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Financial Reporting Council

Plan 2009/10

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APRIL 2009

# The Financial Reporting Council

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The Financial Reporting Council is the UK's independent regulator responsible for promoting confidence in corporate reporting and governance. In pursuing this aim we contribute towards the achievement of the following outcomes:

**Corporate governance** – UK companies with a primary listing in the UK are led in a way which facilitates entrepreneurial success and the management of risk.

**Corporate reporting** – Corporate reports contain information which is relevant, reliable, understandable and comparable, and are useful for decision-making, including stewardship decisions.

**Auditing and related services** – Users of audit reports can place a high degree of reliance on the audit opinion, including whether financial statements show a true and fair view, and users of audit-related services can place an appropriate degree of reliance on the reports provided.

**Actuarial practice** – Users of actuarial information can place a high degree of reliance on its relevance, transparency of assumptions, completeness and comprehensibility.

**Professionalism of accountants and actuaries** – Clients and employers of professionally qualified accountants and actuaries and of accountancy and actuarial firms can rely on them to act with integrity and competence, having regard to the public interest.

The FRC has also made commitments about its own **Effectiveness** – An effective, accountable and independent regulator, operating in the public interest and actively helping to shape UK, and to influence EU and global, approaches to corporate reporting and governance.

The decision-making bodies are the FRC Board and the Operating Bodies:

**The Accounting Standards Board** issues accounting standards for the UK and Ireland but, with the move to IFRS, is increasingly focussed on influencing the setting of standards by the IASB.

**The Auditing Practices Board** issues standards and guidance for auditing, for the work of reporting accountants in connection with investment circulars, and for auditors' integrity, objectivity and independence. It influences the setting of international standards on auditing by the IAASB.

**The Board for Actuarial Standards** sets technical standards for actuarial practice.

**The Professional Oversight Board** provides independent oversight of the regulation of accountants and actuaries by their respective professional bodies. It provides statutory oversight of the regulation of the auditing profession by the recognised supervisory and qualifying bodies, and monitors, through the Audit Inspection Unit, the quality of the auditing function in relation to economically significant entities.

**The Financial Reporting Review Panel** reviews company accounts for compliance with the law and accounting standards.

**The Accountancy and Actuarial Discipline Board** is the independent investigative and disciplinary body for accountants and actuaries in the UK.

**The Executive**, led by the CEO, provides support to the Board and to the Operating Bodies.

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The following supporting information is available from our website at: <http://www.frc.org.uk/about/plans.cfm>

Section A: Risk assessments and work programme 2009/10

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# One – Introduction

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The Financial Reporting Council is the UK's independent regulator responsible for promoting confidence in corporate reporting and governance.

We promote high standards of corporate governance through the Combined Code, but do not monitor or enforce its implementation by individual boards. We set standards for auditing and actuarial practice and for specific aspects of financial accounting. We monitor and enforce accounting and auditing standards for listed and other major public interest entities. We also oversee the regulatory activities of the accountancy and actuarial professional bodies and operate independent disciplinary arrangements for public interest cases involving accountants and actuaries.

This paper sets out our Plan for 2009/10. It is based on our Regulatory Strategy which explains our role, responsibilities, governance and accountability. The Strategy sets out our regulatory approach and our approach to setting our priorities, which is based on our Strategic Framework. The Framework defines the outcomes which we believe that we and our stakeholders should be working towards to promote confidence in corporate reporting and governance in the UK. The Regulatory Strategy was updated in April 2009 and is available on our website at <http://www.frc.org.uk/about>.

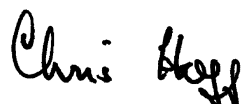
The tougher economic conditions mean that the risks to confidence in corporate reporting and governance are higher than they have been for some years. We recognise that implementing high standards of reporting and governance is more difficult in times of economic stress but in our view it is vital when the number and size of corporate failures are likely to increase. We believe that the risk of failure is likely to be higher for organisations which do not implement high standards of governance, do not apply strong internal controls, and do not keep the market adequately informed about business activities, risks and uncertainties through their financial statements and other reports.

In 2008/09 we issued updates for audit committees, preparers and actuaries on the key questions they might need to address. In 2009/10, the FRC will continue to review and raise awareness of the risks and issue further updates as necessary. We will review market practices in accounting and auditing, and take enforcement action where appropriate. We will consider the impact of our standards in the light of the tougher economic conditions and will, in particular, review the content and application of the Combined Code.

In preparing our Plan in this period of heightened risk, we have sought to take into consideration both the impact of current economic conditions and the medium-term issues affecting corporate reporting and governance, recognising the uncertainty surrounding both the short and medium terms. The Plan reflects our stakeholders' comments on the judgements we have made about our priorities for 2009/10 and on our medium-term priorities.

We will continue to operate on the basis of our commitment to the principles of good regulation. We have been able to identify modest reductions in the total amount which we need to raise from our levy payers compared to the initial proposals which we published in December 2008. Our budget will result in an increase of 5% in our core operating costs in relation to corporate governance, reporting and accounting to £12.5m compared to £11.9m in 2008/09. We have increased our contingency allowance to £0.5m in 2009/10, from £0.3m in 2008/09, to provide an additional degree of flexibility to respond to the heightened risks in confidence in corporate reporting and governance. In relation to actuarial standards and regulation, core operating costs will increase by 4% to £2.3m compared to £2.2m in 2008/09.

We will implement our revised funding arrangements which we consulted on last year. We will publish our finalised levies for 2009/10 in May 2009.



Sir Christopher Hogg, Chair



Paul Boyle, Chief Executive

## Two – Plan 2009/10

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The key themes of our work in 2009/10 will be to:

- Influence market participants to meet high standards of reporting and governance through a combination of measures to raise awareness of major risks, monitor corporate reporting and governance practices, and take enforcement action where appropriate.
- Influence legislators and international standard setters to encourage a proportionate and principles-based approach which promotes high standards of corporate reporting and governance.
- Influence international regulatory authorities to encourage effective co-operation.

### 2.1 Major risks and activities and projects in 2009/10

In developing our annual Plan we focus on the major risks to confidence in corporate reporting and governance based on our assessment of the likelihood that they may materialise and their potential impact. Our planned major activities and projects represent our response to these risks and are intended to make a targeted and proportionate contribution to the achievement of confidence in corporate reporting and governance, taking into account the role of market participants and other agencies.

We recognise that current tougher economic conditions have significantly increased the corporate reporting and governance challenges for boards, preparers of accounts, auditors and actuaries, and that we are publishing our Plan for 2009/10 during a period of volatility in the markets and increased uncertainty in the economy. During this period, risks to confidence in corporate reporting and governance are inevitably heightened.

Table 1 on page 3 summarises what we believe to be the most significant risks arising directly from current conditions and our related major activities and projects for 2009/10. The risks relate to the implementation of high standards of reporting and governance by boards, preparers, auditors, accountants and actuaries. We will keep under review the implications of tougher conditions in implementing these activities and projects. We recognise the potential need for flexibility in our work plan to take account of emerging issues as they arise.

There are a number of significant risks to confidence in corporate reporting and governance which do not arise directly from the tougher economic conditions, but some of which are heightened by these conditions. Table 2 on pages 4-6 summarises what we believe to be the other major risks to confidence in corporate reporting and governance. The two most significant of these risks are the risks to achieving the goal of an effective set of global accounting standards, and the risks arising from the high level of concentration in the audit market. We have shown additional risks which may emerge beyond 2009/10 and how they may be relevant to planning future activities and projects.

We believe that effective action will be taken to respond to most of the risks we have identified. However, there is in our view one significant risk, arising from the high degree of concentration in the audit market, which – although progress is being made to address it – is likely to remain significant in the medium to long term.

**Table 1 – Tougher economic conditions: Significant risks and our related major activities and projects for 2009/10**

Risks	FRC's major activities and projects
<b>Strategic Outcome One - Corporate governance</b>	
<b>UK companies with a primary listing in the UK are led in a way which facilitates entrepreneurial success and the management of risk.</b>	
During a period of volatility and increased uncertainty, boards may find the assessment and management of risk particularly difficult.	Company boards have the primary responsibility for addressing these risks.
Providing adequate information about governance practices may be significantly more challenging for boards in the current environment.	
<b>Strategic Outcome Two - Corporate reporting</b> Corporate reports contain information which is relevant, reliable, understandable and comparable, and are useful for decision-making, including stewardship decisions.	
Current economic conditions may make it more challenging for directors to prepare financial statements which comply fully with the requirements of accounting standards and which show a true and fair view.	Review a risk-based selection of annual and interim accounts and directors' reports. Reviews will focus on the banking, retail, leisure and travel, commercial property and house-building sectors and others which derive significant revenue from the provision of business services such as advertising, media, recruitment and technology.
Current economic conditions may increase the risk of fraud in preparing financial statements.	Keep under review the guidance to audit committees and directors and issue further guidance if appropriate.
During a period of volatility and increased uncertainty, the challenges for directors to describe effectively companies' business models and business risks may increase.	Review narrative reporting in the light of the business review requirements of the Companies Act 2006 and review the need for additional disclosure requirements relating to business models.
<b>Strategic Outcome Three – Auditing and related services</b> Users of audit reports can place a high degree of reliance on the audit opinion, including whether financial statements show a true and fair view, and users of audit-related services can place an appropriate degree of reliance on the reports provided.	
The complexity and volume of risks, including the risk of fraud, arising from the tougher economic conditions may be challenging for auditors to address adequately.	Individual auditors and audit firms have the primary responsibility for addressing this risk.
	Undertake risk based monitoring and report on the quality of audits of publicly traded and other major public interest entities, having particular regard during our inspection work in 2009/10 to audit issues relating to going concern, fair value accounting estimates and disclosures and the impairment of assets including goodwill and other intangibles.  Keep under review the guidance to auditors and issue further guidance if appropriate.
<b>Strategic Outcome Four - Actuarial Practice</b> Users of actuarial information can place a high degree of reliance on its relevance, transparency of assumptions, completeness and comprehensibility.	
Providing information which adequately reflects the uncertainties arising from tougher economic conditions may be challenging for actuaries.	Individual actuaries and actuarial firms have the primary responsibility for addressing this risk.  Keep under review the guidance for users of actuarial information and issue further guidance if appropriate.
<b>Strategic Outcome Five – Professionalism of accountants and actuaries</b> Clients and employers of professionally qualified accountants and actuaries and of accountancy and actuarial firms can rely on them to act with integrity and competence, having regard to the public interest.	
Current economic conditions may increase the pressures on accountants and actuaries to make or accept inappropriately aggressive judgements and take or support inappropriate decisions.	Individual accountants and actuaries and the organisations which employ them, and the accountancy and actuarial professional bodies, have the primary responsibility for addressing this risk.

Table 2 – Other major risks and activities and projects for 2009/10

<b>Strategic Outcome One - Corporate governance</b>	
<b>UK companies with a primary listing in the UK are led in a way which facilitates entrepreneurial success and the management of risk.</b>	
<b>Risks</b>	<b>FRC's major activities and projects</b>
The Combined Code and the 'comply or explain approach' may lose credibility resulting in reduced confidence in corporate governance.	Complete the review of the effectiveness of the Combined Code on Corporate Governance.

<b>Strategic Outcome Two - Corporate reporting</b>	
<b>Corporate reports contain information which is relevant, reliable, understandable and comparable, and are useful for decision-making, including stewardship decisions.</b>	
<b>Risks</b>	<b>FRC's major activities and projects</b>
<b>The goal of a single set of global accounting standards may be undermined if there is a loss in support for the role of the IASB and other standard setters in exercising independent judgement, based on their skills and experience, or by the actions of jurisdictions to carve-out or adapt IFRS, so reducing the quality of their accounting standards.</b>	Promote continued support in the EU for maintaining the IASB and other standard setters' ability to exercise independent judgement in setting accounting standards.
Principles-based standards may be undermined by the inappropriate development of IFRS, towards a more rules-based approach, influenced by intense pressure to achieve the convergence of IFRS and US GAAP.	Continue to influence the development of IFRS during a period in which a large number of important standards are likely to be scheduled for agreement.
Corporate reports may be overly complex and lack relevance.  <i>Beyond the period of the 2009/10 Plan, there is a risk that the proposed actions are not completed.</i>	Finalise our recommendations arising from our review of complexity and relevance of requirements relating to corporate reporting.  <i>Beyond the period of the 2009/10 Plan, we will promote the adoption of the recommendations arising from the review of complexity and relevance of corporate reporting.</i>
Continuing controversy about the extent of fair value accounting undermines confidence in corporate reporting.	Monitor market comment about the use of fair values and influence the IASB projects on measurement and the use of fair values within existing IFRS.

**Note**

- 1) **The risks which we believe are most significant are highlighted in bold**
- 2) *Risks and activities/projects which may be relevant beyond the 2009/10 horizon are shown in italics*

Our risk assessments and the related programme of activities and projects which we propose to undertake in 2009/10 are set out in more detail in our supporting information (section A) which is available on our website at <http://www.frc.org.uk/about/plans.cfm>.



### Strategic Outcome Three – Auditing and related services

Users of audit reports can place a high degree of reliance on the audit opinion, including whether financial statements show a true and fair view, and users of audit-related services can place an appropriate degree of reliance on the reports provided.

Risks	FRC's major activities and projects
<p><b>The high level of concentration in the audit market may result in significant uncertainty and cost in the event of one or more of the Big Four audit firms leaving the market.</b></p> <p><i>Beyond the period of the 2009/10 Plan, there is a risk that the implemented recommendations are not sufficiently effective to reduce the risks arising from concentration in the audit market.</i></p>	<p>Continue to monitor and implement, where appropriate, the recommendations made by the Market Participants Group which aim to enhance the efficiency of the audit markets and to mitigate the risks associated with a major firm leaving the market.</p> <p><i>Beyond the period of the 2009/10 Plan, we will assess the overall effectiveness of the implemented recommendations and consider the need for additional action.</i></p>
<p>Provisions of the Statutory Audit Directive may be difficult to implement cost-effectively.</p> <p><i>Beyond the period of the 2009/10 Plan, we will consider the risks arising from the ending of transitional arrangements for foreign auditors under the Statutory Audit Directive.</i></p>	<p>Continue to work with the EU and BERR to influence the implementation of the Statutory Audit Directive.</p> <p><i>Beyond the period of the 2009/10 Plan, we will review the effectiveness of the arrangements and consider the need for additional action.</i></p>
<p>There is a risk that the changes to the auditing standards may not be effective if they are inherently difficult for auditors to implement in an efficient and/or effective manner.</p>	<p>Implement the decision to apply Clarity ISAs in the UK and Ireland and work positively towards the adoption of Clarity ISAs in the EU.</p>
<p>Regulatory arrangements may be inadequate to facilitate the effective monitoring of firm-wide procedures at firms managed on a global or regional basis.</p>	<p>Contribute to the work of IFIAR and EGAOB and promote effective co-operation between national audit regulatory authorities, in particular gaining an enhanced understanding of the audit networks; and consider the implication for audit quality.</p>

### Strategic Outcome Four - Actuarial Practice

Users of actuarial information can place a high degree of reliance on its relevance, transparency of assumptions, completeness and comprehensibility.

Risks	FRC's major activities and projects
<p>Actuarial standards may not contribute effectively to the reliability and usefulness of actuarial information and advice within the wider regulatory framework for the insurance and pension sectors.</p> <p><i>Beyond the period of the 2009/10 Plan, there will be risks associated with the transition to the new standards and the introduction of Solvency II.</i></p>	<p>Continue to develop a new suite of technical actuarial standards - publishing final standards on data, modelling and reporting, and draft standards on pensions and insurance; and review the implications of the introduction of Solvency II.</p> <p><i>Beyond the period of the 2009/10 Plan, we will review the effectiveness of the new standards and consider the need for additional standards or guidance.</i></p>

**Strategic Outcome Five – Professionalism of accountants and actuaries**

**Clients and employers of professionally qualified accountants and actuaries and of accountancy and actuarial firms can rely on them to act with integrity and competence, having regard to the public interest.**

<b>Risks</b>	<b>FRC's major activities and projects</b>
Failure to agree and implement the changes to the Accountancy Scheme in the next year will leave the AADB facing a substantial risk from costs awards which, in certain circumstances, could impact on the effectiveness of the AADB.	Complete the implementation of changes to the AADB Accountancy Scheme.
The regulatory framework for the enforcement of professional and ethical standards may be incomplete or may not meet the public interest.	Review the effectiveness of the regulatory framework for professional discipline and enforcement of standards, including the FRC's role within the framework.

**Strategic Outcome Six - FRC Effectiveness**

**The FRC is an effective, accountable and independent regulator, operating in the public interest and actively helping to shape UK, and to influence EU and global, approaches to corporate reporting and governance.**

<b>Risks</b>	<b>FRC's major activities and projects</b>
The FRC may not be sufficiently alert to, or be made aware of, relevant developments in the markets or may fail to respond appropriately to those developments.	Review the adequacy of the FRC's arrangements for monitoring emerging events and appropriately prioritise our activities.

## 2.2 Budget 2009/10

The following table shows a summary of our budget for 2009/10. Details of our budget are shown in our supporting information (section B) at <http://www.frc.org.uk/about/plans.cfm>. Our Financial Management and Reporting Framework provides the framework within which we manage and report on the costs of our activities and how they are funded. The framework is available at <http://www.frc.org.uk/about/funding.cfm>.

We expect core operating costs for accounting, auditing and corporate governance to increase by 5%. We have increased our contingency allowance to £0.5m in 2009/10 to provide an additional degree of flexibility to respond to the heightened risks to confidence in corporate reporting and governance. We expect core operating costs for actuarial standards and regulation to increase by 4%. Case costs taken by the AADB are potentially volatile from year to year, depending on the number and complexity of cases and, therefore, cannot be subject to firm budgetary limits.

The budget includes a provisional estimate of costs for those cases which the AADB has formally initiated. If other cases arise they may involve additional expenditure for which no allowance has been made in the budget. In the more difficult economic circumstances it is possible that a larger number of cases may be investigated in 2009/10 than in previous years.

We endeavour to secure value for money in all our expenditure. We intend to operate with approximately the same staffing level (just over 90 staff) over the medium term, i.e. approximately the next three years. We recognise, however, that there is a greater than usual risk that we may need to increase our resources if additional activity is required to address emerging risks.

At the time of publication of this document our financial results for 2008/09 remain subject to audit and are, therefore, described as estimates.

**Table 1 – Budget Summary**

	<b>Budget 2009/10 £m</b>	<b>Estimated 2008/09 £m</b>	<b>Budget 2008/09 £m</b>
<b><i>Accounting, auditing and corporate governance</i></b>			
Core operating costs	12.5	11.8	11.9
Audit inspection costs	2.6	2.2	2.5
Accountancy disciplinary case costs	1.8	1.4	1.3
Review Panel case costs	—	—	—
<b>Total</b>	<b>16.9</b>	<b>15.4</b>	<b>15.7</b>
<b><i>Actuarial standards and regulation</i></b>			
Core operating costs	2.3	2.2	2.2
Actuarial disciplinary case costs	0.5	—	—
<b>Total</b>	<b>2.8</b>	<b>2.2</b>	<b>2.2</b>
<b>FRC total costs</b>	<b>19.7</b>	<b>17.6</b>	<b>17.9</b>

## 2.3 Funding projections 2009/10

The funding requirement primarily relates to our expenditure projections and our intention to maintain our reserves at an appropriate level.

Table 2 summarises our funding projections for 2009/10, including the planned increases in reserves. Table 3 summarises the projected levels of reserves at 31 March 2009 and 2010.

**Table 2 – Funding projections**

	<b>Budget 2009/10 £m</b>	<b>Estimated 2008/09 £m</b>	<b>Budget 2008/09 £m</b>
<b><i>Accounting, auditing and corporate governance</i></b>			
Total expenditure	16.9	15.4	15.7
Increase in general reserves	0.3	—	—
<b>Total</b>	<b>17.2</b>	<b>15.4</b>	<b>15.7</b>
<b><i>Actuarial standards and regulation</i></b>			
Total expenditure	2.8	2.2	2.2
(Decrease)/increase in case cost fund	(0.2)	0.2	0.2
Increase in general reserves	—	—	—
<b>Total</b>	<b>2.6</b>	<b>2.4</b>	<b>2.4</b>
<b>FRC total funding</b>	<b>19.8</b>	<b>17.8</b>	<b>18.1</b>

**Table 3 – Projected level of reserves at 31 March**

	<b>Budget 2010 £m</b>	<b>Estimated 2009 £m</b>	<b>Budget 2009 £m</b>
<b><i>Reserves</i></b>			
FRRP legal cost fund	2.0	2.0	2.0
Accounting, auditing and corporate governance – general	1.2	0.9	0.9
Actuarial case cost fund	0.3	0.5	0.5
Actuarial standards and regulation – general	0.1	0.1	—
<b>FRC total reserves</b>	<b>3.6</b>	<b>3.5</b>	<b>3.4</b>

## Annex - Abbreviations

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<b>AADB</b>	Accountancy and Actuarial Discipline Board	<b>IAASB</b>	International Auditing and Assurance Standards Board
<b>AIU</b>	Audit Inspection Unit	<b>IASB</b>	International Accounting Standards Board
<b>APB</b>	Auditing Practices Board	<b>IFIAR</b>	International Forum of Independent Audit Regulators
<b>BERR</b>	Department for Business, Enterprise and Regulatory Reform	<b>IFRS</b>	International Financial Reporting Standard
<b>EGAOB</b>	European Group of Auditors' Oversight Bodies	<b>ISA</b>	International Standard on Auditing
<b>FRRP</b>	Financial Reporting Review Panel	<b>US GAAP</b>	US Generally Accepted Accounting Practices
<b>FSA</b>	Financial Services Authority		

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For general information about the work of the FRC, please see our website at [www.frc.org.uk](http://www.frc.org.uk). For any further enquiries, please contact us at the above address.

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