Monday 18 April, 2011

Dear Sirs,

**IFRS Foundation Monitoring Board review of the IFRS Foundation’s Governance**

We welcome the opportunity to comment on the IFRS Foundation Monitoring Board’s 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 (Hermes EOS), we also respond to consultations on behalf of many clients from around Europe and the world, including the National Pension Reserve Fund of Ireland, VicSuper, Pensioenfonds PNO Media, Canada’s Public Sector Pension Investment Board and the Lothian Pension Fund (only those clients which have expressly given their support to this response are listed here).

We firmly agree with the Monitoring Board’s identification of the two issues of independence and accountability as crucial to the governance of the IFRS Foundation and indeed of the IASB itself. We are strong supporters of the existence of the IFRS Foundation because we agree with the Monitoring Board that the Foundation is the principal structure through which the independence of the IASB and its decision-making are bolstered.

We note that it is the Monitoring Board’s view that it is its own role to ensure accountability; we are less in agreement with this analysis. Accountability is important, but that accountability must be to the right parties, and while the Monitoring Board is solely composed of capital market regulators it is not clear that it delivers accountability in a broad sense. We would note that all parties recognise that the most important constituency in the development of accounting standards is the investment community. We believe that the IFRS Foundation, through its current membership and availability for dialogue, delivers accountability to this constituency more effectively than does a Monitoring Board solely constituted of capital markets regulators. We believe that the Monitoring Board need to have a broader understanding of how genuine accountability to appropriate parties is to be achieved.

We answer the more detailed questions below.

Yours sincerely,

Paul Lee
Director
Question 1
Do you agree with the proposal to urge concrete efforts to deepen the pool of candidates for IASB membership from diverse geographical and professional backgrounds? Please provide reasons for your agreement/disagreement.

We firmly believe that the IASB is currently sufficiently geographically diverse. We are strongly of the view that membership of the IASB should be driven by ability and relevant skills rather than by any geographical quota system or its equivalent. The drive to have a mix of individuals with ability and relevant skills may lead to a greater diversity of professional backgrounds but we do not think that any further internationalisation of the board’s membership would be of any particular help to the quality of its decisions.

Question 2
Do you agree with the proposal to separate the roles of the IASB Chair and the CEO of the IFRS Foundation, and if so would you have suggestions on how to formalize this? Please provide reasons for your agreement/disagreement.

and

Question 3
Do you agree that clearer division of responsibility between staff dedicated to the IASB operations and staff dedicated to the Foundation’s administrative and oversight functions should be considered, and if so would you have suggestions on how to formalize this? Please provide reasons for your agreement/disagreement.

We agree that the roles of CEO of the Foundation and chair of the IASB should not be combined. But our reasoning is different from that of the Monitoring Board. In our view, the IFRS Foundation is not an executive organisation; rather it is an oversight body, made up of non-executives with a secretariat function. It does not seem appropriate to us for the organisation to have a CEO at all which we fear may blur the Foundation’s independent oversight. The CEO role which the Monitoring Board refers to sounds more to us like a COO role, and a COO role of the IASB rather than one of the Foundation; this COO role could and should be accountable to the IASB chair in our view. The secretariat function for the IFRS Foundation would need to be independent of IASB management structures in order to maintain clarity of its independence, but this would be a relatively small resource focused solely on providing support to the IFRS Foundation’s meetings and decision-making.

Question 4
Please provide comments on any aspects of Trustee composition or appointments that you believe the Monitoring Board should consider.

We note the discussion on the composition of the Trustee board and would simply indicate that the need for geographical and professional diversity which the Monitoring Board notes effectively emphasises the point we have made above about the very significant role which the IFRS Foundation plays in ensuring the accountability of the IASB standard-setting process.

Question 5
Do you agree with the proposal to provide increased transparency into the process for Trustee nominations? Please provide reasons for your agreement/disagreement. To what extent should the Monitoring Board be involved in the nomination process?

Do you agree that further clarification of criteria for the Trustees’ candidacy would help support confidence of the stakeholders? Please provide reasons for your agreement/disagreement.

We agree that greater transparency over the process for nominations and the criteria for candidacy would be helpful.
Question 6
(1) Should the membership of the Monitoring Board continue to be confined to capital markets authorities responsible for setting the form and content of financial reporting in respective jurisdictions?

We note that the Monitoring Board will only deliver one form of accountability while it is constituted solely of capital markets regulators. However, we believe that the IFRS Foundation delivers the necessary accountability to investors and the markets as a whole and so are content to see the Monitoring Board continue to be made up solely of capital markets authorities.

(2) Do you agree with the proposal to expand the Monitoring Board’s membership by adding a mix of permanent members ([four]) representing primarily major emerging markets and rotating members ([two]) from all other markets? Please provide reasons for your agreement/disagreement. How should the major markets be selected? Should a jurisdiction’s application of IFRSs and financial contribution to standard-setting play a role?

We believe that the proposals will create a board which is at the large end and so risks its effectiveness, but we think that a mix of permanent and rotating members is probably appropriate.

(3) Do you agree that rotating members should be selected through IOSCO? Please provide reasons for your agreement/disagreement.

We have no reason to believe that it would be anything other than appropriate for IOSCO to be the vehicle for selecting the rotating members.

Question 7
Do you agree that the Monitoring Board should continue to make its decisions by consensus? Please provide reasons for your agreement/disagreement. Are there any types of decisions taken by the Monitoring Board for which voting other than by consensus (for example, by qualified majority) may be appropriate? If so please describe why and suggest an appropriate voting mechanism.

We have no reason to believe that it would be anything other than appropriate for the Monitoring Board to continue to act by consensus.

Question 8
To ensure increased involvement of public authorities and other international organizations in Monitoring Board activities, do you support the Monitoring Board (a) expanding the number of Monitoring Board observers, (b) holding more formalized dialogue, or (c) establishing an advisory body, and on what basis? What should be the criteria for selecting participants?

and

Question 9
Do you believe that the current arrangements for the standard-setting process adequately ensure the appropriate involvement of all relevant stakeholders and that all relevant public policy objectives are taken into account? Please provide reasons for your agreement/disagreement.

We do not favour any further increase in the involvement of prudential regulators in the Monitoring Board or the IASB and so do not support any of the proposals for observers, formal dialogue or an advisory body. We fear that any further involvement risks undermining investor confidence in IASB standards and the reporting carried out under them. On the contrary, we are firmly of the view that the current arrangements adequately ensure the appropriate involvement of relevant stakeholders and that all relevant policy objectives are taken into account.
Question 10
What are the appropriate means and venues for the Monitoring Board to enhance the visibility and public understanding of its activities?

We would welcome the Monitoring Board itself becoming more publicly accountable in the ways it outlines.

Question 11
Do you believe that the current arrangements for Monitoring Board involvement in the IASB’s agenda-setting are appropriate, or should the Monitoring Board have an explicit ability to place an item on the agenda, or would you consider other alternatives that would enhance the Monitoring Board involvement in the IASB agenda setting? Please provide reasons.

We would strongly oppose the Monitoring Board having any further involvement in IASB agenda-setting. Our firm view is that this would go too far in undermining the independence of the IASB and so also risks undermining investor confidence in IASB standards and the reporting carried out under them.

Question 12
Do you have concrete suggestions on how the Monitoring Board or the Trustees could encourage a move towards a more stable and independent funding model?

It has long seemed to us that the IASB can only gain consistent funding by benefiting from a levy on all organisations which apply IFRS. In practice, this may involve a levy on those capital markets which apply the standards.

Question 13
(1) Do you believe that the Monitoring Board should have a more prominent role in the selection of the IASB Chair? Do you agree with the proposal that the role include involvement in establishing a set of publicly disclosed criteria for the Chair, and assessment of a short list of candidates against those criteria? Please provide reasons.

We do not believe the Monitoring Board should have a greater role in appointing the IASB chair. As the Monitoring Board itself notes, this risks undermining investor confidence in the independence of the IASB; indeed there have been such questions raised in relation to the recent appointment of a new chair of the IASB.

(2) Do you believe that the Monitoring Board should be given any further, specific role in the selection of the IASB Chair? In particular, should the Monitoring Board approve the Trustees’ final selection? Please provide reasons.

For these same reasons of the need to maintain confidence in the IASB’s independence we do not believe the Monitoring Board should have any further role in appointing the IASB chair; in particular this should not include approving the final selection – in practice such a power would give the Monitoring Board very substantial influence over the selection and appointment.

Question 14
Do you agree that the Monitoring Board’s responsibilities should explicitly include consultation with the Trustees as they further develop the framework to ensure proper balance in the composition of the IASB? Please provide reasons for your agreement/disagreement.

We again believe that this proposal risks undermining investor confidence in IASB standard-setting and the reporting carried out under IFRS.
Question 15
Do you agree with the proposal to consider establishing a permanent secretariat for the Monitoring Board to support its increasing roles in overseeing the governance of the standard-setter? Would you support this proposal even if it would require additional financial contributions from stakeholders? Please provide reasons.

We are not convinced that the scale of the role of the Monitoring Board in practice requires a secretariat beyond that which can be provided by small allocations of time from staff of each of the members of the Monitoring Board.

Question 16
Do you agree with the need for regular reviews, and the interval of five years as a benchmark? Should the reviews be aligned with the timing of the Foundation’s mandated Constitution reviews? Please provide reasons for your agreement/disagreement.

A review after 5 years seems appropriate. We would certainly welcome these issues not being reopened again for some time so that the markets can gain confidence in the structures and approach now in place.

Question 17
Do you have any other comments?

No further comments.