

International Accounting Standards Board  
US Financial Accounting Standards Board  
via website

July 19<sup>th</sup> 2010

Dear Sir/Madam

We are pleased to have the opportunity to comment on the joint Boards' Exposure Draft *Conceptual Framework for Financial Reporting: The Reporting Entity*.

By way of background, Hermes is one of the largest asset managers in the City of London. As part of our Equity Ownership Service (EOS), we respond to consultations on behalf of a number of institutional investors – pension funds and others – from the US, Australia and Canada, as well as across Europe. We assist these clients to act as good owners of the companies in which they invest and help represent their interests in public policy debates around the world, seeking a financial system which works in the interests of long-term investors. We currently have around \$92 billion assets under advice.

We welcome the Boards' responsiveness to earlier comments which we and others have made in response to the earlier Discussion Paper and Exposure Draft on the overall Conceptual Framework. We note the very positive changes made and believe that the second half in particular of paragraph RE2 much more effectively captures the need users have for good reporting from entities, to help them make decisions about providing resources and assessing how efficiently and effectively those resources have been used by management. This is not least so that investors can assess the likelihood with which management will be efficient and effective in using those resources going forwards.

We believe though that in this area lies the core of our ongoing concern about the proposals: that for this approach to make sense (and to repeat, we believe it is the correct approach) it requires a line of accountability of a management and governing board to investors, and for this accountability to be effective requires appropriate transparency.



We believe that there are two implications of this need for clarity over the line of accountability between the management and investors:

1. We do not believe that it makes sense to aggregate into the figures reported by the parent company the entire performance of operations where there are minority interests. While we recognise a desire to avoid structuring of legal ownership so as to mask performance, we fundamentally believe that the performance of management is also at risk of being masked where the performance of the business which they control is disclosed including performance that is in fact to the benefit of other parties. We believe that both shareholders and bond investors need to understand the performance of the business which is available for distribution to them, not that which is only available for others to benefit from. Including minorities risks masking the transparency of the performance of management and we need to be reassured that it will be possible for users to disaggregate the information in corporate reports. We are therefore firmly of the view that the understanding of the term 'entity' needs to be read such that minority interests can be excluded from the principal performance reporting for investors.
2. We believe that care is needed in consolidation based on a control criterion. With regards to investment businesses, the performance of the management which matters is the value which they derive from investment management activities and that must not be made less transparent through being masked by consolidating all elements of the circumstances of the underlying investments. It is on the basis of this performance for which management is accountable to investors, and it would be extremely unhelpful to have that performance swamped by the consolidation of every vehicle and asset which is managed by the investment team.

We would welcome further discussion on these issues if that would be of assistance to you.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Paul Lee', written over a horizontal line.

Paul Lee  
Director