

Our approach to setting our priorities

The FRC's resources are very modest in relation to the number and complexity of the issues with which we are concerned, and to the scale of the activities which come within our remit. It is, therefore, essential for us to have a basis for prioritising our work; a basis which takes into account our commitment to follow a risk-based and proportionate approach.

We believe that we can most effectively achieve this if we give those with an interest in corporate reporting and governance the opportunity to comment on the judgements we have made in preparing our Plan. We believe that this helps us to:

- explain the rationale for our selection of the activities and projects we have included in the Plan
- highlight those aspects of confidence in corporate reporting and governance which we believe require particular attention
- explain the basis on which we are seeking to influence market participants and other authorities at UK, EU and global level
- obtain helpful feedback from those with an interest in corporate reporting and governance on the judgements we have made in preparing the Plan.

We determine our priorities each year, following public consultation, on the basis of:

- our assessments of the risks to each of the elements in our Strategic Framework
- our response to the risks, including action in areas for which we are directly responsible and in areas where we seek to influence others.

The main elements of the Strategic Framework

Our Strategic Framework, which we have developed in consultation with our stakeholders, is designed to provide a basis for assessing the major risks to confidence in corporate reporting and governance in the UK over the medium term, and help us to select the activities and projects we include in our annual plan and budget.

It is in the nature of our aim and remit that while some of the elements set out in the Strategic Framework are principally the responsibility of the FRC, most depend principally on market participants or other agencies. We see the Strategic Framework as a way of facilitating co-operation among our wide range of stakeholders to promote justified confidence in corporate reporting and governance in the UK.

The Strategic Framework consists of four elements:

- the overall Aim which the FRC promotes – confidence in corporate reporting and governance
- the six Strategic Outcomes which contribute to our Aim
- the Supporting Outcomes which contribute to the six Strategic Outcomes
- the major Components which contribute to the achievement of the Supporting Outcomes.

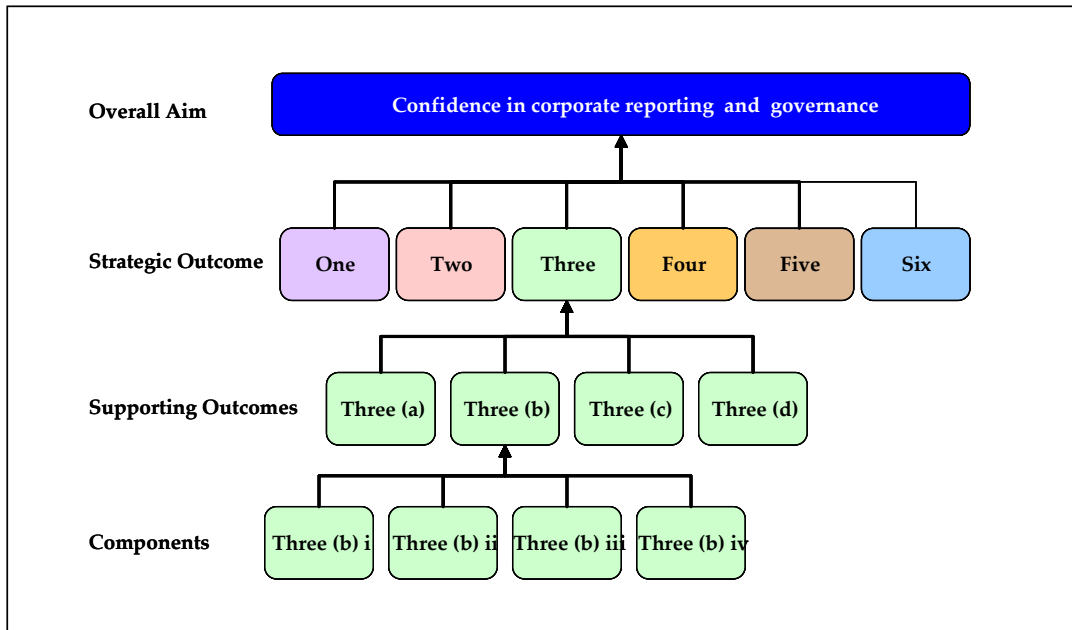
The Supporting Outcomes and major Components are stretching but realistic medium-term aspirations. The Strategic Outcomes are, to a significant degree, mutually supporting in that achievement in relation to one of the outcomes can contribute to achievement in relation to one or more others. It is not essential that all of these elements are found in practice in every case. However, we believe that the greater the extent to which they are found, the greater will be the overall level of confidence in corporate reporting and governance.

Each Strategic Outcome (other than that relating to our own effectiveness) has Supporting Outcomes which have four common themes:

- a. The importance of a *proportionate and effective legislative framework* that provides an appropriate underpinning for the statutory elements of the regulatory framework.
- b. The importance of a *proportionate and effective regulatory framework* that defines high standards in corporate reporting and governance - including standards and guidance on best practice set by the FRC, other regulatory authorities and the professional bodies.
- c. The *central implementation role of practitioners* ie those directly responsible for governance and the preparation of reports, audits, actuarial and other relevant professional advice in meeting the high standards defined. The term “practitioners” includes boards, auditors, members of the accountancy and actuarial professions and the firms to which they belong.
- d. The importance of *effective monitoring* of the quality and integrity of reporting and governance by, for example, institutional shareholders, audit committees, the regulatory authorities (including the FRC) and the professional bodies; and, where appropriate, arrangements for enforcing legislative and regulatory requirements.

Strategic Outcome Six, relating to our own effectiveness, has three Supporting Outcomes: we should meet the principles of good regulation; be recognised in the UK and globally as independent, credible, authoritative and influential; and have adequate resources and management processes and operate efficiently.

Each Supporting Outcome in the Strategic Framework is sub-divided into Components which describe, at a more operational level of detail, those elements which we believe should be in place to underpin the achievement of the Supporting Outcome. The following diagram explains this hierarchical structure:



Note: This illustrates the hierarchy for Strategic Outcome Three. There is a similar hierarchy for all the Strategic Outcomes

Where the FRC or one of our Operating Bodies has the lead responsibility for major Components, this is recorded in the Strategic Framework.

The Strategic Framework is supported by a number of other publications, including statements, standards, guidance and discussion papers published by the FRC – and where appropriate the legislative framework and standards and guidance provided by other authorities. These are available on our website at www.frc.org and contain more in-depth consideration of the Outcomes and Components than is possible in the Framework itself.

In relation to each element defined in the Strategic Framework we make an assessment of the risks under three scenarios:

- **Present:** Our assessment of the extent to which the outcome is achieved at present.
- **Downside:** Our assessment of the extent to which the outcome may not be achieved in two/three years, or sooner if we believe circumstances could change materially, because those responsible do not take effective action to promote the achievement of the outcome or do not adequately mitigate the risks that are likely to arise. This is not intended to represent a “worst case” scenario but rather a realistic assessment of the position should the plausible risks materialise.

- **Upside:** Our assessment of the extent to which the outcome is likely to be achieved in two/three years, or sooner if we believe circumstances could change materially, if those responsible take effective action to promote its achievement and adequately mitigate the risks that are most likely to arise. This is not intended to represent a “best case” scenario but rather an assessment of the realistic prospects – and takes into account our belief that no system of regulation can ever eliminate the possibility of failures.

We believe that it is the responsibility of the FRC and others with responsibility for key aspects of corporate reporting and governance to take appropriate action to contribute to progress towards the **Upside** scenario and avoid the **Downside** scenario.

In particular, we believe that the differences between the **Present**, **Downside** and **Upside** scenarios are primarily attributable to the level and effectiveness of action taken by those responsible for the achievement of the outcomes in the Strategic Framework (including, but not limited to, the FRC) to address the risks. The differences will also be attributable, in part, to the extent to which the FRC can, where appropriate, successfully influence market participants and other agencies to take action to address these risks.

In making our assessments, we draw on a range of evidence, primarily:

- the evidence we have obtained from our monitoring and enforcement activities
- responses to consultations we have undertaken on specific issues
- surveys and research conducted independently by other organisations
- surveys commissioned by the FRC.

We keep our assessments under review in response to external developments and as further evidence becomes available.

The assessments include our judgements about the severity of the risks which might materialise in relation to each outcome and the likelihood that these risks might materialise. On the basis of our assessments, we identify what we believe to be the major risks to confidence in corporate reporting and governance over the medium term. In some cases, we may conclude that the residual risks are such that even in the upside scenarios there are *significant concerns* or that the outcome is *unlikely to be achieved*.

For each scenario we apply our regulatory professional judgement to the available evidence to conclude whether:

- an outcome is *largely achieved* or achieved to a considerable degree
- there are *significant concerns* in relation to the achievement of an outcome
- an outcome is *unlikely to be achieved* or unlikely to be achieved to a considerable degree.

This approach is summarised in the diagram overleaf.

We base our assessments at the levels of the Supporting Outcomes, Strategic Outcomes and our overall Aim on our detailed assessments at Component level. We make these assessments using our regulatory professional judgement rather than using a set formula. In some cases an assessment that a Component is not achieved may, in our judgement, seriously compromise the achievement of the relevant Supporting Outcome; in other cases, we may judge that it will not.

We publish a draft plan, which includes our assessments of the risks and proposed responses; and publish a revised plan, if appropriate, in the light of the input we receive from our stakeholders.

Scenarios

Present - To what extent is the outcome being achieved now?

Based on the evidence available to FRC.

Downside - To what extent is the outcome likely to be achieved if the plausible risks materialise?

Not a "worst case" scenario but a realistic assessment of what could go wrong in two/three years, or sooner if we believe circumstances could change materially.

Assumes those responsible do not take effective action to promote the achievement of the outcome or do not adequately mitigate the risks that are likely to arise.

Upside - To what extent is the outcome likely to be achieved?

Not a "best case" scenario but a realistic assessment of the prospects in two/three years, or sooner if we believe circumstance could change materially. Assumes those responsible for the outcome endeavour to take effective action to promote its achievement and adequately mitigate the risks that are most likely to arise.

Assessments

**Largely
achieved**

**Significant
concerns**

**Unlikely to be
achieved**