

31 March 2008

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The Planning Manager
Financial Reporting Council
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Dear Sir

Financial Reporting Council – draft plan & budget 2008/09

IMA represents the UK-based investment management industry. Our members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes. They are responsible for the management of nearly £3 trillion of funds (based in the UK, Europe and elsewhere), including authorised investment funds, institutional funds (e.g. pensions and life funds), private client accounts and a wide range of pooled investment vehicles. In particular, our members represent 99% of funds under management in UK-authorised investment funds (i.e. unit trusts and open-ended investment companies).

In managing assets for both retail and institutional investors, IMA members are major investors in companies whose securities are traded on regulated markets. Therefore, we have an interest in the Financial Reporting Council (FRC) from the perspective of our members as institutional investors.

IMA welcomes the FRC consulting them on its draft plan and budget for 2008/09 and prioritising its activities to address the risks to confidence in corporate reporting and governance. In particular, the current credit market turbulence poses one of the greatest risks to that confidence for years and we welcomed the FRC's Press Statement on the crisis last December and the further statement on audit issues by the Auditing Practices Board in January. The current market continues to be uncertain and we consider it important that the FRC is flexible in its planning and remains alert to developments that could necessitate changes to its priorities and planned activities.

Our observations on the risks and actions for each of the strategic outcomes in the plan are set out below.

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Strategic outcome one – corporate governance.

We welcome the fact that the FRC does not propose to undertake any major activities in relation to corporate governance. Recently there have been many changes to corporate reports and governance and we consider that these changes should be given the opportunity to bed down before further amendments are considered in that both companies and investors would appreciate a period of stability in corporate reporting.

Furthermore, our members have widespread recognition of the importance of shareholder engagement and fulfilling their responsibilities as owners and we do not necessarily believe that “there is a risk that shareholders may adopt a “box ticking” approach to assessing governance statements¹” as stated in the Plan. Indeed the fact that companies may perceive this to be the case could drive such an approach through:

- a reticence to “explain” non-compliance with the Code and compliance when this may not be in their best interests;
- increasingly standardising disclosures and explanations which are of limited use; and
- not providing adequate explanations for non-compliance and some consider any explanation will suffice.

Strategic outcome two – corporate reporting.

We welcome the FRC recently undertaking a consultation on the complexity and relevance of current reporting requirements. There have been numerous changes of late, particularly with the introduction of IFRS, and not all of these have resulted in enhanced transparency and consistency in annual reports. We would appreciate the opportunity of working with the FRC on this to help ensure any simplification and rationalisation still meets the needs of shareholders.

We also welcome the FRC seeking to influence the IASB and support its objective of developing a single set of high quality global accounting standards. While the acceptance of IFRS by the SEC was an important step forward in this, the IASB’s emphasis on convergence with US GAAP has caused some concern and we believe there is a risk of US domination of the process, given its strong representation on the Trustees and the IASB. For example, we were concerned that the IASB’s discussion paper on the conceptual framework followed the US model and focused solely on accounts being decision useful and did not make stewardship a separate objective and that in IFRS 8 a US standard was in effect adopted unilaterally which requires that the segments reported are based on “internal reports that are regularly reviewed by the entity’s chief operating decision”, without defining who that person is.

As regards the role of the FRRP in monitoring and reviewing accounts, we note that it anticipates “informed referrals from investors²”. In this respect, investors overriding objective is to ensure that the companies in which they invest deliver satisfactory returns for their clients, the beneficial owners. We would, therefore,

¹ Page 12

² Page 29

caution against too much reliance on this as investors may be reticent to refer accounts when such referrals could ultimately affect shareholder value and would like the reference deleted from the Plan.

Strategic outcome three – auditing

IMA supports the FRC's project on Audit Choice and most of the FRC Market Participants Group's Report's recommendations, with the exception of the audit committee's report to be put to a shareholder vote, in that we:

- do not believe that such a vote would necessarily improve the quality of reporting by audit committees - indeed it could potentially encourage more boilerplate reporting which would be a retrograde step;
- question whether, as was put forward in the paper, such a measure would increase engagement on auditor reappointment in that investors already engage with companies and do not necessarily have to vote on a matter before they do so; and
- doubt if a vote would help improve choice in the audit market – the main objective of the paper.

As regards the project to implement the Statutory Audit Directive, the FSA's consultation on implementation proposes the FRRP will be responsible for reviewing compliance with the requirements of the Directive³. We believe that whilst the FRRP's monitoring will enable it to assess whether the statements meet the requirements of the Directive, we do not consider that it will necessarily be able to assess the accuracy of those statements and whether an audit committee exists which satisfies the compositional requirements and if not, whether enforcement action should be taken. The FRRP may need to consider these aspects.

Lastly, there is no mention in the Plan of the FRC's project to provide guidance on auditor liability limitation agreements which was recently consulted on.

Strategic outcome four – actuarial practice

We welcome the FRC's projects on finalising the conceptual framework for and updating actuarial standards which we will continue to monitor.

Budget and the consultation in general

The FRC's proposed budget shows an increase of 9% in its core operating costs in relation to corporate governance, reporting and accounting to £11.9m compared to £10.9m in 2007/08. This is mainly due to a planned increase in headcount from 64 – 68. Furthermore, budgeted actuarial operating costs increase by 22% to £2.2m as compared to £1.8m reflecting an increase in two staff. We note that the Government has recently announced that it plans to cease to contribute to the funding of the FRC with effect from April 2009. In view of this and the budgeted cost increases in 2008/09, it would be helpful if the FRC included budget forecasts for the next two years so that future cost trends and expectations could be considered with the current budget proposals.

³ CP07/24, Paragraphs 2.12 to 2.14

Lastly, the current consultation includes two documents, the Draft Plan and Budget itself and the secondary Supplemental Information document. This has made the consultation quite cumbersome and there is much repetition between the two documents. In the interests of clarity, we suggest that the final Plan and Budget for 2008/09 is issued as one document which is considerably shorter and removes significant areas of duplication.

Please do contact me if you would like clarification on any of the points in this letter or the attached, or if you would like to discuss any issues further.

Yours faithfully



Liz Murrall, Senior Adviser – Corporate Governance