

FINANCIAL ACCOUNTING FOUNDATION

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J. MICHAEL COOK
President

May 20, 1996

The Honorable Arthur Levitt, Jr.
Chairman
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Dear Arthur:

The Trustees of the Financial Accounting Foundation (FAF) appreciate the views expressed in your April 22, 1996 letter and the discussions that we have had with you and members of your staff regarding the composition of the FAF Board of Trustees and the independence of the Financial Accounting Standards Board (FASB). As the parent organization of the FASB, we fully understand the importance of the role of private sector standard setting and that the SEC has relied on the private sector to establish accounting standards for registrants for over 60 years. We share your commitment to safeguarding the independence of the FASB and to ensuring that the FASB not be unduly influenced by any particular group or body.

We also recognize, however, that you have a perception that the composition of the FAF Board of Trustees somehow prevents it from sufficiently supporting the FASB. We emphatically do not agree.

With its formation in 1972 and throughout its history, the FAF has acted to preserve the independence of the FASB and to make continuous improvements to the FAF and FASB structure and operations. This has served to ensure that the FASB achieves its mission of establishing and improving financial accounting and reporting standards for the approximately 12,000 SEC registrants, as well as the hundreds of thousands of nonpublic companies and not-for-profit organizations subject to the FASB standards. We can all be justifiably proud of the accomplishments of the FASB over its 23 year history in developing a conceptual framework and a body of accounting standards that are widely recognized as the best in the world. Those standards contribute in great part to the efficient functioning of our economy and capital markets because decisions about the allocation of resources rely heavily on credible and understandable financial information.

Over the years, the FAF and FASB have periodically considered and implemented changes in their respective organizations to enhance the standard setting process. The FASB recently completed its strategic plan, which the Trustees accepted at the April 1996 FAF meeting. That plan states that the FASB, "along with the FAF Trustees, are committed to improving independent, private-sector standard setting and providing leadership in shaping the debate over the future of financial reporting." The FASB's strategic plan also acknowledges that improvements can and should be made to build broader acceptance for the FASB's process and make standard setting more timely and efficient. The plan further states, "We also must improve the way we operate to ensure that we address the right issues in a timely manner and strengthen our ability to communicate and explain the importance of the role of accounting

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standards in providing financial information to the marketplace. In the past, some of our major projects have taken 10 years or more to complete. That is much too long in today's world." With our full support, the FASB has adopted and is now implementing specific strategies to improve its agenda-setting process, to make FASB standards easier to understand and implement, and to complete projects more rapidly.

The FAF began earlier this year to develop its own strategic plan and consider its operations and structure, including the size and composition of the FAF Board of Trustees. We discussed this with you and you agreed with this initiative. As part of that strategic planning process, the FAF has received recommendations and input from various sources, including sponsoring organizations of the FAF. The Trustees are considering the recommendations received, some of which have already been rejected because those recommendations would reduce, in fact or in appearance, the independence of the FASB. For example, some representatives of one organization, the Financial Executives Institute, suggested that an independent, third-party organization control and oversee the agenda for the FASB. The FAF has rejected that idea and we have elaborated on our rejection in our reply to their suggestion. [See enclosed].

In the meantime, we are moving promptly to appoint two At-large public Trustees. Those new Trustees would be filling positions previously held by the chief financial officer of a major industrial corporation and the vice chairman and chief financial officer of a major banking organization. However, we do not believe it would be appropriate to change the structure of the FAF to eliminate the Securities Industry Association or any other sponsoring organization from nominating individuals for election to the FAF, or to provide for a controlling majority of the Trustees to be "public interest" Trustees, as defined by you. Your definition would exclude from consideration many dedicated individuals who have the knowledge, experience and perspective needed to best serve the public interest. Similarly, we cannot agree with a definition that would exclude elected public officials whose very job is to serve the public interest, nor do we believe that it is necessary to exclude such individuals from FASB matters considered by the FAF. We also see no need or advantage and, indeed, see significant detriment, to creating a separate Board of Trustees for the Governmental Accounting Standards Board. Finally, we could not accept any arrangement which would have the effect of permitting the SEC to approve, in substance, nominations to the FAF.

The cumulative effect of your suggestions would result in control of the FAF by the SEC and, in essence, would remove standard setting from the private sector. Although we have not accepted certain of those suggestions, we remain very mindful of the concerns you have expressed about the independence of the FASB and about the composition and role of the FAF Board of Trustees. We will continue to consider your concerns and will keep you informed as we develop our strategic plan.

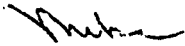
The most important duty the FAF Trustees have is selection of highly qualified, independent, FASB members. The prohibition against FAF involvement in technical matters ensures that there is no conflict of interest in FASB standard setting. The Wheat Committee, an independent advisory group convened in the early 1970s that designed the present structure for establishing

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accounting standards, was very thoughtful in its consideration of the composition of the FAF, as were the study groups and committees that recommended subsequent changes in the composition of the FAF. The Wheat Committee report provided for participation by knowledgeable individuals and groups at all levels of the standard setting process, recommended a broad base of support (financial and institutional), and called for a diverse range of skills and perspectives for both the FASB and the FAF.

We believe that the conclusions of the Wheat Committee are as valid now as ever.

On Behalf of the Trustees of the Financial Accounting Foundation,



J. Michael Cook