The Financial Services Authority

Statutory Report and Accounts for the year ended 31 March 2007

Registered number 01920623

Report of the Directors for the year ended 31 March 2007

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

Table [xx]

Financial Risk Outlook	http //www fsa gov uk/Pages/Library/corporate/Outlook/fro_2007 shtml
Business Plan	http //www fsa gov uk/Pages/Library/Corporate/Plan/index shtml
Corporate Responsibility	http //www fsa gov uk/Pages/About/What/CSR/index shtml
Health & Safety	http //www fsa gov uk/Pages/Library/Other_publications/Staff/staff_handbook/health/index shtml
Equal Opportunity	http //www fsa gov uk/Pages/Library/Other_publications/Staff/staff_handbook/working/equal/index_shtml

The Directors of the FSA during the period reported on are shown in table [xx] along with other information relating to their date of appointment, expiry of term and attendance record at the Board and the Audit, Risk, Remuneration and Non-executive Directors' Committees as appropriate The Remuneration Report is located at page [xx]

Table [xx]

Name	**Board meetings**	**NedCo**	**RemCo**	**AuditCo**	**RiskCo**	**Original appointment date**	**Expiry of current term**
Clive Briault [g]	11/11					1 April 2004	31 March 2010
James Crosby [c,g]	10/11	4/4	2/2	3/4		15 January 2004	14 January 2010
Tom de Swaan [d]	6/8	1/2	1/1		3/3	19 January 2001	18 January 2007
Peter Fisher	3/3	2/2			1/1	19 January 2007	18 January 2010
Brian Flanagan	2/3	1/2	0/1	1/1		19 January 2007	18 January 2010
Karin Forseke	11/11	4/4		4/4		1 December 2004	30 November 2007
Sir John Gieve	11/11	4/4			2/4	16 January 2006	15 January 2009
Kyra Hazou	8/8	2/2		3/3	3/3	19 January 2001	18 January 2007
Dame Deirdre Hutton [a,b,h]	11/11	4/4	2/2		4/4	11 December 1997	10 December 2007
David Kenmir [g]	11/11					1 April 2004	31 March 2010
Sir Callum McCarthy	11/11					22 September 2003	21 September 2008
Professor David Miles [g]	10/11	4/4			4/4	1 April 2004	31 March 2010
Hector Sants [g]	10/11					4 May 2004	3 May 2010
Michael Slack	10/11	4/4	2/2	3/4		1 December 2004	30 November 2007
Hugh Stevenson [e,f,g]	11/11	4/4			3/3	1 June 2004	31 May 2010
John Tiner [g,i]	11/11					22 September 2003	21 September 2009
Clive Wilkinson	8/8	2/2		3/3		19 January 2001	18 January 2007

Key

a Chairman of NedCo	b Chairman of RemCo	c Chairman of AuditCo
d Chairman of RiskCo during the year from 1 April 2006 to 2 January 2007	e Chairman of RiskCo from 3 January 2007	f Chairman of FSA Pension Plan Trustee Ltd
g Director serving second concurrent term	h Director serving fourth concurrent term	i John Tiner has resigned from his position ear with effect from 19 July 2007

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

Sir John Gieve is the Deputy Governor, Financial Stability at the Bank of England and is an ex-officio member of the Board of the FSA In a reciprocal arrangement with the Bank of England, Sir Callum McCarthy serves as a member of the Court of the Bank of England

All the FSA's directors are appointed by HM 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 on page [xx], and they have three-year renewable terms as Directors

Business Review

Principal activities

The FSA is the principal statutory regulator of financial services in the UK Its activities are set out in FMSA which requires the FSA to regulate most financial services markets, exchanges and firms in wholesale and retail markets Through FSMA, the FSA has rule-making, investigatory and enforcement powers so that it can meet its statutory objectives Further information on the principal activities can be found 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 FSA's Risk Committee and Audit Committee keep under review risks which may interfere with the attainment of the statutory objectives The Risk and Audit Committee reports, which provide more detail on risks and uncertainties that face the company, can be found on pages [xx] The Financial Risk Outlook 2007 (which is available on the FSA's website) also provides information on what the FSA considers to be priority risks

Development and performance of the company's business

Analysis of the development and performance of the company's business is set out in the first three sections of this Annual Report The fourth section also reports on the position of the FSA at the end of the financial year, whilst the FSA's Business Plan for 2007/08 (available on the FSA's website) provides information relating to the FSA's budget and priorities.

Directors' accounting responsibilities

The Directors are responsible for preparing the financial statements in accordance with applicable law and international financial reporting standards, to show a true and fair view of the state of affairs of the company and of its income and expenditure for the period In preparing these financial statements, the Directors consider that the company has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that all applicable accounting standards have been followed

The Directors have responsibility for ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the accounts comply with the Companies Act 1985 They are also responsible for the system of internal controls, safeguarding the assets of the company and, hence, for taking reasonable steps for the prevention and detection of fraud and other irregularities

Financial position

The primary source of income for the FSA is the fees charged to those firms that the company regulates Information on the FSA's financial position is in the accounts, starting on page [xx] and in the Financial Review on page [xx] The Financial Review explains how the FSA manages its pension 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 company has adequate resources to continue its business for the foreseeable future and consequently the going concern basis continues to be appropriate in preparing financial statements

Corporate Responsibility

As part of its overall approach to Corporate Responsibility, the FSA has a number of policies which state its principles and proposed activities with regard to areas such as the environment, community affairs and equal opportunity of employment These policies, and in some cases, the company's performance against objectives in these areas may be accessed through the website

The FSA recognises the impact its operations can have on the environment and on the community in which it operates As part of this, the FSA is committed to measuring, reporting and, where practical, reducing its impact on the environment The FSA's performance against its targets set with regard to energy usage, material usage and waste produced and recycled can be found on the website The FSA has also committed to reducing its carbon footprint and intends to offset the carbon emissions caused by all its business travel The company will be in a position to report on this at the end of the 2007/08 financial year With regard to social and community issues, the FSA aims to be a good corporate citizen and develop projects which will both help the community and also be of benefit to staff Details of these projects, managed by the Community Affairs team, can also be found on the website

The FSA has recently undertaken a programme to unite Corporate Responsibility projects throughout the company It is intended that this will allow a more efficient utilisation of resources and provide opportunity to identify areas within the programme that could be improved upon A further aspect of this programme is to establish a clear accountability and reporting framework for all Corporate Responsibility activities In due course, performance against targets will also be reported on the website

The FSA aims to adopt Corporate Responsibility best practice where it is relevant and practical and is aligned with the FSA's overall business strategy

Charitable donations

The FSA made the donations shown below as part of its Community Affairs programme

Recipient	Amount	Reason
Crisis	£10,210	In lieu of producing a corporate Christmas Card
Police Community Clubs of Great Britain	£660	To purchase copies of a booklet against bullying and vandalism for use in Tower Hamlets
West Ham and Plaistow Old People's Club	£80	From the sale of old mobile phones
Children's Safety Society	£100	Towards the emergency services visiting schools
Isle of Dogs Community Foundation	£577	Sponsorship of the IDCF Newsletter

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 The FSA endeavours to provide a working environment where all are treated with dignity and respect and no one suffers discrimination or disadvantage because of gender, race, disability, sexual orientation, religion, belief or age The FSA's Equal Opportunity policy can be found on the website

In accordance with the Disability Discrimination Act 2005, the FSA aims to eliminate unlawful discrimination and harassment, and promote disability equality The FSA also works to fulfil its statutory duties under the amended Sex Discrimination Act 1975 (introduced on 6 April 2007) which includes eliminating unlawful discrimination and harassment and promoting equal opportunities between men and women

Health and Safety

The FSA is committed to providing a healthy and safe environment for all staff and visitors to FSA premises This commitment is promoted by the Health and Safety policy, which may be found on the website

Employee Involvement

The FSA uses a variety of methods of communication, including an intranet, email briefings and staff meetings, to keep employees up to date with developments within the company and the industries which it regulates. Employees are invited to give feedback on the FSA and its operations through formal and informal surveys performed throughout the year

Opportunities are also provided for in-house and external training, and during the year each employee spent an average of 6 1 days training

The Staff Consultative Committee provides channels of communication and consultation between the FSA and employees The Committee gives employees the opportunity to contribute to and influence the development of the FSA, and to have their views heard at the highest levels in the organisation over matters affecting the staff in general The FSA recognises the importance and value of ensuring this process is effective The Committee is also the forum through which the FSA complies with the EU Information and Consultation Directive 2004

Supplier payment policy

The FSA's policy is to aim to pay 90% of invoices within 30 days of receipt of invoice The average time taken to pay suppliers from receipt of invoice was 28 58 days

Auditor

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 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

A resolution to re-appoint RSM Robson Rhodes as Auditor will be put to members at the Annual General Meeting

By Order of the Board
K Iain Brown
Secretary
May 2007

Corporate Governance Statement for the year ended 31 March 2007

Table [xx] shows website references referred to in this statement, including the functions and terms of reference of the various Committees

As a company limited by guarantee, without shareholders, the FSA is not subject to the requirements of the Combined Code on Corporate Governance (the Code) However, the FSA is committed to meeting high standards of corporate governance, therefore, the company chooses to comply with the Code, as far as practicable, according to the nature of its business

Given the FSA's position, the Board does not report on areas of non-compliance by exception It does aim, through this report, to show the areas in which it does meet the requirements of the Code

Members of the Board, of which the majority are Non-executives, come from a variety of backgrounds with a wide range of skills and experience Non-executives are independent of the FSA, although, on occasion, conflicts of interest may arise where a position is held within a firm regulated by the FSA In these cases there are stringent procedures in place to ensure that any such conflicts will not interfere with the FSA's activities or fulfilment of its statutory objectives As it is the FSA's opinion that all Non-executive Directors are independent of management, the Board has concluded that it is neither necessary nor appropriate to appoint a senior independent director In addition, FSMA established the Non-executive Directors' Committee (NedCo), its only members being the Non-executive Directors, to keep under review the Authority's discharge certain of its functions More information on the role of NedCo is on page [xx]

The Board met 11 times last year Further details of individual Directors' attendance can be found on page [xx] Meeting agendas are set by a rolling schedule and supplemented with items which arise according to current business needs The Company Secretary ensures sufficient preparatory information is provided in good time for Directors to review before the meeting and he, or his Deputy, records decisions made and discussions leading to them, at the meetings

The roles of the Chief Executive and the Chairman are clearly split The Chairman heads the Board, whose role is to lead and control the affairs of the FSA There is a schedule of matters reserved to the Board which includes but is not limited to

- making strategic decisions,
- ensuring the organisation has sound financial controls in place,
- developing and maintaining good relationships with other organisations, including the Government,
- overseeing the day-to-day business of the executive officers,
- succession planning, and
- providing a means of accountability

New Directors undergo a comprehensive induction procedure which includes opportunities to meet key employees throughout the business Directors have access to the Company Secretary who maintains an ongoing training programme and provides regular opportunities for them to update their skills and knowledge The Company Secretary will also arrange for Directors to take independent professional advice, if necessary

The FSA operates independently of Government but is accountable to Parliament, through Treasury Ministers In accordance with FSMA, the FSA is also required to maintain effective arrangements for consulting practitioners and consumers, which it has done through the establishment of the Consumer, Practitioner and Smaller Businesses Practitioner Panels All Panels are independent and are free to publish their views on the FSA's work

Table [XX]

Accountability mechanisms	http //www fsa gov uk/Pages/About/Who/Accountability/index shtml
Role of the Chairman	http //www fsa gov uk/pages/About/Who/Management/Chairman shtml
Role of the Chief Executive	http //www fsa gov uk/pages/About/Who/Management/CEO shtml
Schedule of matters reserved to the Board	http //www fsa gov uk/pubs/other/SoM pdf
Board delegations, including terms of reference of Committees	http //www fsa gov uk/pubs/other/Gov_memo pdf
Directors' Biographies	http //www fsa gov uk/Pages/About/Who/board/index shtml
NedCo membership	http //www fsa gov uk/Pages/About/Who/board/committees/index shtml
NedCo functions	http //www fsa gov uk/pubs/other/Gov_memo pdf
RemCo	http //www fsa gov uk/Pages/About/Who/board/committees/index shtml
AuditCo	http //www fsa gov uk/Pages/About/Who/board/committees/index shtml
RiskCo	http //www fsa gov uk/Pages/About/Who/board/committees/index shtml
Regulatory Decisions Committee membership	http //www fsa gov uk/Pages/About/Who/board/committees/RDC/index shtml
Listing Authority Committees membership	http //www fsa gov uk/pages/about/who/board/committees/laa/index shtml

Evaluations

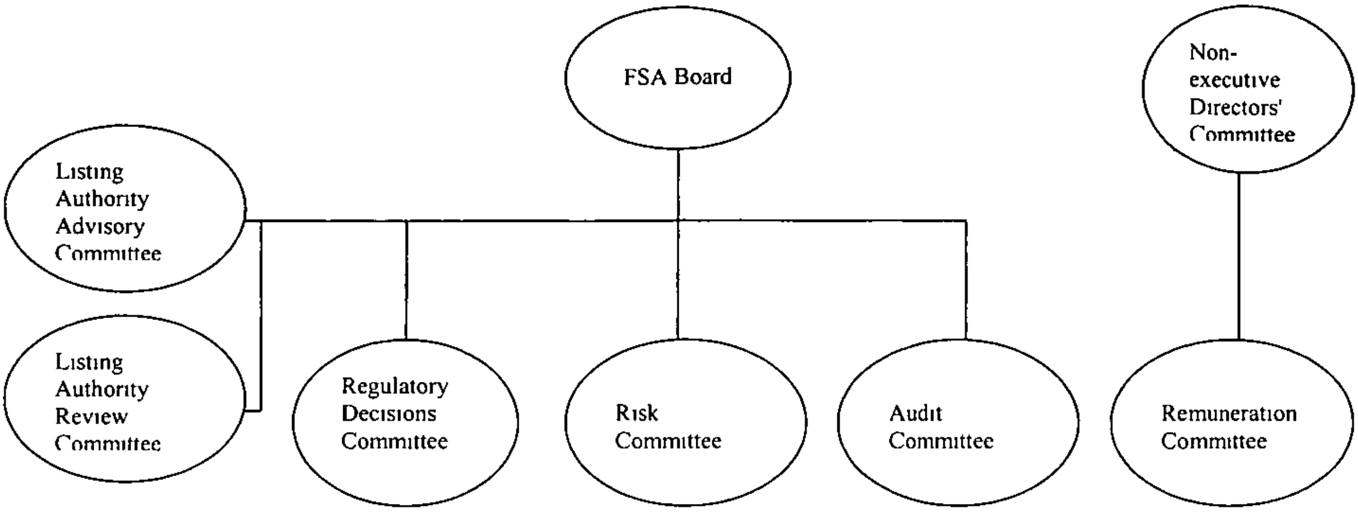
During the year, a number of evaluations relating to the Board and its members were carried out

NedCo reviewed the performance of the Chairman in consultation with HM Treasury and the Chairs of the Independent Panels Likewise, the Chairman assessed the effectiveness of the Non-executive Directors on the basis of one-to-one discussions

In compliance with the Code, the Board carried out an evaluation of its effectiveness This year the Board evaluation was done by a combination of bespoke questionnaires and follow-up discussions by the Board

The results of the effectiveness review were analysed and the findings were discussed by the Board. The Board agreed that overall its performance was effective although there remained some areas for further development

Governance Structure



The Committee of the Non-executive Directors (NedCo)

NedCo has been established and operates in line with the provisions of Schedule 1 to FSMA Further details on its composition and the statutory functions it discharges can be found on the FSA website NedCo met on four occasions during the year to ensure that its statutory functions were being satisfactorily discharged [bullet points describing work to be inserted]

Report of the Non-executive Directors

The unitary Board 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 the Audit Committee (AuditCo) The Remuneration Committee (RemCo) reports on its work to NedCo

Efficiency and Economy

During the year, NedCo kept under review whether the FSA is using its resources efficiently and economically 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, sought further explanations when appropriate and encouraged enhancements to the reporting framework on a continuous improvement basis

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 The full statement on internal financial controls is on page [xx]

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

RemCo

The composition, functions and terms of reference of RemCo can be found on the website During the year, Tom de Swaan retired from RemCo He was replaced by Brian Flanagan

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 on page [xx] and in the remuneration table on page [xx] The Executive Directors have continuous contracts of employment that provide for 12 months' prior notice of termination by either party, with a maximum of 12 months' total remuneration (as described below) payable in the event of early termination of the contract by the FSA In determining the remuneration of the Executive Directors, the Committee undertook an evaluation of their performance, assisted by an assessment of performance against objectives The objectives for each Director took account of the FSA's overall objectives by reference to the Business Plan and the individual Director's areas of responsibility The Committee also considered feedback on each individual Director from HM Treasury and the Chairs of the Practitioner and Smaller Businesses Practitioner Panels It has the benefit of advice from the Director, Human Resources, and market data from Watson Wyatt, its external consultants. The Company uses Watson Wyatt on an ad-hoc basis for salary benchmarking exercises 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, the Committee 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 for a performance related bonus up to a maximum of 25% of basic pensionable salary At his request, the Chairman was not considered for a bonus

- 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 [xx] 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 the table on page [xx]

Table [xx]

Director	Callum McCarthy	John Tiner	Clive Briault	David Kenmir	Hector Sants
Flexible account (£)	25,381 46	25,986 10	20,072 22	19,378 52	22,046 40

- Pensions

There are two sections to the pension plan operated by the FSA, both of which are non-contributory, a defined benefit section (closed to new entrants), and a defined contribution section Callum McCarthy, David Kenmir and Clive Briault 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

John Tiner and Hector Sants are not members of the pension 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 the table on page [xx]

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 2006 the Panel reviewed the fees payable, the Panel increased the fees for Non-executive Directors and the Chairman of FSA Pension Plan Trustee Ltd as shown in the table [xx]

Emoluments Tables

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

Table [xx]

	Accrued pension at 31 March 2006 £'000	Real increase/(decrease) in accrued pension £'000	Inflation £'000	Accrued pension at 31 March 2007 £'000[1]
Clive Briault	71	-	3	74
David Kenmir	52	-	2	54

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 [xx]

	Transfer value at 31 March 2006 £'000	Transfer value of real increase in accrued pension £'000	Other changes to transfer value £'000	Transfer value at 31 March 2007 £'000
Clive Briault	690	-	182	872
David Kenmir	386	-	102	488

At the end of the year, a deferred defined benefit pension was held in the Plan for two current 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 the 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 [xx]

Table [xx] 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

Members of the FSA Pension Plan have the option to pay Additional Voluntary Contributions, neither contributions nor the resulting benefits are included

Table [XX]

	Board fee £	Salary £	Performance related bonuses £	Other emoluments and benefits £	2007 Total £	2006 Total £
Callum McCarthy (Chairman)	-	360,000	-	73,565	433,565	436,142
Executive Directors						
Clive Briault	-	285,000	65,000	58,029	408,029	379,540
David Kenmir	-	285,000	65,000	83,453	433,453	383,121
Hector Sants	-	315,000	71,000	96,829	482,829	445,303
John Tiner[1]	-	430,000	95,000	127,577	652,577	572,619
Non-executive Directors[2]						
Dame Deirdre Hutton CBE (Deputy Chairman)[3]	60,000	-	-	-	60,000	60,000
James Crosby[5,6]	32,500	-	-	-	32,500	26,813
Tom de Swaan[4,5]	25,720	-	-	-	25,720	28,250
Brian Flanagan	4,905	-	-	-	4,905	-
Karin Forseke	25,000	-	-	-	25,000	22,500
Sir John Gieve[7]	-	-	-	-	-	-
Kyra Hazou[4]	20,095	-	-	-	20,095	22,500
Sir Andrew Large[7]	-	-	-	-	-	-
Professor David Miles	25,000	-	-	-	25,000	22,500
Michael Slack	25,000	-	-	-	25,000	22,500
Hugh Stevenson[5,8]	44,375	-	-	-	44,375	37,500
Stephen Thieke[9]	-	-	-	-	-	7,063
Clive Wilkinson[4]	20,095	-	-	-	20,095	22,500
	282,689	1,675,000	296,000	439,453	2,693,142	2,488,851
Of which fees for service as Directors					282,689	272,126
Remuneration as executives					2,410,453	2,216,725
					2,693,142	2,488,851

1 The total emoluments of the highest paid director during the year, John Tiner, were £652,577 (2006 £572,619), including a supplement of £49,468 (2006 42,553), paid during the year towards the funding of his personal pension

2 The fee for a non-executive director was set by the independent panel, established with the approval of HMT, at £25,000 per annum with effect from 1 April 2006

3 Dame Deirdre Hutton CBE was appointed as Deputy Chairman from 1 April 2004 The fee payable to the Deputy Chairman was set by the independent panel at £60,000 per annum with effect from 1 April 2005 and is unchanged for 2006/07

4 Tom de Swaan, Kyra Hazou and Clive Wilkinson all retired as Directors on 18 January 2007 and their fees for 2007 were pro-rated

5 An additional fee of £7,500 per annum is paid to any non-executive director (other than the Deputy Chairman) who has been appointed to chair a committee of the Board Two Directors chaired the Risk Committee during the year Tom de Swaan from 1 April 2006 to 2 January 2007, and Hugh Stevenson from 3 January 2007 to 31 March 2007 James Crosby chaired the Audit Committee throughout the year

6 The fee for James Crosby was paid directly to his previous employer, HBOS, for the three months to 30 June 2006, and from 1 July 2006 his salary was paid through the FSA payroll

7 Sir Andrew Large retired as a director on 15 January 2006, and Sir John Gieve was appointed from 16 January 2006 Both Directors waived their Board fees in respect of the years concerned

8 Hugh Stevenson also chaired the Board of FSA Pension Plan Trustee Ltd in the year The annual fee was set at £17,500 by the independent panel with effect from 1 April 2006

9 Stephen Thieke retired as a director on 30 June 2005

Committees of the Board

Audit Committee

The role of the Audit Committee is to advise the Board on the quality of the FSA's financial management and the adequacy of its internal control systems The Committee's terms of reference, and information on its membership, can be found on the FSA's website Committee members would like to thank Clive Wilkinson and Kyra Hazou, who retired from the Board during the year, for their work as members of the Committee

During the year, the Committee has

- invited senior management to attend its meetings and held private sessions with the internal and external auditor at each meeting,
- monitored the integrity of the financial statements and provided challenge to management on the FSA's financial performance,
- reviewed judgement and disclosure issues for the FSA's financial statements, including the adoption of international financial reporting standards,
- overseen the continuing work to re-structure the Information Systems function in order to address shortfalls in its performance previously identified,
- reviewed the internal financial controls and risk management systems, in conjunction with the Non-executive and Risk Committees,
- reviewed steps taken by management, to ensure that staff across the FSA understand the importance of compliance with all key internal processes and procedures,
- overseen the development of an online system, accessible to all staff, setting out the way in which the Board's delegated authority is exercised by senior management and staff committees,
- undertaken a review of the effectiveness and independence of the external Auditor, RSM Robson Rhodes, following the firm's appointment in early 2006,
- in conjunction with the Risk Committee, overseen work by the Strategy and Risk Division to streamline risk review and mitigation methodologies, to facilitate the allocation of responsibility for reviewing specific risk areas between both Committees,

- has considered whether the Executive has correctly assessed the risk by challenging the Executive on the risk rating and the actions taken to address the risk,

- overseen the implementation of improvements to the operation of the Internal Audit Division (formerly the Business Review and Audit Division), following an external review,

- reviewed the Director of Internal Audit's plans and specific reports produced throughout the year,

- considered updates on potential litigation against the FSA, and

- reviewed its own terms of reference to ensure that they remain in line with best practice and are consistent with those of the Risk Committee

RSM Robson Rhodes is not permitted to tender for internal audit work or for other work within the FSA above a pre-set financial limit based on a multiple of the audit fee Further information is provided in Note [xx] of the Accounts All services provided by RSM Robson Rhodes to the FSA are subject to defined procurement procedures

Risk Committee

The Committee's purpose is to assist the Board in reviewing risks to its statutory objectives The Committee's terms of reference, and information on its membership, can be found on the FSA's website Committee members would like to thank Tom de Swaan and Kyra Hazou, who retired from the Board during the year, for their work as members of the Committee Hugh Stevenson took over as Chairman from Tom de Swaan, whilst Peter Fisher joined the Committee

For 2006/07, the Committee has focused on the risks to the environment in which the FSA regulates, whilst the Audit Committee has reviewed risks to the FSA's day-to-day operations

The Committee has made use of the FSA's own risk management and reporting system This system records all risks identified and reviewed by local business areas Those risks are then reviewed and appropriate mitigation strategies put in place by the Executive

In reviewing the risks, the Committee has considered whether the Executive has correctly assessed the risk by challenging the Executive on the risk rating and the actions taken to address the risk The Committee has analysed the risk so as to form their own conclusion on whether the risk rating is appropriate and the mitigation strategy effective The Committee has also considered whether there are other risks that should be reviewed The Committee is aware that a proportionate approach to risk management is required, given that it is not possible to eliminate risks from the system The Committee's feedback on risk areas is reported back to the Board at its next meeting and into the risk management system as required

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

- international crisis management and co-operation including the consequences of avian flu on financial markets and markets' resilience to external shocks,

- the difficulties involved in tackling financial crime,
- excessive levels of credit,
- high levels of leveraged finance and the likelihood of a failure,
- the impact of changes in UK bankruptcy law for consumers and firms,
- private equity, focusing on the level of capital moving from public markets into private equity funds, and
- the implications of credit derivatives for financial markets

Internal Controls

The Board is responsible for ensuring that a system of internal controls is in place, and for reviewing its effectiveness 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 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

In accordance with FSMA Schedule 1 Part 14 (3) (b) NedCo, in conjunction with the Audit and Risk Committees, assists the Board by undertaking reviews of the adequacy of the control processes and challenging the executive on their effectiveness

Regulatory Decisions Committee (RDC)

Members of the RDC are appointed by the Board The Board receives quarterly reports from the RDC Chairman, who also attends Board meetings to discuss significant matters in those reports During the year the RDC Chairman reviewed the balance and composition of the Committee and discussed general succession planning with the Board 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, twice by attendance During the year LAAC reviewed its terms of reference and composition LAAC also oversaw a market user survey following the implementation of the new listing and prospectus rules More information can be found on page [xx]

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

Financial Statements
for the year ended 31 March 2007

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 2007 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 2007 and of its surplus 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 complying with its legal obligation to apply IFRSs adopted by the European Union, has also complied with the IFRSs as issued by the International Accounting Standards Board

In our opinion the financial statements give a true and fair view, in accordance with IFRSs, of the state the company's affairs as at 31 March 2007 and of its surplus for the year then ended

RSM Robson Rhodes LLP

RSM Robson Rhodes LLP
Chartered Accountants and Registered Auditors

London, England
25 May 2007

Income statement
for the year ended 31 March 2007

	Notes	2007 £m	2006 (Restated) £m
Administrative costs		(295 8)	(282 7)
Interest on bank deposits		5 1	4 4
Other net finance income/(costs)	15	1 0	(0 8)
Other revenue	7	26 0	22 8
Net costs for year		(263 7)	(256 3)
Fee revenue		282 1	265 1
Surplus before taxation		18 4	8 8
Taxation	8	(1 5)	(1 3)
Surplus after taxation	5	**16.9**	**7.5**

All results are derived from continuing operations

Statement of recognised income and expense for the year ended 31 March 2007

	Notes	2007 £m	2006 £m
Surplus for the year		16 9	7 5
Actuarial gains and losses for the year in respect of the defined benefit pension scheme	15	(14 2)	(20 1)
Total recognised income and expense for the year		2 7	**(12.6)**

Balance sheet as at 31 March 2007

	Notes	2007 £m	2006 £m
Non current assets			
Intangible assets	9	15 1	10 1
Property, plant and equipment	10	18 2	19 5
		33.3	**29.6**
Current assets			
Trade and other receivables	11	10 6	9 9
Trading investments	12	1 9	18 2
Cash and cash equivalents	11	47 8	37 6
		60.3	**65.7**
Total assets		**93.6**	**95.3**
Current liabilities			
Trade and other payables	13	(79 1)	(72 9)
Current tax liabilities		(0 8)	(0 8)
		(79.9)	**(73.7)**
Total assets less current liabilities		**13.7**	**21.6**
Non current liabilities			
Trade and other payables	13	(13 1)	(11 9)
Long term provisions	14	(2 1)	(2 5)
Net (liabilities)/assets excluding retirement benefit obligation		**(1.5)**	**7.2**
Retirement benefit obligation	15	(79 9)	(91 3)
Net liabilities, including retirement benefit obligation		**(81.4)**	**(84.1)**
Accumulated deficit	16	**(81.4)**	**(84.1)**

The financial statements were approved and authorised for issue by the Board on 24 May 2007, and were signed on its behalf by

Callum McCarthy — Chairman
John Tiner — Chief Executive Officer

Statement of cash flows
for the year ended 31 March 2007

	Notes	2007 £m	2006 £m
Net cash generated from operations	21	**8.5**	**28.4**
Corporation tax paid		(1 5)	(1 1)
Net cash from operating activities		**7.0**	**27.3**
Investing activities			
Interest received on bank deposits		5.1	4 4
Expenditure on software development	9	(10 3)	(4 5)
Purchases of property, plant and equipment	10	(7 9)	(6 1)
Sale / (Purchase) of trading investments		16 3	(1 2)
Net cash generated from/(used in) investing activities		**3.2**	**(7.4)**
Net increase in cash and cash equivalents		**10.2**	**19.9**
Cash and cash equivalents at the start of the year		37 6	17 7
Cash and cash equivalents at the end of the year		**47.8**	**37.6**

Notes to the financial statements – 31 March 2007

1. General information

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

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

- IFRS 7 Financial Instruments Disclosures, and the related amendments to IAS 1 on capital disclosures
- IFRS 8 Segmental Reporting
- IFRIC 8 Scope of IFRS 2
- IFRIC 9 Reassessment of embedded derivatives
- IFRIC 10 Interim reporting and impairments
- IFRIC 11 IFRS 2 – Group and Treasury Share Transactions
- IFRIC 12 Service Concession Arrangements

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

a. Income statement

The format of the income statement on page 4 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

UKLA fees have been reclassified and presented in the income statement as sundry income rather than fee income The impact is an increase in sundry income, and reduction in fee income, of £5 9m (2005/06 £5 5m)

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

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 10 years
Computer equipment (excluding software)	Up to 3 years
Furniture and equipment	Up to 10 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, for its employees There are two sections in the pension 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 long term 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 The FSA's policy for doing so is to use the penalties received in each financial year to reduce the amount owed by fee-payers in the relevant fee block in the following financial year Penalties received are included in current liabilities. trade and other payables

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 the 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 [xx].

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 £10 3m have been capitalised Management judgement has been applied in quantifying the benefit expected to accrue to the FSA over the useful life of the relevant assets If the benefits expected do not accrue to the FSA, then the carrying value of the asset will 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 in relation to rate of increase in salaries, corporate bond discount rates, retail price inflation and future pension increases 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

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 below

2007	Wholesale & Institutional Markets	Retail Markets	Regulatory Services	Corporate Services and Board	Total for continuing operations
	Year ended 31 March 2007	Year ended 31 March 2007	Year ended 31 March 2007	Year ended 31 March 2007	Year ended 31 March 2007
	£m	£m	£m	£m	£m
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 revenues					5 1
Other net finance (cost)/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)

2006 (Restated)	Wholesale & Institutional Markets	Retail Markets	Regulatory Services	Corporate Services and Board	Total for continuing operations
	Year ended 31 March 2006	Year ended 31 March 2006	Year ended 31 March 2006	Year ended 31 March 2006	Year ended 31 March 2006
	£m	£m	£m	£m	£m
Revenue					
Fees			265 1		265 1
Sundry income	5 5	0 9	13 0	3 4	22 8
Result					
Segmental surplus / (deficit)	(64.1)	(96 0)	231 9	(66 6)	5 2
Investment income					4 4
Other net finance (cost)/income					(0 8)
Surplus before tax					8 8
Income tax expense					(1 3)
Surplus for year					7 5
Other information					
Capital additions					
Tangible			6 1		6 1
Intangible			4 5		4 5
Depreciation			(8 7)		(8 7)
Amortisation			(5 3)		(5 3)
Trade receivables impairment losses			(0 7)		(0 7)
Current and past pension service costs	(1 8)	(2 4)	(2 7)	(1 6)	(8 5)

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 for the year

Surplus for the year has been arrived at after charging/(crediting) the following, which are included in administrative costs

	Note	**2007 £m**	2006 £m
Depreciation of property, plant and equipment		9 1	8 7
Amortisation of intangible assets		5 3	5 3
Staff costs	6	186 7	175 6

Auditor's remuneration for audit services (see below)

RSM Robson Rhodes LLP were the auditor for the full financial year

Total fees	**12 months to 31 March 2007 £'000**	**%**	**12 months to 31 March 2006 £'000**	**%**
Fees payable to the FSA's auditor for the audit of the FSA's annual accounts	79	98	98	68
Fees paid to the FSA's auditor or their associates in connection with non-audit work				
• Secondments	-	-	46	32
• Other services	2	2	-	-
Total	81	100	144	100

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

RSM Robson Rhodes LLP were appointed as auditor on 15 September 2005, accepting the appointment on 13 January 2006 Their audit fee for 2005/06 included non-recurring costs of

£21,150 (including VAT) for work undertaken by RSM Robson Rhodes LLP in auditing the implementation of our decision to adopt IFRS

The Audit Committee has reviewed the nature and content of non-audit work performed by the auditor to ensure that audit independence is 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 The FSA's auditor has announced negotiations for a prospective merger with Grant Thornton, to take place on 1 July 2007 Should that merger proceed to time, then the combined firm may, at that time, be charging fees for non-audit services that exceed the annual audit fee Both the FSA and its auditor are committed to bringing the level of fees for non-audit services in-line with its policy on such fees, within a year

6. Employee information

The average number of employees (including executive directors) during the year was 2,659 (2006 2,610) The average number of employees in each function during the current year was as follows

	2007	**2006 (restated[1])**
Retail Markets Business Unit	773	738
Wholesale & Institutional Markets Business Unit	572	556
Regulatory Services Business Unit	795	819
Corporate Services and Board (excluding enforcement)	273	261
Enforcement	246	236
	2,659	**2,610**

At 31 March 2007, the FSA had 2,606 (2006 2,667) employees

Employment costs (including executive directors) comprise	**Notes**	**2007 £m**	2006 £m
Gross salaries and taxable benefits		150 6	144 8
Employer's National Insurance costs		16 4	13 4
Employer's pension costs included in administrative costs		19 7	17 4
	5	186 7	175 6
Employer's pension income/ (costs) reported elsewhere			
Included in other finance income / (costs)	15	(1 0)	0 8
Included in statement of total recognised income and expenditure	15	14 2	20 1
Total employment costs		**199.9**	**196.5**

[1] The activities within each Business Unit were subject to some minor changes during the year 2006 comparatives have been restated accordingly

7. Other revenue

Other revenue comprises

	2007	2006 (Restated)
	£m	£m
Information and training services	6 8	8 4
Application fees and other regulatory income	9 7	10 9
Other sundry income	9 5	3 5
	26.0	**22.8**

8. Tax

The tax charge on ordinary activities is

	2007	2006
	£m	£m
Current tax on continuing operations	1 5	1 3
Corporation tax charge for the year	**1.5**	**1.3**

Corporation tax is calculated at 30% (2006 30%) of the estimated assessable surplus for the year The total charge for the year can be reconciled to the accounting surplus as follows

	2007	2006
	£m	£m
Surplus before tax on continuing operations	18 4	8 8
Tax at 30% thereon	5 5	2 6
Effects of		
Activities not subject to corporation tax	(4 0)	(1 3)
Current tax charge for the period	**1.5**	**1.3**
Effective tax rate for the period	**8%**	**15%**

Under an agreement with the HM Revenue & Customs 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 2005	**16.8**
Additions – internally generated	4 5
At 1 April 2006	**21.3**
Additions – internally generated	10 3
At 31 March 2007	**31.6**
Amortisation	
At 1 April 2005	**5.9**
Charge for the year	5 3
At 1 April 2006	**11.2**
Charge for year	5 3
At 31 March 2007	**16.5**
Net book value	
At 31 March 2007	**15.1**
At 31 March 2006	10 1

At 31 March 2007 expenditure totalling £10 0m had been capitalised on software developments that had not yet gone into operation (2006 £0 8m)

10. Property, plant and equipment

	Leasehold improvements £m	Computer equipment £m	Furniture and equipment £m	Total £m
Cost				
At 1 Apnl 2005	**19.8**	**36.8**	**10.7**	**67.3**
Addıtıons	0 1	5 2	0 8	6 1
Dısposals	-	(0 4)	-	(0 4)
At 1 Apnl 2006	**19.9**	**41.6**	**11.5**	**73.0**
Addıtıons	0 9	6 8	0 2	7 9
Dısposals	-	(0 3)	(0 2)	(0 5)
At 31 March 2007	**20.8**	**48.1**	**11.5**	**80.4**
Accumulated depreciation and impairment				
At 1 Apnl 2005	**11.9**	**25.6**	**7.7**	**45.2**
Charge for year	2 0	6 0	0 7	8 7
Dısposals	-	(0 4)	-	(0 4)
At 1 Apnl 2006	**13.9**	**31.2**	**8.4**	**53.5**
Charge for year	2 3	5 9	0 9	9 1
Dısposals	-	(0 2)	(0 2)	(0 4)
At 31 March 2007	**16.2**	**36.9**	**9.1**	**62.2**
Carrying amount				
At 31 March 2007	**4.6**	**11.2**	**2.4**	**18.2**
At 31 March 2006	6 0	10 4	3 1	19 5

The FSA has revıewed the resıdual values used for the purposes of depreciatıon calculatıons The revıew dıd not ıdentıfy any requırement for adjustment to the resıdual values used ın the current or pnor penods Resıdual values wıll be revıewed and updated annually

11. Other financial assets

Trade and other receivables

	2007 £m	2006 £m
Fee receivables	2 4	2 7
Other debtors	0 9	0 9
Prepayments and accrued income	7 3	6 3
	10.6	**9.9**

The average credit period taken is 50 days (2006 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%

An allowance has been made for the estimated irrecoverable amounts from fees invoiced of £0 5m (2006 £0 7m) 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

Cash and cash equivalents

Bank balances and cash comprise cash held by the FSA and short term 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 4% (2006 4 54%) and the average maturity of 45 days (2006 29 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

The FSA has no sıgnıficant concentratıon of credıt rısk as ıts exposure ıs spread over a large number of counterpartıes

12. Trading investments

	2007 **£m**	2006 £m
Avaılable for sale ınvestments – faır value	1 9	18 2

Investments relate to cash deposıts wıth an orıgınal maturıty date ın excess of 90 days

13. Trade and other payables

Current

	2007 **£m**	2006 £m
Trade credıtors and accruals	47 9	46 6
Other taxatıon and socıal securıty	2 8	2 8
Fınancıal penaltıes to be applıed agaınst fees receıvable	15 6	16 9
Fees ın advance	12 8	6 6
	79.1	**72.9**

Trade credıtors and accruals prıncıpally comprıse amounts outstandıng for trade purchases and ongoıng costs The average credıt perıod taken for trade payables ıs 29 days (2006 16 days) The dırectors consıder the carryıng amount of trade payables approxımates theır faır value

Non-current

A lease accrual of £13 1m (2006 £11 9m), beıng the cumulatıve dıfference between cash paıd and expense recognısed on operatıng leases for land and buıldıngs, ıs recognısed as a long term lıabılıty

At 31 March 2007 the FSA had avaılable £100m (2006 £nıl) of undrawn commıtted borrowıng facılıtıes ın respect of whıch all condıtıons precedent had been met The facılıty was taken out on 26 January and ıs repayable ın full on 26 January 2010 The facılıty ıs unsecured and carrıes ınterest rate at 0 08% above LIBOR

14. Provisions

	Total
	£m
At 1 April 2006	2.5
Utilised in the year	(1.2)
Charge in the year	0.8
At 31 March 2007	**2.1**
Included in current liabilities	-
Included in non-current liabilities	**2.1**

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

15. Retirement benefit obligation

The FSA operates a tax-approved pension scheme, the FSA Pension Plan, that 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 1 April 2004 by an independent actuary, using the projected unit method. The results of this valuation have been updated for the purpose of IAS 19 as at March 2007, in order to allow for any changes in assumptions and movements in liabilities over the period. The next full actuarial valuation is expected to be carried out as at 1 April 2007, and should be available during 2007/08

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

	At 31 March 2007	At 31 March 2006
Expected rate of salary increases	4 0%	4.0%
Corporate bond discount rate	5 2%	4.9%
Expected return on scheme assets	7 3%	6.9%
Retail price inflation (RPI)	3 0%	2.8%
Future pension increases	2 9%	2.8%

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 2007 mortality assumptions are based on an actuarial table 'PA1992, projected to allow for future improvements using medium cohort projections and by an individual's year of birth' The 2006 mortality assumptions were based on an actuarial table PA92c2010 for current pensioners and PA92c2030 for future pensioners

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)

		2007	2006
		years	years
Retiring today			
Males		26.7	23.5
Females		29 7	26 5
Retiring in 15 years			
Males		27 7	25 2
Females		30 5	28.2

The amount recognised in the balance sheet is as follows

	2007 £m	2006 £m
Fair value of plan assets	289 1	250 6
Less Present value of funded obligations	(367 1)	(340 1)
Deficit in the scheme	**(78.0)**	**(89.5)**
Unfunded pension liabilities	(1 9)	(1 8)
Net liability recognised in the balance sheet	**(79.9)**	**(91.3)**

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 2007 the liability is £1 9m (2006 £1 8m) to cover the cost of these promises An amount of £0 1m (2006 £0 4m) is included in the total pension cost for the year in note 6, representing the value of the additional benefits accrued

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

	2007 £m	2006 £m
Current service cost	9 4	8 2
Past service cost	0 3	0 3
Administration expenses	**9.7**	**8.5**
Expected return on plan assets	18 0	13 7
Interest on scheme liabilities	(17 0)	(14 5)
Other finance income / (costs)	**1.0**	**(0.8)**

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 gains and losses of £14 2m (2006 £20 1m) are recognised in the period in which they occur as part of the Statement of recognised income and expense

The actual return on plan assets was £9 3m (2006 £52 5m)

Changes ın the present value of the defined benefit oblıgatıon are as follows

	2007 £m	2006 £m
Openıng oblıgatıon	(340 1)	(261 1)
Current service cost	(9 4)	(8 2)
Past servıce cost	(0 3)	(0 3)
Benefits paıd	5 2	2 9
Interest cost	(17 0)	(14 5)
Actuarıal losses	(5 5)	(58 9)
Closing obligation	**(367.1)**	**(340.1)**

Changes ın the faır value of plan assets are as follows

	2007 £m	2006 £m
Openıng faır value of plan assets	250 6	182 2
Expected return on plan assets	18 0	13 7
Actuarıal (losses)/gaıns	(8 7)	38 8
Contrıbutıons by the employer	34 4	18 7
Benefits paıd	(5 2)	(2 8)
Closing fair value of plan assets	**289.1**	**250.6**

The faır value of plan assets and the expected rates of return were

	Expected rate of return at 31 March 2007	Faır value at 31 March 2007 £m	Expected rate of return at 31 March 2006	Faır value at 31 March 2006 £m
Equıtıes	7 9%	180 8	7 4%	199 3
Corporate Bonds	5 4%	68 4	4 9%	45 1
Property	7 9%	26 4	-	-
Currency Management	7 9%	11 1	-	-
Cash	5 25%	2 4	4 5%	6 2
Closing fair value of plan assets	**7.3%**	**289.1**	**6.9%**	**250.6**

Cumulative actuarial losses recognised in equity

	2007 **£m**	2006 £m
1 April	(23 9)	(3 8)
Net actuarial losses recognised in the year	(14 2)	(20 1)
At 31 March	**(38.1)**	**(23.9)**

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

	2007	2006	2005
Defined benefit obligation (£m)	(367 1)	(340 1)	(261 1)
Fair value of plan assets (£m)	289 1	250 6	182 2
Net deficit (£m)	(78 0)	(89 5)	(78 9)
Experience adjustments on scheme assets			
Amount (£m)	(8 7)	38 8	2 4
percentage of scheme assets	3 0%	15 5%	1 3%
Experience gains and losses on scheme liabilities			
Amount (£m)	(0 7)	0 1	(0 3)
percentage of the present value of scheme liabilities	0%	0%	0%

The contribution rate for 2006/07 was 23 7% of pensionable earnings plus £26 0m (75 5% of pensionable earnings) as an additional deficit reduction contribution The agreed contribution rate for 2007/08 is 23 0% of pensionable earnings plus £2 5m (approximately 7 4% of pensionable earnings) as an additional deficit reduction contribution

Defined contribution scheme

The total expense recognised in the income statement of £8 7m (2006 £7 9m) 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 2005	(71 5)
Surplus for the year	7 5
Actuarial gains and losses for the year in respect of the defined benefit pension scheme	(20 1)
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)
	(81.4)

The Financial Services Authority 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 2007 for capital expenditure totaling £1 8m (2006 £0 5m), which are not provided for in the accounts

18. Operating lease arrangements

	2007 £m	2006 £m
Minimum lease payments under operating leases recognised as an expense in the year	11 8	10 6

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

	2007 £m	2006 £m
Within 1 year	12 2	11 0
In the second to fifth years inclusive	46 9	43 9
After five years	83 7	96 5
	142.8	**151.4**

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 RPI subject to a minimum annual increase of 2 5% per annum and a maximum of 5% per annum As mentioned in note 15, our current assumptions for RPI is 3 0%

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 audit part of the Corporate Governance Statement on pages [x to x]

	2007	2006
	£m	£m
Short term benefits	2 7	2 5
Post-employment benefits	0 3	0 1
	3.0	**2.6**

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 2007 was £0 3m (2006 £0 1m). The charge for the service was £0 2m (2006 £0 2m)

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 the 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 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 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 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 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 2,209 (2006 2,237) of which 2,069 are, or were, employees of the FSA (2006 2,098) and 139 of the FOS (2006 139)

In 2005/06 the FSA entered into an agency agreement with 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 2007 £1 1m of on-account fees for 2008/09 had been collected but not paid to FOS (£1 0m at 31 March 2006)

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 (2006 £15m) available for draw down from 24 January 2003 and repayable by 2011 Amounts outstanding under the facility are guaranteed by the FSA As at 31 March 2007, £7 5m (2006 £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 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 the FOS funding arrangements, no fair value was assigned on inception

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 2006/07, the FSA has transferred £0 4m (2006 £0 5m) to the OCC to cover the latter's running costs, which have been expensed in the FSA's income statement At 31 March 2007, the balance owing to the FSA from the OCC was £0 1m (2006 £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 (2006 £ nil)

20. Contingent Liabilities

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

The FSA is aware that certain parties are considering the possibility of making claims against it relating to the regulation of Independent Insurance Limited and Equitable Life No material claims have 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	**2007 £m**	2006 £m
Surplus for the year from continuing operations		16 9	7 5
Adjustments for			
Interest received on bank deposits		(5 1)	(4 4)
Corporation tax expense	8	1 5	1 3
Amortisation of other intangible assets	9	5 3	5 3
Depreciation of property, plant and equipment	10	9 1	8 7
Decrease in provisions	14	(0 4)	(0 4)
Difference between pension costs and normal contributions		0 5	1 5
Additional cash contributions to reduce pension scheme deficit	16	(26 0)	(10 5)
Operating cash flows before movements in working capital		1 8	9 0
(Increase) / decrease in receivables	11	(0 7)	8 6
Increase in payables		7 4	10 8
Net cash generated from operations		**8.5**	**28.4**

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 2007

Introduction

The FSA sets fees by reference to blocks of fee payers conducting similar activities, which so far as possible, reflect the FSA's costs applicable to the respective fee blocks The statement of allocation of costs on page 39 shows the allocation of costs for the year ended 31 March 2007, analysed by those fee blocks

Costs are allocated according to the method set out in note 1 on page 38 The report of the auditors is set out on page 40

Notes to the statement of allocation of costs for the year ended 31 March 2007

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 2007 £m
Net costs for the year	265 2
Add difference between accounting changes for provisions in the statutory accounts and the related cash costs of pension contributions paid	5 6
Less costs of implementing principles-based regulation	(1 5)
Net costs for the year on statement of allocation of costs	**269.3**

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 and expenditure account 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 cost £1m 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 2007/08 are included in Consolidated Policy Statement on our fee-raising arrangements and regulatory fees and levies 2007/08, including feedback on CP07/3 and 'made rules', published in May 2007

Statement of allocation of costs for the year to 31 March 2007

	Fee Block	Net assets, excluding pensions obligation at 1 April 2006 £m	Net costs for the year £m	Pensions amortisation £m	Fees for the year £m	Funding principles-based regulation £m	Net assets/(liabilities), excluding pensions obligation, at 31 March 2007 £m
A 1	Deposit acceptors	3 3	(52 8)	(0 9)	58 4	(3 0)	5 0
A 2	Mortgage lenders and administrators	(0 6)	(5 6)	(0 1)	5 8	(0 3)	(0 8)
A 3	General insurers	(0 8)	(14 2)	(0 3)	15 8	(0 8)	(0 3)
A 4	Life insurers	1 0	(39 4)	(0 7)	40 8	(2 2)	(0 5)
A 5	Lloyd's Managing Agents	(0 2)	(1 0)	-	0 8	(0 1)	(0 5)
A 6	The society of Lloyd's	0 1	(1 0)	-	1 1	(0 1)	0 1
A 7	Fund managers	1 8	(24 6)	(0 4)	26 6	(1 4)	2 0
A 9	CIS operators, trustees and depositories	0 5	(3 3)	(0 1)	4 7	(0 2)	1 6
A 10	Firms dealing as principal	0 1	(14 4)	(0 3)	12 9	(0 8)	(2 5)
A 12	Advisory arrangers holding client money and/or assets	0 3	(18 0)	(0 3)	17 8	(1 0)	(1 2)
A 13	Advisory arrangers not holding client money and/or assets	2 8	(37 9)	(0 7)	36 3	(2 1)	(1 6)
A 14	Corporate Finance Advisors	0 8	(5 5)	(0 1)	5 5	(0 3)	0 4
A 18	Mortgage lenders, advisers, and arrangers	(1 1)	(11 0)	(0 2)	10 2	(0 6)	(2 7)
A 19	General insurance mediation	(1 0)	(27 1)	(0 5)	29 8	(1 5)	(0 3)
B	RBs	0 3	(3 4)	(0 1)	3 6	(0 2)	0 2
C	CIS	0 1	(1 4)	-	1 4	(0 1)	-
D	DPBs	0 3	(0 2)	-	0 2	-	0 3
E	UKLA	(0 5)	(6 8)	(0 1)	9 1	(0 4)	1 3
F	Registrant only	-	(1 7)	-	1 3	(0 1)	(0 5)
Total		7 2	(269 3)	(4 8)	282 1	(15 2)	-
	Less costs incurred in introducing principles-based regulation						(1 5)
	Net deficit excluding pensions obligation						**(1 5)**

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 2007 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 RSM Robson Rhodes 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

RSM Robson Rhodes LLP

RSM Robson Rhodes LLP
Chartered Accountants
London

25 May 2007