in 2019.

2.26 In 2018/19 we recommended the following improvements:

- The introduction of procedures and criteria for specialist reviews of International Financial Reporting Standards (IFRS) financial statements which are only being carried out on some audit monitoring visits with IFRS audit entities; and
- Planning audit monitoring visits to firms which have complex and higher risk audits to ensure that the team conducting the reviews has appropriate knowledge and experience.

CAI

2.27 During our 2017 inspection we raised concerns in relation to the consistency and extent of CAI audit quality monitoring documentation and required that both the rationale for the scope of its work and the basis for its conclusions should be evident and clear going forward. CAI updated its inspection methodology and checklist to address our concerns in 2018. This requirement also continues to remain open until we have concluded our audit monitoring work in 2019.

ICAS

2.28 We did not identify any systemic issues in respect of ICAS' audit quality monitoring processes, however, we found some areas for improvement. We recommended that ICAS should include the FRC's AQR team's priority sectors and areas of focus in its audit monitoring selection criteria. ICAS confirmed that it updated its manual accordingly in January 2019. We also recommended that ICAS should communicate all findings relating to financial statement disclosures to the audit firm so it can improve its audit procedures in this area. There should be clear documentation of decisions not to include in the firm's report, findings relating to financial statement disclosures. If audit file or firm visit grades have not been impacted this should also be clearly documented.

Reviewing prior year requirements and recommendations

2.29 The review of actions taken in respect of prior year requirements and recommendations did not raise any significant concerns. However, some of these requirements and recommendations remain open as actions taken by the RSBs are currently in progress or are going through the appropriate RSB's internal governance process. We considered it appropriate to give the RSBs more time to complete their processes in these areas. We will assess progress during future monitoring visits.

Compliance with the Delegation Agreements

2.30 Based on our work to assess compliance with the conditions for Delegated Tasks in Appendix 1 to 4 of the Delegation Agreements, we have concluded that each RSB:

- Has adequate arrangements in place to process audit registrations and withdrawals.
- Has adequate policies and procedures to monitor Registered Auditors who have carried out Companies Act audits.
- Has adequate arrangements in place to carry out CPD monitoring of Registered Auditors and confirm they maintain an appropriate level of competence in the conduct of Companies Act audits.
- Has adequate arrangements in place to carry out enforcement activities effectively.

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RQB Section

Key findings from oversight and monitoring of RQBs 2018/19

2.31 We assessed whether the RQB qualifications continued to meet the Act's requirements, which include the requirements of Article 10 of the EU Audit Directive 2006/43/EC. We assessed the process used by each of the RQBs to approve and monitor Training Offices. We continue to make recommendations for improvements through our ongoing oversight activities, which are summarised below:

AIA

2.32 We are concerned that there have been further significant delays in updating the AIA syllabus. The AIA was due to introduce the new syllabus for the May 2020 exam sitting, however, this is now expected to be introduced at the November 2020 exam sitting. Although this delay represents a low risk as AIA has no audit trainees at the current time, we will continue to monitor AIA's progress and expect to review the completed revised syllabus, learning materials and sample examination papers during 2019 for any future AIA audit trainees.

ICAEW

2.33 There were no significant findings. However, we recommended that the ICAEW improves its controls to ensure that visits to Training Offices are carried out within the required time frame.

CAI

2.34 We found that in a small number of Training Offices the person appointed as the Training Principal did not meet all the requirements of CAI's training regulations. The CAI required the affected Training Offices to rectify this and implemented additional procedures.

2.35 In previous years we made recommendations that were due to be addressed by the implementation of the CAI's new IT system which became fully operational in 2017. During our visit we assessed the changes made to the Charted Accountants Diary System (Diary). The new system addresses our prior recommendations, however, the system had implementation problems which the CAI were working to address. We have recommended that the CAI implement a system of testing to ensure that the system provides accurate information and we will review the CAI's approach to testing in 2019/20.

2.36 The CAI relies upon the mentor and Training Principal at the Training Office to ensure that the work experience in the CAI Diary is completed and categorised correctly. During our review we identified one student who had been awarded the audit qualification based on invalid work experience. There were no adverse consequences in respect of the work carried out by the student and the individual's audit qualification has since been withdrawn. We recommended that the CAI improve the guidance it provides to firms and should consider alternative methods to gain assurance that the experience is categorised accurately. CAI has agreed to perform additional checks to reduce the risk of the audit qualification being awarded to individuals who have not obtained the correct work experience. We also identified a potential concern regarding the adequacy of resources to meet the CAI's regulatory objectives. The CAI has assured the FRC that additional resources will be made available. We will obtain updates from the CAI on a regular basis.

ICAS

2.37 To ensure that the training provided meets ICAS' requirements, we recommended that the ICAS improves two areas in its processes for monitoring Training Offices; i) the assessment of CPD; and ii) the link between its review of the quality of training provided by the Training Office and the students records of their training experience.

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3 Oversight of local audit

3.1 Following the winding up of the Audit Commission, a new regulatory regime for the audit of local government and National Health Service (NHS) bodies (local audit) was established by government through the Local Audit and Accountability Act 2014 (LAAA). MHCLG set up a Delivery Board, responsible for identifying the risks and overseeing the implementation of the new regime. The FRC together with the local audit RSBs and other bodies involved in the oversight and regulation of local audit are members of this Board. Its objective is to ensure that the effectiveness of the new regime is maximised, and risks are identified and managed, through engaging with the large number of interested bodies involved.

3.2 The Secretary of State delegated to the FRC responsibility for overseeing the RSBs and RQBs for local audit. Because of the transition to implementation, some of the functions of the RSBs for local audit are not yet in operation. The FRC is required to enforce the requirements for recognition of local audit RSBs and the award of the local audit qualification by local audit RQBs under sections 1252 and 1253 of the Act. Section 1252(10) and paragraph 10(3) of Schedule 13 of the Companies Act 2006 as they apply to local audit by virtue of Schedule 5 to the LAAA, require the FRC to report to the Secretary of State once in each calendar year on the discharge of its powers and responsibilities.

3.3 Individuals and audit firms that wish to be appointed as a local auditor in the UK must be registered with a local audit RSB and individuals responsible for audit at registered firms must hold an appropriate audit qualification for local audit.

3.4 The ICAEW and the ICAS were recognised as RSBs for local audit in November 2015. In addition to the four statutory RQBs, the Chartered Institute of Public Finance and Accountancy (CIPFA) was recognised as an RQB, for local audit only, in October 2014. The ICAEW is the only RSB, at the time of writing, that has firms registered with it for local audit.

3.5 The MHCLG decided that the transition from the old local audit regime to the new regime under the LAAA should be carried out in two phases; Phase I comprised the NHS bodies which transitioned on 1 April 2017 and phase II comprised all other local public bodies which transitioned on 1 April 2018. The first full financial year for the phase I bodies ended on 31 March 2018 and the audits of these financial statements were reviewed by the AQR team and RSB on a sample basis during 2019. We will monitor the RSB's reviews as part of our 2019/20 oversight activity.

3.6 After the implementation of the LAAA, the audit regulatory regime for company audits changed as a result of the Audit Regulation and Directive (ARD). There are now significant differences between the company and local audit regimes, even though the intention of LAAA was to align them. In particular, the FRC is not the Competent Authority for local audit. There is a public interest risk that users of the accounts of local authorities and bodies mistakenly believe that corporate and local audit regimes are the same. There are differences in audit quality monitoring procedures as well as the determination of sanctions following failures identified through monitoring. Increasing economic constraints on the public sector and public scrutiny of failures in such bodies further heighten the risks. As indicated above (3.1) we are working with MHCLG and other bodies to address the risks.

Key findings from local audit oversight and monitoring 2018/19

3.7 During 2018/19 our oversight of the local audit RSBs focussed on ensuring that they had implemented our previous recommendations in their registration of key audit partners and local audit firms and their monitoring of CPD. We also assessed the appropriateness of all updated policies, procedures and systems for supervising relevant audit firms and key audit partners.

3.8 We are satisfied that the ICAEW has implemented our previous recommendations. We are also satisfied that both the ICAEW and the ICAS have appropriate procedures for monitoring the ongoing competence of key audit partners and local audit firms.

3.9 We conducted a monitoring visit at the CIPFA during 2018/19. The purpose of the visit was to review the procedures to award the Local Audit Qualification. The audit qualification was awarded correctly, but we found that improvements should be made to the checklist to make it clearer that all the CIPFA requirements have been met.

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4 Oversight responsibilities as the Independent Supervisor of Auditors General

4.1 The Statutory Auditors (Amendment of Companies Act 2006 and Delegation of Functions etc.) Order 2012 designates the FRC as the Independent Supervisor of the Comptroller and Auditor General (C&AG) and the other Auditors General, in respect of their work as statutory auditors of companies under the Act.

4.2 Section 10, Schedule 13 of the Act requires the Independent Supervisor to report on the discharge of its responsibilities at least once in each calendar year to the Secretary of State, the First Minister of Scotland, the First Minister and the Deputy First Minister in Northern Ireland, and to the First Minister for Wales. This report meets the statutory reporting requirements.

4.3 The C&AG and the other Auditors General are eligible for appointment as the statutory auditors of companies under the Act, subject to meeting certain conditions.

4.4 One of those conditions is that an Auditor General is subject to oversight and monitoring by an "Independent Supervisor" in respect of Companies Act audit work. To date, only the C&AG has entered into the necessary arrangements with the FRC and undertakes audits under the Act. The year to 31 March 2018 was the tenth year in respect of which staff at the NAO undertook Companies Act audit work, auditing the accounts of 62 companies. The NAO fulfils this role alongside its other work, which it undertakes under different statutory provisions. As a statutory auditor the NAO may audit those companies that are owned by Government Departments and other public bodies whose financial statements it audits. The responsibilities of the Independent Supervisor do not extend to the wider work of the C&AG and the term "statutory audit" should be read as meaning the NAO's remit under the Act.

Supervision arrangements

4.5 Section 1229 of the Act requires the Independent Supervisor to establish supervision arrangements with any Auditor General who wishes to undertake Companies Act audit work, for:

- Determining the ethical and technical standards to be applied by an Auditor General;
- Monitoring the performance of Companies Act audits carried out by an Auditor General; and
- Investigating and taking disciplinary action in relation to any matter arising from the performance of a Companies Act audit by an Auditor General.

4.6 These supervision arrangements are set out in a Statement of Arrangements and Memorandum of Understanding (MOU) between the FRC and the C&AG and include a requirement for the monitoring of the C&AG's Companies Act audit work by the FRC's AQR team, on behalf of the Independent Supervisor.

Reporting requirements

4.7 We report below in accordance with section 1231 of the Act and article of Statutory Auditors (Amendments of Companies Act 2006 and Delegation of Functions etc.) Order 2012 (SI 2012/1741).

Discharge of supervision function

4.8 The supervision arrangements require that the C&AG and relevant NAO staff follow technical and ethical standards prescribed by the FRC when conducting Companies Act audits and set out the investigation and disciplinary procedures that would apply were there a need to discipline the C&AG in his/her capacity as a statutory auditor. The relevant standards are those set by the FRC for auditors generally.

4.9 We meet periodically with the C&AG and senior staff responsible for the audit practice of the NAO on behalf of the C&AG. We have familiarised ourselves with the NAO procedures to discharge these responsibilities and keep abreast of any changes.

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Compliance by Auditors General with duties under the Act

Scope of 2018/19 inspections

4.10 As noted above, to date only the C&AG has undertaken Companies Act audits, all of which were of companies within the public sector.

4.11 During 2018/19 the AQR team's inspection of the C&AG's Companies Act 2017/18 audit work comprised updating its understanding of the NAO's policies and procedures supporting audit quality that applied to these audits; and reviewing the performance of selected aspects of four of the 62 statutory audits carried out by NAO staff in respect of financial periods ended on 31 March 2018 (we reviewed four 2016-17 audits during 2017/18). The sample chosen covered audits of varied complexity, size and risk. Given the increased number and complexity of Companies Act statutory audits performed by the C&AG, including five public interest entity (PIE) audits, we keep under review the number of Companies Act audits that we review each year.

4.12 The responsibilities of the Independent Supervisor do not extend to the work of the C&AG other than in relation to statutory audit.

Key findings

4.13 The overall results of our reviews of the NAO's Companies Act audits have declined since last year, with two of four assessed as requiring more than limited improvements, as compared with one of four in 2017/18. Two Companies Act audits were assessed as good or requiring limited improvements. Across the reviews, there are findings that the NAO needs to address.

4.14 The NAO should consider the learning from these inspections and ensure it is applied consistently throughout its audit practice. The NAO's root cause analysis should consider why, given the wider improvements the NAO has made during the year, the overall results of the audits have declined compared to last year.

4.15 We set out below the key improvements required to safeguard and enhance audit quality and safeguard auditor independence:

- Broaden and intensify the extent of challenge in areas of judgement and key assumptions used in valuations and estimates. Audit teams should also consider contradictory evidence in assessing valuations and estimates.
- Ensure substantive testing procedures are appropriate to provide a sufficient level of audit evidence in relation to revenue and inventory to conclude whether the risk of material misstatement has been sufficiently mitigated.

4.16 Our review of the NAO's processes, policies and procedures supporting audit quality included a review of the complaints procedures, staff matters and a follow-up review of prior year findings. The NAO should continue to monitor the independence of their business relationships and ensure transparency and safeguards are applied in respect of all audited entities.

Progress made in the year

4.17 We recognise the NAO's continuing work to enhance its policies and procedures supporting and promoting audit quality. Examples of this work include addressing lessons learnt from previous AQR reports, improving the scope and coverage of its own internal cold reviews and identifying thematic issues so that these are more effectively embedded within individual audits.

4.18 The NAO has increased the number of responsible individuals authorised to perform statutory audits on behalf of the C&AG to seven (2017/18: six).

4.19 We recommended in our report last year that the NAO perform root cause analysis on the one Companies Act audit assessed by the FRC as requiring more than limited improvements. The findings on this review included how the role of the NAO's engagement quality control review (EQCR) is discharged and evidenced so that the responsibility for the audit direction, supervision and performance of the audit is consistently performed and evidenced on the NAO's files for contracted out audits.

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4.20 The NAO carried out reviews on three thematic areas:

(i) Contracted-out audits, in consideration of the prior year AQR review findings on a Companies Act contracted review and to address internal concerns raised by the NAO over contracted-out audits;
(ii) Delegated audits for non-Companies Act audit, given the lower NAO cold review scores; and
(iii) What leads to a 'good' audit?

4.21 We reviewed NAO's root cause analysis performed on AQR's prior year findings and we are satisfied that the NAO has taken appropriate actions. We will review the impact of these actions on audit quality in 2019/20.

Notification by Auditors General under Section 1232 of the 2006 Act

4.22 No Auditor General was required to notify the Independent Supervisor of any other information under Section 1232 of the Act.

Independent Supervisor's enforcement activity

4.23 We issued no enforcement notices and made no applications for compliance orders in 2018.

Account of activities relating to the Freedom of Information Act

4.24 We received no requests for information under the Freedom of Information Act in our role as the Independent Supervisor.

5 Regulation of TCAs

5.1 The Act, the Statutory Auditors and Third Country Auditors Regulations 2013 (SATCAR 2013) and SATCAR 2016 set specific requirements for the regulation of the auditors of UK traded non-EEA companies (Third Country Auditors or TCAs). The FRC is responsible for applying these requirements to TCAs in the UK.

5.2 All TCAs are required to be registered with the FRC before they may sign any UK audit reports for their UK traded non-EEA entities. Where a TCA is not subject in its home country to a system of oversight, quality assurance review and discipline which is recognised by the European Commission as being equivalent, the FRC is required to subject the registered TCA to its systems of oversight and quality assurance review. The underlying principle is that all auditors of companies traded on EU-regulated markets should be subject to equivalent regulation, regardless of where the relevant issuer is incorporated.

Audit quality monitoring

5.3 The FRC is required to review the audit quality of TCAs from jurisdictions which have not been assessed as equivalent[11] or transitional[12] on a cyclical basis. We apply a system which is proportionate to the risk profile of the issuer and the jurisdiction. Our audit quality monitoring of TCAs focuses on those UK market-traded companies considered to be of significance to UK investors.

5.4 In the year to 31 March 2019, our sixth year of inspections, we completed inspections of selected aspects of five audits at five TCA firms; one in each of five countries: India, Oman, Vietnam, Nigeria and Kazakhstan. Four of the audits were categorised as "limited improvements required" and one as "significant improvements required". AQR will follow up on actions to improve audit quality with the firm that performed the audit requiring significant improvements during 2019/20.

11 Where it is determined that a country has a public oversight, quality assurance, investigation and penalty system for auditors and audit entities that operate under similar rules to those set out in Article 29,30 and 32 of Directive 2006/43/EC.

12 Is based on an assessment that the jurisdiction is making substantial progress towards setting up an audit regulatory system equivalent to that required in the EU.

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5.5 Carrying out inspections of audit firms widely scattered across the world, and with typically only one or two relevant audited entities, poses legal and practical challenges in some jurisdictions. Local confidentiality laws can hinder access to audit working papers for the purposes of the FRC performing an inspection. We endeavour to overcome these challenges when they arise and require TCAs to confirm, at the point of registration as a TCA and during annual renewals of registration, whether there are legal restrictions that would preclude the FRC from performing an inspection of its relevant audit(s). Where such restrictions exist, we require the TCA to resolve them by, for example, obtaining consent from the audited entity or by redacting certain information in its audit working papers to satisfy local confidentiality laws. However, TCAs are not always able to resolve such restrictions and therefore the FRC is not able to register them as TCAs.

De-registration procedures

5.6 The FRC also has the power to remove a TCA from the UK register of TCAs in certain circumstances set out in the Act and SATCAR 2013. The procedures followed by the FRC in such instances are set out in the Third Country Auditor Register Procedures, available on the FRC website[13].

EU Exit

5.7 A significant objective in the year was to ensure that the UK's audit regulation arrangements remain fit for purpose after the UK exits the EU. The focus has been on preparations for a "no deal" exit with the EU, as this would result in the most additional work for the FRC, the audit firms and the entities subject to audit. The FRC has been the central point of contact between BEIS, the professional bodies and the audit firms in relation to EU Exit work.

TCA registration

5.8 Arrangements are in place for audit firms in EEA member states to register with us where they audit an entity traded on a regulated market in the UK. We also contacted EEA competent authorities to encourage them to be ready to register UK audit firms who need to do so.

Equivalence and Adequacy

5.9 We undertook preparatory work aimed at ensuring that the UK is ready to submit its applications to the EU for assessment of Equivalence and Adequacy status in relation to audit as soon as possible after the UK has left the EU. We also considered and evaluated options for assessing the Equivalence and Adequacy of EEA states.

The Committee of European Auditing Oversight Bodies (CEAOB)

5.10 During the year the FRC continued to participate in the International Equivalence and Adequacy sub-group of the CEAOB. This group considers the equivalence of audit regimes and the adequacy of data protection laws of non-EEA countries. On 31 July 2019 the transitional equivalence of four countries and the transitional adequacy of two countries are due to expire. The FRC has been involved in the reassessments of these countries.

5.11 We also continue to participate in the CEAOB's market monitoring subgroup. This sub-group has been responsible for producing market monitoring indicators and an audit committee survey for use in producing the European Commission's triennial report on developments in the audit market. The next report will relate to the three years ending 16 June 2019 (three years after implementation of the ARD).

5.12 Our ongoing participation in these CEAOB subgroups depends on the outcome of EU Exit.

Ireland

5.13 EU Exit will end the long-standing arrangements whereby UK auditors and Irish auditors are able to sign audit reports for entities in each other's jurisdictions. This has been possible because the RSBs that registered these auditors were themselves recognised in both jurisdictions. After EU Exit, UK auditors will have to cease providing audit services to their Irish clients until they have passed an aptitude test and registered as Irish auditors. We, together with BEIS have held meetings with Irish government officials, the Irish Auditing and Accounting Supervisory Authority (IAASA) and representatives from the RSBs and major audit firms to discuss how the process of re-registration might be simplified where appropriate.

13 https://www.frc.org.uk/auditors/professional-oversight/third-country-auditors/regulatory-background

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Communications

5.14 We communicated with audit firms, professional bodies and competent authorities to ensure they have the information necessary to make decisions and that we become aware of any problems that may arise as a result of the process of the UK leaving the EU. We have held discussions with firms and bodies and have issued a public letter from both BEIS and the FRC providing guidance for individual auditors and for audit firms.

6 Oversight of the IFoA

6.1 The FRC assumed responsibility in 2006, at the request of Her Majesty's Treasury, for the non-statutory oversight of the regulation of the actuarial profession by the IFoA. This followed the recommendation of the Morris Review of the Actuarial Profession (published 2005).

6.2 This oversight arrangement is established through a MOU with the IFoA, updated in 2014. Under the MOU, the FRC oversees the way in which the IFoA regulates its members when acting in their professional capacity.

6.3 The FRC undertakes an annual programme of work to discharge its oversight responsibilities, established in consultation with the IFoA. This programme of monitoring visits, oversight of relevant activities and recommendations to the IFoA is risk-based and focuses on issues that could have an adverse effect on the public interest and on public confidence in actuaries. Matters arising from the FRC's 2018/19 work programme are summarised below.

The IFoA's proposals for monitoring the quality of actuarial work

6.4 Neither the quality of actuarial work nor compliance with actuarial standards is directly monitored. As a result, there remains a lack of independent evidence of the quality of actuarial work and of compliance with actuarial standards in the public interest. This restricts the opportunity to pre-empt potential detriment to the public interest.

6.5 To bridge this gap, the IFoA plans to introduce a scheme to monitor its members' work. During the first quarter of 2018/19, we continued to provide significant input to the IFoA's development of its proposal and its consultation material, to increase the likelihood that an effective monitoring regime is established. After the IFoA's consultation closed in September 2018, we reviewed the independent analysis of the consultation results and the IFoA's project plan. We have continued to impress upon the IFoA the need for detailed planning with milestones and the commitment of appropriate resources to develop an effective regime. The IFoA has met all of its project milestones to date. Owing to the significant amount of work needed to implement the monitoring regime, we remain concerned about the timely delivery of this project.

6.6 The IFoA announced its post-consultation conclusions in February 2019. The first phase of the IFoA's monitoring scheme will comprise thematic reviews complemented by wider information gathering activities. We support the thematic review approach as these have the potential to cover the full spectrum of actuaries' work in the public interest; a weakness is that they will rely on voluntary submission of information for monitoring. We have urged the IFoA to include some direct review of actuarial work in the initial phase of thematic reviews. We have set out our expectation that these reviews should commence in line with the IFoA's original proposed deadline of September 2019 as we are not persuaded that the case for introducing monitoring at the earliest opportunity has diminished. The IFoA continues to explore alternatives to the mandatory enhanced level of monitoring previously proposed for IFoA members who hold practising certificates (PCs) as their work includes public interest roles.

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The IFoA's review of its practising certificate framework

6.7 The IFoA completed a review of its PC framework in 2018/19 and concluded it was not necessary at that point to propose any new PC requirements but that this would be kept under review.

6.8 We have asked the IFoA to develop a framework in 2019/20 to review regularly whether there are other areas of actuarial involvement where it would benefit the public interest to introduce PCs, based on its consideration of the underlying risks. From our oversight of the IFoA's review, we are currently unpersuaded that any of the existing PC requirements should be withdrawn.

Draft guidance to the Actuaries' Code

6.9 The IFoA published the revised Actuaries' Code on 18 May 2018 as scheduled; this took effect from May 2019. During 2018/19, we engaged with the IFoA until it had addressed our concerns about the clarity of its draft guidance to the Actuaries' Code (the Code) and the potential for the guidance to undermine the Code's enforceability. We consider that the guidance is now fit to support the new Code.

Implementation of standards

6.10 We continue to oversee the IFoA's initiatives to raise its members' awareness of both regulation and standards of professionalism and ensure that the IFoA keeps current regulation on its members' agenda once it has become 'business as usual'. The IFoA published further professional skills training materials for its members in 2018/19 which were embedded through significant member engagement and this was well received. The IFoA continues to promote changes to the technical actuarial standards (TASs) produced by the FRC, through regulatory updates sent to all members in answer to professional support queries and at regulatory and professionalism CPD events. During 2018/2019, the IFoA provided TAS training to volunteers in key roles in the professional body and developed some TAS training materials for use in professional skills training. While the IFoA has many face-to-face opportunities through its regulatory update events, it is not clear that it uses them to remind actuaries of all the applicable standards, particularly TASs. We would encourage the IFoA to portray the technical standards as core to the profession and promote them to the same extent as the non-technical standards developed by the IFoA. It is clearly in the public interest to do so.

6.11 We reviewed the IFoA's report on the post-implementation review of Actuarial Profession Standard (APS) X2: Review of Actuarial Work, which it completed in the second quarter of 2018. We were concerned that the sample size was too low and insufficiently representative across public interest practice areas to give credible information upon which to base regulatory policy. We have asked the IFoA to seek further evidence that APS X2 is being applied appropriately, both now and in the future, for example through its proposed monitoring activities. We recommended that the IFoA's proposed follow up actions should be more clearly targeted to firmly address any concerns it identified in the post-implementation review.

Quality Assurance Scheme (QAS) for employers of actuaries

6.12 We have received quarterly reports from the IFoA on the operation of its voluntary QAS including the IFoA's initiative to monitor the progress made by accredited members in applying best practice to their quality control procedures. Of the IFoA's UK members, 22% now work in QAS accredited entities. While this is a very positive take up for a voluntary compliance regime, the UK figure is similar to last year. It is regrettable that no UK insurers have applied for QAS accreditation so far, as this could facilitate the IFoA's monitoring work in some areas of public interest. We continue to encourage the IFoA to promote QAS membership actively to a wide cross-section of UK actuarial employers.

Key findings from actuarial oversight and monitoring 2018/19

6.13 We carry out our oversight through monitoring relevant IFoA regulatory activities. In 2018/19, we visited the IFoA's offices in Oxford and completed an interim desktop review of progress against the recommendations made in 2017/18. The results of our visit and our desktop review are set out below.

6.14 Building on our 2017 visit to IFoA's Oxford office, we selected a sample of cases during our 2018 visit to assess further the effectiveness and practical application of IFoA policies and procedures in relation to professional examinations. We also followed up our prior year recommendations and points to note and reviewed updated documents and procedures.

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6.15 We recommended the following improvements to the examination procedures, based on the findings from our 2018 visit to Oxford. Our recommendations were consistent with the IFoA's planned activities and significant progress has already been made to date:

- The IFoA should complete the planned implementation of its e-marking approach as soon as possible as this will reduce the risk of human error when uploading candidates' marks. E-marking was recently implemented for many of the IFoA's examinations at the April 2019 sitting.
- The IFoA executive should manage, train and review self-employed contractors in exam related roles more closely and should ensure that exam markers' input is always clearly documented. New processes and documentation were implemented to facilitate this recommendation.

6.16 We also carried out a desktop review to follow up the recommendations and points that arose from our 2017 visit to IFoA's Edinburgh office in the areas of complaints and discipline, PCs and CPD.

6.17 We are generally content with the progress IFoA made on our prior recommendations other than one in relation to non-standard PC applications. We have set targets for this and four other open recommendations to be concluded in 2019/20. The majority of the other prior year recommendations will be addressed through IFoA's planned review of its Disciplinary Scheme, or otherwise, in 2019/20.

7 Governance review of the RSBs and the IFoA

7.1 During the year the FRC commenced a review of the RSBs' governance arrangements for the performance of the delegated regulatory tasks. We also commenced a similar review of the IFoA's governance arrangements for actuarial regulation. At the time of writing we have completed a desktop review of documents setting out the governance arrangements of each of these bodies. We need to follow up on our interim findings during 2019/20. This will include an in-depth review of how governance is effectively implemented in practice and how it promotes a strategy for ongoing development of regulation at each body. We will focus on how each body's governance arrangements ensure due consideration of the public interest. For the purpose of this report we have summarised below our interim findings to date. The term body (bodies) refers to the RSBs and the IFoA in this section only.

7.2 All the bodies have a complex arrangement of boards and committees, reporting directly or indirectly to a council, which represents the professional membership. The details of these arrangements are set out in the bodies' charters, bye-laws, rules and regulations. Most of these documents are publicly available on their websites. Based on our review to date, we consider that improvements could be introduced by the bodies to make their governance processes more transparent. We will require further guidance and clarification from the bodies to improve our understanding of the structure of their boards and committees under council and their respective responsibilities. Although all the bodies produce public reports and some produce separate reports on their regulatory activities, these do not always provide specific evidence of the influence and impact of the governance arrangements. We will engage with the bodies to identify actions to increase the transparency of the governance arrangements over their regulatory activities.

7.3 The public interest is represented by engaging lay-persons on boards and committees who are not members of the professional body. We will investigate further whether the composition of boards and committees with regulatory responsibilities enables appropriate discussion on technical and public interest matters. As well as considering the core skills required, some bodies also consider the diversity of their lay persons. All the bodies have procedures to consider independence of members for some of their governance entities, however, the transparency of these procedures varies.

7.4 We will report on our overall findings, together with our final conclusions and recommendations, in next year's report.

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8 Oversight of accountancy professional bodies

8.1 By agreement with the six chartered accountancy bodies[14], we exercise a degree of oversight in relation to the bodies' regulation of the non-statutory activities of their members who are not registered auditors. This voluntary arrangement between the accountancy bodies and the FRC operates in the public interest and is governed by an exchange of letters in 2003 between the FRC and the Consultative Committee of the Accountancy Bodies (CCAB). In discharging this oversight responsibility, the FRC makes recommendations and seeks to influence but cannot enforce these recommendations against these bodies.

8.2 In 2017/18 the FRC and the bodies were developing MOUs with the CCAB bodies and the Chartered Institute of Management Accountants (CIMA) for our non-statutory oversight of non-audit accountancy-based activities. However, these MOUs were placed on hold pending the outcome of the independent review of the FRC, which has recommended that the FRC should continue its oversight role of the accountancy profession, but with a work programme sufficiently wide and expert to identify any emerging concerns of public interest. The FRC intends to re-engage with the bodies during 2019/20 to finalise MOUs on the future scope of its work.

Current oversight activities

Complaints

8.3 Most of the FRC's accountancy oversight currently relates to the processing of complaints made by members of the public who are dissatisfied about the way in which their original complaint has been handled by one of the bodies. When such complaints are referred to the FRC, any ensuing reviews focus on whether the body followed its own rules, processes and procedures in its consideration of the complaint. Where the FRC finds that a body has not followed its own procedures, it makes a recommendation to the body to address any failings.

8.4 This year the FRC has seen an increase in the number of complaints about the bodies, particularly in complaints received from student members about the examination procedures. No trends have been identified across the range of complaints received and there has been no increase in the number of complaints upheld.

14 At the time this agreement included ACCA, ICAEW, ICAS, CAI, CIPFA and CIMA. Although CIMA is no longer a member of the CCAB, the FRC continues its oversight role in respect of CIMA much in the same way as it does with the CCAB members.

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Abbreviations

Acronym	Name in full
ACCA	Association of Chartered Certified Accountants
AIA	Association of International Accountants
AIM	Alternative Investment Market
APS	Actuarial Profession Standards
ARAC	BEIS Partner Bodies Audit and Risk Assurance Committee
ARGA	Audit, Governance and Regulation Authority
BAME	Black, Asian and Minority Ethnic
BEIS	Department for Business, Energy and Industrial Strategy
C&AG	Comptroller and Auditor General
CAI	Institute of Chartered Accountants in Ireland
CCAB	Consultative Committee of Accountancy Bodies
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CIMA	Chartered Institute of Management Accountants
CIPFA	Chartered Institute of Public Finance and Accountancy
CPD	Continuing Professional Development
EEA	European Economic Area
EFRAG	European Financial Reporting Advisory Group
EU	European Union
FCA	Financial Conduct Authority
FRS	Financial Reporting Standard
GDPR	General Data Protection Regulation
GIAA	Government Internal Audit Agency
IAASB	International Auditing and Assurance Standards Board
IASB	International Accounting Standards Board
ICAEW	Institute of Chartered Accountants in England and Wales
ICAS	Institute of Chartered Accountants of Scotland
IFIAR	International Forum of Independent Audit Regulators
IFoA	Institute and Faculty of Actuaries
IFRS	International Financial Reporting Standards
ISA	International Standards on Auditing
ISAs (UK)	International Standards on Auditing (UK)
JFAR	Joint Forum on Actuarial Regulation

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LAAA	Local Audit and Accountability Act 2014
MoU	Memorandum of Understanding
NAO	National Audit Office
NHS	National Health Service
PIEs	Public Interest Entities
PRA	Prudential Regulation Authority
PSAA	Public Sector Audit Appointments
QAS	Quality Assurance Scheme
RQBs	Recognised Qualifying Body
RSB	Registered Supervisory Body
SATCAR	Statutory Auditor and Third Country Auditor Regulations
SORP	Statement of Recommended Practice
SoS	Secretary of State
TAS	Technical Actuarial Standard
TCA	Third Country Auditor
TEG	Technical Experts Group
UK GAAP	United Kingdom Generally Accepted Accounting Practice
XBRL	eXtensible Business Reporting Language

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