

30 Cannon Street
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31 January 2011

Dear Sir/Madam,

IFRS Future Strategy – Consultation Response

We welcome the Trustees' consultation regarding the future strategy of the IFRS Foundation. This is well-timed given the transition on the IFRS board later this year and the scope this offers to step back and review.

By way of background, Hermes is one of the largest asset managers in the City of London. As part of our Equity Ownership Service, we also respond to consultations on behalf of many clients from around Europe and the world, including Highland Good Steward (USA), the Lothian Pension Fund, The National Pension Reserve Fund of Ireland, PNO Media (Netherlands), Canada's Public Sector Pensions Investment Board and VicSuper of Australia (only those clients which have expressly given their support to this response are listed here).

We answer the specific questions in the consultation paper below.

Yours sincerely,



Paul Lee
Director

Response to the IFRS Foundation Trustees' future strategy review

Mission: How should the organisation best define the public interest to which it is committed?

1. The current Constitution states, "These standards [IFRSs] should require high quality, transparent and comparable information in financial statements and other financial reporting to help investors, other participants in the world's capital markets and other users of financial information make economic decisions." Should this objective be subject to revision?

As we have indicated in prior letters, both to the IFRS Foundation and to the IASB, we are firmly of the view that the purpose of the IFRS standards must be to generate information of use to investors. We believe furthermore that standards should be designed around the needs of current shareholders. We believe that the information needs of lenders and other stakeholders are a subset of the information needs of equity providers; as owners of businesses, equity providers share in the marginal returns of the enterprise as they are generally the most subordinate class of stakeholder. We believe that the clarity and simplicity which will come from designating the perspective of current shareholders alone as primary would be extremely valuable in the future development of Financial Reporting Standards. This would lead to Standards requiring a high baseline of information which would serve the needs of all stakeholders.

2. The financial crisis has raised questions among policymakers and other stakeholders regarding the interaction between financial reporting standards and other public policy concerns, particularly financial stability requirements. To what extent can and should the two perspectives be reconciled?

Prudential regulators have much greater access to information than that available to investors in the public markets; unlike investors, they are not reliant on publicly available data and information produced according to IFRS standards. We therefore believe that the needs of such regulators should not influence the information which the public markets receive, and are clear that IFRS standards should not be written with the needs of regulators in mind; they must be written for the benefit of investors.

An issue which the crisis has highlighted is the need to join up accounting and auditing standards. It has become apparent that too many accounting standards are written with little attention paid to how the reporting by companies can be effectively audited. We therefore believe that accounting standard-setting needs to incorporate some concept of the need for the auditability of reporting under those standards such that users can have greater confidence in the information with which we are presented.

Governance: how should the organisation best balance independence with accountability?

3. The current governance of the IFRS Foundation is organised into three major tiers: the Monitoring Board, IFRS Foundation Trustees, and the IASB (and IFRS Foundation Secretariat). Does this three-tier structure remain appropriate?

We are comfortable with the 3 tier structure. In particular, we believe that it is important to have a buffer between the IASB and the political influence which the Monitoring Board might represent, so as to maintain the confidence of the markets. This requires a robust IFRS Foundation to provide that buffer.

4. Some stakeholders have raised concerns about the lack of formal political endorsement of the Monitoring Board arrangement and about continued insufficient public accountability associated with a private-sector Trustee body being the primary governance body. Are further steps required to bolster the legitimacy of the governance arrangements (including in the areas of representation of and linkages to public authorities?)

We believe that the structure is appropriate and that the legitimate parties are represented on the Monitoring Board, which has appropriate and sufficient political legitimacy. If other organisations feel they need input on the Monitoring Board they should consider how to input their views through the existing members or formally propose an expansion of the Monitoring Board.

Process: how should the organisation best ensure that its standards are high quality, meet the requirements of a well functioning capital market and are implemented consistently across the world?

5. Is the standard-setting process currently in place structured in such a way to ensure the quality of the standards and appropriate priorities for the IASB work programme?

We believe there should be much more field-testing of ideas in the market before they are proposed, such that the proposals are practical and effectively carry through the IASB's intent. Staff should prepare descriptions of the impacts of proposals in practical cases, so that users can consider concretely whether the proposals assist them in their work, rather than needing to interpret the implications of abstract concepts.

In a similar way, we believe that the Board should more actively solicit input from the market about standards which currently include problematic areas and should thus be priorities on the agenda. There should not be change for its own sake, only where there is an actual need. We believe the shift of focus away from a convergence agenda will assist a move to focus the agenda on issues which need to be addressed, not just those required to deliver convergence or adoption.

Implementation reviews need to be active processes which are considered and seek to uncover practical problems with standards and the implementation of standards. There may be aspects of standards which can and should be dropped altogether as well as others which need amendment.

6. Will the IASB need to pay greater attention to issues related to the consistent application and implementation issues as the standards are adopted and implemented on a global basis?

As indicated above, we would welcome the board moving towards more active consideration of such practical issues. We believe that standards need to be auditable and capable of application in practice without excessive additional work. These two requirements are likely to lead to greater consistency in the adoption and implementation of standards.

It is important to note that poor adoption and implementation may be evidence of a poor standard, not just failures on the part of those attempting to implement that standard.

Financing: how should the organisation best ensure forms of financing that permit it to operate effectively and efficiently?

7. Is there a way, possibly as part of a governance reform, to ensure more automaticity of financing?

We would welcome the creation of a system whereby those markets which apply IFRS provide the consistency of funding which the IASB requires in order to deliver high quality standards.

Other issues

8. Are there any other issues that the Trustees should consider?

We continue to be firmly of the view that membership of the IASB should be determined by quality and skills rather than by geographical origin.

We believe that the Trustees will need to consider over time how to bring the governance of the IAASB together with that of the IASB because we do not believe that the IAASB being part of IFAC is sustainable for much longer. Such a move is also likely to assist efforts to ensure that accounting standards are auditable.