Financial Reporting Council

April 2016

Plan & Budget and Levies 2016/17

The FRC is responsible for promoting high quality corporate governance and reporting to foster investment. We set the UK Corporate Governance and Stewardship Codes as well as UK standards for accounting, auditing and actuarial work. We represent UK interests in international standard-setting. We also monitor and take action to promote the quality of corporate reporting and auditing. We operate independent disciplinary arrangements for accountants and actuaries, and oversee the regulatory activities of the accountancy and actuarial professional bodies.

Contents **Page**

Section One - Overview

Our mission

The Financial Reporting Council's (FRC) mission is to promote high quality corporate governance and reporting to foster investment. We encourage companies to produce the trustworthy information necessary for informed investment decisions; and encourage trustworthy behaviour by directors and professionals and engagement with them by investors.

Our role

The FRC is responsible for maintaining codes and standards for corporate governance, investor engagement, corporate reporting, audit and other forms of assurance, and actuarial information. We monitor compliance with corporate reporting and auditing standards. We oversee the accountancy and actuarial professional bodies in their regulatory roles and operate independent disciplinary schemes for accountants and actuaries. Our Financial Reporting Lab helps companies and investors collaborate on improvements to reporting. We represent UK interests in the EU and internationally across a range of issues.

Ultimately it is for boards, companies, auditors, actuaries and other professionals to implement the standards we set. Our role is to support them by reinforcing best practice and challenge them through an effective and proportionate regulatory framework. Across all our activities we seek to act in the public interest.

Our 2016/19 strategy and objectives

In October we published our strategy for 2016/19. Fostering investment and the importance of effective, but proportionate, regulation will guide our priorities over the next three years. We will concentrate on promoting a step change in audit quality and on driving up standards of governance, stewardship and reporting. Our goal is to ensure that reporting and audit in the UK are world-leading in order to give the greatest possible confidence to investors globally, and by doing so help drive growth. We will work closely with companies, investors and the accountancy and actuarial professions to make the most of the changes to codes, standards and regulations introduced in recent years. We will avoid further changes to our codes and standards during the new strategy period as far as possible – not least in relation to the UK Corporate Governance Code. We will also seek to remove regulatory burdens wherever possible. We will remain influential in the EU and internationally and continue to invest in our own skills and capabilities.

Our objectives for 2016/19 build on those we established for our 2013/16 strategy. We will promote:

- Corporate governance and corporate culture that support the long-term success of companies.

- Effective investor stewardship and engagement between companies and investors.
- Clear and concise corporate reporting that meets users' needs.
- High quality auditing in the public interest - using our powers and influence as the UK Competent Authority for audit regulation.
- A framework for overseeing and monitoring actuarial work, underpinned by sound standards.

Our Plan for 2016/17

In December 2015 we consulted stakeholders on our priorities and resources for the first year of the new three year strategy. We are grateful for the responses we received, which are published on our website is at www.frc.org.uk/frcplanandbudget. Our priorities and effectiveness indicators met with broad support. We have made some changes to the funding proposals we published in December 2015 in response to stakeholder feedback and more recent data.

Our priorities for 2016/17 are:

- On audit, our major task is to establish and make the most effective use of the new role we have been given by Government as UK competent authority for audit regulation. This will require particular attention and additional resource in 2016/17. We will seek to ensure that the new framework established under the new Audit Regulation and Directive (ARD) serves the interests of investors in the reliability of financial statements; and that it supports the UK audit profession in delivering statutory audit to the necessary high standards and with close regard to the public interest. Our aim is that by the end of the strategy period at least ninety percent of FTSE 350 audits will require no more than limited improvements as assessed by our monitoring programme.
- On corporate governance, we will focus on good practice, including through our work on corporate culture and promoting effective engagement between boards and investors.
- On corporate reporting, we will focus on embedding recent changes, influencing the development of IFRS, and helping smaller listed and AIM companies with the quality of reporting.
- We will complete our update of the framework for actuarial standards by implementing a standard to cover a broader range of actuarial work and refocusing our specific Technical Actuarial Standards. And we will in 2017 consult publicly on the future of actuarial regulation.

Our budget

We need to ensure that we are adequately resourced to deliver our new responsibilities in relation to audit. It is also important that we have sufficient resources, including adequate reserves, to deliver our other statutory responsibilities and tackle emerging issues of concern to our stakeholders.

Our budget for 2016/17 reflects the new responsibilities we have been given, which will require us to recruit additional people, and the final withdrawal of Government funding.

Assuming that in future we are not given additional responsibilities, we will aim to limit any increase in our annual budgets for the remainder of the strategy period to no more than the average increase in salaries across the sectors from which we recruit.

Our people

We have implemented changes to our executive structure to help us meet the objectives of our strategy for 2016/19 effectively and efficiently. We will continue to invest in the skills and capabilities of all in the FRC; and to recruit, develop and value colleagues with strong leadership and communication skills, as well as the necessary technical skills. An effective approach to driving up standards by working constructively with market participants means continuing to invest in our Financial Reporting Lab, developing similar approaches in other areas, and ensuring good, early communication with companies, investors and the professions on difficult issues.

Sir Winfried Bischoff

Chairman

Stephen Haddrill

Chief Executive Officer

Section Two – Regulatory approach

After completing the changes already in hand we will not seek to change the codes and standards for which we are responsible for at least the remainder of the 2016/19 strategy period, and longer if possible. In particular, we intend to avoid making further changes to the UK Corporate Governance Code in the next three years. We will, however, continue to monitor application of the codes and standards to assess their impact and to identify whether any change is needed.

Our approach to our corporate reporting and audit quality review functions will be developed in the light of the independent review of their effectiveness we commissioned in 2015. The review of our monitoring activity concluded that it is regarded by stakeholders as a force for good. Our work has driven substantial improvements in the quality of reporting and audit, and is seen as a benchmark by regulators in other jurisdictions.

The review identified a number of challenges, including the need to implement our new responsibilities under the ARD, and areas where we could further develop or improve our approach to our monitoring work in line with the experience and expectations of our stakeholders, particularly investors. In response to its recommendations we are taking a number of related actions to:

- Enhance the degree of investor involvement in our work. The review concluded that investors want better to understand the overall findings from our inspection programmes and want more information about our reviews of individual audits and of reports and accounts. We will seek to achieve this through consultation on our procedures and priorities, reporting by audit committees and by communicating more clearly the outcome of our review activity in terms that investors find helpful.

- Establish a regulatory stance that promotes continuous improvement in standards of reporting and auditing. This will be based on a careful analysis of what constitutes good practice, and on identifying and addressing the root cause of problems. We will concentrate primarily on collaborating with market participants, focusing on action that helps companies and auditors improve standards. We believe that our approach will be effective in driving up standards without compromising our ability to take tough action when necessary. As an essential part of our new approach we will continue to consult extensively on our regulatory priorities and procedures.

- Invest in the skills and capabilities of our Audit Quality and Corporate Reporting Review teams to benefit from their combined expertise. Delivering the new regulatory approach will require continuing investment in our knowledge of the sectors and businesses whose reports and audits we review as well as in our technical and communication skills.

- Simplify and standardise our processes to promote greater transparency in the way we operate.

- The review suggested that our new regulatory approach should be supported by certain specific changes. We propose that in future we should pilot naming in advance a small proportion of those reports and audits we intend to review; we should inform companies when their reports have been reviewed and we do not intend to take any further action; and we should make clear our expectation that audit committees should when appropriate report on the outcomes of the FRC's audit quality and corporate reporting reviews.

- Support our new approach by implementing a new strategic stakeholder communications programme, looking at new ways to communicate the outcomes of our work (for example through our annual assessments of the quality of reporting and auditing), and enhancing our ability to gather and analyse large quantities of relevant data.

The lessons from the review have been helpful in considering our regulatory approach across all our responsibilities. We will enhance our collaborative approach by strengthening our engagement with stakeholders. Given the investment focus of our mission we will pay particular attention to our engagement with investors, ensuring that the perspective of long-term investors is reflected in all our work - including our conduct activities - and increasing our outreach to international investors active in the UK market.

We need to take tough action to hold people to account where we determine that this is necessary in the public interest. We will enhance our ability to achieve this through our procedures and sanctions, including the new Audit Enforcement Procedure to be introduced following the implementation of the ARD. We will aim to take any necessary enforcement action in a timely and cost-effective way and will continue to focus on the effective delivery of our disciplinary schemes for public interest cases involving accountants and actuaries. We will aim to complete our investigations under the Audit Enforcement Procedure and disciplinary schemes in two years, from the date on which our Conduct Committee decides to instigate an investigation by Executive Counsel until the service of a Proposed Formal Complaint (under the Audit Enforcement Procedure) or when the case is closed.

Our overall regulatory approach is in line with the Government's initiative to reduce regulatory burdens on business, including the Regulators' Code and the planned Business Impact Target. We will seek opportunities to remove or reduce burdens, subject to the need to pursue our mission effectively and efficiently - and taking account of the strong public interest in maintaining, and where necessary improving, standards of corporate reporting and governance in the UK.

Significant elements of the UK regulatory framework for corporate governance and reporting are determined or influenced by EU or international developments. An important element of our overall regulatory approach is that we should remain influential in EU and international groups. We will contribute to the technical quality of EU and international standard-setting: promoting the importance of regulatory principles, and the benefits of the ‘comply or explain’ approach, rather than detailed prescription. We will continue to work constructively with fellow regulatory authorities in Europe and other jurisdictions to drive improvement in the quality of reporting and auditing.

Section Three – Priorities for 2016/17

This section sets out the specific elements of our three year strategy that will be the focus of our work in 2016/17.

We included in the 2015/16 plan a set of indicators, quantified where possible, that help underpin our assessment of the state of key aspects of corporate governance and reporting in the UK. For the 2016/17 Plan we have included a wider range of indicators. Some of these are activity measures, others relate to outcomes which are influenced by a range of factors, including the impact of the UK regulatory framework.

We will take these indicators, and other evidence, into account in developing and publishing our future annual assessments of the state of corporate governance and stewardship, corporate reporting, and auditing in the UK, and our consideration of the risks associated with actuarial work. We will commission survey evidence of stakeholders' perceptions of key aspects of corporate reporting and governance in the UK and of our own effectiveness as a regulatory authority.

Corporate governance

The FRC sets the UK Corporate Governance Code. The Code is based on the underlying principles of good governance including the exercise of judgement, accountability, transparency, probity and a focus on the sustainable success of an entity over the long-term. It includes a clear principle that boards should provide annual reports and accounts that present a fair, balanced and understandable assessment of the company's position and prospects.

Our overall objective for our 2016/19 strategy will continue to be to promote corporate governance and corporate cultures that support the long-term success of companies.

In 2015 we launched a market-led initiative to gather practical insight into corporate culture and the role of boards to understand how boards can shape, embed and assess culture and to identify and promote good practice. We have created a broad coalition of stakeholders to provide diverse input into the debate. During 2016/17, we will publish a report of our observations, identify good practice and develop practical and market-led 'how to' resources. Our aim is to help boards, across a broad range of sectors and industries, take effective action on culture.

Following on from that we will also replace the FRC's Guidance on Board Effectiveness with new material that has culture at its heart, to support the application of the principles in the UK Corporate

Governance Code. We have published a discussion paper – 'UK Board Succession Planning' – seeking views on board succession for both executives and non-executives in order to support a suitably talented, diverse pipeline of directors ready to serve on the boards of UK listed companies. We will publish feedback early in 2016/17.

We are currently consulting on limited changes to the UK Corporate Governance Code linked to the implementation of ARD and we will finalise these ahead of ARD implementation in June 2016.

There are many factors influencing the quality of corporate governance. We have identified a number of indicators which, taken together, will contribute to our annual assessments over the period of our 2016/19 strategy. Our indicators focus on FTSE 350 companies. We note the comments from stakeholders on the importance of good governance for smaller companies, and on the need to interpret data on compliance with the Code with proper regard to the 'comply or explain' approach.

Indicators

% of FTSE 350 companies stating that they have met all or all but one or two of the UK Corporate Governance Code's provisions; and our assessment of the quality of explanations where companies have chosen not to meet particular provisions

% of listed companies providing a clear, broad and longer term view of risk management, internal control and viability in line with the changes to the Code introduced in 2014.

The headline figure for female directorships in FTSE 350 companies.

The quality of reporting by audit committees on corporate reporting and audit quality matters and on FRC regulatory interventions.

Relevant evidence of greater focus on the importance of company culture from surveys by market commentators.

Investor stewardship

The FRC sets the UK Stewardship Code. This Code sets out the principles of effective stewardship by institutional investors, which help build confidence in the system and give force to the 'comply or explain' approach as well as increasing accountability to clients and beneficiaries.

During 2016/19, our overall objective will be to promote effective investor stewardship.

Effective investor stewardship supports the long term success of companies, delivering sustained benefits to their shareholders. We are seeking an improvement in the extent and quality of engagement; for asset managers to be more accountable to their clients, who should in turn generate the demand for stewardship; and for proxy advisers to be more accountable for the quality of their advice.

During 2016/17, we will:

- Focus on promoting effective investor engagement, including by monitoring reporting by Stewardship Code signatories and encouraging advisers and intermediaries to help to facilitate engagement.
- Implement those parts of the EU Shareholders Rights Directive for which the FRC is responsible in a way that minimises costs for companies and investors.
- Continue to publish our annual assessment of the quality of engagement. We will reflect both our assessment and independent survey evidence; and will look at a number of indicators.

We have recently announced how we intend to scrutinise adherence to the Stewardship Code, encouraging asset managers and owners to provide better accounts of their stewardship policies and practices. We will scrutinise reporting and other action by signatories, and subject to giving signatories time to consider and take action where necessary - will issue a public statement on those who have met Code requirements and those who have not.

In the light of this approach, and informed by the feedback we received in response to the Draft Plan, we will draw on the following indicators.

Indicators

Survey evidence of the extent to which asset owners are satisfied with the standard of reporting from asset managers.

Evidence of the impact of FRC scrutiny of statements by UK Stewardship Code signatories.

Survey evidence of the extent and effectiveness of companies' engagement with investors.

Corporate reporting

We promote clear and concise reporting that is fair, balanced and understandable. This has included publishing guidance on the Strategic Report, reports on our reviews of corporate reports and accounts, and the work of the Financial Reporting Lab. Our aim is to encourage all those involved in the financial reporting process to focus on communication and the clear presentation of information that is material and relevant, including in relation to the longer-term viability of the company.

Our overall objectives for our 2016/19 strategy will be to promote clear and concise reporting that meets users' needs and high quality and relevant standards coming from international standard-setters.

In pursuing our strategy we will direct our corporate reporting review work towards encouraging improvements in the quality of reports and accounts, and increase the transparency of that element of our work. We will continue to consult on any associated changes to our Corporate Reporting Review Operating Procedures.

We will provide thought leadership on how reporting frameworks should respond to technology and the developing interests of investors and other stakeholders.

We will continue to influence EU and international developments, consulting a wide range of UK interests and engaging with our fellow regulators in the UK and overseas.

During 2016/17 we will:

- Undertake and report on our annual programme of reviews of corporate reports. We will direct our reviews at companies of economic significance where a material misstatement could have implications not just for the individual company but for confidence in the market as a whole. We plan to undertake 250 reviews during the year. Our priority sectors will be the extractive industries and companies servicing extractive companies, companies servicing the public sector, and media businesses.

- Undertake a targeted review of tax disclosures. We will share what we observe to be best practice; our aim will be to stimulate improvements in this area of corporate reporting.

- Follow up the FRC's project to improve the quality of reporting by smaller listed and AIM traded companies. This will include issuing an annual reminder to smaller quoted companies at the start of the reporting season to foster improved quality in areas of particular importance to investors such as the Strategic Report, accounting policies, estimates and judgments and cash flow statements; and targeting participation by smaller quoted companies in Lab projects and in the clear and concise reporting initiative.

- Continue to influence EU and international developments. This includes: contributing to the work of the International Accounting Standards Board (IASB)/ IFRS Foundation; direct involvement in the European Financial Reporting Advisory Group and the European Securities Markets Authority; influencing developments in IOSCO; and contributing to the development of integrated reporting. During 2016/17 we will continue to influence the IASB's agenda and work on its Conceptual Framework and its standards on financial instruments, leasing and insurance. We will continue to promote prudence and stewardship as cornerstones of the IASB's work.

- Continue to support the FRC's 'Clear & Concise' initiative through Financial Reporting Lab case studies and other work. We will aim to identify reporting practices that investors find helpful, relating to both the content and presentation of corporate reporting information. In particular, we will:

  - Deliver the Lab's project report on Business Model reporting, and build on this through work on disclosure of principal risks, and viability statement reporting.

  - Develop the Lab's project on the Digital Future, working with market participants.

  - Assist BIS and develop our Strategic Report guidance in the UK implementation of the Non-Financial Reporting Directive.

  - Carry out research on the role and scope of preliminary reports.

  - Input to actions from the EU Capital Markets Union (CMU) focused on standards and reporting requirements of growing smaller companies.

We will in future publish an annual assessment of the quality of UK corporate reporting, based on the evidence we gather through the various aspects of our work and evidence from our stakeholders. This assessment will include our findings from our corporate reporting reviews.

We are developing a set of indicators aligned with our strategic objectives. Our starting point is:

Indicators

Evidence from our corporate reporting reviews, including (a) the quality of reporting by large public companies and (b) by smaller listed and AIM traded companies.

Our assessment of the impact of the Lab's initiatives on corporate reporting.

Our views on the development and impact of international standards.

The outcome of our thematic reviews.

Evidence on the quality of reporting from surveys by market commentators.

Audit and Assurance

Audit underpins public confidence in corporate governance and reporting by UK companies. Since the financial crisis, the FRC has introduced measures to enhance confidence in the quality of audit and increase the value of auditor reporting to investors. The measures include retendering, enhanced and extended auditor and audit committee reporting, and increased transparency of the results of the FRC's audit quality reviews. It is essential that within audit firms there is a culture of commitment to delivering consistent and rigorous audit quality.

Our overall objectives for our 2016/19 strategy will be to implement fully the Audit Regulation and Directive, and to secure improvements in audit quality in line with our strategic goal. Our aim is that by the end of the strategy period at least ninety percent of FTSE 350 audits will require no more than limited improvements as assessed by our monitoring programme.

In September 2015 the FRC published a consultation on revisions to Ethical and Auditing Standards, and related Guidance on Audit Committees. The proposals include:

- A revised Ethical Standard for audit and other public interest assurance engagements;
- Revised quality control and auditing standards and guidance, which address UK and Irish legislation and cultural and business issues.

- Revised ‘Guidance on Audit Committees’, to take account of amendments to the UK Corporate Governance Code, and of recommendations put forward by the Competition and Markets Authority (CMA) - many of which coincide with amendments made by the ARD.

We expect to publish the finalised documents in May 2016 together with a Feedback Statement noting the broad support for our proposals. The changes will apply to financial periods beginning on or after 17 June 2016, the implementation date for the ARD.

We will direct our audit quality review activities in line with our new regulatory approach - focusing more strongly on identifying and promoting good practice and on supporting innovation by the audit profession.

During 2016/17 we will:

- Continue our statutory oversight of the regulation of auditors by the Recognised Supervisory Bodies, amending our approach where necessary to reflect our new responsibilities as the competent authority under the ARD.

- Implement the ARD with a clear delineation of responsibility between the FRC and the professional bodies.

- Monitor and report on the quality of around 140 individual engagements. Where poor quality audit work is identified we will make use of our regulatory powers to impose appropriate sanctions. We will pay particular attention to the quality of first year audits, revenue recognition policies, tax provisioning, and the audit of IT controls. We will implement the CMA recommendation that all FTSE 350 audits should be inspected on average once every five years.

- Extend our thematic reviews, which allow us to drill deeper into specific audit risk areas. In 2016/17, we will undertake thematic reviews of firms’ quality review processes, the use of data analytics on audits, and firms’ root cause analysis of the findings from internal and external monitoring.

- Plan to undertake monitoring of smaller audit firms auditing Public Interest Entities (PIEs) to meet the requirements of the ARD.

- We will also continue our statutory oversight of the Recognised Qualifying Bodies. Education and training of auditors is an area of rapid change and we need to ensure that the statutory requirements continue to be met.

- Commence our responsibilities under the Local Audit and Accountability Act for the oversight of supervisory bodies recognised for this purpose and for monitoring the quality of local audit reporting. For some local public entities the Act will become effective from 1 April 2016.

- Continue to register non-EU auditors of non-EU issuers listed on regulated UK exchanges who meet the requirements of the Statutory Audit Directive.

- Assess the impact of recent changes in extended audit committee and auditor reporting, which focus on making the audit more transparent. We will assess the consequences of retendering and rotation, in particular whether firms are competing on quality and innovation. In doing so we will engage more with audit committees and investors - including through the reporting of our audit inspection findings and the practice aids we published in May 2015, over which were designed to assist audit committees in assessing audit quality.

- Consider the most effective and proportionate way to respond to the challenge of delivering high quality audit of SMEs.

- Support the important role of audit firm and network firm culture in promoting audit quality - including by issuing a revised Audit Firm Governance Code.

- Continue to take a leading role in EU and international regulatory networks, reflecting the international dimension to many audits - including the International Federation of Independent Audit Regulators and the new Committee of European Auditing Oversight Bodies.

- Contribute, with the International Audit and Assurance Standards Board, to the development of international standards for auditing.

We will also consider the consequences of the post-ARD arrangements for our non-statutory oversight of the accountancy profession and the disciplinary scheme we run for its members, including members of the accountancy profession in business in non-audit roles.

We will in future issue an annual assessment of the quality of audit in the UK. This will be broader in scope than our current annual report on our monitoring activity. It will include our assessment of the quality and usefulness of audit from an investor perspective, the impact of our new role under the ARD, and views on the current state of the audit market. We will include the following indicators of progress in enhancing audit quality:

Indicators
The findings from the FRC's annual audit quality review activities.
Progress towards our aim that by the end of the strategy period at least ninety percent of FTSE 350 audits will require no more than limited improvements as assessed by our monitoring programme.

A further survey of views on the quality of audit following on from the 2013 benchmark YouGov survey, 'Improving Confidence in the Value of Audit' (https://www.frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Research-Report-Improving-Confidence-in-the-Value.pdf)

A survey of audit committee chairs' views of audit quality.

Survey evidence of the impact of auditor retendering; of enhanced and extended auditor and audit committee reporting; and of increased transparency of the results of the FRC's audit quality inspections.

Actuarial work

Actuarial work is central to many financial decisions in insurance and pensions and is an important element in other areas requiring the evaluation of risk and financial returns. High-quality actuarial work promotes well-informed decision-making and mitigates risks to users and the public.

The FRC sets technical actuarial standards and oversees the regulatory activities of the Institute and Faculty of Actuaries (IFoA).

During 2016/19, our overall objective will be to promote actuarial work that is underpinned by sound standards.

The Joint Forum on Actuarial Regulation (JFAR) was established in 2013 by the FRC, the IFoA, the Financial Conduct Authority (FCA), the Prudential Regulation Authority (PRA) and The Pensions Regulator to coordinate the identification of, and response to, public interest risks to which actuarial work is relevant.

During 2015/16, we have published a new framework for Technical Actuarial Standards. The FRC agreed that TAS 100 will now be introduced at the same time as revisions to the FRC's Specific TASs, currently covering insurance, pensions, transformations, and funeral plans.

During 2016/17 we will:

- Complete our work on the new framework of Technical Actuarial Standards; seeking thereafter to maintain the framework in response to identified emerging risks and changes in the regulatory environment. We will work with the IFoA and the JFAR on risk identification, monitoring and mitigation, taking the steps set out in our 'Risk Perspective'. We will report on the feedback we have received.

- Collaborate with the IFoA and other bodies to develop guidance designed to promote high quality actuarial work.

- Ensure that our oversight role adds value. We will contribute to the IFoA's regulatory projects, which include reviews of its ethical code and its implementation of standards for quality assurance and work review; and will provide independent challenge to the IFoA's regulatory strategy and processes.

- Continue to influence international standard-setting bodies and regulators.

Later in 2016/17, we will consult on the future of actuarial regulation, including whether independent oversight of the actuarial profession remains necessary and appropriate. We will take account of the response to our updated standards and other developments - such as regulatory change in insurance and pensions and the introduction of independent standards since the current regulatory arrangements were established in 2006.

A key measure of our effectiveness will be to ensure that our new standards are issued in 2016 and are implemented in 2017. In assessing the broad outcomes we promote through our standards we will consider the following indicators.

Indicators

JFAR 'Risk Perspective' updated and shows an improving trend through coordinated efforts.

Feedback on the new TASs.

The evidence from our consultation on the regulatory framework for actuaries.

Enforcement

The FRC is currently (April 2016) consulting on proposals for the Audit Enforcement Procedure, developed to implement our forthcoming responsibility for audit enforcement. This is intended to deal with the full range of audit enforcement within the terms of the ARD and will apply to the investigation and sanctioning of breaches of the various requirements of the statutory audits of Public Interest Entities (PIEs) and any other cases retained by the FRC. The procedure will, in relation to statutory audit cases, replace the FRC's Accountancy Scheme and the Auditor Regulatory Sanctions Procedure and provide a single, administrative procedure for audit enforcement The FRC will delegate the vast majority of investigation and sanctioning of non-PIE cases to the professional bodies.

During 2016/17, we will consider the implications for accountancy disciplinary cases that do not involve audit. We will make further progress in closing or concluding disciplinary cases.

In developing the arrangements for managing case costs under the new Enforcement Procedure the FRC will build on its experience of operating the current independent disciplinary schemes for accountants and actuaries. In particular it will consider establishing for cases addressed through the new procedure – and, potentially, for non-audit accountancy cases – a 'case costs fund'. This would be comparable to the fund currently maintained to help manage the costs of actuarial disciplinary cases. In developing this consideration the FRC will consult appropriately on the basis on which a fund should be established and maintained, and the source of funds – taking into account the implementing legislation for the Audit Regulation and Directive, the terms of which are currently under consideration.

Section Four - Budget and Funding 2016/17

Our annual budget sets out the resources we need to carry out our responsibilities for the year. The budget for 2016/17 reflects the new regulatory responsibilities we will be given as the competent authority for audit.

Expenditure

Moving forward we will determine the key elements of our budget aligned to our re-scoped responsibilities. The key elements are:

- Separate audit, corporate governance and reporting, and actuarial activities.
  - Audit activities include our programme of audit quality reviews, including those we carry out for other authorities (which we present separately given the established practices for its funding), oversight of the relevant professional bodies, and standard setting.
  - Corporate governance and reporting activities encompass our work on the UK Corporate Governance and Stewardship Codes, financial reporting standard-setting, influencing IFRS, and our programme of corporate reporting reviews.
  - Actuarial activities include setting technical actuarial standards, oversight of the profession, and actuarial enforcement cases.
  - The cost of central functions is allocated to audit, corporate reporting and governance, and actuarial activities on a pro rata basis.

- Enforcement - that is the costs of investigating and prosecuting cases in connection with audit, accountancy and actuarial matters (case costs).

In our draft budget we set out an initial allocation of our core operating costs between our audit and non-audit responsibilities based on our judgement of the future scope of our ARD responsibilities. We are now in a better position to assess that allocation. During 2016/17 we will further review our expenditure and funding arrangements to reflect our new responsibilities under the ARD.

Expenditure £m	Budget 2015/16	Expected 2015/16	Budget 2016/17
Core Operating Costs – Audit activities	9.8	9.8	10.4
Audit Quality Review	5.4	4.9	5.3
Audit Enforcement case costs	5.8	3.4	4.2
Total Audit	**21.0**	**18.1**	**19.9**
Core Operating Costs – Corporate Governance and Reporting	9.9	9.7	11.1
Core Operating Costs - Actuarial	1.2	1.1	1.2
Accountancy Enforcement case costs	1.2	0.7	0.8
Actuarial Enforcement case costs	0.4	0.1	0.5
Total Corporate Governance and Reporting	**12.7**	**11.6**	**13.6**
Overall Total	**33.7**	**29.7**	**33.5**

Excluding case costs, which are variable, the budget for 2016/17 provides additional resources of £1.0m to support our new role as the UK competent authority for audit regulation compared to the 2015/16 expected result. This includes an additional £0.4m for our audit quality review activities, which is staff related, and £0.6m for core costs, again mainly due to additional staff plus increased overhead allocation of £0.2m.

The budget provides additional resources of £1.5m for our other work in corporate governance and reporting compared to the 2015 expected result. This includes an additional £0.7m for our corporate reporting review activities, to bring our resources up to the budgeted level in 2015/16 that is required to deliver the 250 case reviews, and to implement the recommendations of the 2015 review of the effectiveness of our monitoring work. Staff costs across the other parts of the Corporate Governance and Reporting Division are £0.3m higher and the amount allocated to overheads is £0.5m higher.

Actuarial enforcement case costs are expected to be higher by £0.4m as we expect one case to reach tribunal stage during 2016/17.

The allocation by type of expenditure is as follows:

Expenditure £m	Budget 2015/16	Expected 2015/16	Budget 2016/17
Staff costs	18.6	18.0	20.1
Directors fees	1.5	1.4	1.5
Facility costs	1.8	1.8	1.9
IT & Website	0.8	0.7	0.8
Travel & conferences	0.7	0.6	0.8
Recruitment	0.3	0.4	0.5
Training	0.3	0.3	0.4
Legal, professional & audit	1.2	1.3	1.0
Research	0.2	0.1	0.2
Other costs	0.9	0.9	0.8
Total	**26.3**	**25.5**	**28.0**
Audit & Accountancy Enforcement case costs	7.0	4.1	5.0
Actuarial Enforcement case costs	0.4	0.1	0.5
Total	**7.4**	**4.2**	**5.5**
Overall Total	**33.7**	**29.7**	**33.5**

Staff costs, the largest item, will increase in 2016/17 as we complete the process begun in 2015/16 of recruiting additional staff to deliver our new responsibilities as single competent authority under the ARD, and implement our new approach to our corporate reporting and audit quality monitoring activities. Some of the recruitment took place across 2015/16 (10 roles, of which 5 are audit related). More will be needed in 2016/17 (a further 10 roles, of which 8 are audit related).

The budget also includes a pay award for all staff of 2.5%, a level we feel necessary to allow us to retain and recruit the staff needed to deliver our regulatory responsibilities

Funding

The chart below sets out our funding requirement for 2016/17. The Government no longer contributes to our funding.

		2015/16 Expected				2016/17 Budget		
Funding provided by:	Activity Funded	**Audit**	**Other**	**Total**		**Audit**	**Other**	**Total**
Accountancy Professional Bodies:	Audit Quality Review	3.9		3.9		4.3		4.3
	Enforcement case costs	3.4	0.7	4.1		4.2	0.8	5.0
	Professional oversight and other audit related activities plus contribution to overheads	4.4	0.7	5.1		5.0	0.8	5.8
	Rebalancing - year 1			0		1.0		1.0
Companies	Corporate Governance and Reporting (including Actuarial policy plus contribution to overheads		12.2	12.2			14.1	14.1
Insurance Companies			1.3	1.3			1.4	1.4
Pension Funds			1.1	1.1			1.2	1.2
Actuarial Profession			0.2	0.2			0.2	0.2
Government			0.2	0.2			0	0
Other income		1.2	0.5	1.7		1.1	0.5	1.6
TOTAL FUNDING		12.9	16.9	29.8		15.6	19.0	34.6
% of total		43.3%	56.7%	100.0%		45.1%	54.9%	100.0%
TOTAL EXPENDITURE		18.1	11.6	29.7		19.9	13.6	33.5
% of total		60.9%	39.1%	100.0%		59.4%	40.6%	100.0%
SURPLUS / DEFICIT		-5.2	5.3	0.1		-4.3	5.4	1.1

**AQR income of £1.0m in 2016/17 derives from our contractual work on behalf of other authorities*

Note: these figures are rounded to the nearest £0.1m

Funding audit regulation

The new EU audit legislation requires our work in audit to be securely funded. We believe that, to ensure that we meet this requirement, the audit profession should meet the full costs of audit regulation within the new regulatory framework to be implemented in June 2016. To achieve this, we will increase the funding requirement for the audit profession over the period of our three year strategy; and reflect this adjustment in the funding requirement for our other funding groups.

We included an initial rebalancing amount of £1.5m in the draft budget we published in December 2015. To give the audit profession more time to adjust to the new funding arrangements we have reduced the initial rebalancing amount to £1.0m for 2016/17. We intend to complete the realignment in the second and third years of the strategy period.

Reserves

Given the voluntary nature of much of our funding, we believe that we need to maintain an appropriate level of reserves to ensure that we can deliver our regulatory responsibilities effectively. The total amount of FRC reserves has remained broadly unchanged at £7.5m since 2011. However £4.0m of this amount is held to meet legal costs in specified circumstances. Only £3.5m is held as a general reserve that could be used to meet unforeseen developments, including the costs of winding down our operations, to cover any shortfall in funding or to provide for an adverse outcome in an enforcement case not already covered by the existing legal cost funds.

There is a reserve power in company legislation to introduce a statutory levy should we experience a reduction in our funding, but this would require Government action and time to put in place. We believe that it would be prudent significantly to increase our general reserve. The overall funding requirement set out above will allow us to add £1.1m to reserves in 2016/17. Our aim over the period of the new three year strategy will be to establish reserves equal to six months operating costs. We will continue to consult each year on the level of our reserves, taking into account the impact of our new role in relation to audit regulation and our other responsibilities.

Section Five – Levies 2016/17

The FRC's funding requirement for 2016/17 is £34.6m, of which £16.7m will come from our three levies: a preparers levy that applies to the preparers of accounts; an insurance levy that applies to life and general insurance companies; and a pension levy that applies to pension schemes with 1,000 or more members.

Preparers levy

The preparers levy is the annual levy that we charge to:

- Companies listed on the London Stock Exchange with a Premium or Standard listing.
- UK companies traded on AIM and listed on ISDX (previously known as PLUS) Market group.
- Large private entities with a turnover of £500m or more.
- Global Depository Receipts issuers.
- Government Departments, local authorities and other public sector organisations.

The amounts payable under the preparers levy are determined through a minimum levy and further amounts for organisations above a certain size, with the rate per £m declining in five levy bands, aligned with the FCA levy arrangements.

The total amount of the preparers levy for 2016/17 will be:

	Budget 2015/16	**Budget 2016/17**
	£m	**£m**
Preparers levy	12.1	14.1
UK contribution to the funding of the IASB*	0.9	0.9
Total preparers levy	**13.0**	**15.0**

**International Accounting Standards Board*

We will increase the minimum fee and the rates for levy bands one and two for listed and other companies with a market capitalisation/turnover of less than £1bn by 2%; and increase the levy rates for bands three, four and five by 20%. The amounts finally charged to individual levy payers will be affected by changes in their market capitalisation (for listed companies), turnover (for other companies) or annual expenditure (for public sector organisations).

On the basis of the latest data on levy populations we expect that overall receipts in 2016/17 will be £15.0m – compared to the £14.5m we estimated in the levy proposals we published in December

2015.

The following preparers levy rates will be applied:

	Organisation size per £m*	2016/17 Preparers levy rate	2015/16 Preparers levy rate
Minimum fee	Up to 100m	£1,044	£1,024
Band		**Per £m***	**Per £m***
1	100m - 250m	£10.23	£10.03
2	250m - 1,000m	£7.80	£7.65
3	1,000m - 5,000m	£7.07	£5.70
4	5,000m - 25,000m	£0.1151	£0.0959
5	> 25,000m	£0.0218	£0.0182

**determined by market capitalisation for listed companies; and turnover or annual expenditure for other entities*

Discounts: Main market companies with a Premium listing pay the full levy; companies with a Standard listing receive a 20% discount. UK AIM traded and ISDX listed companies receive a 50% discount. Private entities with a turnover of more than £500m receive a 50% discount. Public sector organisations receive a 75% discount. The following table gives examples of the levy that will be charged to different types of entity:

Organisation	2015/16 levy	Proposed 2016/17 levy	% increase
UK AIM company with £100m market cap	£512	£522	2%
Private company with £750m turnover	£3,177	£3,299	4%
Premium listed company: £100bn market cap	£34,349	£40,646	18%

Global Depositary Receipt issuers will pay the same levy as in 2015/16: £3,450 for companies that have designated the UK as their home competent authority and £2,750 for other issuers. The FCA's Home Competent Authority list is available at http://www.fsa.gov.uk/ukla/hcaList.do.

Insurance levy for 2016/17

The insurance levy will be allocated to insurance companies in the same proportion as the FCA regulatory fees and charged to insurance companies on the same invoice as the FCA fees. Based on the FCA regulatory fees and levy proposals published in April 2016 we will set a levy equivalent to 1.1% of the fees charged by the FCA and PRA for their fee blocks A3 (insurers – general) and A4 (insurers - life) - rather than 1.0% as we estimated in our Draft Plan & Budget and Levy Proposals 2016/17.

Pension levy for 2016/17

We will charge a pension levy rate of £2.95 per 100 members and will apply this on the basis of the latest data on scheme membership held by The Pensions Regulator.

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