

Section five

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The Board of the Financial Services Authority



Sir Callum McCarthy,
Chairman



Carolyn Fairbairn,
Director of Strategy and Development,
ITV plc
Non-executive Director, Digital UK



Sir James Crosby,
Deputy Chairman
Non-executive Director, ITV plc
Non-executive Director, Compass
Group plc
Trustee, Cancer Research (UK)



Peter Fisher,
Managing Director, BlackRock Inc.



Hector Sants,
Chief Executive



Brian Flanagan,
Non-executive Director, William
Morrison Supermarkets plc
Non-executive Director, Personal
Navigation Systems Ltd.



Sally Dewar,
Managing Director, Wholesale and
Institutional Markets



Karin Forseke,
Member, Financial Markets Advisory
Council, Sweden
Non-executive Director, Royal Opera in
Stockholm
Non-executive Director, Wallenius Lines



Sir John Gieve,
*Deputy Governor (Financial Stability),
Bank of England*



Hugh Stevenson,
*Chairman, Equitas Ltd.
Chairman, The Merchants Trust plc.
Senior Independent Director, Standard
Life plc.*



David Kenmir,
Managing Director, Retail Markets



Iain Brown,
Company Secretary



Professor David Miles,
*Managing Director and Chief UK
Economist, Morgan Stanley and Co. Ltd.
Visiting Professor of Financial
Economics, Imperial College, London*



Andrew Whittaker,
General Counsel



Michael Slack,
*Chairman, Temporary Cover Ltd.
Board Member, British Insurance
Brokers Association
Formerly, Chairman, The Fyfe Group
Ltd.*

Report of the Directors for the year ended 31 March 2008

Throughout the Directors' Report, references are made to the FSA's website. The full addresses are detailed below.

Table 5.1

Financial Risk Outlook	www.fsa.gov.uk/pubs/plan/financial_risk_outlook_2008.pdf
Business Plan	www.fsa.gov.uk/pubs/plan/pb2008_09.pdf
Corporate Responsibility	www.fsa.gov.uk/Pages/About/What/cr/index.shtml
Health & Safety	www.fsa.gov.uk/Pages/Library/Other_publications/Staff/staff_handbook/health/index.shtml
Equal Opportunities	www.fsa.gov.uk/pages/library/other_publications/staff/staff_handbook/working/equal/index.shtml

Table 5.2

Name	Board meetings	Board meetings*	NedCo	RemCo	AuditCo	RiskCo	Original appointment date	Expiry of current term
Clive Briault ^d	9/10	4/5					1.4.04	30.4.08
Sally Dewar	3/3	2/2					9.1.08	8.1.11
Sir James Crosby ^d	9/10	5/5	6/6	1/1	5/5		15.1.04	14.1.10
Carolyn Fairbairn	3/3	2/2	2/2			1/1	11.12.07	10.12.10
Peter Fisher	8/10	4/5	4/6			4/5	19.1.07	18.1.10
Brian Flanagan	9/10	4/5	5/6	1/1	4/5		19.1.07	18.1.10
Karin Forseke ^d	10/10	3/5	6/6		5/5		1.12.04	30.11.10
Sir John Gieve	10/10	3/5	6/6			4/5	16.1.06	15.1.09
Dame Deirdre Hutton ^e	6/7	1/3	4/4	0/0		3/3	11.12.97	10.12.07
David Kenmir ^d	9/10	5/5					1.4.04	31.3.10
Sir Callum McCarthy	10/10	5/5					22.9.03	21.9.08
Professor David Miles ^d	10/10	5/5	6/6			5/5	1.4.04	31.3.10
Hector Sants ^{c & d}	10/10	4/5					4.5.04	19.7.10
Michael Slack ^d	10/10	5/5	6/6	1/1	5/5		1.12.04	30.11.10
Hugh Stevenson ^{a & d}	10/10	5/5	6/6	1/1		5/5	1.6.04	31.5.10
John Tiner ^b	3/3	0/0					22.9.03	19.7.07

Key

a Chairman of FSA Pension Plan Trustee Ltd

b Chief executive until 19 July 2007

c Chief executive from 20 July 2007

d Director serving second concurrent term

e Director serving fourth concurrent term

* Additional meetings to those scheduled at the start of the year, held due to market conditions

Committee membership during the year

Audit Committee (AuditCo)

Sir James Crosby (Chair of AuditCo until 30 September 2007)

Brian Flanagan

Karin Forseke (Chair of AuditCo from 1 October 2007)

Michael Slack

The only members of the FSA are the directors. Each current director has undertaken to guarantee the liability of the FSA up to an amount of £1.

The executive directors are not directors of any UK-listed companies and have no other paid positions.

Risk Committee (RiskCo)

Carolyn Fairbairn (member from 24 January 2008)

Peter Fisher

Sir John Gieve

Dame Deirdre Hutton (member until 10 December 2007)

Professor David Miles

Hugh Stevenson (Chair of RiskCo)

The Deputy Governor (Financial Stability) at the Bank of England is a member of the Board of the FSA. In a reciprocal arrangement with the Bank of England, the FSA's chairman serves as a member of the Court of the Bank of England.

All the FSA's directors are appointed by the Treasury in line with the code of practice issued by the Commissioner for Public Appointments. The chairman of the FSA is appointed for a five-year term and all other directors are appointed for three-year terms. The executive directors have continuous employment contracts with the FSA, details of which are given in the Remuneration Report, and they have three-year renewable terms as directors. Sir Callum McCarthy's five-year term as the FSA's chairman comes to an end on 21 September 2008.

Remuneration Committee (RemCo)

Sir James Crosby (Chair of RemCo from 11 December 2007)

Brian Flanagan

Michael Slack

Hugh Stevenson (member from 24 January 2008)

Dame Deirdre Hutton (Chair of RemCo until 10 December 2007)

Committee of the Non-executive Directors (NedCo)

All Non-executives are members of NedCo

Dame Deirdre Hutton was Chair of NedCo until 10 December 2007

Sir James Crosby became Chair of NedCo from 11 December 2007

Principal activities

The FSA is the primary regulator of financial services in the UK and has statutory responsibilities set out in FSMA. Detailed information on the FSA's principal activities for the year can be found in the first three sections of the Annual Report.

Business review

As a company, it is necessary for the FSA to provide a fair review of its business. This requirement is fulfilled by information provided in the first three sections of the Annual Report.

Principal risks and uncertainties

The principal risk for the FSA is the failure to meet its statutory objectives. The issues that pose risks to the FSA's ability to meet its statutory objectives are explained in the Financial Risk Outlook 2008 (available on the website). All identified risks and uncertainties are kept under review throughout the organisation including at the highest level by the Risk Committee and the Audit Committee. Further information on some of the key areas recently reviewed can be found in the Committees' reports.

Development and performance of the FSA

Analysis of the FSA's performance during the year and the position at the end of the financial year are set out in the Financial Review and the Financial Statements for the year. Future developments of the FSA can be found in the Business Plan for 2008/9 which is available on the FSA's website and provides information relating to the FSA's budget and priorities.

Directors' responsibilities in respect of the accounts

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare financial statements in accordance with international financial reporting standards as adopted by the European Union. The financial statements are required by law to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable international financial reporting standards as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

In so far as the directors are aware:

- there is no relevant audit information of which the company's auditors are unaware; and
- the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Financial position

The FSA's primary source of income is the fees charged to regulated firms. Specific information on the FSA's financial position is provided in the Financial Statements and in the Financial Review. The Financial Review explains how the FSA manages its pensions liabilities. The directors agree with the analysis in the Financial Review and believe the FSA remains able to meet its liabilities as they fall due.

Going concern

The directors are satisfied that the FSA has sufficient resources to continue its business for the foreseeable future and therefore the going concern basis continues to be appropriate in preparing financial statements.

Corporate social responsibility

With regard to corporate responsibility (CR), the FSA aims to be a good corporate citizen and develop projects which will both help the community and be of benefit to staff.

For the FSA to consider undertaking a CR activity it must pass one of three tests. It must:

- support the FSA’s statutory objectives;
- make the FSA a better regulator, as defined in the FSA’s principles of good regulation; or
- it must be considered best practice by the industry and be seen as appropriate for the FSA.

Previously it was reported that the FSA had undertaken a programme to unite its various CR projects. A comprehensive and structured approach is demonstrated on the enhanced CR section of the FSA’s website. A brief summary is provided under the following headings:

Work

The first three sections of the Annual Report detail the FSA’s objectives and strategic aims in terms of work.

People

The FSA aims to be a responsible and diverse employer providing an environment where employees and visitors may feel safe and free from prejudice of any nature. The FSA has policies which outline its approach to diversity, flexible working, learning and development, and wellbeing. Each of these emphasise the FSA’s commitment to its people. The FSA has key performance indicators which focus on these areas. Performance, where possible, is measured and reported on the CR section of the website.

The FSA continues to seek appropriate measures for those areas which are not currently assessed.

Environment

The FSA is conscious of the impact of its operations on the environment and the increasing expectations that organisations should manage these impacts. The FSA aims to reduce CO² emissions, energy use, water and the waste it produces, as well as increase the amount of that waste that is recycled. In order to achieve these aims the FSA seeks to raise awareness of environmental issues among its staff. The relevant targets are measured and reported on the website.

Community

The FSA strives to have a positive impact on society. It encourages, supports and enables staff to play an active role within the local community. Key performance indicators assess the numbers of employees involved in volunteering and the number of community recipients of the FSA’s various projects. Staff are encouraged to view volunteering as a part of their personal development and, to facilitate that, in the coming year all applications for volunteering will be channelled through the FSA’s internal learning and development booking system.

Charitable donations

The FSA made the donations shown in Table 5.3 as part of its community affairs programme.

Health & safety

The FSA is committed to providing a healthy and safe environment for all staff and visitors. It pursues a policy to promote health and safety at work and seeks the cooperation of all employees and visitors in this endeavour.

Equal opportunities

The FSA values inclusiveness and confirms its continuing commitment to the principles of equal opportunities in employment, and in all the activities it undertakes. It endeavours to ensure that all members of staff, visitors and applicants are treated on the basis of their merits and abilities and that no one suffers discrimination or disadvantage regardless of gender, race, disability, sexual orientation, religion or belief and age.

In accordance with the Disability Discrimination Act 2005 and the amended Sex Discrimination Act 1975 the FSA works to eliminate unlawful discrimination and harassment and promote both disability equality and equal opportunities between men and women.

Employee involvement

A variety of media is used to communicate with employees, including the intranet, email, forums and staff meetings. Employees are invited to give feedback on the FSA and its operations both informally and formally through the annual staff survey.

Table 5.3

Recipient	Amount	Reason
Crisis	£8,300	In lieu of producing a corporate Christmas card
Isle of Dogs Community Foundation (IDCF)	£655	Sponsorship of the IDCF Newsletter

Staff are given opportunities to undertake in-house and external training and, during the year, each employee spent an average of 4.5 days training.

The Staff Consultative Committee (SCC) is the forum through which the FSA complies with the EU Information and Consultation Directive 2004. The SCC also provides a clear channel of communication and consultation between the FSA and its staff. It gives staff the opportunity to contribute to and influence the development of the FSA, and to provide their views to the highest levels in the organisation. The FSA recognises the importance and value of ensuring this process happens effectively.

Supplier payment policy

The FSA's policy is to aim to pay 90% of invoices within 30 days of receipt of the invoice. The average time taken to pay suppliers from receipt of invoice was 28 days.

Auditors

In the case of each of the persons who are directors of the company at the date when this report was approved:

- so far as each of the directors is aware, there is no relevant audit information (as defined by Section 234ZA in the Companies Act 1985) of which the company's auditor is unaware; and
- each of the directors has taken all the steps that he or she ought to have taken as a director to make him or herself aware of any relevant audit information (as defined) and to establish that the company's auditor is aware of that information.

RSM Robson Rhodes LLP (Robson Rhodes) merged its audit practice with that of Grant Thornton UK LLP (Grant Thornton) with effect from 2 July 2007, with the successor firm being Grant Thornton. Robson Rhodes resigned as auditors on 6 September 2007, creating a casual vacancy which the Directors filled by appointing Grant Thornton. The members appointed Grant Thornton on 31 October 2007. A resolution to reappoint Grant Thornton as auditors of the company will be proposed at a General Meeting in July 2008.

By Order of the Board
K Iain Brown
Secretary

22 May 2008

Corporate governance statement and remuneration report

Corporate governance statement for the year ended 31 March 2008

Table 5.4

Accountability mechanisms	www.fsa.gov.uk/Pages/About/Who/Accountability/index.shtml
Role of chairman	www.fsa.gov.uk/pages/About/Who/Management/Chairman.shtml
Role of chief executive	www.fsa.gov.uk/pages/About/Who/Management/CEO.shtml
Schedule of matters reserved to the Board	www.fsa.gov.uk/pubs/other/SoM.pdf
Board delegations including terms of reference of the committees	www.fsa.gov.uk/pubs/other/Gov_memo.pdf
Directors' biographies	www.fsa.gov.uk/Pages/About/Who/board/index.shtml
NedCo, RemCo, AuditCo and RiskCo membership	www.fsa.gov.uk/Pages/About/Who/board/committees/index.shtml
Regulatory Decisions Committee membership	www.fsa.gov.uk/pages/about/Who/board/committees/RDC/RDCM/index.shtml
Listing Authority Advisory Committee	www.fsa.gov.uk/Pages/About/Who/board/committees/laa/index.shtml

The FSA is a company limited by guarantee, and as such is not obliged to comply with the Combined Code on Corporate Governance (the Code). However, the Board is committed to meeting high standards of corporate governance and has decided that it is appropriate for the company to comply with the Code insofar as it is applicable to it. Due to this approach, the way in which the FSA is incorporated and the additional legislation applicable to its governance, this report seeks to explain where the FSA complies with the principles in the Code.

FSMA requires that the company has a number of accountability mechanisms, including an Annual Public Meeting. It operates independently of government, but is accountable to Parliament through Treasury ministers. The company is required to consult on its rules and general policy with consumers and practitioners and it does so through the Consumer, Practitioner and Smaller Businesses Practitioner Panels. More information about the accountability mechanisms can be found on the website.

The Board leads the company as a unitary Board and approves the company's strategy and annual operating plan and budget. There is a schedule of matters reserved to the Board and a governance memorandum setting out the delegation of various functions which can be found on the website. The majority of the Board is made up of non-executive directors, who have specific obligations under FSMA. FSMA requires that there is a non-executive directors' committee (NedCo) which keeps under review certain functions of the company. Information on its work is set out in the Report of the non-executive directors.

The Board meets regularly. Details of the number of Board and committee meetings held this year and attendance at those meetings are set out in Table 5.2. The membership of the various committees can also be found in Table 5.2 and on the website.

The roles of the chairman and chief executive of the FSA are split, and responsibilities are set out on the website. The chairman leads the Board, and the chief executive develops and delivers the strategic objectives agreed with the Board. The chairman is independent and the executive directors are not directors of any UK-listed companies, and have no other paid positions.

The non-executive directors of the Board have a variety of skills and experience that are appropriate for the requirements of the company. Notwithstanding any contact they may have with the FSA as a result of being connected with a regulated firm, or as consumers of regulated firms, the non-executive directors are judged to be independent of the company. Where any conflicts of interest arise relating to personal or business matters, there are stringent procedures that are followed to ensure that no director is exposed, and that decisions are taken without undue influence. The Board members also adhere to a code of conduct, which was reviewed during the year.

The chairman ensures, with the company secretary, that the Board's agendas are set in line with the priorities of the company. The company secretary and the chairman review papers in advance of circulation to Board members to ensure that information is accurate and clear. Papers are usually circulated one week before meetings.

One of the non-executive directors acts as chair of the non-executive directors' committee, and is seen as the senior independent director.

Directors of the company are appointed by the Treasury, with input on the selection panel from at least one incumbent member of the FSA Board. The procedures followed are in line with the code of practice issued by the Office of the Commissioner for Public Appointments.

When directors are appointed the company secretary arranges an induction that is appropriate for their knowledge and experience. The Board receives ongoing professional development on issues which are relevant; during the year this included papers for information and presentations on the Companies Act 2006, financial crime and the supervisory process. Information flows have been facilitated during the year with the introduction of a secure website for use by all directors.

The company secretary advises the Board on all aspects of governance matters and will provide access to external professional advice for directors, if required.

Evaluations

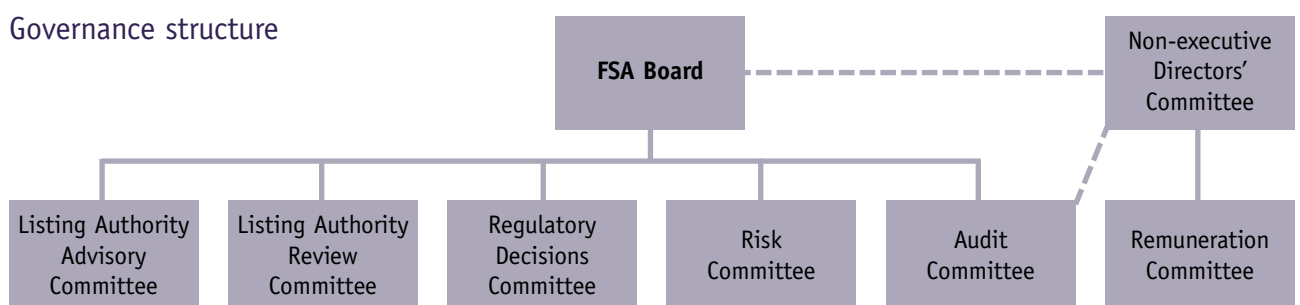
The Board has been involved in several evaluations of performance during the year.

The chairman meets regularly with each director and discusses their individual contribution to the Board.

The non-executive directors have reviewed the performance of the chairman through a combination of the Remuneration Committee, the Board evaluation and discussions at NedCo.

The Board has commissioned a formal evaluation of its own performance, and of the Audit and Risk Committees and the Non-executive Committee. This evaluation was undertaken by external consultants from the Institute of Chartered Secretaries and Administrators. The consultants met with individual directors to discuss aspects of the Board and committees' processes and work. The results of the review were consolidated and the directors discussed these in order to agree an action plan.

Governance structure



The Committee of the Non-executive Directors (NedCo)

NedCo operates in line with the provisions of Schedule 1 to FSMA. Members of NedCo received reports in respect of other Board committees and met together on six occasions during the year to ensure that its statutory functions were being satisfactorily discharged by:

- reviewing reports on the efficient and economic use of the FSA's resources;
- receiving reports on the Audit Committee's (AuditCo) work in keeping under review the question of whether the FSA's internal financial controls secured the proper conduct of its financial affairs;
- receiving reports from the Remuneration Committee (RemCo) on the remuneration awards to the executive directors and the chairman; and the performance-related bonus payments made to the executive directors. Receiving reports from RemCo on its review of the priorities and focus of the executive directors' objectives and approving those objectives;
- considering the position of senior management following the internal audit report on the supervision of Northern Rock; and
- receiving reports from the deputy chairman on the chairman succession process.

NedCo's composition is shown in Table 5.2. Further details on the statutory functions it discharges can be found on the FSA website.

Report of the non-executive directors

The unitary Board (which includes all non-executive directors) is the FSA's primary decision-making body. It also exercises a broad oversight of all the FSA's policy, strategic and operational activities. The extent of the Board's role and the provision of timely and relevant information to the Board, its committees and NedCo, allows NedCo to rely largely on the Board's work while sharing other functions, including oversight of internal controls, with AuditCo. RemCo reports on its work to NedCo.

Efficiency and economy

During the year, NedCo kept under review whether the FSA is using its resources in the most efficient and economic way. Data relating to the measurement of efficiency and economy within the FSA forms part of the management information presented to the Board quarterly, and which is reviewed specifically by NedCo. NedCo challenged information provided to it and sought further explanations when appropriate. NedCo also encouraged enhancements to the reporting framework on a continuous improvement basis and oversaw the development of 'Value for Money' indicators.

Internal financial controls

During the year, NedCo has kept under review the question of whether the FSA's internal financial controls secure the proper conduct of its financial affairs, in conjunction with AuditCo, which is a Board committee. The full statement on internal financial controls is on page 66.

Remuneration of the executive directors

NedCo has delegated to RemCo the function of determining the remuneration of the chairman, the chief executive and the executive directors.

Remuneration Committee (RemCo)

The composition of RemCo is provided in Table 5.2. The functions and terms of reference of RemCo can be found on the website. The terms of reference were redrafted in March 2008 to enable the development of a framework remuneration policy which will enhance scrutiny and oversight in the future. The framework will be summarised in next year's report.

Remuneration report

This section of the Remuneration Report is not subject to audit.

Information on the appointment of the chairman and the executive directors can be found in the Report of the Directors and in the remuneration table (Table 5.9). The executive directors have continuous contracts of employment that provide for 12 months' prior notice of termination by either party.

During the financial year, RemCo approved the financial settlement paid to Clive Briault on his departure from the FSA on 30 April 2008. The settlement is included in the remuneration table below for the year 2007/08 because the FSA was contractually liable to these terms from 13 March 2008. The departure payment comprised £356,452 in respect of salary and bonus, £36,000 in respect of pension contributions, and £202,500 in respect of compensation for loss of office. In addition, external professional fees of £17,500, plus VAT, were approved for payment.

In determining the remuneration of the executive directors, RemCo undertook an evaluation of their performance, assisted by an

assessment of performance against objectives. The objectives for each director took account of the achievement of the FSA's collective FSMA objectives by reference to the Business Plan and the individual director's objectives relating to their areas of responsibility and their leadership abilities. RemCo has the benefit of advice from the director, human resources, and market data from Watson Wyatt, its external consultants. The total remuneration package of the executive directors comprises the same four elements as apply to other FSA employees.

- **Basic pensionable salary**

Salaries are reviewed annually. In setting base salaries for the chairman and executive directors, RemCo aimed, so far as possible, to position these at or around the median market level applying in the private sector.

- **Performance-related bonus**

The executive directors are eligible to be considered for a performance related bonus up to a maximum of 35% of basic pensionable salary. As in previous years, the chairman requested that he was not considered for a bonus. In reaching decisions on

bonus, RemCo took proper account of all aspects of the FSA's performance in a year when the organisation suffered considerable reputational damage.

- **Other benefits**

A sum is available for each employee which may be spent against a range of benefits. The sum for the chairman and executive directors is shown in Table 5.5. The chairman and executive directors also have access to a car and driver, and an appropriate portion of these costs is included in 'other emoluments' in Table 5.9.

- **Pensions**

There are two sections to the FSA Pension Plan (the Plan) operated by the FSA, both of which are non-contributory; a defined benefit section (closed to new entrants) and a defined contribution section. David Kenmir, Clive Briault and Sally Dewar are members of the defined contribution section of the scheme. Before they were appointed as managing directors, David Kenmir and Clive Briault were members of the FSA's defined benefit scheme, and they retain deferred benefits in that section. Sir Callum

Table 5.5

Director	Sir Callum McCarthy	Hector Sants	Sally Dewar	Clive Briault	David Kenmir
Flexible account (£)	29,521.60	27,041.42	6,865.28	20,756.00	19,999.72

McCarthy and Hector Sants are not members of the Plan and are contractually entitled to receive a non-pensionable supplement to their base salary, in lieu. The sums paid to the chairman and each of the executive directors in respect of each component are in Table 5.9.

Non-executive directors

In order to facilitate the independent assessment of fees for non-executive directors, their remuneration is set by an independent panel, the membership of which comprises the chairs of the Practitioner and

Consumer Panels, or their nominees, and an external moderator. In April 2007 the Panel reviewed the fees payable; the Panel increased the fees for non-executive directors, chairs of Board committees and the chairman of FSA Pension Plan Trustee Ltd as shown in Table 5.9.

Emoluments tables

This section of the report, which contains information on directors' emoluments, contains audited information.

At the end of the year, a deferred defined benefit pension was held in the Plan for two executive directors, as a result of their active membership in the defined benefit section of the Plan up to 1 April 2004. From 1 April 2004 those two current executive directors joined the defined contribution section of the Plan. Details of accrued benefits in the defined benefit section are set out in Table 5.6.

Table 5.6

	Accrued pension at 31 March 2007 £'000	Real increase/(decrease) in accrued pension £'000	Inflation £'000	Accrued pension at 31 March 2008 £'000 ¹
Clive Briault	74	–	3	77
David Kenmir	54	–	2	56

¹ The defined benefit entitlement is based on pensionable service to 1 April 2004 and final pensionable salary as at 1 April 2004. The directors ceased to accrue any further benefits in the defined benefit section of the Plan from 1 April 2004. The directors' pension entitlement at their normal retirement date will be the leaving service pension at 1 April 2004 increased broadly by the change in the retail price inflation index (capped at 5% p.a.) between 1 April 2004 and date of retirement, calculated in accordance with legislation and the rules of the Plan. Any pension from the defined contribution section of the Plan will be paid in addition to this pension.

Table 5.7 sets out the transfer values of those directors' benefits under the scheme, calculated in a manner consistent with 'Retirement Benefit Schemes – Transfer Values (GN11)', published by the Institute of Actuaries.

Table 5.7

	Transfer value at 31 March 2007 £'000	Transfer value of real increase in accrued pension £'000	Other changes to transfer value £'000	Transfer value at 31 March 2008 £'000
Clive Briault	872	–	59	931
David Kenmir	488	–	5	493

Members of the Plan have the option to pay additional voluntary contributions; neither contributions nor the resulting benefits are included.

During the year, payments were made into the defined contribution section of the pension scheme for three executive directors, these payments are set out in Table 5.8 below.

Table 5.8

Director	Clive Briault ¹	Sally Dewar	David Kenmir
Pension contributions into the defined contribution section of the pension scheme – £'000	36	6	36

¹ In addition to the above figure, a contribution of £36,000 was paid into the defined contribution section of the pension scheme as part of Clive Briault's departure terms.

Table 5.9

	Board fee £	Salary £	Performance related bonuses £	Other emoluments and benefits £	Compensation for loss of office £	2008 Total £	2007 Total £
Sir Callum McCarthy (Chairman)	–	396,000	–	84,553	–	480,553	433,565
Executive Directors							
Clive Briault ¹	–	300,000	30,000	24,759	528,952	883,711	373,829
Sally Dewar ²	–	67,295	–	4,372	–	71,667	–
David Kenmir	–	300,000	75,000	24,003	–	399,003	399,253
Hector Sants ³	–	417,179	114,000	130,769	–	661,948	482,829
John Tiner ⁴	–	138,250	–	307,371	–	445,621	652,577
Non-executive Directors⁵							
Dame Deirdre Hutton CBE ⁶	45,692	–	–	–	–	45,692	60,000
Sir James Crosby ^{6,7}	42,726	–	–	–	–	42,726	32,500
Tom de Swaan ⁸	–	–	–	–	–	–	25,720
Carolyn Fairbairn ¹¹	8,154	–	–	–	–	8,154	–
Peter Fisher ⁹	–	–	–	–	–	–	–
Brian Flanagan	26,500	–	–	–	–	26,500	4,905
Karin Forseke ⁷	30,500	–	–	–	–	30,500	25,000
Sir John Gieve ⁹	–	–	–	–	–	–	–
Kyra Hazou ⁸	–	–	–	–	–	–	20,095
Professor David Miles	26,500	–	–	–	–	26,500	25,000
Michael Slack	26,500	–	–	–	–	26,500	25,000
Hugh Stevenson ^{7,10}	53,500	–	–	–	–	53,500	44,375
Clive Wilkinson ⁸	–	–	–	–	–	–	20,095
	260,072	1,618,724	219,000	575,827	528,952	3,202,575	2,624,743
Of which fees for service as Directors					–	260,072	282,690
Remuneration as executives					–	2,942,503	2,342,053
						3,202,575	2,624,743

- Clive Briault left the company on 30 April 2008. His compensation for loss of office figure includes various elements, including £326,452 in respect of salary. Further information on his departure terms are reported at page 62.
- Sally Dewar was appointed as an executive director from 9 January 2008.
- The total emoluments of the highest paid director during the year, Hector Sants, were £661,948 (2007: £482,829).
- John Tiner resigned as a director of the company on 19 July 2007. Included in other emoluments and benefits is an amount of additional salary and benefits of £227,500, which covered the period from 20 July 2007 to 19 January 2008. Mr Tiner remained on the payroll until January 2008 because under the terms of his agreement he was not allowed to work for any other financial services business or listed company during that time.
- The fee for a non-executive director was set by the independent panel, established with the approval of the Treasury, at £26,500 per annum with effect from 1 April 2007.
- Dame Deirdre Hutton CBE stood down from the Board and as deputy chairman on 10 December 2007. Sir James Crosby was appointed as deputy chairman from 11 December 2007. The fee payable to the deputy chairman was set by the independent panel at £66,000 per annum with effect from 1 April 2007 (2006/7: £60,000, fee set on 1 April 2005).
- An additional fee of £8,000 a year is paid to any non-executive director (other than the deputy chairman) who has been appointed to chair a committee of the Board. (2006/7: £7,500) Hugh Stevenson chaired the Risk Committee throughout the year. James Crosby chaired the Audit Committee until 30 September 2007. Karin Forseke assumed the role of chair of the Audit Committee on 1 October 2007.
- Tom de Swaan, Kyra Hazou and Clive Wilkinson all retired as directors on 18 January 2007 and their fees were pro-rated for 2006/07.
- Sir John Gieve and Peter Fisher both waived their Board fee in respect of the years concerned.
- Hugh Stevenson also chaired the Board of FSA Pension Plan Trustee Ltd in the year. The annual fee was set by the independent panel at £19,000 with effect from 1 April 2007 (2006/7: £17,500).
- Carolyn Fairbairn was appointed as a non-executive director from 11 December 2007.

Committees of the Board

Audit Committee (AuditCo)

The role of AuditCo is to advise the Board on the robustness of the FSA's financial management and the adequacy and effectiveness of the internal controls used by the executive to manage the organisation's operational risk. AuditCo also has primary responsibility for recommending to the Board the appointment of the external auditors. AuditCo's terms of reference can be found on the FSA's website.

Karin Forseke succeeded Sir James Crosby as Chair of AuditCo on 1 October 2007, although Sir James remains a member of AuditCo. The composition of AuditCo can be found in Table 5.2. AuditCo's members have considerable financial and commercial experience and further details can be found on the FSA's website.

AuditCo met on five occasions during the year; an additional meeting was added to the normal schedule to review the internal audit review of the regulation of Northern Rock. Members of senior management attended each of the four regular meetings by invitation. In accordance with its normal practice AuditCo also held private sessions with both the external and the internal auditor, at each of the regular meetings, without management being present. At the additional meeting a private session was held with the internal auditor only.

AuditCo considered a number of fixed agenda items at each meeting, as well as other matters as appropriate. The activities carried out by AuditCo during the year included:

- monitoring the integrity of the financial statements and providing challenge to management on the FSA's financial performance;
- reviewing judgement applied and disclosure issues in relation to the FSA's financial statements;
- a review of the FSA's treasury management policy;
- consideration of the internal audit review of the regulation of Northern Rock;
- regular reviews of key risks to the FSA's operations, including knowledge management, human resources and IT risks, such as the development of the alerts and risk indicator engine and consideration of management's assessment of the risks through challenge to the risk ratings and actions taken to address the risks;
- reviews of compliance by FSA staff with all key internal processes and procedures;
- consideration of quarterly reports from the internal audit division including approval and ongoing reviews of the Audit Universe and Audit Plan;
- continued oversight of the implementation of operational improvements by the internal audit division;
- consideration of the disclosure of summary internal audit reports;
- a review of the adequacy and effectiveness of the internal audit function;
- a review of the quality, reliability, independence and effectiveness of the external auditor, Grant Thornton UK LLP;
- consideration of the external auditor's audit strategy for the financial year;
- a review of the organisation's whistleblowing policy;
- consideration of updates on potential litigation against the FSA; and
- a review of AuditCo's terms of reference to ensure they remained in line with best practice.

In order to provide a safeguard in respect of the external auditor's objectivity and independence, the FSA has a policy relating to the restriction of non-audit work. Further information is provided in Note 5 to the financial statements.

Risk Committee (RiskCo)

RiskCo's purpose is to assist the Board in reviewing risks to its statutory objectives, focusing on the risks to the environment in which the FSA regulates. RiskCo does not review internal risks or day-to-day risks to the FSA's operations, which are the responsibility of AuditCo, nor does it review individual firms. Further information on RiskCo's terms of reference can be found on the FSA's website. Information on RiskCo's membership and attendance at meetings can be found in Table 5.2.

RiskCo has made use of the FSA executive's risk management and reporting system which records all risks identified and reviewed by local business areas. The risks are reviewed and appropriate mitigation strategies put in place by the executive.

In reviewing the risks, RiskCo has considered whether the executive has appropriately assessed the risk by challenging the risk rating, whether the action taken to address and mitigate the risk is effective, and whether the timescales are appropriate. RiskCo has also considered whether there are other risks that should be reviewed and advised the executive accordingly.

RiskCo reports to the Board on its consideration of the risk areas and provides feedback into the risk management system as required.

Over the year RiskCo has considered a diverse range of risks and mitigation strategies including:

- the structure of the FSCS for coping quickly with failures by major deposit takers;
- the effectiveness and communication of the FSA's small firms strategy;
- sub-prime lending in the United States and the possible effect on FSA regulated firms and consumers as a result;
- the possible effects of risk-based regulation on increases in the FSA's scope;
- payment protection insurance sales;
- the various risks relating to financial crime (including information security standards, consumer driven fraud, money laundering controls and politically exposed persons);
- the implications of firms or the FSA failing to deliver on treating customers fairly;
- effects of reduced liquidity, credit derivatives, valuations and confidence in the tripartite arrangements and the financial system; and
- international crisis management effectiveness.

Internal controls

The Board is responsible for ensuring that a system of internal controls is in place, and for reviewing its effectiveness in respect of financial, operational and compliance controls and risk management systems. The system is designed to provide reasonable, but not absolute, assurance against material misstatement or loss and to manage, rather than eliminate, risks to the FSA's statutory objectives. The Board's policy on internal controls and risk management includes established processes and procedures for identifying, evaluating and managing the significant risks faced by the FSA.

The Board believes that the processes are in line with the guidance set out in the Turnbull Report. They have been in place throughout the year under review and up to the date of the approval of the Report and Accounts. They are intended to ensure that, in the event of a problem arising, it is drawn to the attention of management in a timely way and appropriate remedial action taken.

AuditCo assists the Board and NedCo by receiving and considering reviews conducted by the internal audit division of the adequacy of the control processes and challenging the executive on their effectiveness. These reviews are conducted throughout the year.

Regulatory Decisions Committee (RDC)

The RDC takes those enforcement, authorisation and supervisory decisions that are of material significance for the firms and individuals concerned. Members of the RDC are appointed by the Board. The Board receives quarterly reports from the RDC chairman, who also attends Board meetings twice a year to discuss significant matters in those reports. More details on the role and membership of the RDC can be found on the FSA website.

Listing Authority Committees

The Board has two listing committees made up of external practitioners to advise the Board and review elements of the FSA's function as the competent authority for listing in the UK. The Listing Authority Advisory Committee (LAAC) met three times during the year, with smaller sub-groups meeting more frequently to consider particular issues. The chairman provided reports to the Board on relevant issues.

The Listing Authority Review Committee, whose role is as a technical appeal committee, has not been called during the year. More details on membership of the committees can be found on the FSA website.

Independent auditors' report to the members of the Financial Services Authority

We have audited the financial statements of the Financial Services Authority for the year ended 31 March 2008 which comprise the income statement, the statement of recognised income and expense, the balance sheet, the statement of cash flows and related notes 1 to 21. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Corporate Governance Statement regarding directors' remuneration that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, the part of the Corporate Governance Statement regarding directors' remuneration to be audited, and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements and the part of the Corporate Governance Statement regarding directors' remuneration to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Corporate Governance Statement regarding directors' remuneration to be audited are properly prepared in accordance with the Companies Act 1985. We report to you whether in our opinion the information given in the

Directors' Report is consistent with the financial statements. The information given in the Directors' Report includes the specific information presented in the Financial Review that is cross referred from the Business Review section of the Directors' report.

In addition, we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report, and consider whether it is consistent with the audited financial statements. The other information comprises only the Directors' Report, the unaudited part of the Corporate Governance Statement, the Chairman's Statement and the Financial Review. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Corporate Governance Statement regarding directors' remuneration to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Corporate Governance Statement regarding directors' remuneration to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Corporate Governance Statement regarding directors' remuneration to be audited.

Opinion

In our opinion:

- The financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of affairs of the company as at 31 March 2008 and of its deficit for the year then ended.
- The financial statements and the part of the Corporate Governance Statement regarding directors' remuneration to be audited have been properly prepared in accordance with the Companies Act 1985.
- The information given in the Directors' Report is consistent with the financial statements.

Separate opinion in relation to IFRS

As explained in Note 2, the company, in addition to applying the IFRS adopted by the European Union has also complied with the IFRS as issued by the International Accounting Standards Board.

In our opinion the financial statements give a true and fair view, in accordance with IFRS, of the state of the company's affairs as at 31 March 2008 and of its deficit for the year then ended.

Grant Thornton UK LLP
Chartered Accountants and
Registered Auditors

London, England
22 May 2008

Financial statements for the year ended 31 March 2008

Income statement for the year ended 31 March 2008

	Notes	2008 £m	2007 £m
Administrative costs		(332.7)	(295.8)
Interest on bank deposits		5.7	5.1
Other net finance income	15	1.8	1.0
Other revenue	7	20.5	26.0
Net costs for year		(304.7)	(263.7)
Fee revenue		303.3	282.1
(Deficit)/Surplus before taxation	5	(1.4)	18.4
Taxation	8	(1.7)	(1.5)
(Deficit)/Surplus after taxation		(3.1)	16.9

All results are derived from continuing operations.

Statement of recognised income and expense for the year ended 31 March 2008

	Notes	2008 £m	2007 £m
(Deficit)/Surplus for the year		(3.1)	16.9
Actuarial gains and losses for the year in respect of the defined benefit pension scheme	15	(13.9)	(14.2)
Total recognised income and expense for the year		(17.0)	2.7

Balance sheet as at 31 March 2008

	Notes	2008 £m	2007 £m
Non current assets			
Intangible assets	9	31.3	15.1
Property, plant and equipment	10	41.0	18.2
		72.3	33.3
Current assets			
Trade and other receivables	11	13.7	10.6
Trading investments	12	–	1.9
Cash and cash equivalents	11	24.8	47.8
		38.5	60.3
Total assets		110.8	93.6
Current liabilities			
Trade and other payables	13	(103.1)	(79.1)
Current tax liabilities		(0.9)	(0.8)
		(104.0)	(79.9)
Total assets less current liabilities		6.8	13.7
Non current liabilities			
Trade and other payables	13	(13.3)	(13.1)
Long term provisions	14	(0.3)	(2.1)
Net liabilities excluding retirement benefit obligation		(6.8)	(1.5)
Retirement benefit obligation	15	(91.6)	(79.9)
Net liabilities, including retirement benefit obligation		(98.4)	(81.4)
Accumulated deficit	16	(98.4)	(81.4)

The financial statements were approved and authorised for issue by the Board on 22 May 2008, and were signed on its behalf by:

Callum McCarthy..... Chairman

Hector Sants..... Chief executive officer

Statement of cash flows for the year ended 31 March 2008

	Notes	2008 £m	2007 £m
Net cash generated from operations	21	27.0	8.5
Corporation tax paid		(1.6)	(1.5)
Net cash from operating activities		25.4	7.0
Investing activities			
Interest received on bank deposits		5.7	5.1
Expenditure on software development	9	(23.8)	(10.3)
Purchases of property, plant and equipment	10	(32.2)	(7.9)
Sale of trading investments		1.9	16.3
Net cash (used in) / generated from investing activities		(48.4)	3.2
Net (decrease) / increase in cash and cash equivalents		(23.0)	10.2
Cash and cash equivalents at the start of the year		47.8	37.6
Cash and cash equivalents at the end of the year		24.8	47.8

Notes to the financial statements – 31 March 2008

1. General information

The Financial Services Authority (the Authority) is a company incorporated in the United Kingdom under the Companies Act 1985. The address of the registered office is given on page 2. The nature of the Authority's operations and its principal activities are set out on page 56.

These financial statements are presented in pounds sterling because that is the currency of the primary economic environment in which the Authority operates.

At the date of the authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective:

- IAS 1 Presentation of Financial Statements (revised 2007) (effective 1 January 2009)
- IAS 23 Borrowing Costs (revised 2007) (effective 1 January 2009)
- Amendment to IAS 32 Financial Instruments: Presentation and IAS 1 Presentation of Financial Statements - Puttable Financial Instruments and Obligations Arising on Liquidation (effective 1 January 2009)
- IAS 27 Consolidated and Separate Financial Statements (revised 2008) (effective 1 July 2009)
- Amendment to IFRS 2 Share-based Payment - Vesting Conditions and Cancellations (effective 1 January 2009)
- IFRS 3 Business Combinations (revised 2008) (effective 1 July 2009)
- IFRS 8 Operating Segments (effective 1 January 2009)
- IFRIC 12 Service Concession Arrangements (effective 1 January 2008)
- IFRIC 13 Customer Loyalty Programmes (effective 1 July 2008)
- IFRIC 14 IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective 1 January 2008). If in future years a net surplus on our pension obligation does arise, then this standard would apply. However, it is currently considered unlikely that we will be in this situation next year.

The directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material impact on the financial statements of the Authority.

2. Significant accounting policies

The financial statements have been prepared on an historical cost basis, except for revaluation of financial assets. The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). The financial statements have also been prepared in accordance with IFRS as adopted by the European Union. The principal accounting policies adopted are set out below:

a. Income statement

The format of the income statement on page 69 has been designed to show net costs before fees levied to cover those costs. It is considered that this format best represents the nature of the activities of the FSA, which involves carrying out statutory functions and levying fees to meet the net cost of those functions.

b. Revenue recognition

All fee revenue is receivable under the Financial Services and Markets Act 2000 (FSMA), is measured at fair value, and represents the fees to which the FSA was entitled in respect of the financial year.

Sundry income is recognised so as to match revenue to the cost of delivering the relevant services we provide (e.g. training courses).

Interest received on bank deposits is accrued on a time basis by reference to the principal outstanding and the effective interest rate applicable.

c. Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses.

Depreciation is calculated to write off the cost less estimated residual value on a straight-line basis over the expected useful economic lives. The principal useful economic lives used for this purpose are:

Leasehold improvements	Up to ten years
Computer equipment (excluding software)	Up to three years
Furniture and equipment	Up to ten years

If events or changes in circumstances indicate the carrying value may not be recoverable then the carrying values of tangible fixed assets are reviewed for impairment.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

d. Recognition of enforcement expenses

All costs incurred to the end of the year are included in the accounts, but no provision is made for the costs of completing current work unless there is a present obligation.

In the course of its enforcement activities, the FSA gives indemnities to certain provisional liquidators and trustees. Provision is made in the accounts for costs incurred by such liquidators and trustees to the year end and estimated to be recoverable from the FSA under such indemnities. The amount provided is discounted to present value.

e. Retirement benefit costs

The company operates an occupational pension scheme, the FSA Pension Plan (the Plan), for its employees. There are two sections in the Plan: the Final Salary section (a defined benefit arrangement which is closed to new members) and the Money Purchase section (a defined contribution arrangement for new entrants).

Defined contribution scheme – payments to the defined contribution section are recognised as an expense in the income statement, as they fall due.

Defined benefit scheme – the charge to the income statement is the current service, past service, and interest costs of the scheme liabilities, less the expected return on the scheme's assets.

The obligation in respect of the defined benefit pension scheme represents the present value of future benefits owed to employees in return for their service in the current and prior periods. The discount rate used to calculate present value of those liabilities is the market rate at the balance sheet date of high quality corporate bonds having maturity dates approximating to the terms of those liabilities. The calculation is performed by a qualified actuary using the projected unit credit method at each balance sheet date.

Past service cost is recognised immediately to the extent that the benefits are vested, and otherwise is amortised on a straight-line basis over the average period until the benefits become vested.

The net liabilities of the defined benefit scheme are calculated by deducting the fair value of the scheme's assets from the present value of its obligations, and disclosed as a non-current liability on the balance sheet.

Actuarial gains and losses arising in the defined benefit scheme (for example the difference between actual and expected return on assets, effects of changes in assumptions and experience losses arising on scheme liabilities) are recognised in full in the statement of recognised income and expense in the period in which they are incurred.

f. Financial penalties received

Under the FSMA, the FSA has the power to levy financial penalties, but it is required to apply those penalties for the 'benefit of its fee-payers' which means that though the penalty payments are collected by the FSA, the FSA have no rights to recognise these amounts as revenue. If the FSA were to cease activities, then penalties held at that time would be payable to fee-payers.

Accordingly, any remaining balance is then included in current liabilities: trade and other payables. The FSA is required to apply penalties received in each financial year to reduce the amount owed by fee-payers in the relevant fee-block in the following financial year.

g. Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are treated as operating leases.

Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the lease. Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

h. Intangible assets

Costs associated with the development of software for internal use are capitalised only if the design of the software is technically feasible, and the FSA has both the resources and intent to complete its development and ability to use it upon completion. In addition, costs are only capitalised if the asset can be separately identified, it is probable that the asset will generate future economic benefits, and that the development cost of the asset can be measured reliably. Expenditure on research activities is recognised as an expense in the period in which it is incurred.

Only costs that are directly attributable to bringing the asset to working condition for its intended use are included in its measurement. These costs include all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in a manner intended by management.

Internally generated intangible assets are amortised on a straight-line basis over their expected useful lives, generally between three and seven years with the expense reported as an administration expense in the income statement. Subsequent expenditure is only capitalised when it increases the future economic benefits embodied in the specific asset to which it relates.

Where no internally generated intangible asset can be recognised, development expenditure is charged to the income statement when incurred.

i. Impairment of tangible and intangible assets

At each balance sheet date, the FSA reviews the carrying value of its tangible and intangible assets to determine whether there is any indication that those assets have suffered impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and risks to the

specific asset for which the estimates of future cash flows have not been adjusted. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

When an impairment loss subsequently reverses, the carrying amount is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

j. Financial instruments

Trade receivables – Trade receivables are measured at amortised cost. Appropriate allowances for estimated irrecoverable amounts are recognised in the income statement when there is objective evidence that the asset is impaired. The allowance recognised is measured as the difference between the asset's carrying value and the estimated future cashflows deriving from the continued use of that asset, discounted if the effect is material.

Investments – Cash deposits with a maturity date in excess of 90 days at inception are reported at fair value and are not subject to a significant risk of changes in value.

Trade payables – Trade payables are not interest bearing and stated at nominal value.

Financial guarantee contracts – Financial guarantee contracts are initially recognised at fair value. Subsequently, they are measured at the higher of an amount determined in accordance with IAS 37 'Provisions, contingent liabilities and contingent assets', and the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with IAS 18 'Revenue'.

The company's financial risk management policy is disclosed on page 49.

k. Cash and cash equivalents

Cash and cash equivalents comprise cash-in-hand, demand deposits and other short-term liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

l. Provisions

Provisions are recognised when the FSA has a present obligation as a result of a past event, and it is probable that the FSA will be required to settle that obligation. Provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the balance sheet date and are discounted to present value where the effect is material.

Legal challenges – On occasion, legal proceedings are threatened or initiated against the FSA. The FSA provides for the estimated full cost of any such challenges where at the end of the year it is more likely than not that there is an obligation to be settled. The amount provided is discounted to present value where the effect is material.

m. Taxation

The tax expense represents the sum of tax currently payable.

3. Critical accounting judgements and key sources of estimation uncertainty

Critical judgements in applying the Authority's accounting policies

In the process of applying the Authority's accounting policies, which are described in note 2, management has made the following judgements that have the most significant effect on the amounts recognised in the financial statements (apart from those involving estimations, which are dealt with below):

- Intangible assets – under IAS 38, internal software development costs of £23.9m (2007: £10.3m) have been capitalised. Internally developed software is designed to help the Authority carry out its various statutory functions by, for example: holding details relating to regulated firms, for example their Part IV permissions under the FSMA 2000, and to their senior management; facilitating the collection and collation of regulatory data from those firms; assisting our staff in the supervision of those firms by generating reports and alerts; and operating the ARROW II methodology for regulating authorised firms. These functions are particular to the FSA, so our internally-developed software generally has no market value. Management judgement has been applied in quantifying the benefit expected to accrue to the FSA over the useful life of the relevant assets. Those expected benefits relate to the fact that such software allows us to carry out our functions more efficiently than by using alternative approaches (for example manual processing). If the benefits expected do not accrue to the FSA (for example, if some aspect of our approach to discharging our statutory functions changes, perhaps due to the impact of implementing a European Directive), then the carrying value of the asset would require adjustment.

Key sources of estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to carrying amounts of assets and liabilities in the next financial year are discussed below:

Pension deficit – the quantification of the pension deficit is based upon actuarial assumptions made by the directors (as listed in note 15) relating to rate of increase in salaries, the discount rate, the expected return on the Plan's assets, retail price inflation and future pension increases.

- The assumptions regarding returns on assets are based on market observables for cash (Bank of England's base rate), corporate bonds (15-year AA-rated corporate bond index) and, for equities, the yield on the ten-year benchmark gilt index adjusted by an assumed equity risk premium of 3.0% p.a.
- The discount rate was determined with reference to the market rate of a selection of corporate bonds at the year end, allowing for the anticipated maturity of the Plan's projected benefit cash-flow profile. The increase in the discount rate assumption since last year (from 5.2% to 6.0% p.a.) decreased the pension liability by £65.4m.
- The assumption for long-term retail price inflation (r.p.i.) is based on market expectation of long-term future inflation at the year end, as measured by the difference between yields on fixed interest and index-linked government bonds, reduced by 0.2% p.a. so as to allow for other data sources, such as the Bank of England's long-term inflation target and other long-term consensus indicators. The increase in the r.p.i. assumption from 3.0% to 3.4%p.a. increased the pension liability by £28.2m.
- The rate of salary increases is consistent with that used by the directors for long-term budgeting purposes. Generally, the level of annual pension increases awarded by the Plan for pensions in payment is the annual increase in r.p.i., or 5%p.a. if lower, although some of the pensions rights transferred in from the FSA's predecessor organisations receive different level of pensions increases.
- The assumptions relating to the mortality of current and future pensioners have changed since last year to reflect more up to date projections of future mortality improvements. In particular, the projection of improvements to post retirement mortality has been changed from a 'medium cohort' projection to a 'long cohort' projection. The cohort effect describes the phenomenon in the UK whereby population cohorts born between 1925 and 1945 have experienced faster improvements in mortality over their lifetime than adjacent generations. There are 'short', 'medium' and 'long' cohort projections and these represent how long into the future it is expected mortality will continue to improve. The medium cohort projection assumes improvements to 2020 and the long cohort projection to 2040. This is consistent with the assumption used in our Scheme Specific Valuation at 1 April 2007. The change in this assumption increased the pensions liability by £12.9m.
- The effect of any change to these assumptions will be accounted for in the next financial year through the statement of recognised income and expense.

4. Business and geographical analysis

Business units

For management purposes, the FSA is currently organised into four business units – Wholesale & Institutional Markets, Retail Markets, Regulatory Services and Corporate Services and Board.

The principal activities for the four business units are as follows:

Retail Markets – helping retail consumers obtain a fair deal. This business unit's work is aimed at establishing the four main features of an effective and efficient retail market: capable and confident consumers; clear, simple and understandable information from the industry and the FSA, available for, and used by, consumers; responsible firms who treat their customers fairly, are soundly managed and adequately capitalised; and risk-based regulation, through firm-specific and thematic supervision and policy.

Wholesale & Institutional Markets – maintaining efficient, orderly and clean markets. Much of this business unit's work is aimed at establishing and maintaining high standards in the markets which operate in the UK. This embraces questions of disclosure, corporate governance and market behaviour, for which the FSA has varying degrees of responsibility and of influence, as well as other matters, such as supervision, capital adequacy, or the listing regime where the FSA's responsibilities and powers are unambiguous.

Regulatory Services – making the FSA a more effective organisation. Providing an accurate and timely service to firms, consumers and other stakeholders (for example, in processing application for waivers and guidance, handling calls to our consumer help lines, and in receiving and processing regulatory returns). The business unit also manages the FSA's office facilities, IT systems and working capital.

Corporate Services and Board – provides the resources that the Board requires to discharge its stewardship and corporate governance responsibilities, and to devise, implement and monitor the FSA's strategy. This includes the cost of the FSA's enforcement activities.

Segment information about the FSA's continuing operations is presented on the next page.

2008 Year ended 31 March 2008	Wholesale & Institutional Markets	Retail Markets	Regulatory Services	Corporate Services and Board	Total for continuing operations
	£m	£m	£m	£m	£m
Revenue					
Fees			303.3		303.3
Sundry income	7.3	0.9	10.9	1.4	20.5
Result					
Segmental (deficit)/surplus	(77.6)	(124.3)	259.9	(66.9)	(8.9)
Investment income					5.7
Other net finance income					1.8
Deficit before tax					(1.4)
Income tax expense					(1.7)
Deficit for year					(3.1)

Other information

Capital additions:

Tangible			32.2		32.2
Intangible			23.8		23.8
Depreciation			(8.8)		(8.8)
Amortisation			(5.2)		(5.2)
Trade receivables impairment losses recognised			(0.6)		(0.6)
Current and past pension service costs	2.0	2.8	4.0	1.5	10.3

2007**Year ended 31 March 2007****Revenue**

Fees			282.1		282.1
Sundry income	7.0	1.3	17.0	0.7	26.0

Result

Segmental surplus/(deficit)	(69.9)	(102.8)	244.3	(59.3)	12.3
Investment income					5.1
Other net finance income					1.0
Surplus before tax					18.4
Income tax expense					(1.5)
Surplus for year					16.9

Other information

Capital additions:

Tangible			7.9		7.9
Intangible			10.3		10.3
Depreciation			(9.1)		(9.1)
Amortisation			(5.3)		(5.3)
Trade receivables impairment losses recognised			(0.6)		(0.6)
Current and past pension service costs	(2.1)	(2.8)	(2.9)	(1.9)	(9.7)

Balance Sheet analysis

Whereas the FSA allocates its costs to business segments, as set out above, it does not allocate assets and liabilities to those segments. This is for two reasons: first, as fees are not set on the basis of the costs we incur in regulating individual firms, our working capital cannot be allocated to business segments; and second, as we are not a profit making organisation, we do not consider return on capital measures.

Geographical analysis

The FSA regulates entities that operate within the UK financial services industry including the regulation of foreign domiciled entities operating within the UK. The foreign domiciled entities account for less than 10% of the fee base of the FSA. No further geographical analysis is presented.

5. Surplus before taxation for the year

Surplus for the year has been arrived at after charging the following, which are included in administrative costs:

	Note	2008	2007
		£m	£m
Depreciation of property, plant and equipment	10	8.8	9.1
Amortisation of intangible assets	9	5.2	5.3
Impairment loss on intangible fixed assets	9	2.4	–
Staff costs	6	185.7	186.7
Operating lease rentals	18	12.4	11.8

Auditor's remuneration for audit services as set out below.

In accordance with our accounting policy, we review the carrying value of intangible assets to determine whether there has been any impairment loss, and if so, the extent. During the year, in support of our Small Firms Strategy, we amended the design of our Alerts and Risk Indicator (ARI) system part of the way through the development project, building on part of the development to date and not pursuing further other original design and build elements. This resulted in an impairment charge of £2.4m.

RSM Robson Rhodes LLP were appointed as auditor on 15 September 2005, accepting the appointment on 13 January 2006. On 1 July 2007, RSM Robson Rhodes LLP merged with Grant Thornton to form a new partnership, Grant Thornton UK LLP (GTUK). Accordingly, on 6 September 2007 Robson Rhodes LLP resigned as auditor and on 27 September 2007 GTUK accepted the appointment.

Total fees	12 months to 31 March 2008		12 months to 31 March 2007	
	£'000	%	£'000	%
Fees payable to the FSA's auditor for the audit of the FSA's annual accounts	82	57	79	98
Fees paid to the FSA's auditor or their associates in connection with non-audit work				
• Secondments	63	43	–	–
• Other services	–	–	2	2
Total	145	100	81	100

All fees payable to the auditor are stated inclusive of VAT, as VAT is not generally recoverable by the FSA.

Staff seconded by GTUK to the FSA worked as forensic accountants on various investigations conducted by our Enforcement division. They were not involved in the preparation of the FSA's statutory accounts. The Audit Committee has reviewed the nature and content of that non-audit work performed by the auditor to ensure that audit independence was not impaired.

In order not to impair the actual and perceived independence of its auditor the FSA has a policy of limiting the amount of fees its auditor charges for non-audit services to no more than the fee for performing the audit of its annual accounts. Both the FSA and its auditor are committed to keeping the level of fees for non-audit services in-line with its policy on such fees.

6. Employee information

The average number of employees (including executive directors) during the year was 2,489 (2007: 2,659). The average number of employees in each function during the current year was as follows:

	2008	2007
Retail Markets Business Unit	750	773
Wholesale & Institutional Markets Business Unit	555	572
Regulatory Services Business Unit	734	791
Corporate Services and Board (excluding enforcement)	252	277
Enforcement	198	246
	2,489	2,659

At 31 March 2008, the FSA had 2,535 (2007: 2,606) employees.

Employment costs (including executive directors) comprise:

	Notes	2008 £m	2007 £m
Gross salaries and taxable benefits		150.3	150.6
Employer's National Insurance costs		16.1	16.4
Employer's pension costs included in administrative costs		19.3	19.7
	5	185.7	186.7
Employer's pension (income)/ costs reported elsewhere			
Included in other finance (income)	15	(1.8)	(1.0)
Included in statement of total recognised income and expenditure	15	13.9	14.2
Total employment costs		197.8	199.9

7. Other revenue

Other revenue comprises:

	2008 £m	2007 £m
Application fees and other regulatory income	12.2	15.7
Transaction Reporting	3.0	3.3
Publications and training services	2.8	3.4
Benchmarking income	0.2	0.1
Other sundry income	2.3	3.5
	20.5	26.0

Application fees are recognised when received, as is the revenue associated with the sale of publications and training services and other sundry income. Fees paid by firms that use our transaction reporting gateways to report their transactions are recognised in a way that matches the income received to the cost of operating our SABRE system. Benchmarking income invoiced relates to a three-year period, and is recognised on a straight-line basis over that time.

8. Tax

The tax charge on ordinary activities is:

	2008 £m	2007 £m
Current tax on continuing operations	1.7	1.5
Corporation tax charge for the year	1.7	1.5

Corporation tax is calculated at 30% (2007: 30%) of the estimated assessable surplus for the year. The total charge for the year can be reconciled to the accounting surplus as follows:

	2008	2007
	£m	£m
Surplus/(Deficit) before tax on continuing operations	(1.4)	18.4
Tax at 30% thereon	(0.4)	5.5
Effects of:		
Surplus/(Deficit) on activities not subject to corporation tax	2.1	(4.0)
Current tax charge for the period	1.7	1.5
Effective tax rate for the period	(121%)	8%

Under an agreement with the Inland Revenue the company is not subject to corporation tax on income arising from its regulatory activities. Consequently, the tax charge arises solely on interest receivable.

9. Intangible assets

	Software Development costs
	£m
Cost	
At 1 April 2006	21.3
Additions – internally generated	10.3
At 1 April 2007	31.6
Additions – internally generated	23.8
Impairment	(2.4)
At 31 March 2008	53.0
Amortisation	
At 1 April 2006	11.2
Charge for the year	5.3
At 1 April 2007	16.5
Charge for year	5.2
At 31 March 2008	21.7
Net book value	
At 31 March 2008	31.3
At 31 March 2007	15.1

At 31 March 2008 expenditure totalling £14.2m had been capitalised on software developments that had not yet gone into operation (2007: £10.0m).

10. Property, plant and equipment

	Leasehold improvements £m	Computer equipment £m	Furniture and equipment £m	Total £m
Cost				
At 1 April 2006	19.9	41.6	11.5	73.0
Additions	0.9	6.8	0.2	7.9
Disposals	–	(0.3)	(0.2)	(0.5)
At 1 April 2007	20.8	48.1	11.5	80.4
Additions	5.9	18.9	7.4	32.2
Disposals	(1.9)	(0.4)	(3.6)	(5.9)
At 31 March 2008	24.8	66.6	15.3	106.7
Accumulated depreciation and impairment				
At 1 April 2006	13.9	31.2	8.4	53.5
Charge for year	2.3	5.9	0.9	9.1
Disposals	–	(0.2)	(0.2)	(0.4)
At 1 April 2007	16.2	36.9	9.1	62.2
Charge for year	2.7	5.0	1.1	8.8
Disposals	(1.7)	(0.4)	(3.2)	(5.3)
At 31 March 2008	17.2	41.5	7.0	65.7
Carrying amount				
At 31 March 2008	7.6	25.1	8.3	41.0
At 31 March 2007	4.6	11.2	2.4	18.2

The FSA has reviewed the residual values used for the purposes of depreciation calculations. The review did not identify any requirement for adjustment to the residual values used in the current or prior periods. Residual values will be reviewed and updated annually.

11. Other financial assets

Trade and other receivables

	2008 £m	2007 £m
Fee receivables	0.8	2.4
Other debtors	0.8	0.9
Prepayments and accrued income	12.1	7.3
Amounts due within one year	13.7	10.6

The average credit period taken is 40 days (2007: 50 days). A late penalty fee of £250 is payable on periodic fees not paid by the due date. If payment is not received within 15 days of the due date, interest is charged on the outstanding balance at Bank of England Repo rate plus 5%.

All of the FSA's fee and other receivables have been reviewed for indications of impairment. Certain fee receivables were found to be impaired and an allowance of £0.6m (2007: £0.5m) has been made for the estimated irrecoverable amounts from fees invoiced. This allowance has been determined by reference to past default experience.

The directors consider that the carrying amount of trade and other receivables approximates their fair value.

In addition, some of the unimpaired fee receivables are past due as at 31 March 2008. The age of fee receivables past due, but not impaired is as follows:

	2008	2007
	£m	£m
Not more than three months	1.1	0.5
More than three months, but not more than six months	0.2	–
More than six months, but not more than one year	0.2	0.2
	1.5	0.7

Our policy is to begin to review receivables systematically for recoverability when they are more than three months past due. The amounts above were recently invoiced, in the course of collection, and we have had no specific evidence that any of these receivables are impaired.

There are a small number of receivables more than three months old, but less than six, where we are in discussion with high-quality counterparties as to the exact amount due, but do not believe that the balances are impaired.

The balances which are between six months and a year old are relatively low value amounts owed by a large number of debtors. We prioritise the use of resource applied to the collection of these amounts such that they are usually followed up in early summer. Experience indicates that we would normally expect to collect the proportion of those classes of debtor that are listed above.

Cash and cash equivalents

Bank balances and cash comprise cash held by the FSA and short-term, fixed-rate, bank deposits with an original maturity of three months or less. The carrying amount of these assets approximates their fair value.

The effective interest rate on short-term deposits is 5.7% (2007: 5.4%) and the average maturity of 30 days (2007: 45 days).

Credit risk

The FSA's principal financial assets are bank balances and cash and fee and other receivables. The credit risk on liquid funds is limited because the counterparties are banks with high credit ratings assigned by international credit rating agencies.

The FSA's credit risk is primarily attributable to its fee receivables. The amounts presented in the balance sheet are net of allowances for doubtful receivables. An allowance for impairment is made where there is an identified loss event which, based on past experience and management's forecasts, is evidence of a reduction in the recoverability of the cash flows. See above for further information on impairment of financial assets that are past due.

The FSA has no significant concentration of credit risk as its exposure is spread over a number of counterparties.

Interest rate risk

Other than cash held in bank accounts, all of the FSA's cash and cash equivalents and trading investments are fixed rate deposits, and so are not sensitive to variations in interest rates.

Liquidity risk

The FSA manages its liquidity by carefully monitoring the projected income and expenditure related to its day-to-day business. Liquidity needs are monitored in various time bands, on a day-to-day, week-to-week and rolling 30-day basis. Each month, we identify long-term liquidity in a 180 and 360 day window, up to the point when we next expect to bill the majority of our fees.

12. Trading investments

	2008	2007
	£m	£m
Available for sale investments – fair value	–	1.9

Last year, investments related to fixed rate cash deposits with an original maturity date in excess of 90 days.

13. Trade and other payables

Current

	2008	2007
	£m	£m
Trade creditors and accruals	73.4	47.9
Other taxation and social security	4.9	2.8
Financial penalties to be applied against fees receivable	4.5	15.6
Fees in advance	20.3	12.8
	103.1	79.1

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. The average credit period taken for trade payables is 28 days (2007: 29 days). The directors consider the carrying amount of trade payables approximates their fair value.

Non-current

A lease accrual of £13.4m (2007: £13.1m), being the cumulative difference between cash paid and expense recognised on operating leases for land and buildings, is recognised as a long term liability.

As at 31 March 2008, the FSA's liabilities have contractual maturities which are summarised below:

	Current				Non-current			
	Within 6 months		6 to 12 months		1 to 5 years		later than 5 years	
	2008	2007	2008	2007	2008	2007	2008	2007
	£m	£m	£m	£m	£m	£m	£m	£m
Trade creditors and accruals	69.8	43.7	5.4	4.3	2.2	1.0	11.1	12.1
Other taxation and social security	3.1	2.8	-	-	-	-	-	-
Financial penalties to be applied against fees receivable	4.5	15.6	-	-	-	-	-	-
Fees in advance	17.5	11.7	2.8	1.0	-	-	-	-
	94.9	73.8	8.2	5.3	2.2	1.0	11.1	12.1

At 31 March 2008 the FSA had available £100m (2007: £100m) of undrawn committed borrowing facilities in respect of which all conditions precedent had been met. The facility was taken out on 26 January 2007 and any future drawings are repayable in full on 26 January 2010. The loan is unsecured and carries interest rate at 0.08% above LIBOR.

14. Provisions

	Total £m
At 1 April 2007	2.1
Utilised in the year	(2.1)
Charge in the year	0.3
At 31 March 2008	0.3

Repairs

Under the terms of Deed of Variation on the lease for 25 The North Colonnade, the FSA has obligations to repair and replace certain items of equipment in the premises, in order to maintain the infrastructure of that building during the period that we occupy it. The estimated cost of the FSA's remaining obligation is charged to the income statement over the life of the lease and the cumulative cost less amounts spent is included in provisions for liabilities and charges. In order to help support our plans to introduce more flexible working space, the timing of that programme was moved forward in 2007/08. Consequently, all of the provision built up at 31 March 2007 has been applied against costs incurred in the year and the remainder charged to the income statement.

The charge for the year relates to repairing provisions in respect of the premises we rent at 25 Bank Street, Canary Wharf, London, which will become due when we leave those premises during 2008/09 when our leases expire.

15. Retirement benefit obligation

The FSA operates a tax-approved pension scheme, the FSA Pension Plan, which is open to permanent employees. The pension scheme was established on 1 April 1998 and operates on both a defined benefit (the Final Salary section) and defined contribution (the Money Purchase section) basis. Since 1 June 1998, all employees joining the FSA, other than those joining from other regulatory bodies whose functions were transferred to the FSA, have been eligible only for the Money Purchase section of the scheme. Since the Final Salary section of the scheme is closed to new members and the age profile of the active members is increasing, under the projected unit credit method, the current service cost will increase as members of the scheme approach retirement. The Final Salary section of the scheme is non-contributory for members. The Money Purchase section is part of a flexible benefits programme and members can, within limits, select the amount of their overall benefits allowance that is directed to the pension scheme.

Final Salary section

The most recent actuarial valuation of the FSA Pension Plan was carried out as at 31 March 2007 by an independent actuary, using the projected unit method, and was signed in March 2008. The results of this valuation have been updated for the purpose of IAS 19 as at March 2008, in order to allow for any changes in assumptions and movements in liabilities over the period.

The major assumptions used for the purpose of actuarial assumptions were as follows:

	At	At
	31 March 2008	31 March 2007
Expected rate of salary increases	4.0%	4.0%
Corporate bond discount rate	6.0%	5.2%
Expected return on scheme assets	7.1%	7.3%
Retail price inflation (r.p.i.)	3.4%	3.0%
Future pension increases	3.4%	2.9%

In assessing the value of funded obligations, the mortality assumptions for the Pension Plan are based on current mortality tables and allows for future improvements in life expectancy. The 2008 mortality assumptions are based on an actuarial table 'PA1992, projected to allow for future improvements using long cohort projections and by an individual's year of birth'. The 2007 mortality assumptions were based on the same table, projected to allow for future improvements using medium cohort projections and by an individual's year of birth.

The table below illustrates the assumed life expectancies at retirement of staff when they retire (staff are assumed to retire at the age of 60).

	2008 years	2007 years
Retiring today		
Males	28.5	26.7
Females	31.6	29.7
Retiring in 15 years		
Males	29.5	27.7
Females	32.5	30.5

The results of the valuation are sensitive to changes in the assumptions referred to above. The table below provides an estimate of the sensitivity of the estimates of the present value of pension obligation, and the cost of servicing those obligations, to small movements in those assumptions.

Assumption	Sensitivity	Increase/(decrease) in pension obligation at 31 March 2008		Increase/(decrease) in pension cost in 2008/09	
		£m	%	£'000	%
Base line	Assumptions as above – no change	363.0	N/A	8,786	N/A
Discount rate	0.1%	8.8	2.4%	216	2.5%
Longevity	1 additional year of life at age 60	7.1	2.0%	154	1.8%
Inflation	0.1%	6.9	1.9%	123	1.4%
Salary increases	0.1%	1.9	0.5%	92	1.1%

The amount recognised in the balance sheet is as follows:

	2008 £m	2007 £m
Fair value of plan assets	273.3	289.1
Less: Present value of funded obligations	(363.0)	(367.1)
Deficit in the scheme	(89.7)	(78.0)
Unfunded pension liabilities	(1.9)	(1.9)
Net liability recognised in the balance sheet	(91.6)	(79.9)

A small number of current and former employees have benefit promises that cannot be delivered entirely through the tax-approved scheme described above. At 31 March 2008 the liability is £1.9m (2007: £1.9m) to cover the cost of these promises. In 2007 an amount of £0.1m was included in the total pension cost for the year in note 6, representing the value of the additional benefits accrued. This year the increase in the value of benefits accrued were offset by the amount of benefits paid to one employee.

Amounts recognised in the income statement in respect of the defined benefit plan are as follows:

	2008	2007
	£m	£m
Current service cost	9.2	9.4
Past service cost	1.1	0.3
Administration expenses	10.3	9.7
Expected return on plan assets	21.2	18.0
Interest on scheme liabilities	(19.4)	(17.0)
Other net finance income	1.8	1.0

Current service costs and past service costs are disclosed as administration expenses, expected return on plan assets and interest cost are disclosed as interest income in the income statement and actuarial losses of £13.9m (2007: £14.2m) are recognised in the period in which they occur as part of the statement of recognised income and expense.

The actual (loss)/return on plan assets was (£19.7m) (2007: £9.3m).

Changes in the present value of the defined benefit obligation are as follows:

	2008	2007
	£m	£m
Opening obligation	(367.1)	(340.1)
Current service cost	(9.2)	(9.4)
Past service cost	(1.1)	(0.3)
Benefits paid	6.8	5.2
Interest cost	(19.4)	(17.0)
Actuarial gains / (losses)	27.0	(5.5)
Closing obligation	(363.0)	(367.1)

Changes in the fair value of plan assets are as follows:

	2008	2007
	£m	£m
Opening fair value of plan assets	289.1	250.6
Expected return on plan assets	21.3	18.0
Actuarial losses	(40.9)	(8.7)
Contributions by the employer	10.6	34.4
Benefits paid	(6.8)	(5.2)
Closing fair value of plan assets	273.3	289.1

The fair value of plan assets and the expected rates of return were:

	Expected rate of return at 31 March 2008	Fair value at 31 March 2008 £m	Expected rate of return at 31 March 2007	Fair value at 31 March 2007 £m
Equities	7.4%	167.0	7.9%	180.8
Corporate Bonds	6.9%	69.1	5.4%	68.4
Property	7.4%	24.8	7.9%	26.4
Currency Management	7.4%	9.4	7.9%	11.1
Cash	5.25%	3.0	5.25%	2.4
Closing fair value of plan assets	7.2%	273.3	7.3%	289.1

Cumulative actuarial gains and losses recognised in equity:

	2008 £m	2007 £m
1 April	(38.1)	(23.9)
Net actuarial losses recognised in the year	(13.9)	(14.2)
At 31 March	(52.0)	(38.1)

There are no deferred tax implications of the above deficit as corporation tax is only payable on interest receivable by the company.

The plan assets do not include any of the FSA's own financial instruments, nor any property occupied by, or other assets used by the FSA.

The expected rates of return on individual categories of plan assets are determined by reference to relevant market expectations at the beginning of the period for returns over the lifetime of the obligations.

The history of differences between expected and actual returns on plan assets and gains and losses on scheme liabilities are as follows:

	2008	2007	2006	2005
Defined benefit obligation (£m)	(363.0)	(367.1)	(340.1)	(261.1)
Fair value of plan assets (£m)	273.3	289.1	250.6	182.2
Net deficit (£m)	(89.7)	(78.0)	(89.5)	(78.9)

Experience adjustments on scheme assets:

Amount (£m)	(40.9)	(8.7)	38.8	2.4
percentage of scheme assets	15.0%	3.0%	15.5%	1.3%

Experience gains and losses on scheme liabilities:

Amount (£m)	(0.3)	(0.7)	0.1	(0.3)
percentage of the present value of scheme liabilities	0%	0%	0%	0%

The contribution rate for 2007/08 was 23% of pensionable earnings plus £3.4m (11.3% of pensionable earnings) as an additional deficit reduction contribution. The Scheme Specific Valuation (SSV) as at 31 March 2007, which more closely reflects our Directors' view of the true economic cost of funding our Final Salary pensions obligations, showed a deficit of £29m. The agreed contribution rate for 2008/09 is 29.5% of pensionable earnings. In addition, we have committed to clear the SSV deficit over nine years by making additional pension deficit reduction contributions of £3.8m a year (approximately 12.3% of pensionable earnings), beginning in 2008/09.

Defined contribution scheme

The total expense recognised in the income statement of £9.0m (2007: £8.7m) represents contributions payable to the plan by the FSA at rates specified in the rules of the Plan.

16. Accumulated deficit

	£m
At 1 April 2006	(84.1)
Surplus for the year	16.9
Actuarial gains and losses for the year in respect of the defined benefit pension scheme	(14.2)
At 1 April 2007	(81.4)
Deficit for the year	(3.1)
Actuarial gains and losses for the year in respect of the defined benefit pension scheme	(13.9)
At 31 March 2008	(98.4)

The FSA is a company limited by guarantee. The members of the company have agreed to contribute £1 each to the assets of the company in the event of it being wound up.

17. Capital commitments

The FSA had entered into contracts at 31 March 2008 for capital expenditure totalling £10.9m (2007: £1.8m), which are not provided for in the accounts.

18. Operating lease arrangements

	2008	2007
	£m	£m
Minimum lease payments under operating leases recognised as an expense in the year	12.4	11.8

At the balance sheet date, the FSA has outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2008	2007
	£m	£m
Within one year	11.6	12.2
In the second to fifth years inclusive	48.1	46.9
After five years	71.0	83.7
	130.7	142.8

Operating lease payments represent rentals payable by the FSA for certain of its office properties.

The lease on 25 The North Colonnade, Canary Wharf, London, will expire in 2018. Under the terms of the lease, the rent for the period from 4 November 2003 to 3 November 2004 was agreed at £9.5m. Thereafter, the rent payable until 3 November 2008 will increase by 2.5% each year. From 4 November 2008 until 3 November 2018 rent will increase in line with r.p.i. subject to a minimum annual increase of 2.5% p.a. and a maximum of 5% p.a. As mentioned in note 15, our current assumption for r.p.i. is 3.4% p.a.

The lease on 18th Floor, Canary Wharf Tower, London, was taken out in January 2008 and contains no provision for rent reviews. The lease will expire in 2018.

The lease on 15th Floor, 25 Bank Street, Canary Wharf, London, was taken out in January 2007 and contains no provisions for rent reviews. The lease will expire in 2008.

The lease on 16th Floor, 25 Bank Street, Canary Wharf, London, was taken out in March 2005 and contains no provisions for rent reviews. The lease will expire in 2008.

The lease on Quayside, Edinburgh was taken out in September 2005, contains provision for a rent review in September 2010 and September 2015 and is due to expire in August 2020.

19. Related party transactions

Remuneration of key management personnel

The remuneration of directors, who are the key management personnel of the Authority, is set out below in aggregate for each of the categories specified in IAS 24 Related Parties Disclosures. Further information on individual directors is provided in the audited part of the Corporate Governance Statement on pages 59 to 66.

	2008	2007
	£m	£m
Short-term benefits	3.2	2.6
Post-employment benefits	0.1	0.3
	3.3	2.9

There were no other transactions with directors in either year.

Significant transactions with other financial services regulatory organisations

The FSA enters into transactions with a number of other financial services regulatory organisations. The significant transactions were:

a) The Financial Services Compensation Scheme Limited (FSCS)

The FSA appoints, and has the right to remove, directors to the board of FSCS and it establishes the rules under which the Scheme operates. Under statute (FSMA) and the Memorandum of Association of FSCS, the FSA has to ensure that the terms of appointment of the directors procure their operational independence from the FSA. Accordingly, the FSA does not control FSCS, but does consider it to be a related party.

During the year, the FSA provided an agency service to FSCS to collect tariff data, issue levy invoices and collect levy monies on its behalf. The net amount of fees collected that remained to be paid over by the FSA to FSCS at 31 March 2008 was £0.1m (2007: £0.3m). The charge for the service was £0.2m (2007: £0.2m).

During the year, the FSA also provided services to FSCS relating to the implementation of the FSCS's revised funding arrangements. The net charge for those services, after taking into account the cost of two members of staff seconded by the FSCS to the FSA to assist in that process, was £0.1m (2007: £nil).

The FSA is a party to the lease agreement for FSCS's premises, occupied from 18 June 2001 at the 7th floor at Lloyds Chambers, Portsoken Street, London, as guarantor of performance of the lease. This lease is for a term from 13 February 2001 to 21 June 2018 at a current annual rental and related out-goings of £1.1m. This guarantee was provided when the FSCS was in its start-up phase, ahead of its formal fee-raising powers being granted under FSMA. The FSCS did not provide any consideration in return for that guarantee. As there is not an active market for such guarantees of this nature, no valuation technique could be used to calculate a fair value. Consequently, given the lack of consideration, and the strength of the financial covenant of both the FSCS funding arrangements, no fair value was assigned on inception.

b) The Financial Ombudsman Service Limited (FOS)

The FSA established the FOS, a company limited by guarantee, in accordance with FSMA to exercise the functions of the operator of the ombudsman scheme. Under the FSMA and the Memorandum of Association of the FOS, the FSA has to ensure that the terms of appointment of the directors procure their operational independence from the FSA. Accordingly, the FSA does not control the FOS, but does consider it to be a related party.

The FSA is the principal employer in the FSA Pension Scheme described in note 15. The FOS is also a participating employer in the same scheme making contributions at the same overall rate as the FSA. The assets and liabilities disclosed in note 15 represent only those that relate to the employees of the FSA. The total number of scheme members is 2,160 (2007: 2,209) of which 2,021 are, or were, employees of the FSA (2007: 2,069) and 139 of the FOS (2007: 139).

In 2005/06 the FSA entered into an agency agreement with the FOS to collect tariff data, issue levy invoices and collect levy monies on its behalf in respect of its fees for 2006/07 onwards. The charge for that service is £0.1m. At 31 March 2008 £0.1m of fees relating to 2007/08 invoices had been collected but not paid to FOS together with a further £2.7m in respect of on-account fees for 2008/09 (2007: £1.1m).

The FSA is a party to the lease agreement for part of the FOS premises at South Plaza II, London, as guarantor of performance of the lease, which is for a 15-year term from 2 November 1999, at a current annual rental of £1.1m. FOS has a revolving loan facility of £15m (2007: £15m) available for draw down from 24 January 2003 and repayable by 2011. Amounts outstanding under the facility were guaranteed by the FSA until February 2008, when the guarantee was revoked by the FSA's Board, with the agreement of the bank. As at 31 March 2007, £7.5m of the facility was drawn down. Both those guarantees were provided when the FOS was in its start-up phases, ahead of its formal fee-raising powers being granted under the FSMA. The FOS did not provide any consideration in return for those guarantees. Given the lack of consideration, and the strength of the financial covenant of the FOS funding arrangements, no fair value was assigned on inception. The current market value of these guarantees has been calculated and determined to be immaterial.

The Office of the Complaints Commissioner

The FSA funds the activities of the Complaints Commissioner through the periodic fees it raises. Up to 31 August 2004, the costs of those activities were met directly by the FSA. In August 2004, however, the Office of the Complaints Commissioner (OCC), a company limited by guarantee, was incorporated. Since 1 September 2004, the purpose of this company has been to administer complaints against the FSA that are handled by the Complaints Commissioner. In doing so, it employs staff, owns assets used by the Commissioner and his staff, and enters into contracts for goods and services in furtherance of complaints handling activities. During 2007/08, the FSA has transferred £0.5m (2007: £0.4m) to the OCC to cover the latter's running costs, which have been expensed in the FSA's income statement. At 31 March 2008, the balance owing to the FSA from the OCC was £0.1m (2007: £0.1m).

By virtue of certain provisions contained in the Memorandum of Association of the OCC the FSA has the right to appoint and remove the Complaints Commissioner, who is both a member, and a director of the company. Because of this, the OCC is actually a subsidiary of the FSA. However, the scale of the activities of the OCC is immaterial compared to that of its parent company. Accordingly, the FSA has not prepared group accounts, including the OCC, on the grounds that the exclusion of the OCC from the FSA's accounts is not material to those accounts providing a true and fair view.

Other than disclosed above, there were no related party transactions during the year (2007: £ nil).

20. Contingent Liabilities

As described in note 19 the FSA acts as guarantor for leases entered into by the FSCS and the FOS. Given the strength of those organisations' fee-raising arrangements, no liabilities are expected to crystallise in respect of those guarantees.

In discharging its responsibilities under the FSMA and its predecessor legislation, the FSA faces the possibility of certain parties making claims as a result of that work. No material claims of this nature have yet been made against the FSA. On the basis of the information presently available to it, the FSA believes that any claims would have no real prospect of success. Accordingly, no provision has been made in the accounts for these matters.

21. Notes to the cash flow statement

	Notes	2008 £m	2007 £m
(Deficit)/Surplus for the year from continuing operations		(3.1)	16.9
Adjustments for:			
Interest received on bank deposits		(5.7)	(5.1)
Corporation tax expense	8	1.7	1.5
Amortisation of other intangible assets	9	5.2	5.3
Impairment loss on intangible fixed assets	9	2.4	–
Depreciation of property, plant and equipment	10	9.4	9.1
Decrease in provisions	14	(1.8)	(0.4)
Difference between pension costs and normal contributions	15	1.3	0.5
Additional cash contributions to reduce pension scheme deficit	15	(3.4)	(26.0)
<hr/>			
Operating cash flows before movements in working capital		6.0	1.8
Increase in receivables		(3.1)	(0.7)
Increase in payables		24.1	7.4
Net cash generated from operations		27.0	8.5

Cash and cash equivalents comprise cash at bank and other short-term highly liquid investments with a maturity of three months or less.

Statement of allocation of costs for the year ended 31 March 2008

Introduction

The FSA sets fees by reference to blocks of fee-payers conducting similar activities, which as far as possible, reflect the FSA's costs applicable to the respective fee-blocks. The statement of allocation of costs on page 101 shows the allocation of costs for the year ended 31 March 2008, analysed by those fee-blocks.

Costs are allocated according to the method set out in note 1 on page 99. The report of the auditors is set out on page 102.

Notes to the statement of allocation of costs for the year ended 31 March 2008

1 Method of allocation

The Financial Services and Markets Act 2000 provides that the FSA may make rules providing for the payment of fees to meet its expenses in carrying out its function, or for any incidental purposes and to maintain adequate reserves.

Under the current fee-raising arrangements, the FSA's fees are set by reference to costs applicable to categories of firms or bodies, or individual bodies (fee-payers). These categories are known as fee-blocks. The allocation of costs to fee-blocks is primarily made by reference to costs applicable to each fee-payer. Where costs cannot be directly attributed to individual fee-payers they have been allocated to fee-blocks on a basis considered appropriate by the Directors, such as on the headcount of departments, or the estimated time or resources spent on the supply of services for each fee-payer within departments.

2 Allocation of net liabilities, excluding pensions liabilities

We apply IAS 19 in accounting for the costs of our defined benefit pension scheme. Given the long-term nature of our final salary pension liabilities, and the fact that we cannot predict with certainty how our resources will be allocated over this time scale, we do not allocate those pensions liabilities to fee-blocks.

3 Reconciliation from the income statement to net costs for the year as shown on the cost allocation statement

	Year ended 31 March 2008
	£m
Net costs for the year	306.4
Add: difference between accounting charges for provisions in the statutory accounts and the related cash costs of pension contributions paid	2.2
Less: costs of implementing more principles-based regulation	(13.7)
Less: change in scope and deferred IS costs	(3.6)
Net costs for the year on statement of allocation of costs	291.3

While adopting IAS 19 provides greater transparency of the impact of pension costs on our financial position, it introduces significant volatility into both the figures reported in our income statement and in our balance sheet. In order to prevent IAS 19 transmitting this volatility into our fee calculations, we exclude any non-cash elements of pension costs from our Annual Funding Requirement (AFR). The main non-cash item excluded is the net finance income of £1.8m. Our AFR is calculated to include only the cash value of the pension contributions we need to make in a year to cover the increase in the scheme's final salary liabilities due to additional years' service and to salary increases. Also, the AFR includes any deficit reduction contributions aimed at reducing the size of the scheme's deficit to ensure that it can meet its obligations. This is consistent with the fact that, as mentioned above, we have not allocated the pensions liabilities to fee-blocks.

Full details of the calculation of the AFR for 2008/09 are included in the Consolidated Policy Statement on our fee-raising arrangements and regulatory fees and levies 2008/09, including feedback on CP08/2 and 'made rules', published in May 2008.

Statement of allocation of costs for the year ended 31 March 2008

Fee-block	Net assets, excluding pensions obligation, at 1 April 2007	Net costs for the year	Fees for the year	Net assets/(liabilities), excluding pensions obligation at 31 March 2008
	£m	£m	£m	£m
A.1 Deposit acceptors	5.0	(55.4)	55.3	4.9
A.2 Mortgage lenders and administrators	(0.8)	(5.8)	5.7	(0.9)
A.3 General insurers	(0.3)	(17.3)	16.4	(1.2)
A.4 Life insurers	(0.5)	(39.0)	44.2	4.7
A.5 Lloyd's Managing Agents	(0.5)	(1.2)	0.9	(0.8)
A.6 The society of Lloyd's	0.1	(1.3)	1.2	-
A.7 Fund managers	2.0	(28.2)	28.8	2.6
A.9 CIS operators, trustees and depositories	1.6	(5.6)	5.6	1.6
A.10 Firms dealing as principal	(2.5)	(15.6)	15.1	(3.0)
A.12 Advisory arrangers holding client money and/or assets	(1.2)	(19.8)	19.2	(1.8)
A.13 Advisory arrangers not holding client money and/or assets	(1.6)	(40.3)	39.4	(2.5)
A.14 Corporate finance advisers	0.4	(6.2)	6.4	0.6
A.18 Mortgage lenders, advisers, and arrangers	(2.7)	(10.3)	9.2	(3.8)
A.19 General insurance mediation	(0.3)	(29.2)	31.3	1.8
B RBs	0.2	(3.8)	4.0	0.4
C CIS	-	(1.6)	1.3	(0.3)
D DPBs	0.3	(0.2)	0.3	0.4
E UKLA	1.3	(8.3)	10.0	3.0
F Registrant only	(0.5)	(1.8)	1.5	(0.8)
G Firms registered under Money Laundering Regulations	-	(0.4)	-	(0.4)
Total	-	(291.3)	295.8	4.5
More principles-based regulation	13.7	(13.7)	5.0	5.0
Amortisation of £20m pension contribution	(15.2)	-	2.5	(12.7)
Change in Scope and deferred IS costs	-	(3.6)	-	(3.6)
Net deficit excluding pensions obligation	(1.5)	(308.6)	303.3	(6.8)

The fee-block descriptions above have been summarised for the purposes of this statement. A full description of the fee-block can be found in the relevant section of the FSA's Handbook.

Report by independent auditors to the directors of the Financial Services Authority on the statement of allocation of costs

We have examined the statement of allocation of costs to regulated fee-payers ('the Statement') for the year ended 31 March 2008 and the related notes 1 to 3, as prepared by the directors of the company. The Statement has been prepared on the basis set out in note 1.

This report is made solely to the directors of the company. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the directors of the company, as a body, for our review, for the statement, or for the opinions we have formed.

Respective responsibilities of directors and Grant Thornton UK LLP

The company's directors are responsible for the assumptions and basis on which the costs are allocated to fee-payers and the preparation of the Statement in accordance with note 1. We have performed certain procedures on the Statement, in accordance with our engagement letter dated 2 December 2005, to verify that the assumptions made by the directors have been applied to the allocated amounts.

Basis of opinion

The procedures we performed did not constitute a review or an audit of any kind and consisted primarily of verifying whether the figures in the Statement have been compiled from amounts extracted from the company's accounting records, and in accordance with the basis set out in note 1.

The procedures we performed were not designed to and are not likely to reveal fraud and there is no assurance that our procedures will reveal all matters of significance related to the Statement.

Opinion

In our opinion, the Statement has been compiled from amounts extracted from the accounting records and has been prepared in accordance with the basis set out in note 1.

Grant Thornton UK LLP
Chartered Accountants
London

22 May 2008