



FINANCIAL REPORTING COUNCIL

ANNUAL REPORT 2006/07

MAY 2007



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One - Chair's Statement

The FRC's Work

The FRC's remit is to define high standards in corporate governance, reporting, auditing and actuarial practice; to be concerned with the application of those standards in practice; and to work with the accountancy and actuarial professions to promote the professionalism of their members.

Fulfilment of this remit is substantially a matter of thought leadership and influencing practitioners. "Success" is difficult to define and measure and is seldom to the credit of the FRC alone. The FRC's task would be impossible without extensive and continuous contact with practitioners.

We have no doubt that our work makes a significant contribution to the healthy functioning of the UK market economy and is increasingly influential overseas. The nature and extent of this work in 2006/07 is well covered in the Chief Executive's Report.

The FRC's Governance

In the course of the year the FRC Board and Council, supported by Government, thoroughly reviewed the FRC's governance. Their conclusions were reported to Parliament and published by the FRC on 29 March, along with a Consultation Paper, available at: www.frc.org.uk/publications/pubs.cfm.

Since the considerable enlargement of its remit in 2004, the FRC has been evaluating the effectiveness of its organisation with three particular objectives in mind. The first is to make the most of the interconnections between the various parts of the FRC's remit while preserving appropriate autonomy for the Operating Bodies. The second is to have governance arrangements which are clear and well able to provide challenge and focus to the FRC's strategy and priorities, while being credibly independent of any particular stakeholder bias. The third is for the FRC to be appropriately accountable and credible as a national regulator notwithstanding its necessarily close working relationships with market practitioners.

The main features of the published proposals are that:-

- The Board and Council will be merged into a single governing body – the new Board, comprising 16 members in total
- The Chairs of the Operating Bodies will be members of the new Board
- The non-executive members, plus the Chairman and the Deputy Chairman, will form a majority of the new Board
- Only the Chair and Deputy Chair will in future be appointed by Ministers.

Members of the new Board will be appointed on their individual merits rather than as representatives of particular interests. The intention is that they should bring to the table a very wide practical

experience in reporting and governance, as well as intra-professional understanding, international knowledge and experience, and diversity. The new Board will have a Committee on Corporate Governance, as the Council does at present, which may include members drawn from outside the Board. Appointments will be made in line with the principles set by the Office of the Commissioner of Public Appointments. There will be a Temporary Nominations Committee to manage the transition from the present structure to the new Board.

The consultation period ends on 1 June and, subject to the consultation feedback and to final endorsement of the proposals by Government and Council, the Temporary Nominations Committee will then begin its work. It is hoped that the new Board will be fully in place by the end of 2007.

The Council

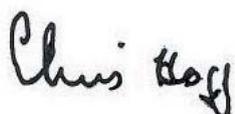
The Council met four times during the year and provided significant guidance on a number of major issues, including the development of our Strategic Framework and the proposed changes to our governance structure. My report on the work of the Council's Committee on Corporate Governance is on page 20. I would like to record my thanks to the two members who departed from the Council during the year: Sir George Mathewson and Ed Sweeney.

The FRC's Staff and Market Support

I want to pay warm tribute to the hard work and skills of the FRC's staff. Their impact is powerfully reinforced by the leadership of the Chief Executive and the Chairs of the Operating Bodies and the indispensable help the FRC receives from the host of practitioners engaged in its Board and Council, the Operating Bodies and their committees, working parties and consultations generally. We are truly a market-led regulator and it is crucial to our effectiveness.

Looking Forward

The FRC, as I have said, is increasingly influential overseas and the engagement to secure this will inevitably strain further both our human and financial resources, even if it is kept to the minimum necessary to serve the UK's interests. We are planning as well as we can to take account of this and believe we will be helped considerably by the focus of our Strategic Framework and by the proposed changes in organisation. The UK is well placed to impact constructively the development of global markets and it is important that the FRC is equipped to play its own part in this endeavour and that it ensures it continues to be as well supported by its stakeholders in the future as it has been in the past.



Sir Christopher Hogg

Two – Chief Executive’s Report

Introduction

This section of the Annual Report summarises the key issues which the FRC has worked on during 2006/07. I have covered these issues under four headings:

- Delivering our 2006/07 commitments
- Establishing a Strategic Framework for the FRC
- Making the FRC a more capable organisation
- Performance assessment.

Delivering our 2006/07 commitments

In our Plan & Budget for 2006/07 we explained that the key themes of our work were intended to be:

- Lead public debate in the UK on the major issues affecting future confidence in corporate reporting and governance
- Shift our resources from developing UK standards and guidance towards the development of high quality international standards and effective cross-border regulatory co-operation
- Monitor corporate reporting and governance practices in the UK and take enforcement action where appropriate
- Contribute to modifying the UK regulatory regime to take account of changes in European and UK legislation.

I believe that we can fairly claim to have met our commitments on each of these themes. I have summarised below the most important aspects of our work on these four themes. Further details of many of these projects can be found in the operating body reports in section Three. A summary report covering all of the major activities and projects which we undertook during 2006/07 can be found on the FRC website at: www.frc.org.uk/about/annual.cfm.

Public debate on the major issues affecting corporate reporting and governance

2006/07 was the year in which we commenced our new responsibilities for actuarial standards and regulation as a consequence of the acceptance by the Government of the recommendations of the Morris Review. Most of our work has been devoted to the development of a conceptual framework for actuarial technical standards. The BAS published a preliminary consultation paper in April 2007. We shall issue a draft of the framework for public comment in the second half of 2007.

One of our most important projects during 2006/07 has been our work on Choice in the UK audit market. In April 2006 we hosted a public meeting to discuss the findings of a report prepared by OXERA which had been commissioned jointly by us and the DTI. Over forty organisations and

individuals responded to our discussion paper and the key conclusions from those responses were debated at a second public meeting in September. In view of the widespread recognition of the significance of the risks presented by the current characteristics of the audit market in the UK, we established a Market Participants Group to identify and assess possible actions which market participants could take to mitigate those risks. The MPG published its interim report in April 2007. In parallel we have been working with the FSA, DTI and HMT in the UK, and with fellow regulatory organisations in other jurisdictions, to identify potential regulatory actions to mitigate the risks. The continuation of this project will be a major feature of our work in 2007/08.

In November we published a discussion paper on audit quality. The paper identifies those drivers that we believe are central to achieving a high quality audit of listed companies and considers whether there are threats which weaken the operation of those drivers. The paper has been prepared in the context of the current financial reporting framework in the UK and the Republic of Ireland but has also been widely circulated internationally because of the increasingly international context in which financial reporting and auditing take place. The paper has been discussed at meetings of the IAASB and IFIAR. We have been encouraged by the fact that over thirty five organisations and individuals have responded to our paper. We are currently considering these responses.

We also made progress on drafting a revised statement on 'true and fair', with a view to updating our statement published in August 2005 to take account of recent developments, including the Companies Act 2006. We informally consulted a number of accounting experts and have commissioned an opinion from leading counsel. We are reflecting on their comments and intend to publish a further statement during 2007.

In 2006/07, the ASB issued two important publications on pensions accounting and disclosure. In December, the ASB issued an amendment to FRS 17 ('Retirement Benefits') to align the disclosure requirements with the equivalent international standard (IAS 19). In January the ASB published a Reporting Statement ('Retirement Benefits – Disclosures') which is designed to promote greater transparency in the reporting of pension obligations. The Statement is designed as a best practice guide and has persuasive rather than mandatory effect.

The issue of narrative reporting has been highly topical over the past few years, particularly in the context of the possible requirement for a statutory OFR. In January the ASB published an assessment of how UK listed companies were complying with the legal requirement to publish a Business Review and of the extent to which companies had chosen to adopt the best practice suggested in its Reporting Statement on the OFR. This topic will continue to be of importance to us in future years as the FRRP will have a statutory duty to monitor compliance with the requirement for Business Reviews for financial years commencing in and after April 2007.

Influencing international standards and cross-border regulatory co-operation

We have devoted considerable attention to the IASB's projects relating to convergence with US GAAP and updating the conceptual framework for financial reporting. The ASB has submitted comments on several of the convergence projects and has taken a leading role in strengthening the capability of European standard-setting bodies to influence the IASB's thinking. The ASB also hosted a public meeting to discuss the conceptual framework project and has submitted a paper calling for the IASB to revise its thinking on some important elements of the proposed framework. These projects will continue to be at the forefront of our work in 2007/08. In the light of the continuing uncertainty about the future direction of international standards, the ASB has decided to defer finalisation of a strategy for converging UK accounting standards with IFRS.

We have also devoted considerable resources to the IAASB's "Clarity" project, which is intended to improve international auditing standards, on which the APB's UK standards are based. This is especially important as the Statutory Audit Directive provides the basis for the adoption of IAASB's standards throughout the EU. The focus of our efforts has been on supporting the idea of principles-based standards and challenging calls for overly prescriptive requirements which might undermine the importance of professional judgement. The Clarity project is not planned to be completed until 2008 and will continue to be a priority for us in 2007/08.

The emergence in recent years of independent regulation of auditing, coupled with the international nature of capital markets, has made co-operation between national audit regulatory authorities an important priority for us. In the EU, we are founder members of the EGAOB and have played a leading role in it and in the various sub-groups established under it. We also played a leading role in the establishment of IFIAR and I was honoured to have been appointed as its first Vice-Chair. Our participation in these international organisations means that the UK is able to play an important role in the development of auditing regulation internationally.

Our work on international co-operation has already provided practical benefits. A particular feature of the work in 2006/07 has been AIU-led inspections together with the US Public Company Accounting Oversight Board at two of the "Big 4" UK audit firms. These inspections have been helpful in developing the PCAOB's understanding of how the UK system for inspections of the major audit firms operates in practice, thereby helping to pave the way for arrangements under which the UK (and the EU as a whole) and the US are able to place reliance on one another's regulatory arrangements in the future.

During 2006/07 we developed our relationship with the US Securities and Exchange Commission. A particular focus was on our common objective in ensuring that the large number of companies which are listed in both the UK and the US prepare their financial statements in accordance with accounting standards and other regulatory requirements. In April 2007 we, the SEC and the FSA signed a protocol which will enhance our ability to co-operate on this objective.

We have also supported the DTI in responding to the European Commission's Company Law Action Plan. The focus of our input has been to ensure the preservation of the essential features of the UK's approach to corporate governance, including "comply or explain".

Monitoring corporate reporting and governance practices

The AIDB's workload in operating an independent investigation and discipline scheme relating to the accountancy profession increased substantially during the year. The independent tribunal in the Mayflower case concluded that the allegation of misconduct had been proven in respect of only one of the respondents. The tribunal awarded costs totalling £1.0m to the other respondents. The outcome of this case has potentially serious implications for the operation of the AIDB's scheme and we are undertaking a review of these implications. If we conclude that changes to the relevant regulatory requirements are appropriate we shall bring forward proposals for consideration.

The investigation into the conduct of Deloitte & Touche LLP as auditors in relation to MG Rover continued, although important aspects of that work were deferred so as not to interfere with the work of the DTI Inspectors who are conducting a wider investigation into the affairs of MG Rover. Investigations in relation to four new cases were commenced.

The principal focus of the FRRP's review of annual and interim accounts was the first-time implementation of IFRS by listed companies. The FRRP issued a report in December which found a good level of compliance but highlighted a number of recurring issues which companies should consider in preparing their reports in future years.

In July 2006 the AIU published the results of its work in monitoring audit quality at the 9 largest audit firms in the UK. It concluded that the audits reviewed had generally been conducted to a high or acceptable standard, with the key audit judgements reviewed generally being both appropriate and soundly-based. The report noted a number of areas in which firms could improve the quality of their work. The scope of the AIU's work was expanded in 2006/07 to the full range envisaged in the DTI's 2003 Review of the Regulatory Regime of the Accountancy Profession. In addition to the 9 largest audit firms, the scope included for the first time a selection of the audits of listed and other major public interest entities undertaken by other UK audit firms. The AIU will report publicly on the key findings and themes arising from these inspections in the summer of 2007.

Modifying the UK regulatory regime

The 8th Company Law (Auditing) Directive was formally adopted by the EU in June 2006 and we have been heavily involved in preparations for its implementation, which is scheduled for mid-2008. The two aspects which are likely to have the greatest impact on our stakeholders are the provisions relating to foreign auditors and to audit committees. Our primary focus in our discussions with the DTI and with the EU Commission has been to ensure that the Directive can be implemented in a proportionate manner. We have also been anxious to ensure that UK stakeholders are fully aware of the implications

of these provisions, which are not limited to the audit profession. In February 2007, we and the DTI hosted a meeting for UK stakeholders to assist them in developing their responses to the Commission's consultation paper. The implementation of this Directive remains a considerable challenge and will continue to be a priority for us in 2007/08.

The amendments to the 4th and 7th Company Law (Accounting) Directives are due to be implemented in the UK in 2008. The main implications for corporate reporting in the UK relate to the requirement for a corporate governance statement and disclosures of related party transactions. We have been working closely with the DTI to ensure that these changes are implemented in a proportionate manner.

The Transparency Directive, which came into force in January 2007, will also have an impact on corporate reporting in the UK. The primary responsibility for implementing the Directive rests with the FSA but the implementation of the Directive in the UK also has important implications for us and has involved a significant amount of preparatory work in 2006/07. It is intended that the FRRP's scope will be expanded to include for the first time non-UK companies with a listing on a UK regulated market. The success of the LSE in attracting overseas listings means that a large number of companies will come within the FRRP's scope for the first time, which will have an impact on our workload in 2007/08.

The Companies Act 2006 contains a number of provisions which affect us and we have been heavily involved in discussions with the DTI during the Act's passage. One of the more important provisions of the Act makes it lawful for the first time for auditors to agree with their clients' limitations on their liability. The wording of the Act is open to a range of interpretations and a number of our stakeholders have asked us to establish guidance as to how the Act might be implemented in practice. We have included this project in the Plan for 2007/08. The Act also contained provisions applying the Freedom of Information Act to the POB. During 2007/08 we shall continue to prepare for the implementation of these provisions, which are expected to come into force in April 2008.

Establishing a Strategic Framework for the FRC

In December 2006 we published for comment a draft Strategic Framework which set out the outcomes and other elements which we believe contribute to our overall aim of promoting confidence in corporate reporting and governance. The Framework makes explicit the fact that the nature of our aim and remit means that, whilst some of its elements are principally the responsibility of the FRC, most depend principally on market participants or other agencies. We intend the Framework to be a way of facilitating co-operation among our wide range of stakeholders to promote well-founded confidence in corporate reporting and governance in the UK.

We are very grateful to those organisations and individuals who provided us with thoughtful comments on the draft Framework. In April 2007 we published a version of the Framework which takes into account those comments. The Framework is available on our website at: www.frc.org.uk/about/. Our priorities for 2007/08 have been set in the context of the Framework and in 12 months' time we shall report against the Framework. We shall keep the Framework under review and will make changes, following consultation, if and when circumstances change.

Making the FRC a more capable organisation

The benefits and costs of our work can have a significant impact on our stakeholders. For this reason we take seriously the need for the FRC to be a capable organisation. The Chairman has described in his report the steps which we are planning to take to make the FRC a better-governed organisation. This section of my report explains some of the steps which we took in 2006/07 to make the Executive more effective.

We are primarily a knowledge-based organisation whose success depends crucially on our staff. I am grateful to them for their expertise and efforts during the past year. We have tried to assist them to become even more effective by paying closer attention to aligning their objectives with the FRC's Plan and by encouraging them to take a greater degree of ownership of their professional and personal development.

We have been pleased at our ability to recruit experienced professional accountants, actuaries and lawyers to work for the FRC. I continue to believe that the FRC can offer rewarding and constructive employment opportunities for skilled and innovative staff. I am particularly pleased at the way in which we have been able to make the staff recruited in relation to our new responsibilities for actuarial standards and regulation feel at home in the FRC.

We have continued to invest in IT systems to help manage the complex flows of work and information in the FRC. We have taken steps to increase our resilience in the face of potential disruptions.

One aspect of being a capable regulatory organisation is the ability to influence the behaviour of market participants. A pre-requisite for influence is communication and the independent survey of our stakeholders which Ipsos MORI undertook in 2006 revealed that we should do more to publicise our work and enhance our ability to engage with our stakeholders. In response to this feedback we have made a number of changes to the way we work. We now publish a quarterly update on developments in corporate reporting and governance which contains a summary of the major developments since the previous report and outlines those expected in the next quarter. We have organised a number of public meetings for stakeholders on important topics; the level of attendance at these meetings suggests that our stakeholders have found them useful. We have also devoted much more time to meetings with market participants, either individually or in small groups, to seek their views and to explain at first hand what we are working on. We have found these changes to be useful and expect to continue to operate in this way in future.

In last year's Annual Report I reported that our stakeholders had emphasised the need for the FRC to assess possible regulatory interventions thoroughly at an early stage to gauge their likely impact, particularly on smaller enterprises. We have followed this approach during 2006/07. For example: In January 2007 the ASB published an updated version of the Financial Reporting Standard for Smaller Entities, which included a major simplification of the requirements relating to share-based payments as a result of views expressed on the Exposure Draft. Also in January, the APB began consultation on

the need for guidance on implementing Auditing Standards on smaller entity audits and new draft guidance on applying the documentation requirements of ISAs (UK and Ireland) to smaller entities.

Performance Assessment

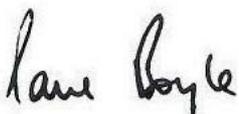
As I noted in my report last year, there are few quantifiable measures, such as market value or market share, which can be used to measure the performance of the FRC. We have identified three aspects of our performance (Outcomes, Outputs and Effectiveness) which we believe are relevant to an assessment of our performance. In section Five we have set out a self-assessment based on the evidence which we have collected during the course of our work and on external evidence, including the results of an independent survey of our stakeholders conducted by Ipsos MORI in March 2007. We are grateful to all those who took time to contribute to that survey.

The survey shows that levels of confidence in corporate governance, corporate reporting, auditing and in the accountancy profession in the UK have remained at the very high levels seen in previous years. This year, for the first time, the survey assessed confidence in the actuarial profession. The key findings in respect of actuaries are that there are high levels of confidence in the reliability of actuarial information and in the integrity and competence of the actuarial profession. The survey also found an improvement in awareness of the work of the FRC and in our communications but that we still need to do more in relation to the investor community.

One aspect of our performance which is quantifiable is cost management. Our core operating costs in relation to our responsibilities for accounting, auditing and corporate governance were £10.8m, compared to a budget of £10.2m. The over-spend is wholly attributable to the Mayflower costs award of £1.0m. The budget for 2006/07 was less than the budget originally proposed for 2004/05. Our core operating costs in relation to our responsibilities for actuarial standards and regulation were close to budget at £1.3m. When these costs are considered against the range and significance of our responsibilities I believe that we are a very cost-effective organisation.

Looking ahead to 2007/08

Our Plan for 2007/08, which we published in April 2007, has been updated to reflect comments received from stakeholders and additional information which was not available in December 2006 when we published the initial version. The Plan contains a wide range of activities and projects which have considerable potential to reinforce confidence in corporate reporting and governance in the UK. However, the most important determinant of the level of confidence is not the work of the FRC but the skills and behaviour of the large number of market participants who are responsible for corporate reporting and governance.



Paul Boyle

Three – Operating Body and Committee on Corporate Governance Reports

Accounting Standards Board (ASB)

The ASB continues to work on influencing the international accounting standard-setting agenda. During the year, the ASB has devoted a good deal of resource to monitoring the joint project by the IASB and US FASB to develop a common conceptual framework that both Boards can use in preparing new and revised accounting standards. The project is important in that it will have a significant influence on the future direction of financial reporting.

The Boards issued their first discussion paper in July 2006, setting out their preliminary views on the objective of financial reporting and the qualities that make the information useful for decision-making. To raise awareness of the issues and engage UK constituents, the ASB hosted a public meeting in September, which helped inform the ASB's response. The ASB also carried out work to articulate the importance of stewardship as an objective of financial reporting and, together with a number of other national standard-setters, the implications of the conceptual framework project for public-benefit entities.

The ASB seeks to influence other IASB agenda projects, responding to all consultation documents and holding public meetings on issues of particular importance, including sessions on measurement in financial reporting and leasing. During the year, the ASB has continued work on its research project to reconsider the fundamental principles of pensions accounting, which I hope will contribute to the development of improved international accounting standards, which may provide a suitable basis for a review of FRS 17. The full research will be published as a discussion paper during 2007, but on pensions disclosures the ASB has already issued an amendment to FRS 17, to align the disclosures with those in the equivalent international standard (IAS 19) and a Reporting Statement of best practice 'Retirement Benefits – Disclosures'. The Reporting Statement is designed to promote greater transparency in financial reporting for defined benefit schemes.

Working within the EU remains an important element of the ASB's work, given that listed companies in the UK and Republic of Ireland are required to use EU-adopted IFRS in their group financial statements. During the year, the ASB has continued to play an active role in the European Financial Reporting Advisory Group, in both its work in advising the Commission on the endorsement of IFRS and in its Pro-active Accounting Activities in Europe initiative.

The ASB has continued to discuss its strategy for convergence of UK standards with IFRS. Respondents to a consultation on convergence held during the year broadly support a two-tier approach: full convergence with IFRS for listed companies and other publicly accountable entities; and a lower level potentially (and ideally) being based on the outcome of the IASB's project on an IFRS for SMEs, on which the IASB issued an Exposure Draft in February 2007. The ASB has decided to defer any final decisions on convergence until there is a much clearer understanding of the outcome of the IASB project on SMEs, at which time a judgement can be made on whether or not it is suitable for the UK's needs.

The ASB continues to encourage improvements in narrative reporting. In January 2007, the ASB published a review of narrative reporting by UK listed companies in 2006. The purpose of the review was to highlight the strengths and weaknesses of current narrative reporting, in the interests of widespread adoption of best practice.

An important element of the ASB's work is its engagement with UK and Irish constituents, in informing its own standards and its interaction with the IASB and Europe.

There have been some changes in the membership of the ASB during the year. Jon Symonds stood down as a member of the Board, and I thank him for his contribution to the work of the Board. I welcome three new members of the Board: Peter Elwin, Geoff Whittington (a former member of the IASB) and Edward Beale.



Ian Mackintosh (Chair)

Auditing Practices Board (APB)

Auditing standards

In 2004 the APB issued new auditing standards as well as ethical standards on auditor integrity, objectivity and independence. Pressure for international harmonisation is likely to result in changes to these standards in the foreseeable future. In the interim period, the APB has focussed on contributing to the improvement of international auditing and ethical standards and has not sought to change UK standards unless this is necessitated as a direct result of a change in UK legislation.

The finalisation of the EU's Statutory Audit Directive in June 2006 provides the platform for the adoption of ISAs issued by the IAASB throughout Europe. Although no date has yet been specified for the adoption of ISAs by the EU this will become feasible once IAASB's Clarity Project has been completed at the end of 2008.

The APB anticipated this development and has been actively involved in the work of the IAASB for many years - contributing directly to some IAASB projects and indirectly, through commenting on exposure drafts, on all others. The APB has also, through its press releases and other material published on its website, sought to raise the awareness of UK and Irish auditors, investors and preparers of financial statements of the important changes that are being made to the ISAs and to facilitate their input to the process.

There is inevitably a tension between the desire for standards that promote the exercise of professional judgement in conducting audits and standards that add specificity to the audit process to help those involved in monitoring compliance. This is one of the issues raised in the November 2006 FRC Discussion Paper "Promoting Audit Quality", which the APB made a significant contribution to developing. This paper:

- identifies those drivers that the FRC believes are central to achieving a high quality audit of listed companies
- considers whether there are 'threats' which weaken the effective operation of those drivers
- seeks opinions as to whether, within the existing legal and regulatory framework, all appropriate steps are being taken to maintain and enhance the quality of audits and, if not, what more could or should be done.

The responses to "Promoting Audit Quality" will help the APB shape its future work programme.

Ethical standards

The APB attaches the same degree of importance to its role in influencing the development of international ethical standards. During the year the UK has taken the Chair of the IESBA Consultative Advisory Group and has been closely involved with IESBA's work to update its Code of Ethics. Just before the end of the year an exposure draft of proposed changes to section 290 of its Code of Ethics on auditor independence was published. During 2007 the APB will review, and comment on IESBA's proposals and commence a review of its own ethical standards for auditors. As the IESBA has moved towards the APB's position in many areas, there is not expected to be a need for major changes to UK standards. As with auditing standards the challenge will remain how to balance the need for standards that are sufficiently robust to meet the public interest test, especially on listed companies, with maintaining a workable approach to smaller audits.

The APB is conscious that auditing and ethical standards must be appropriate to all audits including the audits of smaller entities. Despite recent increases in the audit exemption threshold, many small companies are still audited and there remain statutory requirements for other small entities including charities and pension funds.

During the year the APB's SME audit sub-committee has reviewed ISA exposure drafts and, through the APB's responses, has been effective in eliminating some proposed requirements which are not appropriate on smaller audits and adding to the guidance material on how the requirements can best be applied on smaller audits.

A particular concern of the SME audit sub-committee has been the cost effectiveness of the documentation requirements in ISAs. In January 2007 the APB issued draft guidance intended to help auditors to understand what audit documentation is required on a smaller audit, which includes illustrative examples of audit documentation that are relevant to the requirements of the audit risk and

fraud standards. The illustrative examples can be viewed as training material and therefore not directly falling within the APB's remit. During 2007 we intend to discuss with the accountancy bodies the important question of who provides training support on the application of auditing standards to audit firms, especially smaller audit firms. This will be an important issue when revised ISAs are adopted by the EU and the degree of change involved is likely to be considerable.



Richard Fleck (Chair)

Board for Actuarial Standards (BAS)

The BAS was established on 1 April 2006. This is my first Chair's report.

The BAS was established, following the Morris Review of the actuarial profession, to set actuarial standards with the aim of ensuring that users of actuarial information can place a high degree of reliance on its relevance, transparency of assumptions, completeness and comprehensibility. The Board has a membership drawn from a wide base (including lay members) representing a cross-section of groups with an interest in actuarial matters, and has agreed the BAS Aim and Objectives, which are available on the FRC website at: www.frc.org.uk/bas/about/aims.cfm.

The first tasks undertaken by the BAS concerned the preparatory work for its future operations. Part of this resulted in a MoU between the FRC and the Actuarial Profession in May 2006. The MoU set out the respective responsibilities for actuarial regulation, including a commitment on the part of the Actuarial Profession to publicise BAS standards and to require actuaries to observe them. Under the division of responsibilities the BAS is responsible for standards of a technical nature and the Actuarial Profession is responsible for standards of an ethical nature. Arrangements for communications between the Actuarial Profession and the FRC were agreed in October 2006.

In May 2006 the BAS resolved to adopt all existing Actuarial Profession Guidance Notes (GNs) of a technical nature. However, some of these GNs are referred to directly in legislation and were not finally adopted until April 2007 when appropriate amending legislation became effective.

Since adoption several of these GNs have been amended; in some cases this is because of changes that were in progress at the time of the handover and which were subsequently adopted by the BAS when they were completed. In other cases the BAS made changes to reflect changes in underlying regulation.

(In the case of four GNs applying to life assurance business, this was done by removing all direct and implied references to FSA rules and guidance, in order to obviate the present and future need to update those references). All current and previous versions of adopted GNs are available on the FRC website.

The FRC recruited a second full-time actuary in May 2006 to support the work of the BAS. This remained its level of professional support for the year.

As recommended by the Morris Review the main initial priority of the BAS has been to develop a conceptual framework of the concepts and principles underlying actuarial work. Our aim is to develop a high quality, enduring framework and we believe the project is breaking new ground for actuarial practice anywhere in the world. To this end we formed three working groups, who have been considering the issues of, respectively, value, risk and stakeholders' interests; we are most grateful to the many participants, including our Board members, who have spent a great deal of time and thought on these issues. We published a paper in April 2007 with a preliminary indication of the issues the conceptual framework might contain, and we aim to follow this up in the Autumn with a full discussion paper setting out the issues on which we will be inviting views.

Jointly with the POB, the BAS commissioned research with pension scheme trustees and non-executive directors of insurance companies to help understand their experience and needs when dealing with the Actuarial Profession. The results of this research are now being considered by the Stakeholder Interests Working Group, which comprises those familiar with taking decisions based on actuarial input (such as pension trustees and representatives of the insurance world) as well as people with a particular concern with the "end-user" - the beneficiaries (such as policy holders or pension scheme members) and the public interest (journalists and consumer advocates).

A great deal of activity has gone into establishing liaison arrangements, not only with the Actuarial Profession and some of its related bodies and societies, but also with regulators, government departments, academic and research bodies, etc. This has been achieved through a mixture of regular meetings and more ad hoc arrangements to address specific issues as they arise. At this stage of our development, the BAS has been largely concerned with the UK, but bearing in mind the far-reaching importance of the EU's Solvency II project to insurance (and, in due course, to pensions), we have now begun to involve ourselves in this; in time, we expect international developments to form a significant part of our activity.

A handwritten signature in black ink, appearing to read 'Paul Seymour', with a long horizontal flourish extending to the right.

Paul Seymour (Chair)

Professional Oversight Board (POB)

The POB continued to work closely with other parts of the FRC on most aspects of its work. In particular in 2006/07 the POB has been heavily involved in the FRC project on Choice in the UK audit market and with the APB in the work to develop the FRC Discussion Paper “Promoting Audit Quality”.

Monitoring the quality of the audits of economically significant entities through the Audit Inspection Unit (AIU) continued to be a major focus of the POB’s work in 2006/07. The scope of this work was similar to 2005/06 in that the AIU visited both the four largest audit firms and the five other firms that audit the largest number of entities within their remit. In addition the AIU reviewed for the first time a sample of audits within scope undertaken by other UK audit firms. The AIU will report publicly on the key findings and themes arising from these inspections in the summer of 2007.

A particular feature of the work in 2006/07 has been AIU-led inspections together with the US Public Company Accounting Oversight Board at two of the “Big 4” UK audit firms. These inspections have been helpful in developing the PCAOB’s understanding of how the UK system for inspections of the major audit firms operates in practice, thereby helping to pave the way for arrangements under which the UK (and the EU as a whole) and the US are able to place reliance on one another’s regulatory arrangements in the future.

The POB initiated a debate with stakeholders during the year on the way in which AIU findings on audit firms are reported, with a view to seeing if more information on individual firms could be made available publicly and whether information on individual audits reviewed might be made available to the company’s Audit Committee. The POB expects to publish firm proposals shortly.

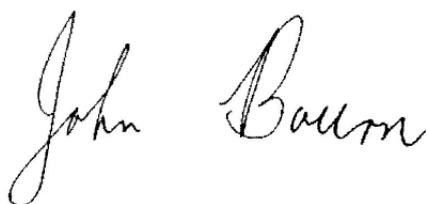
This was the second year in which the POB has carried out a full programme of monitoring visits to those accountancy bodies that offer a recognised UK audit qualification, or are recognised to supervise UK auditors. This involves updating the map of each body’s regulatory systems, testing these in practice, reporting findings and making recommendations to the bodies, and following up on the responses to previous recommendations. The POB reports on this work to the Secretary of State for Trade and Industry, and this Report should be publicly available in July 2007. Overall, whilst the Board has made a further series of detailed recommendations to all of the recognised bodies in this year, it continues to be satisfied that the recognised bodies take their regulatory responsibilities seriously, that with minor exceptions they have adequate resources to undertake these functions effectively, and that they meet their statutory obligations. The recognised bodies have responded for the most part positively to the recommendations we made last year.

The POB also undertakes projects to consider a particular aspect of the bodies’ regulatory activities in greater depth and has started a project in 2006/07 on how the bodies meet practical training requirements for auditors.

The international dimension of the POB's work continued to grow in 2006/07. In particular the arrangements for regulatory cooperation amongst EU audit oversight bodies are developing and the POB has played a significant role within the European Group of Auditor Oversight Bodies, on which the POB represents the FRC. The principal focus is on implementation of the new 8th Company Law Directive on audit regulation, which came into force on 17 May 2006 and which Member States must implement by 29 June 2008. In particular the Directive's provisions on the regulation of the third country auditors of companies traded on EU regulated markets pose a complex challenge and the POB has worked closely with the European Commission and other Member States to try to find a practical and proportionate way forward.

In 2006/07 the POB assumed its new responsibilities for oversight of the regulation of the Actuarial Profession, as part of the package of reforms recommended by Sir Derek Morris in March 2005. In December 2006, the POB published a review of the profession's progress in implementing the recommendations made to it by the Morris review, and set out its ongoing approach to oversight of the profession. The POB concluded that the profession had made good progress in education and training, but that further work was needed in the areas of ethical principles and CPD requirements for reserved roles, including in topical areas such as mortality projections. Another Morris recommendation was that the FRC should, within 2-3 years, satisfy itself that appropriate monitoring and scrutiny of actuaries is occurring. The POB established arrangements with the profession and the relevant statutory regulators to assess the existing monitoring systems as the initial phase of this review which is continuing into 2007/08. The POB has also worked with the BAS on a number of matters, including an FRC survey of the needs of the principal users of actuarial services, with input from the FRC's Actuarial Stakeholder Interests Working Group, and consideration of the drivers of quality in actuarial practice which will also continue into 2007/08.

There were no departures from POB during the year. I was delighted to welcome Anthony Carus, who joined the Board in May 2006.

A handwritten signature in cursive script that reads "John Bourn". The signature is written in black ink and is positioned above the printed name.

Sir John Bourn (Chair)

Financial Reporting Review Panel (FRRP)

The FRRP carried out 312 reviews in 2006/07, including interim accounts and annual accounts of overseas issuers. 20 sets of accounts were also subject to restricted review in respect of their pensions disclosures. This year the Panel concentrated on monitoring the implementation of IFRS in the annual group accounts of listed companies in the UK.

The Panel published its findings in respect of its early reviews of IFRS annual accounts in December 2006. This report followed the Panel's earlier work on interim accounts of listed companies which were required to be prepared in accordance with the valuation and measurement principles of the international accounting standards. The move from UK GAAP to IFRS was a major challenge for UK companies and the Panel applauded the work that had been put into producing the first annual accounts under the new framework. The Panel found a good level of compliance with IFRS, but noted that as everyone becomes more familiar with the new requirements it is likely that there will be further changes and improvements. The Panel made a number of suggestions in that direction and encourages a more focused and thoughtful consideration of certain of the accounting requirements which could reduce the overall length and complexity of the accounts. The Panel believes that, like convergence, consistent application of IFRS is a medium term objective that will be achieved through experience and familiarity.

During the year the Panel conducted a review of defined benefit pension disclosures by companies reporting under IFRS and UK GAAP. The Panel was encouraged by the results of its review and the general level of compliance with the complex disclosure requirements. Its report, published in July 2006, identified areas where the quality of pensions reporting could be improved and complemented the work being carried out by the ASB in developing its Reporting Statement of best practice on pensions reporting.

In October 2006 the Panel published a detailed report on the results of its reviews for the 2005/06 financial year which were prepared in accordance with UK GAAP. The Panel found no evidence of systemic weakness in the accounts that it examined but indicated a number of areas where reporting could be improved which were also relevant for companies who continue to report in accordance with UK standards.

Throughout its work during the year, the Panel was impressed by the thoroughness and technical understanding demonstrated by companies in their responses to the Panel's enquiries. In many cases there was evidence of effective involvement of audit committees.

The introduction of IFRS for the group accounts of listed issuers has heightened the importance of our relationships with overseas regulators. In April 2007, as stated in the report of the Chief Executive, the FRC signed a protocol with the US Securities and Exchange Commission and the FSA. The agreement allows for the exchange of information between SEC and the Panel in connection with the accounts of issuers listed in the UK and registered with the SEC in the US. It is hoped that the arrangements will

help better manage the potential regulatory burden on dual listed entities trading on both the UK and US markets.

The Panel continues to be an active participant in European enforcer sessions (EECS), a forum for national enforcers of accounting standards co-ordinated under the CESR. In addition to technical issues, matters of common interest are discussed to further an understanding of different approaches to enforcement and encourage consistent application of international accounting requirements.

There have been a number of changes to the FRRP membership during the year. Rosemary Thorne, David Mallett and Nigel Macdonald all left the Panel, having served three full terms. Tony Wedgwood also retired when his term expired in March 2007. My thanks go to them for their valuable contribution and support to the Panel during their years of service. I was pleased to welcome new members: Daniel Abrams, James Coyle, Jimmy Daboo, Mary Keegan, David Lindsell, Chris Moulder and Richard Pinckard.

A handwritten signature in black ink that reads "W. Knight". The signature is written in a cursive, flowing style.

Bill Knight (Chair)

Accountancy Investigation and Discipline Board (AIDB)

The Accountancy Investigation and Discipline Board (AIDB) is the independent, investigative and disciplinary body for accountants in the UK. It operates and administers an independent disciplinary scheme covering members of the following accountancy professional bodies: the Association of Chartered Certified Accountants, the Chartered Institute of Management Accountants, the Chartered Institute of Public Finance and Accountancy, the Institute of Chartered Accountants in England and Wales, the Institute of Chartered Accountants of Ireland and the Institute of Chartered Accountants of Scotland, which joined the Scheme in 2006.

The AIDB only considers matters which raise important issues affecting the public interest. During 2006/2007 the Board considered 18 potential matters. The AIDB also monitored a number of other potential cases, which came to its attention from a variety of sources.

In June 2006 the AIDB announced that it had decided to investigate the conduct of Mr Geoffrey Stuart Pearson in relation to events at Langbar International Limited. This decision was taken following consultation with the ICAEW (the professional body of which Mr Pearson is a member), which has agreed that the matter should be investigated by the AIDB. In July 2006 it announced an investigation into events at European Business Trust, as a result of a referral by the ICAI. In October 2006 the

AIDB announced it would investigate the conduct of RSM Robson Rhodes LLP, auditors, and senior executives at iSoft plc, again after consultation with the ICAEW.

In 2006 the Board commissioned a review of the AIDB Scheme by its legal advisors. The objective of the review was to ensure that the disciplinary process operates in a fair, transparent and efficient manner, consistent with the principles of good regulation. A number of recommendations have been or are being implemented.

In January 2007 the AIDB completed its first full disciplinary case. After a total of 20 days of hearings, the independent Tribunal set up by the AIDB to consider disciplinary complaints arising out of the collapse of the Mayflower Corporation plc completed its deliberations and issued its findings. The independent Tribunal in the Mayflower case upheld the allegation of misconduct against one of the respondents and excluded the individual in question from membership of the ACCA for a period of 12 months. The Tribunal dismissed allegations of misconduct against the other two respondents and awarded costs in their favour.

The Tribunal's decision has serious implications for the conduct of future disciplinary cases by the AIDB. Consequently, the Board decided to widen the scope of its review of the Scheme's operation and is considering a number of additional changes designed to ensure that the independent disciplinary process in public interest cases continues to operate smoothly and effectively.

Also in 2006/07, in line with recommendations contained in the Morris Review of the Actuarial Profession, the AIDB has worked closely with the FRC and the Actuarial Profession to agree the draft Scheme and detailed Regulations that would underpin the inclusion of the Actuarial Profession in the discipline scheme later in 2007.

In early 2007, Board Members Sarah Brown, Stuart McKee and David Thomas were reappointed for a second three year term. I am delighted that they have chosen to continue their involvement with the AIDB.

A handwritten signature in black ink on a light grey background. The signature is cursive and appears to read 'Mike Fogden'.

Mike Fogden (Chair)

Committee on Corporate Governance

The Committee on Corporate Governance is a committee of Council with full authority to keep under review developments in corporate governance generally and in particular to keep under review the Combined Code and its implementation by companies and their shareholders. I have chaired it since assuming the Chair of the FRC, following the example of my predecessor.

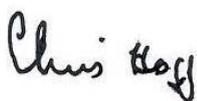
The Committee carried out a formal but light touch review of the Code in 2005 and has started a similar exercise to take place in the rest of 2007. A consultation paper was issued on 18 April 2007, available on the FRC website at: www.frc.org.uk/corporate/combinedcode.cfm.

As preparation for this review I held a series of meetings during the year with company chairmen and senior investors to learn at first hand about their experience of implementing the Code. Overall the view was positive, with the Code seen as having contributed to improvements in the governance of listed companies and a more constructive dialogue between boards and shareholders. However some concerns were raised, for example about the impact of the Code on smaller listed companies and whether the 'comply or explain' mechanism was working as effectively as it might. These issues will need to be addressed as part of the forthcoming review.

During 2006, the FRC provided assistance to the Pre-Emption Group, which was set up following a report carried out for the DTI by Paul Myners to update the Pre-Emption Guidelines. A revised Statement of Principles was published in May 2006.

2006/07 has seen a lot of activity at EU level. Revised versions of the 4th and 8th Company Law Directives – which respectively introduce new mandatory requirements on listed companies to make a corporate governance statement in the annual report and to have an audit committee – were finalised, and a new Directive intended to make it easier for cross-border investors to exercise their rights is close to being agreed. In substance the requirements set out in the Directives are largely in line with existing market practice in the UK, but the DTI is nonetheless required to incorporate the Directives into UK law. It is possible that some consequential amendments to the Combined Code may be needed as a result.

Almost all EU Member States now have a national corporate governance code such as the Combined Code. While the detailed content of these codes and the way they are enforced will understandably differ as a result of different market structures and legal traditions, by and large they are all trying to address the same sort of issues. For that reason during 2006 the FRC initiated an informal network of some of the organisations responsible for these national codes, to provide an opportunity to exchange experiences and best practices. We hope to develop these contacts further during 2007/08.



Sir Christopher Hogg (Chair)

Four – Expenditure and Funding

Our Financial Management and Reporting Framework set out in Annex D provides the framework within which we manage and report on the costs of our activities and how they are funded. While we endeavour to secure value for money in all our expenditure, we believe that the cost of our core operating activities is the best indicator of our effectiveness in managing our costs.

Summary of expenditure

	Actual 2006/07 £m	Budget 2006/07 £m	Actual 2005/06 £m
<i>Accounting, auditing and corporate governance</i>			
Core operating costs	10.8	10.2	9.0
Audit inspection costs	2.1	2.5	1.7
Accountancy disciplinary case costs	0.9	0.5	0.5
Review Panel case costs	-	-	-
Total	13.8	13.2	11.2
<i>Actuarial standards and regulation</i>			
Core operating costs	1.4	1.3	-
Actuarial disciplinary case costs	-	-	-
Total	1.4	1.3	-
Total	15.2	14.5	11.2

The Framework is consistent with the way in which we manage our costs and the basis on which they are funded. Our audited financial statements are in Annex A on pages 45 to 60. The expenditure as reported above can be reconciled to the audited financial statements as follows:

	£m
Total expenditure in the table above	15.2
Deduct: Capital expenditure included in core operating costs	(0.2)
Payments in respect of onerous lease in core operating costs	(0.4)
Release of Onerous Lease Provision in statutory accounts	(0.3)
Add: Depreciation not included in core operating costs	0.3
Net operating expenditure per audited financial statements	<u>14.6</u>

Accounting, auditing and corporate governance

Core operating costs

Core operating costs, analysed by category of expenditure, were as follows:

	Actual 2006/07 £m	Budget 2006/07 £m	Actual 2005/06 £m
Staff Costs	7.2	7.0	6.2
Accommodation costs	1.1	1.0	1.3
AIDB costs award	1.0	-	-
Professional fees	0.3	0.7	0.5
IT costs	0.5	0.5	0.6
Other costs	1.1	0.9	0.8
Contingency	-	0.3	-
	<u>11.2</u>	<u>10.4</u>	<u>9.4</u>
Sundry income	(0.6)	(0.3)	(0.6)
Capital expenditure	0.2	0.1	0.2
Total	<u><u>10.8</u></u>	<u><u>10.2</u></u>	<u><u>9.0</u></u>
Staff numbers	55	61	49

The AIDB cost award arose from the decision of the independent tribunal in the Mayflower case.

Excluding the AIDB cost award, core operating costs would have been £0.4m below budget.

Accommodation costs include the settlement in respect of the surrender of the lease of the former premises of the Accountancy Foundation, one of the FRC's predecessor bodies, which was surrendered in March 2007.

The additional sundry income arose from higher than budgeted royalties on publications.

Core operating costs, analysed by operating unit, were as follows:

	Actual 2006/07		Budget 2006/07		Actual 2005/06	
	£m	Staff	£m	Staff	£m	Staff
ASB	1.8	13	2.5	16	2.1	13
APB	0.9	6	1.2	7	0.8	6
FRRP	1.4	10	1.7	11	1.2	7
POB	1.5	7	1.3	7	1.1	6
AIDB	1.9	4	1.0	5	0.8	4
CGU	0.1	1	0.1	1	0.1	1
Planning & Resources	2.0	9	1.3	9	2.0	8
Corporate	1.2	5	1.1	5	0.9	4
Total	10.8	55	10.2	61	9.0	49

These figures represent the core operating costs of each operating unit plus an allocation of the central overheads based on the number of full time staff in each operating unit.

The AIDB costs were significantly higher than budgeted due to the cost awards in the Mayflower case.

Audit Inspection Unit

The costs of the AIU represent the costs of the programme of independent audit inspections. The costs in 2006/07 were £2.1m compared to a budget of £2.5m and £1.7m in 2005/06. The average number of AIU staff increased to 16 from 13 in 2005/06.

Investigation and disciplinary case costs

During the year the AIDB incurred costs of £0.9m in relation to investigating and prosecuting individual cases. These costs are not susceptible to firm budgetary limits because the number and complexity of cases is unpredictable.

The levy on listed companies for 2006/07

The levy on listed companies is collected on our behalf by the FSA at the same time that it collects its own fees, which helps to reduce the costs of collection. The levy rates set at the beginning of 2006/07 resulted in collections of around £0.2m more than planned. This excess will be used to set levy rates for 2007/08 which will be lower than would otherwise have been the case.

Actuarial standards and regulation

Core operating costs

Our responsibilities for actuarial standards and regulation commenced during 2006/07. Core operating costs comprise the cost of BAS, the cost of the work undertaken by POB and AIDB in relation to actuarial matters, and a fair apportionment of the cost of our support services and corporate costs of £0.4m. The budget reflected a progressive build-up phase for our new responsibilities and our expenditure was marginally more than budgeted, due principally to staff costs. The average number of staff working on actuarial standards and regulation was 5.

Actuarial disciplinary case costs

The formalities relating to the extension of the scope of the AIDB's work to include actuarial costs are expected to be completed in the first half of 2007/08. There was no expenditure on cases in 2006/07.

Actuarial Standards and Regulation – Funding Requirement

The amount which we needed to collect in relation to our work on actuarial standards and regulation is as set out below:

	Actual	Budget
	2006/07	2006/07
	£m	£m
Core operating costs	1.4	1.3
Actuarial disciplinary case costs fund	-	0.2
Recovery of set-up costs	0.3	0.2
Total	1.7	1.7

Actuarial disciplinary case cost fund

As set out in our Financial Management and Reporting Framework, it is our intention to establish a fund to cover actuarial disciplinary case costs and it was our intention to raise an initial contribution of £0.2m in 2006/07. In view of the delay in completing the legal formalities relating to the extension of the AIDB's responsibilities to include actuarial cases, this fund will not now be established until 2007/08.

Recovery of set-up costs

We incurred set-up costs of £0.3m when we assumed responsibility for actuarial standards and regulation in 2005/06 and it was our intention to recover this over three years starting in 2006/07. We have taken advantage of the delay in establishing the actuarial disciplinary case costs fund to accelerate the recovery of these costs. The balance of costs to be recovered is less than £0.1m and this will be recovered in 2007/08 and 2008/09.

The levies for actuarial standards and regulation for 2006/07

The funding of our work on actuarial standards and regulation comes from the actuarial profession (10%), insurance companies (45%) and pension funds (45%). A total of £1.7m was receivable during 2006/07, which was very close to the amount planned.

Reserves

The Directors believe it is prudent to maintain reserves to meet unforeseen circumstances in recognition of the fact that the FRC has entered into a number of long-term commitments. The target level of reserves is kept under review by the Directors.

At 31 March 2007 our General Fund showed a surplus of £1.1m compared to a surplus of £1.0m as at 31 March 2006. The Directors believe that the level of reserves is appropriate but will continue to keep the level under review.

Five – Performance Assessment

We have assessed three aspects of our performance:

- the outcomes we are seeking
- our outputs in terms of the activities and projects we have taken forward
- our effectiveness.

Outcomes

We assess the outcomes of our work through:

- an annual survey of confidence in corporate reporting and governance (the most recent survey was conducted on our behalf by Ipsos MORI in March 2007)
- the evidence we obtain from our monitoring and enforcement activities.

The following sections of the report set out the evidence we have obtained, together with the results of the Ipsos MORI survey, in relation to corporate governance, corporate reporting, auditing, actuarial information, and the integrity, competence and transparency of the accountancy and actuarial professions.

The sequence of outcomes follows that set out in our Strategic Framework.

Outcome One – Corporate Governance

Our 2007 survey evidence showed the following levels of confidence in corporate governance:

	2007		2006		2005	
	Very confident	Fairly confident	Very confident	Fairly confident	Very confident	Fairly confident
	%	%	%	%	%	%
Directors	36	59	31	63	24	68
Investors	29	66	22	70	12	82
Auditors	28	64	10	78	n/a	n/a

Our 2005 report on the implementation of the Combined Code found that overall the Code was bedding down well and having a positive impact on confidence in corporate governance, contributing to improvements in corporate governance practice and disclosure and greater engagement between boards and shareholders. The report identified a number of issues that were to be kept under review.

During 2006/07, the FRC Chair held a series of meetings with company chairs and senior investors to hear their views on the impact of the Combined Code and the effectiveness of the UK's corporate

governance framework. The feedback from these meetings was broadly positive and confirmed that there was general support for the UK's "comply or explain" approach. The Code was considered to be working reasonably well, though concerns were raised about "box-ticking" and the potential compliance costs for smaller listed companies.

During 2007/08, we will conduct a review of the impact of the Code to consider whether it is appropriately enabling UK listed companies to be led in a way that facilitates entrepreneurial success and the management of risk (Outcome One of our Strategic Framework).

Outcome Two – Corporate Reporting

Our 2007 confidence survey showed the following level of confidence in corporate reporting:

	2007		2006		2005	
	Very confident	Fairly confident	Very confident	Fairly confident	Very confident	Fairly confident
	%	%	%	%	%	%
Directors	52	42	36	60	32	63
Investors	36	58	26	68	22	76
Auditors	44	54	24	68	n/a	n/a

The FRRP reviewed 312 sets of accounts in the year to 31 March 2007. 20 sets of accounts were also subject to restricted review in respect of their pensions disclosures.

In August 2006, the FRRP published the results of its review into disclosures of defined benefit pension schemes in annual accounts. The review evaluated the completeness and clarity of disclosures provided by companies reporting under IFRS or UK GAAP. The report identified some ways in which the quality of reporting could be improved.

In October 2006, the FRRP published an activity report summarising the results of the reviews it had conducted during the year to 31 March 2006 and which had been prepared under UK GAAP. 284 sets of accounts, including 76 interim reports, were reviewed. Of these, 82 companies were approached for further information leading to 49 companies undertaking to reflect the Panel's comments in future accounts. The Panel found no evidence of systemic weakness as a result of its reviews. The improvements it agreed with companies were considered to enhance the clarity and quality of corporate reporting rather than address inappropriate accounting treatments.

In December 2006, the FRRP published a report on its preliminary findings in respect of IFRS implementation by UK listed companies in their annual accounts. The Panel identified a number of recurring issues which it drew to the attention of companies to help in their planning of their next IFRS annual accounts.

The FRRP issued three press notices in the period in respect of its reviews of company accounts where the matters at issue were such as to be brought to the market and users' attention. A generic press announcement was also made to draw attention to a trend that the Panel had identified in the accounts of certain companies in the oil and gas industry relating to their accounting for material acquisitions and which it found inappropriate.

The ASB's first review of narrative reporting by UK listed companies was published in January 2007 with the aim of keeping the spotlight on narrative reporting and the importance of encouraging continuing improvement in this area. In undertaking the review, the ASB analysed the annual reports of 23 listed companies, with a year-end of March 2006 or later (and so required to comply with the current legal provisions to prepare a Business Review). It also drew on surveys by a number of other organisations and the work of other parties with an interest in narrative reporting. Together these reviews of annual reports covered a significant number of the FTSE 350 leading quoted companies.

The review found that while most companies were good at describing their strategy and current performance, they were weaker on providing forward looking information and identifying their principal risks and how they are managed. The review noted that narrative reporting is still evolving and, whatever name is given to the narrative sections of the annual report, the overall impression is that there appears to be a willingness by many companies to go beyond strict legal requirements and to move towards best practice reporting. The ASB hopes that trend will continue.

Outcome Three - Auditing

Our 2007 confidence survey showed the following level of confidence in auditing:

	2007		2006		2005	
	Very confident	Fairly confident	Very confident	Fairly confident	Very confident	Fairly confident
	%	%	%	%	%	%
Directors	53	42	41	53	37	50
Investors	27	67	20	66	20	70
Auditors	70	30	38	58	n/a	n/a

In July 2006, the AIU issued its second public report covering the principal issues arising from its 2005/6 audit quality inspections of the four largest UK audit firms and the five other UK firms with a significant number of audit clients within the AIU's remit. The report stated that the quality of auditing in the UK was considered to be fundamentally sound, while identifying various areas in which improvements needed to be made by some or all of the firms. It also stated that the progress made by each of the firms in implementing recommendations for improvement would be reviewed during 2006/7. The report is available on the FRC website at: www.frc.org.uk/pob/audit/publications/.

In the year to 31 March 2007 the AIU completed or commenced further inspections of all nine firms. Inspections of two of the “Big 4” firms were conducted jointly with the US Public Company Accounting Oversight Board, by agreement with the firms concerned, but led by the AIU. In addition, the AIU reviewed for the first time a sample of audits within scope undertaken by other UK audit firms.

The AIU will report publicly on the key findings and themes arising from its 2006/7 inspections, and the progress made by firms in implementing prior year recommendations, in the summer of 2007.

Outcome Four – Actuarial Practice

Our 2007 confidence survey showed the following level of confidence in the reliability of actuarial information.

	2007		Reported change in confidence over the last four years		
	Very confident	Fairly confident	Increased	Stayed the same	Decreased
	%	%	%	%	%
Insurance Directors	22	33	22	67	11
Pension scheme trustees/managers	31	62	18	72	10
Actuaries	38	43	38	38	10

This is the first year in which the FRC has assessed the level of confidence in actuarial information, following the commencement of our responsibilities for actuarial standards and regulation in April 2006.

One of the recommendations of the Morris review was that the FRC should, within 2-3 years, satisfy itself that appropriate monitoring and scrutiny of actuaries is occurring. The POB established arrangements with the profession and the relevant statutory regulators to assess the existing monitoring systems as the initial phase of this review which is continuing into 2007/08.

The BAS and the POB have also worked together on a number of initiatives to help institutional recipients and users of actuarial information know what the main drivers of quality are and be proactive in challenging the quality of the actuarial information they achieve. These include an FRC survey of the needs of the principal users of actuarial services, with input from the FRC’s new Actuarial Stakeholder Interests Working Group, and consideration of the drivers of quality in actuarial practice, which will also continue into 2007/08.

Outcome Five – Professionalism of accountants and actuaries

Accountants

Our 2007 confidence survey showed the following levels of confidence in the integrity and competence of the accountancy profession:

The integrity of the accountancy profession

	2007		Reported change in confidence over the last four years		
	Very confident	Fairly confident	Increased	Stayed the same	Decreased
	%	%	%	%	%
Directors	71	28	20	77	2
Investors	33	62	11	71	15
Auditors	90	10	36	62	0

The competence of the accountancy profession

	2007		Reported change in confidence over the last four years		
	Very confident	Fairly confident	Increased	Stayed the same	Decreased
	%	%	%	%	%
Directors	50	46	24	67	8
Investors	35	60	13	73	11
Auditors	72	28	48	48	2

The POB followed up with the professional accountancy bodies their response to and implementation of the recommendations in three previously published reports on important areas of their regulation of accountants – on Training and Education in the Accountancy Profession (April 2005), on the Procedures for Complaints and Discipline (February 2005) and on How Accountants Support the Needs of Small and Medium-sized Companies and their Stakeholders (March 2006).

In November 2006, the POB published a new edition of 'Key Facts and Trends in the Accountancy Profession' (available on the FRC website at: www.frc.org.uk/pob/publications). This brings together in one place a range of information both on the major accountancy bodies and on the major audit firms. The POB reported that the overall picture presented by the Survey was of an accounting profession in good health with the numbers of students and members continuing to grow.

Actuaries

Our 2007 confidence survey showed the following levels of confidence in the integrity and competence of the actuarial profession:

The integrity of the actuarial profession

	2007		Reported change in confidence over the last four years		
	Very confident	Fairly confident	Increased	Stayed the same	Decreased
	%	%	%	%	%
Insurance Directors	56	33	22	67	11
Pension scheme trustees/managers	54	46	11	87	3
Actuaries	71	24	15	71	14

The competence of the actuarial profession

	2007		Reported change in confidence over the last four years		
	Very confident	Fairly confident	Increased	Stayed the same	Decreased
	%	%	%	%	%
Insurance Directors	22	56	22	67	11
Pension scheme trustees/managers	38	62	15	82	3
Actuaries	57	38	39	43	19

In December 2006, the POB reported on its review of the Actuarial Profession's progress in implementing the recommendations made to it by the Morris Review. This was the first report by the POB covering its new responsibility for independent oversight of the actuarial profession, which it assumed in April 2006 as part of the package of reforms recommended by Sir Derek Morris's Review of the Actuarial Profession in March 2005.

Given the time required for these new procedures to take effect, it was not appropriate for the POB to report on whether the Morris Review's desired outcomes had been achieved through the implementation of its recommendations. The POB's follow-up work will include an assessment of the direct impact of recent reforms on features such as pass rates and qualification times, as well as indirect

impacts on the competence of actuaries, the quality of their work and compliance with professional and ethical standards.

The review also identified areas where the POB believes that the Profession should do more, and matters it considers important which go beyond the analysis in the Morris Review. In particular it will look to the Profession to make substantive progress in the coming year in the areas of ethical principles and CPD requirements for actuaries performing roles which are reserved to Fellows of the Faculty or Institute of Actuaries, and in topical areas such as mortality projections.

Outputs

We have assessed our outputs by reference to our published Plan & Budget for 2006/07.

Sections Two and Three of this report and the supplementary report on our website demonstrate that we have substantially completed or made significant progress on the activities and projects included in our Plan.

Effectiveness

We have assessed three aspects of our effectiveness:

(a) Our adherence to our regulatory principles:

We work on the basis that a well-informed market is the best regulator.

We have published, in consultation with our stakeholders, a Strategic Framework which sets out the outcomes and other elements which we believe contribute to well-founded confidence in corporate reporting and governance. This Framework emphasises the importance of a proportionate approach by the FRC and other regulatory authorities and is based on our market-led approach to regulation.

We target the use of our powers, taking a proactive, risk-based and proportionate approach, making effective use of Regulatory Impact Assessments and having particular regard to the impact of regulation on small enterprises.

In May 2006, we published on our website a statement of the FRC approach to the preparation of regulatory impact assessments at: www.frc.org/about. During 2006/07, we have continued to take account of the impact of our proposals on the regulated community.

We emphasise principles and clarity in our standard-setting and rule-making and seek to ensure, as far as it is appropriate to do so, that we are consistent with international standards.

The accounting, auditing, reporting and actuarial standards issued in 2006/07 were in general principles-based. In influencing international-setting, we have emphasised the importance of a principles-based approach.

We are consultative - involving preparers, auditors, actuaries, users of corporate reports and other regulatory organisations in our decision-making and allowing adequate time for consultation, without compromising our independence or confidentiality.

We have consulted in a timely and effective way on significant proposals during the course of the year and have taken account of stakeholder responses in finalising our proposals.

We recognise the importance of professional judgement in the way in which standards and rules are applied and enforced.

We have continued to lead the debate on the significance of the “true and fair” view.

Where we discharge a judicial or quasi-judicial function, we do so in accordance with our formal powers and the rules of natural justice.

We have undertaken our investigative and disciplinary functions in line with the rules of the AIDB scheme and the rules of natural justice.

We are transparent, accountable and efficient in our work, and ensure that it receives appropriate publicity.

See sections (b) and (c) below.

(b) Our accountability

In December 2005, we published our draft Plan for 2006/07. In May 2006 we published our revised Plan taking account of the feedback we received, which we summarised in a statement on our website.

We asked Ipsos MORI to include in the annual confidence survey they undertake on our behalf questions on respondents’ understanding of our role and the extent to which they view us favourably or otherwise. They included similar questions in last year’s survey.

The survey also found an improvement in awareness of the work of the FRC and in our communications but that we continue to need to do more in relation to the investor community.

Understanding of the FRC’s role:

	2007		2006	
	Well understood	Not well understood	Well understood	Not well understood
	%	%	%	%
Directors	71	29	64	36
Investors	29	71	32	68
Auditors	88	12	70	30

Overall view of the FRC:

	2007			2006		
	Favourable	Neutral or no view	Unfavourable	Favourable	Neutral or no view	Unfavourable
	%		%	%	%	%
Directors	40	49	11	37	52	11
Investors	32	67	2	30	68	2
Auditors	64	24	10	56	42	2

We see the publication of our Strategic Framework as a way of facilitating co-operation between our wide range of stakeholders to promote well-founded confidence in corporate reporting and governance in the UK.

(c) Managing our finances effectively

We explained in section Four of this report that we believe that the cost of our core operating activities is the best indicator of our effectiveness in managing our costs. Section Four explains that our operating costs exceeded the budget by £0.6m in 2006/07 as a result of the AIDB cost award of £1.0m. Excluding the AIDB cost award, core operating costs would have been £0.4m below budget.

Annex A – Directors’ Report and Accounts for the year ended 31 March 2007

Financial Reporting Council Limited – Company number 2486368

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Directors' Report

The Directors have pleasure in presenting their report and financial statements for the year ended 31 March 2007.

Principal Activity

The aim of the FRC is to promote confidence in corporate reporting and governance. The functions we carry out in pursuit of this aim are exercised principally by our Operating Bodies (the Accounting Standards Board, the Auditing Practices Board, the Board for Actuarial Standards, the Professional Oversight Board, the Financial Reporting Review Panel and the Accountancy Investigation and Discipline Board) and by the Council. The Committee on Corporate Governance, whose members are drawn from the Council, assists it in its work on corporate governance. The Operating Bodies and the Council are supported by the FRC's professional staff (the "Executive"). Our organisational structure is shown in Annex C.

Board of Directors

All Directors, with the exception of the Chief Executive, are appointed by the Secretary of State for Trade and Industry.

*Sir Christopher Hogg	Chair
*†The Hon Barbara Thomas Judge	Deputy Chair
Paul Boyle	Chief Executive
*†Tim Breedon	Group Chief Executive, Legal and General
*†Paul Druckman FCA	Chairman, Clear Group
*†Sir John Sunderland	Chairman, Cadbury Schweppes

The Directors who are also members of the Nominations and Remuneration Committees are indicated by * and the Audit Committee are indicated by †.

Under the terms of the FRC's Memorandum and Articles of Association, all Directors are members of the FRC and each has undertaken to guarantee the liability of the FRC up to an amount not exceeding £1. There are no other members and no dividend is payable.

Attendance at Board meetings during the year is shown below, with the attendance shown as a proportion of the numbers of meetings individual Directors were eligible to attend:

Sir Christopher Hogg	7/7
The Hon Barbara Thomas Judge	7/7
Paul Boyle	7/7
Tim Breedon	5/7
Paul Druckman FCA	7/7
Sir John Sunderland	6/7

Committees of the Board

Nomination Committee

The Nomination Committee consists of the Directors of the FRC, other than the Chief Executive, and was chaired by Sir Christopher Hogg. It is responsible for the selection process and succession planning for members and observers of the Council and members of the Operating Bodies. The Committee is also responsible for the oversight of the selection process of the Company's senior management. During the year, the Committee approved 38 appointments and re-appointments to the Council and Operating Bodies including the Board for Actuarial Standards and 3 senior management appointments.

The Nomination Committee met three times during the year. Attendance was as shown below:

Sir Christopher Hogg	3/3
The Hon Barbara Thomas Judge	3/3
Tim Breedon	2/3
Paul Druckman FCA	3/3
Sir John Sunderland	3/3

Remuneration Committee

The Remuneration Committee consists of the Directors of the FRC, other than the Chief Executive, and is chaired by Sir John Sunderland. It is directly responsible for determining and reviewing the remuneration policy for the FRC. It sets the remuneration of the Chief Executive, the remuneration for Chairs and members of the Operating Bodies, and approves the remuneration recommendations of the Chief Executive for the senior management team.

The Remuneration Committee met twice during the year. Attendance was as shown below:

Sir John Sunderland	2/2
Sir Christopher Hogg	2/2
The Hon Barbara Thomas Judge	1/2
Tim Breedon	2/2
Paul Druckman FCA	1/2

Audit Committee

The Audit Committee consists of the Directors of the FRC, other than the FRC Chairman and Chief Executive, and is chaired by Paul Druckman. It is responsible for monitoring the quality and integrity of the accounting, auditing, and reporting practices of FRC Ltd and its subsidiaries. The Committee's purpose is to scrutinise the accounting and financial reporting processes of the Group and Company and the audits of the Group and Company's financial statements. It reviews the qualifications and the performance of the public accounting firm engaged as the independent auditors in the preparation and issue of the audit report on the financial statements. The Committee considers the appointment, compensation, retention and oversight of the independent auditor, making recommendations to the Board on these matters.

The Committee met four times during the year. Attendance was as shown below:

Paul Druckman FCA	4/4
The Hon Barbara Thomas Judge	3/4
Tim Breedon	4/4
Sir John Sunderland	4/4

The FRC is a small organisation with a relatively small proportion of its staff having a role in the financial reporting processes. The Committee has reviewed the need for an internal audit function and concluded that it would be neither necessary nor cost effective for the FRC.

The independent auditor has in the year provided some non-audit services to the FRC. Objectivity and independence has been safeguarded through a robust process to avoid conflicts of interest and requiring the partners and staff of the auditors to declare their independence on an annual basis. The Committee are agreed that the objectivity of the audit engagement partners and audit staff are not impaired.

Following a re-tendering process the Committee agreed during 2006 that Horwath Clark Whitehill LLP should be reappointed as auditors. Horwath Clark Whitehill LLP will be proposed for re-appointment for the financial year 2007/08.

FRC Council

The Council has up to 30 members (including the 6 Directors of FRC Ltd and the Chairs of the Operating Bodies) and in addition a number of observers from other bodies with an interest in the work of the FRC. It has wide and balanced representation from the business, investor, professional and other communities with an interest in corporate reporting and governance.

Staff

The Company values the involvement of its employees in its affairs, policy development and performance. Feedback from staff on Company affairs and performance is encouraged through regular team and staff meetings presided over by their senior manager and the Chief Executive respectively. Staff participate in HR policy development through focus groups and consultation.

The Company recruits staff on the basis of fair and open competition and selection on merit. Applications are invited from suitably qualified people without regard to gender, disability, ethnicity, sexual-orientation, nationality, age or religion. The Company strives towards best practice in its HR policies, and is aware of and tries to ensure a reasonable work-life balance amongst its employees, and strives toward best practice.

The Company appreciates its responsibilities to protect the health and safety of its employees and enhance their potential through targeted training, professional and personal development. The Company regards it as a fundamental right for everyone to be able to work in an environment which is free of harassment and discrimination, and does not tolerate any form of unacceptable behaviour.

Business and Financial Review

The activities of the FRC during 2006/07 and the expected developments in 2007/08 are summarised on pages 1 to 20. Since the FRC is a not-for-profit organisation and does not sell goods or services, the Directors consider that non-financial factors are of greater relevance than financial key performance indicators to an understanding of the performance of the company. An assessment of the performance of the FRC is set out on pages 26 to 34. However, the Directors do attach particular importance to the level of core operating costs as the primary indicator of the FRC's effectiveness in managing its costs. A comparison of core operating costs against budget and against the previous year is shown on page 21.

Total operating expenditure was £15,599,000 (2005/06 £11,893,000). Investigation costs of £14,000 were charged to the Legal Costs Fund during the year (2005/06 £11,000). The Legal Costs Fund may be used only to meet legal, professional and other costs of the FRRP's investigations.

Gross income from publications was £765,000 (2005/06 £822,000). Interest, including interest on the Legal Costs Fund, has been used to offset general operating costs, and amounted to £287,000 before taxation (2005/06 £275,000).

The Company obtained funding for the year from the following organisations:

- Department of Trade and Industry
- Consultative Committee of Accountancy Bodies
- Listed companies
- Actuarial Profession
- Insurance companies
- Pension schemes

Contributions from sponsors under the tri-partite funding arrangement for operating costs and capital expenditure for accounting, auditing and corporate governance amounted to £10,182,000 (2005/06 restated £9,583,000). £153,000 (2005/06 £250,000) of the income relating to capital expenditure, was deferred in accordance with SSAP 4 (Accounting for government grants). £314,000 of the deferred income has been released in year (2005/06 £273,000).

£11,000 was received during the year from sponsors earmarked for the Legal Costs fund as these costs were incurred in 2005/06. As is indicated in Note 7 to the accounts, sponsors' contributions to make good drawings on the Legal Costs Fund are not sought until the financial year following the drawings.

The audit inspection and the investigation and discipline case costs were funded entirely by the relevant CCAB bodies.

Contributions from sponsors under the tri-partite funding arrangement for operating costs and capital expenditure for actuarial standards and regulation amounted to £1,679,000 (2005/06 nil).

There was a surplus for the year on general activities of £117,000 (2005/06 restated £1,263,000). The accumulated surplus at 31 March 2007 was £1,070,000 (2005/06 restated £953,000).

The principal risks and uncertainties facing the company are as follows:

- The continued willingness of funders to contribute to the costs of the Company's activities
- The potential for awards of costs relating to the enforcement activities undertaken by certain of the Company's Operating Bodies.

The Directors keep these risks and uncertainties facing the company under review and believe that appropriate steps to mitigate them have been taken or are planned.

Directors' Emoluments

The Directors' remuneration, with the exception of the Chief Executive, are determined and reviewed by the Secretary of State for Trade and Industry. The total remuneration and benefits excluding pension contributions received by Directors is shown in the table below. Unless indicated otherwise all Directors served throughout each of the two financial years.

	2006/07	2005/06	
	£'000	£'000	
Sir Christopher Hogg	130,000	32,500	(3 months)
Sir Bryan Nicholson	-	75,000	(9 months)
The Hon Barbara Thomas Judge	20,000	20,000	
Paul Boyle	312,783	74,714	(3½ months)
Tim Breedon	15,000	15,000	
Paul Druckman FCA	15,000	15,000	
Sir John Sunderland	15,000	15,000	

The only Director who is entitled to receive pension benefits is the Chief Executive, in respect of whom contributions of £25,707 were paid to a personal pension arrangement.

Other matters

The Company's policy and practice is to make payments to creditors on a weekly basis. No contributions were made for political or charitable purposes. The Company is not listed; consequently there are no directors' shareholdings and no acquisition by the company of its own shares.

We, the Directors listed above, at the date of this report, confirm that, as far as we are aware there is no relevant audit information of which the company's auditors are unaware. The Directors have taken all necessary steps to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

BY ORDER OF THE BOARD



Anne McArthur

Company Secretary

22 May 2007

Statement of Directors' Responsibilities

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The financial statements are required by law to give a true and fair view of the state of affairs of the Company and Group and of the surplus or deficit of income over expenditure of the Group for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of each Company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of each Company and hence taking reasonable steps for the prevention and detection of fraud or other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Group's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Independent Auditor's Report to the Members of the Financial Reporting Council Limited

We have audited the group and company financial statements ("the financial statements") of the Financial Reporting Council Limited for the year ended 31 March 2007 which comprise the consolidated income and expenditure account, the statement of total recognised gains and losses, the group and company balance sheets, the consolidated cash flow statement and the related notes numbered 1 to 22. These financial statements have been prepared in accordance with the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditors

As described in the Statement of Directors' Responsibilities the company's directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view, the financial statements are properly prepared in accordance with the Companies Act 1985 and the information given in the directors' report is consistent with the financial statements. We also report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report, and consider whether it is consistent with the audited financial statements. The other information comprises only the Chair's statement, Chief Executive's Report, Operating Body and Committee on Corporate Governance reports, the reports headed "Expenditure and Funding" and "Performance assessment" and Annexes B to F. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information beyond that referred to in this paragraph.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the group's and the parent company's affairs as at 31 March 2007 and of the group's surplus of income compared to expenditure for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information provided in the directors' report is consistent with the financial statements.

Horwath Clark Whitehill LLP
Chartered Accountants and
Registered Auditors
London
22 May 2007

The Financial Reporting Council Limited
Consolidated Income and Expenditure Accounts
Year Ended 31 March 2007

	Notes	2006/07 £'000	2005/06 <i>Restated</i> £'000
OPERATING EXPENDITURE			
Staff costs	2	9,998	7,470
Other operating charges	4	3,991	3,717
Credit for onerous lease	5 & 17	(315)	(188)
Costs awarded against AIDB	6	988	-
AIDB case costs		923	538
FRRP case costs	7	14	11
Actuarial standards & regulation set-up costs	8	-	345
TOTAL OPERATING EXPENDITURE		15,599	11,893
Income from publications		(765)	(822)
Interest receivable	9	(287)	(275)
Other finance costs	17	42	67
NET OPERATING EXPENDITURE		14,589	10,863
CONTRIBUTIONS FROM SPONSORS FOR:			
Core operating costs	10	10,343	9,606
AIU costs		2,131	1,702
Actuarial standards & regulation costs		1,378	-
AIDB case costs		923	538
FRRP case costs	7	11	-
Actuarial standards & regulation set-up costs	8	-	345
TOTAL CONTRIBUTIONS FROM SPONSORS		14,786	12,191
SURPLUS/(DEFICIT) ON ORDINARY ACTIVITIES BEFORE TAXATION			
Accounting, auditing & corporate governance		200	1,339
Actuarial standards & regulation		-	-
FRRP legal costs fund	7	(3)	(11)
		197	1,328
TAXATION	11	(83)	(76)
SURPLUS OF INCOME OVER EXPENDITURE FOR THE FINANCIAL YEAR			
Accounting, auditing & corporate governance		117	1,263
Actuarial standards & regulation		-	-
FRRP legal costs fund	7	(3)	(11)
	18	114	1,252

The notes on pages 49 to 60 form part of these financial statements.

The Financial Reporting Council Limited
Statement of Total Recognised Gains and Losses
Year Ended 31 March 2007

		2006/07	2005/06
		£'000	<i>Restated</i>
	Notes	£'000	£'000
Surplus for the financial year		114	<u><u>1,252</u></u>
Prior year adjustment	10	270	
Total gains and losses recognised since last annual report		<u><u>384</u></u>	

The notes on pages 49 to 60 form part of these financial statements.

The Financial Reporting Council Limited

Balance Sheets

31 March 2007

	Notes	Group		Company	
		2007 £'000	2006 <i>Restated</i> £'000	2007 £'000	2006 <i>Restated</i> £000
FIXED ASSETS					
Tangible assets	12	1,027	1,199	1,027	1,199
CURRENT ASSETS					
Debtors:					
falling due within one year	13	1,610	1,149	1,610	1,149
falling due after more than one year	13	-	239	-	239
Cash at bank and in hand:					
General	14	2,728	2,888	2,728	2,888
FRRP legal costs fund	14	1,999	2,012	-	-
		4,727	4,900	2,728	2,888
		6,337	6,288	4,338	4,276
CREDITORS:					
Amounts falling due within one year	15	(3,228)	(1,938)	(3,215)	(1,915)
NET CURRENT ASSETS					
		3,109	4,350	1,123	2,361
TOTAL ASSETS LESS CURRENT LIABILITIES					
		4,136	5,549	2,150	3,560
CREDITORS:					
Amounts falling due after more than one year	16	(915)	(1,158)	(915)	(1,158)
PROVISIONS FOR LIABILITIES					
	17	(165)	(1,449)	(165)	(1,449)
NET ASSETS					
		3,056	2,942	1,070	953
CAPITAL AND RESERVES					
Accumulated surplus	18	1,070	953	1,070	953
FRRP legal costs fund	7 & 18	1,986	1,989	-	-
		3,056	2,942	1,070	953

Approved by the Board of Directors on 22 May 2007 and signed on its behalf by:

Sir Christopher Hogg, Chairman

Paul Boyle, Chief Executive

The notes on pages 49 to 60 form part of these financial statements.

The Financial Reporting Council Limited
Consolidated Cash Flow Statement
31 March 2007

	Notes	2006/07 £'000	2005/06 £'000
NET CASH OUTFLOW FROM OPERATING ACTIVITIES	19	<u>(382)</u>	<u>(312)</u>
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE			
Interest received		<u>287</u>	<u>275</u>
TAXATION			
Corporation Tax paid		<u>(78)</u>	<u>(50)</u>
CAPITAL EXPENDITURE			
Cash paid for fixed assets		(153)	(250)
Contributions from sponsors towards capital expenditure		153	250
Proceeds from disposal of fixed assets		-	5
		<u>-</u>	<u>5</u>
NET CASH OUTFLOW BEFORE AND AFTER FINANCING		<u><u>(173)</u></u>	<u><u>(82)</u></u>
DECREASE IN CASH IN THE YEAR	14	<u><u>(173)</u></u>	<u><u>(82)</u></u>
RECONCILIATION OF MOVEMENT IN NET FUNDS			
Net funds at 1 April 2006		4,900	4,982
Decrease in cash in the year		(173)	(82)
Net funds at 31 March 2007		<u><u>4,727</u></u>	<u><u>4,900</u></u>

Net funds consist solely of cash at bank

The notes on pages 49 to 60 form part of these financial statements.

1. ACCOUNTING POLICIES

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Group's financial statements.

a) **Basis of Preparation**

The financial statements are prepared under the historical cost convention and in accordance with applicable United Kingdom Accounting Standards.

b) **Accounts presentation**

In order to reflect more fairly that the Group's expenditure is met by contributions from sponsors, the directors have presented the Income & Expenditure Account to focus initially on the group's net operational expenditure and funding requirement and thereafter on the various contributions received from its sponsors. Further categories have been included to provide a fairer representation of the company's income & expenditure.

c) **Basis of Consolidation**

The consolidated financial statements include the financial statements of the Company and its subsidiaries, after elimination of balances and transactions between members of the Group.

d) **Contributions from Sponsors**

Contributions from sponsors towards general operational expenditure, FRRP legal costs (note 7), AIDB case costs and AIU costs are credited to the Income and Expenditure Account when they become receivable.

Contributions in respect of AIDB case costs and AIU costs are set out at a level which precisely matches the costs incurred in each financial year. The contributions in respect of FRRP legal costs are set at a level which meets the costs incurred in the preceding financial year. The contributions in respect of core operating costs are determined primarily by reference to budgeted expenditure and are likely to differ from the actual expenditure incurred in each financial year.

Contributions from sponsors towards capital expenditure are included as deferred income and are credited to the Income and Expenditure Account over the expected useful life of the relevant tangible fixed assets on a basis consistent with the depreciation policy applied in respect of those assets.

e) **Case Costs**

The legal and professional costs of AIDB and FRRP cases cannot be estimated with reasonable certainty until the investigation is substantially complete. Provision is made to the extent that costs have been incurred at the balance sheet date. Legal and professional investigation costs of FRRP cases are charged to the Legal Costs Fund.

f) Depreciation

Depreciation is provided on all tangible fixed assets at rates calculated to write off the cost, less estimated residual value, over their expected useful lives, as follows:

Office equipment	3 years	straight line basis
Fixtures, Fittings & Furniture	5 years	straight line basis
Leasehold improvements	term of lease	straight line basis

g) Leased Assets

Total rentals payable under operating leases are charged to the Income and Expenditure account over the term of the lease on a straight line basis.

h) Dilapidations

Provision is made for the estimated costs of dilapidation repairs. Estimated costs of removing leasehold improvements are provided and capitalised in accordance with FRS15, such expenditure being amortised over the term of the lease.

i) Deferred Taxation

The Group is only subject to Corporation Tax on its interest receivable and analogous income. There is no timing difference between the recognition of that income in the financial statements and the tax computation, and no timing differences arise. Accordingly, there is no provision for deferred tax.

2. STAFF COSTS (INCLUDING DIRECTORS)

	2006/07	2005/06
	£'000	£'000
Permanent staff:		
Salaries	6,261	4,998
Social security costs	764	595
Other pension costs	378	287
	<u>7,403</u>	<u>5,880</u>
Seconded staff and contractors	1,470	893
Fees to operating body and committee members	957	560
Other costs	168	137
	<u>9,998</u>	<u>7,470</u>

The Group does not operate a pension scheme. Other pension costs comprise payments to personal pension schemes.

The Financial Reporting Council Limited
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Year Ended 31 March 2007

The average monthly number of employees during the year was as follows:

	2006/07	2005/06
	No.	No.
ASB	13	13
AIU	16	13
APB	6	6
FRRP	10	7
POB	9	6
AIDB	4	4
BAS	3	-
Support Services and Corporate	15	13
	<u>76</u>	<u>62</u>

3. DIRECTORS' EMOLUMENTS

	2006/07	2005/06
	£'000	£'000
Fees and salaries (included in staff costs)	508	247

Details of the emoluments of the directors are contained in the Directors' Report on page 41.

4. OTHER OPERATING CHARGES

	2006/07	2005/06
	£'000	£'000
Depreciation (note 12)	325	284
Operating leases (note 1g)		
- office equipment	7	6
- land and buildings	448	448
Gain on disposal of fixed assets	-	(3)
	<u>2006/07</u>	<u>2005/06</u>
	£'000	£'000
The auditors' remuneration is as follows:		
Fees payable to the company's auditors for the audit of the company's annual accounts	7	5
Fees payable to the company's auditors for other audit services to the group:		
The audit of the company's subsidiaries pursuant to legislation	16	14
Total audit fees	<u>23</u>	<u>19</u>
Other services		
- Tax services	3	3
- Payroll services	9	6
Total non-audit fees	<u>12</u>	<u>9</u>

5. CREDIT FOR ONEROUS LEASE

In 2004/05 the company assumed the obligations attaching to the leasehold property formerly occupied by the Accountancy Foundation, whose activities were transferred to the company as from 1st April 2004. This property is no longer occupied by the company and accordingly full provision was made in 2004/05 for the value of future net obligations. The provision was reassessed in 2005/06, resulting in a reduction in the provision of £188,000. In March 2007, the lease at Houndsditch was surrendered to the landlord and a settlement payment was made. In 2004/05 the Department of Trade and Industry (DTI) made an exceptional contribution of £1,000,000 in respect of these lease obligations on a condition that it may only be used for this purpose. As a result of the surrender of the lease, £532,000 became repayable to the DTI. The balance of the provision for the onerous lease was released to the income and expenditure account.

6. COSTS AWARDED AGAINST AIDB

During 2006/07 the AIDB's case relating to certain matters arising out of the collapse of the Mayflower Corporation Plc was completed. In January 2007, the independent tribunal made awards totalling £988,000 in respect of the costs incurred by two of the respondents in the case.

7. FRRP LEGAL COSTS FUND

Contributions have been received to enable the Financial Reporting Review Panel to take steps to ensure compliance with the accounting requirements of the Companies Act 1985, including applicable accounting standards, and to investigate departures from those standards and requirements. Those funds may be used only for this purpose and may not be used to meet other costs incurred by the Group. The Financial Reporting Review Panel may be liable to repay the balance on the Legal Costs Fund to the contributors if it ceases to be authorised by the Secretary of State for Trade and Industry for the purposes of section 245B of the Companies Act 1985.

Since the costs of Review Panel investigations in a financial year cannot be forecast with sufficient certainty, sponsors' contributions to make good expenditure on the Legal Costs Fund are sought in the financial year following the expenditure.

The Financial Reporting Council Limited
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	2007	2006
	£'000	£'000
The fund is represented by:		
Cash at bank and in hand	1,999	2,012
Amounts due from parent company	11	-
Taxation payable	(24)	(23)
At 31 March	<u>1,986</u>	<u>1,989</u>

	2006/07	2005/06
	£'000	£'000
The movements in the fund during the year were as follows:		
Contributions from sponsors	11	-
Costs of Review Panel investigations and legal advice	(14)	(11)
(Deficit) for year	<u>(3)</u>	<u>(11)</u>

8. ACTUARIAL STANDARDS & REGULATION SET-UP COSTS

The costs incurred during 2005/06 in setting up the new regime for setting actuarial standards and overseeing the regulation of the actuarial profession were not covered by existing funding arrangements. It was agreed with HM Treasury to recover these costs through the funding arrangements for actuarial standards and regulation which were consulted upon and finalised during 2005/06. Recovery of £304,000 was made in 2006/07 and the balance will be recovered over the next two years.

9. INTEREST RECEIVABLE

	2006/07	2005/06
	£'000	£'000
Bank interest – general	193	184
Bank interest – FRRP legal costs fund (note 7)	94	91
	<u>287</u>	<u>275</u>

Interest on the legal costs fund is used to offset general operating costs.

10. CONTRIBUTIONS FROM SPONSORS – CORE OPERATING COSTS

Contributions from sponsors towards core operating costs include £314,000 (2005/06 £273,000) of deferred income released in accordance with note 1(d).

The FRC has changed the application of its accounting policy relating to recognition of revenue from sponsors in respect of core operating costs to more appropriately reflect the operation of the funding arrangements under which the various categories of funds contribute specified proportions of the FRC's costs. In previous years, the amount of revenue recognised was adjusted at the end of each financial year so that the amount recognised equalled the specified proportions of the planned level of contributions, which was determined primarily by reference to the budgeted expenditure for the financial year. Following the extension of FRC's responsibilities to include Actuarial Standards and Regulation the Directors have concluded that this policy no longer most appropriately reflects the FRC's practice which is to take any difference between the actual and planned amounts receivable in each financial year into account in determining the target amounts receivable in future years.

The effect of this change has been to increase income from sponsors in 2006/07 by £221,000 compared to the previous accounting policy.

The comparative figures in respect of 2005/06 have been restated to reflect these amendments. As a result, the income for 2005/06 has been increased by £270,000 and other creditors reduced by the same amount, resulting in a corresponding increase in reserves at 31 March 2006.

11. TAXATION

	2006/07 £'000	2005/06 £'000
Corporation Tax at 29% (2005/06: 26%) on general interest received	57	53
Corporation Tax at 25% (2005/06: 25%) on interest received by the FRRP legal costs fund (note 7)	24	23
Adjustment in respect of previous year	2	-
	<u>83</u>	<u>76</u>

Tax is payable only on interest and analogous income.

12. TANGIBLE ASSETS

	Group and Company			
	Leasehold	Office	Fixtures, Fittings &	Total
	Improvements	Equipment	Furniture	
	£'000	£'000	£'000	£'000
Cost at 1 April 2006	655	524	437	1,616
Additions	-	128	25	153
Cost at 31 March 2007	<u>655</u>	<u>652</u>	<u>462</u>	<u>1,769</u>
Depreciation at 1 April 2006	107	212	98	417
Charge for year	66	170	89	325
Depreciation at 31 March 2007	<u>173</u>	<u>382</u>	<u>187</u>	<u>742</u>
Net book value at 31 March 2007	<u>482</u>	<u>270</u>	<u>275</u>	<u>1,027</u>
<i>Net book value at 31 March 2006</i>	<u>548</u>	<u>312</u>	<u>339</u>	<u>1,199</u>

13. DEBTORS

	Group		Company	
	2007	2006	2007	2006
	£'000	£'000	£'000	£'000
Amounts falling due within one year:				
Trade debtors	663	96	663	96
Amount due from subsidiary undertaking	-	-	202	335
Other debtors	613	731	411	396
Prepayments and accrued income	334	322	334	322
	<u>1,610</u>	<u>1,149</u>	<u>1,610</u>	<u>1,149</u>
Amounts falling due after one year:				
Other debtors	-	239	-	239
	<u>-</u>	<u>239</u>	<u>-</u>	<u>239</u>

14. CASH AT BANK AND IN HAND

	Company & Group General Accounts £'000	Group FRRP Legal Costs Fund Accounts £'000	Group Total £'000
At 31 March 2006	2,888	2,012	4,900
Net cash outflow for 2006/07	<u>(160)</u>	<u>(13)</u>	<u>(173)</u>
At 31 March 2007	<u>2,728</u>	<u>1,999</u>	<u>4,727</u>

The amount in the FRRP legal costs fund accounts may be used only for the purposes described in note 7.

15. CREDITORS: amounts falling due within one year

	Group		Company	
	2007	2006	2007	2006
		<i>Restated</i>		<i>Restated</i>
	£'000	£'000	£'000	£'000
Trade creditors	750	283	750	283
Corporation tax payable	81	76	57	53
Due to subsidiary company	-	-	319	283
Accruals	1,041	908	1,041	908
Deferred income	443	302	443	302
Other creditors	913	369	605	86
	<u>3,228</u>	<u>1,938</u>	<u>3,215</u>	<u>1,915</u>

16. CREDITORS: amounts falling due after more than one year

	Group		Company	
	2007	2006	2007	2006
	£'000	£'000	£'000	£'000
Accruals	296	366	296	366
Deferred income	619	792	619	792
	<u>915</u>	<u>1,158</u>	<u>915</u>	<u>1,158</u>

17. PROVISIONS FOR LIABILITIES

Group and Company	Lease Obligations	Leasehold Improvements	Dilapidations	Total
	£'000	£'000	£'000	£'000
At 31 March 2006	1,247	110	92	1,449
Cash payments in the year	(442)	-	-	(442)
Unwinding of the discount	42	-	-	42
Amount repayable to DTI (Credit) to income and expenditure account	(532)	-	-	(532)
	<u>(315)</u>	<u>-</u>	<u>(37)</u>	<u>(352)</u>
At 31 March 2007	<u>-</u>	<u>110</u>	<u>55</u>	<u>165</u>

The provision for lease obligations relates to the matter described in note 5.

Provisions have been made for obligations under the lease at Aldwych House. These are to remove the leasehold improvements and return the property at the end of the lease to its original state and to meet the tenant repairing clause for dilapidations.

18. ACCUMULATED SURPLUS OF INCOME OVER EXPENDITURE FOR THE FINANCIAL YEAR

The Company has taken advantage of the exemption conferred by section 230 of the Companies Act 1985 not to present its own individual income and expenditure account in these financial statements. The Company's surplus for the year was £117,000 (2005/06 £1,263,000). Changes in the Company and Group's capital and reserves were as follows:

	Company & Group	Company & Group	Company & Group	Group	Group
	Accounting, auditing & corporate governance	Actuarial standards & regulation	General Fund	FRRP Legal Costs Fund	Total
	£'000	£'000	£'000	£'000	£'000
At 31 March 2006	683	-	683	1,989	2,672
Accounting policy adjustment (Note 10)	270	-	270	-	270
Restated 31 March 2006	953	-	953	1,989	2,942
Surplus / (deficit) for 2006/07	117	-	117	(3)	114
At 31 March 2007	1,070	-	1,070	1,986	3,056

Contributions from Government in 2006/07 were £3,415,000 (2005/06: £3,100,000).

Differences between the actual and planned contribution receivable from the individual categories of sponsors are taken into account in planning contribution receivable from those sponsors in future years. As at 31 March 2007, the major difference was £221,000 more than planned from the listed companies in respect of accounting, auditing and corporate governance.

19. CASH FLOW STATEMENT - RECONCILIATION OF OPERATING RESULT TO NET CASH (OUTFLOW) / INFLOW FROM OPERATING ACTIVITIES

	2006/07	<i>2005/06</i>
	£'000	<i>£'000</i>
Surplus on ordinary activities before taxation	197	<i>1,328</i>
Interest receivable	(287)	<i>(275)</i>
Depreciation	325	<i>284</i>
Release of deferred income	(314)	<i>(273)</i>
Release of provision or onerous lease	(315)	<i>(188)</i>
Unwinding of the discount	42	<i>67</i>
Provision for dilapidations	(37)	<i>11</i>
(Gain) on disposal of fixed assets	-	<i>(3)</i>
Increase in debtors	(222)	<i>(891)</i>
Increase / (decrease) in creditors and accruals	229	<i>(372)</i>
Net cash (outflow) from operating activities	<u>(382)</u>	<i><u>(312)</u></i>

20. COMMITMENTS

There were no capital commitments outstanding at 31 March 2007 (2006: nil).

At the balance sheet date, the annual commitment for the Group and the Company relating to its Aldwych leasehold property was £448,000. This lease extends beyond five years but there is a tenant's break clause in the lease with effect from August 2009.

Annual commitments for the Group and Company under non-cancellable operating leases other those relating to leasehold property are as follows:

	2006/07	<i>2005/06</i>
	£'000	<i>£'000</i>
Leases which expire within one year	7	<i>6</i>

21. SUBSIDIARY UNDERTAKINGS

Name	Activity
	Contribute to confidence in corporate reporting and governance by:
The Accounting Standards Board Limited ('ASB')	Establishing and improving standards of financial accounting and corporate reporting.
The Financial Reporting Review Panel Limited ('FRRP')	Seeking to ensure that the provision by public and large private companies of financial information and other information falling within its remit complies with relevant reporting requirements.
The Auditing Practices Board Limited ('APB')	Setting standards and giving guidance for: the performance of external audit and other activities undertaken by accountants that result in reports or other output that is published, required by law or otherwise relied on in the operation of the financial markets ("assurance services"); and in relation to the independence, objectivity and integrity of external auditors and the providers of assurance services.
The Accountancy Investigation and Discipline Board Limited ('AIDB')	Providing an independent body to investigate the conduct of members or member firms of the professional accountancy bodies and take disciplinary action in public interest cases – matters which raise or appear to raise important issues affecting the public interest.
The Professional Oversight Board Limited ('POB')	Strengthening the independence and transparency of the regulatory regime for auditing and for the accountancy and actuarial professions.

The activities of these five subsidiaries are undertaken by unincorporated bodies established under the articles of association of each subsidiary. The Board for Actuarial Standards is established as an unincorporated body established under the articles of association of the Company.

22. LIABILITY OF MEMBERS

The members of the Company have undertaken to contribute a sum not exceeding £1 each to meet the liabilities of the Company if it should be wound up.

Annex B – Membership of Council, Operating Bodies and Committees

THE FINANCIAL REPORTING COUNCIL

Chair

Sir Christopher Hogg

Deputy Chair

The Hon Barbara Thomas Judge Chairman, UK Atomic Energy Authority, Deputy Chairman,
Friends Provident

Directors

Paul Boyle Chief Executive, FRC
Tim Breedon Group Chief Executive, Legal and General
Paul Druckman FCA Chairman, Clear Group
Sir John Sunderland Chairman, Cadbury Schweppes

Members

Sir John Bourn KCB (ex officio) Chair POB
Richard Fleck (ex officio) Chair APB
Mike Fogden (ex officio) Chair AIDB
Bill Knight (ex officio) Chair FRRP
Ian Mackintosh (ex officio) Chair ASB
Paul Seymour (ex officio) Chair BAS
Charles Allen-Jones Formerly Senior Partner, Linklaters
John Alty Director General, Fair Markets, DTI
Sir Victor Blank Chairman Lloyds TSB Group plc
Sir David Clementi Chairman, Prudential plc
Sir Don Cruickshank Non Executive Director of Qualcomm Inc
Sir Christopher Gent Chairman of GlaxoSmithKline plc
Baroness Sarah Hogg Chairman, 3i Group plc
Douglas Kerr Group Finance Director, CPL Industries Ltd
Sir George Mathewson CBE Chairman, The Royal Bank of Scotland Group plc
– to 5 October 2006
Colin Perry Chairman, LTE Scientific Ltd
Ian Robertson Group Chief Executive, Wilson Bowden plc, past President ICAI
Hector Sants Managing Director, Wholesale & Institutional Markets,
Financial Services Authority
Vincent J Sheridan Chief Executive, Vhi Healthcare and Deputy President of ICAI
Ed Sweeney Joint Deputy General Secretary, Amicus – to 5 December 2006

Rosemary Thorne Group Finance Director, Ladbrokes plc
 Lindsay Tomlinson Vice-Chairman, Barclays Global Investors
 Graham Ward CBE Senior Partner Global Energy and Utilities,
 PricewaterhouseCoopers LLP
 Tony Watson Director, Vodafone Group plc, Hammerson Group plc,
 Witan Investment Trust and Chairman of M&S Pension Trust

Observers

Richard Dyson Deputy President, ICAEW to 6 December 2006, Chairman, CCAB
 (and President, ICAEW) from 6 December 2006
 Dr Clive Grace CIPFA Council Member and Chairman Supporta plc
 Mary Keegan Managing Director, Government Financial Management,
 HM Treasury

Company Secretary

Michael Lewington to 31 May 2006

General Counsel and Company Secretary

Anne McArthur from 1 June 2006

The number of meetings individual Council members attended out of those which they were eligible to attend was as follows.

Sir Christopher Hogg	4/4	Sir Christopher Gent	1/4
The Hon Barbara Thomas Judge	4/4	Baroness Sarah Hogg	3/4
Paul Boyle	4/4	Douglas Kerr	2/4
Tim Breedon	4/4	Sir George Mathewson	1/2
Paul Druckman	4/4	Colin Perry	4/4
Sir John Sunderland	4/4	Ian Robertson	3/4
Sir John Bourn KCB	4/4	Hector Sants	3/4
Richard Fleck	3/4	Vincent J Sheridan	2/4
Mike Fogden CB	3/4	Ed Sweeney	1/2
Bill Knight	4/4	Rosemary Thorne	4/4
Ian Mackintosh	2/4	Lindsay Tomlinson	3/4
Paul Seymour	4/4	Graham Ward CBE	3/4
Charles Allen-Jones	4/4	Anthony Watson	4/4
John Alty	4/4	Richard Dyson	4/4
Sir Victor Blank	3/4	Clive Grace	3/4
Sir David Clementi	3/4	Mary Keegan	3/4
Sir Don Cruickshank	1/4		

ACCOUNTING STANDARDS BOARD

Chair

Ian Mackintosh

Members

Mike Ashley	Partner, KPMG LLP
Edward Beale	Chief Executive, City Group plc – <i>from 13 March 2007</i>
Marisa Cassoni	Finance Director, John Lewis Partnership
Peter Elwin	Head of Accounting and Valuation Research, JP Morgan Cazenove (Cazenove Equities) – <i>from 4 September 2006</i>
David Loweth	Technical Director, ASB
Roger Marshall	Partner, PricewaterhouseCoopers LLP
Robert Overend	Technical Partner, Ernst & Young LLP
Jonathan Symonds	Chief Finance Director, AstraZeneca plc – <i>to 31 August 2006</i>
Helen Weir	Group Finance Director, Lloyds TSB
Peter Westlake	Nestlé SA. Former UK Head of Research, Deutsche Asset Management
Professor Geoffrey Whittington CBE	Judge Business School, Cambridge University – <i>from 4 September 2006</i>

Observers

Mary Keegan	Managing Director, Government Financial Management, HM Treasury
Geoffrey Dart	Director, Corporate Law & Governance, Department of Trade and Industry
Ian Drennan	Chief Executive, The Irish Auditing and Accounting Supervisory Authority – <i>from 9 February 2006</i>
Bob Garnett	International Accounting Standards Board – <i>from 3 July 2006</i>

Secretary

David Loweth

AUDITING PRACTICES BOARD

Chair

Richard Fleck Partner, Herbert Smith LLP

Members

Prof. Andrew Chambers Director of Management Audit LLP – *from 1 May 2006*
Jon Grant Executive Director, APB
Lew Hughes CB Formerly Assistant Auditor General, UK National Audit Office
Keith Nicholson Partner, KPMG LLP
Ronan Nolan Partner, Deloitte Ireland
Graham Pimlott Chairman of Export Credit Guarantee Department
Minnow Powell Partner, Deloitte & Touche LLP
Will Rainey Partner, Ernst & Young LLP
David J. Thomas Head of Business Risk, Invensys plc
Tom Troubridge Partner, PricewaterhouseCoopers LLP
Stuart Turley Professor of Accounting, University of Manchester
Martin Ward Partner, Dodd & Co – *from 1 May 2006*

Observers

Ian Drennan Irish Auditing & Accounting Supervisory Authority
Richard Leyland Department of Trade and Industry
David Loweth Technical Director, Accounting Standards Board
Richard Thorpe Financial Services Authority

THE BOARD FOR ACTUARIAL STANDARDS

Chair

Paul Seymour Director BGI Endowment Fund II, SCOR Global Life Reinsurance UK Limited

Members

Mike Arnold Principal and Head of the Life Practice at Milliman in London

Nigel Bankhead Director, Actuarial Standards

David Blackwood Former Group Treasurer, ICI Group

Lawrence Churchill Chairman of the Pension Protection Fund and Senior Independent Director at The Children's Mutual and Monkton Group

Harold Clarke Independent General Insurance Consultant, formerly Actuarial Partner at Deloitte & Touche LLP

Christopher Daws Consultant to and Former Financial and Deputy Secretary, Church Commissioners; Trustee, NCH; Trustee – Director NCH Superannuation Fund

Steven Haberman Professor of Actuarial Science and Deputy Dean of Cass Business School, City University

Dianne Hayter Chair of the Consumer Panel of the Bar Standards Board, member of the Board of the National Consumer Council, the Insolvency Practices Council and the Determinations Panel of the Pensions Regulator, and formerly the Vice Chair of the Financial Services Consumer Panel

Julian Lowe Actuarial Director, Aviva GI

Jerome Nollet Corporate Finance Advisor in Risk and Capital management for the insurance industry

Tom Ross Senior Independent Director of Royal London Mutual Insurance Society

Sir Derek Wanless Chairman of the Audit and Risk Committees of Northern Rock plc, Vice Chairman, Statistics Commission

Martin Weale Director, National Institute of Economic and Social Research. Also a Statistics Commissioner and Hon. Treasurer of the Alzheimer's Research Trust

Observers

Peter Askins Head of Policy for Defined Benefit Pension Schemes, DWP

Jim Kehoe Consulting Actuary – representing Groupe Consultatif Actuariel Europeen

Sue Rivas Head of Defined Benefits, Research and Determinations Panel, The Pensions Regulator

Paul Sharma Head of Department for Risk Modelling and Review, FSA

Secretary

Anna Colban *from 1 November 2006*

PROFESSIONAL OVERSIGHT BOARD

Chair

Sir John Bourn KCB Comptroller and Auditor General of the United Kingdom

Members

Richard Barfield Director of Equitas, Umbro plc. Formerly Chief Investment Manager of Standard Life in Edinburgh

Tim Barker Director, Drax Group plc and Electrocomponents plc. Chairman, Robert Walters plc. Formerly Vice Chairman, Dresdner Kleinwort Benson

Anthony Carus Consulting Actuary in private practice and Director, Royal Liver Assurance Limited. Formerly Appointed Actuary, NFU Mutual Life Insurance Society – *from 01 May 2006*

David Crowther Formerly a Senior Partner, PricewaterhouseCoopers LLP, responsible for quality assurance and risk management. Non-Executive Director, TT Electronics plc. Member of the Board of the Financial Ombudsman Service

Hilary Daniels Formerly Chief Executive, West Norfolk Primary Care Trust and Interim Chief Executive, Norfolk Primary Care Trust

Roger Davis Formerly a partner and Head of Professional Affairs PricewaterhouseCoopers LLP. Member of the Competition Commission

Stella Fearnley Professor of Accounting, University of Portsmouth Business School

Paul George Director, POB

Michael Jones Head of Management Services & Administration, Trades Union Congress

Anne Maher Formerly Chief Executive, The Pensions Board for Ireland. Board member of the Irish Auditing and Accounting Supervisory Authority and of Allied Irish Banks plc

Secretary

John Grewe

FINANCIAL REPORTING REVIEW PANEL

Chair

Bill Knight Formerly Senior Partner, Simmons & Simmons

Deputy Chair

Ian Brindle Formerly Chairman, PricewaterhouseCoopers LLP

Members

Daniel Abrams Formerly Chief Financial Officer CDT Inc. – *from 01 March 2007*
Charles Allen-Jones Formerly Senior Partner, Linklaters
Rupert Beaumont Formerly Partner, Slaughter and May
Sir John Bourn KCB Comptroller and Auditor General of the United Kingdom
Stephen Box Formerly Finance Director, The National Grid Group plc
Michael Brindle QC Barrister
David Cairns IFRS Consultant and Visiting Professor, London School of Economics
Anthony Carey Partner, Mazars
Jim Coyle Group Chief Accountant, HBOS plc – *from 01 March 2007*
Jimmy Daboo Partner KPMG LLP. Vice Chairman of KPMG's Global Energy and Natural Resources Practices – *from 01 March 2007*
Richard Delbridge Formerly Group Chief Financial Officer, NatWest Group
Martin Eadon Partner, Deloitte & Touche LLP
Christopher FitzGerald Formerly Chairman, Regulatory Decisions Committee, Financial Services Authority
John Grieves Formerly Senior Partner, Freshfields
Gordon Hamilton Formerly Partner, Deloitte & Touche LLP
Robert Hildyard QC Barrister
Stephen Hodge Deputy Chairman of the Franchise Board & Chairman of the Audit Committee, Lloyds of London. Chairman, Shell Pensions Trust
Alun Jones Formerly Partner, PricewaterhouseCoopers LLP
Mary Keegan Managing Director, Government Financial Management, HM Treasury – *from 01 March 2007*
David Lindsell Partner, Ernst & Young LLP - *from 01 March 2007*
Nigel Macdonald Formerly Partner, Ernst & Young LLP – *to 31 December 2006*
David Mallett Vice Chairman of the Guernsey Financial Services Commission – *to 31 December 2006*

Desmond McCann	Formerly Risk & Quality Partner, PricewaterhouseCoopers LLP
Barbara Moorhouse	Director General of Finance at Department of Constitutional Affairs
Chris Moulder	Partner KPMG LLP - <i>from 01 March 2007</i>
Richard Murley	Managing Director, NM Rothschild & Sons
Richard Pinckard	Partner KPMG LLP, Consumer and Industrial Markets business unit – <i>from 01 March 2007</i>
Brian Pomeroy	Management Consultant, formerly Senior Partner, Deloitte Consulting
Andrew Popham	Partner, PricewaterhouseCoopers LLP – <i>to 28 February 2007</i>
John Reizenstein	Chief Financial Officer, Co-operative Financial Services Limited
George Rose	Finance Director, BAE Systems plc
Rosemary Thorne	Group Finance Director, Ladbrokes plc – <i>to 31 October 2006</i>
Colin Walklin	Chief Financial Officer, Barclaycard
Tony Wedgwood	Formerly Partner, KPMG LLP – <i>to 31 March 2007</i>
<i>Secretary</i>	
Carol Page	Director, Panel Operations

ACCOUNTANCY INVESTIGATION AND DISCIPLINE BOARD

Chair

Mike Fogden CB Deputy Chairman Civil Service Appeal Board, formerly Chairman,
National Blood Transfusion Service

Members

Sarah Brown OBE Reporting Member of the Competition Commission
Chris Lainé Formerly President of ICAEW & formerly Chairman
Allied Textile Companies plc
Elizabeth Llewellyn-Smith CB Formerly Department of Trade and Industry and
Office of Fair Trading, then Principal of St Hilda's College, Oxford
Stuart McKee Corporate Finance Partner, PricewaterhouseCoopers LLP
James Miller Member of the ICAS
Laurance Shurman Formerly Managing Partner, Kingsley Napley and
Banking Ombudsman
David Thomas Corporate Director and Principal Ombudsman of the
Financial Ombudsman Service

Executive Counsel

Cameron Scott

Secretary

Anne McArthur To 31 May 2006
Anna Colban From 1 November 2006

COMMITTEE ON CORPORATE GOVERNANCE

Chair

Sir Christopher Hogg

Members

Charles Allen-Jones
John Alty
Sir Victor Blank
Paul Boyle
Tim Breedon
Colin Perry
The Hon Barbara Thomas Judge
Graham Ward CBE

Secretary

Chris Hodge

ACCOUNTING STANDARDS BOARD COMMITTEES

URGENT ISSUES TASK FORCE

Chair (Non-voting)

Ian Mackintosh Chair, ASB

Technical Director

Hans Nailor Project Director, ASB

Members

Kathryn Cearns Consultant Accountant, Herbert Smith LLP - *from 23 November 2006*

Peter Chidgey Partner, BDO Stoy Hayward LLP

Matthew Curtis Director, Ernst & Young LLP

Una Curtis Professional Standards Director, KPMG, Dublin

Howard Evans Finance Director, Misys plc

Rona Fairhead Chief Financial Officer, Pearson plc – *to 31 August 2006*

Bill Hicks Director, External Financial Reporting, AstraZeneca plc
– *from 14 September 2006*

Peter Holgate Senior Accounting Technical Partner, PricewaterhouseCoopers LLP

Guy Jubb Investment Director, Head of Corporate Governance,
Standard Life Investments

Marion MacBryde Director, Makinson Cowell Ltd

John McDonnell Partner, PricewaterhouseCoopers, Dublin

Geoffrey Mitchell Mizhuo International plc

Christopher Nunn Formerly Professional Standards Partner, Andersen

Brian Shearer Technical Partner, Grant Thornton UK LLP

Andy Simmonds Technical Partner, Deloitte & Touche LLP

Andrew Vials Partner, KPMG LLP

Observers

David Tyrall Accountancy Advisor, DTI – *from 30 October 2006*

Secretary

David Loweth Technical Director, ASB

THE COMMITTEE ON ACCOUNTING FOR SMALLER ENTITIES

Chair

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Ian Mackintosh	Chairman, Accounting Standards Board – <i>from 18 January 2007</i>

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Liam McQuaid	Partner, Duignan Carthy O'Neill
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Dr Richard Roberts	Head of SME Research, Barclays plc

Observer

Valerie Carpenter	Company Law and Investigations Directorate, Department of Trade and Industry
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Secretary

Alan O'Connor	Project Director, ASB
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David Loweth	Technical Director, ASB – <i>from 18 January 2007</i>

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Susan Nyman Director, Grant Thornton LLP
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Graham Pimlott Member of APB
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Simon Edge Compliance Partner, Wales Audit Office
Janet Eilbeck Head of Public Sector Audit, PricewaterhouseCoopers LLP
Russell Frith Director of Audit Strategy, Audit Scotland
Rita Greenwood Executive Director, Finance and Planning, London Borough of Havering
Nigel Johnson Partner, Deloitte & Touche LLP

David Richards	Formerly Principal Finance Officer, National Assembly for Wales
Martin Sinclair	Assistant Auditor General, National Audit Office

Secretary

David Aldous	Audit Commission
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OTHER FRC COMMITTEES

FRC STANDING ADVISORY GROUP ON PROACTIVITY

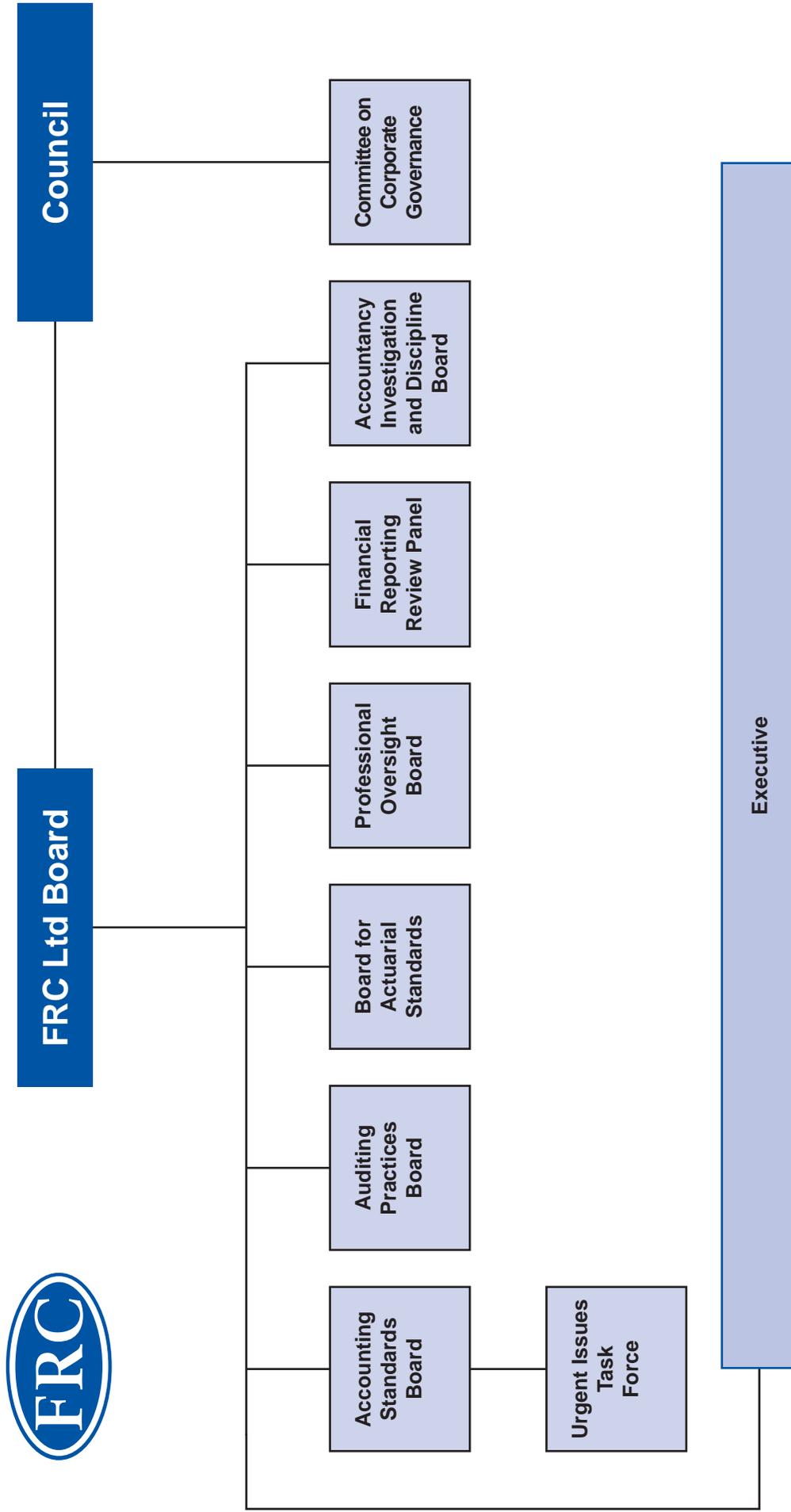
Chair

Bill Knight	Chair, FRRP
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Members

Richard Brumby	Director, UK Charitable funds and Corporate Governance, Credit Suisse Asset Management Limited
Sally Dewar	Director of Markets, Financial Services Authority
Alistair Ross Goobey	Hermes Pensions Management Ltd
Richard Greenhalgh	Formerly Chairman Unilever UK
Michael Izza	Chief Operating Officer, Institute of Chartered Accountants in England and Wales
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David Knox	Managing Director, Cazenove & Co Ltd
Lynn Percy	Technical Partner, KPMG LLP
Vicky Price	Department of Trade and Industry
Dr Andrew Sentance	Monetary Policy Committee, Bank of England

Annex C – Organisational structure



Annex D - Financial Management and Reporting Framework

Our Financial Management and Reporting Framework, set out in our Regulatory Strategy, provides the framework within which we manage and report on the costs of our activities and how they are funded.

Accounting, auditing and corporate governance

The Framework identifies four categories of cost in relation to our responsibilities for accounting, auditing and corporate governance:

Core operating activities - Accounting, auditing and corporate governance

- Core operating activities (accounting, auditing and corporate governance) cover all our activities in relation to accounting, auditing and corporate governance other than audit inspection, disciplinary case and Review Panel case costs.
- The costs of the core operating activities are measured in accordance with applicable accounting standards but the amount of funds raised is adjusted for significant non-cash items, principally depreciation and capital expenditure.
- The funds are provided in equal proportions by the FRC's three sponsors: the accountancy profession (the six major professional bodies); the business community (primarily listed UK companies); and the Government. This is the "tri-partite funding arrangement".
- Our intention is to raise in each financial year the funds expected to be required for that year.

Audit inspection costs

- Audit inspection costs include only the specific and variable costs of the AIU. The AIU's fixed overheads (principally office accommodation and shared IT systems) are included in core operating costs.
- Audit inspection costs are met by the individual Recognised Supervisory boards with which the firms that are subject to inspection are registered.
- Our intention is to raise in each financial year the costs incurred in that year.

Accountancy disciplinary case costs

- Accountancy disciplinary case costs include only the specific and variable costs of cases taken by the AIDB. The other costs of the AIDB (principally staff, accommodation, shared IT systems and other overheads) are included in core operating costs.
- Case costs are potentially volatile from year to year, depending on the number and complexity of cases and, therefore, cannot be subject to firm budgetary limits.

- Case costs are met by the individual participating bodies to which the members or firms that are the subject of each case belong. In the event of disciplinary complaints being brought, the disciplinary tribunals have powers to award costs against those found guilty of misconduct.
- Our intention is to raise in each financial year the costs incurred in that year.

Review Panel case costs

- Review Panel case costs include only the specific and variable costs of cases which the FRRP decides to take to Court or prepares to take to Court. The other costs of the FRRP (principally the staff, office accommodation and shared IT systems) are included in core operating costs.
- Case costs are potentially volatile from year to year, depending on the number and complexity of cases and, therefore, cannot be subject to firm budgetary limits. These costs are met in the first instance from the Review Panel case costs fund, which is then replenished in the following financial year under the tri-partite funding arrangement.

Actuarial standards and regulation

The Framework identifies three categories of cost in relation to our responsibilities for actuarial standards and regulation.

With the agreement of HM Treasury, these costs are met from an annual contribution from the Actuarial Profession (10% of total costs) and a levy on insurance companies (45%) and pension funds (45%) - the actuarial funding arrangements.

Core operating costs - Actuarial standards and regulation

- Core operating activities (Actuarial standards and regulation) cover all of our activities in relation to actuarial standards and regulation other than disciplinary case costs. They include a proportion of our overheads.
- The costs of the core operating activities are measured in accordance with applicable accounting standards but the amount of funds raised is adjusted for significant non-cash items, principally depreciation and capital expenditure.
- Our intention is to raise in each financial year the funds expected to be required for that year.

Actuarial disciplinary case costs

- Actuarial disciplinary case costs include only the specific and variable costs of actuarial cases taken by the AIDB. The other costs of the AIDB (principally staff, accommodation, shared IT systems and other overheads) are included in the two categories of core operating costs in proportion to the relative costs of accountancy and actuarial cases.

- Case costs are potentially volatile from year to year, depending on the number and complexity of cases and, therefore, cannot be subject to firm budgetary limits. We have decided to establish a fund to cover these costs.
- The level of the fund will be kept under review in the light of experience of the number and size of cases.
- The contribution that will be required to maintain the fund at an appropriate level will be reviewed each year. If in one year case costs exceed the annual contribution, the additional cost will be recovered in the following year from insurance companies, pension funds and the actuarial profession in the same proportion as their contributions to the FRC's other costs in relation to the new arrangements.
- Any fine income received or legal costs awarded to the FRC in relation to disciplinary cases will be used to replenish the fund. Should the fund exceed the target level, the excess will be used to meet the FRC's actuarial operating costs, thereby reducing the costs to the funding groups.

Recovery of set-up costs

We incurred set-up costs arising from the need to establish the new arrangements. These costs were approximately £345,000, and we intend to recover them over the first three years of the operation of the new arrangements.

Measuring our effectiveness in managing costs

While we endeavour to ensure that we secure value for money in all our expenditure, the Directors believe that the cost of our core operating activities is the best indicator of our effectiveness in managing our costs.

Reserves

The Directors believe that it is prudent for the FRC to maintain reserves to meet unforeseen expenditure and in recognition of the fact that the FRC has entered into a number of long-term financial commitments.

In relation to our responsibilities for accounting, auditing and corporate governance, the level of reserves in recent years has been between £0.5m and £1.0m but is kept under review by the Directors. The Directors have undertaken to consult on any proposal to vary the level of reserves in the context of the annual Plan & Budget.

A separate reserve will be held in relation to our responsibilities for actuarial standards and regulation, built up from the actuarial funding arrangements. The Directors will keep the level of actuarial reserves under review and will consult on them each year in the context of the annual Plan & Budget.

Annex E - Abbreviations

ACCA	Association of Chartered Certified Accountants
AIDB	Accountancy Investigation and Discipline Board
AIU	Audit Inspection Unit
APB	Auditing Practices Board
ASB	Accounting Standards Board
BAS	Board for Actuarial Standards
CCAB	Consultative Committee of Accountancy Bodies
CESR	Committee of European Securities Regulators
CGU	Corporate Governance Unit
DTI	Department of Trade and Industry
DWP	Department for Work and Pensions
EECS	European Enforcers Co-ordination Sessions
EFRAG	European Financial Reporting Advisory Group
EGAOB	European Group of Auditors' Oversight Bodies
FASB	Financial Accounting Standards Board
FRC	Financial Reporting Council
FRRP	Financial Reporting Review Panel
FRS	Financial Reporting Standard
FRSSE	Financial Reporting Standard for Smaller Entities
FSA	Financial Services Authority
HMT	Her Majesty's Treasury
IAASB	International Auditing and Assurance Standards Board
IAS	International Accounting Standard
IASB	International Accounting Standards Board
ICAEW	Institute of Chartered Accountants in England and Wales
ICAI	Institute of Chartered Accountants in Ireland
ICAS	Institute of Chartered Accountants of Scotland
IEASB	International Ethics Standards Board for Accountants
IFRS	International Financial Reporting Standard
IFRIC	International Financial Reporting Interpretations Committee
IFIAR	International Forum of Independent Audit Regulators
ISA	International Standard on Auditing
LSE	London Stock Exchange
OFR	Operating and Financial Review
PCAOB	Public Company Accounting Oversight Board
POB	Professional Oversight Board
SEC	Securities and Exchange Commission
SIR	Statement of Investment Circular Reporting Standard
SME	Small and Medium sized Enterprises
SSAP	Statement of Standard Accounting Practice
UITF	Urgent Issues Task Force
UK GAAP	UK Generally Accepted Accounting Practices

Annex F - Contact Details

Questions about the Annual Report should be sent to:

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5th Floor, Aldwych House
71-91 Aldwych
London
WC2B 4HN

e-mail: enquiries@frc.org.uk

Telephone: 020 7492 2300
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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.

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