

STAFF PAPER

March 2020

IASB® Meeting

Project	Management Commentary		
Paper topic	Cover paper		
CONTACT(S)	Jelena Voilo	jvoilo@ifrs.org	+44 (0)20 7246 6914
	Yulia Feygina	yfeygina@ifrs.org	+44 (0)20 7332 2743

This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (Board) and does not represent the views of the Board or any individual member of the Board. Comments on the application of IFRS® Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Technical decisions are made in public and reported in IASB® *Update*.

Purpose of this paper

1. This paper:
 - (a) provides a recap on the Management Commentary project (paragraphs 2–5);
 - (b) introduces Agenda Papers to be discussed at this month’s meeting (paragraph 6); and
 - (c) sets out the staff’s plans for discussing the remaining topics:
 - (i) sequencing of topics (paragraphs 7–10);
 - (ii) approach to developing guidance (paragraphs 11–12); and
 - (iii) next steps (paragraph 13).

Recap

2. In November 2017, the International Accounting Standard Board (Board) added to its work plan a project to revise IFRS Practice Statement 1 *Management Commentary* (Practice Statement).
3. In July 2018, the Board established the Management Commentary Consultative Group (Consultative Group). The Consultative Group met four times and discussed potential guidance for inclusion in the revised Practice Statement. The staff also

sought input on particular topics from the Accounting Standards Advisory Forum (ASAF), Capital Markets Advisory Committee (CMAC) and Global Preparers Forum.

4. To date, the Board has discussed the following topics:
 - (a) the objective of management commentary (November 2018);
 - (b) the staff's approach to revising the Practice Statement (May 2019);
 - (c) guidance on the characteristics of useful information in management commentary, including:
 - (i) relevance and materiality (July 2019);
 - (ii) completeness and neutrality (September 2019);
 - (iii) comparability, verifiability and understandability (October 2019); and
 - (d) particular aspects of guidance on the business model (October–November 2019).
5. A summary of the Board's discussions and tentative decisions to date is included in the appendix to this paper.

Papers for this meeting

6. At this month's meeting, the staff present:
 - (a) Agenda Paper 15A *The objective of management commentary*. This paper builds on the Board's initial discussion of the objective in November 2018 and asks the Board for decisions.
 - (b) Agenda Paper 15B *Disclosure objectives*. This paper considers disclosure objectives for particular types of content in management commentary. This paper does not ask the Board for decisions. However, the staff will welcome Board members' comments on the ideas presented in the paper. The staff will also discuss disclosure objectives at the March 2020 CMAC meeting and April 2020 ASAF meeting. The staff plan to ask the Board for decisions on disclosure objectives when discussing individual topics at future meetings (see paragraph 11).

Plan for discussing the remaining topics

Sequencing of topics

7. The focus of the Board's discussion at future meetings will be on the types of content that is expected to be covered in management commentary. Given the interaction between topics, the staff plan to discuss them in clusters rather than in isolation. For example, the staff plan to group the following topics together:
 - (a) business model, resources and relationships, strategy and opportunities;
 - (b) operating environment and risks; and
 - (c) performance, position and progress.
8. The order of discussing the topics set out above is not intended to:
 - (a) indicate the structure of the revised Practice Statement. The staff will consider how to organise and present the proposed guidance in the most efficient and reader-friendly way once the Board completes its discussions.
 - (b) prescribe the structure of discussion in management commentary. The guidance on the topics is intended to help preparers determine what information to include in management commentary. It is up to management to decide how it organises that information in its commentary.
9. After the Board has discussed the topics listed in paragraph 7, the staff plan to ask it to discuss the status of the Practice Statement and questions related to identification of management commentary.
10. Finally, the staff plan to ask the Board to consider whether the proposed guidance sufficiently and appropriately addresses topics of particular interest to the Board's stakeholders such as:
 - (a) environmental, social and governance (ESG) matters;
 - (b) intangible resources and relationships; and

- (c) information to help primary users¹ reach conclusions about an entity's long-term prospects.

Approach to developing guidance

11. The staff plan to approach each topic using a consistent template identifying areas that the staff will consider. These areas include:
 - (a) a disclosure objective for the topic that is intended to support the objective of management commentary as a whole. For example, the guidance on discussing an entity's business model could require management to provide information to help the primary users understand how the entity creates value (see Agenda Paper 15B for more information).
 - (b) the main components of disclosure. For example, the guidance on the discussing an entity's business model could require management to cover the entity's structure, its inputs, processes and outputs, and the impacts of its operations.
 - (c) the need for management commentary to provide an overview of the topic. For example, the guidance on discussing an entity's business model could require management to include an overview of the entity's main activities.
 - (d) the principle for identifying 'key' items to be discussed and guidance for applying that principle. For example, the guidance on discussing risks could require management to focus on 'key' risks that could be described as those that can reasonably be expected to affect the entity's ability to generate cash flows or to execute its strategy. The supporting guidance on identifying 'key' risks could, for example, discuss common sources of risks.
 - (e) guidance on the types of information about the identified 'key' items that would be useful to primary users. For example, guidance on discussing

¹ Agenda Paper 15A recommends retaining the statement in the Practice Statement that management commentary is prepared for existing and potential investors, lenders and other creditors. This group of users is referred to as 'primary users' in this paper.

resources could suggest that primary users need information about the availability, depletion and replenishment of the entity's key resources.

- (f) guidance that promotes providing a long-term view in management commentary. For example, the guidance on discussing an entity's strategy could require management to cover the entity's strategy for all time horizons, including over the long term.
- (g) guidance on ESG matters. For example, the guidance on discussing an entity's performance, position and progress could require management to include key non-financial performance metrics that are monitored by management (for example employee satisfaction) and could help primary users understand how ESG matters affect the entity's performance.
- (h) guidance that encourages links to other topics in management commentary. For example, the guidance on performance, position and progress could require management to discuss progress in implementing its strategy.

12. It may not be necessary to cover each area of guidance for each topic. Also, the staff do not plan to ask the Board for decisions on each area of guidance to be included in the Exposure Draft. Instead, the staff plan to:

- (a) ask the Board for decisions on the main aspects of the proposed guidance, such as disclosure objectives or main components of disclosure, and
- (b) invite Board members' comments on other aspects of the proposed guidance, for example on possible disclosures or examples to be considered by management.

Next steps

13. The staff plan that the next discussion with the Board will cover business model, resources and relationships, strategy and opportunities.

Appendix—Summary of the Board’s previous discussions

Ref	Topic and discussion date	Board’s tentative decision(s)
A1	<p>Approach to revising the Practice Statement (May 2019)</p>	<p>The Board noted that the revision of the Practice Statement is intended to promote preparation of management commentaries that better meet the information needs of the primary users of financial reports. The revised Practice Statement will provide guidance that:</p> <ul style="list-style-type: none"> (a) consolidates innovations in narrative reporting; (b) addresses gaps in reporting practice; and (c) remains principles-based but contains sufficient detail to support rigorous application. <p>The Board was not asked to make any decisions.</p>
A2	<p>The objective of management commentary (November 2018)</p>	<p>The staff recommended that the objective of management commentary should be to give context for the financial statements by providing primary users with historical financial and operational information and analysis that is useful in assessing the prospects for the entity’s future net cash inflows, and its management’s stewardship of the entity’s economic resources.</p> <p>The Board did not formally vote at this meeting but agreed in broad terms with that objective, and with the staff’s recommendations for guidance to support it.</p> <p>The Board asked the staff to consider whether it is possible to provide further clarity on:</p> <ul style="list-style-type: none"> (a) the roles that historical information and forward-looking information play in management commentary; and (b) the difference between the objective of management commentary and the objective of financial statements.

A3	Approach to guidance on qualitative characteristics (July 2019)	<p>The Board noted that the plan for the revised Practice Statement is to:</p> <ul style="list-style-type: none"> (a) include a brief description of each qualitative characteristic based on its description in the <i>Conceptual Framework for Financial Reporting (Conceptual Framework)</i>; and (b) provide specific guidance on considering particular qualitative characteristics where such guidance is needed due to the nature of information included in management commentary. <p>The Board was not asked to make any decisions.</p>
A4	Making relevance and materiality judgements (July 2019)	<p>The Board tentatively decided to introduce in the revised Practice Statement guidance on making materiality judgements in preparing management commentary that would:</p> <ul style="list-style-type: none"> (a) incorporate key elements of the guidance from Practice Statement 2 <i>Making Materiality Judgements (Materiality Practice Statement)</i> supported, where necessary, by cross-references to further guidance in the Materiality Practice Statement; (b) provide additional guidance where it is necessary because the nature of management commentary differs from the nature of financial statements; and (c) focus on explaining the materiality process, in particular on identifying material information. <p>Further, the Board tentatively decided that the guidance on identifying material information in the revised Practice Statement would:</p> <ul style="list-style-type: none"> (a) recognise the guidance in the Practice Statement on elements of management commentary (content elements) as a general source of identifying such information; (b) provide the following guidance on considering primary users' common information needs in identifying material information: <ul style="list-style-type: none"> (i) make an explicit link between identification of material information and the objective of management commentary—that is providing information that is useful in assessing the prospects for future net cash inflows to the entity and in assessing management's stewardship of the entity's economic resources; and (ii) describe practical sources that could help management identify matters that may need to be discussed in management commentary. Those sources include the entity's capital markets communications,

		<p>information management uses in managing the business and information identified through engagement with the entity's key stakeholders; and</p> <p>(c) explain how management would consider what information to provide about such matters in each content element to deliver a coherent narrative.</p> <p>Finally, the Board tentatively decided to include in the revised Practice Statement guidance on the other steps of the materiality process that would prompt management to:</p> <p>(a) consider the likelihood of a matter occurring, not just the size of the impact, in assessing the quantitative factors when making materiality judgements;</p> <p>(b) consider the appropriate level of aggregation when assessing what information an entity needs to provide in management commentary; and</p> <p>(c) highlight the links between different pieces of information when organising the information within management commentary.</p>
A4	Faithful representation (September 2019)	<p>The Board tentatively decided that the revised Practice Statement would:</p> <p>(a) include guidance on the qualities that make up faithful representation—completeness, neutrality and freedom from error; and</p> <p>(b) explain that these qualities should be maximised to the extent possible.</p> <p>The Board tentatively decided that the revised Practice Statement would include a description of completeness based on paragraph 2.14 of the <i>Conceptual Framework</i>. In particular, that description would explain that:</p> <p>(a) a complete depiction of a matter should include material information about the nature of that matter and about factors and circumstances that might affect it.</p> <p>(b) completeness of a depiction of a matter is determined by reference to primary users' information needs. To be complete, a depiction of a matter does not necessarily require management to provide all information it has about that matter.</p> <p>The Board tentatively decided that the revised Practice Statement would:</p> <p>(a) require that the management commentary be neutral. To facilitate that:</p> <p>(i) each matter that needs to be discussed in the management commentary should be given due prominence; and</p>

		<ul style="list-style-type: none"> (ii) the overall tone and language used in management commentary should contribute to an unbiased depiction of the entity's performance and position. (b) include a description of neutrality based on paragraph 2.15 of the <i>Conceptual Framework</i>. In particular, that description would explain that, for the depiction of a matter to be neutral, information about it cannot be omitted, obscured, given undue prominence or otherwise be manipulated to influence primary users' view of the matter favourably or unfavourably. (c) require explanatory information to help primary users understand the likelihood of outcomes within a range when the range of possible outcomes is given. <p>The Board also discussed what guidance on freedom from error should be included in the revised Practice Statement but did not make a decision on this topic. The Board also highlighted the importance of using plain language in describing the qualitative characteristics of useful financial information in the revised Practice Statement.</p>
A5	Enhancing qualitative characteristics (October 2019)	<p>The Board tentatively decided that the revised Practice Statement would:</p> <ul style="list-style-type: none"> (a) include a description of comparability reflecting paragraphs 2.24, 2.26 and 2.28 of the <i>Conceptual Framework</i>; (b) explain that although comparability with other entities is desirable, it should not override the requirement to provide relevant entity-specific information; (c) state that in preparing management commentary, an entity's management should consider the fact that primary users need to make comparisons with information provided by other entities, with information reported in management commentary in previous periods and with other information published by the entity; and (d) require an entity's management to: <ul style="list-style-type: none"> (i) explain the assumptions made and methods of calculation used in producing a performance measure, and state whether the performance measure in question is a commonly used metric; (ii) explain any changes since the previous year in those assumptions and methods, and the reason for them; (iii) highlight where new information is provided on a matter reported in previous management commentary;

		<p>(iv) provide comparative information for each performance measure over a period that is long enough to show the emergence of trends; and</p> <p>(v) consider whether information presented in management commentary is consistent with information reported in the entity's financial statements, in investor presentations, in other reports in the public domain, and on the entity's website.</p> <p>The Board tentatively decided that the revised Practice Statement would:</p> <p>(a) include in its discussion of understandability the current guidance in the Practice Statement on presentation;</p> <p>(b) explain that making management commentary concise is an important part of making it understandable;</p> <p>(c) permit the incorporation of information in management commentary by cross-reference, subject to the overarching principle that the information incorporated by cross-reference is part of management commentary and, therefore, must possess the qualitative characteristics of useful financial information. To help management apply the overarching principle, the revised Practice Statement should include guidance:</p> <p>(i) on enhancing the understandability of management commentary when information is incorporated by cross-reference; and</p> <p>(ii) on conditions that must be met by a report when management commentary incorporates information by cross-reference to that report.</p> <p>The Board tentatively decided that the revised Practice Statement would:</p> <p>(a) include a description of verifiability based on paragraphs 2.30 and 2.32 of the <i>Conceptual Framework</i>;</p> <p>(b) require management to:</p> <p>(i) distinguish information based on judgement from factual information; and</p> <p>(ii) explain the process and sources used to produce the information, describe the assumptions and methods used to calculate it, and state the information's limitations; and</p> <p>(c) retain the statement that it does not mandate the level of assurance to which management commentary should be subjected.</p> <p>The Board tentatively decided that the revised Practice Statement would not include guidance on timeliness.</p>
--	--	---

A6	Business model (November 2019)	<p>The Board tentatively decided that the revised Practice Statement should, in explaining ‘business model’, refer to:</p> <ul style="list-style-type: none">(a) value the entity creates for itself. The Practice Statement should also make clear that the notion of value created for an entity is related to the entity’s ability to generate cash flows.(b) the link between an entity’s business model and the entity’s stated purpose.(c) the elements of the business model—that is, inputs, processes and outputs.(d) a business model being a matter of fact and observable through an entity’s actions. <p>The Board also tentatively decided that the Practice Statement should require an entity’s management to discuss indirect wider consequences or impacts of the operation of the entity’s business model if those impacts could affect the entity’s ability to generate cash flows in the future.</p>
----	-----------------------------------	--