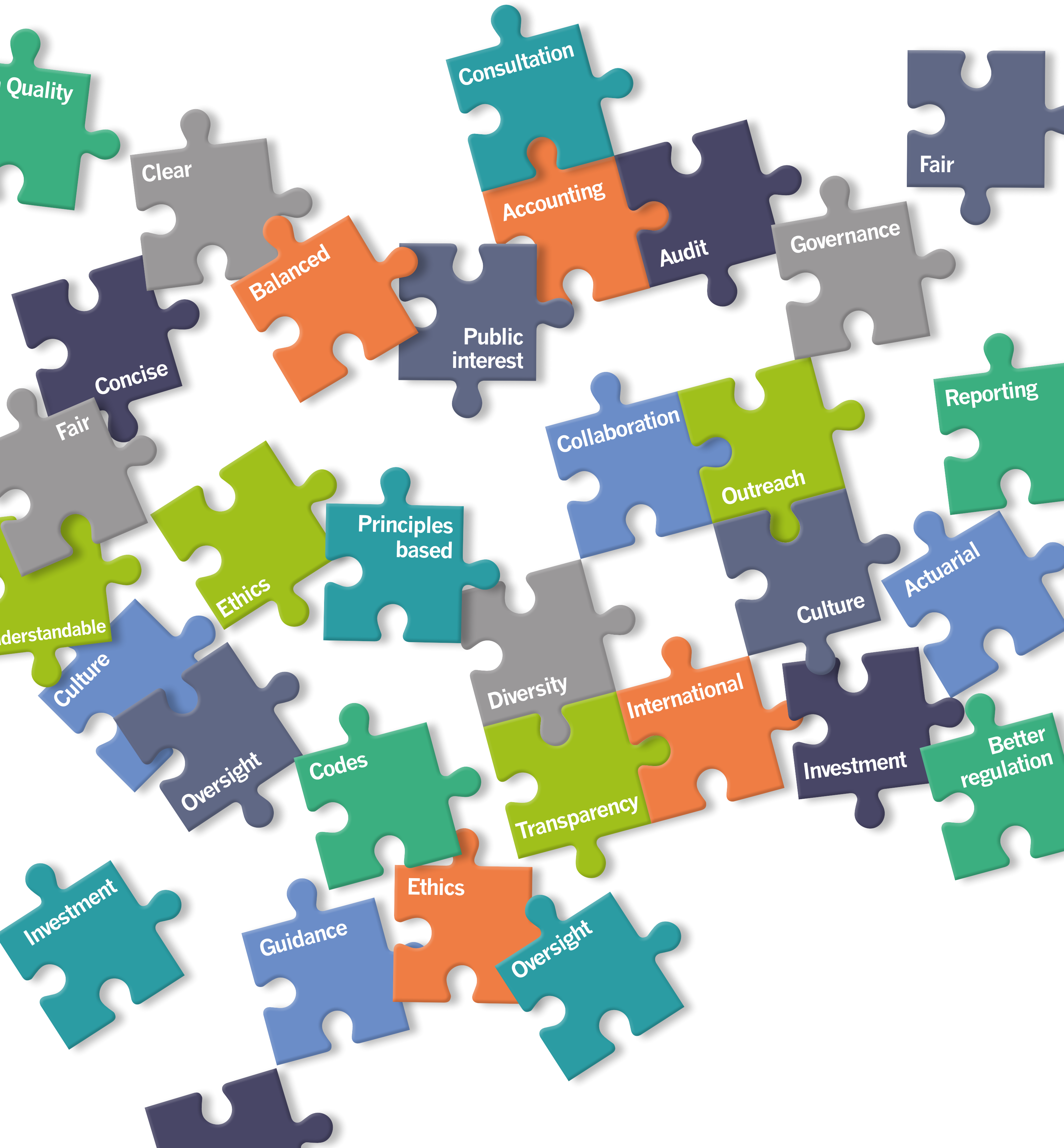
Financial Reporting Council

Annual Report and Accounts 2014/15



ANNUAL REPORT AND ACCOUNTS OF THE FINANCIAL REPORTING COUNCIL

- INCLUDING THE REPORT OF THE INDEPENDENT SUPERVISOR

YEAR TO 31 MARCH 2015

The Report of the FRC 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.

Accounts presented to Parliament by command of Her Majesty.

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.

HC325

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Contents

Our Mission

To promote high quality corporate governance and reporting to foster investment

Our Values

We work in the public interest, seeking at all times:

- to be **joined up** to make the most of the breadth of our role
- to **reach out** to our stakeholders to secure their expertise
- to be **evidence-based** to ensure our decisions are soundly-reached and respected
- to be **decisive** to ensure problems are addressed in a timely manner
- to **show respect** to others; recognising the value in different perspectives

Chairman's Statement

The fact that successive governments and the market have asked the FRC to take on additional responsibilities suggests that we have a track record of exercising them effectively. But no matter how good our past record has been, we cannot take our future success for granted.

Sir Winfried Bischoff – Chairman

2015 marks the FRC's 25th anniversary. Originally established in 1990 to be responsible for setting and monitoring UK accounting standards, the organisation has evolved significantly since then. We have taken on an increasing range of responsibilities, which now also cover corporate governance and investor stewardship, audit and assurance, actuarial work and oversight of the accounting and actuarial professions, and have grown as a result. However, we are and wish to remain a relatively small organisation, even though we will expand further if we are asked to become a competent authority for the regulation of the audit profession under the EU Audit Regulation and Directive.

The fact that successive governments and the market have asked the FRC to take on additional responsibilities suggests that we have a track record of exercising them effectively. But no matter how good our past record has been, we cannot take our future success for granted.

When I succeeded Baroness Hogg as Chairman in May 2014 after her four successful years in the role, I was keen to make my own assessment of whether we are well placed to deal with the challenges ahead. We set in hand the necessary work to develop our next three year strategy, for 2016/19, including the way we raise our funds and develop our people. We are evaluating the impact of the reforms to our structure and statutory powers in 2012. And we have instituted a review of the effectiveness of our monitoring of the quality of corporate reporting and auditing.

I have personally spoken to many of those we regulate, those who benefit from our activities, and those whom we seek to work with and influence. We have also undertaken a stakeholder survey to understand better how we are viewed.

Overall the feedback has been positive. The FRC is seen as being close to the markets, consultative and willing to listen, with greater coherence and focus to our structure and statutory powers than before the 2012 reforms. We are also seen as influential by those organisations we deal with in the EU and internationally.

Of course, there is room for improvement. In common with other regulators, we have begun to see signs of regulatory fatigue amongst those with whom we deal. We also heard that we need to do more to understand the views of, and impact of our work on, investors.

During the year we undertook an internal review of the effectiveness of our board, committees and advisory councils, and assessed progress following the independent evaluation carried out in 2013/14. The results of the review are reported on page 37.

In addition, the Nominations Committee has reviewed the FRC's non-executive succession planning across the full governance structure. We concluded that the skills and stakeholder representation were appropriate but identified the need to appoint to the Board individuals with actuarial experience and experience in the non-listed sector. I am pleased that John Coomber and Ray King will join the Board shortly. Ray will now chair the Audit and Assurance Council and both will join the Codes & Standards Committee.

While we will not underestimate the challenges facing us, I believe we are in a good position to cope with them.

In developing our three-year strategy for 2016/19 we must not lose sight of our primary mission to foster investment and must keep the needs of investors at the front of our mind. We need to remain focused on our priorities, measuring success by the impact we make, not by our level of activity. We need to maximise that impact by continuing to work collaboratively with fellow regulators and others such as the professional bodies. We need to avoid imposing unnecessary burdens on those we regulate, taking a non-regulatory approach wherever possible, being particularly mindful of any adverse impact on small, growing companies.

We will continue to improve how we communicate with all of our stakeholders, including a number of initiatives focussed on the investor community. We are particularly keen to engage closely with Government and Parliament to ensure there is good understanding of our work and its effectiveness. And we need to make sure we have the right structures, people and resources to carry out our responsibilities effectively and efficiently.

Our approach to governance has enabled us to focus on key strategic issues, with our Board, Committees and Councils taking on much of the 'heavy lifting' on matters that require detailed scrutiny. This has enabled us to make further progress in delivering the priorities we set for our 2013/16 strategy – including updating the UK Corporate Governance Code to promote a clearer focus on risk, internal control and the assessment and reporting of companies' longer-term viability.

I should like to take this opportunity to thank the many Committee and Council members who support the work of the Board and also to thank Stephen Haddrill and the executive team for their continuing support and commitment.

In January 2015 we announced that Jim Sutcliffe had stood down from the Board and from his Chairmanship of the Codes & Standards Committee, having formerly served as Chairman of the Board for Actuarial Standards. His contribution in these capacities has been highly valued. John Stewart stood down from the Board and the Codes & Standards Committee from July. I would like to take this opportunity to thank both Jim and John for their advice and commitment to the work of the FRC.

Sir Winfried Bischoff

Chairman

13 July 2015

1 Strategic Report

1.1: Chief Executive's Overview

We aim for our codes and standards to be adopted because companies, their investors and the professions believe they make sense.

Stephen Haddrill – Chief Executive

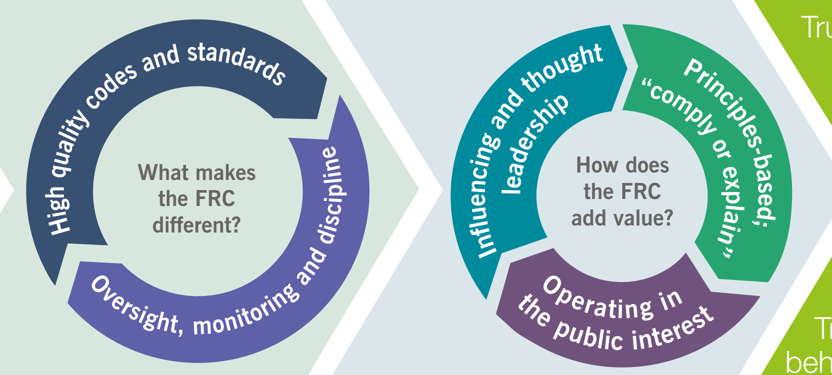
Our Mission

The FRC's Mission is to promote high quality corporate governance and reporting to foster investment. A secure flow of investment into the UK's capital markets, driven by high quality governance and reporting, helps underpin the growth of our economy and our competitiveness.

Our work is designed to encourage the provision of trustworthy information to investors and to encourage trustworthy behaviour by boards of companies and the professions. In addition, we seek to build justified confidence internationally in the UK regulatory framework for corporate governance and reporting.

Our business model:

The FRC is the UK's independent regulator responsible for promoting high quality corporate governance and reporting to foster investment



Our Values and Approach

We have a wide range of responsibilities in relation to corporate reporting and audit quality. However, we do not rely on legal powers alone. We also set codes and standards and promote best practice. We aim for our codes and standards to be adopted because companies, their investors and the professions believe they make sense, rather than because they have to comply. We achieve this through reaching out to our stakeholders – consulting with all parties in developing our proposals, seeking always to listen and adapt to better ideas.

We also try to ensure that our codes and standards are based on principles that promote the exercise of good judgement by directors and others. They are not sets of rules to be followed without proper thought. In some areas, such as corporate governance, we enable companies to 'comply or explain'. This gives them time to think through new priorities and to take steps that best meet the needs of their shareholders. Knowing there is such flexibility, companies have sometimes supported more radical proposals.

However, there is also a need for strict requirements in certain circumstances, backed by consistent and fair monitoring and enforcement.

Accounting standards must be followed to ensure trustworthiness and comparability of information between companies to aid investment decisions. We therefore monitor compliance with standards, require companies to apply them and, if necessary, take action to secure compliance.

Successive governments and the EU have required companies to have an external, independent, audit. Audit exists to provide investors with confidence in the trustworthiness of the company's financial statements and it is essential to that goal that the auditor is also worthy of trust. We also, therefore, set, monitor and enforce compliance with auditing standards.

As a final safeguard of quality and integrity, if accountants, auditors or actuaries do not deliver on the professional standards they espouse, we will take disciplinary action to address misconduct.

> Our stakeholder survey shows, however, that we need to do more in building bridges across the board to investors, listening better to them and achieving this is a focus for us this year.

The monitoring and enforcement of principles-based standards is a challenge. Testing judgements made by companies under principles is harder than assessing compliance with rules. We therefore ensure that our regulatory conclusions are subject to close review within the FRC executive and to governance oversight by experienced non-executives.

Some stakeholders find it confusing that the FRC seeks to be both attentive to the views of its stakeholders and tough if it finds poor performance, but we think this combination of approaches serve investors well, and the FRC does hold to one overriding principle, that across all its operations it should focus on achieving outcomes that are evidence-based and proportionate to the challenge it seeks to address. Nevertheless, feedback from stakeholders makes it clear that we need to communicate more effectively the rationale for our decisions and we are considering how to do this.

Our Strategy

We established our current three year strategy to deliver our mission in 2013 in the wake of the review and reform of the organisation and its powers conducted jointly with the Department for Business, Innovation and Skills (BIS). The strategy sought to address the issues that had emerged from the financial crisis in relation to governance and reporting.

Our analysis of the effectiveness of governance and reporting in the UK at that time was that it was generally strong and compared well with that in other capital markets. However, we also identified some important impediments to the delivery of our mission:

- Some boards had not taken a sufficiently long-term view of their company's prospects and as a result had failed to identify and report effectively the risks they faced. Indeed, a small number of companies had failed shortly after confirming themselves to be a going concern.
- Although there was generally constructive engagement between the larger listed companies and their shareholders this was not the case across the listed sector or Stewardship Code signatories as a whole.
- Corporate reporting was growing in volume, but not quality. It was not providing a clear agenda for shareholders in relation to their engagement with directors and, in consequence, their impact on boards was sub-optimal.
- There was reduced confidence in the audit profession following the financial crisis.
- The FRC's work in monitoring the quality of company reports and auditing was generally well regarded. However, our sanctioning of poor performance was felt to be weak and slow, and the lessons of our monitoring work were known to too few directors and others in business.

Actuaries came through the financial crisis without such criticism. In this case, the need was to ensure that the FRC's standards for actuarial work remained up to date, reflecting changes in the nature of actuarial work and lessons from how well the standards were applied in practice.

In the light of this analysis, the FRC adopted five strategic priorities:

- High quality corporate governance and investor stewardship which foster trust in the way companies are run.
- High quality corporate reporting that is fair, balanced and understandable.
- High quality audit and confidence in the value of audit.
- Actuarial oversight and standards which underpin high quality actuarial practice, and the integrity, competence and transparency of the actuarial profession.

- Effective, proportionate and independent investigative, monitoring and disciplinary procedures.

Our progress on each of these priorities is summarised in the next section of the report. We believe we have made significant progress.

We recognised that for effective delivery of our strategy our work needs to be joined up. We aim to create integrated solutions making the most of our range of powers and responsibilities. For example, we have used the UK Corporate Governance Code, auditing standards and audit monitoring together to enhance confidence in audit.

Our work also needs to be pursued in collaboration with other regulators, both in the UK and overseas. Businesses, and the professions, cross national borders. The quality of the audit of a multinational British business, for example, is highly dependent on work done and, in many cases, regulated abroad. The FRC therefore needs to continue to influence and provide thought leadership at an international level. Our work is highly respected and shows leadership in key areas such as extended audit reporting.

At the same time, investors and those we regulate have a reasonable expectation that UK regulators will be joined up to ensure their work is effective, without gaps or overlaps. To that end, the FRC has signed Memoranda of Understanding covering its relationships with other regulators and meets regularly with them to identify emerging risks. This year the Joint Forum on Actuarial Regulation, for example, produced a map of risks in actuarial work to help regulators and the profession focus on and mitigate risk.

Challenges to our strategy

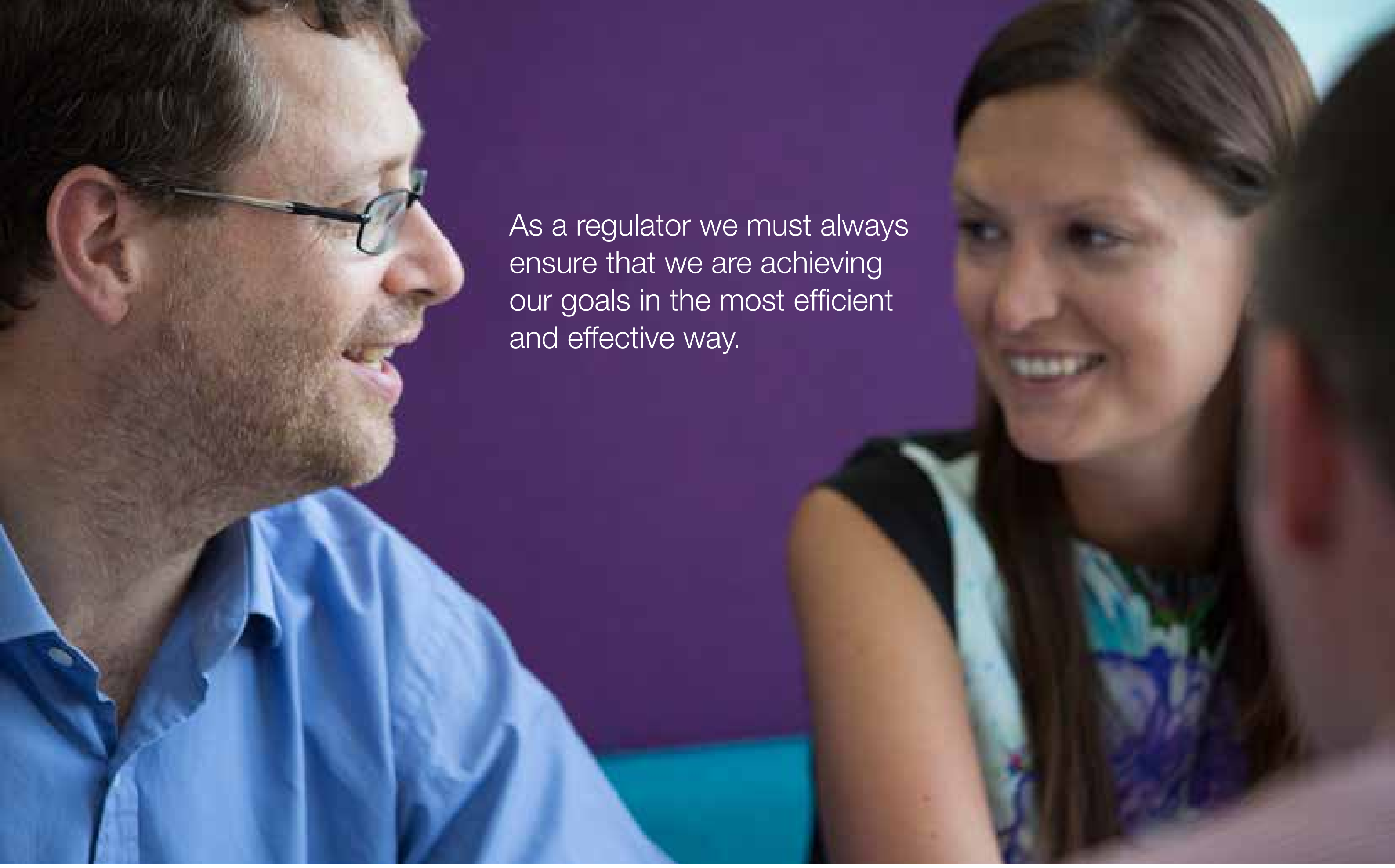
The effectiveness of the FRC's strategy could be thrown off course by unintended consequences of the changes we have introduced. These concerns are reflected in the principal risks to our ability to deliver our mission (page 29) and include:

- That strengthening the framework could undermine confidence in the short term by highlighting deficiencies. We recognise this risk. However, we feel it is more important to demonstrate that material concerns are being tackled.
- That new requirements could create exhaustion with regulation rather than higher standards, with directors and other professionals responding in formulaic ways rather than by enhancing the quality of their judgement and communication, resulting in more clutter and 'boilerplate' in reports undermining transparency for investors. We have therefore monitored implementation closely, such as through our review of extended auditor reporting; promoted clear and concise reporting; and supported implementation through the work of the Financial Reporting Lab.
- That more competition in audit could undermine rather than stimulate quality. We are therefore monitoring the impact on pricing and on quality. Initial signs are that there is emerging competition, primarily on grounds of quality rather than price, in relation to large companies' audit retendering, and that audit committees are paying more attention to the results of our audit inspections.

These concerns are reflected in the principal risks to our ability to deliver our mission (page 29).

We also face a mixture of challenges of an on-going nature, to which we are applying close attention:

- That investors do not meet the expectations of the Stewardship Code and make the most of the changes to reporting through good quality engagement with companies. We have worked closely with the Investment Association and Investors' Forum to understand the quality of engagement and are now reviewing the Stewardship Code and its impact.
- That the FRC's leadership and staff may not keep pace with the changes in the market and the way companies approach governance and reporting. We must aim continually to improve. We are wholly committed to being a great place to work that invests in its people. We have introduced a regular and detailed Board-led review of executive succession planning and invested more in staff development, including a 'Future Leaders' programme.
- As noted above, the pace of our disciplinary work has been a concern. Our 2013/16 Strategy included a step increase in the speed and effectiveness of our disciplinary processes whilst at the same time clearing the backlog of cases, and we have made good progress. However, the MG Rover disciplinary case highlighted the challenge of operating the disciplinary scheme efficiently. This is the first case under our accountancy disciplinary scheme that has gone through the full process of investigation, prosecution, tribunal and appeal tribunal. The appeal tribunal supported a number of the original tribunal's findings in favour of the FRC and rejected others. It also correctly drew attention to the length of time it took to complete the investigation, the quality of the expert advice and the cost of the investigation. The reforms to the disciplinary scheme since 2012 address many of these issues. We will reflect very carefully on the lessons of the MG Rover case and consider whether further reforms are necessary.
- Our oversight of the actuarial profession was reviewed in 2013. We have since consulted on changes to our technical standards. We have also established the Joint Forum on Actuarial Regulation (JFAR) with the Prudential Regulation Authority, Financial Conduct Authority, the Pensions Regulator and the Institute and Faculty of Actuaries. We now need to address the monitoring of actuarial work. At present, in the absence of monitoring, we lack hard evidence of the effectiveness of the regime. Following on from the publication of its Risk Perspective, JFAR will conduct a number of in-depth reviews into specific risks where actuarial work is relevant, including understanding the size of any potential issue, defining the relevant actuarial work more precisely and testing controls.



As a regulator we must always ensure that we are achieving our goals in the most efficient and effective way.

- We are supporting BIS in their consultation on the implementation of the new Audit Regulation and Directive, which was introduced in June 2014. The work of the FRC is likely to expand however the legislation is implemented, with a significant increase in the number of audit firms to be monitored and a new arrangement for the oversight of the professional bodies in relation to audit matters. The legislation requires the new regime to be in place by June 2016. Given the scale of change required this timeframe is very tight. We have had to commit considerable resource to planning and implementation at the expense of some delay to other projects.

- As a regulator we must always ensure that we are achieving our goals in the most efficient and effective way. The implementation of the Audit Regulation and Directive will represent an important step in our regulatory responsibilities for audit. It should also be a moment when we consider more generally how well we go about our job as a regulatory authority. Our approach should be proportionate; our standards should promote quality without inhibiting innovation; our monitoring and enforcement activities should support the achievement of high standards. And we must ensure that we are, and are seen to be, accountable to investors and all those with an interest in our work. As part of committing to continuous improvement we have contracted McKinsey to undertake a major review of how our monitoring work can be most effective.

- Across all its work the FRC is affected by EU Law. We work hard to ensure that the strengths of the UK regulatory framework are respected and that new EU legislative proposals reflect UK conditions. We have had particular success in making the case for 'comply or explain' in governance and in moderating the costs of the original proposals for audit regulation. In the next two years the UK referendum creates a risk that other EU members will pay less attention to UK concerns. We will therefore work even harder to ensure our expertise is provided and listened to. The FRC Board has, for example, met recently in Brussels to engage with key members of EU institutions.

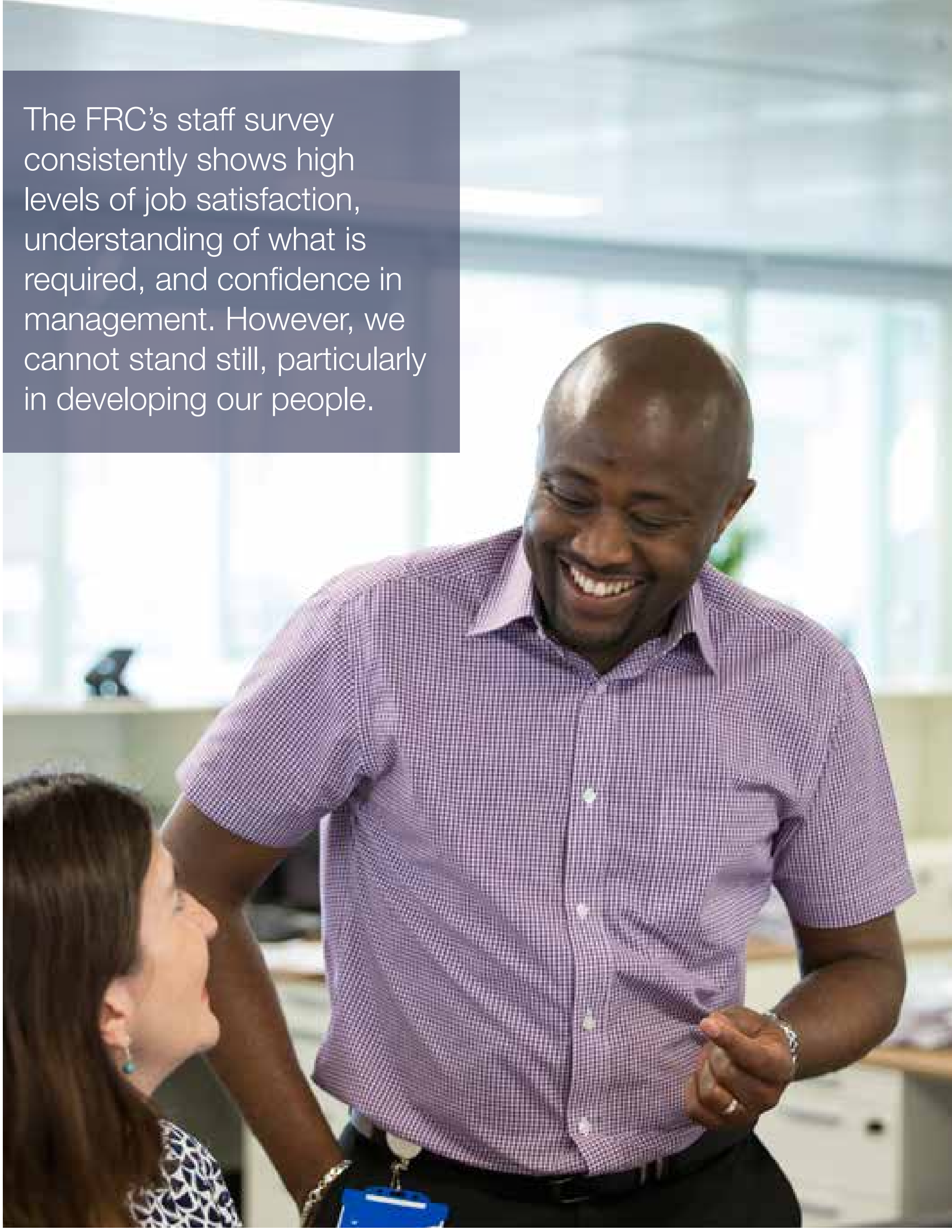
Our future strategy

I believe that the FRC has made good progress in delivering the priorities that we set ourselves in 2013. However, some of the issues we address cannot be solved quickly – particularly where we are seeking to bring about changes in culture and behaviour – and some of the risks and challenges we face will always be with us. Many of these issues will therefore also be major components of our next three year strategy, covering 2016/19.

We have begun to lay the groundwork for the new strategy during 2014/15. As the Chairman reported in his statement, we are reviewing our strategic objectives and our regulatory approach, including by looking at the effectiveness of our monitoring of corporate reporting and audit quality. The results of these considerations will be set out in a draft strategy that will be published for consultation later in 2015. We will also look at the effectiveness of our influencing of International Financial Reporting Standards (IFRS).

We are also considering whether as an organisation we are fit for the future. We are assessing and will report in our next strategy whether the reforms to our structure and statutory powers in 2012 have had the intended impact, and whether further changes might be needed as we prepare to take on new and expanded responsibilities. We are also reviewing our funding arrangements and are developing our people to ensure that we have the capabilities to carry out our role effectively and efficiently.

> The FRC's staff survey consistently shows high levels of job satisfaction, understanding of what is required, and confidence in management. However, we cannot stand still, particularly in developing our people.



Our people

The FRC is a good place to work for both our experienced professional staff and for people in their earlier careers who are looking to gain experience in an organisation that works in the public interest, provides real intellectual challenge and focuses on developing talent. The FRC's staff survey consistently shows high levels of job satisfaction, an understanding of what is required, and confidence in management. However, we cannot stand still, particularly in developing our people.

Our strategy requires us to have a wide range of skills and capabilities amongst our staff. As a standard setter and monitor of work in the largest and most complex companies, we need people who, for example, are amongst the most technically strong accountants in the country. We also need excellent communicators who can explain the reasoning behind policy and regulatory decisions and demonstrate that those decisions make business as well as technical sense. In these respects we need to invest more in sectoral business knowledge.

Communication and business skills also need to be allied to knowledge of the international environment in which we operate so we can strengthen our influence. Development is also needed to strengthen our talent pool for senior positions. Our efforts are guided by a new approach to performance management that involves development plans for all and systematic succession planning for senior positions. We have also increased our investment in training and development across the company.

Our success also depends on the effectiveness of the relationship between the executive, the Board and its Committees. The governance reviews showed this to be strong and constructive. This is most important to me and my senior team and we commit to preserving it. The executive as a whole particularly appreciate the attention given by the Board to their development, with a number of Board members mentoring staff, and listening to staff issues including through review of the staff survey and the Chairman's breakfasts with staff groups.

Our External stakeholders

Our effectiveness depends on having good, constructive, and when necessary, appropriately challenging relationships with our stakeholders. We seek to achieve this by reaching out – one of our values – in a systematic series of engagements. We have two public meetings a year to hold ourselves accountable for our plans. We have regular meetings at every level with the professional bodies who are co-regulators in raising professional standards and with whom we need to maintain a strong partnership whilst properly discharging our oversight role. We have started having an annual policy conference and on individual issues we have regular roundtables. The Financial Reporting Lab alone has involved nearly 300 people in its work. Our stakeholder survey shows, however, that we need to do more in building bridges across the board to investors, listening better to them and achieving this is a focus for us this year.

Our Funding

We need a stable revenue stream to discharge our responsibilities and pursue our strategy. Many of our responsibilities are imposed by law and cannot be cut. Other work is the subject of strong public expectation that it will be delivered. Some of our funding is provided by the professional bodies on the basis of contractual arrangements; the other elements of our funding are provided on a voluntary basis. We seek to ensure that we continue to have a stable and secure basis on which to operate.

Stephen Haddrill

Chief Executive Officer

1.2: Progress against 2013/16 Strategy

Overview

First Steps

Our new strategy was designed to be unfolded gradually over 2013/16. We sought initially to strengthen the commitment of boards to the importance of reporting being fair, balanced and understandable. We felt this would stimulate a change in mind-set based on realism and openness and that that would create the right conditions for future change. We also believed this requirement would act as an antidote to formulaic, boilerplate text.

The effectiveness of audit was a central theme for 2013/14. We asked audit committees to report on all significant matters they had discussed, including their assessment of the audit. We believed this would also encourage realism and openness and underpin our expectation that audit committees would more robustly drive audit quality and take greater charge of finding and overseeing the auditor. We reinforced their work by sharing our audit inspection reports with audit committee chairmen and by offering to brief them on the findings.

These steps had value in their own right, but we also felt they were a necessary precursor to the introduction of audit retendering every ten years. We felt that retendering was necessary to help deliver our goal of restoring confidence in the value of audit by revitalising the market, promoting innovation through competition, and enhancing auditor independence.

However, we also saw the risk of price competition undermining the firms' capacity to do quality work. We felt that the best mitigant of this risk was engaged audit committees committed to quality.

The final element of the strategy on audit was the introduction of extended auditor reporting, through which the auditor would give an overview of how they had conducted the audit; including the audit risks they identified and how they had addressed them; and the level of materiality they applied. Our goal was to remove the mystery around audit for investors and, combined with the fuller audit committee reports, give them a better basis for engaging with directors on financial matters and risk. Audit firms responded innovatively and investors welcomed this, which we hope will in turn further reinforce the commitment of audit committees to quality.

We also made progress in other areas: consulting on how the UK Corporate Governance Code covers remuneration, promoting the Stewardship Code, promoting clearer, more insightful company reporting through the Strategic Report, continuing our reforms to accounting and reporting requirements for smaller entities by overhauling UK GAAP, establishing the Joint Forum on Actuarial Regulation and focusing on the overall effectiveness of our conduct activities. Across all these activities, we contributed to EU and international developments.

2014/15

We continued to implement key elements of the strategy during the period covered by this Report and have begun to test its effectiveness.

We amended the UK Corporate Governance Code to promote a better focus on risk, internal control and the assessment and reporting of the longer-term viability of the companies. The changes were intended to address directly the concern of many investors that banks and other companies had paid insufficient attention to risk in the run-up to the financial crisis. They build on the changes already introduced in relation to audit committees and auditors and promote judgement by putting the onus on directors to choose the period over which they report on longer-term viability.

Our Financial Reporting Lab looked at the quality of audit committee reporting in 2013. In March 2015 we issued a report on the take-up of requirements on extended auditor reporting. The report suggested that the new requirements were beginning to make key aspects of the audit process more transparent for investors. Some auditors are reporting that audit committees are taking into account audit firm partners' audit inspection results, which suggests they are paying close attention to quality. We hope that, over time, this will lead to improved justifiable confidence in audit. We are now looking at the impact of audit retendering.

We reviewed the implementation and operation of the Audit Firm Governance Code. Our report **(https://www.frc.org.uk/Our-Work/Publications/FRC-Board/Consultation-Audit-Firm-Governance-Code-File.pdf)**, published in May 2015, considered the progress made in terms of governance of UK audit firms following the Code's implementation and sought feedback on strengthening the Code to put more focus on the public interest in, and governance of, audit work within the firms' total business. The report concluded among other things that the firms have taken a major step forward in bringing in Independent Non-Executives. As firms grow their consultancy business, it is important that the principle of external challenge remains focussed on the audit practice as well as across the firm as a whole. It also proposed that the principle of external challenge should be adopted in the international network as well as at national level.


We will consider the overall effectiveness of our work to review the quality of corporate reporting and auditing; and continue to enhance the pace and effectiveness of our independent disciplinary arrangements.

The independent survey we commissioned of perceptions of the quality of actuarial work (**https://www.frc.org.uk/News-and-Events/FRC-Press/Press/2015/April/Actuarial-profession-must-face-up-to-new-challenge.aspx**), and our own testing of opinion, have shown a high level of confidence by users in actuarial work. We have, however, reviewed and are consulting on our technical standards.

Further details of actions taken during 2014/15 to address our five strategic priorities, our international activities and our assessment of progress against those priorities, can be found on pages 17 to 24.

2015/16

In 2015/16 we intend to complete the delivery of our three-year strategy by building on or embedding actions taken in the previous two years. We will continue the programme of work to promote audit that is of a consistently high standard and meets investor needs. We will take forward our work on corporate governance and investor stewardship. We will promote clear and concise corporate reporting, including through our project to help smaller listed and AIM companies with the quality of their reporting. We will continue to focus on the quality and value of audit. And we will finalise the project to identify and respond to public interest actuarial risks and update our technical actuarial standards.

Major new projects will focus on company culture and succession planning and how to promote good practice in both areas.

A significant element of our work during the year will be to support BIS in implementing the amended EU Audit Regulation and Directive. During 2015/16 we will take on a number of additional responsibilities as a result of the Competition and Markets Authority recommendations on the audit market. Both these developments will require the expansion of some of our teams and will widen the range of the work we do to monitor audit quality.

We will consider the overall effectiveness of our work to review the quality of corporate reporting and auditing; and continue to enhance the pace and effectiveness of our independent disciplinary arrangements.

The details of our plan and budget for 2015/16 are at **https://www.frc.org.uk/FRCplanandbudget.**

1.2 – 2013/16 Strategy – Progress in key areas

This section describes our work in 2014/15 for each of our strategic priorities.

Corporate governance and investor stewardship

Corporate governance

The FRC sets the **UK Corporate Governance Code.** The Code is based on the underlying principles of good governance including: the exercise of judgement, accountability, transparency, probity and a focus on the sustainable success of an entity over the long-term. It includes a clear principle that boards should provide annual reports and accounts that present a fair, balanced and understandable assessment of the company's position and prospects.

During 2014/15, we have:

- Revised the Code. The aim was to enhance significantly the quality of information investors receive about the long-term health and strategy of companies and to raise the bar for risk management. We also included amendments to the remuneration sections to introduce a longer-term focus.
- Commenced an assessment of the quality of board succession planning. This is frequently identified in board reviews as an area where improvements can be made, and consideration given as to how to develop best practice.
- Initiated a project on how best to assess culture and practices and how they embed good corporate behaviour.
- Reviewed the impact of the revised 2012 UK Corporate Governance Code including changes in relation to audit committee reports, and developed practical guidance for audit committees on assessing audit effectiveness, published in May 2015.

Effectiveness indicators

The FRC publishes an annual report on the impact and implementation of the UK Corporate Governance and Stewardship Codes which draw on a wide range of quantitative and qualitative evidence. The latest report, issued in January 2015, suggests that:

- 94% of FTSE 350 companies state that they have complied with all, or all but one or two, of the Code's provisions (2013: 85%).
- 99% (2013: 97%) of smaller listed companies have a separate chairman and CEO; while 93% (2013: 96%) and 99% (2013: 99%) adopt the audit and nomination committee composition requirements respectively.
- Board diversity has been improving since 2012; the headline figure for female directorships in FTSE 100 companies is up from 18.9% to 22.8% when combining executive and non-executive directorships.
- Approximately two-thirds of FTSE 350 audit committees provide detailed discussion of significant accounting issues.
- 27 FTSE 350 companies disclosed in their 2013/14 annual report that they had carried out an audit tender, with 19 changing auditors as a result.

Investor stewardship

The FRC also sets the **UK Stewardship Code.** This Code sets out the principles of effective stewardship by institutional investors, which help build confidence in the system and give force to the 'comply or explain' system as well as increasing accountability to clients and beneficiaries.

We have sought an improvement in the quality and quantity of engagement and for asset managers to be more accountable to their clients. In turn, that should generate the demand for effective stewardship and for proxy advisers to be more accountable for the quality of their advice.

To achieve change in behaviour and transparency, we have:

- Worked with the markets and investors in the UK and internationally to try to ensure that investors in the capital markets have the information they need to invest for the long-term.
- Led the stewardship debate in the UK and internationally, including influencing the development of the new Shareholder Rights Directive.
- Pressed fund managers and asset owners to provide better accounts of their engagement with companies and how they are meeting the expectations of clients and beneficiaries.

Effectiveness indicators

Surveys carried out by the Investment Association (June 2015) and National Association of Pension Funds (November 2014) show that among the respondents:

- 74% (2014: 83%) of asset managers have mandates that refer explicitly to stewardship, while just over 50% of pension funds have awarded such mandates, with a further 30% considering doing so in the future.
- 90% (2014: 92%) of asset managers report to clients or beneficiaries with approximately three quarters doing so regularly (most commonly on a quarterly basis). 68% (2013: 46%) of pension funds were very or quite satisfied with the standards of these reports.
- 18% (2014: 18%) of asset managers had obtained an independent opinion on both their voting and engagement processes in the previous 12 months

Corporate reporting

An important theme of our work in this area has been to promote clear and concise reporting. This has included publishing guidance on the Strategic Report, the messages we can give preparers based on our reviews of corporate reports in addition to compliance issues and the work of the Financial Reporting Lab. Our aim is to encourage all those involved in the financial reporting process to focus on communication and the clear presentation of information and materiality.

During 2014/15, we have:

- Undertaken our annual programme of review of corporate reports, with a particular focus on companies of economic significance where a material error could have implications not just for the individual company but for confidence in the market as a whole. We will separately report on these activities and share our findings on areas where there is opportunity for improvement and where we had particular focus.
- Continued to challenge companies whose strategic reports were either inadequate or incomplete or where there appeared to be inconsistencies with the balance of their reporting. We will remind boards of quoted companies that we expect their significant accounting policies to reflect key aspects of their business model, which they are now required to describe.
- Published an analysis of steps companies have taken to make their annual reports more clear and concise, and the first of a series of Financial Reporting Lab case studies supporting the Clear & Concise initiative.
- Initiated a project with the aim of looking at whether the quality of reporting matters to investors in smaller quoted companies and how to support companies to improve the quality of their reporting. In June 2015, the FRC published a report on the first phase of the project which set out our assessment of the root causes of poor quality reporting and the actions that the FRC proposes to take to address its findings.
- Continued to influence the IASB's agenda, particularly its work on the Conceptual Framework, focusing on promoting the exercise of caution and stewardship; its work on disclosures (including the proposal for a debt reconciliation following the Financial Reporting Lab's work on debt and cash flows); and also working on the development of a new leasing standard and on the post implementation review of IFRS 3 on business combinations. We have initiated research to influence developments in cash flow reporting to help influence the IASB's work in this area.

- Following the restructuring of the European Financial Reporting Advisory Group (EFRAG), we are now represented on its Board and Technical Expert Group, supporting its work to reinforce the EU's contribution to the development of IFRS. We are pleased that Roger Marshall was appointed as acting President of EFRAG.
- Published through the Financial Reporting Lab, a report on accounting policy disclosure and integration of related financial information, and developed a project on dividend policy and capacity in groups. In May 2015, we also published the first Lab report on digital reporting, looking at how companies and investors are using digital means of reporting at present. In 2015/16 we will build on this to identify how to optimise the opportunities digital corporate reporting offers to companies and investors.
- Continued to support the implementation of new UK GAAP to improve standards of reporting by non-listed entities. We have responded quickly to resolve implementation issues identified by reporting entities and their advisors by issuing amendments to the new standards before they are first applicable. We have overseen the completion and publication of all Statements of Recommended Practice (SORPs) and developed the digital tagging taxonomies for the new UK GAAP to enable companies to report in eXtensible Business Reporting Language (XBRL) format. We have consulted on the implementation of the EU Accounting Directive into our standard framework and will issue the various changes to the finalised standard in 2015/16.

Effectiveness indicators

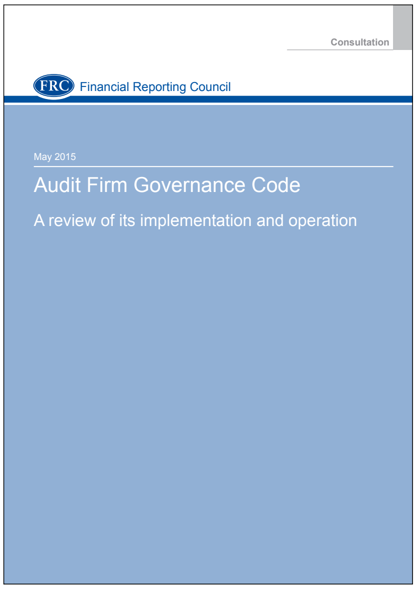
On the evidence of our Corporate Reporting Review (CRR) Team's reviews this year we have seen a good level of corporate reporting by large public companies while smaller listed and AIM quoted companies face a different set of challenges.

We had proposed to review the adoption of FRS 101 – Reduced Disclosure Framework to help assess its fitness for purpose. However, given the small number of early adopters there is currently insufficient data for an effective review. Whilst we understand companies are considering whether to adopt FRS 101, many will not adopt the new standards before the effective date of 2015. Once data is available, we will initiate a project to assess adoption and fitness for purpose of FRS 101.

The Financial Reporting Lab continues to build its base of project participants, which have now included over 130 individuals from 65 companies and 160 individuals from 60 investment community organisations. We continue to, in particular, target increased participation from smaller listed companies, with 17% of participant companies coming from FTSE 250, and 12% below that.

Audit

The FRC is taking forward a series of reforms designed to enhance the quality of audit and its usefulness for companies and investors. For this to succeed we need to see a number of different interests and incentives work together. The FRC has a role in encouraging boards and audit committees to take a close interest in audit; and in setting high quality auditing standards, which we monitor and enforce. It is essential that within audit firms there is a commitment to delivering consistent and rigorous audit quality.



During 2014/15, we have:

- Undertaken and reported on our annual programme of work to monitor the quality of individual audit engagements. Based on the 126 engagements we inspected, our assessment is that the quality of individual audits continued to show an improvement; and the proportion of audits assessed as requiring improvements or significant improvements reduced. To promote further improvements we require firms to develop action plans to address the weaknesses identified in individual audit engagements and firm-wide procedures, and to undertake a detailed root-cause analysis of the factors contributing to the issues arising from our inspections.
- Made use of our new Auditor Regulatory Sanctions Procedure to impose sanctions where poor quality audit work is identified. Of the matters arising from our 2014/15 inspections which were considered under this procedure, two were concluded with sanctions determined and another was reported to the relevant accountancy professional body's disciplinary procedures.
- Undertaken a thematic inspection to review the progress made by the major firms in improving the audit of loan loss provisions and related IT controls in banks and building societies.
- Ensured that the recent UK audit reforms are implemented effectively, including by: reviewing extended audit committee and auditor reporting for sound and meaningful implementation; and articulating what audit quality is and how it might be assessed, in particular by audit committees.
- In particular, published a survey of the use of extended audit reports to determine how auditors have provided greater transparency and value for investors in their first year of application (**https://frc.org.uk/Extended-auditors-reports.pdf**). We concluded that the take-up of the new requirements has been positive. The requirements for auditors to describe assessed risks of material misstatement, materiality and the scope of audit were beginning to make more transparent a process that had previously been seen as a 'black box' by investors.
- Published a report on the implementation and operation of the Audit Firm Governance Code, which, as noted on page 15, sought feedback on strengthening the Code to put more focus on the public interest in, and governance of, audit work within the firms' overall business.
- Undertaken and reported on our independent oversight of the regulation by the UK accountancy professional bodies of those of their members practising as statutory auditors. We describe the outcome of this work in the Appendix to this Report and identify specific areas of focus based on the findings of our 2014/15 reviews. The conclusions from our work in this area are largely positive: much of the regulatory work we see continues to be of a high standard and we receive good cooperation from the bodies. Even so, we continue to have some concerns about the effectiveness in improving audit quality from the measures that the bodies may impose on firms following an audit monitoring visit that is graded unsatisfactory.
- We undertook five third-country auditor inspections, covering four audits in 2014/15. The results of these inspections are now incorporated within our Audit Quality Review's Team (AQR) Annual Report.
- Continued to contribute significantly to the work of the International Auditing and Assurance Standards Board (IAASB) on the new suite of audit reporting standards, the International Forum of Independent Audit Regulators (IFIAR) and the European Audit Inspection Group (EAIG).

- Made good progress in implementing the audit quality review aspects of the Competition and Markets Authority's (CMA) recommendations. The recommendations, in particular that all FTSE 350 audits should be reviewed on average every five years, have lead to a significant expansion of our audit quality review inspection activities.
- Worked closely with BIS in planning for the implementation of the requirements of the new EU Audit Regulation and Directive, agreed in 2014. These requirements are significant for the remit of our audit quality reviews and our oversight of audit regulation and ethical standards. The number of firms our AQR team will be required to inspect will increase significantly.
- Prepared for the implementation of local public sector audit inspection regimes in line with the new regime introduced under the Local Audit and Accountability Act 2014.
- Worked closely with the FCA to develop, for consultation, a standard to support assurance engagements for 'client assets audits'. This will support enhanced audit quality and support appropriate oversight and disciplinary arrangements.

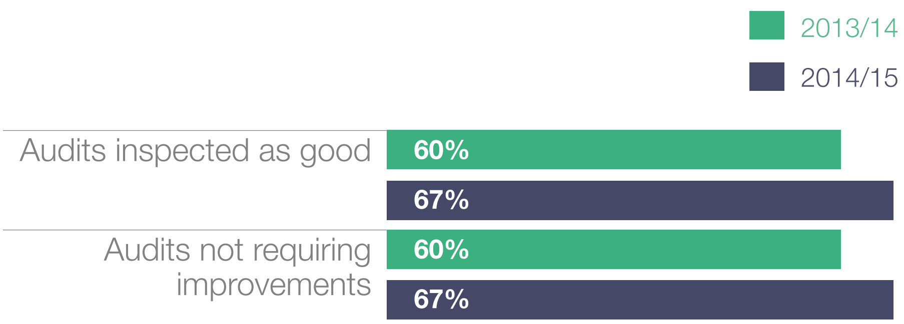
These changes to our role have required us to recruit additional staff with the necessary skills and have required changes to the structure and governance of our audit inspection and oversight activities.

Effectiveness indicators

The FRC inspected 126 individual audit engagements in 2014/15 (compared with 101 engagements in 2013/14).

The findings from the FRC's annual audit quality inspection activities for 2014/15 published in May 2015 found that:

- 67% of audits inspected were assessed as either good or requiring only limited improvements compared with 60% in 2013/14.
- 33% of audits inspected were assessed as requiring improvements or significant improvements compared with 40% in 2013/14.
- A benchmark YouGov survey, 'Improving Confidence in the Value of Audit', commissioned by the FRC in 2014 (**https://www.frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Research-Report-Improving-Confidence-in-the-Value.aspx**) indicated that stakeholder perceptions of audit quality and value seem to vary according to their involvement with, and experience of audit. A further study will be undertaken in 2016 to identify any changes in stakeholder perceptions.



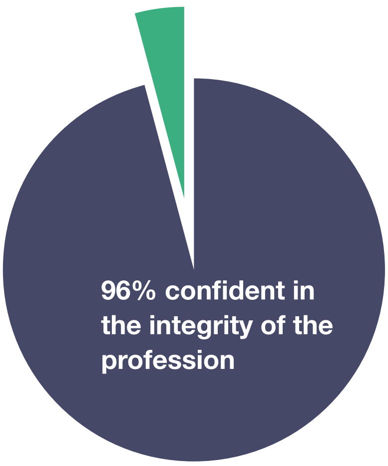
Actuarial oversight and standards

Actuarial work is central to many financial decisions in insurance and pensions and is an important element in other areas requiring the evaluation of risk and financial returns. High-quality actuarial work promotes well-informed decision-making and mitigates risks to users and the public.

The Joint Forum on Actuarial Regulation was established in 2013 by the FRC, the Institute and Faculty of Actuaries (IFoA), the FCA, the PRA and the Pensions Regulator to coordinate within the context of its member bodies' objectives, the identification of, and response to, public interest risks to which actuarial work is relevant.

During 2014/15, we have:

- Issued jointly with the IFoA a statement on actuarial standards. This confirmed the FRC and IFoA's respective responsibilities for setting actuarial standards but introduced scope for greater flexibility in the way these responsibilities are discharged. The FRC's Memorandum of Understanding with the IFoA was updated to reflect this greater flexibility and to give the FRC a reserve ability to issue ethical standards for actuaries when it considers such action necessary and in the light of consultation with the IFoA.
- Developed and consulted on, with the assistance of the Joint Forum, an assessment of the risks to the public interest associated with actuarial work.
- Engaged with the Department for Work and Pensions (DWP) and other regulators on the implications for Actuarial Standards of the Pensions Reforms announced in the March 2014 budget statement, including the role of AS TM1 in pensions illustrations and the wider approach to defined contribution pensions.
- Worked with the Prudential Regulation Authority (PRA) and IFoA to influence the development of an effective competence and standards regime for the actuarial function and other actuarial roles in the run up to the implementation of Solvency II.



Effectiveness indicators

The FRC's 2015 survey of perceptions of actuarial quality (**https://www.frc.org.uk/News-and-Events/FRC-Press/Press/2015/April/Actuarial-profession-must-face-up-to-new-challenge.aspx**) suggested that the actuarial profession continues to be held in high regard by stakeholders. Of those surveyed 96% (93%: 2012) were fairly or very confident in the integrity of the profession.

Our monitoring, investigative and disciplinary procedures

We have continued to develop our Supervisory Inquiries function to enable the FRC to respond to matters of public concern and provide the Conduct Committee with a good evidence base to make informed decisions before launching disciplinary investigations. Companies and audit firms have continued to co-operate with our requests for information to be provided to us on a voluntary basis.

We commissioned an independent review of both our Audit Quality and Corporate Reporting review functions to assess their efficiency and effectiveness. The review is being carried out by McKinsey & Company. McKinsey's work has confirmed that our initiative to improve the efficiency and effectiveness of our CRR and AQR monitoring activity starts from a position of strength. Stakeholders see the FRC as a force for good, having driven substantial improvements in the quality of reporting and auditing, and as a benchmark for peers internationally.

The McKinsey preliminary recommendations focus on: enhanced investor involvement; greater transparency; establishing a 'continuous improvement-focused' regulatory stance; investing in AQR and CRR talent; improving strategic and stakeholder communications and engagement; and standardised and simplified processes.

Professional discipline

The FRC's independent disciplinary arrangements enable us to deal with cases of potential misconduct involving Members and Member Firms of the participating accountancy and actuarial bodies. The FRC addresses cases which raise or appear to raise important issues affecting the public interest in the UK.

Contributing to the overall reforms to the FRC's powers and structure introduced in 2012, the FRC has made a number of changes designed to enhance the efficiency and effectiveness of the disciplinary arrangements. These have included introducing revised Accountancy and Actuarial Disciplinary Schemes and, in June 2014, publishing Guidance on Sanctions for tribunals convened under the Accountancy Scheme. In December 2014, we published updated Accountancy and Actuarial Schemes intended to make the Schemes more efficient and effective by providing for joint Tribunals in cases involving both accountants and actuaries. In May 2015, we published guidance designed to enhance the timetabling of disciplinary and appeals Tribunals.

During 2014/15 the Professional Discipline team closed or concluded nine disciplinary cases. Details of the FRC's work on individual cases are available on our website at **(https://frc.org.uk/Our-Work/Conduct/Professional-discipline.aspx)**.

We highlighted a number of themes arising from the outcome of individual cases and our work generally. These include:

- High standards of professional conduct are expected from accountants who take up executive positions in business.
- There is a clear message to all major accountants and accountancy firms carrying out advisory work that not only do they have a responsibility to carry out their professional work diligently and in accordance with the applicable technical standards but that they must consider the different and opposing commercial interests of all those involved. Accountants must not allow undue influence of others to override their professional judgements and they must have a clear understanding of who their client actually is.
- It is essential that investors in smaller listed and AIM companies are able to rely upon the audited accounts of such companies in informing their investment decisions. In one case, for example, breaches of auditing standards of fundamental importance, in particular in relation to the audit of the accounting for revenue and costs on long-term contracts, had a real impact on the reliability of the financial statements at a critical stage of the company's history, and on investors' decisions.
- The central importance of the Ethical Standards for Auditors to the audit process. They are at the heart of trust in the audit process on which public confidence in capital markets and the conduct of public entities depends.

In relation to the case concerning MG Rover, the FRC welcomed the Appeal Tribunal's decision that there were some significant issues of misconduct in this case concerning the need for accountants to act with objectivity. Firms should identify who the client is at as early a stage as possible so that any conflicts of interests can be addressed. In the event of a change in clients it is also essential to inform a previous client of the change and of the need to obtain independent advice. Threats of self-interest in relation to fees must also be safeguarded. These are important measures in safeguarding and maintaining confidence in the accountancy profession and in upholding the standards expected of members.

The FRC will continue its work to pursue individual cases effectively and to ensure that the Schemes support confidence in the Members and Member firms of the accountancy profession and members of the actuarial profession.

Professional oversight – accountancy profession

As part of its non-statutory oversight role the FRC considers complaints about the way in which the six 'chartered' accountancy bodies have handled individual complaints about their members. During the year we conducted a small number of reviews of the handling of particular complaints by professional bodies. These reviews did not indicate any systemic issues with the complaints process at any of the bodies about which we received complaints.

Our people

As a small organisation with a wide-ranging mission, we recognise that our people are our most important asset and without their professionalism and dedication we would not be able to achieve our mission.

We need people at all levels of the organisation who have the necessary technical skills as well as the ability to exercise judgement, influence others, communicate with our stakeholders, and manage projects and people. We also need all our people at all levels to be committed to the culture and behaviours that we expect within the organisation. Our Citizenship Values – including the importance of showing respect to colleagues within the FRC and, equally important, to those we regulate – are embedded across the organisation.

Our organisation has a relatively flat management structure with only three levels between CEO and business support functions. This has many advantages in making us a great place to work. Promotions represent big jumps in responsibility and we have therefore often recruited from outside the FRC to fill vacancies. The need for high levels of expertise has also reduced the scope for lateral moves. This risks demotivation and increases cost. We have therefore increased our expenditure and time spent on training and development across the organisation, with particular focus on preparing people to take leadership positions. The Future Leaders Scheme is a major element of this programme. Our efforts are guided by a new approach to performance management that involves departmental plans for all and systematic succession planning for senior positions.

During 2014/15 we have recruited expert staff across the organisation with particular focus in our AQR and Professional Discipline teams. We currently employ 151 staff, of whom, 32 are in our Codes & Standards team, 83 in our Conduct team and 36 in our Corporate team. Further recruitment will be necessary as we take on additional responsibilities as a result of the Competition and Markets Authority (CMA) recommendations and the implementation of the Audit Regulation and Directive.

We aim to offer a competitive benefits package. This includes flexible working arrangements, which candidates have highlighted as a significant factor that influences their decision to join us (and of which 24% of our current staff take advantage).

We have continued to provide opportunities for work experience candidates and interns as part of our Early Talent programme and we have successfully gained accreditation from ICAEW as a training provider. Our first apprentice is working in our Business Support team and we have extended our mentoring programme.

Employee engagement

Our annual Employee Survey provides us with an insight on where to focus our people activities. In March 2015, 97% of our people stated that that they feel proud to work for the FRC, 97% believe that we are a good organisation to work for, and 91% feel that we value the job that they carry out. The survey also identified a need for us to pay further attention to learning and development.

Diversity and Inclusion

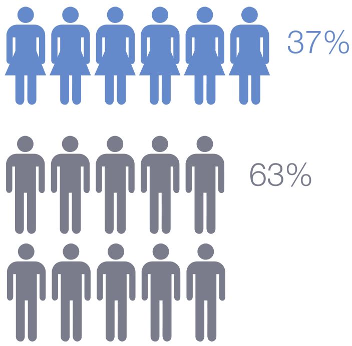
We recognise the importance of diversity and inclusion both as an employer and as a regulator. By consciously seeking to understand and reflect the perspectives of colleagues from diverse backgrounds we believe that the FRC can operate more effectively. We value and demonstrate equal opportunity in recruitment, career development, promotion, training and reward for all employees.

During 2014/15, we signed up to 'Think, Act, Report', a voluntary Government initiative aimed at driving greater transparency on gender employment issues and we are currently reviewing our equality, diversity and inclusion programme activities to ensure that they are in line with best practice and demonstrably effective.

Gender diversity within the FRC(*)

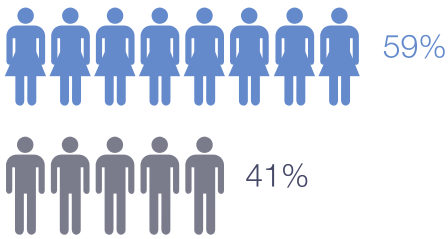
Senior managers

6 Female, 10 Male



All other staff

80 Female, 55 Male



(*) Figures for senior managers include executive directors. Data on the composition of the Board and its committees can be found on pages 35-44

Financial review

Our revenue and expenditure are managed under four main headings:

- Core operating activities
- Audit quality review costs
- Accountancy and actuarial disciplinary case costs
- XBRL taxonomy development

The cost of our **core operating activities**, including our responsibilities for corporate governance, corporate reporting and audit are funded through voluntary levies on publicly traded, large private and public sector organisations plus contributions from the accountancy profession and from Government. Our actuarial activities are funded by levies on pension funds and insurance companies plus a contribution from the actuarial profession. Ad-hoc income streams, such as from publications, registration fees and inspection fees are accounted for as part of total revenue.

Audit quality review costs are recovered from the accountancy professional bodies.

Disciplinary case costs are recovered from the accountancy professional bodies for accountancy cases and from the actuarial funding groups for actuarial cases.

XBRL taxonomy development direct costs are funded by Companies House with people being provided by the FRC and HMRC.

The expenditure necessary to carry out the FRC's activities and meet key objectives is published each year in our Plan & Budget. Stakeholders are invited to comment on the priorities identified in the plan and the associated levels of funding. The grant from Government and the amounts to be collected from the professional bodies, apart from case costs, are agreed at the start of the year as part of the consultation process.

During the year revenue increased by £2.8m and expenditure by £3.1m. Our general reserves reduced by £198k, a larger deficit than budgeted of £65k.

Expenditure

Total expenditure is set out in detail in note 2 to the financial statements. Expenditure across the main headings is analysed below.

Total expenditure by activity	Actual 2014/15 £m	Actual 2013/14 £m	Budget 2014/15 £m
Core operating costs	20.1	18.0	19.9
Audit quality review costs	4.3	3.3	4.8
Accountancy – disciplinary case costs	4.2	3.1	7.2
Actuarial disciplinary case costs	0.2	0.2	0.2
XBRL taxonomy development	0.3	1.3	0.3
Total	**29.1**	**26.0**	**32.4**

*Note: * The budget included in the Plan & Budget 2014/15 was £32.1m. This did not include £0.3m of publishing costs which was netted from projected publication receipts in forecast revenues. The core operating cost budget above includes this expenditure.*

Comparison to prior year

The increase in core costs was mainly in respect of staff costs (£1.6m) and travel and conferences (£0.2m) including holding the FRC's first annual conference. During the year we moved to 125 London Wall from Aldwych House to avoid a substantial increase in rent. We incurred £0.6m of additional facility costs (rent, rates and service charge) during the fit-out.

Legal and professional fees include the costs (£0.3m) of an ongoing review of the effectiveness of our CRR and AQR activities carried out by McKinsey.

AQR expenditure grew by 30% to £4.3m, reflecting the increased team size and number of reviews carried out in order to implement the CMA recommendations following their review of the audit market (see page 21).

The gross expenditure on disciplinary case costs (accountancy and actuarial taken together) was flat at £5.6m in both years. The amounts recovered for cost awards were £2.25m in 2013/14 and £1.15m in 2014/15.

XBRL taxonomy development costs are lower as the majority of the work to build the taxonomies was completed in 2013/14. The expenditure in 2014/15 related to hosting and maintenance of the IT platform.

Comparison to budget

Total expenditure was £3.3m (10%) lower than budget, the notable variance being in accountancy disciplinary case costs which accounted for £3.0m of the shortfall. The number and complexity of the cases progressed during the year was as expected; although the number reaching tribunal was lower. We have sought to reduce costs by carrying out more work in-house. In addition there were successful outcomes in a number of cases leading to awards of costs being made against other parties. These totalled £1.15m compared to a nil budget.

Revenue

Revenue is analysed across our main headings as follows:

Revenue

£m	Actual 2014/15	Actual 2013/14	Budget 2014/15
For Core Operating Costs			
Preparers levy	11.3	9.5	11.1
Insurance & pension levies	2.2	2.0	2.1
Accountancy professional bodies	5.0	4.9	5.0
Actuarial profession	0.2	0.2	0.2
Government	0.5	0.5	0.5
Publications	0.5	0.7	0.8
Subscription and sundry income	0.2	0.3	0.2
Sub Total	**19.9**	**18.1**	**19.9**
For Accountancy Disciplinary Case Costs			
Accountancy professional bodies	5.3	5.3	7.2
less cost awards recovered	(1.1)	(2.2)	0.0
Sub Total	**4.2**	**3.1**	**7.2**
For Actuarial Disciplinary Case Costs	0.2	0.2	0.2
For Audit Quality Review	4.3	3.3	4.8
For XBRL Development	0.3	1.3	0.3
Total	**28.8**	**26.1**	**32.4**

*Note: * The budget included in the Plan & Budget 2014/15 was £32.1m and publications revenue was shown net of related expenditure of £0.3m. The core operating cost budget above includes the total publications revenue. Revenue figures have been rounded to the nearest £0.1m.*

Comparison to prior year and budget

The preparers' levy provided most of the additional amount of £1.8m compared to last year. Levy rates increased on average by 4% and there was a 7.5% increase in the market capitalisation of listed entities (a factor in determining the amounts individual companies pay). We benefited from better collection rates from listed and public sector entities, but this was offset by lower collection rates from private companies. The contribution received from the accountancy professional bodies increased by 2%.

Publications income was lower than budget following a change in our publishing agent at the beginning of the year, which had not been anticipated when the budget was set. The new arrangement involved investment in a publication marketing infrastructure that will initially cost more but should generate higher demand and therefore higher future revenues.

The annual funding we seek each year for the investigation and prosecution of accountancy cases is set to match the net anticipated expenditure and accordingly has reduced in line with the expenditure incurred.

Balance Sheet

The balance sheet at 31st March 2015 is included in the financial statements.

The significant movements on the balance sheet reflect our move to London Wall in June 2014. Tangible assets have increased by £1.6m representing the capital costs incurred to fit-out the new office and to acquire additional furniture and IT equipment. Cash and investments have reduced by £1.4m net due to the capital spend.

Debtors reduced by £0.7m as an amount due from the new landlord that was outstanding at last year end, was collected during the year.

Creditors falling due within one year reduced by £0.7m reflecting the settlement of previous expenditure on the fit-out.

Principal risks

Reflecting our current assessment of the state of corporate governance and reporting in the UK, we identified the following principal risks to the pursuit of the FRC's mission which were monitored by the Board during 2014/15. These include the potential impact of events or developments in the markets and risks that, if they materialised, might significantly compromise the FRC's ability to play its proper role within the wider regulatory framework.

Risk	How the FRC addresses this
Corporate failures or scandals undermine confidence in the UK governance and reporting model	We monitor the quality of reporting and audit; report findings; and highlight potential areas of concern. Where appropriate we make necessary changes to FRC codes and standards. We undertake Supervisory Inquiries to respond to matters of public interest and determine the most appropriate course of action to take. Where appropriate we will take disciplinary action against members of the professions and professional firms. As part of the FRC's overall regulatory framework the updated UK Corporate Governance Code issued in 2014 is intended to enhance significantly the quality of information investors receive about the long-term strategy and viability of companies and to raise the bar for risk management.
The actions of investors and the professions do not support the UK governance and reporting model	We set out our expectations of investors and the professions – for example through the Stewardship Code, the Audit Firm Governance Code and auditing and actuarial standards – and monitor directly or indirectly whether they are being met.
There is a critical loss of capacity in the UK audit market	We co-ordinate with other public bodies and with the major audit firms to maintain contingency plans to minimise the impact on the quality of reporting and audit in the UK in the event of a major audit failure or a major firm exiting the UK market.

Risk

The FRC takes actions that are ineffective or misguided, with damaging consequences for UK markets and the FRC's reputation

How the FRC addresses this

We gather evidence to inform our policies through our monitoring, inspection and disciplinary activities and consult widely. For example, we consult on all changes to codes and standards; base our monitoring activities on an analysis of the entities and sectors where problems are most likely to arise; and through the work of our Supervisory Inquiries team, develop a robust evidence base before initiating investigations.

We keep the effectiveness of the FRC's powers and functions under review following the reforms to its powers and structure introduced jointly with the Government in 2012.

Risk

The complexity of the regulatory framework in the UK and internationally frustrates the effective delivery of regulatory goals

How the FRC addresses this

We maintain a close dialogue with the Government and other regulators to ensure that the FRC's work supports and is supported by others' regulatory activities. We have a formal Memorandum of Understanding with the PRA and FCA. We maintain constructive working relationships with the accountancy and actuarial professional bodies.

We are working to help secure a satisfactory outcome to the implementation of the Audit Regulation and Directive, which provides a number of Member State options and therefore involves a degree of uncertainty over the final details of the new arrangements.

We ensure that sufficient priority and resource is dedicated to influencing EU and international bodies, including the EU institutions and the work of the international standard setters (notably the IASB, IAASB and the IAA). In doing so, we work closely with other regulators and Member States.

Risk	How the FRC addresses this
The FRC has insufficient financial resources to fulfil its regulatory responsibilities	Our current funding arrangements, established in 2008, have enabled the FRC to secure the necessary resources for our regulatory activities. We are planning to review the basis on which we are funded in the context of the next three year strategy, for 2016/19, to ensure that we continue to have a stable and secure basis on which to operate. We consult annually on the FRC's budget to ensure that it is adequate and on our levies and to ensure that they continue to operate fairly and efficiently. There are reserve powers in company law to provide statutory levies; to date these have not been needed. The disciplinary schemes provide for costs orders to be made against the FRC where a Tribunal finds that no reasonable person would have pursued a formal complaint under the relevant scheme. Checks and balances are in place to ensure that formal complaints are pursued appropriately: there is a test for laying a formal complaint and the Conduct Committee has issued guidance in relation to the consideration of those tests; the Case Management Committee monitors the merits of the approach taken by the Executive Counsel and advises the Executive Counsel of any factors to be considered when deciding whether to proceed with a formal complaint; and external independent advice is sought on the various aspects of any particular case.
Shortcomings in the quality of leadership and staff undermine the FRC's effectiveness	We undertake a thorough annual review of the Board and its Committees and address any issues that are identified as requiring attention, including ensuring the necessary range of knowledge and experience for Board and Committee members. We have introduced new performance management systems for staff, and are currently implementing a leadership and development programme to enhance the skills and competence of our people. We are also focusing on succession planning.
The FRC's information security is inadequate to protect confidential information	We maintain policies and standards to secure IT and other information systems. During 2014/15 we updated our policies and processes for safeguarding price sensitive information.

Viability statement

This statement covers the period to March 2019, which will mark the end of the FRC's next three-year planning period.

For the reasons stated below, the directors have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of the assessment. We have therefore applied the going concern basis of accounting in preparing the annual financial statements.

In making this assessment, the Directors acknowledge the authority of Government and Parliament in determining the FRC's future. While recognising that regulatory arrangements inevitably evolve over time in response to changing circumstances, we believe that it is reasonable to operate on the basis that the statutory and other responsibilities exercised by the FRC will continue to be required, and that the FRC will continue to be the organisation asked to deliver them.

The role of the FRC was reviewed and confirmed by Government in 2012 and our powers were then extended. Since then, we have increased our monitoring of individual audits in response to the 2013 report by the Competition and Markets Authority on the provision of statutory audit services to FTSE 350 companies. It is possible that the Government may extend our responsibilities further by designating the FRC a competent authority for the purposes of audit regulation under the new Audit Regulation and Directive.

The Directors anticipate that the FRC would have to increase its funding in order to carry out any additional responsibilities, and we are currently reviewing the basis on which we are funded.

We anticipate that the direct grant funding we receive from BIS will cease at some point in the current Parliament.

The majority of the FRC's income is raised from companies and the accountancy profession. A proportion of this is currently secured through voluntary arrangements, which, by their nature, carry a degree of risk. If we considered there was a serious prospect that we could not raise sufficient funds to carry out our core functions, we could ask the Government to exercise the reserve powers in company law that would enable some or all of our funding to be placed on a statutory basis.

To date we have been able to raise the funds we require on the basis of non-statutory arrangements, to a level that enables us to maintain reserves to meet unexpected costs arising from our regulatory role. Our reserves provide a buffer against volatility and we look to increase them over time.

The FRC's costs of investigating and pursuing disciplinary cases are recovered from the accountancy professional bodies and actuarial funding groups. The disciplinary schemes provide for costs orders to be made against the FRC where a Tribunal finds that no reasonable person would have pursued a formal complaint under the relevant scheme. Were such an order to be made, the FRC could not recover the relevant sums from the professional bodies or funding groups. We have put checks and balances in place to ensure that formal complaints are pursued appropriately, including taking independent advice.

Approval of Strategic report

This report was approved by the Board of Directors on 13th July 2015 and signed on its behalf by

Stephen Haddrill

Chief Executive Officer

13 July 2015

2 Governance

Introduction

The governance structure of the FRC has been designed to facilitate effective oversight and management and deliver the long-term success of the organisation.

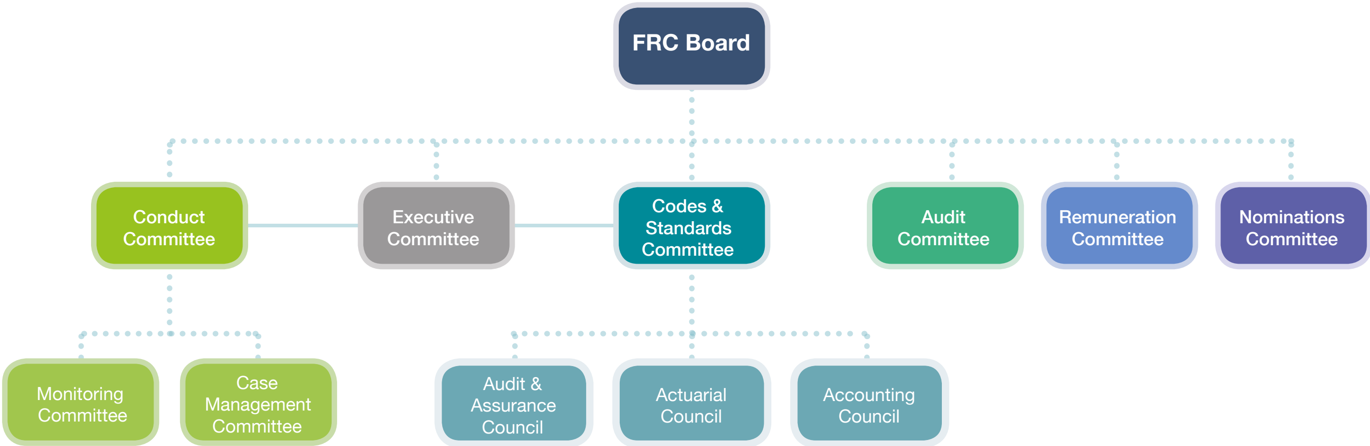
The Board is committed to high standards of governance and believes that the UK Corporate Governance Code (the Code) is the appropriate benchmark for how it conducts itself to the extent that it is applicable to the FRC. The Board complies with the Code or explains how the underlying principles have been met.

The FRC does not have shareholders in the usual sense. However, it has a wide range of stakeholders and conducts an extensive dialogue with them through an annual open meeting, the annual business plan, the annual report and individual consultations.

The Financial Reporting Council Limited is a company limited by guarantee incorporated in England and Wales, with its primary operations based at 8th Floor, 125 London Wall, London EC2Y 5AS. The principal activities of the FRC are set out on pages 15 – 25.

Governance Overview

The Schedule of Matters reserved to the Board and the terms of reference for each of the Committees and Councils together with the FRC's Articles of Association are published on the FRC website **https://frc.org.uk/About-the-FRC.aspx.**



The **Board** determines the FRC's overall strategy and its management and culture as well as determining the nature and extent of the significant risks to be taken in achieving the FRC's strategic objectives. Regulatory powers reserved to the Board include the issuing and maintenance of codes and/or standards for corporate governance, stewardship, corporate reporting, accounting, auditing and assurance services, and actuarial work; the exercise of the functions of the Secretary of State under Part 42 Companies Act 2006 i.e. the oversight of the regulation of statutory auditors and the exercise of the function of the Independent Supervisor of the Comptroller & Auditor General. The Board is supported by three governance committees – Audit Committee, Nominations Committee and Remuneration Committee – and by the Executive Committee, the Codes & Standards Committee and the Conduct Committee.

The **Executive Committee** assists the Chief Executive in his role including recommending the strategic direction of the FRC to the FRC Board, providing the day-to-day oversight of the work of the FRC, implementing the FRC's annual business plan and advising the Board on the FRC's budget.

The **Codes & Standards Committee** advises the FRC Board on maintaining an effective framework of UK codes and standards for corporate governance, investor stewardship, accounting, auditing and assurance, and actuarial technical standards.

The **Conduct Committee** exercises the statutory powers delegated to it by Government in relation to the review of corporate reports, and advises the Board on audit quality reviews, monitoring Recognised Supervisory and Qualifying Bodies, professional discipline, and oversight of the regulatory responsibilities of the accountancy and actuarial professional bodies.

Board of Directors

As at 13 July 2015

1	Sir Winfried Bischoff	2	Gay Huey Evans	3	Stephen Haddrill*
4	Mark Armour	5	Sir Brian Bender	6	David Childs
7	Elizabeth Corley	8	Olivia Dickson	9	Paul George*
10	Nick Land	11	Roger Marshall	12	Melanie McLaren*
13	Keith Skeoch				

* Executive Director

Changes to Board Membership, Rotation and Diversity

Changes to Board membership from 1 April 2014 to 31 March 2015

	Term start date	Term end date
Baroness Hogg		30 April 2014
Sir Winfried Bischoff	1 May 2014	
Peter Chambers		30 April 2014
David Childs	1 May 2014	
Richard Fleck		30 April 2014
Glen Moreno		30 April 2014
Jim Sutcliffe		16 January 2015

Changes to Board membership from 31 March 2015 to 1 July 2015

	Term start date	Term end date
John Stewart		1 July 2015

At least half the Board excluding the Chairman comprises independent non-executive directors. This assessment is based not only on the circumstances set out in the Code but also, given the functions of the FRC, on any relationships or significant links with those regulated by the FRC.

The biographies and terms of appointment for each Board Member are available on the FRC website.

Board Rotation

As the Directors of the FRC are also its members, the submission of Directors for re-election would not be meaningful. The Board has put in place an alternative to annual re-election; its annual effectiveness evaluation includes consideration of the continuation of each of the Directors and the Secretary of State has been invited to consider the continuation of the Chairman and Deputy Chairman on an annual basis.

Board Diversity

The FRC's commitment to promoting equality and diversity extends to the membership of the Board and its Committees. The Board satisfies this commitment by keeping under review the mix of skills and experience required on the Board and its Committees. Particular attention is paid to gender diversity. Although no specific targets are set, 30% of Board members, 23% of Conduct Committee members, 37% of Codes & Standards Committee members and 33% of Executive Committee members are female.

The work of the Board in 2014/15

During the year the Board

- Focused on the FRC's work in pursuit of the five broad objectives in the FRC's Plan for 2014/15, whilst taking account of emerging developments and reviewing the risks associated with each of the objectives. The key decisions taken are reported in the Strategic Report and include the approval of various standards and SORP statements.
- Started working on the FRC's next three year strategy (2016/2019).
- Considered the challenges arising out of the circumstances arising from the resignation of Jim Sutcliffe and developed the FRC's processes in relation to Board and Committee members notifying the Board of appointments to other entities.
- Considered the potential consequences of the EU Audit Regulation and Directive and worked with BIS on the FRC's role following implementation.
- Consulted on and issued amendments to the UK Corporate Governance Code;
- Under its responsibilities in the Companies Act 2006, required one of the Recognised Supervisory Bodies to carry out an external review of its process for approving statutory auditors and to implement the review's recommendations. It also consulted on and issued Guidelines in relation to enforcement measures against Recognised Supervisory and Qualifying Bodies under the Act.
- Received periodic reports from the Executive Directors of Conduct and Codes & Standards together with quarterly reports of progress on all key projects in addition to individual reports on specific projects.
- Through a group led by Mr Land, agreed the lease of premises at 125 London Wall and the detailed arrangements in relation to its refurbishment and the surrender of the lease at Aldwych House.

The minutes of FRC Board meetings and all its decisions are published and available on the FRC website.

Board and Committee Effectiveness

Board effectiveness is reviewed every year. Having commissioned an independently led review last year, this year the Board commissioned an internal review of the Board, its Committees and Councils. The evaluation process was undertaken over the autumn of 2014 and involved the completion of surveys by, and interviews of, each of the members of the respective Board/Committee/Council by the relevant chairman who then reported on both the survey and the interviews. The review was completed in stages concluding with a Board review which took account of the reports from each of the Chairmen of the Committees and Councils. The Deputy Chair also interviewed all Board members and reported on the effectiveness of the Chair.

As concluded last year during the independently led review, the Board was noted to have the following strengths: Board contribution, Chairmanship of the Board and its Committees, knowledge of the stakeholder landscape, ability to contribute to strategy and support from the Executive and the Committees and Councils. Whilst clarity of the governance structure was concluded to be a challenge last year, it was noted to be a strength this year with the Board and all the Committees and Councils reporting a good understanding of their roles and how they relate to each other.

Considerations and challenges for the Board identified during the review were: both executive and non-executive succession planning, induction arrangements, scheduling of Board meetings and Board papers and agreeing and monitoring progress against the plan. Specific action already taken to address the challenges includes a review of non-executive succession planning leading to improved procedures and reporting to the restructured Nominations Committee, a review and report to the Nominations Committee of the Executive succession plan; the commencement of a review of induction and training plans; a review of the Board calendar with a view to improving the scheduling of meetings in 2017; further training to support continuing improvement in the preparation of papers and ensuring more time is available for approval of the plan and monitoring performance against it.

The wider governance structure effectiveness review identified strengths in the following areas: the clarity of the governance structure and the contribution and composition of each element of the structure, Chairmanship of the various committees and councils, the support and contribution of the executive and the structure of the agendas.

Challenges common to more than one element of the governance structure were: reporting across and up and down the governance structure; horizon scanning; the appropriate focus on actuarial issues; overcrowded agendas; succession planning; induction and ongoing training and continued improvement in the quality of papers and presentations by the Executive. Actions to address each of these areas have already been taken and further actions have been planned and approved by the Board. Actions taken thus far, and in addition to the action described above in relation to the findings of the Board review, include the design of a new approach to horizon scanning and strategy development; the review of forward agendas to ensure appropriate time is given to reporting on the work of other Committees/Councils and actuarial issues; and increased numbers of meetings where agendas are becoming crowded.

Overall the review demonstrates that the Board, its Committees and Councils are working well and displaying significant strengths. Good progress has been made since the review last year, but there are some areas where further action is being taken.

The Board also noted at the conclusion of its review that there may be a need to change elements of its structure and operations in the light of the EU Audit Regulation and Directive and depending on how BIS decide to implement the Directive and the body or bodies designated as a Competent Authority. Over the coming year the FRC will review the FRC's governance structure in the light of the decisions made.

Board Committees

Audit Committee

The Audit Committee assists the Board in fulfilling its responsibility for monitoring the quality and integrity of the accounting, auditing and reporting practices of the FRC. The Committee's main purpose is to scrutinise the FRC's accounting and financial reporting and the audit of the FRC's financial statements.

Responsibilities

- Reviewing the financial statements to ensure compliance with relevant statutory requirements.
- Reporting to the Board on the appropriateness of the accounting policies used in preparing the financial statements.
- Advising the Board on whether the Committee believes the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for stakeholders to assess the company's performance, business model and strategy.
- Overseeing the relationship with the external auditor and making recommendations concerning their performance.
- Reviewing the risk and internal controls system and carry out specific reviews of key areas of financial reporting risks.
- To monitor and review the need for an internal audit function.

Committee Meetings

Meetings are attended by the three independent non-executive directors and, by invitation, the Chief Executive, the Company Secretary, the Finance Director and the Head of Finance. The external auditor, haysmacintyre is also invited to attend each meeting. The Committee meets with the external auditor in private at least once a year and, in addition, the Chair of the Committee meets with the auditor privately from time to time.

During the year the Committee focussed on:

Financial reporting

The Committee considered:

- The suitability of accounting policies and practices.
- The clarity of disclosures and compliance with financial reporting standards and relevant financial and governance reporting requirements.
- Advising the Board on whether the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for stakeholders to assess the company's performance, business model and strategy.

To assist with this review, the Committee receives reports from the Finance Director and from the external auditor on the outcomes of the annual audit.

In relation to the 2014/15 financial statements, the key reporting issues considered by the Committee were as follows:

- The accounting treatment of fees in relation to a review being carried out into the effectiveness of our AQR and CRR activities by a third party consulting firm. The Committee agreed that it was appropriate to recognise the costs incurred during the year as expenditure in the year
- The accounting treatment and recognition of cost awards received in respect of an accountancy disciplinary case. Costs awards received are included in the financial statements as a reduction to total expenditure incurred.
- The completeness of accountancy case costs incurred and the process for charging the costs of in-house resources to cases. Case managers have the responsibility for agreeing the necessary expenditure accruals for their cases. These figures are confirmed by statements from individual suppliers at quarter-ends setting out the total amount owing to them including for unbilled work. Internal costs are charged to cases under the Case Cost agreement only for staff who have been employed for that purpose.

External audit

Haysmacintyre were appointed as auditor in 2013 following a tender process involving three firms.

The Committee reviewed the detailed audit plan put forward by Haysmacintyre which included their assessment of the key areas of risk. For the 2014/15 financial year these were identified as:

- **Revenue recognition**
- **Disciplinary case costs and provisions**
- **Cost recognition and allocation**

To assess the effectiveness of the auditor, the Committee reviewed the extent to which the auditor fulfilled the agreed audit plan and any variations from it. The Committee also reviewed the auditor's report of major issues arising during the course of the audit. The Committee challenged the work performed by the auditor to test management's assumptions and estimates made for each risk area. The Committee also received feedback from management in their assessment of the auditor.

Based on their own interaction with the auditor, together with input from management, the Audit Committee is satisfied with the auditor's effectiveness.

To protect the objectivity and independence of the external auditor, the FRC has a policy whereby no non-audit services are permitted to be carried out by the external auditor.

Internal control

The Committee reviewed key aspects of the internal controls system, including IT and data security. A number of areas for improvement were identified for implementation by the IT department. These included:

- Encryption of all data held on third party application
- Regular mandatory training for all staff on data security measures
- Extending the use of the Boardpad application for the secure distribution of Board papers

The Committee received regular updates on the financial performance of the company including its expenditure compared to budget and progress made in collecting the funds required to fully support its operations.

The Committee monitored the provision of funding for the XBRL taxonomy development project and approved the associated expenditure. The Committee also monitored the expenditure and risks associated with the office relocation to London Wall, receiving updates on the actual expenditure incurred.

Because of its size and nature it has not previously been considered necessary for the company to have an internal audit function. Regular dialogue has been maintained with the external auditor and the Committee takes into account the assurance derived from their work. In view of the recent and expected further expansion of the FRC, the Committee has initiated a review of the benefits of an internal audit function and how it might best be provided.

Risk management

We have carried out an assessment of the principles risks facing the company to ensure that significant risks were clearly identified and appropriately managed. Reports were received from management identifying key strategic and operational risks to the FRC and on the mitigating actions put in place. The FRC's principal risks are set out on pages 29-31.

Nick Land

Chairman, Audit Committee

Nominations Committee

Responsibilities:

- Leading the selection process and making recommendations for Directors of the FRC (except for the Chair and the Deputy Chair who are appointed by the Secretary of State) and co-opted members of the Conduct Committee and Codes & Standards Committee.
- Approving the selection process for members of the Case Management Committee, Monitoring Committee and Accounting, Audit & Assurance and Actuarial Councils.
- Overseeing the selection process and approving the appointments of the FRC's General Counsel & Company Secretary, Executive Counsel and the Convener to the FRC's Accountancy and Actuarial Schemes.

During the year the Committee's terms of reference were amended in the light of the Effectiveness Review to reduce its membership and to reflect the FRC's commitment to diversity. The Committee:

- Reviewed the FRC's non-executive succession planning. This included a review of the skills and stakeholder representation on the Board and across the full governance structure. The review concluded that the skills and stakeholder representation were appropriate but identified the need to appoint to the Board an actuary and an individual with experience in the non-listed sector. These findings led to a search led by the Nomination Committee and resulted in a recommendation to the Board to appoint John Comber and Ray King to the Board and the Codes & Standards Committee. Ray King was also appointed Chair of the Audit & Assurance Council. The review led more generally to strengthened succession planning processes.
- Recommended to the Board the appointment of Nick Land as the Chair of the Codes & Standards Committee following the resignation of Jim Sutcliffe and the reappointments of Mark Armour, Olivia Dickson and Keith Skeoch.
- Approved the FRC's nomination of Roger Marshall for membership of EFRAG.
- Led the selection process for the Chair of the Audit & Assurance Council to replace Nick Land. The selection process was conducted with the involvement of an independent assessor, Sarah Anderson. Ms Anderson does not have any other connection with the FRC. The process involved open advertising and interviews by all members of the Committee and Ms Anderson.
- Approved the processes for appointments to the Conduct Committee, Councils, Case Management Committee and Monitoring Committee and recommended to the Board appointments and reappointments to the Codes & Standards Committee and Conduct Committee. In particular, the appointment of Geoffrey Green to the Conduct Committee following his appointment as Chair of the FRRP.
- Approved the appointment of the Convener, Rosemary Rollason and the appointments committee under the Accountancy and Actuarial Schemes and the Auditor Regulatory Sanctions Procedure.

Remuneration Committee

Responsibilities:

- Determining and reviewing the remuneration policy for the FRC and for determining the remuneration of the Chief Executive, the Executive Committee and the Executive Counsel.

During the year the Committee:

- Reviewed the reward benchmarking exercise undertaken by the Executive and approved changes to the life assurance and Private Health Insurance (PHI) benefits provided to staff.
- Reviewed and approved the collective and individual objectives of the Executive Committee.
- Approved the budgetary limits for the salary review and bonus pool for all employees, and agreed that the criteria for the award of a companywide bonus had been met and supported a recommendation to the Board by the Chief Executive in that regard.
- Reviewed and approved the remuneration of the Chief Executive pursuant to recommendations from the Chairman; reviewed and approved the remuneration of members the Executive Committee and the Executive Counsel pursuant to recommendations from the Chief Executive; and reviewed remuneration proposals in relation to the Senior Leadership Group.
- Reviewed the expenses of both the executive and non-executive Board members.
- Reviewed the remuneration of Board, Committee and Council members and resolved not to make any changes to remuneration across the structure but to review again this year in the light of any changes consequent to the implementation of the EU Audit Directive and Regulation. The Committee did approve an increase in fees for the Group of the Monitoring Committee responsible for the audit monitoring work to £21,000 with effect from 1 April 2015. This increase was to reflect the increase in volume of work following the CMA recommendations.
- Reviewed the remuneration of the Chair of the Monitoring Committee and Financial Reporting Review Panel (FRRP) in the light of the proposed appointment of Geoffrey Green and approved annual fees of £60,000.

The Committee's determination of the remuneration of the executive directors was in accordance with the criteria set out in the Remuneration Policy described below and against the collective and individual objectives approved at the beginning of the year as well as affordability. The salary reviews determined by the Committee were consistent with the standard salary reviews awarded to all FRC employees. The Committee was assisted in its consideration by the views of the non-executive directors on the performance of the FRC Executive and all members of the Executive Committee and by the results of the annual FRC staff survey.

Executive Committee

Responsibilities

Ensuring that the FRC is joined up and assisting the Chief Executive in the performance of his duties including:

- Recommending strategic direction to the FRC Board.
- Providing day-to-day oversight of the work of the FRC, its operational policies and protection of the FRC reputation.
- Overseeing the implementation of the FRC business plan.
- Making recommendations to the FRC Board on the budget, business plan, Board agenda and management of the organisation.
- Debating and resolving issues affecting the Codes and Standards and Conduct Divisions.

- Recommended strategic direction to the Board through its work on the Board Strategy Day and Annual Plan & Budget and on discrete issues reserved to the Board. The Committee exercised oversight of the work of the FRC, regularly reviewing progress against the FRC Plan, the resources available for the work, the FRC budget, risk (including reputational risk) and whether operational policies were fit for purpose. The Committee reported to the Board regularly on progress.
- Kept under review the operations to move premises and to change IT provider.
- Continued its drive to raise the quality of the performance of FRC staff by responding to the feedback from the FRC Employee Survey and the further development of the FRC's Learning and Development policy and Performance Management processes. In particular, the Committee launched the FRC's first Future Leaders Programme.

The Executive Committee met 11 times during the year on a formal basis and more often on an informal basis. Membership of the Committee was as follows:

Stephen Haddrill	Chief Executive
Paul George	Executive Director, Conduct
Melanie McLaren	Executive Director, Codes & Standards
Anne McArthur	General Counsel & Company Secretary
Graham Clarke	Finance Director
Chris Hodge	Executive Director, Strategy

Codes & Standards Committee

Responsibilities:

- Advising the Board on maintaining an effective framework of UK codes and standards for governance, accounting, auditing and actuarial work.
- Monitoring international developments to ensure appropriate and effective UK input in to international standard setting.
- Identifying and assessing the current, emerging and potential risks to the quality of corporate governance and reporting in the UK and approving the adequacy of actions to mitigate those risks.
- Approving operating plans for the FRC's codes and standards activities and overseeing the quality of work and delivery of the principal elements of those plans.
- Overseeing the work of the Councils in accordance with the strategic direction provided by the FRC Board, ensuring that the resources of the whole of the FRC relevant to a particular issue are properly deployed.
- Appointing members to the Accounting, Audit & Assurance and Actuarial Councils and overseeing the appointment of any groups by the Councils.

During the year the Committee exercised oversight of the work of the Codes & Standards Executive and the Accounting, Audit & Assurance and Actuarial Councils. This included the approval of work plans and monitoring progress against the plans. The Committee also noted the progress made by the Financial Reporting Lab on various initiatives.

The Committee reviewed all draft codes and standards to be tabled to the Board with the advice of the respective Council. Following its work in the previous year on the development of principles to inform decisions on the development of codes, standards and guidance the Committee developed a Standards and Guidance Framework.

The Committee approved Guidance on the Strategic Report, the FRC Statements on the Investment Association SORP and the Social Housing SORP and approved the Northern Ireland Federation of Housing Associations as a SORP making body.

On the FRC's role in influencing international standards and guidance, the Committee monitored developments at the IASB and the IAASB.

On Corporate Governance, the Committee considered a range of issues including Proxy Advisers, the Investor Forum and Stewardship strategy.

The Committee approved appointments and reappointments to the Councils: details of Council Memberships can be found on the FRC website **https://www.frc.org.uk/About-the-FRC/FRC-structure.aspx.**

Conduct Committee

Responsibilities:

- Exercising the functions delegated to the Conduct Committee by the Secretary of State under the Companies Act 2006 and the Companies (Audit, Investigations and Community Enterprise) Act 2004.
- Advising the Board on the exercise of the functions delegated to the Board by the Secretary of State under the Companies Act 2006.
- Advising the Board on the approach to be taken to non-statutory oversight of the actuarial and accountancy professions.
- Exercising the functions delegated to the Conduct Committee in accordance with the Accountancy and Actuarial Schemes.
- Deciding whether to commence a supervisory inquiry, determine the scope of any such inquiry and what, if any, action to be taken on its conclusion.
- Identifying and assessing the current, emerging and potential risks to the quality of corporate governance and reporting in the UK and approving the adequacy of actions to mitigate those risks.
- Appointing members of the Financial Reporting Review Panel, the Monitoring Committee and Case Management Committee.

During the year the Committee had oversight of the varied work of the Conduct Executive. In doing so the Committee approved the Conduct Executive's work plan and monitored progress against the plan with a focus on the quality, timeliness and consistency of the work and also the adequacy of resources both during the year and in the future. In this regard the Committee had a particular focus on the potential impact of the EU Audit Regulation and Directive and agreed a restructure of the Audit Quality Review team.

On Corporate Reporting Review the Committee approved amendments to the CRR Operating Procedures and approved the CRR Annual Report.

On Professional Discipline, in addition to reviewing progress on cases, the Committee has various specific responsibilities under the Accountancy and Actuarial Schemes: pursuant to these responsibilities, the Committee commenced five investigations and amended the scope of six cases. The Committee received Formal Complaints in relation to three matters and decisions to close investigations in eight matters and set and reviewed the budgets in all active disciplinary cases. The Committee also reviewed the Scheme, Regulations and Guidance and recommended changes to the Schemes to the Board.

The Committee reviewed progress on cases under the Auditor Regulatory Sanctions Procedure.

The Committee determined that there should be a review of the effectiveness of the FRC's monitoring activities and appointed a Project Steering Group to determine the terms of reference and to select an independent reviewer. The Group recommended the appointment of McKinsey's which was approved by the Committee. In view of the costs involved, the Board was notified and endorsed the appointment.

On Professional Oversight, the Committee monitored the progress of oversight work done throughout the year, approved the work plan for 2015/16, advised the Board on the appropriate response to failings by one of the Recognised Supervisory Bodies and approved the publication of the FRC's Key Facts and Trends Report.

The Committee approved the appointment of Geoffrey Green as Chair of the Financial Reporting Review Panel and also agreed a number of reappointments to the Panel. The Committee also approved appointments and reappointments to the Case Management Committee. Details of the Panel and Case Management Committee Memberships can be found on the FRC website.

Directors' Remuneration Report

Remuneration Policy

The remuneration of non-executive directors, including the Chairman and Deputy Chairman is determined by the Board. The Board determines the remuneration of non-executive directors by assessing the responsibility, workload and time commitment to the role and by calculating a daily rate of fees comparable to fees paid by other regulators and in relation to comparable roles within the public sector. Non-executive directors are paid basic annual fees of £25,000, additional fees for membership of the Conduct Committee or Codes & Standards Committee of £10,000 and for chairmanship of the Audit and Remuneration Committees of £5,000. The Deputy Chairman receives a basic annual fee of £35,000 to reflect additional responsibilities. The Chair of the Conduct Committee is paid fees of £90,000 and the Chair of the Codes & Standards Committee is paid £60,000. Council Chairs are paid annual fees of £50,000 plus any supplemental fees determined by the Remuneration Committee for work falling outside a Chair's normal duties.

The fees detailed above were determined on the review undertaken during the FRC reforms in 2012. Board member fees were reviewed by the Remuneration Committee during the year but no changes were recommended to the Board.

The Remuneration Committee determines the framework and policy for the remuneration of the FRC Chairman and the Executive Directors and determines the total individual remuneration package of the FRC Chairman and the Executive Directors. The FRC does not have shareholders in the usual sense and so has not consulted shareholders on remuneration. The remuneration of the executive directors comprises the following components: salary, bonus of up to 20% of annual salary, pension contributions of up to 10% and other contractual benefits including private health and dental cover, death in service and permanent health insurance. As with all members of the Executive, both salary review and bonus eligibility depends on executive directors achieving the necessary ratings bandings for performance and citizenship – living the FRC Values. Executive directors are treated differently from other members of staff in that they are required to achieve higher citizenship ratings to qualify for a bonus and higher performance and citizenship ratings to achieve a salary review. The performance of Executive Directors is assessed against both individual and collective objectives. 25% of each Executive Director's bonus potential is assessed on the extent to which the collective objectives have been achieved and the executive Director's contribution to achievement.

The total remuneration and benefits received are shown in the following table, which has been subject to audit (see also note 3 to the Financial Statements).

Non-executive Directors	2014/15 Fees/ Salary	2014/15 Bonus	2014/15 Pension	2014/15 GHI	2014/15 Private Medical / Dental	2014/15 Total	2013/14 Total
Sir Winfried Bischoff (from 1 May 2014)	110,000					110,000	
Baroness Hogg (to 30 April 2014)	10,000					10,000	120,000
Gay Huey Evans (Deputy Chair from 1 May 2014)	44,167					44,167	35,000
Glen Moreno (to 30 April 2014) (1)	-					-	23,333
Mark Armour	25,000					25,000	25,000
Sir Brian Bender	35,000					35,000	2,917
Peter Chambers (to 30 April 2014)	2,917					2,917	37,917
David Childs (from 1 May 2014)	82,500					82,500	
Elizabeth Corley (2)	30,000					30,000	27,083
Olivia Dickson	50,000					50,000	50,000
Richard Fleck (to 30 April 2014) (3)	7,500					7,500	90,000
Nick Land	56,667					56,667	55,000
Roger Marshall	85,000					85,000	85,000
Sir Steve Robson (to 31 October 2013)	-					-	20,417
Keith Skeoch (4)	35,000					35,000	35,000
John Stewart	35,000					35,000	2,917
Jim Sutcliffe (to 16 January 2015)	47,727					47,727	60,000
Sub-total	**656,477**	**0**	**0**	**0**	**0**	**656,477**	**669,584**
Executive Directors							
Stephen Haddrill (5)(6)	362,344	65,222	36,234	5,405	-	469,206	462,564
Paul George (5)(6)	294,335	41,000	29,433	3,572	2,323	370,663	364,538
Melanie McLaren (5)(6)	316,123	44,000	-	3,527	-	363,650	347,280
Sub-total	**972,802**	**150,222**	**65,667**	**12,504**	**2,323**	**1,203,518 (7)**	**1,174,382**
Grand Total	**1,629,279**	**150,222**	**65,667**	**12,504**	**2,323**	**1,859,995**	**1,843,966**

Where Directors were appointed during the year, the amounts shown are for the period from the date of their appointment.

(1) Glen Moreno waived his fees from 1 December 2013.

(2) Elizabeth Corley waived her Remuneration Committee Chair fees of £5,000 in favour of charity in 2014/15 (£2,083 in 2013/14).

(3) Richard Fleck's fees as shown are for the period up to the date of the end of his term as a Director and Chair of the Conduct Committee. He continued to receive fees as Chair of the FRRP and a member of the Conduct Committee until the end of the year.

(4) From 1 April 2012 Keith Skeoch waived his fees in favour of charity.

(5) Executive Directors are entitled to receive pension contributions and other benefits. The figures shown are the cash equivalents of their full pay and benefits

(6) The average salary and reward increases including the cash equivalent benefits were 2% in 2014/15 for all staff including the executive Directors.

(7) Total Directors remuneration in 2014/15 amounted to 11.5% of total company remuneration, including secondees (2013/14: 12.8%).

Board and Committee Member attendance for the period 1 April 2014 to 31 March 2015.

	FRC Board	Nominations Committee	Remuneration Committee	Audit Committee	Codes & Standards Committee	Conduct Committee
Sir Winfried Bischoff	6/6	3/3	3/3			
Baroness Hogg	1/1					
Gay Huey Evans	6/7	2/3				9/11
Glen Moreno	1/1					
Stephen Haddrill	7/7	2/2				
Mark Armour	7/7	1/2		4/4		
Sir Brian Bender	6/7	1/2				9/11
Peter Chambers	1/1					1/1
David Childs	6/6	3/3				10/10
Elizabeth Corley	6/7	2/3	3/3			
Olivia Dickson	6/7	2/2			7/7	
Richard Fleck	1/1					10/11
Paul George	7/7					11/11
Roger Marshall	6/7	1/2			7/7	
Melanie McLaren	7/7				6/7	
Nick Land	7/7	3/3	3/3	4/4	4/7	
Keith Skeoch	7/7	2/2		4/4	4/7	
John Stewart	5/7	2/2			5/7	
Jim Sutcliffe	4/6	2/2			5/5	
Keith Barton					7/7	
Liz Murrall (from 1 August 2014)					5/5	
Allister Wilson					7/7	
Lillian Boyle						10/11
Hilary Daniels						11/11
Mark Eames						11/11
John Kellas						11/11
Lois Moore						10/11
Malcolm Nicholson						10/11
Joanna Osborne						11/11
Martin Slack						9/11
Philip Taylor						11/11
Ian Wright*						4/11

*Acting Deputy Chair, Financial Reporting Review Panel – receives papers and is invited to meetings as necessary.

3 Financial Statements

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE FINANCIAL REPORTING COUNCIL LIMITED

Opinion on financial statements of The Financial Reporting Council Limited ("FRC")

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2015 and of its loss 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.

The financial statements comprise the Profit and Loss Account, the Balance Sheet, the Statement of Changes in Equity, the Cash Flow Statement and the related notes. 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 UK and Republic of Ireland.

Our assessment of risks of material misstatement

We identified the following risks of material misstatement that had the greatest effect on the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team:

Risk	Our response
Given the nature of the FRC's regulatory and disciplinary schemes, a risk arises in connection with the completeness and valuation of litigation cost accruals.	We tested the operating effectiveness of procedures and controls implemented by the FRC in respect of its regulatory activities and disciplinary schemes. We reviewed a sample of cases, specifically checking that the procedures and controls were being followed.
Revenue recognition, including the completeness of levy income.	We tested the operating effectiveness of procedures and controls implemented by the FRC and service organisations engaged by it in respect of revenue recognition. We reviewed the recognition of income around the year-end.
There is a risk of inappropriate allocation of personnel and other expenditure between core operating costs, audit quality review costs and disciplinary case costs which may result in the overstatement of income (due to incorrect recharges to the relevant participant).	We reviewed the systems used to allocate costs incurred by the FRC between the costs of running disciplinary cases and its other activities. We tested a sample of expenditure ensuring that costs incurred have been appropriately allocated and if appropriate, correctly recharged to the relevant participant.

Our 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.

Based on our professional judgement, we determined materiality for the company to be £300,000, based on 1% of total expenditure (gross of the case cost awards). Due to the nature of the company we considered this measure to be the main focus for the readers of the financial statements.

On the basis of our risk assessments, together with 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 £225,000.

We agreed to report to the Audit Committee all audit differences in excess of £15,000, 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 Financial Reporting Council Limited is a standalone entity based in London the scope of our work was an audit of the financial statements of the company. Our audit was scoped by obtaining an understanding of the company and its environment, including internal control, and our testing was focussed on areas where we assessed there to be the highest risk of material misstatement as described above.

We obtained an understanding of how the company uses service organisations in its operations and evaluated the design and implementation of relevant controls at the company that relate to the services provided by service organisations. We visited Mouchel Business Services, the service organisation engaged by the FRC to collect the levy income from large private entities, public sector organisations and pension funds, at their offices in Middlesbrough.

We undertook an interim visit to evaluate the internal controls over those risk areas we identified as being relevant to our audit. During the final audit we performed specifically designed audit tests on significant transactions, balances and disclosures.

The Senior Statutory auditor and Audit Manager met regularly throughout the year with the senior members of the company's finance team in order to maintain and reinforce our knowledge of the FRC and the risks it faces. This dialogue continued throughout the audit process as we reassessed and re-evaluated audit risks where necessary and tailored our approach accordingly.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion 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.

Matters on which we are required to report by exception

Under the ISAs (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with our knowledge of the company acquired in the course of performing our audit; or
- otherwise misleading.

In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the annual report is fair, balanced and understandable and whether the annual report appropriately discloses those matters that we communicated to the audit committee which we consider should have been disclosed.

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept, 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.

We have nothing to report in respect of the above.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

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.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at **www.frc.org.uk/auditscopeukprivate**

David Cox (Senior statutory auditor)

for and on behalf of haysmacintyre,

Statutory Auditor

26 Red Lion Square

London

WC1R 4AG

THE FINANCIAL REPORTING COUNCIL LIMITED

Profit and Loss account for the year ended 31 March 2015

	Note	2014/15 £'000	2013/14 £'000
Revenue		**28,848**	26,058
Operating expenses	2	**(29,103)**	(25,986)
Operating (loss)/ profit		**(255)**	72
Interest receivable		**71**	113
(Loss)/ profit on ordinary activities before taxation		**(184)**	185
Tax on (loss)/ profit on ordinary activities		**(14)**	(23)
(Loss)/ profit on ordinary activities after taxation and (loss) profit for the financial year		**(198)**	162

THE FINANCIAL REPORTING COUNCIL LIMITED

Registered number: 2486368

Balance Sheet at 31 March 2015	Note	31 March 2015 £'000	31 March 2014 £'000
Fixed assets			
Intangible assets	5	**8**	16
Tangible assets	6	**2,803**	1,176
		2,811	1,192
Current assets			
Debtors	7	**3,447**	4,142
Current asset investments	8	**8,008**	5,900
Cash at bank and in hand	8	**476**	3,954
		11,931	13,996
Creditors – amounts falling due within one year	9	**(5,814)**	(6,500)
Net current assets		**6,117**	7,496
Total assets less current liabilities		**8,928**	8,688
Creditors – amounts falling due after more than one year	10	**(1,382)**	(974)
Provisions for liabilities	11	**(30)**	-
Net Assets		**7,516**	7,714
Capital and reserves			
Accounting, auditing and corporate governance:			
- General reserve		**2,420**	2,563
- Corporate reporting review legal costs fund		**2,000**	2,000
Actuarial standards and regulation:			
- General reserve		**1,096**	1,151
- Actuarial case costs fund		**2,000**	2,000
		7,516	7,714

The financial statements and notes on pages 50 to 60 were approved by the Board of Directors on 13 July 2015 and were signed on its behalf by:

Sir Winfried Bischoff

Chairman

THE FINANCIAL REPORTING COUNCIL LIMITED

Statement of Changes in Equity for the year ended 31 March 2015

	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 2014	2,563	2,000	1,151	2,000	7,714
(Loss) for the year	(143)	-	(55)	-	(198)
At 31 March 2015	2,420	2,000	1,096	2,000	7,516

Cash Flow Statement for the year ended 31 March 2015

	Note	2014/15 £'000	2013/14 £'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Cash generated by operations	13	**603**	1,315
Corporation tax paid		**(23)**	(32)
Total cash inflow from operating activities		**580**	1,283
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of tangible assets		**(1,998)**	-
Current asset investments made		**(2,108)**	(400)
Interest received		**48**	81
Total cash outflow from investing activities		**(4,058)**	(319)
NET (DECREASE)/ INCREASE IN CASH AND CASH EQUIVALENTS		**(3,478)**	964
Cash and cash equivalents at 1 April	8	**3,954**	2,990
CASH AND CASH EQUIVALENTS AT 31 MARCH	8	**476**	3,954

1. 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 2AS.

The following accounting policies, which have been applied consistently, are considered material in relation to the FRC.

a) Basis of Preparation

These financial statements for the year ended 31 March 2015 are based on FRS 102, the Financial Reporting Standard applicable in the UK and Republic of Ireland, 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.

The going concern basis of accounting has been applied in preparing these financial statements.

Presentation of Financial Statements

The presentation 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 a variety of sources of revenue and accounts for them as described below:

- Revenue in respect of levies is accounted for on a receipts basis, as they are voluntary contributions.
- Previously the FRC received Government grants for capital purposes. The FRC applied the accrual method of accounting for these capital grants and the grants were amortised over the useful economic life of the assets which they were used to purchase. There was no deferred income carried forward into 2014/15 as the remaining income had been fully amortised by 31st March 2014.
- The following revenue is received from participants to fund specific activities:
  - Revenue receivable from the ICAEW in respect of Audit Quality Review 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 is recognised as the costs to be reimbursed are incurred in each financial year.
  - Revenue in respect of publications of books, guidelines 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 Audit Commission 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 reimbursement is contractual.

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, over their 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

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 other professional costs of accountancy and actuarial disciplinary cases and Corporate Reporting Review cases incurred in the period are included in the accounts 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 under FRS 102 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 profit and loss account of the FRC as a reduction to case costs incurred when they become virtually certain.

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 virtually certain.

f) Costs Funds

The FRC has two costs funds: The Corporate Reporting Review Legal Costs Fund and the Actuarial Case Costs Fund.

The FRC maintains a Fund to enable the Conduct Committee to take steps to pursue compliance with the applicable requirements of the Companies Act 2006, including applicable accounting standards, and to investigate departures from those requirements and standards. The Fund may only be used for this purpose and may not be used to meet other costs incurred by the Company.

Case costs are met in the first instance from the Fund, which is then replenished in the following financial year on the same basis as the costs of the FRC's core operating activities. If the Fund falls below £1m in any one year, the Department for Business, Innovation and Skills (BIS) will make an additional grant to cover legal costs subsequently incurred in that year.

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 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 BIS for the purposes of section 456 of the Companies Act 2006.

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.

2. Operating Expenses

	2014/15 £'000	2013/14 £'000
Staff and related people costs (note 3)	**17,679**	16,071
IT and facility costs	**3,113**	2,064
Depreciation and amortisation costs	**378**	607
Auditor's remuneration:		
- audit	**44**	43
- non – audit services	**-**	-
XBRL taxonomy development costs	**285**	1,300
Accountancy and actuarial case costs – gross	**5,563**	5,573
- Less cost awards recovered	**(1,148)**	(2,250)
Accountancy and actuarial case costs – net	**4,415**	3,232
Other operating expenses		
- Travel and conferences	**762**	599
- Legal and professional fees	**666**	467
- Contribution to EFRAG	**284**	301
- All other costs	**1,477**	1,211
Total operating expenses	**29,103**	25,986

3. Staff and related people costs (including directors)

	2014/15 £'000	2013/14 £'000
Permanent staff:		
Salaries		
	12,972	11,525
Social security costs	**1,732**	1,448
Other pension costs	**1,333**	1,221
Total permanent staff costs	**16,037**	14,194
Other people related costs:		
Seconded staff and contractors	**127**	209
Fees paid to Board, Committee and Council members	**1,292**	1,392
Other costs	**223**	276
Total staff and related people costs	**17,679**	16,071

The average number of permanent staff employed in the financial year was 143 (2013/14: 120). Of this the average number of persons so employed under: accounting, auditing and corporate governance including audit quality review and accountancy disciplinary cases was 136 (2013/14: 114) and actuarial standards and regulation was 7 (2013/14: 6).

The FRC does not operate a pension scheme. Other pension costs comprise payments to individual personal pension schemes.

Directors' emoluments

	2014/15 £'000	2013/14 £'000
Fees (included in staff costs)	**1,794**	1,752
Other pension costs		
	66	92
Total directors emoluments (see page 46)	**1,860**	1,844
Social security costs	**225**	218
	2,085	2,062

Details of the emoluments of the directors are contained in the Directors' Remuneration Report on page 46.

4. 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 at bank and in hand, current investments, loans debtors and creditors that arise directly from its operations.

The financial instruments include surplus funds which will be used to fund future operating costs including case costs. 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 trade receivables for recoverability on an individual basis and to make provisions where considered necessary. In assessing recoverability management takes into account any indicators of impairment up until the reporting date.

The trade debtors were not impaired; hence no impairment losses have been recognised.

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.

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 is 0.9% (2014: 1.2%) and none of the deposits have 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.

5. Intangible Assets

	Software
	£'000
Cost at 1 April 2014	278
Additions	11
Cost at 31 March 2015	289
Amortisation at 1 April 2014	262
Charge for year	19
Amortisation at 31 March 2015	281
Net book value at 31 March 2015	**8**
Net book value at 31 March 2014	16

6. Tangible Assets

	Leasehold improvements	**Office equipment**	**Fixtures, fittings and furniture**	**Total**
	£'000	£'000	£'000	£'000
Cost at 1 April 2014	1,728	1,468	867	4,063
Additions	1,471	171	345	1,987
Disposals	(699)	(7)	(17)	(723)
Cost at 31 March 2015	2,500	1,632	1,195	5,327
Depreciation at 1 April 2014	699	1,411	777	2,887
Charge for year	171	95	94	360
Disposals	(699)	(7)	(17)	(723)
Depreciation at 31 March 2015	171	1,499	854	2,524
Net book value at 31 March 2015	**2,329**	**133**	**341**	**2,803**
Net book value at 31 March 2014	1,029	57	90	1,176

7. Trade Debtors

	2014/15 £'000	2013/14 £'000
Trade debtors		
	595	529
Prepayments	**1,048**	623
Accrued income	**1,517**	1,720
Other debtors	**287**	1,270
	3,447	4,142

Accrued income represents amounts receivable from the accountancy professional bodies in respect of accountancy disciplinary case costs. This amount is invoiced and received after the year end.

8. Cash and Investments Held

	Cash 2015 £'000	Deposits 2015 £'000	Total 2015 £'000	Cash 2014 £'000	Deposits 2014 £'000	Total 2014 £'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	476	4,008	4,484	1,954	3,900	5,854
Totals at 31st March 2015	**476**	**8,008**	**8,484**	3,954	5,900	9,854

Cash at bank and in hand represent cash and cash equivalents and the deposits represent current asset investments.

9. Creditors – Amounts falling due within one year

	2014/15 £'000	2013/14 £'000
Trade creditors	**693**	1,011
Other taxation and social security	**1,029**	1,069
Accruals	**1,483**	2,095
Deferred income	**1,120**	1,008
Deferred lease incentive	**343**	343
Other payables	**1,132**	951
	5,800	6,477
Corporation Tax at an effective rate of 20% (2013/14: 20%) on interest		
Interest Income of £71,000 (2013/14: £113,000).	**14**	23
	5,814	6,500

10. Creditors – Amounts falling due after more than one year

	2014/15 £'000	2013/14 £'000
Deferred lease incentive	**1,382**	974
	1,382	974

11. Provisions for Liabilities

Leasehold improvements and dilapidations	2014/15 £'000
Balance at 01 April 2014	**-**
Amount charged to Profit and Loss account	**30**
Balance at 31 March 2015	**30**

12. Significant transactions with other standard setters

The FRC raises the UK contribution to the funding of the International Accounting Standards Board (IASB) by issuing invoices and collecting monies on its behalf. The FRC makes a small charge for providing this service. The amount of monies collected during the year was £845,000 (2013/14: £885,000), of which £27,000 (2013/14: £50,000) remained to be paid over by the FRC to the IASB as at 31 March 2015.

13. Cash flow statement – cash generated from operations

	2014/15 £'000	2013/14 £'000
(Loss)/ Profit on ordinary activities before taxation	**(184)**	185
Adjustments for:		
- Interest income	**(71)**	(113)
- Depreciation and amortisation	**378**	607
- Increase/ (Release) of dilapidation provision	**30**	(318)
- Decrease/ (Increase) in trade and other debtors	**695**	(713)
- (Decrease)/ Increase in trade and other creditors	**(245)**	1,667
Net cash inflow from operations	**603**	1,315

14. Commitments

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

	2014/15 Total £'000	2013/14 Total £'000
Payments due within one year	**743**	**902**
Payments due within two to five years	**2,953**	**2,947**
Payments due after more than five years	**3,672**	**4,402**
	7,368	**8,251**

The principal lease for London Wall commenced on the 6 January 2014 for a period of 11 years.

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

	2014/15 £'000	2013/14 £'000
Payments due within one year	**14**	9
Payments due within two to five years	**51**	11
Payments due after more than five years	**2**	-
	67	20

15. Related party transactions

Key Management Compensation

The Directors represent key management personnel for the purposes of the FRC's related party disclosure reporting and their compensation is as disclosed in note 3.

Transactions with related parties

The related party transactions are transacted in the normal course of business and are not material.

16. 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.

4 Directors' Report

Directors

We have included information on the names of the persons, who, at any time during the financial year, were directors of the company at page 35.

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.

Directors' insurance and indemnities

The Company 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 Company or its Directors or Officers.

Information on the following matters can be found in other parts of the Annual Report and Financial Statements

The FRC's financial risk management policy – pages 56

Important events affecting the company since the end of the financial year – pages 10 -14

Likely future developments in the business of the company – pages 16

Activities in the field of research and development – pages 17- 24

Disclosure to the auditor

The Directors, at the date of this report, confirm that, as far as each Director is aware, there is no relevant audit information of which the FRC's auditor is unaware. Each Director has taken all steps that he/she 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.

Fair, balanced and understandable

The Directors consider that this annual report is fair, balanced and understandable and contains the information necessary for the user to assess the performance and prospects of the FRC.

by order of the Board

Anne McArthur

Company Secretary

13 July 2015

Appendix 1

Audit Regulation – Delivering our statutory responsibilities

This Appendix reports on:

(i) the FRC's statutory oversight of the regulation of auditors by recognised professional bodies in 2014/15;

(ii) the FRC's statutory responsibilities as the Independent Supervisor of Auditors General;

(iii) the FRC's other oversight responsibilities

(i) the FRC's statutory oversight of the regulation of auditors by recognised professional bodies in 2014/15.

SUMMARY

1.1 Our conclusions from our work in 2014/15 are positive and much of the regulatory practice we see continues to be of a high standard. Whilst this report deals with some matters which gave us concern these should be seen in the context that all the recognised bodies devote substantial resources to their regulatory responsibilities and are open to making improvements to their processes. We are also pleased to report that we have continued to receive a high level of cooperation from the bodies.

1.2 We vary the focus of our work each year in the light of our risk assessments and the outcome of visits in previous years. In 2014/15 our focus at the Recognised Supervisory Bodies (RSBs) was audit monitoring, the investigation of complaints and the follow up of actions taken by the bodies in response to our previous recommendations. At the Recognised Qualifying Bodies (RQBs) our focus was to follow up previous recommendations and the areas we reviewed at each RQB differed. Accordingly we may not identify all errors and weaknesses in each body's systems and procedures for audit regulation.

1.3 Against this background, our principal conclusions are:

- Staff at the bodies carry out audit monitoring competently, and in compliance with each body's regulations and procedures. However, we consider that there is room to improve further firms' responses and action plans following a visit.
- In our view the bodies continue to find unsatisfactory audit work at too many firms during audit monitoring visits and award an unsatisfactory grading to these firms. At our request each of the bodies has taken a number of actions to improve audit quality within their firms as part of a three year plan starting in 2010 and we welcome these actions. However it is not yet possible to see a broad consistent improvement across the bodies. Some areas of weakness are repeated from year to year and we therefore expect each body to continue with measures to improve the quality of audit work within its regulated firms, refining its approach in light of past experience of what measures have proved to be more effective.
- The Association of Chartered Certified Accountants (ACCA) has fulfilled undertakings to commission an external review of its processes and practices for the award of the PCAQ and to prepare an action plan for the implementation of the recommendations in the review report. However we will not be able to confirm the effectiveness of the measures taken by ACCA until we carry out our own further review in 2015/16.
- Our review of the way in which the bodies carry out their investigation of complaints found improved practice in relation to the handling of complaints and the treatment of both complainants and members of RSBs. The bodies appear much more aware than previously of the need to avoid lengthy delays and of the benefits of good systems to manage cases and workloads.
- Overall the bodies have responded positively to recommendations made in our previous reports. However, some recommendations involve change over the longer term, or have prompted bodies to carry out their own more extensive review of their own processes. It often takes some time before the recommendations of such a review are known. That said, there are examples where progress has been slower than we expected such as improving the recording and monitoring of practical training of students.

INTRODUCTION: MONITORING OF RECOGNISED SUPERVISORY BODIES AND RECOGNISED QUALIFYING BODIES

1.4 Section 1252(10) of, and paragraph 10(3) of Schedule 13 to, the Companies Act 2006 (the Act), requires the FRC to report once in each calendar year to the Secretary of State on the discharge of the powers and responsibilities delegated to the FRC under sections 1252 and 1253 of the Companies Act 2006. In essence these responsibilities are to oversee the regulation of statutory auditors by Recognised Supervisory Bodies (RSBs) and the award of the statutory audit qualification by Recognised Qualifying Bodies (RQBs).

1.5 The FRC has the following graduated range of enforcement powers:

- To direct an RSB or RQB to take specific steps to meet its statutory obligations.
- To seek a High Court order requiring the RQB or RSB to take specific steps to secure compliance with a statutory obligation.
- To impose a financial penalty on an RSB or RQB where it has not met a requirement or obligation on it.
- To revoke the recognition of the RSB or RQB, following due process, where it appears to us that a body has failed to meet an obligation under the Act.

1.6 These powers enable us to address both serious and lesser failures by the recognised bodies and we consider that knowledge of the existence of these powers in itself further encourages timely responses by RSBs and RQBs to our recommendations.

1.7 Audit firms that wish to be appointed as a statutory auditor in the UK must be registered with, and supervised by, a Recognised Supervisory Body (RSB). Individuals responsible for audit at registered firms must hold an audit qualification from a Recognised Qualifying Body (RQB).

1.8 The following are both RSBs and RQBs:

- Association of Chartered Certified Accountants (ACCA)
- Institute of Chartered Accountants in England and Wales (ICAEW)
- Chartered Accountants Ireland (CAI)[1]
- Institute of Chartered Accountants of Scotland (ICAS)

1.9[2] In addition :

- Association of Authorised Public Accountants (AAPA) is an RSB[3]
- Association of International Accountants (AIA) is an RQB

1.10 We exercised oversight primarily by:

- Documenting and understanding how each body meets all the statutory requirements for continued recognition, and making recommendations;
- Reviewing and testing the way in which each body's regulatory systems operate in practice, and making recommendations;
- Evaluating the effectiveness of specific aspects of the regulatory system across all the bodies;
- Keeping in regular contact with each body in order to discuss current issues and trends and future developments, for example proposed changes to a body's bye-laws or rules.

1.11 We send our findings from our monitoring visits to each body for comment. Once the body has agreed the factual accuracy of the findings we prepare a private report to the body which may include recommendations. We require the bodies to send us their response to our recommendations including the actions they will take. At subsequent visits we review the progress made by the bodies in responding to our previous recommendations and close any recommendations where we consider that the body's actions have now resolved the issue that we raised.

2014/15 OVERSIGHT AND MONITORING

1.12 We carried out annual monitoring visits to each RSB in 2014/15. The objective of these visits is to test how the RSBs have applied regulatory requirements in practice in one or more specific areas. Most such visits consist of five days' fieldwork at the recognised body involving two staff members. During our visits we also reviewed the bodies' responses to recommendations made in prior years and carried out testing to confirm that the changes that had been made by the bodies were effective in addressing the issues we had raised in our previous reports.

1.13 Our visits to the RQBs lasted two to three days when we followed up the actions taken in response to the recommendations raised in our previous reports. We also carried out a monitoring visit in 2015 to the AIA. The number of students studying for AIA's RPQ remains small but AIA must nevertheless continue to meet in full the requirements for a RQB. Our visit was to ensure that this is the case.

1.14 We also reviewed and approved 23 reports in 2014/15 of inspections of smaller auditors of public interest entities undertaken by the RSBs. This was in support of our responsibilities to approve the inspection methodologies and the assignment of inspectors to undertake this work; and review the RSB's inspection reports on each firm.

1.15 We need good information to carry out this role. Each RSB and RQB provides an annual regulatory report which includes statistical information on their regulatory activities during the previous year. Each body has also provided us since 2012 with an annual Regulatory Plan, covering both RQB and RSB requirements.

1.16 In addition:

- We held meetings with each body to understand their key risks and future plans, as well as to discuss the findings and recommendations arising from our monitoring work;

1 The Chartered Accountants Regulatory Board (CARB) carries out all the functions of the CAI as an RSB, in accordance with the CAI Bye-laws.

2 The Chartered Institute of Public Finance and Accountancy (CIPFA) was recognised as an RQB in 2005, subject to conditions, but did not at that time develop fully the examinations and arrangements for practical training needed for the award of the statutory auditor qualification. CIPFA's RQB status is therefore in abeyance and we did not carry out a monitoring visit in relation to statutory audit in 2014/15.

3 The AAPA, which was formed in 1978 to represent auditors individually authorised by the then DTI, was recognised as an RSB in 1991 following the Companies Act 1989. It became a subsidiary of the ACCA in 1996, since when its members have been supervised by the ACCA. We therefore reviewed the AAPA's regulatory responsibilities as part of our review of the ACCA. The AAPA had 30 firms registered as statutory auditors, as at 31 December 2014.

and

- Each body is expected to inform us of urgent or emerging significant issues relevant to their role as a RSB/RQB as soon as they arise, with a view to ensuring that our views are taken fully into account before decisions are taken.

1.17 We focused our 2014/15 RSB visits on the following areas:

- The processes and practice in respect of audit monitoring. Each body has a team of inspectors who carry out monitoring visits to their audit registered firms. The overall purpose of the visits is to ensure that audits comply with professional standards and meet the requirements of the Audit Regulations. Visits may also provide assistance to firms by assessing the effectiveness of remedial actions where necessary. Each registered audit firm must be inspected at least once every six years. Firms with listed clients or clients falling within the scope of the FRC's Audit Quality Review Team (AQRT) are subject to visits every three years. We reviewed a sample of files for visits closed in 2014. The sample selection focused on:
    - Firms where the inspection is delegated to the RSB from the AQRT; and
    - Firms whose audit monitoring history is poor i.e. more than one audit monitoring visit has had a poor or unsatisfactory outcome.
- The processes and practice in respect of complaints, in particular the handling of complaints closed by the body's Investigation Committee or Complaints Committee. We reviewed the files and case papers for a sample of such complaints cases that were closed during 2014.
- The progress made by the bodies in implementing our recommendations made in prior years.

We report on this work at paragraphs 1.18 – 1.26 below

1.18 Based on our risk assessments our monitoring visits to the RQBs were restricted to following up prior year recommendations. We also continued some work on a thematic review across all the RQBs focusing on the practical training of statutory auditors. This work is not yet complete. We report on our follow up work at paragraphs 1.27-1.34 and progress on the thematic review at paragraphs 1.35-1.37.

RESULTS OF 2014/15 RSB MONITORING – MAIN POINTS

1.19 Where appropriate we refer in this report to the individual bodies to which significant findings and recommendations apply. However, we invite all the bodies to consider the relevance of our findings to their situation. We also look carefully at the manner and speed with which individual bodies have responded to our previous recommendations.

1.20 All the bodies devote substantial resources to their regulatory responsibilities. We continue to see much regulatory practice of a high standard and in most cases our recommendations are aimed at encouraging the bodies to adopt best practice or to raise standards rather than at correcting major failings. As we have now been monitoring the statutory audit regulation for some eleven years, we are able to see whether each individual body has sustained the improvements it has made and to focus on those areas where we have made repeated recommendations over several years. In general most of the areas where improvements are quick or easy to make have been addressed by the bodies some time ago although changes of staff or other circumstances mean that the bodies may sometimes let standards slip. In other areas such as audit monitoring or complaints handling the changes required are more difficult to specify and implement and will take longer to achieve.

1.21 The main points, from our 2014/15 RSB monitoring work in relation to each body are as follows:

ICAEW

- We found that a small number of registered audit firms had not been visited within six years. For some years ICAEW has interpreted the cyclical inspection timescale requirements of the Companies Act in such a way that there were a small number of firms where the period between visits was a few months longer than six years. ICAEW has agreed to amend its procedures to take account of the month as well as the year of the previous monitoring visit.
- We had no major concerns about how the specific complaints we reviewed had been handled by ICAEW. However there continue to be delays in the handling of some complaints and performance against KPIs deteriorated in 2014. ICAEW has taken action to restructure the department, recruit new staff and change its procedures. We have yet to see the impact of these changes.
- We found improvements in the processes for the handling of RI applications including in the assessment of information from applicants about their recent experience of audit work and in the documentation of the basis on which decisions to grant RI status have been reached.

ACCA

- We did not review any further applications for a practising certificate with audit (PCAQ) in 2014/15 as this area was subject to an external review ACCA's processes and procedures. The review report included recommendations which ACCA has undertaken to implement by the end of 2015. We discussed the report and the recommendations with ACCA. It will take some time for ACCA to implement the recommendations in full. Accordingly we have postponed any further review of PCAQ applications until later in 2015.

- We welcome the successful implementation of the new case management system and of a centralised database which working together provide ACCA with an electronic audit trail and an enhanced reporting facility. We were pleased to find that ACCA is now exceeding its target for completion of investigations within six months. However we will wish to review this area again in the future to ensure that the progress made continues.

- We found that ACCA had not carried out audit monitoring visits to a small number of registered audit firms at least once every six years as required by the Companies Act. Most of these firms had declared that they no longer had any audit clients.

- We have some concerns about the action plans produced by firms in response too adverse visit outcomes. In our view some of the action plans from firms which ACCA had reviewed were insufficiently specific as regards the actions to be taken and the timescales. In addition ACCA changed its policy during the year in relation to imposing hot file reviews where there is an adverse visit outcome. There was a delay in explaining this change to firms and as a result a delay in requiring such firms to produce appropriate action plans and in closing the visits.

- We discussed the actions taken by ACCA intended to identify what measures are most effective in bringing about substantial improvement to the quality of these firms' audit work, in particular the completion of action plans following a monitoring visit.

ICAS

- We were pleased to see the actions taken by ICAS in respect of RI applications and RI application forms and the resulting improvements in the assessment of applicants. This has enabled us to close a number of recommendations made in previous years;

- In respect of the complaints cases considered by the Investigations Committee that we reviewed in 2014 we are satisfied that they are being carefully investigated and closed in a timely manner. We consider it important that the Investigation Department continues to improve its document control processes and we are pleased to see the action taken to date.

CAI

- The Chartered Accountants Regulatory Board (CARB) is the regulatory arm of Chartered Accountants Ireland. Since achieving its objective in early 2014 of visiting all UK registered firms within a six year period. CARB's focus has been on reviewing Irish registered firms. There is a very full work load of visits in order to meet the six year cycle for Irish firms. CARB continues to monitor and manage its resources carefully. The appointment of a CARB inspector as a second senior reviewer has helped ensure that visit reports are completed within the require timescales.

- We carried out our review of audit monitoring with the assistance of an inspector from FRC's AQRT. This allowed a helpful comparison between the nature of the audit monitoring carried out by the RSBs and by the AQRT. CARB's processes require that all visit monitoring work is subject to review by a senior reviewer. The extent of a review, over and above a minimum mandated level set out in CARB's procedures, is determined by the senior reviewer in the light of the seriousness of the issues identified and the firm's response.

- We raised only minor points about the handling of the complaints we reviewed. As we mentioned last year the case management system and many other systems within CARB and CAI are in the process of being replaced as part of a major IT project. We understand that the changes within CARB will be in the final phase of this project and will not therefore be completed until 2016. We consider it most important that this project is successfully implemented, as CAI has based its responses to a number of our recommendations in recent years on the expectation that the issues raised will be properly addressed by its new IT systems.

Other Issues

1.22 We report below on other regulatory issues that relate across all the RSBs:

Audit quality

1.23 In 2010/11 we required each body to develop a three-year action plan for raising audit quality at the smaller audit firms, designed to identify the issues underlying the results of monitoring, and to set out the steps they would take to address them. We will hold a meeting of all RSBs in 2015 to share and discuss the outcomes of the three year plans and what further action is required, if any.

Joint Audit Register

1.24 The Joint Audit Register (JAR) is a public record of registered audit firms and individuals eligible to sign audit reports on behalf of their firm. The JAR is maintained by ICAS on behalf of all the RSBs. and is updated on a weekly basis from information provided by the RSBs. Last year we found a small number of cases where individuals within our samples of RI applications had not been correctly included on the JAR. We did not find any further such cases in 2014 and we are satisfied that the measures taken by each of the RSBs to ensure that the JAR is updated promptly and to reconcile their own database to the JAR have been effective.

Complaints

1.25 Schedule 10 of the Companies Act 2006 sets out the requirements all RSBs must meet relating to complaints and discipline, including:

- The RSB must have effective arrangements for the investigation of complaints against (a) persons who are eligible under its rules for appointment as a statutory auditor; and (b) the RSB in respect of matters arising out of its functions as a supervisory body.

1.26 As part of its non-statutory oversight role the FRC considers complaints about the way in which the six 'chartered' accountancy bodies have handled individual complaints about their members. During the year we conducted a small number of reviews of the handling of particular complaints by professional bodies. These reviews did not indicate any systemic issues with the complaints process at any of the bodies about which we received complaints. However we did identify one case where the body had failed to consider all aspects of the complaint in its initial review. The body subsequently agreed to reconsider the complaint in the light of our findings. Based on our reviews, we also made some suggestions for changes to bodies' processes.

1.27 More generally, we recognise that there are significant differences between the professional bodies' approach to complaints and discipline and that adopted by the FRC's Professional Discipline function in respect of cases which raise important issues affecting the public interest in the UK. In many respects these differences are appropriate given the scale and complexity of the cases dealt with by the bodies and the FRC respectively. Nevertheless, there are inevitably cases that fall just outside the public interest test for the FRC Disciplinary Scheme. During 2014/15 we have continued to hold regular meetings with the ICAEW (which regulates most of the largest audit firms) to discuss how best to handle those cases which come close to the threshold for referral to the FRC.

MAIN ISSUES IDENTIFIED AT THE RECOGNISED QUALIFYING BODIES (RQBS)

1.28 Our monitoring visits to the RQBs in 2014/15 were restricted to following up prior year recommendations. We report on that work in this section.

Prior year recommendations: exemptions or credit for prior learning

1.29 In 2014 we again reviewed progress in implementing our recommendations on the award of credit for prior learning, more commonly known as exemptions, at the ACCA. Our sample was students granted five or more exemptions since September 2013. We were disappointed to find evidence that a small proportion of the more complex exemption applications continue to be processed incorrectly.

1.30 ACCA has built a considerable number of checks into its processes for granting exemptions and mean error rates identified by ACCA as a result of these checking processes have improved in 2014 compared with 2013. However we will wish to see ACCA sustain this level of improvement and go further. We consider this to be an area of high priority for a further review in 2015.

1.31 We also reviewed the processing of a sample of applications for credit for prior learning at ICAEW. Whilst we were satisfied that these had been processed correctly, there were some items in our sample where the basis for granting some or all of the credits was inadequately documented and evidence of prior qualifications was lacking.

Prior year recommendations: practical training

1.32 We reviewed a sample of practical training records at ICAEW in order to test progress in implementing its new on-line training record system for students. This enabled us to see how students and firms are using the system.

1.33 The outcome of our review was mixed and it is still too early to reach conclusions. Some students and firms are recording good quality information on the system. In other cases the quality of information was poor and firms had not carried out six-monthly reviews of their students' practical training. We welcome ICAEW's decision to increase the resources available to monitor the new system and approved training offices.

1.34 In 2012/13 we made a number of recommendations directed at improving the way in which audit experience is recorded in CAI's 'CA Diary' system. CAI plans to make improvements to the CA Diary system as part of its project to replace its IT systems. We have emphasised that we attach considerable importance to the successful implementation of this project and that regulatory requirements must be considered at the design stage.

1.35 We discussed some aspects of the design specification of this part of the IT system with CAI in February 2015. However it will be some time before the project is completed and we have asked that we be kept informed of progress.

PROJECT ON PRACTICAL TRAINING OF AUDITORS

1.36 We reported on this project in our 2013/14 report. We are drafting a project report but have made less progress than we planned and need to accelerate progress with the project in 2015. Despite this we continue to believe that the practical training of auditors is an important subject and a key element of our RQB monitoring.

1.37 We intend to update our draft project report for recent developments in this area such the revised IES8 and the conclusions of the projects commissioned jointly by the FRC and ICAS which have recently been completed.

1.38 Whilst we have not yet reached final conclusions, nor discussed possible actions with the bodies, we expect as a result of this work to set out what we consider to be best practice in this area, and, if we conclude that the current interpretations of the statutory requirements are no longer adequate, we will consider with the bodies what changes to the requirements should be made.

(ii) Report of the Independent Supervisor of Auditors General

1. INTRODUCTION

1.1 The Statutory Auditors (Amendment of Companies Act 2006 and Delegation of Functions etc.) Order 2012 names 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 Companies Act 2006 (2006 Act).

1.2 Section 1228 of the 2006 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.

1.3 The Comptroller and Auditor General (C&AG) and the other Auditors General are eligible for appointment as the statutory auditors of companies under the 2006 Act, subject to meeting certain conditions.

1.4 One of those conditions is that an Auditor General is subject to oversight and monitoring by an 'Independent Supervisor' in respect of statutory audit work. To date only the C&AG has entered into the necessary arrangements with the FRC and undertakes statutory audits under the 2006 Act. The year to 31 March 2014 was the sixth year in respect of which staff at the National Audit Office (NAO) undertook statutory audit work, auditing the accounts of 24 companies. This is a minor part of the NAO's work but enables the NAO to undertake the statutory audit of 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 other work of the C&AG.

2. SUPERVISION ARRANGEMENTS

2.1 Section 1229 of the 2006 Act requires the Independent Supervisor to establish supervision arrangements with any Auditor General who wishes to undertake statutory audit work, for:

- Determining the ethical and technical standards to be applied by an Auditor General;
- Monitoring the performance of statutory 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 statutory audit by an Auditor General.

2.2 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 statutory audit work by the FRC's Audit Quality Review (AQR) team, on behalf of the Independent Supervisor.

3. REPORTING REQUIREMENTS

3.1 We report below in accordance with the requirements of Part 4 Appointment of the Independent Supervisor, Article 19 (a) to (e), Article 20 and Article 21 of SI 2012/1741 Statutory Auditors (Amendments of Companies Act 2006 and Delegation of Functions etc.) Order 2012 which came into force on 2 July 2012.

(a) Discharge of Supervision Function

3.2 The supervision arrangements require that the C&AG and relevant NAO staff follow technical and ethical standards prescribed by the FRC when conducting statutory audits and sets out the investigation and disciplinary procedures that would apply were there a need to discipline the C&AG in his capacity as a statutory auditor. The relevant standards are those set by the FRC for auditors generally and compliance with these is reviewed periodically.

3.3 We meet periodically with 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.

(b) Compliance by Auditors General with duties under 2006 Act

As noted above, to date only the C&AG has undertaken statutory audits, all of which have been of companies within the public sector.

The AQR inspection in 2014/15 of the C&AG's statutory audit work comprised:

- Reviewing the processes and procedures supporting audit quality that applied to these audits; and
- Reviewing the performance of 2 of the 24 statutory audits carried out by NAO staff in respect of financial periods ending on 31 March 2014.

3.4 Progress has been made in addressing the prior year inspection findings. There are, however, areas where further action is required.

3.5 The audits that we reviewed this year were larger and more complex than those in previous inspections and the issues we identified were of more significance than in the prior year.

3.6 On the basis of the findings of the AQR, and subject to the NAO's action plan to deal with those findings, in our view the NAO has policies and procedures in place that are generally appropriate to the conduct of its Companies Act statutory audits.

3.7 We found no evidence that any Auditor General was in breach of duties under the 2006 Act.

(c) Notification by Auditors General under Section 1232 of the 2006 Act

No Auditor General was required to notify the Independent Supervisor of any other information under Section 1232 of the 2006 Act.

(d) Independent Supervisor's Enforcement Activity

We issued no enforcement notices and made no applications for compliance orders in 2012.

(e) Account of Activities relating to the Freedom of Information Act

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

4. REGULATION OF THIRD COUNTRY AUDITORS

4.1 The European Union sets specific requirements for the regulation of the auditors ('third country auditors' or TCAs) of companies from outside the EU that issue securities traded on EU regulated markets. The FRC is responsible for applying these requirements, including monitoring the quality of a TCA's audit work in some circumstances where the firm is not separately subject to equivalent external monitoring. Regulation of TCAs is important because there are some 211 issuers from 45 countries outside the EU whose securities are traded on a UK regulated market.

4.2 The legal requirements for an inspection of a TCA firm by the FRC arises from the Statutory Audit Directive (2006/43/EC) ('SAD') which was adopted by the European Union in May 2006 and transposed into UK Company Law in June 2008. The SAD included specific provisions on the regulation of TCA. In particular, the Directive and the UK implementing legislation require the FRC to subject registered TCAs to its systems of oversight and quality assurance reviews. 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.

4.3 Carrying out inspections of audit firms widely scattered across the world and with typically only one or two relevant audit clients poses legal and practical challenges in some jurisdictions, in particular, local confidentiality laws can hinder access to audit working papers. We endeavour to overcome these challenges.

4.4 Our monitoring focuses on those UK market-traded companies considered to be of significance for UK investors. In the year to 31 March 2015, our second year of inspections, we completed inspections of selected aspects of four audits at five TCAs; two in Lebanon, and one in each of Oman, Papua New Guinea and Barbados. One of the audits reviewed was a joint audit. All four of the audits were categorised as 'limited improvements required'. In the prior year we inspected three audits of which one was categorised as 'limited improvements required' and two as 'improvements required'. (The gradings used by the inspection team are explained in the attached annex). A report on this work is included within our annual Audit Quality Inspections Report which is on the website at **https://frc.org.uk/Our-Work/Conduct/Audit-Quality-Review/Audit-Quality-Review-annual-reports.aspx**

5. LOCAL AUDIT AND ACCOUNTABILITY ACT 2014

5.1 The Local Audit and Accountability Act ("LAAA) abolished the Audit Commission on 31 March 2015 and brought into effect a new transitional body, the Public Sector Audit Appointments Company (PSAA). The PSAA will manage local audit contracts until December 2017 when the transitional regime will end. The new arrangements for the regulation in England of the auditors of the accounts of local authorities and some other public bodies are being implemented progressively. We expect that the first audits to be inspected by the FRC under the new structure will be in relation to accounts for the financial year ending 31 March 2017.

5.2 The LAAA delegated three specific responsibilities to the FRC; to issue guidance on the recognition of individuals as key audit partners; to issue regulations for the keeping of the register of Local Auditors; and to issue regulations for local audit firms on the requirement to publish transparency reports. Following approval by the Board these were published in May 2015.

5.3 The FRC approved the Chartered Institute of Public Finance and Accountancy (CIPFA) as a recognised qualifying body for a new local audit qualification in October 2014 following a review of its policies and procedures to ensure these were consistent with the requirements of the LAAA. An application from the ICAEW for recognition as a supervisory body has been received and is currently under review. ICAS has also indicated that it will submit an application for recognition as a supervisory body.

5.4 We continue to work closely with the Department for Communities and Local Government and other interested parties to develop the detailed regulatory arrangements for a smooth transition to the new structure.

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