

31 March 2008

Ms. Nancy M. Morris
Federal Advisory Committee Management Officer
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File Number 265-24
Progress Report of the SEC Advisory Committee on Improvements to Financial Reporting

Dear Ms. Morris:

The CFA Institute Centre for Financial Market Integrity (CFA Institute Centre),¹ in consultation with its Corporate Disclosure Policy Council (CDPC)², appreciates the opportunity to comment on the Progress Report (PR) issued by the U.S. Securities and Exchange Commission (SEC or Commission) Advisory Committee on Improvements to Financial Reporting (CIFiR or Committee).

The CFA Institute Centre represents the views of its investment professional members, including portfolio managers, investment analysts, and advisors, worldwide. Central tenets of the CFA Institute Centre mission are to promote fair and transparent global capital markets, and to advocate for investor protections. An integral part of our efforts toward meeting those goals is ensuring that the quality of corporate financial reporting and disclosures provided to investors and other end users is of high quality. The CFA Institute Centre also develops, promulgates, and maintains guidelines encouraging the highest ethical standards for the global investment community through standards such as the *CFA Institute Code of Ethics and Standards of Professional Conduct*.

¹ The CFA Institute Centre for Financial Market Integrity is part of CFA Institute. With headquarters in Charlottesville, VA, and regional offices in New York, Hong Kong, and London, CFA Institute is a global, not-for-profit professional association of more than 94,000 investment analysts, portfolio managers, investment advisors, and other investment professionals in 133 countries, of whom nearly 82,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 135 member societies in 56 countries and territories.

² The objective of the CDPC is to foster the integrity of financial markets through its efforts to address issues affecting the quality of financial reporting and disclosure worldwide. The Council is comprised of investment professionals with extensive expertise and experience in the global capital markets, some of whom are also CFA Institute member volunteers. In this capacity, the Council provides the practitioners' perspective in the promotion of high-quality financial reporting and disclosures that meet the needs of investors.

Introduction

The work of the Committee highlights that complexity exists in many facets of the financial reporting process. Just as the members of the Committee represent different constituent groups—including preparers, auditors, and users of financial statements—each group is likely to have different opinions as to which areas of financial reporting are in greatest need of improvement. We appreciate the obvious care taken by the Committee to address the many areas of concern across all of the groups involved. As our mission focuses on promoting the highest quality financial reporting and disclosures in the investors’ interests, and given the Committee’s charter to “conduct its work with a view to enhancing financial reporting for the benefit of investors,”³, we suggest that there are areas of great importance to investors⁴ that the committee could investigate further.

While the proposals in the Progress Report certainly address changes to complexity for various groups, some recommendations may not improve financial reporting for investors. We discuss below the following areas we believe would have produced greater enhancements for investors:

- Improvements for Investors
- Mixed-attribute Issues
- Risk Management

We recognize the Committee’s challenges as it moves to bring forth effective recommendations that may be enacted in a short period of time. The Center for Audit Quality, in its November 2007 comment letter⁵ to Subcommittee I, discussed the task of addressing the “root causes of avoidable complexity with short-term recommendations.” As an organization with a long history of working for financial reporting improvements that benefit investors, we know that change often is neither fast nor easy.

Improvements for Investors

Meeting the Committee’s objectives to both increase the usefulness of financial reports for investors and reduce the complexity of the system for investors, companies and auditors represents a difficult undertaking. Increasing the usefulness of financial reporting requires improvements in timeliness, transparency, comparability, and consistency, and priority given to decision relevance. Achieving these results will require companies, auditors, and regulators to change their process and some of those groups will view such changes as a disproportionate

³ “The Committee should conduct its work with a view to enhancing financial reporting for the benefit of investors, with an understanding that unnecessary complexity in financial reporting can be harmful to investors by reducing transparency and increasing the cost of preparing and analyzing financial reports.” The full Committee Charter is available on the SEC website: <http://www.sec.gov/rules/other/2007/33-8817charter.pdf>

⁴ Investors, as noted in this comment letter, include providers of financial capital: both current and potential investors, creditors and other such providers.

⁵ The full comments of the Center for Audit Quality is available on the SEC website: <http://www.sec.gov/comments/265-24/26524-28.pdf>

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increase in complexity for them related to the benefit to investors. Finding the appropriate balance is a major challenge for the Committee.

The CFA Institute Centre adheres to the principle that financial reports are prepared for providers of risk capital in our July 2007 release “*A Comprehensive Business Reporting Model: Financial Reporting for Investors*”⁶ (CBRM). We proposed enhancements to the financial reporting process (Chapter 3) and changes to the current presentation of financial statements and additional disclosures (Chapter 4) that would benefit investors in their decision making process. The goal of financial reports should be to supply the information necessary so that both current and future investors may make properly informed capital allocation decisions.

Innovation and creativity have driven the nature of business activities away from the manufacturing model for which the current reporting framework was developed. Changes in business practice, combined with regulatory changes in response to various innovations, have led to the piecemeal and complex model of financial reporting in existence today. This model has facilitated abuse, further justifying the need for improvements in transparency (both measurement and disclosures).

The PR contains several proposals that we believe would advance the needs of investors. The call for more investor involvement during the development of future standards is an idea the CFA Institute Centre has long expressed. The Committee's recommendations for reducing accounting options and decreasing the reliance on “bright line” thresholds can be expected to positively impact the usefulness of reported information. We support the Committee’s efforts and encourage further development and analysis along similar paths.

We are concerned, however, that several of the recommendations in the PR will do little in the way of making positive changes for investors. Several of the proposals on standard setting, while intended to increase the effectiveness of the Financial Accounting Standards Board (FASB), may potentially slow the process of change. The proposals on materiality may disadvantage investors by increasing the number of undisclosed “immaterial” items. The judgment framework could benefit investors, but most likely only if the documentation of decisions is also provided to investors. We encourage the Committee to review its proposals to ensure that any initiatives undertaken will properly balance the goals of improving financial reporting for investors and reducing complexity for all parties.

Mixed-Attribute Issues

One of the drivers of complexity today is the mixed-attribute reporting model, which combines items reported at historical cost and measured at fair value in the same report. Such reports do not reflect the underlying business economics. Analysts who wish to estimate fair value for the historical cost items for their valuation models are often unable to do so due to inadequate disclosures. Companies, which presumably use fair values for their investment decisions, are in the best position to estimate the fair value of their assets and liabilities.

⁶ The CFA Institute Centre’s “*A Comprehensive Business Reporting Model: Financial Reporting for Investors*” is available on the CFA Institute Centre website: <http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2007.n6.4818>

In addition, the mixed attribute model may create artificial volatility in earnings for items exposed to the same market factor. Based on how companies classify their debt securities, the effects of changes in value of similar investments impact earnings in different periods. Also, the mixed attribute model has resulted in the development of optional hedge accounting practices. These issues further undermine comparability among entities and confound investors' abilities to discern the effects of and exposures to market price changes.

The CFA Institute Centre's CBRM has the underlying goal to move to a reporting model based on fair value measurements. Our recommended enhancements to the presentation of financial statements are intended to improve investors' abilities to value companies today, as well as to estimate their future cash generating capabilities. Our recommendations align nicely with the proposals of the joint FASB and International Accounting Standards Board (IASB) financial statement presentation project⁷. Two particularly significant benefits of the proposal are the cohesive alignment of information across all financial statements, and a reconciliation of cash and non-cash transactions between the cash flow and income statements. These changes reduce complexity for all users of the statements while providing increased transparency of the business operations. These changes provide benefits even under the current mixed-attribute model.

The transition from today's reporting model is undoubtedly going to require preparers to incur some expense. Frequently, the implementation of proposed—even adopted—changes may be delayed when companies object to the potential cost of adhering to new requirements. In just one of many examples, in an October 2007 letter to the FASB⁸ the Financial Executives Institute requested a further delay for SFAS No. 157, citing company infrastructure deficiencies. The new standard already had been issued, and the request was drafted just prior to the required implementation date. To continually allow companies to play “the cost card” when they may simply disagree with the new standard, perpetuates the deficiencies in the industry's current reporting model.

Risk Management

Increasing the transparency of the risks facing a company serves to decrease the complexity of financial reports for investors. Managers are charged with managing the risks associated with their companies' business plan, while protecting the company and investors from potentially adverse effects. In certain risk management strategies, risks are simply transferred from one market or counterparty to another. Increasing and enhancing the disclosures, including sensitivity analysis, is a necessary first step.

The Senior Supervisors Group (SSG), a consortium of global banking and securities regulators, released on 8 March 2008, *Observations on Risk Management Practices during the Recent*

⁷ Additional information on the Financial Statement Presentation project is available on the FASB website:
http://www.fasb.org/project/financial_statement_presentation.shtml

⁸ Request from Financial Executives Institute for a delay in implementing SFAS No. 157 – *Fair Value Measurements*:
<http://www.fasb.org/oc/AR-2007/51607.pdf>

Market Turbulence,⁹ a report that discusses the role risk management strategies have played in recent market fluctuations. Findings include:

- “Some firms retained exposures to obligations that exceeded the firm’s understanding of its risks, and failed to take steps to control those risks.
- Some firms did not understand the impact of the liquidity needs of their off-balance sheet vehicles.
- Firms avoiding these problems showed better firm-wide understanding of exposures and risk and possessed adaptive risk measurement systems.”¹⁰

Based on their findings, the SSG recognized the need for companies to strengthen their risk management practices and controls. They also saw the possible need for providing improved disclosures to both the financial markets and regulators, while addressing the uncertainty of potential losses, the exposure to off-balance sheet vehicles, and the need for better compensation practices.

On 13 March 2008, U.S. Treasury Secretary Henry Paulson, Jr. discussed recommendations from the President’s Working Group (PWG) on Financial Markets.¹¹ As did the SSG, the PWG’s recommendations address issues related to the recent market turmoil. Secretary Paulson commented that continued innovation in capital market transactions created excessive levels of complexity and impacted transparency and efficiency. The PWG provided the following list of objectives to manage complexity and understand risks:

- “One, stronger transparency and disclosure. The challenges of complexity were exacerbated by opacity. The best antidote to opacity is transparency and disclosure.
- Two, stronger risk awareness. Regulators and all market participants must be more aware of and better able to respond to risks. Credit rating agency practices must improve, and the users of their services must rely less on, and appreciate more the limitations of, ratings products.
- Three, stronger risk management. We need improved risk management practices by investors, issuers, financial institutions, rating agencies, and regulators alike. Risk management is everyone’s business.
- Four, stronger capital management. Well-capitalized institutions are better prepared to deal with challenges, foster economic growth and enhance market confidence.

⁹ This report is available on the Federal Reserve Bank of New York website as a member of the Senior Supervisors Group: http://www.newyorkfed.org/newsevents/news/banking/2008/SSG_Risk_Mgt_doc_final.pdf

¹⁰ Ibid

¹¹ The full press release is available on the Treasury Department website: <http://www.treas.gov/press/releases/hp872.htm>

- Five, stronger regulatory policies. Regulatory policies, including capital requirements, must address risk management weaknesses and improve the safety and soundness of our institutions and financial system.
- Six, stronger market infrastructure. Perhaps the best example of innovation is the over-the-counter (OTC) derivatives markets. These markets have grown tremendously; but the infrastructure has not kept up – and it must.”¹²

The CFA Institute CBRM, the PWG, and the SSG report all agree on the need to provide investors with the necessary level of disclosures. Unfortunately, the Committee focused little attention on the area of risk management in the first round of deliberations.

General Concerns

During our review of the Progress Report, several common themes emerged regarding the recommendations and discussions the Committee addressed. In many cases, our concern is not with the proposals themselves, but with the need for additional clarity to understand their intent and to ensure proper application. The body of this letter discusses these general topics and is followed by a discussion of the Committee’s individual developed proposals and conceptual approaches in specific instances.

Defining Investors

A common practice of regulators today is to view changes in the financial reporting process through the eyes of investors. This concept is rooted in the opening chapter of the FASB and IASB proposed conceptual framework for financial reporting, as follows:

The objective of general purpose external financial reporting, as clarified, is to provide financial information about the reporting entity that is useful to present and potential investors and creditors in making decisions in their capacity as capital providers. The objective should pertain to financial reporting as a whole, not just financial statements.¹³

Increasing the involvement of investors represented one of the major objectives of the Financial Accounting Foundation’s (FAF) recently adopted changes for both the FAF and the FASB. Much of the work they have undertaken in this area could benefit investors in the long run.

CIFiR began its work with the stated objective of increasing the usefulness of financial information for investors. In footnote 2 of the PR, the Committee briefly defines “investor” to include multiple classes of users of information, including creditors and rating agencies. The

¹² Ibid

¹³ The objectives of financial reporting are provided in the Summary of Decisions Reached to Date portion of the Conceptual Framework pages on the FASB website: http://www.fasb.org/project/cf_phase-a.shtml

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inclusion of rating agencies in the definition of investor deviates from our views. These organizations do not invest capital in the company and are also provided additional information (often non-public) when requested.

Additionally, we are concerned with qualifiers that are attached to the reference to investors in various recommendations and discussion throughout the PR. Some references are to investors as “current” or “serious retail.” These qualifiers are not defined and present wide latitude for interpretation. The CFA Institute Centre recommends CIFI develop and adopt a single definition for “investor” that is used consistently—and unqualified—throughout the report.

In our comment letter¹⁴ to the FAF on their proposed governance changes, we proposed a definition of investor. Key aspects of our definition include:

- Individuals who have achieved a level of professional competency through education, examination, and experience.
- Investors serving on regulatory bodies should be able to relate standard setting decisions to the usefulness of financial statement data.
- It would not include individuals that have ascended to corporate management (e.g. CEO) as they are more aligned with the views of preparers than investors.

Our proposal is intended to distinguish “investors” from “other users of financial reports.” (The full definition is provided as Appendix I.)

Fair Value

In the introduction to the PR, there is discussion of the causes of complexity and CIFI’s decision to focus on offering recommendations addressing items described as “avoidable complexity.” In Chapter 1 especially, comments regarding the application of fair value based accounting standards appear to place these standards into the “avoidable complexity” category. While the Committee discusses the potential lack of time to properly address fair value practices, it is considering some recommendations which could impede progress in this area.

In our CBRM, fair value information is considered the most relevant for making financial decisions. We also state that recognition should be determined by the relevance of the information and not based solely on the reliability of the measurement.¹⁵ In viewing fair value as a cause of complexity due to the possible difficulty in estimating fair values, the Committee understates the complexity of the current mixed attribute reporting model. Historical cost based accounting treatments, in areas such as depreciation, reserves, write-downs or impairments, use

¹⁴ CFA Institute Centre’s comment letter to the FAF on ‘Proposed Changes to Oversight, Structure and Operations of the FAF, FASB and GASB’: http://www.cfainstitute.org/centre/topics/comment/2008/pdf/faf_proposal_cl.pdf

¹⁵ Representing principles 3 and 4, these topics are further discussed on pages 8-10 of the CBRM: <http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2007.n6.4818>

management estimates and assumptions, resulting in complex calculations with highly subjective measurement and reported amounts.

The practitioner experience, as demonstrated by the beliefs of the global membership of CFA Institute, bears out our recommendations. In response to a CFA Institute survey in 2007 on the measurement of financial items, respondents placed high importance on additional explanation of the measurement bases used by companies. More than 70% of the respondents ranked the following information as being important or very important to their analysis of companies' financial reports:

- Key qualitative and quantitative assumptions—e.g., interest or discount rate—used to determine value (81% of 521 respondents)
- Description of the underlying method and policy for each measurement basis used (75% of 521 respondents)
- Description of changes in measurement bases from prior reported periods, including the reasons for the changes and the effect of making the changes (74% of 520 respondents)
- Timing of cash flows for contract-based assets or liabilities (71% of 522 respondents)

A majority of those respondents who provided comments agreed that having adequate disclosure was necessary to understand the impact of the fair value adjustments and the quality of the estimates/ assumptions used by management.

Another question in that same survey highlighted the fact that these disclosures apply even under today's mixed-attribute model. More than 50% of survey respondents adjusted or removed the following items while performing a valuation analysis of the company's income statement:

- Impairment of goodwill and other intangible assets (69% of 380 respondents)
- Amortization of intangible assets (56% of 385 respondents)
- Actuarial gains or losses in pension or other post-retirement benefits (56% of 346 respondents)
- Impairment of fixed assets (56% of 380 respondents)
- Unrealized gains and losses for equity securities held as investments (55% of 380 respondents)
- Unrealized gains and losses for debt securities held as investments (52% of 377 respondents)

While a transition to the use of fair value measurement remains our long-term goal, these results indicate disclosures that would benefit investors under the current reporting model. It is clear that complexity exists in reporting models that combine both fair value and historical cost measurements. The Committee's stance on fair value should be clarified, as the discussions and proposals could be interpreted as either, 1) CIFI is not making any recommendation on fair value, which we could understand, or, 2) CIFI is against promoting fair value, which we could not support.

Effectiveness and Efficiency of the Standard Setting Process

In the Committee's work on improving the standard setting process, we observed some potential inconsistencies. CIFI supported the governance changes proposed by the FAF, which were subsequently adopted. While the CFA Institute Centre supports the concepts of increased investor participation in the standard setting process, the adopted changes likely conflict with other recommendations, such as adding additional pre- and post-review of new standards. With fewer board members—even if the percentage of investor representatives increased—and more steps in the process, it is difficult to imagine how the process would be more efficient. Most likely, the level of improvement seen will depend on how the changes are implemented.

The proposal for the agenda advisory group may also hinder the development of a more efficient FASB. There currently exist several groups, such as the Financial Accounting Standards Advisory Council (FASAC) and the Investors Technical Advisory Committee (ITAC), that provide input to the FASB. It is unclear as to whether this new group would replace some of the current process or represent another layer to the process. While we share concern over the agenda development process for FASB, the need for another advisory group should be clarified by the Committee.

Transparency

An effective way to address complexity is through improved transparency. The Committee provides examples of additional disclosures with detail in Chapter 1, which we agree could improve the usefulness of financial statements. The Committee also addresses the importance of minimizing the cost to companies by ensuring that new disclosures are beneficial and relevant to investors.

Yet, in establishing its proposals, the Committee appears to have strayed from the goal of improving transparency in some respects. This deviation appears in particular when professional judgment increasingly becomes integrated into the reporting process. We share the long-term goals of establishing a codified resource of accounting literature. This might include a single body authorized to issue and interpret standards, and a move toward a more principles-based approach to standard setting. Each of these modifications creates situations in which well formed professional judgment is required. To benefit investors and increase transparency, parties exercising their professional judgment as part of the financial reporting process should provide company specific disclosures supporting their decisions. The Committee discussed the need to document the process, but did not express the goal of having this information provided to investors.

Overall

The Committee's work addresses several needed changes to the financial reporting process. The changes may have positive implications for several constituent groups or may require a trade-off between them. As the Committee finalizes its report, we hope our comments assist in, at minimum, balancing the recommendations for, or preferably, tipping the scale in favor of investors.

Specific Proposals

Developed Proposal 1.1

The intent of this proposal is in alignment with the CBRM principle of reporting items based on their nature rather than the function for which they are used. We fully support the move toward a single measurement standard for the reporting of similar items and activities. This concept is further supported by the findings of a CFA Institute member survey completed in 2007¹⁶. Survey respondents placed the mean level of importance at 4.5 and 4.3 out of 5 for the attributes of consistency and comparability. This proposal potentially creates information which meets the expectations of investors.

We have some concern as the proposal and discussion does not clearly define "business activity." Some readers understand this proposal to mean that the accounting for a transaction would be the same regardless of the industry in which the firm operates. Others believe that the accounting treatment could be affected by management intent. We believe that the first interpretation is more consistent with the remainder of the PR and urge the Committee to clarify this section. Investors need confidence that a loan to an outside party would be measured and disclosed consistently regardless of the industry focus of the company.

The benefits of the completed FASB codification are many. The Committee's recommendation to use this resource to address the current literature on industry-specific guidance is just one example.

Developed Proposal 1.2

We support the Committee recommendation that future standards eliminate accounting alternatives and believe this especially applies to differences solely based on the intent of management. In another CFA Institute survey in 2007, 72% of 531 respondents indicated that companies should not have accounting options for measuring and recognizing similar assets or liabilities. This response is one of the strongest preferences noted in the survey. A common refrain from those respondents providing elaborative comments is that accounting options make it difficult to compare companies that have similar items—assets and liabilities. As a result, the

¹⁶ As part of the 2007 XBRL Survey, respondents were asked to indicate the importance of a set of data attributes. All of the attributes obtained a mean score of 4.3 or higher on a 5 point scale.

[http://www.cfainstitute.org/centre/topics/reporting/pdf/xbrl_survey_report .pdf](http://www.cfainstitute.org/centre/topics/reporting/pdf/xbrl_survey_report.pdf)

lack of comparability increases “agency costs” and creates unnecessary complexity and inefficiency in analyzing and evaluating a company’s information. Several respondents expressed concern about managers being able to manipulate or “cherry pick” options to arrive at the best result for financial reporting.

Conceptual Approach 1.A

We encourage the Committee to continue advancing its work and analysis on removing bright line measures that form the basis for reporting actions. As the PR describes, the use of such measures allows companies to achieve different reporting results for similar transactions. As Investors prefer that companies provide disclosures that allow for a clear understanding of reported values and the associated risks.

CFA Institute surveys conducted in 1999, 2003, and 2007 consistently highlight the importance of company disclosures to investment professionals.

2007 Corporate Disclosure Survey

Comparative Analysis of Results to Prior Surveys

Please rate the following items from 1 to 5, indicating: the level of importance to your analysis and comparison of financial statements of companies that report in accordance with different sets of GAAP	Importance		
	2007	2003	1999
Off-balance-sheet assets and liabilities (e.g., operating leases, securitized assets, etc.)	4.3	4.5	4.2
Derivatives and hedging activities	3.9	4.0	3.6
Fair value (current or market valuations) of assets and liabilities on the balance sheet	4.0	4.0	
Extraordinary, unusual, or non-recurring charges (e.g., restructuring or discontinued operations)	4.3	4.3	4.5

When comparing the difference between the quality of information provided and the assigned importance of the disclosures, the respondents indicated the above as areas where improved disclosures would benefit users. These areas are examples of financial reporting where companies use bright line or optional accounting practices in determining the reported values.

The notion of moving toward proportionate recognition is viewed positively. We have indicated to the FASB that we support its application to lease accounting.

Conceptual Approach 1.B

The CFA Institute Centre strongly supports the call for additional educational efforts. The nature of the education described should further align the views of all participants with those of many investors today. We believe that one of the barriers to effective financial reporting is that many preparers and auditors do not understand how financial statements are used to make investment decisions. We encourage the Committee to consider expanding listed groups to include regulators, for this same reason. As with the goal of increasing the number of investors involved in the standard setting process, increasing every participant's understanding of the economic aspects of transactions may also benefit the financial reporting process.

Mixed Attribute Model and the Appropriate Use of Fair Value

As mentioned earlier in this letter, we disagree with many of the assertions in the discussions supporting this group of conceptual approaches. We believe the PR places fair value measurements in an overly negative light. As one of the organizations supporting the move to fair value—as supported by our members' survey results—we recommend that the Committee attempt to take a more neutral approach as it establishes its final recommendations.

Also as mentioned earlier, we believe that the mixed attribute model is the source of avoidable complexity. For example, the complexity attributed to SFAS Nos. 159 and 115 relates to the presence of accounting alternatives. When combined with different accounting options, historical cost and fair value measurements create artificial volatility in earnings as the impact of similar factors pass through income in different periods. A move to fair value for these items removes the differences in practice for reporting comparable items. Since businesses most likely use some estimate of fair value to enter into transactions, they should be capable of reporting to investors the economic justification for their decisions. The mixed attribute model undermines comparability among companies and confounds investors' abilities to discern the effects of and exposures to market price changes.

Footnote 40 on page 28 of the PR glosses over the uncertainties associated with historical cost reporting. Most, if not all, values reported by companies incorporate some assumption or estimate. For example, the calculation of depreciation expense requires companies to choose among different methods, as well as to estimate the useful life of the asset and any salvage value. While the actual price paid is potentially verifiable in an audit, the ongoing carrying value represents the reduced value based on these estimates. An additional factor is the requirement that assets be reviewed for possible impairment. This process seems quite similar to a fair value adjustment but is only allowed to decrease the carrying value of the asset.

Following are two statements from the PR (pages 29 – 30) that we believe are biased and unsubstantiated:

But under a full fair value approach, some objectivity would be sacrificed because many amounts that would change to fair value are currently reported on a more verifiable basis, such as historic cost.

Investors may not understand the uncertainty associated with fair value measurements (i.e., that they are merely estimates and in many instances lack precision), including the quality of unrealized gains and losses in earnings that arise from changes in fair value.

We recommend that the Committee support the FASB's recent decisions to adopt standards that require fair value measurements. The use of fair values in identified areas, such as financial assets and financial liabilities, reduces avoidable complexity by only having a single requirement. This also allows preparers and auditors to increase their knowledge and comfort with fair value measurements and disclosures.

Conceptual Approach 1.C

We support the Committee's endorsement of the work under way concerning the joint FASB/IASB conceptual framework. Our CBRM states that an accounting framework serves as the benchmark for judging standards and as a guide for the standard setters in their deliberations. The current frameworks in use by major financial reporting standard setters are believed by many to be in need of updating and refinement. The primary objectives¹⁷ of the joint FASB/IASB project align with our beliefs in the purpose of a conceptual framework.

Conceptual Approach 1.D

We do not support any language that could be interpreted as a recommendation to slow or impede the implementation of fair value reporting. The results of our 2007 survey indicate that 58%¹⁸ of 549 respondents prefer that all financial assets and financial liabilities be measured at fair value with the accompanying historical cost and assumptions provided in the disclosure notes. This view is reinforced by the high level of analytic importance placed on both fair value and derivatives and hedging activities in response to our corporate disclosure surveys.

2007 Corporate Disclosure Survey

Comparative Analysis of Results to Prior Surveys

Please rate the following items from 1 to 5, indicating: the level of importance to your analysis and comparison of financial statements of companies that report in accordance with different sets of GAAP	Importance		
	2007	2003	1999
Derivatives and hedging activities	3.9	4.0	3.6
Fair value (current or market valuations) of assets and liabilities on the balance sheet	4.0	4.0	

¹⁷ Full details of the Conceptual Framework Project is available on the FASB website:

http://www.fasb.org/project/conceptual_framework.shtml

¹⁸ 41% chose all assets and liabilities at fair value (financial assets and financial liabilities are a sub-group of all assets and liabilities) and 17% chose only financial assets and financial liabilities at fair value.

Conceptual Approach 1.E

We agree with the Committee support for the joint FASB/IASB project on improving financial statement presentation. In January of this year, we submitted comments¹⁹ to the FASB on this topic while highlighting the benefits of a matrix format for financial presentations, the presentation of data by nature, and the impact of a cohesive presentation across all statements.

Conceptual Approach 1.F

As discussed earlier, increasing the transparency of reporting reduces avoidable complexity. We support the potential areas being considered and reiterate our view that such disclosures increase the understanding of both fair value and non-fair value measurements.

Conceptual Approach 1.G

We support the topics under consideration by the Committee. Many of the changes were previously recommended to the FASB in the SEC's "*Report and Recommendations Pursuant to Section 401(x) of the Sarbanes-Oxley Act of 2002 On Arrangements with Off-Balance Sheet Implications, Special Purpose Entities, and Transparency of Filings by Issuers.*"²⁰ Many of the key initiatives of the report deal with improving transparency and reducing complexity. It also stated that

More useful and consistent disclosure requirements could be achieved **if a framework were developed that clearly and concisely set forth the objectives and limitations of the notes to the financial statements.** In addition, the Staff hopes to work with the FASB, users, preparers, and others to improve disclosures for financial instruments, so that information is organized, streamlined, and provides adequate specificity and detail, without overburdening preparers and auditors.²¹ [Emphasis added]

FASB's ITAC voiced its recommendation for a new project dealing with a framework for disclosure in a December 2007 comment letter.²² This further promotes the concept that financial reporting is improved by replacing the current piecemeal approach of adding requirements for each new standard.

¹⁹ CFA Institute Centre's comment letter on the IASB-FASB Joint Project on Financial Statement Presentation: http://www.cfainstitute.org/centre/topics/comment/2008/pdf/support_fsp.pdf

²⁰ The full report is available on the SEC website: <http://www.sec.gov/news/studies/soxoffbalancerpt.pdf>

²¹ Ibid page 5

²² Comment letter to FASB from ITAC concerning a disclosure framework: http://www.fasb.org/investors_technical_advisory_committee/ITACDisclosureProposal.pdf

Developed Proposal 2.1

We support the notion that financial reporting is intended to serve providers of risk capital. This concept is the first listed objective in the FASB conceptual framework.²³ We support all efforts to involve investors in the standard setting process both through direct representation and in consultation. The CFA Institute Centre reiterated this message in its comments to the FAF concerning their proposals.²⁴

As previously described, we encourage the Committee to develop and adopt a single definition for the term “investor.” We agree that different groups within the investment community have different perspectives of—and needs from—financial reporting. We believe that the Committee should focus on investors, with a single, yet broad definition to reduce confusion in the standard setting process.

Developed Proposal 2.2

The FAF adopted their proposed changes subsequent to the release of the PR, and without the minor modifications offered by CIFIIR. Our previously mentioned comment letters did not support some of the changes and we would encourage the FAF to monitor the effectiveness of the changes adopted. Remembering the underlying goal of increased investor representation, the process of implementing changes—and long-term improvements to communications with investors—will be the best gauge as to the appropriateness of any changes made.

For the purpose of monitoring and improved communications, we support the Committee’s recommendation for performance metrics and objective updates. Combined, these initiatives will help establish clear expectations for the operations of the FASB. With the resultant increased transparency, investors and preparers will better understand the steps necessary to properly interact with the regulator. We encourage the Committee to expand their recommendations and include the FAF and other regulatory organizations in the reporting process.

Developed Proposal 2.3

Several aspects of this proposal contributed to our general concerns about the Progress Report. It is difficult to understand how the addition of the Agenda Advisory Group (AAG) and additional layers of pre- and post-test of accounting standards would increase efficiency and nimbleness to the standard setting process. With the reduction of the FASB membership, from 7 to 5 representatives, the possibility of improvements further diminishes.

We encourage the Committee to clarify its view of the composition and role of the AAG. Specifically, will the AAG represent another layer of review above the current FASB advisory

²³ The objectives of financial reporting are provided in the Summary of Decisions Reached to Date portion of the Conceptual Framework pages on the FASB website: http://www.fasb.org/project/cf_phase-a.shtml

²⁴ CFA Institute Centre’s comment letter to the FAF on ‘Proposed Changes to Oversight, Structure, and Operations of the FAF, FASB and GASB’: http://www.cfainstitute.org/centre/topics/comment/2008/pdf/faf_proposal_cl.pdf

committees such as the FASAC and ITAC? It appears the proposed new group would serve much of the same role as outlined for the FASAC. From the FASAC mission overview:

The primary function of FASAC is to advise the Board on issues related to projects on the Board's agenda, possible new agenda items, project priorities, procedural matters that may require the attention of the FASB, and other matters as requested by the chairman of the FASB. FASAC meetings provide the Board with an opportunity to obtain and discuss the views of a very diverse group of individuals from varied business and professional backgrounds.²⁵

Under the proposal, would the FASAC still provide feedback to the Board, in addition to the AAG, or would the FASAC be dissolved? We suggest the Committee review the current suite of advisory groups in determining the role of the AAG. One suggestion to consider is to appoint a representative of each advisory group to the AAG. Without additional clarity, we would not support the development of another advisory group for the FASB.

The proposed investor pre-review also needs further clarification. For example, we are puzzled by the reference to "a serious retail investor" in the second bullet point at the top of page 40. There is no definition of serious retail investor provided and we are doubtful that an operational definition would be possible. While we strongly support the concept of investor input in standard setting, we believe such input is best provided as the standard setter considers accounting and disclosure provisions.

We are troubled by the implication that the costs to be considered are the costs incurred to implement a standard and that those are borne by preparers. Clearly we are seeing in the markets today the costs of failure to provide relevant information about various risk exposures. The costs of inadequate transparency are being borne by a vast, global and diverse group of constituents. The CFA Institute Centre included this overview of the cost benefit discussion in a 2006 comment letter to the FASB and IASB:

We believe, and thus agree with the Boards' view, that the benefits of financial reporting should exceed the cost to produce it. Since shareowners both receive the benefits *and bear the costs associated with generating this information*, the cost-benefit analysis should be done within the context of the framework's objective to provide decision-useful information.²⁶

We are supportive of the periodic assessment of existing standards. However, we do not believe that the FASB or other appropriate body should be precluded from issuing interpretive guidance

²⁵ Additional information on the FASAC is provided on the FASB website: <http://www.fasb.org/fasac/>

²⁶ 2006 CFA Institute Centre comment letter to the FASB and IASB on Preliminary Views—Conceptual Framework for Financial Reporting: http://www.cfainstitute.org/centre/topics/comment/2006/pdf/conceptual_framework.pdf

as necessary during the initial implementation period of a new accounting standard. If divergent implementation practices developed investors would face additional situations where the results between companies would lack comparability.

In combining all the recommendations within this proposal, we encourage the Committee to keep in mind the possible delays to the standard setting process. Investors not only bear the actual cost of implementing new standards as it impacts earnings and valuations, but they also bear the cost and the risks associated with insufficient disclosures. If the proposed changes are meant to solve an issue with current reporting, the cost of a delay could greatly exceed the cost of implementation.

Developed Proposal 2.4 and Conceptual Approach 2.A

We support the Committee's proposal regarding the consolidation of U.S. GAAP requirements with the FASB Codification project. With the completion of the codification, it becomes easier to identify areas of difference from International Financial Reporting Standards (IFRS). In execution of these changes, all parties should avoid two unintended consequences: (1) a decrease in the communication flow between the SEC and preparers; and (2) the loss of useful disclosures if certain items do not end up incorporated into the codification.

The SEC plays a vital role in the financial reporting process, including enforcement of a consistent application of GAAP requirements, and identification of areas within the standards that require updates. As each organization's role is clarified, it is essential that the importance of their respective contributions not be minimized.

The work completed in the codification identified some instances where secondary interpretative guidance might differ from that which the formal requirements recommend. Correcting these shifts and preventing future deviations will assist in the comparability of information between companies. In areas where the authoritative literature is silent regarding disclosures, the SEC and other regulators can play a pivotal role in producing the disclosures necessary for investors.

Conceptual Approach 2.B

We support the Committee's stance on the move toward principles- or objective-orientated-based accounting standards. We do question the single study referenced in the discussion and the possible lack of investor input. Since the study is being conducted by the world's six largest audit networks, does the consensus being developed accurately portray the different needs and requirements between users of the financial report—investors and regulators—and the preparers—companies and auditors? The PR references several statements and reports by regulators on the importance of moving toward more principles-based standards.

Conceptual Approach 2.C

We support the Committee's recommendations on the longer-term projects for financial reporting. We are interested in seeing the forthcoming international convergence related

recommendations. Given the comments by Robert Herz, FASB Chairman, in testimony to the U.S. Senate subcommittee on Securities, Insurance and Investment Committee on Banking, Housing, and Urban Affairs,²⁷ calling for all stakeholders to develop a blueprint of conversion, the plan for a move to IFRS is necessary to determine which additional projects might appropriately be added to the agenda.

The CFA Institute Centre has long advocated for a single global set of accounting standards. This view has been repeated in our recent comment letters and is confirmed by our membership's call for such convergence. For example, in 2007, as part of our survey on XBRL, we asked respondents to rank the importance of the global convergence of XBRL taxonomies.²⁸ Even for this emerging technology, 68% of the 264 respondents indicated an importance rank of either 4 or 5 on our five point scale.²⁹ The significance of a single global reporting process increases as both the accounting standards and delivery platforms converge.

Restatements and Materiality

As a group, the developed proposals in Chapter 3 address the topic of materiality and its impact on required restatements of companies' prior financial periods. Since every accounting standard includes the statement that provisions of the standard need not apply to immaterial items, the importance of a proper definition of materiality is essential to a properly functioning financial reporting system.

In meetings with the SEC and FASB, the CFA Institute Centre reiterated its support for the various standards and staff updates concerning materiality and restatements. In a 2006 letter to the FASB, we offered our support for SFAS No. 154:

We agree with the FAS 154 position that retrospective application is appropriate in all cases of changes in financial reporting principles. These changes cause discontinuity in the reported information by affecting its consistency and comparability over time and thus, users' ability to assess changes in trends and their economic cause. Companies, unlike users, have access to information needed to evaluate and determine the effects from changes in accounting principles and policies. Thus, we believe that companies should make the necessary adjustments to amounts reported in prior periods to reflect the effect from such changes. Otherwise, investors and other users will have to engage in a "guessing game" with the resulting negative effect on the quality of information available to the capital markets.

²⁷ Statements by Robert H. Herz, Chairman, FASB before the subcommittee on Securities, Insurance and Investment Committee on Banking, Housing, and Urban Affairs United States Senate 24 October 2007:
http://www.fasb.org/testimony/10-24-07_prepared_statement.pdf

²⁸ Survey results and analysis are available on the CFA Institute Center website:
[http://www.cfainstitute.org/centre/topics/reporting/pdf/xbrl_survey_report .pdf](http://www.cfainstitute.org/centre/topics/reporting/pdf/xbrl_survey_report.pdf)

²⁹ To reach Question 16 of the survey, the respondent had to indicate a minimal knowledge of XBRL. The 68% is broken down as 40% selecting 5 and 28% selecting 4. After factoring in the responses for 1-3, the mean score for this question was 3.9.

These comments reinforce the CBRM principles that investor information requirements must determine the materiality threshold. As discussed previously, a broad definition of investor should be based on education and experience and not be further qualified.

Developed Proposal 3.1

We support the Committee's recommendation that materiality is based on the perception of investors and the total mix of information available. Also, on-going educational and training sessions for all participants is an integral part of an informed and successful financial reporting process. However we disagree with the fundamental concept that anyone other than the investor should determine whether a quantitatively material item is relevant to the analysis of financial performance, position, and expectations.

This is concept put forth with the sliding scale of materiality. Fundamentally, we do not understand how a quantitatively large error could be immaterial due to qualitative factors. The list of possible factors at the top of page 57 of the PR contradicts the intention of materiality factors addressed in *SEC Staff Accounting Bulletin: No. 99—Materiality* (SAB 99). Despite language to the contrary, the PR in fact suggests that any one qualitative factor could make an item immaterial. We believe that SAB 99 provides sound guidance to preparers and auditors, and that it is better to err on the side of providing too much disclosure rather than too little. We note that investors use a variety of investment approaches and models, so attempting to determine if certain changes might alter certain approaches could be problematic. Indeed, the nature of one-time errors could significantly change the performance trends of a company. Until the investor obtains updated information, the measurement of perceptions is purely hypothetical. Finally, measurement precision should not be grounds for or against requiring a restatement. An item's measurement should accurately reflect the known information at the time reported.

Developed Proposal 3.2

There is a tension between the cost of restating prior period financial statements and the potential value it brings to investors. Given the need for comparable information in making informed investment decisions, investors rely upon companies to ensure that the required level of prior period information is provided. Restatement assists investors who rely on external databases for information and those working from published financial statements.

Investors also use many of the individual revenue and expense items, not just net income, in forecasting future company cash flows. As such, companies should be required to correct prior financial periods for material changes in these items even if the impact to net income is deemed immaterial. In viewing the entire mix of information available, investors recognize net income and other aggregate values as the starting points for the valuation process, so companies should not use them as the end point for assessing materiality or restatement needs.

We ask the Committee to define the scope of time referenced by “filed in the near future.” The subjectivity of that statement could lead to very different application between companies. This issue is further clouded by the various venues companies use to release information: required filings, press releases, their website, etc. In referencing future reports, does the recommendation only apply to required filings (10Q/K) or any release by the company?

We agree with the need for an improved flow of information during the period between when an error is identified and the restatements are completed. U.S. companies typically provide a greater number of updated periods for a restatement than do firms in other countries. A possible enhancement would be to create two steps to reach the number of periods currently updated through a restatement. The initial step would apply to the most recent annual and subsequent interim filings. The second step, with a defined timeline, would apply to all earlier periods impacted by the cause of the restatement. This would allow for the earlier release of current information to investors.

Developed Proposal 3.3

We support the Committee’s recommendation to view interim periods as independently reported financial periods.

Developed Proposal 3.4

We believe that the business judgment framework articulated by the Committee exists in substance in practice today. We believe that improvement to that model can be achieved and would support its further development. However, as we discuss later we believe that this is more appropriately undertaken by the FASB. A key aspect of our support is that investors believe that management needs to discuss and disclose the basis for their decisions. Professional judgment is integrated into today’s financial reporting process and will only increase as standards become more principles-based. The investor’s ability to forecast is improved when companies provide sufficient disclosures regarding their assumptions and judgments.³⁰

Survey results have confirmed that investment professionals find the areas of financial reporting that allow for professional judgments by management to be important to the valuation process. Respondents remarked that these areas could further benefit from additional disclosures.

³⁰ Additional discussion on disclosures and judgment is found on pages 42-44 of the CBRM:
<http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2007.n6.4818>

2007 Corporate Disclosure Survey
Comparative Analysis of Results to Prior Surveys

Please rate the following items from 1 to 5, indicating: the level of importance to your analysis and comparison of financial statements of companies that report in accordance with different sets of GAAP	Importance		
	2007	2003	1999
Off-balance-sheet assets and liabilities (e.g., operating leases, securitized assets, etc.)	4.3	4.5	4.2
Non-financial information (e.g., information about business model, key value drivers, key customers and vendors)	4.2	4.0	3.9
Derivatives and hedging activities	3.9	4.0	3.6
Fair value (current or market valuations) of assets and liabilities on the balance sheet	4.0	4.0	
Risks and exposure to risks (e.g., business, financial and market risk factors)	4.1	4.1	3.9
Accounting estimates and reserves, including key assumptions and sensitivity analyses	4.1	4.0	3.9

These items require some application of judgment by management. Investors would have a better understanding of operations directly from management if this framework were used for making decisions and then investors were provided with an explanation of the choices management made.

A recent questionnaire of the CFA Institute membership in the CEO's monthly newsletter³¹ asked whether or not members have any desire for additional disclosures from a company's auditor. The follow-up question of those responding "yes" sought their ranking of the importance of having the auditor discuss or describe certain areas of special interest in their findings. Respondents ranked importance of the following areas on a scale of 1 to 5, with a 5 indicating "very important."

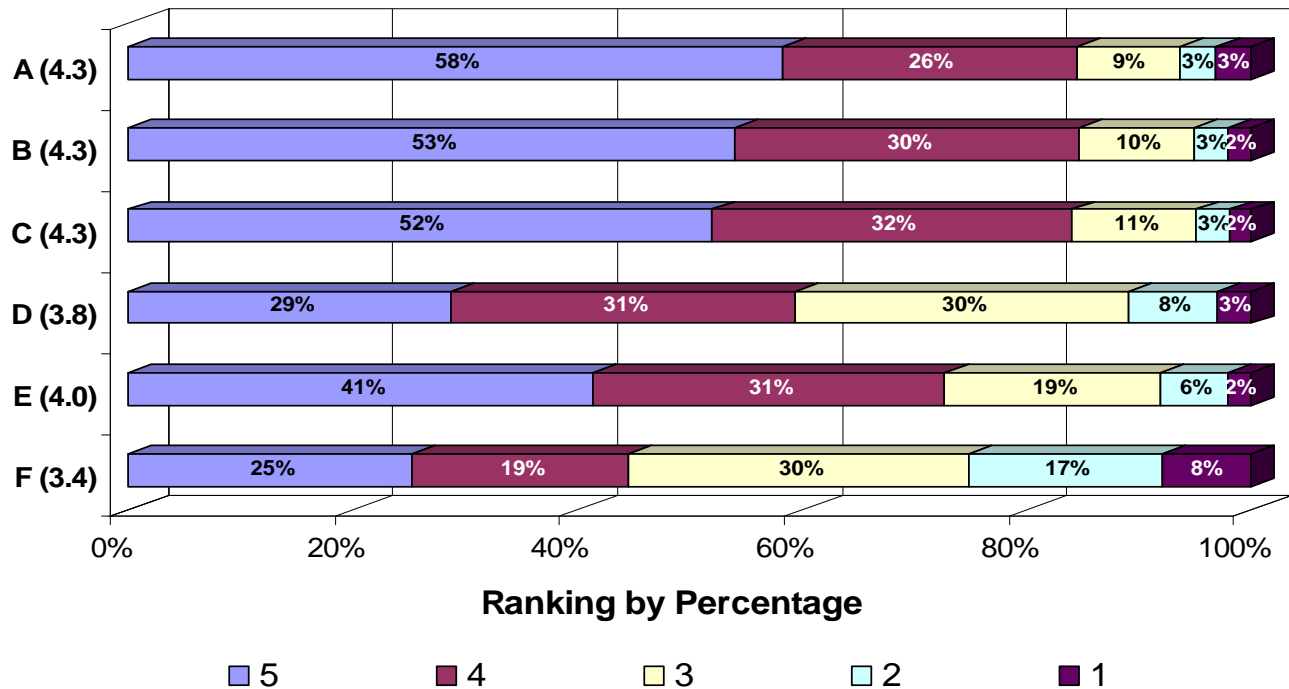
- A. Key risk areas identified as part of the risk evaluation of a company's business model.
- B. Significant changes in risk exposures affecting the audit procedures and/or ability to exercise professional judgment
- C. Reported amounts, or changes in amounts, that have a high degree of uncertainty in measurement, that involve significant assumptions subject to change, or otherwise require a higher level of professional judgment.

³¹ 80% of respondents indicated 'yes' to the question on additional auditor disclosures. The full results of the survey are available on the CFA Institute website: <http://www.cfainstitute.org/memresources/monthlyquestion/2008/february.html>

- D. Assessment of materiality, i.e., the threshold for determining the recognition and disclosure of information in the financial statements
- E. Changes in accounting principles affecting the consistency of reported amounts
- F. Disclosure about the auditors' tenure (e.g., years auditing the company) and other non-audit services provided during the period covered by the auditors' report.

A better understanding of how an auditor addressed each of these areas would increase investors' understanding of the information provided. To be most useful, additional discussion provided by the auditor should be company-specific rather than mere "boilerplate disclosure." The following table displays the response to our CEO's second question, and the importance CFA Institute members place on certain specific areas of interest for auditor disclosures.

Results to Question 2



We question the need for the judgment framework to be developed by the SEC and PCAOB given the work underway to reduce the number of organizations offering guidance on the financial reporting process. We believe the Committee should recommend that the FASB develop the framework for applying their standards.

We would oppose any type of safe harbor, as mentioned in the PR. We believe that the challenges discussed in this section of the PR are best resolved by understandable, plain-language disclosures by the company.

Also, we believe that financial reporting must be of the highest quality, and that lower complexity is a secondary objective. Simplified financial reporting that fails to completely reflect business economics provides questionable benefits. The Committee expresses concern over the length of time necessary to require accounting to show the true economic substance of transactions – the “high road” according to the PR. We encourage the Committee to support the adoption of improved reporting principles that correct inherent weaknesses in today’s standards.

It is essential that any business judgment framework include as a component the disclosure of those judgments in a manner that serves the needs of investors. We encourage the Committee to clarify its expectations for the documentation process and explain how that information would be provided to the investment community. We envision the development of an auditor’s version of a discussion section similar to the MD&A. This would allow investors to better associate the areas of business opportunity described by management and the potential risk of these same areas as viewed by the auditor. Hopefully, this alignment would minimize companies’ concerns about the distribution of proprietary information. We would be eager to assist in the development of those disclosures.

Developed Proposal 4.1

We are extremely encouraged by the move to a full mandate for XBRL-tagged financial information. Admittedly, awareness of this emerging technology is limited, but it is increasing and the potential benefits XBRL offers all participants in the reporting process have been touted for some time. The steps outlined prove that XBRL-tagged reports can allow a variety of companies the flexibility required to accurately complete the SEC filings. As such, we encourage the SEC to move as quickly as practical, even if faster than the Committee’s recommendation, with its mandate.

We support the concept of advancing the use of XBRL tags through different phases. We have a few recommendations for the Committee and the SEC to consider as they develop the path to a full mandate. First, we believe the Committee should recommend that the SEC clarify the scope of their end goal to ensure that the correct steps are taken to reach that goal. The Committee’s recommendations support the mandated use of XBRL, but only address the face of the financial statements and disclosures notes. To be most useful to investors, a single XBRL-based filing will need to include the narrative portions and discrete values provided in today’s filings. The process of how companies complete their filings may differ, but the requirements of the XBRL-tagged filings need to be established. We believe companies will receive greater benefits, in a cost effective manner, through the integration of XBRL earlier in their reporting process than available from the current “bolt-on” process.

Second, the phases mentioned only address the addition of more companies using XBRL tagging. We encourage the Committee (or the SEC) to address phasing in the process of moving beyond the block tagging of note disclosures as well. The initial move could be to phase in tagging disclosures as defined in the standards, such as the pension and income tax disclosures. This would allow companies to increase their tagging each period without potentially requiring company-specific extensions. The tagging of disclosures is one of the greatest expected benefits for investors, as it would facilitate access to information that is very time consuming to extract manually and is not readily available from third-party data vendors.

Finally, as the adoption process continues, additional issues may be addressed, such as the impact of XBRL tagging on the assurance process. By establishing a clear long-term target for XBRL-tagged reports, companies and auditors will be better able to evaluate how XBRL impacts their process and procedures. The current system of producing XBRL reports separate from another filed version creates a level of uncertainty as to the demands of the auditor. As investors, we believe that the benefits from a move to XBRL reporting should outweigh the possible negatives—both for investors and companies.

The CFA Institute Centre, through its established XBRL Working Group, developed a document of guiding principles expected to benefit investors as regulators adopt XBRL reporting frameworks. Those principles follow.

1. Core taxonomy (or structure of tagging elements) should be predefined by current financial reporting standards, including generally accepted accounting principles and other regulatory disclosure and reporting requirements.
2. Taxonomy extensibility should maintain the level of data comparability as defined by GAAP and other regulatory requirements.
3. Ultimately, companies should deliver required financial reports to regulators using the established XBRL framework.
4. The general public should have equal access to the XBRL-tagged information.
5. Regulators should develop the necessary infrastructure and protocol to ensure the timely updating of the established XBRL framework as outlined in the preceding four key principles.

The current SEC project is addressing many of these principles and the Committee's recommendations further enhance the process. (Appendix II to this letter provides further elaboration on each of these principles.)

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31 March 2008
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Developed Proposal 4.2

We support the Committee's recommendation on advancing the level of use and information delivered through company websites. As capital markets continue to evolve into a single global marketplace, access to quality information is essential. There is an area of the proposal we encourage the Committee to clarify.

The proposal indicates that industry participants should coordinate on the creation of a uniform best practice guide. We recommend that the Committee elaborate on the types of organization included as "industry participants." As investors are the most likely beneficiaries of enhanced web-based disclosures, their involvement in the development process is important to its success, and we hope as such there would be strong investor representation on any group of "industry participants."

Conclusion

We support the Committee's efforts to improve financial reporting. We hope the final Committee proposals meet its objective of enhancing financial reporting for the benefit of investors.

We appreciate the opportunity to provide comments to the Commission, its staff, and CIFI members regarding the Progress Report. If any party should have questions or seek further elaboration of our views, please contact Glenn Doggett, CFA, by phone at 434.951.5278 or by e-mail at glenn.doggett@cfainstitute.org.

Sincerely,

/s/Kurt N. Schacht

Kurt N. Schacht, CFA
Managing Director

/s/ Gerald I. White

Gerald I. White, CFA
Chair, Corporate Disclosure Policy Council

cc: Corporate Disclosure Policy Council
Jeffrey D. Diermeier, CFA, President and CEO, CFA Institute
Ray DeAngelo, Managing Director, Member and Society Division, CFA Institute
Scott C. Evans, Executive Vice President, Asset Management, TIAA-CREF
Gregory J. Jonas, Managing Director, Moody's Investors Service
William H. Mann, III, Senior Analyst, The Motley Fool

Appendix I

Definition of Investor

The mission, by-laws, and amendments currently proposed by the FAF and FASB and GASB make frequent reference to the importance of “users” or “investors” in both their targeted purpose and constituencies.

The “investor” targeted for FAF, FASB and GASB purposes should be an individual who has achieved, through education, examination and experience, a level of professional competency. For example, a candidate could include an investment professional with a decade or more of buy-side or sell-side experience who is the holder of a relevant professional designation (such as a CPA or Chartered Financial Analyst[®] (CFA[®])) and/or who has an MBA with a concentration in accounting or finance. An extremely important aspect to the “investor” definition is the ability to bring to accounting standard setting decisions an emphasis on the usefulness of financial statement data for investment decisions, including the need for comparability, consistency, and transparency. Preparers and auditors of financial statements may not understand how those statements are used, and usually have a preference for flexibility and confidentiality (preparers) and auditability (auditors). In essence, an investor is an individual whose career advancement and compensation are tied directly to their success or failure at making significant investment decisions.

As in any profession, “investors” come in a variety of flavors – frequently starting in assistant analyst support positions, moving up to full analyst responsibilities where their recommendations are actively used in investment decisions, advancing further to management roles (i.e., overseeing the activities of other investment professionals), and finally achieving executive positions within their companies or institutions. It is important for the FAF, FASB and GASB to recognize that as an individual makes that last transition, their role as an “investor” may undergo a significant change. The orientation of the CEO or other management level officer of a mutual fund, bank, or brokerage firm is likely to be much more closely associated with the priorities of preparers, since they are themselves responsible for preparing such public financial statements, and less linked to the needs and desires of analysts who are using these statements. While it is extremely important for the FAF, FASB and GASB to receive input from such individuals, it is likely that financial statement users in non-management ranks and their immediate supervisors (such as directors of research) may provide more representative input as “investors.”

Appendix II

Key Principles of an XBRL Framework

The CFA Institute Centre for Financial Market Integrity established the XBRL Working Group of CFA Institute members in early 2007. XBRL (eXtensible Business Reporting Language) represents a new technology for delivering computer readable financial information³². The objectives of the group included conducting a survey on XBRL and incorporating the survey results into a draft position paper on the topic. Through their research, discussions, and analysis of the survey results³³, the Working Group developed the following key principles to outline those XBRL framework attributes they believe are necessary to maximize the investors' benefits from XBRL.

1. Core taxonomy (or structure of tagging elements) should be predefined by current financial reporting standards, including generally accepted accounting principles and other regulatory disclosure and reporting requirements.
2. Taxonomy extensibility should maintain the level of data comparability as defined by GAAP and other regulatory requirements.
3. Ultimately, companies should deliver required financial reports to regulators using the established XBRL framework.
4. The general public should have equal access to the XBRL-tagged information.
5. Regulators should develop the necessary infrastructure and protocol to ensure the timely updating of the established XBRL framework as outlined in the preceding four key principles.

These principles are intended to guide global regulators in the implementation of XBRL as their required reporting standard. As such, our use of the term "GAAP" applies to the broad application of generally accepted accounting principles and not to any specific national or international accounting standards. (The CFA Institute Centre does also hold a longer term goal of seeing the adoption of a single global accounting standard, which would include a unified XBRL taxonomy for the standard.)

³² Additional details about "What is XBRL?" are available on the CFA Institute website:
<http://www.cfainstitute.org/centre/topics/reporting/xbrl/index.html>

³³ The full survey results are available on the CFA Institute website:
<http://www.cfainstitute.org/centre/topics/reporting/xbrl/topline.html>

Appendix II

The XBRL Working Group, while developing the key principles, outlined several sub-topics further clarifying the intention of each principle. The CFA Institute Centre staff and XBRL Working Group members remain open to further discussion on the developed principles so that we maintain a reasonable balance between promoting XBRL's benefits and minimizing the burden that implementation of XBRL places on the companies preparing financial reports.

1. Core taxonomy (or structure of tagging elements) should be predefined by current financial reporting standards, including generally accepted accounting principles and other regulatory disclosure and reporting requirements

- The elements in the core published taxonomy should follow the current approved accounting and/or regulatory requirements.
- Discrete elements for the note disclosures should provide, at a minimum, the same discrete, specified information required in the GAAP literature (e.g., individual values and specific disclosures in notes should be individually tagged in addition to the entire narrative or note disclosure as it appears in the original filing).
- The taxonomy design should allow for the grouping of related topical fields regardless of whether the elements appear on the primary financial statements or in disclosure notes (e.g., all elements related to pension information should be linked and accessible by topical grouping), thus allowing the presentation of elements from the disclosure notes and financial statements under a single topical heading.
- The elements in non-GAAP taxonomies should address the disclosure requirements of the capital market regulator (e.g., management discussion and analysis, other sections of the annual financial reports).
- The disclosure requirements of commonly reported corporate action events of capital market or other regulators (e.g., dividend announcements, stock splits, corporate restructuring, voting results) should be addressed in additional non-GAAP taxonomies.

2. Taxonomy extensibility should maintain the level of data comparability as defined by GAAP and other regulatory requirements

- The taxonomy should allow companies to report their operational performance and financial conditions. A robustly defined taxonomy should limit the need for custom extensions or company-specific tags for unique items not covered in the core taxonomy.
- When custom extensions are necessary, preparing companies should be given a specified protocol as defined by regulations or accounting literature on how to link the company-specific element(s) to the core GAAP taxonomy.

Appendix II

- Custom extensions should not alter the primary element definitions and calculation relationships within the published taxonomy.
- When adding a custom extension, companies should include sufficient detail in the definition and regulatory reference sections of the new element so users can understand the difference from the core taxonomy field.
- New technological features should either reduce or have a neutral impact on the need for company-specific taxonomies in order to maintain a minimum level of comparability as defined by regulations and GAAP.

3. Ultimately, companies should deliver required financial reports to regulators using the established XBRL framework

- Regulators should mandate all reports required by GAAP and other regulations be delivered exclusively through an XBRL framework.
- Reports filed should include a table of contents that identifies each section of the filing (e.g., primary financial statement, disclosure notes, MD&A) and allows for easy navigation between the various sections.
- To provide the same level of assurance currently given to filed reports, the independent review of XBRL filed reports should be part of the regular audit process. The development of a transition process will minimize duplicative efforts and costs during the implementation of the XBRL framework.
- The body of the filed report should include basic information about the reporting entity, such as legal name, industry classification, primary security ticker, report date, form type, etc.
- The XBRL framework should delineate the relationships between the values associated with the XBRL tagged values and the contextual attributes of the information (e.g., audited, restated, time period reference). Contextual information types for segment (e.g., consolidated, segmented, geographical) and scenario information (e.g., audited, restated) should be developed to assist in automated analysis.
- When developing or modifying the taxonomy, an independent, electronically-accessible review should be performed to account for the end user/investor perspective of the technical implementation and the elements (high-level categories and structure) approved.

Appendix II

4. The general public should have equal access to the XBRL tagged information

- Regulators that establish an XBRL reporting framework need to provide, at a minimum, a base-level application, that transforms the XBRL tagged report from a computer-readable format to a human readable/useable format. Such application should include a user-friendly interface to allow online viewing and download capability of XBRL-sourced information.
- The technology regulators use in their XBRL reporting frameworks should remain “open source”³⁴ to promote development of and competition between third-party software providers.
- Regulators that adopt an XBRL framework should encourage the electronic redistribution of filed information—including the values and the tag—in various formats (e.g., spreadsheet, database readable, other applicable software).
- Information should be structured so that users may sort and view data either by individual elements (e.g., net income or dividends paid), by topical grouping of elements (e.g., plant, property and equipment, pension disclosures), or as a complete download of all elements (e.g., complete financial filing or a single primary statement). Also, such information should be downloadable either for individual or multiple companies.
- Regulators that adopt an XBRL framework should only define or provide analytical calculations as defined in the accounting literature. Likewise, they should only provide software that facilitates the investor’s ability to make this type of calculation and analysis.

5. Regulators should develop the necessary infrastructure and protocol to ensure the timely updating of the established XBRL framework as outlined in the preceding four key principles

- The core taxonomy should be modified as needed to keep current with any changes made to the accounting or regulatory standards.
- Regulators should make regularly scheduled reviews of the custom extensions to determine the need to add new common items to the core taxonomy.
- Regulators should promptly review for adoption any technological advances approved by XBRL International.
- Regulators should coordinate updates to regulator-approved XBRL software with changes to the taxonomy and any newly-adopted XBRL technology standards.

³⁴ Open source generally refers to an application and its source code that is available royalty free and allows redistribution without any restrictions. The expectation of keeping XBRL technology in this format is to promote adoption by regulators, companies and investors worldwide. This would also encourage the development of robust processing tools both internally by companies using or producing XBRL tagged information and external software companies.