



## Investors Technical Advisory Committee

401 Merritt 7, P.O. Box 5116, Norwalk, Connecticut 06856-5116 | Phone: 203 956-5311 Fax: 203 849-9714

Via Email

February 12, 2008



LETTER OF COMMENT NO. 49

Ms. Teresa S. Polley  
Chief Operating Officer  
Financial Accounting Foundation  
401 Merritt 7  
Norwalk, CT 06856-5116

Re: Request for Comments on Proposed Changes to Oversight, Structure, and Operations of the FAF, FASB, and GASB<sup>1</sup>

Dear Terri:

The Investors Technical Advisory Committee (“ITAC”) appreciates the opportunity to comment in response to the Proposed Changes to Oversight, Structure, and Operations of the FAF, FASB, and GASB (“Proposal”).<sup>2</sup> The ITAC strongly agrees with the need for, and the authority of,<sup>3</sup> the Financial Accounting Foundation (“FAF”) “to periodically review the structure and governance of” the FAF, the Financial Accounting Standards Board (“FASB”) and the Governmental Accounting Standards Board (“GASB”).<sup>4</sup> We believe any actions to improve the “effectiveness and efficiency” of the FAF, the FASB, and the GASB should be considered in the context of the need to protect the independence of the FASB and the GASB to ensure the development of high quality standards that serve the needs of investors and other users of financial reports.

Per our review of the Proposal, the ITAC neither can support nor meaningfully respond to the Proposal in its current form for the simple reason that we believe it fails to provide a sufficient basis for most of its proposed actions. In that regard, our views are best summarized using a statement made by former FASB member Katherine Schipper who, in commenting on the Proposal, stated: “What is the problem or set of problems to which this [proposal] is the solution?”<sup>5</sup>

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<sup>1</sup> Financial Accounting Foundation (“FAF”), Request for Comments on Proposed Changes to Oversight, Structure, and Operations of the FAF, FASB, and GASB (2008), <http://www.fasb.org/FAF%20Proposed%20Changes.pdf>.

<sup>2</sup> This letter represents the views of the Investors Technical Advisory Committee (“ITAC”) and does not necessarily represent the views of its individual members, the organizations by which they are employed, or the views of the Financial Accounting Standards Board (“FASB”) or its staff. For more information about the ITAC, including a list of the current members and the organizations in which they are employed, see [http://www.fasb.org/investors\\_technical\\_advisory\\_committee/](http://www.fasb.org/investors_technical_advisory_committee/).

<sup>3</sup> FASB, Rules of Procedure 41 (Dec. 1, 2002) (on file with author).

<sup>4</sup> FAF, *supra* note 1, at 1.

<sup>5</sup> Tim Reason & Marie Leone, Downsizing FASB, CFO.Com 1 (Dec. 18, 2007), <http://www.cfo.com/article.cfm/10327925?f=related>.

The absence of a sufficient basis for most of the proposed actions contained in the Proposal has fueled rampant speculation about the “real reasons” for the Proposal.<sup>6</sup> Such speculation does nothing to enhance the credibility of the FAF, is vastly inconsistent with the procedures required for proposals of the FASB,<sup>7</sup> and does nothing to benefit investors or other users of financial reports.

Given the aforementioned lack of clarity regarding the reasons for the proposed actions, ITAC recommends that the FAF re-publish the Proposal for public comment with additional information that more fully explains the basis for the proposed actions, including what other alternatives may have been considered and why they were rejected. We would also welcome the opportunity to meet with representatives of the FAF in person to better understand the basis for the conclusions reached.

Notwithstanding our previously mentioned inability to provide support for the Proposal, we would like to offer the following specific comments in response to the questions raised therein:

***Proposed Action: Expand the breadth of individuals and organizations that are invited to submit nominations for the FAF Board of Trustees with the understanding that final authority for all appointments rests solely with the Board of Trustees.***

The ITAC generally supports expanding the breadth of individuals and organizations that are invited to submit nominations for the FAF Board of Trustees. We believe individuals who serve on the FAF Board of Trustees should have a demonstrated track record of acting in the public interest, sufficient knowledge and understanding of the needs of investors and other users of financial reports, and an ability and interest to actively protect the independence of the FASB and GASB while at the same time providing an appropriate level of oversight.

We note that the proposed action would be a modest revision to current procedures because: (1) it contemplates that the Financial Nominating Organizations (“FNOs”) would continue to participate in the nominating process;<sup>8</sup> and (2) five of the current sixteen FAF Board of Trustees seats are “at large” selections and, therefore, are presumably the result of well qualified nominees solicited or received from parties other than the FNOs and the Governmental Nominating Organizations (“GNOs”).<sup>9</sup>

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<sup>6</sup> See, e.g., Letter from Robert H. Colson, Chair, AAA Financial Accounting Standards Committee, to Teresa S. Polley, Chief Operating Officer (“COO”), FAF 10 (Feb. 1, 2008).

<sup>7</sup> FASB, *supra* note 3, at 13.

<sup>8</sup> FAF, *supra*, note 1, at 3.

<sup>9</sup> *Id.* at 2.

We also note that historically the FNOs involvement in the selection of FAF Board of Trustees appears to have been based, in significant part, on a commitment by those organizations to participate in the raising of funds required for the operation of the FASB.<sup>10</sup> That purpose is currently less relevant as a result of the accounting support fee requirements of the Sarbanes-Oxley Act of 2002 (“SOX”).<sup>11</sup> Thus, it makes some sense to us that the nominating process be formally expanded beyond the FNOs and GNOs to solicit additional “at large” nominations.

Finally, if the Board of Trustees decides to expand the breadth of those invited to submit nominations for the Board of Trustees, the ITAC would welcome the opportunity to participate in that process.

***Proposed Action: Change the term of service for Trustees from two three-year terms to one five-year term.***

The ITAC generally does not object to changing the term of service for Trustees from two three-year terms to one-five year term. We, however, do not understand how such a change would “provide the opportunity for a larger number of qualified Trustees to bring their skills and perspectives to the FAF.”<sup>12</sup>

It seems questionable to us that a one-five year term would be more attractive to qualified candidates than a three-year term with the possibility of serving a second term. We believe the better argument is that the proposed action would actually reduce the number of qualified candidates interested in serving because some candidates would likely feel uncomfortable agreeing to a five year commitment and, therefore, remove themselves from consideration.

Finally, we believe the existing two three-year terms might provide a better opportunity for new Trustees and the existing Trustees to mutually explore potential suitability issues and make more timely adjustments when appropriate.

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<sup>10</sup> See American Institute of Certified Public Accountants (“AICPA”), Report of the Study on Establishment of Accounting Principles, Establishing Financial Accounting Standards 9 (Mar. 1972) (on file with author) (The original financial nomination organizations were the Financial Executives Institute, the National Association of Accountants, the Financial Analysts Federation, and the American Accounting Association).

<sup>11</sup> See Sarbanes-Oxley Act of 2002, Section 109(e) (2002),

<http://f11.findlaw.com/news.findlaw.com/hdocs/docs/gwbush/sarbanesoxley072302.pdf>.

<sup>12</sup> FAF, *supra*, note 1, at 3.

***Proposed Action: Change the size of the Board of Trustees from sixteen to a range of fourteen to eighteen members.***

The ITAC generally does not object to changing the size of the Board of Trustees from sixteen to a range of fourteen to eighteen members. We, however, again do not understand how such a change would “enable the Board of Trustees to better react to a changing environment by having the ability to add particular experience and expertise as needed.”<sup>13</sup> It seems to us that if the objective of the proposed action is to enhance the ability to *add* particular experience and expertise in response to a changing environment than the appropriate proposed action would be to change the size of the Board of Trustees from sixteen to a range of sixteen to eighteen or more members.

We also note that this proposed change appears to be in direct conflict with the preceding proposed change regarding the terms of the Board of Trustees. If the objective is to be able to react more quickly to a changing environment by adding additional Trustees, why would you also propose to increase the term of service from a three-year to a five-year term?

Finally, we believe there are other potential approaches to obtaining, at least in the short-term, particular experience and expertise to better react to a changing environment. One such approach might be to assemble an ad-hoc advisory committee of individuals with the particular experience or expertise deemed necessary. If this approach were to be pursued, the ITAC would welcome the opportunity to assist in identifying individuals from the investor community who might be appropriate members of such a committee.

***Proposed Action: Strengthen and enhance the governance and oversight activities of the Trustees as to efficiency and effectiveness of the standard-setting process.***

The ITAC generally does not object to strengthening and enhancing the governance and oversight activities of the Trustees as to the efficiency and effectiveness of the standard setting process. The ITAC, however, does object to the Trustees having greater involvement in the FASB’s “agenda setting” process as described in the proposed action.<sup>14</sup>

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<sup>13</sup> *Id.* at 4.

<sup>14</sup> *Id.*

We believe that expressly providing the Trustees a role in the agenda setting process increases the real risk of inappropriate special interest group influence on the standard setting process that would be inconsistent with the needs of investors and the capital markets. We note that when the FAF and FASB were originally founded, their respective roles were carefully, and we believe appropriately, designed to provide for a structure that would result in accounting standard setting “free of any private interests which might conflict with the public interest.”<sup>15</sup> Within that structure, the part-time FAF Trustees were limited to (1) appointing members of the FASB and the Financial Accounting Standards Advisory Council (“FASAC”); (2) raising and allocating the funds required for the operation of the FASB; and (3) periodically reviewing and, if deemed necessary, revising the structure of the FASB.<sup>16</sup>

Distinct from the FAF, the FASB was designed to be the standard setting organization free “from client and other pressures.”<sup>17</sup> Thus, the FASB was required to be composed of “full-time” board members with “no business affiliations.”<sup>18</sup> Consistent with that designation, the FASB was given the authority to establish its own agenda and “priorities” with input from the FASAC.<sup>19</sup> The existing by-laws of the FAF appropriately reflect this important division of roles and responsibilities by expressly prohibiting the FAF from “undertak[ing] any particular project or activity or otherwise affect the exercise by the FASB or GASB of their authority, functions, and powers in respect to standards of financial accounting and reporting.”<sup>20</sup>

Consistent with the original purposes of the FAF and FASB, we believe it is appropriate for the FASB to continue to be solely responsible for developing its own agenda with input from the FASAC,<sup>21</sup> the ITAC, and other interested parties. We can identify no compelling basis for inserting the FAF into the agenda setting process.

***Proposed Action: Reduce the size of the FASB from seven members to five.***

The ITAC generally opposes reducing the size of the FASB from seven members to five. We note that the Proposal indicates that the proposed action will make the FASB “more nimble and responsive to domestic and global demands,” and “more effective and efficient.”<sup>22</sup> We find the basis for this proposed action less than convincing.

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<sup>15</sup> See AICPA, *supra* note 10, at 10.

<sup>16</sup> *Id.* at 9.

<sup>17</sup> *Id.* at 8.

<sup>18</sup> *Id.* at 9.

<sup>19</sup> *Id.* at 76.

<sup>20</sup> FASB, *supra* note 3, at 39-40.

<sup>21</sup> AICPA, *supra* note 10, at 76.

<sup>22</sup> FAF, *supra* note 1, at 5.

The FASB was originally designed to have seven members because seven was viewed as “small enough to be efficient and large enough to provide for a variety of views and backgrounds.”<sup>23</sup> The Proposal provides no basis for overturning that conclusion. Moreover, given the significant issues facing the FASB today, including addressing major topics on international convergence and transparency related to the market disruption caused by the sub prime crisis, reducing the aggregate expertise at the FASB might dangerously weaken accounting standard setting at a critical time.

More specifically, it is our view that reducing the size of the FASB from seven members to five will likely make the Board *less* nimble and responsive and *less* effective and efficient for at least two reasons: (1) there will be fewer Board members available to take leadership roles on standard setting projects and related research and technical activities, and (2) there will be fewer Board members to engage in external communications with domestic (including the ITAC) and international constituents.

For similar reasons, the FAF rejected a March 2002 proposal to reduce the size of the FASB from seven members to five members to improve “the FASB’s efficiency.”<sup>24</sup> On that occasion the reaction from preparers, auditors, and users was generally negative<sup>25</sup> and the FAF ultimately decided to retain a seven-member Board.<sup>26</sup> We are not persuaded that a different conclusion is now appropriate.

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<sup>23</sup> AICPA, *supra* note 10, at 72.

<sup>24</sup> News Release, FASB, *Financial Accounting Foundation Considers Changes to Streamline FASB Process; Emphasizes Need for Independent Accounting Standard Setter* (Mar. 14, 2002), <http://72.3.243.42/news/nr031402.shtml>.

<sup>25</sup> *See, e.g.*, Letter from Richard J. Swift, Chairman, Financial Accounting Standards Advisory Council, to Joseph S. LaGambina, Executive Vice President, FAF 1 (Apr. 1, 2002) (on file with author) (“The general consensus of the FASAC members is that a reduction in the number of FASB members is not advisable . . .”).

<sup>26</sup> News Release, FASB, *Financial Accounting Foundation Changes Financial Accounting Standards Board’s Voting to Increase Efficiency* (Apr. 24, 2002), <http://72.3.243.42/news/nr042402b.shtml>.

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We also find of some import that many of the commentators to the Proposal that are the most familiar with the FASB have expressed strong opposition to this proposed change, including three former FASB members,<sup>27</sup> and the current Chair and most recent former Chair of the FASAC.<sup>28</sup>

Finally, we again note the inconsistencies in the proposed actions. The stated basis for this proposed action is, in part, to make the FASB more nimble. The previous proposed action contemplating inserting more than a dozen Trustees into the FASB agenda process would almost certainly make that FASB process *less* nimble.

***Proposed Action: Retain the FASB simple majority voting requirement.***

The ITAC generally supports retaining the simple majority voting requirement. We agree that requiring “a supermajority . . . vote would have the potential to give too much weight to a minority view.”<sup>29</sup> We also believe that requiring a super majority vote might add additional pressure on the Board to “sacrifice decisiveness and principle to acceptability”—a result generally inconsistent with the needs of investors and the capital markets.<sup>30</sup>

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<sup>27</sup> Letter from James J. Leisenring, Former FASB Board Member, to Teresa Polley, COO, FAF 2-3 (Jan. 28, 2008), [http://www.fasb.org/faf/comment\\_letters/51884.pdf](http://www.fasb.org/faf/comment_letters/51884.pdf) (“It is most inopportune to propose this when pressures have increased on Board members to much more extensively deal with outside constituents”); Letter from Robert J. Swieringa, Professor of Accounting, The Johnson School, Cornell University, to Teresa S. Polley, COO, FAF 1 (Jan. 28, 2008), [http://www.fasb.org/faf/comment\\_letters/51875.pdf](http://www.fasb.org/faf/comment_letters/51875.pdf) (“I do not believe that reducing the number of FASB Board members from seven to five would result in the FASB being ‘more nimble and responsive to domestic and global demands’”); Letter from Edward W. Trott, Former FASB Board Member, to Teresa S. Polley, COO, FAF 2 (Jan. 28, 2008), [http://www.fasb.org/faf/comment\\_letters/51883.pdf](http://www.fasb.org/faf/comment_letters/51883.pdf) (“I did not in 2002 and do not today believe that reducing the Board to five will make the FASB ‘more nimble and responsive to domestic and global demands’”).

<sup>28</sup> Letter from Dennis H. Chookaszian, Chairman, Financial Accounting Standards Advisory Council, to Teresa S. Polley, COO, FAF 3 (Feb. 4, 2008), [http://www.fasb.org/faf/comment\\_letters/51893.pdf](http://www.fasb.org/faf/comment_letters/51893.pdf) (“The proposed change seems more like a solution that is in search of a problem, rather than a problem in need of a solution”); Letter from Richard J. Swift, to Terri Polley, President and COO, FAF 2 (2008), [http://www.fasb.org/faf/comment\\_letters/51792.pdf](http://www.fasb.org/faf/comment_letters/51792.pdf) (“The reduction of the FASB members to 5 doesn’t make any sense to me”).

<sup>29</sup> FAF, *supra* note 1, at 6.

<sup>30</sup> AICPA, *supra* note 10, at 62

**Proposed Action: Realign the FASB composition.**

The ITAC generally supports a realignment of the FASB composition that would increase the representation of the main customers of the FASB's product—investors and other users of financial reports. More broadly, we believe that *all* FASB member appointments should be the result of a selection process that considers candidates to be the “best qualified” in terms of: (1) independent-mindedness; (2) financial accounting and reporting expertise; and (3) a commitment to improving financial accounting and reporting for the benefit of investors and other users of financial reports.<sup>31</sup>

**Proposed Action: Provide the FASB Chair with decision-making authority to set the FASB technical agenda.**

The ITAC generally opposes providing the FASB Chair with the decision-making authority to set the FASB technical agenda. We note that this proposed action would result in a significant structural change to the FASB's historic standard setting process which was designed, in part, to broaden the base and variety of skills involved in standard setting decisions.<sup>32</sup> This notion is reflected in the FASB's current rules of procedure, which specify that the FASB Chair shall prepare “an agenda of projects and priorities,” but that any agenda must be submitted “for approval” by the FASB members.<sup>33</sup>

We are troubled by the fact that the proposed action would appear to provide the FASB Chair the authority to remove a project from the technical agenda even if the project was supported by all of the other FASB members and the ITAC. Our concern is heightened by the public reports over the past year of efforts by the United States Securities and Exchange Commission to exert more control over the standard setting process in direct conflict with the language and intent of SOX.<sup>34</sup> We believe maintaining the existing agenda decision making process “driven by Board member consensus” with input from the FASAC,<sup>35</sup> the ITAC, and other constituent groups lessens the opportunity for the FASB's independence to be impaired by self interested special interest groups to the detriment of investors and the capital markets.<sup>36</sup>

Finally, we are also concerned that providing the FASB Chair with decision-making authority to set the FASB technical agenda will inhibit the ability to attract strong candidates to the FASB. Some high quality candidates would likely have concerns about joining a board in which their ability to effect improvements in particular areas may be stymied by the Chair's control over the agenda.

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<sup>31</sup> FAF, *supra* note 1, at 6.

<sup>32</sup> AICPA, *supra* note 10, at 10-11.

<sup>33</sup> FASB, *supra* note 3, at 51.

<sup>34</sup> *See, e.g.*, Marie Leone & Alan Rapoport, SEC Said No to FASB Raises, CFO.com (Apr. 2, 2007), <http://www.cfo.com/article.cfm/8952913>.

<sup>35</sup> FAF, *supra* note 1, at 6.

<sup>36</sup> FAF, *supra* note 1, at 6.



**Proposed Action: *Secure a stable mandatory funding source for the GASB.***

Although the ITAC has limited interaction with the GASB, we generally support securing a mandatory funding source for the GASB so that it can meet the needs of the users of the financial reports of state and local governmental entities. We believe that the GASB, like any accounting standard setter, must be adequately funded to provide high quality and timely standards.<sup>37</sup> We also believe that the key criterion for evaluating the appropriateness of a funding source for the GASB or any other accounting standard setter is whether the source enhances rather than detracts from the independence of the standard setter.<sup>38</sup>

**Proposed Action: *Retain the current size, term length, and composition of the GASB.***

The ITAC generally does not object to retaining the current size, term length, and composition of the GASB. However, to the extent that additional funding becomes available, we would support having seven full-time GASB Board members subject to a prudent evaluation of other needs and the potential benefits.

In addition, as with the FASB, we believe that all GASB member appointments should be the result of a selection process that considers the best qualified candidates in terms of: (1) independent-mindedness; (2) financial accounting and reporting expertise; and (3) a commitment to improving financial accounting and reporting for the benefit of the users of financial reports.

**Proposed Action: *Provide the GASB Chair with decision-making authority to set the GASB technical agenda.***

The ITAC generally opposes providing the GASB Chair with decision-making authority to set the GASB technical agenda for the same reasons we oppose providing the FASB Chair with that authority.

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<sup>37</sup> See Letter from Jack Ciesielski, Member, Investors Technical Advisory Committee to Nancy M. Morris, Secretary, Securities and Exchange Commission 3 (Nov. 2, 2007), [243.42/investors\\_technical\\_advisory\\_committee/11-02-07\\_ifrs\\_concept\\_release.pdf](https://www.sec.gov/243.42/investors_technical_advisory_committee/11-02-07_ifrs_concept_release.pdf).

<sup>38</sup> *Id.*

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Thank you for the opportunity to comment on the Proposal. Should you have any questions, or would like to further discuss any of our comments in more detail, please contact me at 202.261.7081 or [jeff@cii.org](mailto:jeff@cii.org).

Sincerely,

A handwritten signature in black ink that reads "Jeff Mahoney". The signature is written in a cursive style with a large, stylized initial "J".

Jeff Mahoney  
Co-Chair  
Investors Technical Advisory Committee