



Financial Reporting Council

Plan & Budget 2011/12



Financial Reporting Council Plan & Budget 2011/12

April 2011

Contents

Section 1: CEO Overview	1
Section 2: Major activities and projects	6
Section 3: Budget 2011/12	8

Section 1 CEO Overview

Outcomes

In 2011/12 we will focus our 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.
- New powers and a new structure for the FRC that reflect the Government's Agenda for Growth and command widespread support from those who rely on the quality of corporate governance and reporting in the UK.

We will contribute to these outcomes during the year by:

- Supporting investors' and other stakeholders' assessments of the effectiveness of boards in discharging their stewardship obligations.
- Seeking continuous improvement in the quality of corporate governance and reporting in the UK.
- Contributing to the establishment and improvement of standards for financial reporting, and setting standards for auditing and actuarial practice and taking into account the needs of SMEs.
- Monitoring compliance with financial reporting and auditing standards, taking action to enforce them when appropriate.
- Overseeing the regulatory activities of the accountancy and actuarial professional bodies.
- Operating independent disciplinary arrangements for public interest cases involving accountants and actuaries.
- Influencing and responding to EU and global initiatives relevant to our objectives in line with our principles-based approach.

- Reforming our powers and structure, with the support of Government and in consultation with our stakeholders, and tightly focusing our limited resources on the areas of greatest risk.

Corporate governance

We believe that good corporate governance is essential to the effective operation of a free market. Good governance improves boards' ability to manage effectively as well as providing accountability to shareholders. The more ingrained good governance becomes in a business community, the less the need for detailed regulation to ensure effective compliance with high standards of behaviour. We emphasise the needs of investors for relevant and clearly communicated information on governance, business models and company performance.

The quality of engagement between investors and companies can help improve long-term returns to shareholders and the efficient exercise of governance responsibilities. Engagement includes pursuing purposeful dialogue on strategy, performance and the management of risk, as well as on issues that are the immediate subject of votes at general meetings.

Supporting investors' and other stakeholders' assessments of the effectiveness of boards in discharging their stewardship obligations.

The FRC's Stewardship Code was published, following extensive consultation, in July 2010. The Code sets out good practice on engagement with investee companies to which the FRC believes institutional investors should aspire. It is intended to enhance the quality of engagement between company boards and investors, and between fund managers and the beneficial owners of companies, as a basis for improving the quality of corporate governance and long-term company performance. The FRC sees the Stewardship Code as complementary to the UK Corporate Governance Code for listed companies, which was revised in June 2010.

The Stewardship Code has attracted support from many major institutional investors, including international investors, and from clients such as pension funds. The FRC will monitor the degree to which the Code is leading to more effective engagement and greater transparency.

Seeking continuous improvement in the quality of corporate governance and reporting in the UK.

We have consulted on ways in which the policy and regulatory infrastructure can be adapted to support the stewardship concept and ensure that it is fit for purpose in the modern global business environment.

The FRC is considering a new vision of corporate reporting where directors' narrative reports, company accounts and audited financial information will each deliver greater value to investors and serve the public interest. This was set out in our document "Effective Company Stewardship." The main proposals were:

- Reforms to the way that companies provide information to ensure it is timely, accessible and useful.
- Better quality reporting of business models, strategies and risk management.
- Improved communication between auditors and audit committees and greater clarity in the responsibilities of auditors across the full range of narrative and financial statements in the annual report.
- Greater transparency by audit committees on the way that they have discharged their responsibilities in relation to the integrity of the annual report and particular aspects of their remit (such as, for example, their oversight of the external audit process and the appointment of external auditors).
- More innovation in the audit and financial reporting markets to promote healthy competition and a high quality of service.

The FRC is now considering responses to this document and will seek to ensure that this and other current initiatives aimed at improving aspects of

corporate reporting (including, for example, sustainability reporting) are properly joined-up from the perspective of users and preparers of accounts.

Contributing to the establishment and improvement of standards for financial reporting, and setting standards for auditing and actuarial practice.

The Accounting Standards Board (ASB) is currently seeking the views of UK stakeholders to assess support for a UK strategy of convergence with international standards, that UK accounting standards reflect market developments, and that the needs of smaller companies are addressed. The future of financial reporting in the UK and the need to balance the needs of preparers and users of accounts will remain a major issue in 2011/12, as a number of our stakeholders recognised in their responses to the Draft Plan.

The Auditing Practices Board (APB) will take forward issues emerging from the Effective Company Stewardship consultation in relation to the future role of audit. It will also follow up on its joint consultation with the Professional Oversight Board (POB) on auditor scepticism.

The FRC welcomed the House of Lords Economic Affairs Committee's report on '*Auditors: market concentration and their role*'. Several of the Committee's recommendations are similar to proposals made by the FRC in its own evidence to the Committee, in particular its emphasis on an increased role for audit committees. We will take the Committee's views fully into account in considering the responses to that consultation.

We will also keep under review the risks associated with concentration in the UK audit market and will pursue the need for an effective contingency plan in the event of the failure of a major firm.

The Board for Actuarial Standards (BAS) completed its suite of technical actuarial standards (TASs) during 2010/11. It has now issued seven TASs, covering a broad range of actuarial work including pensions and insurance, which will come into force during 2011.

The new suite of standards for actuarial practice is the first in the world to have been set on an independent basis by a body which represents the users as well as the providers of actuarial information. During 2011/12 the BAS will promote the standards and start to assess their effectiveness.

Monitoring compliance with financial reporting and auditing standards, taking action to enforce them when appropriate.

The Financial Reporting Review Panel (FRRP) has found continuing improvement in the general quality of financial statements prepared under International Financial Reporting Standards (IFRS). However, the FRRP continues to have some concern about the quality of the reports and accounts of some smaller listed and AIM quoted companies.

A key area of interest for the FRRP in its 2011/12 reviews will be: the extent to which there are clear linkages between narrative reports and the accounts; principal risks and uncertainties; and the descriptions of business models. It will focus on: companies involved in commercial property, insurance, support services and travel.

The Audit Inspection Unit (AIU) focuses on matters where it believes improvements are required to safeguard and enhance audit quality. The actions taken by firms in response to its inspection findings in recent years have contributed to an improvement in the overall quality of audit work in the UK. It is now focusing more on the behavioural changes necessary to deliver and enhance audit quality, such as the need to exercise professional scepticism.

The AIU's inspections in 2011/12 will therefore focus on areas of high subjectivity and professional judgement and the application in practice of the new Clarity International Standards on Auditing (Clarity ISAs) which applied for the first time to December 2010 audits.

Overseeing the regulatory activities of the accountancy and actuarial professional bodies.

The Professional Oversight Board (POB) will continue to monitor the regulatory activities of the accountancy and actuarial professional bodies, in relation to their members, assessing those issues that could adversely affect public confidence in accountants and actuaries and, where appropriate, undertake more detailed research and make recommendations to the professional bodies or recommend the development of new standards. Issues include the progress achieved by the Actuarial Profession in response to our recommendations concerning quality control at actuarial firms.

Operating independent disciplinary arrangements for public interest cases involving accountants and actuaries.

The Accountancy and Actuarial Discipline Board (AADB) case-load has continued to increase and it is likely that a number of cases will continue into 2011/12. Some cases may progress to the disciplinary tribunal stage.

Stakeholders have commented on the importance of balancing the pressures on the AADB to pursue cases against their overall costs and benefits and the time taken to reach a conclusion the FRC will monitor this closely.

Influencing and responding to EU and global initiatives relevant to our objectives in line with our principles-based approach.

The regulatory framework for corporate governance, corporate reporting and auditing in the UK is crucially influenced by decisions taken at EU and international level. We must therefore influence policy-makers and standard setters in the EU and globally, and will work to enhance this aspect of work, particularly in partnership with other institutions.



The EU is currently engaged in a major debate about the appropriate response to the lessons of the financial crisis. The European Commission has published proposals on corporate governance and the future of audit. We have responded to their consultations and are playing an active and on-going role in the debate, including with the European Parliament and other Member States.

The FRC has, together with BIS, formed a consultative European Issues Steering Group to coordinate influencing activities and approaches across the range of UK stakeholders.

Over the last year the work of the International Accounting Standards Board (IASB) and the European Financial Reporting Advisory Group (EFRAG) has increased as the IASB pursues its objective of globally-accepted accounting standards. We support this objective providing quality is maintained and will continue to influence the development of IFRS and its adoption by the EU in the form proposed by the IASB. We also encourage moves to enhance the governance and openness of the IASB, its trustees and Monitoring Boards.

The FRC will also seek to work closely with the European Securities Market Authority (ESMA), the new European authority for securities regulations. In particular, the FRRP will continue to be an active member of the European Enforcement Co-ordination Sessions which will operate under the auspices of the ESMA from 2011.

The continued emergence of independent audit regulators in many countries around the world, together with the continuing dominance of the major global audit networks in the audits of public interest entities, has led to an increased focus on international cooperation amongst audit regulators. Globally, this is through the International Forum of Independent Audit Regulators (IFIAR) and in Europe through the European Group of Audit Oversight Bodies (EAOB) and the European Audit Inspection Group (EAIG). The UK has taken a lead in seeking to develop international cooperation amongst independent audit regulators through IFIAR and has also been at the forefront of developing cooperation within the EU under the Statutory Audit Directive.

We strongly believe that audit quality should be promoted internationally. We will continue to play a leading role in IFIAR, and welcome Paul George's recent appointment as its Chairman.

The FRC will also continue to work directly with other independent audit regulators and through joint inspections, for example, with the US Public Company Accounting Oversight Board (PCAOB).

The APB will continue to take an active role in influencing the work of the International Auditing and Assurance Standards Board (IAASB) and work towards the adoption of International Standards on Auditing (ISAs) in the EU.

We will also contribute to the continuing development of the EU Solvency II project, and will participate in the development of a European approach to actuarial standards, building on our experience as the world's leading independent actuarial standard-setter.

Reforming our powers and structure, with the support of Government and in consultation with our stakeholders, and tightly focusing our limited resources on the areas of greatest risk.

FRC reform

The Government is challenging regulators to do more to reduce the costs of regulation and focus on risks and outcomes rather than processes. Our intention is that, working with Government, the FRC will further develop to ensure that it has the right powers and structure to deliver with full effectiveness its mission of promoting high quality corporate governance and reporting – so contributing to the efficiency of the capital markets in the UK and fostering investment. We will consult fully where appropriate with Government on any proposed changes, including our analysis of their costs and benefits.

Our budget

We need sufficient resources to enable us to deliver our objectives on behalf of our stakeholders – who include investors, business, the professions, employees, insurance policyholders, members of pension schemes, and other interests. This includes the resources necessary to influence a wide range of international developments.

We are acutely aware of the importance of delivering our functions in a manner that represents value for money. Our total budget is higher than the budget for 2010/11 because we estimate that accountancy disciplinary case costs will increase, reflecting the stage that a number of major cases will have reached in 2011/12. However, our focus on cost reduction has enabled us to set a budget for core operating costs for accounting, auditing and corporate governance which is £0.7m lower than the 2010/11 budget of £12.9m.

The net effect of the budget is that we have fully absorbed a £0.7m reduction in government funding and will reduce the amount which accounts preparers will pay, on average, under the preparers levy by a little over 7%. We will announce the finalised levies for 2011/12 in May following the receipt of the necessary data from the Financial Services Authority and the Pensions Regulator.

We believe that the costs associated with our work to reform our powers and structure can be accommodated through a small reduction in our general reserves. We will consult on any proposals that may impose additional costs on our funding groups.

Stephen Haddrill
Chief Executive Officer

Section 2 Major activities and projects

The major activities and projects we will undertake in 2011/12 are as follows:

The FRC Board will:

- Oversee the effectiveness of the FRC and its Operating Bodies in delivering their regulatory functions and ensure that they achieve high levels of accountability and transparency.
- Work with Government to ensure that the FRC has the powers and structure necessary to carry out its responsibilities; and consult on any proposed changes.

Advised by the Committee on Corporate Governance, the FRC Board will:

- Monitor the effectiveness of the UK Corporate Governance Code in promoting good governance practices.
- Monitor the effectiveness of the Stewardship Code for institutional investors in contributing to a significant improvement in the stewardship of UK listed companies.
- Work with the EU and the Department for Business, Innovation and Skills (BIS) to influence the development and implementation of legislative provisions relating to corporate governance.

The Accounting Standards Board will:

- Stimulate improvements to corporate reporting, including narrative reporting, focusing on business model and risk disclosures.
- Take a lead role in influencing the development of IFRS and the IASB strategy when the convergence with US GAAP project ends in 2011.
- Play an active role in EFRAG and European proactive projects, including the development of a disclosure framework.

- Seek to ensure continued support in the EU for implementing IFRS as issued by the IASB.
- Implement an agreed approach for the future of UK Generally Accepted Accounting Practice (UK GAAP).
- Play a leading role in the global group of National Standard Setters.
- Continue to monitor sustainability information in annual reports and consider publishing guidance on sustainability reporting if appropriate.

The Auditing Practices Board will:

- Take forward audit-related issues emerging from the consultation on improvements to the annual reporting, accounting and audit infrastructure; and issues arising from the APB/POB consultation on auditor scepticism.
- Review, together with the IAASB, the impact of the introduction of the Clarity ISAs.
- Complete the review of standards and APB guidance in relation to reports provided to the Financial Services Authority (FSA) on client assets in the financial services sector which commenced in 2010/11, and update and issue appropriate professional standards for work in this area.
- Keep under review, with the POB, issues and conditions that may impact on the work of auditors, and issue updated standards if appropriate.
- Use audit inspection findings in setting standards and related guidance.
- Play a leading role in the IAASB and work effectively with the International Ethical Standards Board for Accountants.

The Board for Actuarial Standards will:

- Maintain a suite of technical actuarial standards and start to assess the effects of TASs in meeting the needs of users of actuarial information, including the governing bodies of insurers and pension schemes.

- Contribute to the continuing development of UK pensions legislation.
- Influence the development of international actuarial standards, including those for Solvency II.
- Work with Government and other regulators to ensure consistency between BAS standards and other regulatory requirements.

The Financial Reporting Review Panel will:

- Review a selection of annual and interim accounts and directors' reports for compliance with the Companies Acts, including applicable accounting standards; and aim to review around 300 sets of accounts in total in 2011/12.
- Respond to matters drawn to its attention as a result of complaints or public comment, and encourage referrals from the investment community, professional advisers and others.
- Influence the development of international enforcement practices.

The Professional Oversight Board will:

- Through its Audit Inspection visits, monitor and report on the quality of audits, based on the reviews of some 100 audits, of which the majority will relate to the largest audit firms, focusing on areas of high subjectivity and professional judgement and the application in practice of the new Clarity ISAs.
- Keep under review the risks associated with concentration in the UK audit market and, if appropriate, make proposals on further action.
- Respond to the outcomes of the House of Lords inquiry into the audit market and the European Commission's green paper on auditing.
- Influence the work of IFIAR and EGAOB to promote effective regulatory oversight of audit firms, including those managed on a regional basis, and taking a leading role in such regulation within Europe.

- Oversee the regulatory processes of the Recognised Supervisory Bodies (RSBs) and Recognised Qualifying Bodies (RQBs) in respect of auditing.
- Ensure that the legislative framework and practical measures for audit regulation in Europe under the Statutory Audit Directive appropriately address the issues relating to third country auditors.
- Participate in the arrangements for the co-ordination of the regulation of audit and the oversight of the auditing profession in the EU.
- Monitor the regulatory activities of the accountancy and actuarial professional bodies.

The Accountancy and Actuarial Discipline Board will:

- Make significant progress on, and where possible finalise, the matters with which it is currently dealing and identify and investigate other matters which meet the criteria for AADB investigations.
- Explore measures, including measures potentially relating to the powers and resources of the AADB, to reduce the time and cost involved in handling public interest disciplinary cases without compromising on the fairness, thoroughness or quality of the disciplinary process.

Section 3 Budget 2011/12

The FRC's budget distinguishes between the costs relating to accounting, audit and corporate governance and those relating to actuarial standards and regulation. Within the two categories we distinguish between the costs of our core activities, which are under our immediate control, and costs which are dependent on external factors, notably the number and complexity of the public interest cases which fall within the scope of our disciplinary arrangements.

Table 1 shows the impact of these different elements of our costs on our proposed total budget. The total budget is higher than the budget for 2010/11 because we estimate that accountancy disciplinary case costs will increase significantly, reflecting the stage that a number of major cases will have reached in 2011/12. However, we are reducing core operating costs for accounting, auditing and corporate governance by £0.7m and for actuarial standards and regulation by £0.2m compared with the budget for 2010/11.

Table 1: Budget Summary

	Budget 2011/12 £m	Budget 2010/11 £m	Forecast 2010/11 £m
Accounting, auditing and corporate governance			
Core operating costs	12.2	12.9	12.4
Audit inspection costs	2.8	2.6	2.4
Accountancy disciplinary case costs	4.4	2.9	2.2
Review Panel case costs	-	-	-
Total	19.4	18.4	17.0
Actuarial standards and regulation			
Core operating costs	2.2	2.4	2.1
Actuarial disciplinary case costs	0.4	0.8	0.4
Total	2.6	3.2	2.5
FRC Total costs	22.0	21.6	19.5

Table 2 sets out our planned expenditure and funding for core operating costs in relation to accounting, auditing and corporate governance. Table 3 sets out our expenditure and funding in relation to actuarial standards and regulation. Table 4 summarises our projected level of general reserves, and Table 5 our projected level of funds for FRRP and actuarial case costs.

Accounting, auditing and corporate governance

Core operating costs

These cover all our costs in relation to accounting, auditing and corporate governance other than audit inspection, disciplinary case and Review Panel case costs. They are funded by a levy on preparers of accounts, a contribution from the accountancy professional bodies and a Government grant. They also reflect an expected contribution of £0.6m from general reserves, reflecting higher than forecast receipts from the preparers levy in 2010/11 - our levy forecast underestimated the size of the levy group and the scale of additional levy payers who joined the market during the year and became subject to the levy. We plan to use the higher than forecast receipts in 2010/11 to reduce the preparers levy that would otherwise have applied in 2011/12.

Table 2: Expenditure and Funding Projections

	Budget 2011/12 £m	Budget 2010/11 £m	Forecast 2010/11 £m
Core operating costs (Notes 1 and 2)	12.2	12.9	12.4
Review Panel case costs	-	-	-
Total costs	12.2	12.9	12.4
Increase/(decrease) in reserves (See Table 4)	(0.6)	-	1.0
Funding requirement	11.6	12.9	13.4
Funded by:			
Preparers levy – Publicly traded companies	4.4	4.7	5.0
Preparers levy – Large private companies	1.6	1.8	2.1
Preparers levy – Public sector organisations	0.4	0.5	0.4
Accountancy professional bodies	4.7	4.7	4.7
Government (Note 3)	0.5	1.2	1.2
Total	11.6	12.9	13.4

Notes:

- 1) Costs include a contribution of €0.35m (£0.3m) towards the costs of EFRAG.
- 2) Costs are net of publication income of £0.4m which is estimated on a year-on-year basis and therefore subject to fluctuation.
- 3) The Government contribution is included as a planning assumption and is subject to confirmation by BIS.

Audit inspection costs

The costs summarised in Table 1, and further analysed below, include only the specific and variable costs of the AIU. They are met by the individual RSBs with which the firms that are subject to inspection are registered. The AIU's fixed overheads (accommodation and shared IT systems) are included in core operating costs.

The budget for 2011/12 reflects the costs of the planned inspection programme and a reduction in income from the Audit Commission:

	Budget 2011/12 £m	Budget 2010/11 £m	Forecast 2010/11 £m
Core operating costs	3.1	3.0	2.8
Less: Income	(0.3*)	(0.4)	(0.4)
Total	2.8	2.6	2.4

*reflects expected reduction in income from audit inspection services provided to the Audit Commission.

Accountancy disciplinary case costs

The costs shown in Table 1 include only the specific and variable costs of accountancy cases taken by the AADB. The AADB's fixed overheads (staff, accommodation and shared IT systems) are included in core operating costs. Case costs are funded by the accountancy professional bodies to which the individuals or firms which are subject to each case belong within the terms of a formal case-costs agreement. Case costs are forecast on the basis of the available information on actual or prospective cases. However, the accuracy of the forecast will depend on assumptions made as to the progress of cases and is subject to a significant degree of uncertainty.

The forecast for 2010/11 is lower than budget, but it is likely that costs associated with current cases flow through to 2011/12. The forecast case costs for 2011/12 also reflect a likely increase in tribunal cases.

Review Panel case costs

Review Panel case costs include only the specific costs of cases which the FRRP decides, or prepares, to take to court. If incurred, they are met in the first instance from the Review Panel Case Costs Fund. No costs have been incurred in 2010/11.

Actuarial standards and regulation

Table 3: Expenditure and Funding

	Budget 2011/12 £m	Budget 2010/11 £m	Forecast 2010/11 £m
Core operating costs	2.2	2.4	2.1
Actuarial disciplinary case costs	0.4	0.8	0.4
Total costs	2.6	3.2	2.5
Increase/(decrease) in reserves			
Increase/(decrease) in actuarial case costs fund	0.3	(0.3)	0.5
Funding requirement	2.9	2.9	3.0
Funded by:			
Actuarial profession	0.3	0.3	0.3
Insurance levy	1.3	1.3	1.3
Pension levy	1.3	1.3	1.4
Total	2.9	2.9	3.0

The significant reduction in estimated case costs reflects the latest assumptions of the stage that individual cases should have reached by 2011/12. Actuarial disciplinary case costs are funded on the same basis as core operating costs.

General reserves

Table 4: Projected Level of General Reserves

	Budget March 2012 £m	Forecast March 2011 £m	Actual March 2010 £m
Accounting, auditing and corporate governance	2.7	3.3	2.2
Actuarial standards and regulation	0.1	0.1	0.1
Total	2.8	3.4	2.3

In 2008 we consulted on a proposal to increase our general reserves in relation to accounting, auditing and corporate governance from around £1m to around £2m, reflecting the uncertainties arising from the reduced Government contribution and our non-statutory funding arrangements.

Subject to any other significant developments we forecast that the accounting, auditing and corporate governance reserve of £3.3m at March 2011 will reduce to £2.7m at March 2012. We believe that this level will be appropriate for 2011/12 given the continued uncertainties over funding and the risks associated with those elements of the accountancy disciplinary scheme which are not covered by the arrangements with the professional bodies. We plan to utilise the general reserve to fund any costs associated with our proposals to reform our powers and structure.

We plan to maintain the general reserves in relation to our responsibilities for actuarial standards and regulation during 2011/12 at its forecast level at March 2011 of £0.1m.

Table 5: Projected level of case costs funds

	Budget March 2012 £m	Forecast March 2011 £m	Actual March 2010 £m
FRRP Legal costs fund	2.0	2.0	2.0
Actuarial case costs fund	1.8	1.5	1.0
Total	3.8	3.5	3.0

We believe that it is prudent to plan for an increase of £0.3m in the actuarial case costs fund to reflect the possibility that the AADB will investigate further cases involving actuaries, the number and complexity of which cannot be accurately forecast.

Contact details

Policy and Planning Officer
Financial Reporting Council
5th Floor, Aldwych House
71-91 Aldwych
London
WC2B 4HN

e-mail: planning@frc.org.uk

Fax: 020 7492 2301

For general information about the work of the FRC, please see our website at www.frc.org.uk

For any further enquiries, please contact us at the above address.

© The Financial Reporting Council Limited 2011

The Financial Reporting Council Limited is a company limited by guarantee. Registered in England number 2486368.

Registered Office: 5th Floor, Aldwych House, 71-91 Aldwych, London WC2B 4HN.