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Dear Sir John,

Independent Review of the Financial Reporting Council: Call for Evidence

We welcome the opportunity to respond to the independent review of the Financial Reporting Council (FRC) call for evidence.

As Britain prepares to leave the European Union and rethink the way it conducts business at home and abroad, this independent review of the FRC is particularly timely.

Overall, we consider the FRC's mission statement to be too broad for a single body. Public trust in business has remained low since the 2007/08 financial crisis; the FRC's wide-ranging functions have reduced its effectiveness in reversing this trend.

Whilst we remain open-minded as to the specific structure of the FRC, or alternative institutional framework, we do believe that this independent review represents a unique opportunity to rethink the relationship between regulators and companies in the UK.

Going forward, we believe that the government should legislate for the FRC, or similar body, to put it on a more conventional, consolidated footing, such as that used for the Financial Conduct Authority. As a body which clearly serves the public interest, we consider this essential. However, it is equally clear that any such body is fully independent from the government.

Any successful and sustainable framework for regulating business must be underpinned by three principles:

1) Placing proportionality at the heart of regulation making. The needs and size constraints of smaller companies must be at the forefront of regulators' thinking when formulating new standards and regulatory requirements. This is a key component to stimulating the growth and development of smaller companies, as well as overall growth in the UK economy, whilst ensuring that businesses are not overburdened by compliance requirements. We would recommend that this should be explicitly stated in the FRC's statutory objectives.

The Quoted Companies Alliance is the independent membership organisation that champions the interests of small to mid-size quoted companies.

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- 2) **Ensuring the representation of all companies across the market on the committees and governing bodies of regulatory bodies.** Smaller companies must be sufficiently represented at all levels of regulatory institutions – including boards and committees.
- 3) **A clear separation of responsibilities for standard setting and enforcing rules.** The current model whereby one body is responsible for setting standards and codes, regulating those standards, conducting investigations and issuing sanctions is unsustainable in the long-term.

We will be sending a supplementary paper outlining how the concept of proportionality and representation could be built into the objectives and duties of the FRC in the coming weeks.

In the meantime, we have responded below in more detail to the specific questions from the point of view of our members, small and mid-size quoted companies.

If you would like to discuss our response in more detail, we would be happy to attend a meeting.

Yours sincerely,



Tim Ward
Chief Executive

A. FRC purpose and function

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

We consider the FRC's present mission statement to be too broad and, ultimately, not achievable by a single body.

The FRC's steady accumulation of functions and responsibilities has increasingly hindered its ability to pursue its mission in an effective and coherent manner. Indeed, many parts of the small and mid-size quoted company community – including those that advise them – believe that the FRC's wide remit has meant that it has not been able to concentrate effectively on any one area.

Therefore, any mission statement must be more succinct and specific, in order to enable the FRC to function more successfully.

Q2 Does the FRC's name remain right?

No – we do not consider the FRC's name to be right for the simple reason that its remit extends far beyond just financial reporting.

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?

The UK stands alone in giving one regulator such an extensive remit. As we show in Appendix A, no other major economy gives a single institution so much responsibility.

We believe this has led to the situation whereby the FRC is – as currently constructed – no longer able to effectively promote transparency and integrity in business in a coherent and consistent way. Furthermore, we believe that the FRC's responsibility for thought leadership, standard setting, monitoring regulatory compliance, investigating breaches and deciding on sanctions has led to an increase in a disproportionate regulatory framework which restricts the growth of small and mid-size quoted companies.

This independent review of the FRC therefore represents a unique opportunity to fundamentally rethink, and potentially reform, the structural relationship between regulators and business in the UK.

Any future regulatory framework should be formed with three principles in mind:

- 1) Placing proportionality at the heart of regulation making.** The needs of smaller companies must be at the forefront of consideration when formulating new standards and regulatory requirements. This is necessary to enable smaller, growing companies and the UK economy to create long-term value for shareholders.

As of 29 June 2018, the largest company on the UK's FTSE All-Share index – HSBC – has a market capitalisation of £142.7 billion. Meanwhile, the smallest company in the index has a market capitalisation of £41 million – 0.03% of its size. The top 10 companies in the index account for 35% of the index's market capitalisation, which comprises 640 companies in total.¹

¹ <https://www.ftse.com/Analytics/factsheets/Home/Search>

Requirements targeted at the largest companies will therefore often be ill-suited for small, growing companies. Such disproportionate requirements will subsequently erect unnecessary barriers to growth for these companies. Such requirements are not in the public interest.

- 2) **Ensuring the representation of all companies across the market on the committees and governing bodies of regulatory bodies.** In order for proportionate regulation to be developed and implemented, those that work at or advise smaller, growing companies must be represented in sufficient numbers on regulators' boards, as well as committees such as those for codes and standards, and audit quality.
- 3) **Establishing a clear separation of responsibilities for standard setting and enforcing rules.** We consider the current model whereby the FRC is responsible for setting standards and codes, acting as a regulator, conducting investigations and issuing sanctions as ineffective.

As Britain prepares to leave the European Union and present itself as an attractive place to create and run a business, we believe that the UK regulatory architecture regarding corporate conduct must be renewed to reflect this worthwhile objective.

Ten years have passed since the 2007/08 global financial crisis; public trust in business remains low.² As governments have sought to find solutions to these reasonable societal concerns, the regulatory infrastructure which companies must navigate has become increasingly difficult. This, alongside the ever rising administrative and compliance burden, has been felt most keenly by small and mid-size quoted companies.

Any new structure must communicate, and abide by, a coherent set of values which secure a high level of trust and confidence from the public and the business community: open, transparent and proportionate.

With this in mind, we highlight two possible models which could realise the three principles outlined above:

Model 1 – Retaining the current FRC but separating its standard setting and enforcement responsibilities with a clear, well-defined mission

If the Review decides that the FRC, as currently constituted, should largely remain intact, then we recommend that a governance structure is established that recognises the conflicting activities undertaken. We believe that a reformed FRC must fully separate its responsibilities for:

- **Standard setting; and**
- **Enforcing rules.**

Establishing separate entities for each of these responsibilities will ensure that neither of these discrete teams can influence the other within the FRC. We consider erecting such information barriers within the FRC – which should be outlined within its governance in a transparent way – as imperative to improving business conduct in the UK.

² Edelman Trust Barometer 2018 – UK findings (22 January 2018): <https://www.edelman.co.uk/magazine/posts/edelman-trust-barometer-2018/>

Model 2 – Reforming the UK institutional infrastructure

Alternatively, if the Review considers that a more fundamental reform of the institutional infrastructure through the decentralisation of the FRC’s current remit into entirely separate bodies is required, we suggest the following could act as a means for achieving reform:

- **Transferring the responsibility for corporate governance, corporate reporting and investor stewardship of UK listed companies into a new organisation or another appropriate institution.** This institution could then provide oversight in these areas, in order to protect investors, maintain fair and efficient markets and facilitate the efficient allocation of capital without distraction from other tangential activities. This could enable a clearer and more precise mission to be defined; **and**
- **Creating two separate, independent regulators for (1) accounting and audit standard; and (2) actuarial standards.** As we discuss in our response to Q7, we believe that the FRC has become too unwieldy an institution to regulate such a broad range of competencies effectively and coherently. This could provide the opportunity to create organisations with a clearer and more precise mission and related operational objectives.

These proposals, while a significant step change from the current regulatory structure in the UK, should not be considered controversial. As Appendix A shows, the UK is somewhat of an international outlier in allowing one regulator to possess such a wide remit.

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

The Public Company Accounting Oversight Board (PCAOB)³ in the United States is much stricter and arguably has more authority than the FRC does in the audit market.

The PCAOB is a well-established, renowned and respected audit regulator in the US. Registered audit firms, including foreign registered audit firms, are more aware of, and seek to actively comply with, the PCAOB requirements because of the strength and weight of their powers of inspection, investigation and enforcement.

The PCAOB appears to have less restrictions in its ability to address poor standards of audit quality by registered audit firms as well as sanctioning such firms for non-compliance with the applicable laws, rules and standards. Whether this is a reality in practice should be determined as part of the review of the FRC’s existing powers, however, the perception in the market and general audit practice is that the PCAOB has more presence through its public reporting of inspections and sanctions levied on registered audit firms both within and outside of the US than the FRC does.

The review would therefore benefit from understanding the audit regulatory system that operates in the US in order to determine if the existing roles and responsibilities for the FRC as the UK competent authority for audit is sufficient and fit for purpose.

³ <https://pcaobus.org/>

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?

The FRC has been relatively ineffective in influencing wider debates that affect its ability to deliver its objectives, such as around audit competition, and accounting and audit standards. This is reflected by a lack of meaningful change in the competitiveness of the audit market since the last review in 2013.

Indeed, the FRC has been far too timid in displaying thought-leadership on these and other matters. This has ultimately hindered its ability to influence government policy and global standard setters.

For example, the FRC's desire to retain maximum convergence with IFRS, despite the shortcomings in IFRS, has meant that it has not taken advantage of the opportunities that have arisen in the last decade to display thought leadership.

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

We consider the FRC's cross-cutting, thematic reviews to be extremely valuable and can help drive improvements in corporate reporting quality and auditing – particularly when these are announced ahead of time.

A good example of this was when the FRC announced that it would write to 40 smaller listed and AIM quoted companies prior to their year-end, informing them that it will review two specific aspects of their next published reports and accounts.⁴ This followed the FRC's annual letter to smaller issuers setting out the themes that such issuers should focus on to encourage improvement in the quality of annual reports.

B. Impact and effectiveness

Q7 What are the FRC's strengths and weaknesses?

Strengths

- **High quality staff:** FRC staff have attended our Corporate Governance and Financial Reporting Expert Group meetings on a number of occasions. In our experience, they are incredibly knowledgeable about the subject matter. In particular, they have been collaborative and responsive when discussing areas such as corporate governance and corporate reporting.
- **Internationally respected:** The FRC is well regarded in Europe and beyond. In particular, the UK Corporate Governance Code's pragmatic, principles-based approach is seen as a leader of good governance practice and has been emulated in a significant number of other jurisdictions. Similarly, when the EU was considering introducing EU-wide legislation on corporate governance, the FRC played a key role in ensuring that a 'comply or explain' approach prevailed.
- **The Financial Reporting Lab:** The FRC should be commended for launching the Financial Reporting Lab, which – since its inception in 2011 – has provided a space for investors and companies to discuss the latest developments in financial reporting, as well as to support innovation in this area. The Lab's

⁴ FRC announces 2018/19 thematic reviews to stimulate improvement in corporate reporting and auditing (17 November 2017): <https://www.frc.org.uk/news/november-2017/frc-announces-2018-19-thematic-reviews-to-stimulat>

recent work on the digital future of corporate reporting, the disclosure of dividends and business model reporting have especially played a key role in contributing to dialogue between companies and investors.

The QCA has a representative on the steering group and we see this as a good example of ensuring that smaller issuers have a voice and can contribute to discussions in a meaningful way.

Weaknesses

- **An institution too big to be effective:** The fact that it has oversight over four disparate areas of business conduct – corporate governance and investor stewardship; accounting standards; actuarial standards; and audit regulation – has constrained its ability to promote transparency and integrity in business in a coherent way. As we noted in our response to Q1, the UK is exceptional in this regard.
- **Low level of diversity:** There is insufficient representation of small and mid-size quoted companies on the FRC board and various other committees including – but not limited to – the Codes and Standards Committee and Corporate Reporting Review Committee. Not accounting for this key constituency which bears the impact of FRC decisions more keenly than their large counterparts has inevitably led to the FRC failing to develop a proportionate approach across its workstreams covering corporate governance codes, regulations and reviews of annual reports.
- **Not inclusive:** In any wider debate concerning corporate governance in the UK, the QCA's contribution goes largely unrecognised. The QCA Corporate Governance Code⁵ is used by over 400 companies on AIM; this has not been recognised by the FRC's executive leadership and committees. We believe that the UK governance landscape must acknowledge the FRC's position as a *primus inter pares* of corporate governance, rather than its sole gatekeeper.
- **An ineffectual enforcer:** Recent history has shown that the FRC is not only too slow in responding to breaches of audit quality requirements, but is also incapable of issuing sufficiently punitive sanctions for those breaches.

Q8 The recent joint report on Carillion from the Business, Energy and Industrial Strategy and the Work and Pensions Select Committees considered the FRC to be characterised by “febleness 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.

We believe that the prime cause of business failure, besides poor management, lies in the inaccurate reporting of cash flows. IFRS seeks comparability of profit reporting at the expense of clear reporting of cash flows and liabilities.

The FRC does not sufficiently challenge this failing in IFRS or display thought leadership in how these failings in IFRS can be overcome. Viability statements are no substitute for clearly showing in accounts the sources and applications of funds and the period end liabilities.

⁵ QCA Corporate Governance Code (2018): <http://www.theqca.com/shop/guides/143861/corporate-governance-code-2018-downloadable-pdf.shtml>

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

We have no comments.

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

Any arrangements for financial reporting, audit and corporate governance for the effective delivery of the FRC's mission will depend on the FRC's mission statement.

Audit regulation

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

The FRC does not appear to drive improvements in audit quality other than to penalise smaller firms who do not fully fulfil the FRC's expectations, despite the fact that these companies have fewer resources than the Big 4.

We believe that the FRC should apply a more proportionate approach in determining its expectations of audit quality within different audit practices and audit clients.

Going forward, we believe that the FRC must do more to work with audit firms of all sizes. This could be in partnership with the Recognised Supervisory Bodies, to encourage positive changes in firm culture. The FRC could also consider establishing an 'Audit Lab' to enable wider industry engagement. This would clearly be predicated on a separation of the standard-setting and regulatory functions.

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

No. The FRC's interventions – primarily through sanctions and fines – do not have a sufficient impact and deterrent effect. We believe that interventions must focus on improving the overall culture of audit firms to drive quality improvements. Interventions must occur promptly to have the greatest impact.

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"?

We consider the concern that the FRC is too close to the "Big 4" to be justified. This is reflected by the fact that many senior staff members of the FRC working on highly sensitive and strategic matters concerning audit regulation are former employees of "Big 4" firms.

We believe that, as a result of this situation, the FRC has been too slow in challenging the conduct of the "Big 4" firms. It encourages an acceptance that the audit approach of the "Big 4" is the right one.

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

No – we do not generally consider the investigations of audit work effective, transparent, satisfactorily concluded and unfettered. However, we believe that others are better placed to give examples of this.

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

Any future regulatory strategy to improve audit quality should leverage and maximise the influence of Recognised Supervisory Bodies (RSBs) and five Recognised Qualifying Bodies (RQBs).

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?

The work of an audit regulator – be that the FRC or another independent body – should, through the issuance of robust standards and practical guidance, help facilitate a well-functioning audit market that enables competition. However, the Competition and Markets Authority (CMA) should lead on providing direct remedies which promote competition; this is not the role of a standard setter.

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?

We have no comments.

Accounting and financial reporting

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

We see little evidence to suggest that the FRC has been effective in influencing the development of accounting standards internationally, as well as accountable and effective in setting UK GAAP. From our experience much of this has been agreed through the EU endorsement process of IFRS. The best way to influence IFRS is to demonstrate through UK GAAP that a different approach produces better results.

In our view, the FRC's decision to emulate IFRS in UK GAAP to the greatest extent possible has led to implementation difficulties and additional costs which have a disproportionate effect on smaller companies, especially with regards to valuations. These were identified prior to the adoption of FRS 102.

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

Annual reports and accounts are produced for the benefit of stakeholders – principally investors. It is these stakeholders who should be driving developments in the composition of annual reports and accounts. In our experience, investors have unfortunately been particularly too reticent in engaging in the standard setting process.

We believe that the most effective way to drive change in financial (and corporate) reporting is for investors, in a co-ordinated manner, to communicate regularly with their investee companies about the improvements they would like to see made. Too often, we see a disjointed and contradictory response from investors to company matters and voting patterns on annual general meeting resolutions because corporate governance departments do not appear to communicate with the active fund managers.

We would reiterate our comments outlined in response to Q3 regarding representation. The only effective way to improve the quality of standards for financial reporting across all quoted companies in a way that will enhance investor confidence would be to ensure that investors in, and preparers of financial

statements for, small and mid-size quoted companies are sufficiently represented on regulators' boards and panels, in order to facilitate proportionate responses to issues relating to company reports and accounts.

Similarly, there should be regular, meaningful dialogue between the FRC and small and mid-size quoted companies. The QCA is always willing to broker such interaction.

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?

No. As we mentioned in our answer to Q19, investors are the most effective drivers of higher standards in financial and other reporting. They must be encouraged to articulate the changes they wish to see.

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

We have no comments.

Corporate Governance and Stewardship Codes

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?

We have no comments.

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?

Small and mid-size quoted companies are keen to obtain constructive shareholder feedback on matters relating to business strategy, as well as the composition and remuneration of the board. It is imperative that shareholders are willing and able to challenge directors on key issues affecting the company when required.

The Stewardship Code needs to be developed to encourage better direct engagement between investors and companies as it is this direct engagement that is the best facilitator for change.

Speed and effectiveness of investigations; enforcement and compliance

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

Yes – we believe that the FRC is generally reluctant to undertake investigations or enforcement, and do so at speed. Although, on the one hand, we acknowledge that this is partially due to a lack of resources, we also consider - as mentioned in our response to Q13 – that the FRC is too culturally averse to challenging the conduct of the "Big 4" firms.

We note that this was supported by the recent report by the Business, Energy and Industrial Strategy and the Work and Pensions Select Committees, which indicated that neither committee has “faith in the ability of the FRC to complete important investigations in a timely manner.”⁶

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?

We have no comments.

Actuarial oversight

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?

We have no comments.

C. FRC and corporate failure

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

As we discussed in our response to Q8, corporate failure tends to occur due to poor management or negative cash flows. We do not believe that the FRC can do anything to prevent these things directly. However, it can encourage better quality reporting which might enable those few users which consider the content of such reporting in detail to promptly identify the existence of poor management or negative cash flows. In particular the FRC should encourage the IASB to improve the quality of reporting around cash flows, both directly and by facilitating similar conversations between institutional investors and the IASB.

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?

We have no comments.

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?

We have no comments.

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

We believe that the key issue with the effectiveness of the viability statement is that companies too often provide vague, boilerplate statements because neither the FRC nor investors hold companies to account on those disclosures.

Another element that should be considered is that the information gap arises due to the approach taken by the IASB in setting IFRS which does not clearly communicate information about a company’s sources and application of funds and the nature and timing of its liabilities.

⁶ Carillion, Work and Pensions and BEIS Committees (16 May 2018):
<https://publications.parliament.uk/pa/cm201719/cmselect/cmworpen/769/76902.htm>

D. Powers and sanctions

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

Yes – as the joint report published in May 2018 by the Business, Energy and Industrial Strategy and the Work and Pensions Select Committees remarked, “Under its existing powers, the FRC can only take action against those with accounting qualifications.”⁷

We believe that all directors – regardless of whether they are a chartered accountant – should be subject to the same standards.

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

We do not consider 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?

We have no comments.

E. The FRC’s legal status and its relationship with Government

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

Yes – the government should legislate to put the FRC, or similar regulatory body, on a more conventional consolidated statutory footing. Its mission and remit clearly signifies its status of being a public interest body.

We believe that the model used in Finance Act 2012 to establish the Financial Conduct Authority could be suitable.

That said, we would also emphasise that to maximise flexibility and effectiveness, the FRC must be independent of government to the greatest extent possible.

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?

Accountability can only be judged in relation to roles and responsibilities.

If the FRC’s role is to promote trust in UK stock markets, then those best placed to judge its effectiveness are investors.

To the extent that the FRC has other responsibilities it may be best to transfer those to other bodies accountable to other groups. Depending on the responsibilities these other groups may include government.

⁷ Carillion, Work and Pensions and BEIS Committees (16 May 2018):
<https://publications.parliament.uk/pa/cm201719/cmselect/cmworpen/769/76902.htm>

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

Yes – there is a case for further transparency with regards to the backgrounds of those responsible for the supervision of the FRC, as well as with regards to the composition of the FRC’s workforce, to ensure sufficient diversity across all areas of the market.

F. Governance and leadership

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

We believe that the effectiveness of the FRC’s board is significantly stymied by the fact that its membership is dominated by former staff of the ‘Big 4’ accountancy firms and non-executive directors of large listed companies.

Indeed, we note that the FRC’s board⁸ – 15 in total – is composed of seven individuals who hold senior executive or non-executive posts in large listed companies and two former employees of the ‘Big 4’. Just one member has any links to smaller quoted companies. We also note that women compose just over a quarter of the board – less than the target of 33% of women required for FTSE 350 companies.

This particular configuration of the board means that it is unable to convincingly develop proportionate rules for smaller companies.

We believe that, regardless of the institutional structures the review recommends the government pursues, smaller quoted companies must be adequately represented on not only the boards of regulators, but also on all relevant committees. This is imperative to both ensuring that proportionate regulatory requirements can reliably be formulated, but also securing the long-term trust of smaller companies that their interests are being taken into account.

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

No – the Board’s composition is not appropriate. We consider it to be disproportionately balanced towards finance directors of larger companies, former staff of the ‘Big 4’ accountancy firms and investors in large issuers.

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?

No – the balance of decision-making between the Board, its Committees and the Executive is not right, given the legal constraints. Decision making has been centralised in the Board and taken away from expert groups. For example the autonomy of the old Accounting Standards Board is not reflected in the current structure.

⁸ FRC Board Members: <https://www.frc.org.uk/about-the-frc/structure-of-the-frc/frc-board/frc-board-members>

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?

There is no straightforward answer to this question. The appropriate structure will need to reflect the future roles and responsibilities allocated to the FRC. As a standard setter the board should function in a similar manner to the IASC does in respect of the IASB. However as an enforcer a slightly different arrangement may be appropriate.

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

We have no comments.

G. Funding, resources and staffing

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

If the role of the FRC – or other body – is to promote trust in UK public markets, then it is reasonable that companies and investors contribute – through a levy or contributory charge – to the funding arrangements. However, functions such as audit and actuarial supervision should be paid for by audit and actuarial firms.

With regards to the partially voluntary funded regime, several of our small and mid-size AIM-quoted company members have sent us copies of the invoices they received from the FRC with regards to levy payments in the last 18 months.

In our response to the FRC’s draft budget and levy proposals 2018/19⁹, we asked the FRC to be more explicit about the voluntary basis on which the levy is made. Indeed, we noted that there is only a short statement referring to the fact sheet, which fleetingly mentions the fact that payments are made on a voluntary basis. We do not consider this to be either open or transparent.

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?

We have no comments.

⁹ QCA Response to FRC - Strategy 2018/21 & Draft Budget and Levy Proposals 2018/19 (28 February 2018): http://www.theqca.com/article_assets/articledir_281/140806/QCA%20Response%20to%20FRC%20-%20Strat-Budget-Levy%20Proposals_Feb18.pdf

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?

We believe that the FRC must be far more robust in determining the independence of former “Big 4” employees within the FRC’s committees.

There should be clear and detailed rules to define the basis upon which a former partner or member of staff of a “Big 4” (or indeed, any) audit firm is considered independent of their former firm and thus eligible to be involved in regulating or investigating the conduct of that firm.

These rules should specify (among other things): a minimum time limit following the cessation of partnership or employment, and prohibition against consultancy or any fee-earning relationships with the firm concerned as well as of any unpaid advisory roles with it. It may also be appropriate to consider whether people in receipt of a pension directly from an audit firm are independent of it.

H. Other matters

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

We have no further issues to raise.

Appendix 1

Standard setting authority by country				
	Corporate governance	Accounting standards	Actuarial standards	Audit regulation
UK	FRC	FRC	FRC	FRC
France	Haut Comité de gouvernement d'entreprise ¹⁰	The Autorité des Normes Comptables ¹¹ (ANC)	L'Institut des actuaires ¹²	Haut Conseil du commissariat aux comptes (H3C) ¹³
Germany	Regierungskommission Deutscher Corporate Governance Kodex ¹⁴	Accounting Standards Committee of Germany (ASC)	Deutsche Aktuarvereinigung ¹⁵ (DAV)	Auditor Oversight Commission (AOC)
Italy	Comitato per la Corporate Governance ¹⁶	Organismo Italiano Contabilità ¹⁷ (OIC)		The Commissione Nazionale per le Società e la Borsa ¹⁸ (CONSOB)
USA	-	Public Company Accounting Oversight Board (PCAOB)	Actuarial Standards Board (ASB)	Public Company Accounting Oversight Board (PCAOB)
Canada	-	The Accounting Standards Board (AcSB)	Actuarial Standards Board	The Auditing and Assurance Standards Board (AASB)

¹⁰ High Corporate Governance Committee

¹¹ Accounting Standards Authority

¹² Institute of Actuaries

¹³ High Council of Auditors

¹⁴ Government Commission of the German Corporate Governance Code

¹⁵ German Association of Actuaries

¹⁶ Italian Corporate Governance Committee

¹⁷ Italian Accounting Body

¹⁸ The National Commission for Companies and the Stock Exchange