

LETTER OF COMMENT NO. 13

Terry Warfield
Department of Accounting and
Information Systems

4133C Grainger Hall 975 University Avenue Madison, Wisconsin 53706-1323 Telephone 608/262-1028 Fax 608/263-0477 e-mail: twarfield@bus.wisc.edu



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Ms. Teresa Polley Chief Operating Officer FAF 401 Merritt 7 Norwalk, CT 06856-5116

Re: FAF Governance Proposal

Dear Terri:

I am writing to provide comments on the FAF proposed changes in Oversight, Structure, and Operations of the FAF and FASB. By way of background, as you know, I currently serve on FASAC and I have participated in the FASB's due process in various roles over my career.

As a general comment, the FAF should be commended for undertaking a review of this nature, given the many challenges faced by the standards boards. In an environment characterized by concerns about international convergence and complexity and their potential impacts on the continued effectiveness of the standard-setting process, such reviews are necessary to ensure high quality financial reporting. Indeed, the draft Decision Memorandum of the Pozen Committee (CIFR – January 11, 2008) acknowledged and commended the FAF for its review and preliminary positions in its chapter on the standard-setting process.

I am in general agreement with the stated objectives for the proposed changes but I have some concerns about the basis for some of the recommendations. In brief, I do not believe that some of the "problems" to which the recommendations are directed are that severe. As a result, I think that any changes made should be undertaken with care so as not to negatively impact a standard-setting process that I think is working relatively well.

The focus of my comments is on the general FAF questions and those addressing the FASB.

1. Composition

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.

I agree with this recommendation. Although other individuals and groups do have the opportunity to submit nominations, further broadening the list of invited nominating groups is warranted and could serve to expand the constituencies served by the Board. Retaining final authority for appointments within the FAF is necessary to ensure the continued independence of the FAF and the FASB.

Terms of Trustees

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

This proposal seems reasonable and likely will allow the FAF to adjust membership in response to changing demands.

Size of the Board of Trustees

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

Establishment of a flexible size for the FAF has merit, given the rapidly changing environment facing the FAF. This is consistent with recent changes in the membership of the FASAC, in order to complement the existing Council with members possessing expertise or perspective needed to respond to emerging issues.

Governance and Oversight Activities

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

Although I am not knowledgeable of the specifics of existing FAF oversight of the standard-setting process, my perception is that this is done at both periodic reporting junctures and on an on-going basis. For example, a review of the quarterly FAF meeting agendas does contain a report by the FASB Chair and I suspect that the FAF has ongoing opportunities to monitor the progress of FASB projects. To the extent that these procedures are not sufficient for the FAF to provide input on FASB projects and standard-setting outcomes, a revision of those procedures has merit and is important to ensure FASB accountability to the FAF and to its broader constituencies.

2. FASB

Size of the FASB

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

I am not sure of the problem to which this proposal is being addressed. It is not clear to me at all that a seven member board has been ineffective either in terms of speed or quality of standard-setting outcomes. In fact, I suspect, and I think there is some evidence to support this suspicion, that the recent slowing of progress on a number of projects has been due to lack of agreement between the FASB and IASB with respect to projects that have international convergence implications.

Furthermore, reducing the size of the Board will no doubt result in an increased workload for the remaining Board members with the potential negative consequence of a slowing in the standard-setting process. Finally, shrinking the Board is inconsistent with the goal of expanding the range of perspectives brought to Board deliberations. While the current proposals of some groups (see CIFER report) seek to expand a user orientation on the Board, I don believe this should be accomplished at the expense of qualified and highly motivated Board members. These members may not have user credentials but nonetheless would (indeed should) support standard-setting outcomes that serve user interests (see discussion below on Board composition).

In sum, the case for the negative consequences of the current size of the FASB has not been made for me and the proposal to shrink the Board to five members does not come without risks.

FASB Voting Requirement

Proposed Action: Retain the FASB simple majority voting requirement.

For either a seven or five member board, and for the reasons stated in the Request for Comment, the simple majority voting requirement should be retained.

FASB Composition

Proposed Action: Realign the FASB composition.

As indicated in the Request for Comment: "In a potential move to a five-member FASB, the Trustees recommend that the composition should be changed." Does this suggest that there would be no change in composition, if the size is not reduced? I do not share the view that a Board member's ostensible affiliation necessarily translates into that Board member's perspective and position on various standard-setting positions. Of course, this is why all prior affiliations are severed and Board members are recruited with an eye towards the candidate's orientation and support of the Board's mission – a mission which is clearly driven by investor or user concerns. In addition, Board members who bring with them some experience in preparing

and auditing financial statements bring valuable practical perspectives to the Board's deliberations.

Thus, if the five-member board recommendation is embraced, it is important to have the proposed areas of experience: auditor, preparer, academic, and financial statement user. However, if a seven member board is retained, these core perspectives could be complemented through the use of two at-large, best-qualified members to bring desired additional perspectives to the board. I support no change to the member terms of a maximum of two five-year terms.

I also note that the CIFER Draft Memorandum in this area is silent on Board member affiliations. Some commentators have responded to this silence to recommend elimination of certain perspectives from the Board — specifically, the academic position. Such a change would be unfortunate, given the unique and I believe valued academic perspectives brought to the Board's process. Steve Zeff provides a good historical summary of the effective service of members of academe to standard-setting. According to Steve,

"... at least one academic has regularly been a member of the US, Canadian, UK, Australian, and New Zealand accounting standard setters since their origin, as well as on the IASB. The first chairman of the Accounting Standards Board of Japan (the country's first independent standard setter, set up in 2001), was an academic, and the Chief Accountant of the China Securities Regulatory Commission from 1997 to 2007, who is currently a full-time member of the IASB, was an academic with a doctorate. Karel Van Hulle, the head of the European Commission's unit, from 1990 to about two years ago, which deals with accounting and auditing norms throughout the European Union, is an academic. It is not widely known that Sir David Tweedie, the IASB chairman and former UK ASB chairman, began his career as an academic and holds a doctorate. Academic membership has obviously been seen as indispensable by those who oversee accounting standard setters around the world.

At the FASB, the series of academic members from 1973 to the present--Bob Sprouse, Bob Swieringa, Gerry Mueller, Katherine Schipper and, now, Tom Linsmeier--have been seen as important contributors to the board's work. A former academic, Todd Johnson, has served on the FASB's research staff for more than 20 years. I believe that the GASB has had an academic "seat." One of the most important Chief Accountants of the Securities and Exchange Commission, Sandy Burton (from 1972 to 1976), was a professor at Columbia University."

I would add that a former FASB member Art Wyatt and current member Mike Crooch, although not sitting in an academic "seat" have academic credentials.

To be consistent with my earlier arguments, allocating seats on the board should be dictated by how the identified perspectives contribute to achieving the Board's mission. In this regard, well trained academics bring to the process an objective and conceptual orientation to accounting problems, due to their academic training. Furthermore, many recently minted PhDs in accounting are trained in and have conducted behavioral-economic research addressing the very issues being deliberated by the Board, such as what are the attributes of accounting numbers that make them more or less useful in investing and credit decisions. Thus, an academic brings a unique perspective to the Board and in many cases, represents another user perspective.

Setting the FASB Technical Agenda

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

I do not have a strong view on this recommendation. If the Chair is now being held accountable for agenda decisions, but does not have control of that process, this recommendation could be a good approach to address that issue. My only concern here is that a Chair might use this authority to affect an expected outcome on a standard-setting issue on which the Chair had a minority view. I suspect that other mechanisms and procedures (e.g., enhanced FAF oversight of agenda decisions) could be implemented to address this concern.

Please call or email me with any questions on my comments.

Sincerely,

Terry Warfield, PhD

Associate Professor

Director, Arthur Andersen Center for Financial Reporting and Control