

Independent Review of the Financial Reporting Council

CALL FOR EVIDENCE

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Respond by: 6 August 2018

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Foreword

Trust and quality in financial reporting, audit, corporate governance, and investor stewardship are essential. They are critical to the functioning of financial markets, the economy and to public confidence.

They are what the FRC is for.

The question for the Review is whether the current regulator, and the current regulatory structure, are as effective as they need to be in current circumstances and for the future. As well as reviewing the FRC, its structure, governance, powers and resourcing, this will include examining:

- whether or not the FRC is, as was charged in the recent Select Committee report on Carillion, “chronically passive”, “timid” and requiring culture change;
- whether or not it is too slow, insufficiently proactive, and whether its actions have sufficient deterrent effect; and
- whether or not it is too close to, or unwilling sufficiently to challenge, the “big 4” audit firms – in a market in which there are well-documented structural competition weaknesses. Since, in practice, most consumers of accounts are in no position to apply direct pressure as customers, the need for an effective regulator of audit quality is fundamental.

The Review will aim to be evidence-based, rigorous and fair. But it will also be ambitious and, if necessary, far-reaching.

The Review will put forward proposals which aim to make the regulatory system as effective and credible as it needs to be – the “beacon” called for by the Government in the Review’s terms of reference.

The Review will also do everything it can to ensure that the regulator is a place where extremely talented people want to work.

No regulator can hope that every stakeholder will agree with all its decisions. But an effective regulator must be respected, and where necessary feared. The Review will aim to provide a platform for strengthened credibility, trust and respect.

John Kingman

Review objectives

1. There are two objectives for the Independent Review.
 - To ensure that the Financial Reporting Council (FRC) structures, culture and processes; oversight, accountability, and powers; and its impact, resources and capacity are as good as they could be.
 - To see the FRC standing as a beacon for the best in governance, transparency, and independence.

Issues under consideration

2. The Independent Review is calling for evidence and information, including specific examples, on the effectiveness of the FRC. You may wish to submit information or evidence relating to comparator bodies in the UK or internationally; on the context within which the FRC operates; anticipated shifts in regulation, technology, standards, or the wider landscape.
3. The Review will not directly consider questions which fall outside its terms of reference, such as:
 - Specific questions for which the FRC is responsible, or on the interpretation of the FRC's current policy landscape (for example, whether International Financial Reporting Standards (IFRS) are compatible with Companies Act requirements on 'true and fair' accounts),
 - Matters that require resolution before the end of the Review – such as the structure of a future IFRS endorsement model post-EU Exit, or
 - Issues of competition that sit with the Competition and Markets Authority, particularly competition in the audit market.
4. The Review is, however, keen to understand stakeholder views on the FRC's effectiveness in handling these and other issues, with a view to informing the Review's wider conclusions. In relation to competition in audit, for instance, the Review will consider current market dynamics as context for the FRC's regulatory approach, and whether there are aspects of the FRC's work which either could or should promote, or indeed could inhibit, competition in a well-functioning audit market.

Evidence requested

FRC purpose and function

Background

5. The FRC was established following Sir Ron Dearing's report of 1988 on The Making of Accounting Standards; and it was last subject of review in 2012.¹

6. Sir Ron's report set out a vision for the role of the FRC and its associated Boards, its intended accountability chains, and the interests of various stakeholders. Following evolution and growth of the FRC's role (taking on increased roles on audit; oversight of the chartered accountancy, audit, and actuarial professions; a more proactive role on compliance with accounting standards; and a more active role in relation to corporate governance) the 2012 Review subsequently sought to simplify its structure, replacing multiple subject-specific Boards with one decision-making Board.

7. Since 2012, the FRC has become responsible for Local Authority audit in England, and has been designated the Competent Authority for statutory audit in the United Kingdom.

Current mission and role

8. The FRC describes its mission as to "*promote transparency and integrity in business*".

9. It does that by regulating accountants, auditors and actuaries, and having responsibility for the UK's Corporate Governance Code. The FRC's functions are carried out by its Board, and supported by two Board Committees: on Codes and Standards, and on Conduct.

10. The FRC describes its more detailed roles as follows:

Corporate Reporting

The FRC sets UK accounting standards and works to influence international accounting standards (IFRS).

Through the Conduct Committee, it reviews the financial statements of public and large private companies for compliance with the Companies Act.

Corporate Governance

The FRC monitors and maintains the UK Corporate Governance Code and the Stewardship Code, together with their associated guidance. Compliance with both codes is voluntary although the Listing Rules require companies to report on their compliance with the former.

¹ <https://www.gov.uk/government/consultations/financial-reporting-council-reform>

Audit

As the Competent Authority for audit the FRC has a number of statutory functions including:

- Public oversight of the regulation of statutory auditors by the relevant professional bodies
- The determination and manner of application of technical, ethical and other standards
- Setting criteria for determining the eligibility of persons for appointment as statutory auditors
- Monitoring of statutory auditors and audit work by means of inspections
- Investigations of statutory auditors and audit work; and imposing and enforcing sanctions

In addition, the FRC has responsibility for:

- Recognition (in the capacity of Delegate of the Secretary of State) of the Recognised Supervisory and Qualifying Bodies for audit
- Registration of persons approved to audit non-EU registered companies that have issued securities admitted to trading on EU regulated markets (Third Country Entities and Third Country Auditor) and keeping of the Third Country Audit Register
- Various functions related to local public sector audit
- Independent supervision of Auditors General
- Monitoring of audits of entities listed on an EEA exchange and incorporated in Jersey, Guernsey or the Isle of Man

Accountancy

The FRC provides independent oversight of the regulation of the accountancy profession by the chartered accountancy bodies. This is conducted on a voluntary basis by agreement with the relevant accountancy bodies.

By private arrangement with the relevant accountancy bodies, the FRC provides independent investigation and/or disciplinary hearings in respect of misconduct by chartered accountants in public interest cases.

Actuarial

By agreement with the Institute & Faculty of Actuaries (IFoA), the FRC sets actuarial standards and provides independent oversight of the regulation of the actuarial profession by the IFoA.

By private arrangement with the Institute and Faculty of Actuaries (IFoA), the FRC provides independent investigation and / or disciplinary hearings in respect of misconduct by actuaries in public interest cases.

11. In taking action to drive-up compliance and quality of corporate reporting and audit, the FRC undertakes thematic reviews as well as firm-specific investigations. Those thematic reviews supplement its routine monitoring programme and focus on those aspects of corporate reports² and audits³ where there is particular shareholder interest, and scope for improvement and learning from good practice.

Questions

Q1: What should the FRC's objective(s) be? Is its present mission statement the right one?

Q2: Does the FRC's name remain right?

Q3: Are the functions and structure of the FRC still relevant and appropriate, or is there a case for any structural change? Should any of the FRC's functions move to other regulators?

Q4: What lessons can be learned from other countries' regulatory systems? Which ones?

Q5: How effective has the FRC been in influencing wider debates that affect its ability to deliver its objectives – for example, around audit competition, or its legal powers?

Q6: Is the current balance between cross-cutting reviews and firm-specific investigations most effective?

Impact and effectiveness

12. The Review's terms of reference state that:

“As a critical part of the UK's oversight of the economy, it is important that the FRC is seen as a world class regulator able to take effective action to detect and act on breaches, as well as to deter inadequacy and wrong-doing, and incentivise compliance. The Review will consider what changes would best enable the FRC to achieve this; and how best the FRC can lead globally on issues of governance.”

² <https://www.frc.org.uk/news/november-2017/frc-announces-2018-19-thematic-reviews-to-stimulat>

³ <https://www.frc.org.uk/auditors/audit-quality-review/thematic-inspections>

Questions

Q7: What are the FRC's strengths and weaknesses?

Q8: The recent joint report on Carillion from the Business, Energy and Industrial Strategy and the Work and Pensions Select Committees⁴ considered the FRC to be characterised by “feebleness and timidity” and recommended that a change of culture and outlook is needed. Do you agree? If so, please cite relevant evidence which informs your view.

Q9: Are there changes respondents would like to see to achieve the vision set out in the Review's terms of reference?

Q10: Are arrangements for financial reporting, audit and corporate governance the critical elements for effective delivery of FRC's mission, or are elements missing?

Audit regulation

13. Well-documented weaknesses in competition for the provision of complex audit services mean that effective regulation is critical to ensuring quality. Not all stakeholders, however, believe the FRC has been effective enough in driving improvements in audit quality; and there is a wider question about whether the current arrangements for audit meet wider investor and public expectation.

14. As Competent Authority for audit, the FRC has responsibility for the regular monitoring and mitigation of risks in the audit market; and has recently announced plans to enhance its monitoring of the six largest audit firms. This will include forming a view on how well they meet criteria and expectations in five areas: leadership and governance; values and behaviours; business models and financial soundness; risk management and control; and evidence on audit quality. In some areas, for example leadership and governance, the FRC does not have specific powers, and is looking for firms' cooperation in implementing its new approach.

15. In terms of the quality of audit work carried out outside the UK, the FRC, like other audit regulators, has no authority over the audit firms' international networks. However, UK audits frequently rely on the quality of work overseas. The international networks of the firms must ensure that public interest entity audits are completed to the highest standards by all national firms. The FRC has recently consulted on measures to strengthen the governance and oversight of the international audit-related standard setting bodies in the public interest.⁵

⁴ <https://www.parliament.uk/business/committees/committees-a-z/commons-select/work-and-pensions-committee/news-parliament-2017/carillion-report-published-17-19/>

⁵ <https://www.frc.org.uk/news/november-2017/monitoring-group-consultation-launched-to-strengthen>

Questions

Q11: How effective is the FRC at driving quality improvements in audit? What further improvements would respondents like to see?

Q12: Where quality does fall short, do the FRC's interventions have sufficient impact and deterrent effect?

Q13: What force is there in the concern of some that the FRC may be too close to the "big 4"? Or that the FRC is too concerned with the risk of failure of one of the "big 4"?

Q14: Are investigations of audit work effective, transparent, satisfactorily concluded and unfettered?

Q15: Could a different regulatory strategy or tactics result in greater avoidance of harm?

Q16: Could or should the FRC's work promote competition and a well-functioning audit market? Does the FRC's work undermine competition or a well-functioning audit market in any way?

Q17: Can questions regarding the effectiveness of the FRC be separated from the wider question on whether change is needed to audit arrangements to take account of shifting expectations?

Accounting and financial reporting

16. International Financial Reporting Standards are set by the International Accounting Standards Board and endorsed by the EU; and domestic accounting standards are set by the FRC Board.⁶ The FRC monitors compliance with those standards, and other legal requirements.

17. In relation to accountancy work, (other than statutory audit activities),⁷ the profession remains self-regulating, albeit with the FRC providing independent oversight of the various professional accountancy bodies' regulatory arrangements by voluntary agreement. The FRC's role is to:

- Provide an independent investigation and discipline scheme in respect of misconduct by accountant members/member firms in public interest cases.
- Provide independent oversight of the regulation of the accountancy profession by the professional accountancy bodies, with those bodies committing to consider carefully FRC recommendations and either implement them within a reasonable period or give reasons in writing for not doing so.
- Address unsatisfactory or conflicting interpretations of accounting standards, and by agreement, professional body members are expected to observe the consensus reached by the FRC on relevant issues.

18. In addition to financial reporting in company accounts, some have called for the FRC to play a stronger role in ensuring the quality of other aspects of financial and non-financial information reported by public and large private companies outside of the financial statements.

⁶ <https://www.frc.org.uk/accountants/accounting-and-reporting-policy/uk-accounting-standards>

⁷ In relation to statutory audit activities, as the Competent Authority, the FRC oversees those professional bodies that are Recognised Supervisory Bodies, and Recognised Qualification Bodies.

19. At present, the FRC reviews the reports and accounts of public and large private companies for compliance with the law, focusing on those aspects of corporate reporting where the FRC has delegated powers to monitor compliance – principally the financial statements and strategic and directors' reports (though not the viability statement). The FRC also has the power to go to court to seek the revision of accounts through section 457 of the Companies Act 2006. Monitoring activities include reviews of annual and interim reports together with thematic reviews on particular topics. Most enquiries are resolved through correspondence and informal meetings, although if the FRC believes that the nature of the outcomes requires additional publicity they will issue a press notice or ask companies to provide specific references to its interventions in their next published accounts. Key areas not covered by the FRC's monitoring work include the corporate governance statement and the remuneration report.

Questions

Q18: Has the FRC been effective in influencing the development of accounting standards internationally as well as accountable and effective in setting UK GAAP?

Q19: How else could the FRC improve the quality of financial reporting with a view to ensuring investor confidence?

Q20: Are there wider issues of financial and other reporting on which a stronger regulatory role would be desirable to better meet the information needs of investors and other stakeholders?

Q21: Is the current combination of statutory and voluntary methods of oversight for professional bodies effective, and do they remain fit for the future?

Corporate Governance and Stewardship Codes

20. The UK's Corporate Governance Code is generally respected though its effectiveness relies critically on active engagement from investors.

21. The first UK Stewardship Code, introduced in 2010, was also an important innovation. However, it is not yet clear that the Stewardship Code has had a comparable impact to the Corporate Governance code on improving standards.⁸

Questions

Q22: In relation to the UK Corporate Governance Code, are there issues relevant to the Review's terms of reference that respondents believe the Review should consider?

Q23: How effective has the Stewardship Code been in driving more and higher quality engagement by institutional investors? If not, why? How might quality of engagement be further strengthened?

⁸ The Review notes that in exploring how corporate governance may be strengthened so as better to prevent against insolvency, in its consultation on Insolvency and Corporate Governance, the Government has asked whether revision to the Stewardship Code could promote more engaged stewardship, or otherwise ensure that lessons are learned from large company failure.

Speed and effectiveness of investigations; enforcement and compliance

22. It is vital that the FRC’s enforcement enquiries are undertaken thoroughly and fairly, and without undermining criminal prosecutions; and that action taken to secure compliance and deter wrong-doing is effective.

23. Equally, however, some have strongly criticised the FRC for being very slow in pursuing its investigations and enforcement actions – and, in some cases, there has been a perception that the FRC has been reluctant to act at all.

24. In relation to the timeliness of its audit enforcement action, there has already been recognition by the FRC that – for example in relation to HBOS and MG Rover – it has been too slow either to launch or to conclude investigations, and that it needs to be able to move faster in such cases. However, there remain examples of the FRC’s enforcement work where significant delay appears to remain an issue.⁹ The Review will need to be convinced that remaining delays are, as the FRC believes, often legally unavoidable.

Questions

Q24: Do respondents view the FRC as reluctant to undertake investigations or enforcement, or able to do so at speed?

Q25: How could the FRC better ensure it is able to take swift, effective and appropriate enforcement action? What practical or legal changes would be needed to achieve this?

Actuarial oversight

25. The 2005 Morris Review of the Actuarial Profession examined the regulatory framework for the provision of actuarial work, and recommended that the system of self-regulation be supplemented with independent oversight by the FRC in order to ensure the adequate protection of the public interest. That oversight is given effect through a Memorandum of Understanding (MoU) between the FRC and the Institute and Faculty of Actuaries (the IFoA); with the FRC also responsible for setting actuarial standards.

Question

Q26: Have the arrangements put in place following the 2005 Morris Review stood the test of time, or is there a need for change? Should actuarial regulation be a focus for the Review’s work?

FRC and corporate failure

26. The FRC is responsible for the regulation of statutory audit, which is by its nature retrospective. The FRC is also responsible for the Corporate Governance Code and, in relation to investors, the Stewardship Code. The recent select committee report on Carillion also noted that “the FRC has no business intervening in the day-to-day management of companies

⁹ For example, the FRC announced disciplinary action in relation to Autonomy Corporation PLC on the 31 May following an investigation which has been underway since the firm’s sale to Hewlett Packard in 2011. US Federal prosecutors brought charges against their CFO, a UK resident, in 2016 and he was convicted in April 2018.

to prevent them failing”. Nevertheless, some stakeholders would like to see the FRC playing a more interventionist and forward-looking role in reducing the risk of major corporate failure. The Review is interested to hear views on whether and, if so, how the FRC might do this.

Questions

Q27: Is there more the FRC could or should do to help reduce the risk of major corporate failure?

Q28: Is the FRC quick and effective enough to act on warning signs arising from its work on accounts and financial reporting, or on evidence of concerns over poor corporate governance?

Q29: Is there a case for a more “prudential approach”? If so, how could this operate in practice, and to which category of company might such an approach apply?

Q30: Introduction of the viability statement was an important development, but could it be made more effective?

Powers and sanctions

27. There have been a number of calls to revisit the FRC’s powers and sanctions.

28. There are several key regulators in this space, and there are Memoranda of Understanding¹⁰ in place between regulators to ensure the effective joined-up use of their powers. Alongside the FRC’s role, the Financial Conduct Authority is responsible for ensuring that markets function well, through protection for customers and the promotion of effective competition in the markets for financial services. The Insolvency Service leads on the investigation of companies and individuals entering an insolvency procedure, as well as enquiring into a company’s affairs when its activities are suspected of being conducted contrary to public interest, and seeking the disqualification of directors where it is in the public interest to do so. The Prudential Regulation Authority is responsible for the prudential supervision of banks, insurers, credit unions and building societies particularly to ensure that firms carry on their business in a way that avoids adverse effects on the wider economy.

29. There have been calls for the FRC’s powers to be extended in order to ensure effective oversight and enforcement of non-accountant Directors who exert influence over financial statements. As noted by the Select Committees’ report on Carillion, at present the FRC is only able to take direct action against those with accounting or actuarial qualifications.¹¹ That report also flagged wider concern that arrangements to enforce statutory directors’ duties (as set out in the Companies Act 2006) are insufficient to deter breach. At present, enforcement lies with shareholders as the owners of the company, although the Insolvency Service may act where there is a public interest in doing so (without the need for insolvency to have occurred). Going further than this – moving to stronger statutory enforcement for example – would, however, be a substantial extension of regulation and unusual internationally.¹²

¹⁰ <https://www.frc.org.uk/about-the-frc/procedures-and-policies/memorandum-of-understanding>

¹¹ Paragraph 148 <https://www.parliament.uk/business/committees/committees-a-z/commons-select/work-and-pensions-committee/inquiries/parliament-2017/carillion-inquiry-17-19/>

¹² The Government’s consultation on Insolvency and Corporate Governance seeks views on whether directors are sufficiently aware of their duties. <https://www.gov.uk/government/consultations/insolvency-and-corporate-governance>

30. In relation to its powers, the FRC itself has raised the following four further points:

- First, it does not have powers to test and seek change to some aspects of a company's annual report, including its statements on governance. It considers this a gap that weakens the ability of shareholders to undertake their stewardship duties.
- Second, confidentiality requirements in the Companies Act prevent the FRC from making public concerns it has about poor audit work in relation to individual companies without the auditor's and company's permission. Does this need to be reconsidered against shifting public expectations on transparency?
- Third, whether the current balance of delegation to professional bodies for oversight of audit functions is still right.
- Fourth, regarding the actuarial profession, whether the FRC's oversight and standard-setting functions should change from the current MoU arrangements?

31. Regarding sanctions, an independent review of the FRC's sanctions was undertaken in 2017 by Sir Christopher Clarke, and new updated sanctions guidance will take effect in June 2018.¹³

Questions

Q31: Are there gaps in the FRC's powers? Would its effectiveness be improved with further (or different) powers?

Q32: Are the FRC's powers coherent in relation to those of other regulators?

Q33: Taking account of Sir Christopher Clarke's review of sanctions, and subsequent changes, does the sanctions regime now have the right deterrent effect? Does the FRC make best use of the sanctions at its disposal?

The FRC's legal status and its relationship with Government

32. The FRC is now a public body, albeit unusually without a consolidated base in legislation setting out its powers and functions. The majority of the FRC's functions are, however, delegated or drawn from legislation, but it does conduct some functions via private agreement, MoU, or contract.¹⁴ The FRC was established as a private company limited by

¹³ The FRC operates three enforcement procedures – the Accountancy Scheme, the Actuarial Scheme, and the Audit Enforcement procedure.

The sanctions available to the FRC's Accountancy and Actuarial Scheme include reprimands, fines, waivers/ repayment of client fees, and withdrawal of a member's practicing certificate or a firm's licence. Such sanctions are determined by Tribunal, may be imposed in combination, and may apply to members or member firms. There is no upper limit on the fine that the tribunal can impose, but in the majority of cases the revenue of the firm in question will be taken into account.

Sanctions available under the Audit Enforcement procedure include financial penalties; a statement which may take the form of a reprimand or a declaration that the audit report is unsatisfactory; banning the respondent from carrying out statutory audits or from acting as a director of a Public Interest Entity (PIE); and ordering the respondent to waive or repay client fees. In such cases, the decision makers include the FRC's Executive Counsel, its Enforcement Committee, or Tribunals and Appeal Tribunals. There is no upper limit on the financial penalty the decision maker can impose.

The 2017 Review suggested that financial penalties of £10 million or more could be appropriate when there has been "seriously bad incompetence, in respect of the audit of a major public company" by a Big 4 firm.

¹⁴ <https://www.frc.org.uk/about-the-frc/role-and-responsibilities>

guarantee following the recommendations of the Dearing Report in 1988, but the FRC's designation as a public body inevitably and properly carries consequences for its operations and relationship with Government.

33. In carrying out its functions, it is important that the FRC acts with appropriate independence. In practice, the nature of regulators' operational independence and their relationship with the Government varies quite widely, and the Review will want to make recommendations as to how this balance should best be struck in the FRC's case, going forward.

Questions

Q34: Should the Government legislate to put the FRC on a more conventional consolidated statutory footing?

Q35: What is the optimal structure for the relationship between the FRC and the Government, best balancing proper accountability with enabling the FRC's effectiveness?

Q36: In terms of the FRC's broader accountability, is there a case for further transparency in its actions or functions?

Governance and leadership

34. The FRC's Board structure was simplified in 2012, shifting from a multiple Board structure to a single decision-making Board that is supported by a Codes and Standards Committee, Conduct Committee; and several Councils, subordinate Committees, and Panels.

35. The FRC's role has continued to evolve since 2012, taking on responsibility for oversight of Local Authority audit in England, becoming the Competent Authority for Statutory Audit in the UK, and for the proposed corporate governance principles for large private companies.

36. The FRC Board is responsible for the overall leadership of the FRC, approval of the FRC's strategic aims and objectives, the determination of risks to the FRC's strategic nature, the issuing and maintaining codes and standards, changes to the structure, size and composition of the Board and the appointment and removal of Board and Board Committee members.

37. To ensure an appropriate separation of functions and to maintain independence, the Board delegates certain responsibilities to its Codes & Standards Committee and Conduct Committee. In addition, the Secretary of State has delegated functions to the FRC Conduct Committee pursuant to section 457 of the Companies Act 2006 and section 14(2) of the Companies Act 2004.¹⁵

38. In accordance with these delegations and the FRC's procedures and processes, the FRC Board is not responsible for decisions to open an enforcement investigation (taken by the Conduct Committee) nor is it responsible for decisions on whether to proceed from an

¹⁵ The Conduct Committee exercises these delegated functions in accordance with its operating procedures. Under section 457 the Committee may make an application to the court for a declaration when the annual accounts of a company do not comply, or a strategic report or a directors' report does not comply, with the requirements of the 2006 Act; and it may apply for an order requiring the directors to prepare revised accounts or a revised report. Under section 14(2) the Committee keeps under review periodic accounts and reports that are produced by issuers of transferable securities and are required to comply with any accounting requirements imposed by the Financial Conduct Authority.

investigation to a Formal Complaint (Tribunal) (taken by the by the FRC's Executive Counsel).¹⁶ This is important since it means the FRC board has no involvement in many of the most high-profile and contentious decisions for which the FRC is generally held publicly responsible.

Questions

Q37: How effective is the current leadership and Board of the FRC? Please cite relevant evidence which informs your view.

Q38: Is the Board's composition appropriate? Is it the right size? Does it have appropriate membership?

Q39: Is the balance of decision-making between the Board, its Committees and the Executive described in paragraphs 34-36 above right, given relevant legal constraints?

Q40: Is the Board's structure appropriate, including given the FRC's roles on standard setting, assessment and enforcement? Does the Board's accountability appropriately reflect its role and functions? Are its decisions appropriately transparent, bearing in mind the need to balance public interest and confidentiality?

Q41: How should the Executive's effectiveness be assessed and ensured?

Funding, resources and staffing

39. The FRC is funded through a mixture of statutory and voluntary funding arrangements; and there is a currently unused statutory power for the FRC to be funded by a compulsory levy. Funding is provided in the main by accountancy professional bodies, accounts preparers¹⁷, pension schemes and insurance companies, and third country auditors. In setting its budget, the FRC undertakes consultation on its proposed levies.

40. The Review will consider if the FRC has sufficient resource, skills, experience, and capacity to deliver its responsibilities. It will also consider the FRC's arrangements for managing conflicts of interests.

41. The Review will specifically also consider whether the FRC's structure, recruitment, or culture presents a conflict of interest in its regulation of the audit and accountancy professions, or the "big 4" firms.

¹⁶ The FRC's regulatory powers are underpinned by its responsibility for the exercise of a range of functions including: of the Secretary of State under Part 42 of the Companies Act 2006; as the Independent Supervisor appointed under Chapter 3 of Part 4 of the Companies Act 2006; as the Competent Authority for Statutory Audit in the UK under the Statutory Audit and Third Country Audit Regulations 2016; and with regard to the Secretary of State Direction dated 17 June 2016 in relation to the delegation and removal of tasks to / from Recognised Supervisory Bodies.

¹⁷ Those companies listed on the London Stock Exchange, AIM or NEX; large private entities with a turnover of £500m or more; Global Depository Receipt issuers; and Government Departments, local authorities and other public sector organisations.

Questions

Q42: Who should fund the FRC, and how? What are the impacts of current funding arrangements, including of having a partially voluntary funded regime?

Q43: What skills are needed for the FRC to be most effective? Does the FRC have the people, skills and resources it needs, of the quality it needs?

Q44: Are there conflicts of interest in the FRC's structure, processes, or culture? Are there deficiencies in the FRC's approach to managing conflicts of interests?

Other matters

42. Respondents should not feel constrained by the questions in this call for evidence. If there are other issues germane to the Review's terms of reference, please comment on them.

Question

Q45: Are there any other issues relevant to the terms of reference that respondents would like to raise?

About this call for evidence

Who is this for

43. The Review would welcome views from those affected by the FRC's functions and its effectiveness, including:

- i. Those organisations and companies that fund the FRC,
- ii. Professional bodies, including those regulated by the FRC,
- iii. Those who prepare accounts and conduct audits,
- iv. Investors and other users of accounts,
- v. Individuals or bodies with an interest in the FRC's effectiveness.

How to respond

44. This call for evidence closes on Monday 6 August, 2018. Copies of this document may be found at <https://www.gov.uk/government/consultations/financial-reporting-council-independent-review-call-for-evidence>.

45. Please send any response to FRCReview@BEIS.gov.uk.

46. If you do not have access to email, you can write to the FRC Review Secretariat, Victoria 1, 1st Floor, 1 Victoria St, London, SW1H 0ET.

47. If you would like to participate in a round-table discussion, please email the Review Secretariat at FRCReview@BEIS.gov.uk.

Disclosure of the information you provide

48. Because information provided in response to this call for evidence will be received by the Review Secretariat which is hosted by the Department for Business, Energy, and Industrial Strategy, that information may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004).

49. If you want information you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

50. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances.

51. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding.

Personal data

52. The following is to explain your rights and give you the information you are entitled to under the Data Protection Act 2018.

53. Please note that this section only refers to your personal data (your name address and anything that could be used to identify you personally) not the content of your response to the consultation.

The identity of the data controller and contact details of our Data Protection Officer

54. The Department for Business, Energy and Industrial Strategy is the data controller. The Data Protection Officer can be contacted at dataprotection@beis.gsi.gov.uk

Why we are collecting your personal data

55. Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

Our legal basis for processing your personal data

56. The Data Protection Act 2018 states that, as a government department, BEIS may process personal data as necessary for the effective performance of a task carried out in the public interest. i.e. a consultation.

With whom we will be sharing your personal data

57. Your data will be shared with the Independent Reviewer.

Your rights, e.g. access, rectification, erasure

58. The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right:

- a. to see what data we have about you
- b. to ask us to stop using your data, but keep it on record
- c. to have all or some of your data deleted or corrected
- d. to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law.

59. You can contact the ICO at <https://ico.org.uk/>, or telephone 0303 123 1113.

60. Your personal data will not be sent overseas.

61. Your personal data will not be used for any automated decision making.

62. Your personal data will be stored in a secure government IT system.

Appendix 1

Review Terms of Reference

A: Purpose and Timing

The Secretary of State for the Department for Business, Energy, and Industrial Strategy (BEIS) invites Sir John Kingman to conduct a review of the FRC.

The Review will aim to submit its findings to the Secretary of State for Business, Energy and Industrial Strategy and the FRC Board by the end of 2018. The review process will include a public consultation. The final report will be published, and the Government will consult on its response to the review's recommendations.

B: Review Objectives

Mindful of the FRC's role in helping to ensure the effective functioning of UK capital markets, and in safeguarding the reputation of the UK as a world-leading financial and commercial hub, the review objectives will be to:

- Put the FRC in a position to stand as a beacon for the best in governance, transparency and independence; strengthening its position and reputation.
- Ensure that its structures, culture and processes; oversight, accountability, and powers; and its impact, resources, and capacity are fit for the future

C: Scope

The Review's scope is taken to include the objectives and context included in these terms of reference, and will include the FRC's governance and transparency; the avoidance of conflicts of interest, as well as its independence, oversight and accountability; and finally its impact, resources and capacity. The detail of the Review's scope is set out in Annex A.

D: Context

The FRC and its remit have developed considerably since it was initially established; and it was last the subject of a review in 2011/12. Since then, there have been changes both in regulation, and in expectations of regulators and how they operate. The FRC is a public body. Some stakeholder groups have called for the FRC to demonstrate greater independence from those they regulate.

The Government's expectation is to see the UK at the forefront of corporate governance internationally, including in terms of regulation. In the context of the UK's exit from the EU, it is even more important that our regulatory structures are fit for the future. With reforms to the UK's Corporate Governance Code in hand, it is also appropriate to make sure that the governance of the FRC as the body with responsibility for the Code, is best in class.

E: Governance

The Review will be led by Sir John Kingman.

The Independent Reviewer will be supported by an Advisory Group that will advise on the direction of the Review and sources of evidence and will help to scrutinise and challenge emerging findings and recommendations.

Advisory Group discussions will be held under Chatham House principles to enable free and frank scrutiny of the issues. A summary meeting note will be produced and made available if requested.

F: The Review Secretariat

There will be a small dedicated Review Secretariat acting in support of the Independent Reviewer.

G: Stakeholder Engagement

The Review will undertake engagement with significant stakeholder groups, including those involved in preparing financial accounts, the users of accounts and those affected by other aspects of the FRC's work, including governance and stewardship, in order fully to understand the range of issues, and provide constructive challenge.

Annex A: Detailed Scope

The Review will consider and make recommendations on the issues set out below.

1. Governance

The Review will consider whether current governance arrangements and their transparency are suitable given the FRC's status as a public body; the increasing span of its functions (including in relation to large private companies); and in comparison to the increasing expectations on companies, including those that will flow from anticipated changes to the Corporate Governance Code, and especially so as to promote confidence and emulation.

2. Independence

The Review will consider whether the FRC is sufficiently independent:

- Within Government;
- From those whom it regulates; and
- Including as a result of its funding arrangements, or to the extent that independence is insufficient, the review will propose how this might be addressed.

The Review will also consider, in particular, whether there are sufficient safeguards in place to ensure and assure that independence. Such measures may include FRC's processes, transparency, culture, or other factors.

3. Avoidance of Conflicts of Interest

In addition to the question of independence, it is important that the FRC is able to carry out its broad range of functions and responsibilities without conflicting, or being seen to conflict with other functions. The Review will therefore consider:

- Whether the practices, structure, culture and functioning of the FRCs activities and operations are safeguarded against conflicts of interest, or a perception that there may be conflicts of interest.
- Whether existing mechanisms and practices for the prevention, detection, and resolution of conflicts of interest are adequate, or if additional measures are needed.
- Whether the procurement of legal and consulting services are suitable.

4. Oversight & accountability

Whilst respecting the FRC's operational independence, the Review will consider appropriate mechanisms to realise its accountability to Parliament and Government. The Review will also consider whether current arrangements for the FRC's accountability to stakeholders and the public are appropriate, including on the specific matter of Freedom of Information.

5. Powers

The Review will consider whether the current legal bases for FRC activities are adequate; or whether there is a case for an underpinning statutory architecture. In addition, the Review will look ahead to consider whether any extension of powers is necessary, advisable, or otherwise recommended.

6. Impact

As a critical part of the UK's oversight of the economy, it is important that the FRC is seen as a world class regulator able to take effective action to detect and act on breaches, as well as to deter inadequacy and wrong-doing, and incentivise compliance. The Review will consider what changes would best enable the FRC to achieve this; and how best the FRC can lead globally on issues of governance.

7. Resources & capacity

It is important that the FRC has sufficient resource, skills, experience, and capacity to deliver its responsibilities. The Review will consider this, as well as whether current funding arrangements are adequate and desirable. In so doing, the Review will take account of whether there are lessons that could be taken from international comparator bodies.