Funding the FRC's activities in relation to Accounting, Auditing and Corporate Governance

Feedback Statement and Revised Arrangements

1. Introduction and executive summary

In February 2008 the Government asked us to consult on new funding arrangements based on contributions from market participants (see written Ministerial Statement at Annex A).

In July 2008, we issued a paper consulting on the principles on which our funding for our activities in relation to accounting, auditing and corporate governance should be based and our proposed new funding arrangements.

This paper:

- analyses the responses we received and sets out our feedback on our proposed funding principles (section two), funding groups (section three), the contribution from each group (section four) and the resilience of our financial position (section five)
- indicates the likely impact of the revised arrangements (section six)
- sets out the process we intend to follow to implement the revised arrangements (section seven).

Our proposals

We consulted on the principles that:

- Our funding arrangements should provide a fair, cost-effective and stable basis for us to raise the funds we require to fulfil our statutory responsibilities and promote confidence in corporate reporting and governance in the UK.
- We are committed to securing value for money in all our expenditure, but we believe that the cost of our core operating activities is the best indicator of our effectiveness in managing our costs. We believe that we have consistently met this commitment and that our new governance arrangements will reinforce our commitment to effectiveness and efficiency.
- Our costs should be met by the major groups which are subject, directly or indirectly to our regulatory requirements.

Based on those principles, we proposed that:

- Large private companies and public sector organisations should in future contribute to our costs as additional funding groups - through a levy charged on organisations which prepare financial statements ("the preparers' levy").
- The amounts these groups should be asked to contribute through the preparers' levy should be based on the application of the levy to the entities within each group based on their turnover.

- The benefits of contributions from the two additional groups should be shared equally between our two existing funding groups - publicly traded companies and the accountancy professional bodies.

The responses we received

We received 30 responses to our proposals, all of which we have considered. The 15 respondents who were content for their responses to be published are listed in Annex B. These responses are available on our website at *http://www.frc.org.uk/about/funding*.

A number of respondents noted their general support for the role of the FRC. However, a number of respondents expressed concern about:

i. the withdrawal of the Government contribution
ii. our proposal to base the levy charged to large private companies on their turnover
iii. our proposal to charge the levy on an individual basis to the private subsidiaries of publicly traded companies
iv. the level of the proposed discounts to the levy to be applied to large private companies and public sector organisations
v. our illustrative example of the impact of our proposed approach, which suggested a significant increase in the costs to be met by our existing funding groups when the new arrangements are introduced.

Our decisions

We have considered carefully the consultation responses and have taken them into account as set out in this paper. We have retained the key elements of our proposed approach, and have responded to respondents' main concerns as follows:

i. We have drawn Government's attention to the concerns that were expressed about the impact of the withdrawal of the annual grant.
ii. In the absence of a more appropriate measure, we will retain turnover as the basis for applying the levy to large private companies.
iii. We will change the basis on which we apply the levy on large private companies. Where there is more than one subsidiary within a group we will, whenever possible, calculate the levy on a group basis using the aggregate group turnover. This will mean that groups will benefit from significantly lower marginal levy rates. The effect of this change will, therefore, be to reduce the levy charged to each subsidiary.
iv. We will not change the levels of the discounts to the levy to be applied to large private companies (50%) and public sector organisations (75%) from those proposed, but will keep the levels under review.
v. We intend to take two steps which we believe will ease the transition to the new arrangements both for our existing funding groups and for the new funding groups:

    - We have proposed to BERR that for the purposes of implementing the new arrangements we will plan on the assumption that BERR will substantially reduce the grant to the FRC over the next two years – with grants being paid (at a reduced level) in 2009/10 and 2010/11. BERR has accepted that this is a reasonable planning assumption, although it does not expect to be in a position to formally confirm the level of contribution until the first quarter of 2009.

- We intend to introduce the levy on large private companies on a phased basis. We will apply the levy to private companies with a turnover of £1bn or more from 2009/10; and for private companies with a turnover of £500m or more from 2010/11.

We did not identify any fundamental objections to the approach we proposed. There was broad support for a number of aspects of our proposal. We, therefore, intend that our revised funding arrangements should be introduced from 1 April 2009 for the 2009/10 financial year.

We will update our Financial Management and Reporting Framework, which is published as part of our Regulatory Strategy, as set out in Annex C to reflect the new arrangements.

The likely impact of our revised arrangements

The following table illustrates the likely impact of our revised arrangements for 2009/10.

The table is based on the planning assumptions that our core operating costs increase by 7% compared with 2008/09, that we increase our reserves by £0.3m, and that we receive a Government grant of £2.3m.

Funding groups	**2008/09 Actual**		**2008/09 Example in July consultation paper**		**2009/10 Illustrative example –based on revised funding arrangement**	
	£m	%	**£m**	%	**£m**	%
Existing groups						
Publicly traded Companies	4.2	35	5.1	42	4.6	35
Accountancy professional bodies	4.2	35	5.1	42	4.6	35
Government grant	3.5	30	-	-	2.3	18
Additional groups						
Large private companies	-	-	1.2	11	1.0	8
Public sector organisations	-	-	0.5	5	0.5	4
Total	**11.9**		**11.9**		**13.0**	

It is inevitable that the contributions required from our major funding groups will continue to increase in real terms as the government grant is phased out.

Next steps

We will consult on the rates we propose to apply for the levy in 2009/10 as part of our consultation on our budget for 2009/10. We will publish on our website further guidance on the detailed arrangements for the levy when we consult on our levy proposals.

2. Funding principles

2.1 Funding by market participants

Our proposal

We proposed that our funding arrangements should be based on the principles which we have followed for a number of years:

- Our funding arrangements should continue to provide a fair, cost-effective and stable basis for us to raise the funds we require.
- We are committed to securing value for money in all our expenditure, but we believe that the cost of our core operating activities is the best indicator of our effectiveness in managing our costs. We believe that we have consistently met this commitment and that our governance arrangements reinforce our commitment to effectiveness and efficiency.
- We should continue to consult on the resources we require each year on the basis of our assessment of the current risks to confidence in corporate reporting and governance in the UK and our proposed response.
- Although there are existing powers for our funding to be put on a statutory basis, it is our intention to continue to raise our funds on a non-statutory basis based on the widespread support in the business, investor and professional communities for our work.

We also proposed a new principle:

- Our costs should be met by the major groups of market participants which are subject to, or have regard to, our regulatory requirements and have the primary responsibility for implementing the standards we set or influence, monitor and enforce.

Analysis of responses

The majority of respondents supported the proposed principle that our costs should be met by the major groups of market participants which are subject to, or have regard to, our regulatory requirements.

The majority of respondents suggested that the Government should reconsider its decision to withdraw its contribution to our funding. A number of respondents expressed concern that the withdrawal of the Government grant will increase the risk that the FRC is not seen to be sufficiently independent of the regulated communities.

Some respondents also proposed that we should consider an alternative approach based on defining the beneficiaries of FRC regulation, including investors.

Our decision

We consulted on our proposals on the basis that the Government contribution is primarily a matter for Government to determine and did not, therefore, fall within the scope of our consultation. We have drawn Government's attention to the concerns that were expressed about the impact of the withdrawal of the annual grant.

We believe the FRC's governance arrangements, which have recently been revised, remain appropriate and should enable us to continue to operate effectively as an independent regulator whatever new funding arrangements are put in place. We believe that our governance arrangements reinforce our commitment to effectiveness and efficiency.

As we explained in the July consultation paper, we have considered whether we should raise funds from the main beneficiaries of our regulatory activities, primarily investors, pensioners and policyholders. However, a wide range of groups benefit either directly or indirectly from our work and the population of these groups is very dynamic, making it difficult to clearly identify which groups should contribute. Investors, pensioners and policyholders will in practice contribute through the companies they own or invest in.

Funding principles

We will follow the principles set out in the July consultation paper, including the principle that:

- **The major groups of market participants which are subject to, or have regard to, our regulatory requirements and have the primary responsibility for implementing the standards we set or influence, monitor and enforce, should contribute to our costs.**

Based on this principle:

- **Large private companies and public sector organisations will in future contribute to our costs as additional funding groups through a levy charged on organisations which prepare financial statements ("the preparers' levy").**

2.2 IASB Contribution

Our proposal

We proposed that all the funding groups which prepare financial statements should contribute towards the IASB's costs through the preparers' levy. (At present the UK contribution to the IASB is raised through our business levy.)

Analysis of responses

A number of respondents supported the proposal that funding groups which prepare financial statements should contribute towards the UK share of IASB's costs.

Our decision

It is not intended that the IASB costs should be invoiced separately but will form part of the levy invoice. Collecting the IASB contribution in this way should not involve any additional costs. The amount that the FRC contributes to the IASB is determined through agreement with the IASB and depends on the IASB's costs.

IASB Contribution

The FRC will collect a contribution to the UK share of IASB costs from all those entities which contribute to the preparers levy.

3. Funding groups

3.1 Proposed additional funding groups

Our proposal

In order to replace the Government grant and enable us to continue to discharge our statutory and other functions, we proposed that two additional groups should in future contribute to our costs:

- large private companies
- public sector organisations.

These two groups of preparers of financial statements are subject to, or have regard to, our regulatory requirements and have primary responsibility for implementing the standards we set or influence, monitor and enforce. But they do not currently contribute to our funding. We believe that by seeking a contribution from these additional groups we will spread our costs more fairly.

Analysis of responses

Most respondents supported in principle the proposal to seek contributions from large private companies and public sector organisations.

Some large private companies questioned whether they are market participants by comparison with publicly traded companies and, therefore, whether in principle they should be asked to contribute to our costs.

Most respondents supported the inclusion of public sector organisations as an additional funding group.

Some respondents suggested that we should seek contributions from additional funding groups, including charities and educational institutions and SMEs.

Our decision

The case for including large private companies within the scope of our funding arrangements is that they come within the scope of FRC regulation. In particular, large private companies are required to produce accounts which are subject to audit, and thus come within the scope of FRC regulation.

As set out in our July consultation paper, we do not believe that it would at present be appropriate or cost-effective to seek contributions from the charitable or other not-for-profit sectors.

Funding groups

We will for 2009/10 and future years seek contributions from four funding groups:

- **publicly traded companies**
- **the accountancy profession**
- **large private companies**
- **public sector organisations.**

We will keep under review the question of whether additional groups which are subject, directly or indirectly, to FRC regulation should contribute to our costs.

4. Contributions from each funding group

For the new funding groups, we proposed that we should identify the number and size of individual entities within each group and assess the appropriate contributions from large private companies and public sector organisations by reference to the levy on publicly traded companies which we currently operate.

Respondents raised the following issues in relation to this proposal:

- the proposed level of the discounts for the two groups
- the use of turnover as a measure for the purpose of calculating the levy on large private companies
- the treatment of private companies which form part of a wider group.

Some respondents commented that when calculating future funding requirements, the FRC needed to look at prioritising its work and attempt to cut costs where possible.

4.1 Discounts to be applied

Our proposal

We proposed that:

- A 50% discount should be applied to the levy for large private companies. This reflects the fact that not all our regulatory activities apply to this group. It is in line with the discount we currently apply to all publicly traded companies other than UK companies listed on the London Stock Exchange Main Market.
- A 75% discount should be applied to the levy for public sector organisations. This reflects the fact that not all our regulatory activities apply to this group. It also reflects the fact that the public sector is not directly subject to FRC regulation – though in setting its own accounting and audit standards it has regard to the accounting and auditing standards which we set or influence.

Analysis of responses

The main issues raised by respondents were the proposed discounts to be applied to the levy on large private companies (50%) and public sector organisations (75%). A number of respondents sought more detailed justification for these discounts.

A number of respondents considered that the levels of discounts proposed for the different groups of market participants needed more justification.

Several respondents did not agree that large private companies should pay more than the public sector bodies.

One respondent did not agree that the percentage contribution from the professional bodies should increase, while another respondent felt that increasing the amount of funding by the accountancy bodies could affect the FRC's objectivity in the future.

A number of respondents considered that the public sector contribution was too small.

Our decision

We have based our judgement on the level of discount we should apply on three factors: the extent to which FRC regulation applies to each group; the impact of FRC regulation in terms of the importance of general confidence in standards of governance and reporting for that group; and the need to ensure that our funding arrangements are cost-effective.

For large private companies, we consider that although the extent of FRC regulation is significant, the importance of general confidence in standards of governance and reporting is less salient than for publicly traded companies and it is appropriate to provide a substantial discount on the levy that would otherwise apply.

For public sector organisations, we consider that both the extent of FRC regulation and the saliency of general confidence in standards of governance and reporting is less than for either publicly traded companies or large private companies and that so it is, therefore, appropriate to provide a more substantial discount on the levy that would otherwise apply.

We will not, therefore, change the levels of the discounts to the levy to be applied to large private companies (50%) and public sector organisations (75%) from those proposed in the consultation paper, but will keep the levels under review.

Discounts to be applied

We will explain the discount to be applied for each funding group as part of our annual consultation on our funding proposals. For 2009/10, we propose to apply a discount of 50% to the levy to be applied to large private companies and 75% to the levy to be applied to public sector organisations.

4.2 Basing the levy on large private companies on turnover

Our proposal

We will continue to use market capitalisation as the basis for applying the preparers' levy to publicly traded companies. We proposed that because market capitalisation is not available as a measure of the size of private companies or public sector organisations we should apply the preparers levy to those groups using:

- published data on turnover (or turnover equivalent) for large private companies and public sector organisations which publish appropriate data
- expenditure, for public sector organisations where turnover measures are not available.

Analysis of responses

Some respondents questioned whether turnover would be an appropriate basis for charging the preparers' levy; and suggested that it could lead to an element of double-counting because it would include intra-group trading.

Our decision

We have considered whether there are alternative measures which could be more fairly or consistently applied; but have not identified an appropriate measure. We believe that our proposed treatment of subsidiaries within an individual group (see below) would address the concern in relation to intra-group trading.

Basis for charging the preparers' levy

We will apply the preparers' levy to publicly traded companies on the basis of their market capitalisation.

We will apply the preparers' levy to large private companies on basis of their turnover or, where appropriate arrangements can be put in place, on the basis of the aggregate turnover of eligible companies within a particular group.

We will apply the preparers' levy to public sector organisations on the basis of their expenditure, as the best proxy for economic activity, or on their turnover for organisations where turnover measures are available.

The preparers' levy will apply to the groups of public sector organisations which we identified in our July consultation paper:

Type of body		
Central Government	***Local government***	***Public corporations***
• Departmental Groups • Executive agencies • Foundation Trusts • Primary Care Trusts only	**Local Authorities** • England • Scotland • Wales • Northern Ireland **Police Authorities** • England • Scotland • Wales • Northern Ireland **Fire Authorities** • England • Scotland • Wales • Northern Ireland	• Commercial enterprises controlled by Government • Other public corporations

4.3 Subsidiaries which form part of a group

Our proposal

Our initial proposal was that all the private companies within a group which meet the turnover criterion should pay the levy separately based on their individual turnover - on the basis that FRC regulatory requirements apply directly to each subsidiary.

Analysis of responses

A number of respondents suggested that by including subsidiaries some large private companies would be paying a disproportionately high contribution through multiple invoices.

Our decision

It has become clear that in some cases, because of the number of subsidiaries within a particular group and intra-group trading (which means that the same volume of turnover is booked to a number of different entities within a group), our approach would result in a disproportionately large charge for the group of companies as a whole.

We will, therefore, change the basis on which we apply the levy on large private companies. Where there is more than one subsidiary within a group we will, wherever possible, calculate the levy on a group basis using the aggregate group turnover. This will mean that groups will benefit from significantly lower marginal levy rates. The effect of this change will, therefore, be to reduce the levy charged to each subsidiary.

Treatment of private companies within groups

We will, wherever possible, apply the levy on large private companies on the aggregate turnover of the subsidiaries within a particular group which fall within the size criterion we define (£1bn or more for 2009/10 and £500m or more from 2010/11)

5. The resilience of our financial position

Proposal

We proposed that we should increase the level of our reserves, over time, to a target level of £2m.

Analysis of responses

A number of respondents commented that the level of the reserves was a matter for the FRC Board. Some respondents supported the proposed increase in reserves. Some respondents disagreed with the FRC proposal to increase the reserves without further justification.

Some respondents suggested that it would be helpful to have budget forecasts for the next two to three years. Others noted the FRC's intention to publish three-year forecasts and supported this particularly in light of the proposed changes to the funding arrangements.

One respondent argued that there was a case for the FRC budget to rise given the importance of its international role.

Our decision

We believe that the Government's decision to discontinue its contribution to our core operating costs for accounting, auditing and corporate governance will increase the collection risk in relation to our funding, which is provided on a non-statutory basis by market participants. Additional reserves are required to mitigate the possible effects of this increased risk.

We also believe that the nature of our remit requires us to respond to unexpected developments which affect confidence in corporate reporting and governance. During a period of heightened risk to confidence, it is particularly important to maintain adequate reserves.

FRC reserves

The FRC will continue to consult annually on our budget, which includes the target level of reserves. Our present assessment is that we should establish a target level of reserves of £2.0m, which we should aim to build up to over the next three years.

6. Likely impact of the revised funding arrangements

The following table illustrates the likely impact of our revised arrangements for 2009/10.

We have proposed to BERR that for the purposes of implementing the new arrangements we will plan on the assumption that BERR will substantially reduce the grant to the FRC over the next two years – with grants being paid (at a reduced level) in 2009/10 and 2010/11. BERR has accepted that this is a reasonable planning assumption, although it does not expect to be in a position to formally confirm the level of their contribution until 2009.

The table is, therefore, based on the planning assumptions that that our core operating costs increase by 7% compared with 2008/09, that we increase our reserves by £0.3m, and that we receive a Government grant of £2.3m.

	2008/09		**2008/09**		**2009/10**	
Funding groups	**Actual**		**Example in July consultation paper**		**Illustrative example –based on revised funding arrangement**	
	£m	**%**	**£m**	**%**	**£m**	**%**
Existing groups						
Publicly traded Companies	4.2	35	5.1	42	4.6	35
Accountancy professional bodies	4.2	35	5.1	42	4.6	35
Government grant	3.5	30	-	-	2.3	18
Additional groups						
Large private companies	-	-	1.2	11	1.0	8
Public sector organisations	-	-	0.5	5	0.5	4
Total	**11.9**		**11.9**		**13.0**	

It is inevitable that the contributions required from our major funding groups will continue to increase in real terms as the government grant is phased out.

7. Next steps

We intend to introduce our revised funding arrangements from 1 April 2009 for the 2009/10 financial year.

We will consult on the rates we propose to apply for the preparers levy in 2009/10 as part of our consultation on our budget for 2009/10.

We will publish on our website further guidance on the detailed arrangements for the preparers levy when we consult on our levy proposals.

FRC
25 November 2008

Annex A – Written Ministerial Statement by Gareth Thomas MP: Parliamentary Under Secretary Of State For Trade And Consumer Affairs

6 February 2008

FINANCIAL REPORTING COUNCIL FUNDING

The Financial Reporting Council (FRC) is the UK's independent regulator and standard setter for accounting, auditing and the actuarial profession. The FRC's remit was expanded in 2004 as a result of the Government's review of audit and accounting regulation, and again in 2006 to include actuarial standards and regulation.

The Government believes the FRC has adapted well to its new responsibilities, and in particular welcomes the recent changes it has made to its governance arrangements to increase its effectiveness and efficiency. The Government remains strongly supportive of the FRC. The FRC's operating bodies continue to exercise functions delegated to them by the Secretary of State, and indeed the Secretary of State is in the process of updating the delegation of functions concerning audit regulation in line with the Companies Act 2006 and the Audit Directive.

Corporate reporting and governance in the UK are widely recognised domestically and internationally as being of a very high standard generally. The FRC's integrated and market-led approach to regulation underpins these standards. This approach continues to receive strong support from companies, investors, the accountancy profession and other stakeholders.

For many years the Government contributed one-third of the FRC's core operating costs for its responsibilities for accounting, auditing and corporate governance. However, this position is not consistent with the funding arrangements for other similar regulatory bodies such as the Financial Services Authority and The Pensions Regulator, or with funding for the FRC's actuarial regulation. Nor does it sit well with the FRC's new Board, which is now composed largely of private sector rather than Ministerial appointees. The Government has therefore concluded that, as a market-led regulator, the FRC should in future be funded largely by market participants.

The FRC will consult market participants on the options for new funding arrangements. In order to allow an orderly transition to stable, new, long-term funding arrangements, the Government has confirmed that it will continue to make a substantial contribution to the FRC's costs for at least the 2008/9 financial year.

Annex B - Summary of responses published on the FRC Website

We received a total of 30 responses:

- Four responses from business organisations
- Four responses from large private companies
- Twelve responses from publicly listed companies
- Two responses from investor organisations
- Seven responses from the accountancy and actuarial professional bodies and audit and advisory firms
- One response from a public sector body

Of these, we have published the following 15 responses on our website at *www.frc.org.uk//about*:

- Four responses from business organisations
    - CBI
    - Hundred Group of Finance Directors
    - London Stock Exchange
    - Quoted Companies Alliance (QCA)
- One response from a publicly listed company
    - Unilever
- Two responses from investor organisations
    - Association of British Insurers (ABI)
    - Investment Management Association (IMA)
- Seven responses from the accountancy and actuarial professional bodies and audit and advisory firms:
    - Deloitte & Touche LLP
    - Ernst & Young LLP
    - PricewaterhouseCoopers LLP
    - KPMG LLP
    - Grant Thornton LLP
    - Actuarial profession
    - The Consultative Committee of Accountancy Bodies (CCAB)
- One response from a public sector body
    - Audit Commission.

The remaining respondents requested that their responses should not be published.

Annex C – Updated Financial Management and Reporting Framework

(Updated sections are shaded. The changes will be effective from 1 April 2009)

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.

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 by the our major funding groups:
    - Preparers' of financial statements: publicly traded companies, large private companies and public sector organisations.
    - The accountancy profession: the six major professional bodies.
    - The Government: At present the Government contributes towards core operating activities through a grant-in-aid. However, it has announced its intention to withdraw this contribution. The timing of the withdrawal will be announced in early 2009.
- 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 AADB. The other costs of the AADB (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 on the same basis as the costs of the core operating activities (accounting, auditing and corporate governance).

Actuarial standards and regulation

The Framework identifies two 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 AADB. The other costs of the AADB (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.
- 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.

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.

A reserve is maintained in relation to our responsibilities for accounting, auditing and corporate governance. A separate reserve is 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 reserves under review and will consult on them each year.