



FINANCIAL REPORTING COUNCIL

ANNUAL REPORT 2010/11 - SUPPLEMENTARY REPORT

APRIL 2011

INTRODUCTION

This report provides a detailed summary of progress on the activities and projects in our Plan for 2010/11 as a supplement to the Annual Report 2010/11. The report also refers, where appropriate, to planned activities and projects in 2011/12. Activities and projects shown in bold represent our major activities and projects.

The key priorities for our work as set out in our Plan for 2010/11 were as follows:

- Helping market participants – boards, preparers, audit committees, auditors and actuaries, and investors – address the governance and reporting challenges of current conditions, and monitoring their response to those challenges.
- Identifying and responding to the longer term lessons of the financial crisis.
- Influencing and responding to a range of international initiatives in relation to corporate governance and reporting.
- Enhancing our own effectiveness and efficiency as a regulatory authority.

Our decision-making bodies are the FRC Board and the Boards of our six Operating Bodies:

Accounting Standards Board (ASB)
Auditing Practices Board (APB)
Board for Actuarial Standards (BAS)
Financial Reporting Review Panel (FRRP)
Professional Oversight Board (POB)
Accountancy and Actuarial Discipline Board (AADB).

The FRC Board and its Operating Bodies are supported by the FRC's professional staff.

We hope that you will find this report helpful. If you have any queries please send them to the Policy and Planning Officer, FRC, 5th Floor, Aldwych House, 71-91 Aldwych, London WC2B 4HN. Email: plan@frc.org.uk

Corporate Governance

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| Implement changes to the UK Corporate Governance Code. | The revised Code was published in May 2010, and took effect on 28 June 2010. |
| Take the lead in the introduction of a stewardship code for institutional investors aimed at contributing to a significant improvement in the stewardship of UK listed companies. | The UK Stewardship Code was published on 2 July 2010. In December 2010 the FSA amended its Conduct of Business Rules to require authorized asset managers to state whether or not they applied the code. As of 31 March 2011 there were 148 signatories to the code. |
| Work with the EU and BIS to influence the development and implementation of legislative provisions relating to corporate governance. | Ongoing. The FRC responded to the European Commission's Green Paper on the corporate governance of financial institutions, and held a series of discussions with the Commission in advance of its planned separate consultation on corporate governance in the rest of the listed sector. |

Corporate Reporting

| ACTIVITIES & PROJECTS | PROGRESS REPORT |
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| Consider whether there remains a need to issue updated guidance to audit committees, directors and users of actuarial services about the financial crisis and will publish revised guidance if appropriate. | Updated guidance to audit committees, directors and users of actuarial information was issued in November 2010. |
| Promote increased relevance and reduced complexity of corporate reporting on the basis that reporting should be relevant, reliable, intelligible and comparable, and be useful for decision-making, including stewardship decisions. | Following on from the FRC's publication of 'Louder than Words: Principles and actions for making corporate reports less complex and more relevant ', the FRC has continued its work to promote increased relevance and reduce complexity of corporate reporting. Throughout the year, the FRC took forward a project on 'cutting clutter', with the assistance of an Advisory Panel. This resulted, in early April 2011, in the publication by the ASB of a report entitled ' <i>Cutting Clutter: Combating clutter in annual reports</i> '. The report provides a number of practical aids for reducing clutter and factors to consider when planning the annual report process. |

Corporate Reporting

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| <p>Seek to ensure continued support in the EU for maintaining the IASB and other standard setters' ability to exercise independent judgement in setting accounting standards.</p> | <p>The ASB continued to assess and respond to all European Financial Reporting Advisory Group (EFRAG) draft comment letters and Invitations to Comment (27 during the year). The ASB also continued to play its active role in EFRAG, including attending Technical Expert Group (TEG) meetings each month (except August) and the quarterly meetings of the Consultative Forum of Standard-Setters (CFSS). During the year, the ASB was represented at a number of European Commission stakeholder meetings, notably on the potential for use in the EU of the IFRS for Small and Medium-sized Entities (SMEs), the review of the EU Accounting Directives, and governance reviews of the IFRS Foundation. The ASB has also responded to a number of European Commission consultations in the financial reporting area.</p> |
| <p>Take a lead role in influencing the development of IFRS and in the appropriate IASB strategy when convergence with US GAAP projects ends in 2011 and play an active role in promoting the development of a disclosure framework.</p> | <p>The ASB assessed and responded to all International Accounting Standard Board's (IASB) and International Financial Reporting Interpretations Committee (IFRIC) consultations (22 during the year). In April, the ASB Chairman, together with the FRC CEO, visited the USA to hold meetings with a number of US interests, including the Securities and Exchange Commission (SEC). As noted below, the ASB is working with EFRAG on a pro-active project on a disclosure framework.</p> |
| <p>Lead a wide-ranging debate designed to stimulate improvements to narrative reporting, including disclosures in relation to business models.</p> | <p>The ASB has monitored market comments and reports about narrative reporting contained in annual reports and held meetings with a number of organisations active in this area. In addition, the ASB participated in a Black Sun narrative reporting seminar 'Rethinking Reporting' in June 2010 and BIS workshops on the future of narrative reporting held in the autumn of 2010.</p> <p>The FRC published its consultation paper <i>Effective Company Stewardship</i> in January 2011. The paper included a number of proposals aimed at encouraging higher quality narrative reporting, particularly on business strategy and risk management. The consultation closed on 31 March 2011 and a feedback statement will be published shortly.</p> |
| <p>Continue to monitor sustainability information contained in annual reports and consider publishing guidance on sustainability reporting if and when appropriate.</p> | <p>The ASB has monitored market comments and reports about the preparation of sustainability information contained in annual reports and held meetings with a number of organisations active in this area. The ASB was represented at the Prince of Wales' Accounting for Sustainability Forum held in December 2010.</p> |
| <p>Take a lead role in UK, EU and global debates about the extent of the use of fair value, including hosting roundtables as necessary, and provide written comments in response to</p> | <p>The ASB has monitored market comments and reports about the use of fair value and the relevant IASB projects, including responding to a number of IASB Exposure Drafts (EDs) on relevant issues. The ASB also submitted a response to the US FASB on its ED on accounting</p> |

Corporate Reporting

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| IASB and FASB consultations. | for financial instruments. During April 2010, the ASB was represented at a Technical Assessment meeting hosted by the European Commission on the classification and measurement of financial instruments. The ASB hosted a roundtable meeting in May 2010 to discuss the IASB proposals on impairment of financial assets. |
| Implement an agreed strategy for the future of UK GAAP and its convergence with IFRS. | In October 2010, the ASB published a Financial Reporting Exposure Draft (FRED) on the future of UK GAAP, with a comment deadline of 30 April 2011. The ASB has been undertaking a series of presentations and meetings with interested parties to ensure that constituents are both aware of the proposals and are encouraged to respond. In addition, in February 2011 the ASB issued an ED of a Public Benefit Entities (PBEs) standard to address the differences in financial reporting standards that need addressing for such entities. |
| Continue to play a leading role in the global group of National Standard Setters. | The ASB chaired meetings of the NSS held in April and September 2010. The chairmanship of the group has now passed to Canada and the first NSS meeting under Canadian chairmanship was held in March 2011, with significant support from the ASB staff. |
| Participate in EFRAG and Pro-active Accounting Activities in Europe (PAAinE) projects. | In January 2011, the ASB and EFRAG issued a Discussion Paper 'Considering the Effects of Accounting Standards', which is the first output to be published under the PRC banner. The ASB is playing an active role in other pro-active work, leading projects on (a) accounting for corporate income tax (jointly with the German Accounting Standards Board), (b) a disclosure framework (jointly with EFRAG) and (c) a potential project on the role of business models in financial reporting (jointly with EFRAG and the French ANC). The ASB is also represented on an advisory group on an EFRAG-Italian OIC project on business combinations under common control. This work will continue over the coming months |
| Review a selection of annual and interim accounts and directors' reports for compliance with the Companies Act, including applicable accounting standards; focus on the following industry sectors: commercial property, advertising, recruitment, media and information technology; and aim to review around 300 sets of accounts in total in 2010/11. | <p>The Panel has reviewed around 300 sets of accounts in accordance with its operating procedures. The accounts have been drawn from a broad range of companies but with an emphasis on commercial property, advertising, recruitment, media and information technology industry sectors.</p> <p>The Panel published four company specific press notices in the year. In addition, it issued a generic announcement drawing attention to the challenges of reporting principal risks and uncertainties. The Panel also announced its priority areas for 2011/12 – commercial property, insurance, support services and travel.</p> |

Corporate Reporting

| ACTIVITIES & PROJECTS | PROGRESS REPORT |
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| Respond to matters drawn to our attention as a result of complaints or public comment, encouraging referrals from the investment community, other professional advisers and elsewhere. | The Panel has responded to a range of matters brought to its attention during the year through complaints or referrals from other regulators. |
| Influence the development of international enforcement practices through active involvement in EECS, established under CESR. | The Panel continues to play an active role at EECS (ESMA sub-committee) where it continues to be a member of the Agenda Committee. In addition, it has participated in three working groups established to consider the current CESR Standards on Financial Information, Materiality and practical implementation issues. |

Auditing and related services

| ACTIVITIES & PROJECTS | PROGRESS REPORT |
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| Explore ways in which the usefulness of information contained in audit reports can be significantly enhanced from the perspective of investors and other users. | Following APB working party meetings and a meeting with CRAG (an investor representative group), an expanded audit report was included as one of the proposals to reinforce confidence in corporate reporting in the FRC's paper on Effective Company Stewardship. The evaluation of the feedback on these proposals will determine the future action that needs to be taken. Similar issues are being addressed in a working group of the IAASB addressing "Auditor Reporting". Marek Grabowski is a member of the IAASB working group which is developing a discussion paper for publication in the next few months. In February 2011 the APB issued a revision of ISA (UK and Ireland) 700 which amends the short form description of the scope of an audit included in auditor's reports to refer to the auditor's responsibility to read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the financial statements |
| Make any necessary changes to Ethical Standards for Auditors resulting from its consultation on audit firms providing non-audit services to firms which they audit. | Revisions to the APB Ethical Standards for auditors were approved in November 2010 and were published on 17 December 2010 together with a Feedback Paper and the revised FRC Guidance on Audit Committees. The revised standards will become effective on 30 April 2011. BIS is currently consulting on making related changes to the auditor remuneration disclosure regulations. |

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| <p>Together with the IAASB, begin ongoing monitoring of the implementation of the Clarity ISAs.</p> | <p>Jon Grant is leading the International Auditing and Assurance Standards Board (IAASB) project. With AIU support, the APB will provide input from a UK & Ireland perspective. In addition, members of the APB SME Audit sub-committee and other small and medium sized audit firms have been asked to identify audits to use in completing a questionnaire on the implementation of Clarity ISAs in the UK and Ireland for input to the IAASB project.</p> |
| <p>With the POB, keep under review current issues and conditions, including those arising from the financial crisis, that may impact the work of auditors and issue updated standards and guidance if appropriate.</p> | <p>In March 2011 the APB issued a revision of Practice Note 19, 'The audit of banks and building societies in the United Kingdom'. In addition to updating the guidance for the new auditing standards that came into effect at the end of 2010, the APB also revised and enhanced the guidance in a number of areas, including in relation to the audit of accounting estimates and impairment provisions and related disclosures. The APB has also added guidance on bilateral and other periodic meetings between auditors and the FSA. In <i>Effective Company Stewardship</i> the FRC consulted on whether to expand the audit report to cover certain non-financial data.</p> <hr/> |
| <p>With the support of the POB, make greater use of the findings arising from inspection activities in setting standards.</p> | <p>Protocols have been developed for joint AIU and APB responses to IAASB consultations and responses are now submitted on this basis. The ethical standards in 2010 reflected issues which had been brought to the attention of POB by the AIU.</p> |
| <p>Participate in the IAASB, including improving the linkage between inspections and standard setting activities, and contribute to the IAASB's plans to revise ISAs 610, 700 and 720 and to develop assurance standards on pro forma information in prospectuses, compilation and review engagements, greenhouse gas emissions and XBRL.</p> | <p>The APB responded to the Exposure Draft on Pro forma financial information in prospectuses in August 2010. A joint APB/AIU response letter on ISA 610 was submitted to IAASB in October 2010. APB staff members have attended working party meetings in connection with the international projects on audit reports (ISA 700) and auditor responsibilities in relation to other information in documents containing audited financial statements (ISA 720). The APB Chairman chaired a CCAB roundtable on the exposure draft of the greenhouse gas emissions standard and a response from APB on this standard will be sent in due course.</p> |
| <p>Together with the POB, consider the need to further promote and update the audit quality framework.</p> | <p>Input is being provided to an IAASB project on audit quality. Once conclusions are reached on this international work, consideration will be given to update of the UK's Audit Quality Framework.</p> |
| <p>Review the approach to client asset reporting and consider how this might be updated to help auditors comply with expected new FSA requirements.</p> | <p>APB has established a Client Assets Sub-committee and a working group of market experts to assist in the development of a Bulletin for publication later this year setting out guidance for client asset auditors in light of the changes to the FSA's requirements for client asset reporting published in March 2011.</p> |

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| <p>Together with the POB, consider how to enhance the practical application of professional scepticism by auditors</p> | <p>A Discussion Paper 'Auditor Scepticism: Raising the Bar' was published in August 2010. The APB's Feedback Statement was published on 10 March 2011 concurrently with the Feedback Paper to the joint FSA FRC Discussion Paper 10/03 <i>Enhancing the auditor's contribution to prudential regulation</i> as there are overlapping issues in these documents relating to professional scepticism. Work is now ongoing to progress the actions set out in the Feedback Paper.</p> |
| <p>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 relating to segmental reporting, revenue recognition and fraud, and continue to focus on going concern, fair value accounting estimates, asset impairments and compliance with ethical standards.</p> | <p>In July, the POB published the AIU's Annual Report for 2009/10. The report emphasised that firms responded positively to the challenges arising from the economic downturn, particularly in relation to the audit of going concern, but – despite the quality of firms' policies and procedures – the number of audits assessed by the AIU requiring significant improvements remained high. The findings suggest that firms were not always applying their procedures consistently on all aspects of individual audits or applying sufficient professional skepticism in relation to key audit judgements.</p> <p>The AIU's inspection activities continue to result in improvements to firms' policies and procedures which are now generally good. The AIU expects firms to place greater emphasis on achieving behavioural change to ensure this is the case and we will increase our efforts to see that this occurs.</p> <p>Fieldwork for 2010/11 inspections has been completed and drafting of the public reports is underway.</p> |
| <p>Review progress in implementing the recommendations of the Market Participants Group on concentration on the UK audit market and assess the effectiveness of the recommendations as a whole and make proposals on what further action is required.</p> | <p>The Fifth Progress report on the implementation of the Market Participants Group (MPG) recommendations was published in June 2010.</p> <p>An assessment of the overall effectiveness of the recommendations to date, together with suggestions for further action, is currently being drafted and is expected to be published by the end of the year.</p> <p>In view of the House of Lords inquiry into audit and the European Commission Green Paper on the subject, plans to publish a sixth and final Progress Report, together with an assessment of the overall effectiveness of the recommendations to date and suggestions for further action, have been put on hold. The FRC has provided written and oral evidence to the House of Lords inquiry and will shortly respond publicly to the inquiry's recommendations. Our response to the Green Paper stressed the need to enhance audit quality whilst addressing the systemic issues arising from audit market concentration.</p> <p>Next steps will be considered in light of the above and the OFT's response to the recommendation by the House of Lords Economic Affairs Committee that the audit market should be investigated by them and in light of European Commission's proposals following their Green paper on auditing.</p> |

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| <p>Demonstrably influence the work of IFIAR and EGAOB and its sub groups to promote effective regulatory oversight of audit firms, including those managed on a regional basis.</p> | <p>The POB Director has been elected chair of the International Forum of Independent Audit Regulators (IFIAR) and the FRC provides the secretariat support. The POB continues to play a leading role within the European Group of Auditors' Oversight Bodies (EGAOB).</p> |
| <p>Carry out statutory responsibilities in respect of auditing providing independent oversight of the regulatory processes of the Recognised Supervisory Bodies and Recognised Qualifying Bodies.</p> | <p>The POB completed its annual compliance reviews at each of the bodies and will publish its findings in its Report to the Secretary of State for BIS in July 2011. The Recognised Supervisory Body (RSB) reviews focused on the grant of Responsible Individual (RI) status and the Recognised Qualifying Body (RQB) reviews focused on the award of exemptions and the accreditation of higher education institutions. The next cycle of compliance reviews, part of the 2011/12 work programme, will ensure that the recommendations we have made in prior years have been properly addressed and will review the effectiveness of the bodies' processes for audit monitoring and student examinations.</p> |
| <p>Review the effectiveness of the Professional Bodies action plans to improve underlying audit quality and to assess progress against those plans.</p> | <p>Progress against action plans will be considered as part of the 2011/12 monitoring of the Professional Bodies.</p> |
| <p>Continue to work with the EU and BIS to develop the legislative framework and practical measures for audit regulation in Europe under the Statutory Audit Directive.</p> | <p>The focus of work in 2010/2011 has been the implementation of 'equivalence' and 'adequacy' decisions under Articles 46 and 47 of the Statutory Audit Directive into UK legislation.</p> |
| <p>Participate in the arrangements for the co-ordination of the regulation of audit and the oversight of the auditing profession in the EU.</p> | <p>The AIU continues to lead (along with four other countries) the newly formed European Audit Inspection Group whose objectives include promoting cooperation and consistency amongst European audit inspections 28 European countries are now members of this group which meets quarterly.</p> |
| <p>Review the implementation of regulations and practice on transparency reporting by audit firms and issue guidance as required.</p> | <p>The POB undertook a further review of Transparency Reports by the major audit firms to ensure compliance with the regulations and progress against prior recommendations. Findings will be reported within the POB's report to the Secretary of State which will be issued in July.</p> |
| <p>Issue recommendations to enhance the confidence that can be obtained by the public of the monitoring arrangements of the UK professional accountancy bodies of their members who provide non regulatory accountancy services. Review the responses received ensuring that these adequately address the matters raised and assess the practical implementation of the proposals.</p> | <p>The POB has published the responses of the bodies to its review of the UK professional bodies' monitoring of their members practising in non-regulated areas. The bodies broadly welcomed our review and our recommendations and their responses reflect this. We will consider the progress made by the bodies in implementing the recommendations in 2011/12.</p> |

Actuarial Practice

| ACTIVITIES & PROJECTS | PROGRESS REPORT |
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| Complete its suite of technical actuarial standards, focusing on the needs of users of actuarial information. | Technical Actuarial Standards (TASs) on Modelling, Pensions, Insurance and Transformations were issued in April, October, November and December 2010 respectively. A TAS on Funeral Plans was issued in February 2011, completing the suite. |
| Keep under review the implications of the introduction of Solvency II. | The BAS has kept under review the implications of the introduction of Solvency II. |
| Contribute as appropriate to the continuing development of UK pension legislation and the EU Solvency II project. | The BAS has worked with the DWP on recent amendments to legislation and has contributed to its deregulatory review. It has also contributed comments to the FSA on the level 3 text of actuarial guidance concerning the EU Solvency II project. |
| Continue to work closely with Government and other regulators to ensure consistency as we develop our technical actuarial standards. | The BAS liaised with other regulators and government departments as it developed its technical actuarial standards. |
| With the POB, complete the review of the FRC's actuarial quality framework and promote its use. | A revised actuarial quality framework was issued in June 2010. Both bodies continue to promote the framework. |
| With the POB, keep under review the FRC guidance to users of actuarial work and issue further guidance if appropriate. | An update to the guidance was issued in November 2010. |

Professionalism of accountants and actuaries

| ACTIVITIES & PROJECTS | PROGRESS REPORT |
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| 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 | <p>We encouraged the Actuarial Profession to develop a comprehensive set of ethical and conduct standards, guidance and other materials for practising actuaries to support the TASs – for example in the areas of conflicts and whistle-blowing.</p> <p>We worked with the Actuarial Profession to clarify the expected skills of practising actuaries, and establish a framework for developing, maintaining and confirming their professional competence including awareness and understanding of the BAS's new technical actuarial standards (TASs).</p> |

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| <p>development of new standards.</p> | <p>The POB continued its monitoring of the regulatory activities of the RSBs and RQB's in relation to audit and has continued to provide general oversight of the non-regulatory activities of the UK professional accountancy and actuarial bodies, making recommendations on current practices and following up progress of prior year recommendations. A preliminary review of CPD across the Accountancy and Actuarial professions will consider the need for a more thorough investigation.</p> <p>The POB has continued to monitor developments which could affect public confidence. In addition to making recommendations as a result of our monitoring work the POB completed a project whose objective was to quantify the extent to which audit reports included in financial statements filed at Companies House had been signed by firms that were not registered audit firms. The project found that the extent of the problem was limited to a very small proportion of filed accounts but also concluded that the bodies and POB should continue to take robust action against any of their member firms or members found to have signed audit reports without being registered to do so. The POB also repeated a review of the quality of accounts filed at Companies House in light of recommendations made to the professional bodies five years ago. We concluded that the quality of accounts has improved but the Bodies need to continue putting pressure on their members to improve the quality of their work in the preparation and review of accounts.</p> |
| <p>Continue to follow up the Actuarial Profession's progress in responding to the recommendations made to it by the POB in its May 2009 report.</p> | <p>We encouraged the Actuarial Profession to review the nature and scope of professional regulation of practising actuaries, including the public and regulatory reliance which can be placed on the quality controls at actuarial firms.</p> |
| <p>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.</p> | <p>The AADB has made progress with a number of existing cases, has taken on an additional case(s) over the last year and is actively considering others.</p> |
| <p>Assess the need to establish a case cost fund to provide for any liability for cost awarded against the AADB.</p> | <p>The Actuarial case cost, which already exists, has been increased in 2010/11. We are increasing our general reserves to accommodate any liability related to accountancy case costs.</p> |

FRC Effectiveness

| ACTIVITIES & PROJECTS | PROGRESS REPORT |
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| <p>As part of a wider review of the FRC's regulatory powers, complete the review of the effectiveness of the framework for professional discipline, including the FRC's role within the framework.</p> | <p>The FRC has initiated its Reform Project. The FRC will consult on a wide-ranging set of reforms to the FRC that are designed to build on its strengths, including, but not limited to, a review of the effectiveness of the framework for professional discipline. The consultation document will be issued in August 2011.</p> |
| <p>Review the FRC's overall relationship with the accountancy and actuarial professions.</p> | |
| <p>Secure efficiency savings equivalent to 5% of core operating costs.</p> | <p>Our core operating costs budget for accounting, auditing and corporate governance and for actuarial standards and regulation in 2010/11 was £15.3m. Expenditure was kept at £14.6m.</p> |
| <p>Ensure that there are appropriate mechanisms in place for identifying, monitoring and responding to emerging developments.</p> | <p>The FRC will continue to monitor and, where appropriate, respond to emerging events.</p> |