

CBI response to Financial Reporting Council

Consultation on Draft Work Plan, Budget and Levies 2011/12

March 2011

Introduction and Summary

1. The CBI is pleased to respond to the FRC consultation on its draft Work Plan, Budget Levy proposals for 2011/12.

Regulatory Powers

2. The CBI would welcome the FRC setting out its “big picture” thinking on its future role and place in the regulatory architecture. This would help to provide greater insight regarding the FRC’s comments about a need for greater powers and responsibilities, referred to both in Section 2 of this consultation and in Chapter 5 of that on the current live consultation on “Effective Company Stewardship”.
3. We are cautious, for example, where the FRC states in the “Effective Company Stewardship” consultation, that it is interested in powers to investigate the governance, accounts and audit and extent of compliance of failed companies. At present we are not clear that this is appropriate, given the existing responsibilities of other bodies, and also because of any consequential increase in the FRC Levy that would fall on business.

Response to financial crisis

4. What is now key for business in response to all the reviews and changes made or planned in response to the financial crisis, including in the UK and EU regulatory architecture, is that there follows a significant period of stability for business whilst these new regulatory structures become established and bed down.
5. Ensuring that the UK is vocal and influential in Brussels is important to deliver a proportionate EU response to the financial crisis and the regulation of business. The FRC has an important role to play in influencing the forthcoming EU Governance Green Paper, especially in promoting the UK principles-based “comply or explain” approach to corporate governance, and any EU reforms to the audit market.

Carbon Reporting in response to climate change

6. An area where we do believe that the FRC has a future role is in developing reporting standards and guidance for carbon reporting in response to climate change. The CBI supports the work going on in Government in providing guidance on the reporting of greenhouse gas emissions in response to the requirements of the Climate Change Act 2008.
7. However, a recent UK Government report has shown that the array of multiple and diverse carbon reporting guidelines are inhibiting the uptake of voluntary carbon reporting, and the present lack of consistency and comparability in how companies report their greenhouse gas emissions means that it is time to develop mandatory carbon reporting requirements in the UK for appropriate businesses.



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8. Accordingly, the CBI supports the development of standardised reporting protocols, and for relevant and appropriate companies operating in the UK mandatory carbon reporting in accordance with such protocols. Such requirements need to reflect a proportionate approach, and carbon reporting mechanisms must be based on a methodology that is internationally recognised.
9. To this end, we believe that the UK can play an important role in providing context to the development of standardised and mandatory carbon reporting, allowing companies to demonstrate their commitment to improving transparency and strengthening investor and consumer confidence.
10. The FRC has a role to play in promoting and developing these initiatives.

Corporate Governance

11. Regarding corporate governance matters, the CBI was generally very satisfied last year with the principal outcomes of the FRC consultations leading to the development and publication of the newly-titled UK “Corporate Governance Code”, and the important first publication of the new “Stewardship Code for institutional investors”. We also welcome the new “Guidance on Board Effectiveness”.
12. The CBI is now considering with CBI members the FRC’s latest consultation on “Effective Company Stewardship”, and we will let you have our formal response by the close of the consultation period. Whilst we hope that we will be able to give broad support in principle to your aims for more detailed and informative audit committee and audit firm reporting, we think that it is important that these proposals should first be tested in practice on a voluntary basis before becoming part of the UK Corporate Governance Code or additional auditing standards.
13. Whilst the largest listed companies may have the structures and resources to operate in accordance with these proposals, this may well not be the case for other listed companies, and smaller listed companies and unlisted companies in particular. It should also be assessed whether the proposals for more detailed audit committee reporting and responsibilities will impact on the willingness of individuals to serve on or to chair the audit committee.
14. We would also be concerned, if the Government or the EU adopted such proposals for mandatory compliance through regulation, before the proposals have been tested in practice, and which we consider are better suited to Governance Codes and not regulation.
15. We respond further below to various aspects of the Draft Plan, Budget and Levy proposals.

Work Plan

Major Outcomes

16. We note that in 2011/12 the FRC plans to focus its work on four major outcomes:
 - Stronger and better-informed engagement between institutional investors and company boards
 - Corporate reporting and auditing that deliver greater value to investors and better serve the public interest
 - A strong UK voice in the EU and international debate on the future regulation of corporate governance, reporting and auditing
 - A more effective UK regulatory framework that adds value for investors and other stakeholders at low incremental cost.

17. The CBI supports these outcomes as a reflection of the underlying objectives that the FRC and its operating bodies should have regard to in the performance and discharge of their functions and responsibilities in a fair and proportionate manner at acceptable cost. We also refer to our comments above in this connection.

Corporate Governance and Corporate Reporting

18. We note the following objectives for corporate governance:

- Monitor the effectiveness of the UK Corporate Governance and Stewardship Code for institutional investors
- Support investors' and other stakeholders' assessments of the effectiveness of boards in discharging their stewardship obligations.
- Seek continuous improvement in the quality of corporate reporting, including better quality reporting of business models, strategies and risk management.
- Greater transparency by audit committees on the way they have discharged their responsibilities, and improved communication between auditors and audit committees.
- More innovation in the audit and financial reporting markets to promote healthy competition and a high quality service.
- Work with the EU and BIS to influence the development and implementation of legislative provisions relating to corporate governance.

19. We support these objectives in principle, subject to our earlier comments.

Women on Boards

20. Following Lord Mervyn Davies' recent Report and recommendations, we are pleased to note that the FRC now plans to consult on changes to the UK Corporate Governance Code.

21. The CBI supports companies reporting on diversity on a "comply or explain" basis. We believe that they should report their progress against internally-set targets appropriate to their current gender diversity position, culture and sector. Where companies fall short of their own target they should report on the action they are taking to address the position. However, we consider that a prescribed target for FTSE 100 directors, as recommended by Lord Davies, would not reflect the different circumstances of individual companies. It should be for companies, not the Government, to set an appropriate target.

Financial Reporting and Auditing

22. We note the following objectives:

- Contribute to the improvement of standards for financial reporting, and auditing, monitoring compliance, and taking enforcement action when appropriate.
- Take a lead role in influencing the development of IFRS and the IASB strategy when convergence with US GAAP projects ends in 2011.
- Seek to ensure continued support in the EU for implementing IFRS as issued by the IASB.
- Implement an agreed approach for UK GAAP and convergence with IFRS – major ASB consultation currently in train for response by 28 March.

- Continue to monitor sustainability information in annual reports and consider publishing guidance on sustainability reporting if appropriate.

23. We support all these objectives in principle.

24. We are currently discussing with CBI members the ASB consultation on the future of UK GAAP, and will respond to this separately. We have responded to the IFRS Foundation Trustees Strategy Review consultation, and we will be pleased to share our response with you. We will also be responding to the Monitoring Board report on the governance of the IFRS Foundation structure.

Regulatory Responsibilities

25. We note the following objectives:

- Enhance the effectiveness and efficiency of the FRC in carrying out its regulatory functions, focusing on the outcomes it is seeking and demonstrating its commitment to the principles of good regulation, including high levels of accountability and transparency.
- Work with Government to ensure that the FRC and its operating bodies have the powers and resources necessary to carry out their responsibilities;
- Following the completion of the Government review of public bodies, any reforms affecting the FRC that the Government introduces should strengthen the FRC's independence and deliver greater transparency in the regulatory functions it undertakes.

26. We note that the Draft Plan and Budget does not take account of any possible reforms or changes in FRC responsibilities. As indicated above, we are keen to learn more about what the FRC has in mind for increasing its powers and responsibilities, referred to both in this consultation and that on Effective Company Stewardship.

27. What is now key for business in response to all the reviews and changes made or planned in response to the financial crisis, including in the UK and EU regulatory architecture, is that there is now a significant period of stability for business whilst these new regulatory structures bed down, and so that the UK also pulls its weight in Brussels in ensuring a proportionate EU response to the financial crisis and the regulation of business. The FRC has an important role to play here in securing a stable regulatory platform.

Proposed Budget 2011/12

28. We note that the FRC estimates its total costs will be £22 million, an increase on current year forecasts of £20.4 million, due to estimated increase in accountancy disciplinary case costs. However, the FRC aims to reduce core operating costs for accounting, auditing and corporate governance by £0.7 million and for actuarial regulation by £0.2 million. We also note that the FRC does not propose to raise any additional funds to increase general reserves. We have commented above on the impacts of any increase in the FRC's powers and responsibilities on FRC funding needs and sources of funding. We are content with these proposals, and have no other specific comments.

Levy Proposals 2011/12

29. We note that the proposals should result in a reduction in the minimum levy threshold, and a 7% reduction on average on the levy paid by individual organisations according to size and status. The anticipated reduction for listed companies is 5.7%, but some individual companies could pay more if their size has grown. We are content with these proposals as currently formulated, and have no other specific comments.