



## Financial Reporting Council

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Dear Tamara,

### **IASC Foundation Review of the Constitution: Public Accountability and the Composition of the IASB – Proposals for Change**

The Financial Reporting Council (FRC) is the United Kingdom's independent regulator responsible for promoting confidence in corporate reporting and governance.

The FRC is a strong and committed supporter of the IASC Foundation and the IASB and welcomes the opportunity to comment on the Constitution Review proposals set out in the July 2008 consultation document. Our responses to the questions posed in the consultation document are set out below, and build on the remarks I made at the Trustees' roundtable session held on 21 June.

#### **Questions related to the Monitoring Group**

*Q1 Do you support the creation of a link to a Monitoring Group in order to create a direct link of public accountability to official institutions?*

Yes, the FRC supports the creation of such a link, which should help to address the concerns that have been expressed for a number of years about the legitimacy of the IASC Foundation (and, as a consequence, the IASB) and its public accountability.

*Q2 Proposed composition of the Monitoring Group*

The proposed composition of the Group is a mix of national, regional and international organisations. At the 21 June roundtable, I asked the Trustees for an explanation of the principles on which the composition of the Monitoring Group is based. The FRC notes that the references to the membership in paragraphs 13 and 14 of the consultation document and what that membership should reflect in paragraph

19 could be seen as a starting point for setting out such principles, but we think that this needs to be more clearly specified. For example, looking at the proposed initial composition, it does appear to have a heavy weighting of securities regulators. What is the rationale for this? When considering the global market conditions over the past year or so, is there any reason why other official organisations with a specific financial stability mandate, such as the Financial Stability Forum (FSF) and central bank organisations, should not also be members?

Articulating the principles for membership will help all market participants to understand the rationale for the proposed composition of the Monitoring Group. It will also, in our view, be important, not only in providing a framework for how additional claims to join the Monitoring Group might be handled (the FRC is already aware of a number of organisations that have expressed an interest), but also in providing a basis for how any changes in membership in the future might be considered.

*Q3 Does the formulation of the Monitoring Group's mandate and the Trustees' reporting responsibilities, as described in the proposed Section 19, appropriately provide that link, while maintaining the operational independence of the IASC Foundation and the IASB?*

Yes. The FRC believes it is important that it is made clear that the Trustees remain the body primarily responsible for the governance of the organisation and the oversight of the IASB. In this respect, we support the proposal for a Memorandum of Understanding (MoU), to be agreed between the Monitoring Group and Trustees describing their interaction, which would be developed after the Monitoring Group has been established. Paragraph 16 of the consultation document states that the MoU would be made public when agreed, but also notes that the Trustees would recommend that the MoU should be subject to public consultation before its completion. The FRC strongly supports the Trustees' recommendation. The MoU should be subject to public consultation and not represent the outcome of a 'private' agreement.

*Q4 Given the proposed creation of a Monitoring Group, would there be a continued need for the Trustee Appointments Advisory Group in the selection of Trustees? If so, what should be the role and composition of the Trustee Appointments Advisory Group?*

Yes, the FRC believes that there is a continued need for the Trustee Appointments Advisory Group. Given the overlap in membership between the Advisory Group and the Monitoring Group, one could argue that the Advisory Group could go. That said, the membership of the Advisory Group is broader, which would allow for a wider range of perspectives to be considered in the selection of Trustees. Paragraph 18 of the consultation document notes that the Monitoring Group would be entitled to recommend candidates as Trustees, but that the Trustees themselves would administer the process. In that circumstance, it would seem appropriate to retain the Advisory Group.

*The Trustees would welcome any additional comments related to the Monitoring Group proposal.*

The only additional comment the FRC would make is to emphasise the importance of ensuring that the proposal to establish a direct link to a Monitoring Group does not entail any major transfer of power from the Trustees to the Monitoring Group.

#### **Questions related to the IASB's composition**

*Q5 Do you support the principle behind expanding the IASB's membership to 16 members in order to ensure its diversity, its ability to consult, liaise and communicate properly across the world, and its legitimacy?*

No. The FRC does not support an expansion to 16 Board members. A Board of 14 members is challenging enough to manage; expansion to 16 members will make that management harder still and runs the risk of impairing the effectiveness of the Board's decision-making, as well as slowing it down.

The current Constitution (paragraph 21) already requires the Trustees to select IASB members from diverse backgrounds, so as to provide "an appropriate mix of recent practical experience among auditors, preparers, users and academics". Taking the expansion together with the proposed geographical formulation, there is a danger that Board members could be seen as having their own particular constituencies for consultation, liaison and communication. In the first Constitution Review, concluded in 2005, the Trustees removed a reference in the Constitution to a number of IASB members having formal liaison relationships with certain national standard-setters to emphasise a more general (non-geographic) liaison role. The current proposals imply a backward step and would seem to the FRC to impair, rather than enhance, the Board's legitimacy.

The FRC is aware of, and appreciates, the extensive 'outreach' work undertaken by IASB members, but that should not detract from their primary purpose, which is to take technical decisions to improve the quality of financial reporting. It is also the case that senior staff of the IASB spend a good deal of time in consultation, liaison and communication of the Board's proposals and decisions, and these tasks in our view can be achieved effectively without an increase in IASB membership.

*Q6 Do you agree with the geographical formulation suggested by the Trustees?*

No. Introducing a specific geographical quota would appear to run counter to the emphasis in paragraph 19 of the current Constitution that professional competence and practical experience should remain paramount criteria for the selection of IASB members. The FRC acknowledges that the consultation document (paragraph 23) makes clear that the Trustees believe that this remains the case and that members shall act in the public interest, not as representing geographical constituencies. However, there remains a danger that appointments to the Board could be made more for political reasons than technical ones. The current Constitution (paragraph

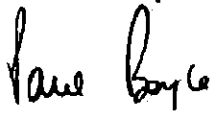
6) requires that there is a geographical spread in the body of Trustees, which seems more appropriate than introducing such a spread at Board member level.

*Q7 The Trustees are suggesting that the Constitution should provide flexibility on the matter of part-time membership. Do you support that proposal?*

Yes, although we recognise the challenges of being a part-time member of the IASB and a danger that they could be seen as being 'delegates' of their parent organisations.

If you would like to discuss any of the comments made above, then please contact Ian Wright on 020 7492 2330 or me on 020 7492 2390

Yours sincerely



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