Setting the global standard for investment professionals

November 6, 2009

The Honorable Barney Frank
Chairman
Committee on Financial Services
U.S. House of Representatives
Room 2129 Rayburn House Office Building
Washington, DC 20510

The Honorable Spencer Bachus
Ranking Member
Committee on Financial Services
U.S. House of Representatives
Room 2129 Rayburn House Office Building
Washington, DC 20510

The Honorable Paul Kanjorski
Chairman
Subcommittee on Capital Markets,
Insurance and Government Sponsored Entities
House of Representatives
Room 2129 Rayburn House Office Building
Washington, DC 20510

The Honorable Scott Garrett
Ranking Member
Subcommittee on Capital Markets,
Insurance and Government Sponsored Entities U.S.
U.S. House of Representatives
Room 2129 Rayburn House Office Building
Washington, DC 20510

Dear Chairman Frank, Subcommittee Chairman Kanjorski, Ranking Member Bachus and Subcommittee Ranking Member Garrett:

We understand that Congressman Ed Perlmutter (D-CO) is considering proposing language to amend the Financial Stability Improvement Act and that Congressman Gary Miller (R-CA) has proposed an amendment that has been incorporated into the Investor Protection Act. Both amendments would seek to, albeit to differing degrees, establish more Federal regulatory oversight of the Financial Accounting Standards Board (FASB) which would be less independent that the current oversight of the FASB by the Securities and Exchange Commission (SEC).

We strongly oppose these proposed amendments which we believe will interfere with independent oversight of the FASB. It was the great insight and wisdom shown by Congress during the Great Depression which created the SEC in the first place, and that gave it the mission of protecting investors. A key part of that mission is requiring complete, fulsome, timely, and accurate disclosure of financial information which affects investment decisions through financial statements that adhere to independently established accounting standards. To ensure that the relevance and reliability of this decision-useful information continues, CFA Institute strongly supports – as we have repeatedly conveyed in our communications during the recent financial crisis – the independence of the accounting standard setting process and believes that the oversight relationship between FASB and the SEC should continue unamended.

Recognizing that an independent standard setter makes it more likely that accounting standards will serve the needs of those who read and review financial reports, the SEC has delegated the standard setting process to the FASB. Accounting standards are developed to provide investors, and other users of financial statements, with

Charlottesville Hong Kong London
560 Ray C. Hunt Drive
PO Box 3668
Charlottesville, VA
22903-0668 USA
434 951 5499 tel
434 951 5262 fax
info@cfainstitute.org
www.cfainstitute.org

faithful representation of economic reality. Without independence, neutrality, and a rigorous and inclusive due process, the development of accounting standards will not meet this objective.

These proposed amendments seek to make the FASB beholden to a board of regulators – principally banking regulators. We believe these proposed structures will increase the potential for political influence in the accounting standard setting process, and may imply to investors that accounting standards are developed principally for banks, not other financial institutions, investors, or the wide variety of other industries that are essential to our economy.

We believe the notion that the FASB needs to be governed by a board of regulators stems from two mistaken beliefs. First, that fair value accounting caused the financial and/or banking crisis, was pro-cyclical, and created or exacerbated systemic risk. Fair value accounting did none of these. It is a method of accounting for economic events and, as a consequence, reflects such events rather than creates them. Problems at financial institutions were the result of a number of factors and parties, not the least of which included bad loans, poor business practices and decisions, and misguided management. These issues were made worse by the poor level of transparency in financial reporting. Fair value accounting only demonstrates the results of these underlying business practices.

A CFA Institute study of 2,006 of our members conducted in March 2008 revealed that 79% of respondents believe that fair value improves financial institution transparency and understanding of the risk profile of a reporting entity and 74 % believe that it improves market integrity. Respondents were essentially divided on the question whether fair value aggravated the global credit crisis. These findings reaffirm our position that continuing the use of fair value is vital to the integrity and transparency of markets.

Admittedly, the fair value measurement basis is not without limitations and the recent financial crisis caused standard setters, preparers, auditors, and users to debate its application in inactive and/or disorderly markets. Such debate and due process is a part of what makes independent standard setting effective. However, controversy over one accounting standard – which our study shows users overwhelmingly support – during a period of severe market disruption does not warrant the entire accounting standard setting process being more regulated, especially not by banking regulators.

Second, the effect that fair value had on bank capital adequacy created an inaccurate perception that accounting standard setting and financial statement preparation are done solely in the context of regulating solvency, and more specifically, the capital adequacy of one industry. The mission of accounting standard setting is much broader. While in times of severe economic distress it may appear that financial statements – particularly bank financial statements – are prepared for purposes of assessing financial stability, this is but one purpose of reporting financial results. Rather, accounting standard setting and financial reporting is done with the objective of providing complete, transparent, timely, and relevant financial information to all types of investors across many different industries. This enables investors to make effective capital allocation decisions in both good and bad economic times.

It is our view, that these mistaken beliefs about fair value accounting and its effects on bank capital adequacy are resulting in legislation which, while perhaps well intended, will ultimately harm investors. These actions will cause investors to receive less relevant and reliable financial information stemming from politically motivated standard setting. Further, we offer that banks, as providers of capital, could very well be unduly advantaged if given a greater hand in the standard setting process.

To reiterate, we strongly oppose these proposed amendments to the Investor Protection Act and Financial Stability Act and we believe the activities of the FASB should remain under the exclusive oversight of SEC.

Sincerely,

/s/ Kurt N. Schacht

Kurt N. Schacht, JD, CFA
Managing Director
CFA Institute Centre for
Financial Market Integrity

/s/ Sandra J. Peters

Sandra J. Peters, CPA, CFA
Head, Financial Reporting Policy
CFA Institute Centre for
Financial Market Integrity

cc:
The Honorable Ed Perlmutter
The Honorable Gary Miller
Chairman Mary Schapiro, Securities and Exchange Commission
Mr. Robert Herz, Financial Accounting Standards Board