

Meeting notes – Management Commentary Consultative Group

The Management Commentary Consultative Group (Consultative Group) held its first meeting on 28 September 2018 at the London offices of the International Accounting Standards Board (Board).

Recordings of meeting discussions, the agenda and related papers are available on the [meeting page](#). For more information on the Management Commentary project please refer to the [project page](#), and details of the Consultative Group can be found [here](#).

Members discussed the following topics:

- Overall approach to the project (paragraphs 1—7);
- Objective of management commentary (paragraphs 8—17);
- Application of materiality (paragraphs 18—20); and
- Principles for preparing management commentary (paragraphs 21—27).

Overall approach to the project

1. Hans Hoogervorst and the staff provided a brief introduction which included:
 - (a) an overview of the approach to the project;
 - (b) the reasons for undertaking the revision of IFRS Practice Statement 1 *Management Commentary* (Practice Statement), namely:
 - (i) gaps in current reporting practice;
 - (ii) recent developments in corporate reporting; and
 - (iii) concerns with short-term focus; and
 - (c) the focus and structure of the meeting's discussion.
2. Members expressed their support for the Board undertaking the Management Commentary project and, overall, they agreed with an approach to the revision of the Practice Statement that is based on the *Conceptual Framework for Financial Reporting (Conceptual Framework)*, and focuses on users' assessments of future cash flows and stewardship of economic resources.
3. Some members, especially standard setters, expressed a preference for the Practice Statement to become mandatory, at least as a future aspiration that might be achieved in stages. However, most members recognised that mandating it would be a challenge in the short term.
4. Some members stated that the principles developed for management commentary should be capable of application to other types of corporate reporting. They stated that this would help keep the Practice Statement relevant as different forms of reporting evolve, and encourage more uptake of the Practice Statement. Some members said that the Board should keep in mind the use of

technology in delivering information that possesses the qualitative characteristics of useful financial information. This could include using different presentation formats, such as infographics and online presentation, to address the reality that new generations of users consume information differently and not in a traditional printed format.

5. Members expressed an expectation that this project and the Practice Statement should be linked to other projects by the Board, such as the project on Primary Financial Statements, and reflect similar principles.
6. Some members emphasised that the Board needs to keep in mind that the preparers of management commentary are not restricted to accountants or members of the finance team. Others across the company will need to be involved and engaged in its preparation to address the different elements which contribute to business success. This may need to be acknowledged in the Practice Statement but also considered when drafting the Practice Statement so that the language and terminology are simple and understandable.
7. In response to the topics chosen for discussion in the meeting, some members highlighted that the guidance in the Practice Statement on achieving qualitative characteristics identified in the *Conceptual Framework* should specifically include a discussion of verifiability. Members representing users emphasised they want information to be reliable and easily corroborated, and also expressed an appetite for management commentary to be subject to assurance, which they considered would make management commentary more useful.

Objective of management commentary

8. The staff outlined the approach to updating the objective of management commentary, which sets out in more detail than the existing Practice Statement how the objective can be achieved, and aligns with the *Conceptual Framework's* focus on the assessments of prospects for future cash flows and of stewardship of the entity's economic resources. The staff's suggested approach also considered both the information that users need and the matters that management considers important for the success of the entity. Illustrative drafting for the revised Practice Statement did not make explicit reference to value creation or different time horizons.
9. Members agreed that the objective of management commentary should be consistent with the objective of other forms of financial reporting and targeted towards the same primary users as for financial statements, as defined in the *Conceptual Framework*. Some noted that the Practice Statement should emphasise that management commentary and the financial statements are treated as one package (including when making the materiality assessment).

10. Some members commented that there should be no separation or distinction between information that users need and matters that management considers important, but instead the emphasis should be on users' information needs and on ensuring that the information provided relates to what is important for the success of the entity.
11. A few members also expressed a view that explicit references in the Practice Statement to value creation and different time horizons, particularly 'long-term', would be helpful, because a reference only to cash flows may not be sufficient to capture the information needed. A few members suggested that management could be asked to provide their definition of short, medium and long term for the entity.
12. Some members also stated that an entity's purpose and its business model should be the starting point for a management commentary from which other content follows, including long-term strategy, performance metrics (the measures of the entity's success) and the related incentivisation for management.
13. Members agreed that disclosures on risks and risk management, which allow users to see how they could affect an entity in meeting its strategic objectives, needed to be prominent in management commentary and some said that such disclosures should be further emphasised in the Practice Statement.
14. Several members highlighted that guidance on communication principles, such as understandability and conciseness, would be helpful and may merit inclusion within the discussion of the objective. A few members noted that duplication of information and lengthy reports were problematic issues they encountered in their analysis of reports, so guidance to address this would be welcome.
15. The discussion on future net cash inflows included reference to discounted cash flow valuation methodology which would capture the cash flows into perpetuity and long-term view of the entity. However, a few members said that management commentary should also provide information on capital structure and capital allocation, which would not be captured by reference to such valuation methodology. Some also noted that care was needed on the wording used in the Practice Statement on future cash flows so as not to be misinterpreted as a need to disclose forecasts.
16. Other areas which members highlighted as needing careful phrasing or wording in the Practice Statement included:
 - (a) the term 'operational information'—while some agreed that it was preferable to using the term 'non-financial information' or 'ESG'¹ (which may be interpreted too narrowly), others were

¹ Environmental, social and governance information

concerned that it may be confusing to have a new term and it may not capture what it is intended to, due to its current usage for internal operations;

- (b) the assumed knowledge of users—one member felt some wording implied that the users of management commentary had less knowledge than users of financial statements, and another suggested that preparers should not assume that users of the management commentary have no knowledge of the entity, as there are other sources of information available through the internet and investor relations channels.

17. There were various views on what the Practice Statement should include about forward-looking information. Some members felt there should be an emphasis on prospective information and were interested in what management decides to highlight, but others felt that providing such information could be sensitive or lead to litigation.

Application of materiality

18. The staff presented their suggested approach to the section in the Practice Statement on applying materiality. This referred to the *Conceptual Framework* and IFRS Practice Statement 2 *Making Materiality Judgements* (Materiality Practice Statement). To determine what information to disclose (step one of the approach described in the *Materiality Practice Statement*), a two-tiered approach, of first identifying the matters which are significant to management commentary and then the material information on those matters, was suggested.
19. Members agreed that the Materiality Practice Statement and the *Conceptual Framework* should be the basis for the approach to materiality for management commentary, but examples and supplemental guidance applicable to management commentary should be provided. Moreover, some members agreed that the guidance could include separating consideration of matters from the identification of material information on those matters. Some members found that the use of 'significant matters' could be confusing or pose translation issues, and thought that a distinction between 'significant' and 'material' is best avoided.
20. Some members highlighted that there are different perspectives on what is material, but agreed that the focus should be on what is material for assessments by the primary users. A few members suggested that the Practice Statement should emphasise that the assessment of materiality for management commentary needs to take into consideration forward-looking information.

Principles for preparing management commentary

21. The staff gave an overview of the principles that were chosen for discussion at this meeting:
- (a) completeness and coherent narrative;

- (b) neutrality; and
 - (c) other matters, including comparability and other published information about the entity.
22. When discussing completeness of management commentary, members agreed with the concept of narrative coherence which includes alignment with the financial statements and other sources of information, as well as coherence throughout the 'story' presented in the management commentary. However, they noted that clearer terminology may be needed in the Practice Statement as coherence could be interpreted to only mean understandability.
23. The Consultative Group also discussed other practical considerations for assessing completeness by reference to information used in other capital market communications or for internal decisions, and knowledge of external factors and insights from other stakeholders. Some members said that the information considered by an entity's board should be included in its management commentary (because they were of the view that such information would be material), and that better alignment was needed between segmental disclosures in the notes and management commentary.
24. A few members were of the view that there was an overlap between the guidance for completeness and that for materiality, and suggested that some parts of the discussion would fit better in the section on materiality.
25. On neutrality, some noted that specific guidance was needed on aggregation and disaggregation of information. Others also suggested using the phrase 'fair, balanced and understandable'.
26. When discussing comparability, some members raised concerns on a requirement for comparability with or reconciliations to industry measures and other measures commonly provided by peers as this could lead to having to disclose sensitive information. In relation to trend information, a few members emphasised that the Practice Statement should be clear that this relates to historical information.
27. There were differing views on whether the entity's website could be used for standing data instead of repeating it annually in management commentary. The majority agreed there was a need for a historical record and trail, which would not be possible on a website. Some members also noted that local regulatory requirements may prevent entities from excluding such information from management commentary.

Next steps

28. The staff will consider the feedback from the Consultative Group in preparing the agenda papers for discussion by the Board at its meetings from November onwards. The next Consultative Group meeting is on Friday 11 January 2019.