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Empower Users of Financial Information as the IASC Foundation's Stakeholders

Testimony to the IASC Foundation's Constitution Review Round Table in London, 19 June 2008

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Empower Users of Financial Information as the IASC Foundation's Stakeholders

Presentation by Nicolas Véron, Research Fellow at Bruegel

Constitution Review Round Table held by the International Accounting Standards Committee (IASC) Foundation in London, 19 June 2008

Background Note

EXECUTIVE SUMMARY

The creation of a new body with authority over Trustee appointments and reappointments is a crucial step for the IASC Foundation. This body is likely to be granted more authority in the future over other key governance functions, including the Foundation's funding.

In this respect, the proposed Monitoring Group contains significant flaws, the primary one being its inability to credibly represent at global level the investors and other capital-market users which should be considered the Foundation's key stakeholders.

Moreover, the very short timetable proposed for the first part of the Foundation's Constitution Review is not warranted by the circumstances. The Foundation's Trustees should take a step back and consider a revised concept of oversight body as part of a one-phase Constitution Review to be completed in 2009.

This note is intended for use by the International Accounting Standards Committee (IASC) Foundation following the presentation I was invited to give on 19 June 2008 at the Constitution Review Round Table organised in London under the Chairmanship of Gerrit Zalm, Chairman of the Foundation's Trustees. The note's content is essentially the same as my oral presentation during that meeting, with additional quotes from written sources.

Bruegel is a European think tank devoted to international economics, which started operations in Brussels in 2005 with the support of a number of European member state governments and international companies. Bruegel aims to contribute to the quality of economic policymaking in Europe through open, fact-based and policy-relevant research, analysis and discussion. Its publications, research programme, and other detailed information are available on www.bruegel.org.

This testimony represents my personal views as a research fellow, not those of Bruegel as an organisation. The governance of accounting standard-setting is a topic to which I have devoted significant research work since 2002, including in a book published first in France and later in the United States[1] and in a policy paper published by Bruegel in its Blueprint series[2]. I consider that my work at Bruegel, private consulting activity, and other activities including as a member of the Accounting and Auditing Practices Committee of the International Corporate Governance Network (a position for which I receive no remuneration) do not introduce a commercial or special-interest bias in my views nor do they impair the integrity of my research in the debate about the IASC Foundation's governance.

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[1] Respectively *L'Information financière en crise* (Odile Jacob, 2004) and *Smoke & Mirrors, Inc.: Accounting for Capitalism* (Cornell University Press, 2006), co-authored with Matthieu Autret and Alfred Galichon

[2] *The Global Accounting Experiment* (April 2007), available on www.bruegel.org

Most of the following comments are devoted to the IASC Foundation's proposal to create a Monitoring Group as 'part one' of the envisaged Constitution Review. I also comment on the proposal to reform the size and composition of the International Accounting Standards Board (IASB), at the end of this text.

1. Constitution Review Background

International Financial Reporting Standards (IFRS) have met with extraordinary success since the creation of the IASB and IASC Foundation in the early 2000s and subsequent IFRS adoption by the European Union followed by a large number of jurisdictions around the world which either implement them or have announced a clear timetable leading to such implementation in the next 4-5 years. This worldwide success, including the recognition of IFRS use by non-US issuers decided by the US Securities and Exchange Commission (SEC) in November 2007, attests that IFRS as they currently stand are considered a broadly adequate response to the requirements of global capital markets for high-quality accounting standards.

At the same time, the IASB and IASC Foundation have faced criticism and received suggestions as to their governance, funding, and accountability. Based on a draft proposed by Alexander Radwan MEP on 24 September 2007, the European Parliament on 24 April 2008 adopted (by 373 votes to 21, with 13 abstentions) a resolution in which it *'considers that, lacking satisfactory solutions to problems regarding the establishment and oversight of the IASCF/IASB, a debate should be launched on the conditions for integrating the IASCF/IASB into the system of international governance, for example with the International Monetary Fund, the Organisation for Economic Co-operation and Development and the World Bank.'* In the same text, the European Parliament *'takes the view (…) that governance and accountability must be improved through the following measures: (a) setting up a public oversight body involving all IASCF/IASB public stakeholders including, in particular, legislators and supervisors; and setting up a body allowing representative market participants, including preparers and users from jurisdictions where IFRS are mandatory, to deliver annually a report on the functioning of international accounting standard setting to the governing bodies of the IASCF/IASB; (b) such an oversight body could be responsible for selecting and appointing the trustees in a transparent procedure ensuring both the competences of the candidates and a balanced geographical representation of all stakeholders; this would help make the appointment procedure more transparent and significantly enhance the legitimacy of the trustees (…).'*

In the US, Senators Christopher Dodd, Chairman of the Committee on Banking, Housing and Urban Affairs, and Jack Reed, Chairman of the Subcommittee on Securities, Insurance and Investment, have written in a letter to the SEC on 14 November 2007 (the day before the decision to eliminate the reconciliation requirement for foreign issuers using IFRS) their concern that *'The IASB's lack of an independent funding source is troubling and inconsistent with the framework set by Congress* [namely, Section 108(a) of the Sarbanes-Oxley Act of 2002] *for the SEC's recognition of any accounting principles established by a standards-setter other than the SEC itself.'*

There is no clear precedent to address these concerns. The IFRS standard-setter is unique in its combination of de facto global policymaking power and private-sector governance, and therefore has to invent its own solutions to the challenge of global accountability. The sometimes-cited example of the Public Interest Oversight Board of the International Federation of Accountants, a global professional organisation which has public-interest functions such as setting International Standards on Auditing (ISA), does not apply adequately, primarily because the direct impact of IFRS is much more significant than that of ISA.

The governance of the IASC Foundation and IASB is enshrined in the IASC Foundation Constitution (hereinafter the 'Constitution') whose current Section 17 introduces the obligation to review the Constitution every five years, which, given the timing of the previous Review which was completed in June 2005, would imply implementing any agreed changes by June 2010 at the latest. The currently considered reform is proposed as a first part of the Constitution Review, the second part being scheduled for 2009.

On 6 November 2007, days before the SEC's decision on the reconciliation requirement, the IASC Foundation announced its intent to *'establish a link to a representative group of official institutions, including securities regulators'* that *'would approve Trustee appointments and review Trustee oversight activities.'* This proposal was refined when, on 11 February 2008, the Foundation announced its decision to *'accelerate consideration of their proposals on the size, composition and mandate of a monitoring group with the goal of reaching conclusions in the second half of 2008. Initial proposals will be published in the second quarter of 2008.'* On 8 April 2008, the Foundation announced the Trustees' intent *'to publish later this month for public comment their proposals regarding the Monitoring Group and the composition of the IASB.'* However, no document was released in April, and on 12 May the Foundation announced: *'A round-table discussion will be held in the coming weeks before the publication of the official consultation document.'* On 30 May 2008, the Foundation published a tentative document titled 'Proposals and Issues for the Constitution Review' (hereinafter 'the proposal') and simultaneously announced the date of 19 June for the round-table discussion.

2. A Crucial Step that Shapes the IASC Foundation's Future Governance

The importance of setting up the Monitoring Group should not be underestimated. For the first time, the Constitution would give an external party direct authority over the Foundation, through granting it the essential power to shape the composition of the Trustees.

The proposal gives the Monitoring Group the right to recommend candidates for Trustee positions, and to discretionarily approve or refuse Trustee appointments or reappointments (Proposed Section 5). Thus, the authority to appoint or reappoint Trustees would be effectively transferred from the Trustees, who currently hold it, to the Monitoring Group.

The statement made in the proposal (page 6, §18) that *'under the new arrangement, the governance of the IASC Foundation would remain with the Trustees, and the responsibilities of the Trustees and the independence of the standard-setting function (…) would remain unaltered'* is open to question. In reality, appointing and reappointing the trustees is a key governance function which would not 'remain with the Trustees' but on the contrary would be transferred to a third party not controlled by the Trustees, namely the Monitoring Group.

By doing this, the proposal if implemented would create the IASC Foundation's de facto highest body, i.e. a body that has formal authority over the Trustees through its control of their appointment and reappointment, as well as other rights to information and interaction with the Trustees and IASB as set out in the proposed new Section 19 of the Constitution. This is entirely different from consultative processes set up in the past, including the Trustee Appointments Advisory Group created in November 2005, in which the ultimate decision-making authority had always remained with the Trustees.

The ability to appoint and reappoint Trustees is one of the most essential governance functions in an organisation such as the IASC Foundation. However, it is not the only one, and other key governance aspects, such as the Foundation's funding framework and the very nature of its formal governance arrangements as set out in the Constitution, may also come under the spotlight of the public debate in the future, with public pressure building up to guarantee more stakeholder input. Such future developments are likely to be heavily path-dependent, i.e. the decisions made at each step will be largely determined by those made at earlier steps including the current one. It can thus be confidently predicted that any new powers over the Trustees, on issues such as funding or the process to revise the Constitution, will be granted to the Monitoring Group, as it would be the only existing body which represents stakeholders and already has authority over the Trustees on some governance functions.

Thus, the proposal if implemented would probably pave the road for a Monitoring Group that not only would ultimately control the composition of the Trustees, but could acquire other direct governance tasks as well. Trustees should keep these future consequences in mind when considering the current proposals.

3. Identifying the IFRS' Stakeholders

The proposal presents the creation of the Monitoring Group as an initiative to 'enhance public accountability' (page 5) of the IASC Foundation. However, accountability can only be defined with reference to one or several groups of stakeholders to which the Foundation would be made accountable.

The IASC Foundation is a private-sector organisation tasked with an economic policymaking responsibility, accounting standard-setting, at global level – or, as the proposal puts it, *'de facto setting law in many jurisdictions'* (page 6, §16). This unique situation means that the question of who its key stakeholders are exactly is far from straightforward. In national environments, accounting standards are set in reference to a sovereign authority, which in democratic jurisdictions belongs to the people. In the context of the European Union, that authority is shared between the people and member states, all of which are themselves democracies, with a common legal basis for EU matters. But there is no comparable setting at global level. Specifically, many of the countries in which IFRS are now implemented are not themselves democracies, and there is no overarching global framework of law. Thus, the accountability framework that exists in national democratic environments cannot effectively be replicated or emulated by the IASC Foundation at global level. From that point of view, it would be hazardous to describe the Monitoring Group, as did a joint communication by regulators on 18 June, as *'a mechanism (...) that approximates the historical relationship between securities authorities and national standard setters'*[3].

The proposal specifically makes the point that *'the Trustees are accountable not to a single group, but to the wide range of international stakeholders that have an interest in the IASC Foundation's efforts to achieve its objectives.'* However, this language does not provide much clarity on who such stakeholders actually are or should be. It is a truism that different stakeholders may have different demands on financial reporting standards, and therefore the recognition of key stakeholders is bound to have a significant influence on the standard-setting process and eventually the content of the standards themselves.

Article 2 of the Constitution, which specifies the objectives of the IASC Foundation, mentions as its first aim *'to help participants in the world's capital markets and other users make economic decisions'.* Since the 2005 revision, it also introduces consideration for *'the special needs of small and medium-sized entities and emerging economies'*. This is as close as exists to a constitutional definition of the organisation's stakeholders. Furthermore, the IASB's Framework for the Preparation and Presentation of Financial Statements (adopted by the IASC in 1989 and readopted by the IASB in 2001) indicates that *'While all of the information needs of these users* [as previously listed: investors, employees, lenders, suppliers and other trade creditors, customers, governments and their agencies, and the Public] *cannot be met by financial statements, there are needs which are common to all users. As investors are providers of risk capital to the enterprise, the provision of financial statements that meet their needs will also meet most of the needs of other users that financial statements can satisfy'* (Section 10). A new text for the Framework is being considered (as part of a revision project that started in 2004, an exposure draft was published on 29 May 2008 and is currently undergoing consultation), with a new description of the objective of financial reporting including the following text: *'The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to present and potential equity investors, lenders and other creditors in making decisions in their capacity as capital providers. Capital*

[3] Joint press release of SEC Chairman Christopher Cox, IOSCO Executive Committee Chair Jane Diplock, Japanese Financial Services Agency Commissioner Takafumi Sato and European Commissioner Charlie McCreevy, 18 June 2008, available on www.ec.europa.eu.

providers are the primary users of financial reporting.' It would appear from these indications that investors and creditors, and more generally users of financial information for financial decision purposes, are the key stakeholders of IFRS standard-setting, with due consideration to other capital market participants, small- and medium-sized enterprises (SMEs), and public authorities including those in emerging economies.

Indeed, the past successes of the IASB and its predecessor body can be largely attributed to their focus on the needs of investors and other financial users of financial information when setting accounting standards. In key developments such as the adoption of the IFRS 2 standard on share-based payments, or the 2003-04 controversy over the IAS 39 standard on financial instruments, the focus on users' needs (as opposed to individual national constituencies and their public representatives including governments, securities regulators, and financial supervisors) is reckoned by many observers to have had the effect of enhancing standards' quality.

However, other indications given by the IASC Foundation provide a different picture of whom it considers its key stakeholders. User representatives are notoriously few among the Foundation's Trustees and members of the IASB, and investors are even less represented than other users. Also, in at least one key recent standard-setting development, the IFRS 8 standard on operating segments adopted in November 2006, the IASB gave the impression that it was insensitive to user's concerns on an issue which is essential to them and particularly to investors[4].

In the same vein, the proposal twice mentions actual consultation with stakeholders, with no specific reference to investors or users: *'the Trustees met key stakeholders from around the wor[l]d with an interest in accounting standard-setting, including regulators, accounting and business organisations'* (page 3, §6) and *'the Trustees have identified stakeholder groups with which they maintain regular contact and are establishing mechanisms to receive input outside formal consultations. These stakeholder groups include official organisations, policymakers and private sector institutions from around the world'* (page 5, §15).

The current lack of clarity on the nature of the IASC Foundation's primary stakeholders bears risks for the Foundation and IFRS standard-setting. Unlike commercial enterprises, non-profit organisations generally have a complex pattern of accountability involving multiple stakeholder groups, and they need an accordingly well-structured governance framework to perform[5]. This is even truer for the IASC Foundation with its unique public responsibility.

4. The Proposed Monitoring Group

In this context, the proposed composition and functioning of the Monitoring Group raise several awkward questions. By proposing to devolve the power to appoint its Trustees to a small group of securities regulators and other national and international public agencies, the Trustees may well create more problems than they solve.

The set of initial members proposed for the Monitoring Group is heteroclite. It mixes the heads of two securities regulators, the SEC and Japanese Financial Services Agency (JFSA), a European Commissioner, the heads of two international organisations which have no direct regulatory authority over financial reporting, the International Monetary Fund and World Bank, and two members of the International Organisation of Securities Commissions (IOSCO). Why these, and not others, have been selected is not explained in the proposal.

The functional rationale is not obvious. National institutional settings as regards financial reporting are extremely diverse. In the US, the SEC has wide authority both to set accounting standards, a task it has delegated to the Financial Accounting Standards Board

[4] I documented a number of users' positions in this discussion in 'EU Adoption of the IFRS 8 Standard on Operating Segments', Bruegel Policy Contribution, September 2007 (available on www.bruegel.org).
[5] See for example Peter Drucker, *Managing the Non-Profit Organization: Principles and Practices*, Collins, 1992

(FASB) since 1973, and to enforce them. In the EU, the European Commission is responsible for the IFRS endorsement process (with input from the Council and European Parliament), while public enforcement is left to national authorities. These involve to varying degrees securities regulators (though not in all EU countries), other public or semi-public bodies (such as the Financial Reporting Review Panel, which is part of the UK Financial Reporting Council, or the German Financial Reporting Enforcement Panel), and the courts, while EU-level coordination is brought by the Committee of European Securities regulators (CESR). The proposal ignores this diversity when it states that '*The Monitoring Group would include regulatory and other official bodies generally charged with the establishment and enforcement of financial reporting standards*'. Referring to the proposal for the Monitoring Group, the chairman of CESR specifically pointed out that the European Commission has no role in the enforcement of IFRS[6].

Neither is the geographical rationale straightforward. Among other potentially contentious points, the absence of major jurisdictions such as China (whose large listed companies, including those listed in Hong Kong, now have a much larger aggregate market value than Japan's[7]) is not explained. Emerging countries no longer form a marginal group from the perspective of capital markets, and most of their market participants would not necessarily consider themselves represented by the individual who happens to chair the IOSCO Emerging Markets Committee at a given point in time.

In the particular case of the EU, by including the responsible European Commissioner in the Monitoring Group, the proposal creates a potential conflict of interest which could hamper the integrity of the endorsement process of IFRS standards. As the European Commission is entrusted under this process with the task of assessing whether individual IFRS standards serve the European public interest, the fact that the responsible official is simultaneously involved in the governance of the standard-setting organisation does not appear an optimal institutional choice. Similar difficulties could appear regarding the SEC and JFSA, if and when the US and/or Japan eventually adopt IFRS as the standards applicable to listed companies in their respective jurisdictions and if these agencies are given central roles in the corresponding endorsement processes.

The future evolution of the Monitoring Group is an intriguing puzzle. The proposal describes the Group as an entity not governed by the Constitution, except for its initial composition, but by a Charter which shall be independently developed by its Members (proposed Section 20). Simultaneously, the interaction between the Monitoring Group and the Trustees shall be governed by a memorandum of understanding agreed by the Trustees, not with the Monitoring Group itself but with each of its members (proposed Section 18). No indication is given on the possible content of the said memorandum of understanding.

It seems particularly remarkable that the IASC Foundation would entrust a key governance function, the power to appoint and reappoint its own Trustees, to an entity or group of entities whose own governance (the Charter) is outside the scope of the Foundation's Constitution, as is also the specific relationship with the Trustees (the memorandum of understanding). This is an extremely awkward abandonment of responsibility and may sow the seeds of future dysfunction and threats to the IASC Foundation's independence. The fact that the Monitoring Group initially has no designated chair and is supposed to make all its decisions by consensus creates additional conditions that may prove favourable to institutional deadlock. The proposal is not even entirely clear as to whether the Monitoring Group is composed of individuals or of organisations.

Perhaps most importantly in view of the previous section, it is difficult to see the proposed Monitoring Group as a trusted representative of the key stakeholders otherwise often mentioned in the context of IFRS standard-setting, namely investors and other capital-markets users of financial information, as well as SMEs and emerging economies as the Constitution mentions them. Many securities regulators have a mandate to protect

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[6] Letter of Eddy Wymeersch, Chairman of CESR, to the Chairman of the IASC Foundation, 13 June 2008, available on www.iasb.org.

[7] Based on the FT Global 500 ranking of the world's largest companies by market capitalisation, 31 March 2008.

investors, but many have many other missions as well; more importantly, such a mandate is not enough to create universally accepted legitimacy, and it is well known that in most jurisdictions the investor community does not consider the local securities regulator to be its only or even its main advocate, if it is considered an advocate at all.

The proposed Monitoring Group seems likely to be welcomed by the European Commission, SEC and JFSA, which play a central role in the endorsement of IFRS in their respective jurisdictions. But there is a high risk that this proves far from sufficient to create broad acceptance and legitimacy.

5. Timing Considerations

The proposal (page 1, Introduction) asserts that as regards the creation of the Monitoring Group, *'delay in implementation to 2010 is not appropriate'*. This assertion is unsubstantiated and highly debatable.

The stated desire to complete the creation of the Monitoring Group before the end of 2008 has led the Trustees to envisage a very short consultation phase for the Monitoring Group. Even though the intent was announced in November 2007, an actual proposal was only made public on 30 May 2008. The final document open to consultation is expected to be published in July, for response possibly before 15 September 2008 as the proposal suggests (page 1). This means that a large part of the consultation period, which itself is unusually short, will be during the weeks of the summer recess when many market participants are not available. Such a short consultation could be advocated if there existed a strong consensus on the proposal; but this does not appear to be the case even inside the regulatory community as the position of CESR attests[8], let alone among market participants.

Such a rushed and unsatisfactory procedure could be justified if there was a clear emergency to have a change enshrined in the Constitution. But there is no indication of such emergency. On the contrary, the Constitution being the most important and basic document of the IASC Foundation and of IFRS standard-setting, one would expect that the due process for any changes brought to it be particularly demanding and unquestionable.

On page 4 (§12) the proposal states that *'in launching the Constitution Review, the Trustees are seeking to balance their immediate priority – addressing issues related to public accountability – and the need to have a thorough and inclusive process on other elements of the Constitution'*. This is an extraordinary statement. One would imagine that 'issues related to public accountability' require 'a thorough and inclusive process' even more than any 'others elements'.

If there is a specific reason to have a decision made by the Trustees no later than October 2008, as the proposal envisages (page 5), then the public is entitled to know which reason it is. A brief look at the situation in key jurisdictions suggests however that such is not the case.

In the European Union, whose decision in 2000-02 to implement IFRS *'provided the necessary encouragement for other countries to adopt a similar approach'*[9] and thus was the trigger for the IFRS' recent success, there is longstanding concern about the IASB's legitimacy and accountability, as the above quoted resolution of the European Parliament of 24 April 2008 attests. But there is no immediate threat to IFRS adoption in the EU; on the contrary, these are long-term concerns in a project whose short-term track record has been very positive, with less disruption in the transition to IFRS in 2004-06 than had been anticipated by many observers. The Parliament's resolution calls for 'launching a debate' and explicitly mentioned legislators, as well as 'representative market participants including preparers and users', among the stakeholders who should be given a role in new

[8] The letter of the chairman of CESR to the chairman of the IASC Foundation, dated 13 June 2008, states that *'CESR is really concerned about the consequences for the European Union of the [proposed] composition of the Monitoring Group'*.

[9] David Tweedie, Statement before the Subcommittee on Securities, Insurance and investment of the US Senate, 24 October 2007 (available on www.senate.gov)

formal governance arrangements. The proposal, which reduces the public debate phase to an extremely short summertime period, is not of a nature to assuage these concerns, which could only be satisfied with a more substantive public consultation and deliberation process.

In the United States, the SEC has consulted market participants about the possible adoption of a roadmap towards endorsement of IFRS for domestic issuers. Since large US business organisations such as the US Chamber of Commerce have started advocating a shift to IFRS in the past few years, eventual adoption of IFRS now seems a near-certainty. However, there is bound to be an animated debate as to the modalities of the transition. This debate is likely to involve close congressional attention at some point, in which the concerns expressed in the above quoted letter of Senators Dodd and Reed could feature highly, and to include a discussion about the accountability of the IASB and the alignment of its objectives with investors' interest.

In order to meet this challenge successfully, the IASC Foundation's interest is to build a broad and bipartisan base of acceptance and, crucially, to win backing from key US institutional investors and their representatives, including large public pension funds. There is every indication that many such stakeholders are not satisfied with the current proposal for the Monitoring Group[10]. The proposal (page 3, §7) states that *'a clear organisational objective'* for *'the IASB is to become the world's accounting standard-setter'*, implying the recognition of IFRS in all significant jurisdictions including the US. With this strategic objective in mind, the IASC Foundation should consider the risks of implementing a major governance reform with a base of acceptance which does not include key US constituents. The likelihood of the US adopting IFRS in the next few years is very high, but provided it is not derailed by an unnecessary backlash that could be caused by too narrow an approach to force a decision this year.

Nor is there any public indication that a specific deadline in 2008 serves the Foundation's interest in other key jurisdictions such as Canada, China, India, Japan, or Russia.

6. Size and Composition of the IASB

The intent to rebalance the geographical composition of the IASB is welcome and has already triggered remarkable progress in the last few years through well-thought-out appointments of highly respected individuals. However, this rebalancing in itself does not require a change in the Constitution and can be implemented by the Trustees under the current Constitution, including when several mandates expire towards the end of 2008. Therefore, from the point of view of geographical balance there is no need to implement changes to the Constitution this year.

The proposed increase in the size of the Board is a matter of mild concern. Experience suggests that the optimal size of a group of Board members to enable unity of action and substantial internal debate is around 10-13 members, which is reflected by widespread corporate practice. From that perspective, the current IASB with 14 members is already on the high side.

In order to maximise the quality of individuals appointed to the IASB, the geographical balance should be governed by principles rather than narrow rules. Assigning only one geographical zone to each Board member does not fit well with the fact that many of the relevant individuals have had highly international careers which give them a sensitivity and knowledge of different parts of the world.

In consistency with the general recommendation that capital-market users be recognised as the key stakeholders of IFRS standard-setting, one could rather imagine a broad principle that the combined experiences of the IASB members remain representative of the geography of global capital markets as measured by countries' market capitalisations. By contrast, rather rigid rules such as the one proposed risk become obsolete very quickly.

[10] See for example the International Corporate Governance Network's successive comment letters of 19 March and 18 June 2008, on www.icgn.org.

One may keep in mind that Japan represented over a third of global market capitalisation in the late 1980s, and that Asia could well overtake either North America or Europe by this criterion in the decade to come. Rather than having to change the geographical rule at each Constitution Review to adapt it to such market developments, a more flexible principle would appear advisable.

7. Policy Recommendation

The Constitution is the IASC Foundation's most august document. An organisation that seeks public accountability should envisage bringing changes to such a document only under unimpeachable due process, especially if the changes are themselves about organising formal channels of accountability. The introduction of checks and balances is unlikely to be successful if done in a rushed or authoritarian manner.

Such changes are indeed necessary. The Trustees cannot credibly remain a self-appointed group over the mid-term. But they are not urgent, and should be thought of thoroughly.

Establishing a new body above the Trustees, even if initially tasked only with approving their appointments and reappointments (a significant power by itself), creates the distinct possibility that this body would at a later stage grow its scope of responsibility to include items such as the Foundation's funding and/or future Constitution revisions. Such a body should be governed by the Constitution itself, absent which the risk of loss of independence of the Foundation and institutional dysfunction would be high. It should include a broad representation of IFRS standard-setting's key stakeholders and particularly of users, or alternatively there could be several bodies entrusted with parallel powers to represent different groups of stakeholders.

This is not a straightforward debate. There is no meaningful existing precedent to build upon. Identifying the best option and creating sufficient consensus about it is bound to take some time. In this context, the 'fast-track' approach envisaged for the creation of the Monitoring Group appears misguided and should be reexamined by the Trustees. Taking into account current political dynamics in the US and in Europe, there is no convincing rationale for a timetable that would not include the necessary broad public debate. In any event the current concept of the Monitoring Group, which neglects investors and other users and submits the Trustees to the control of a group outside the Constitution's scope, must be reconsidered.

My recommendation is for the Trustees to take a step back and to include the creation of the Monitoring Group (or of a likewise oversight body under a different name: the power to appoint and reappoint Trustees goes beyond mere monitoring) in a comprehensive, one-phase Constitution Review to start in the autumn of 2008 and to be completed in 2009. The oversight body or bodies should be based on a clear assertion of the centrality of capital-market users in the Foundation's stakeholder base.

Far from causing a loss of momentum, such a decision would highlight the Trustees' concern for the legitimacy of their process and would enhance their public profile as well as the prospect for successful adoption of IFRS in the US and other jurisdictions. By contrast, keeping the current proposal unchanged would introduce unnecessary risks to the sustainability of an otherwise highly successful IFRS project.

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