

**IASB® meeting**

Project	<b>Management Commentary</b>		
Paper topic	The objective of management commentary		
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**Purpose of this paper**

1. The purpose of this paper is to discuss the objective of management commentary to be included in the revised IFRS Practice Statement 1 *Management Commentary* (Practice Statement). The paper also discusses:
  - (a) how the Practice Statement should describe the primary users of management commentary; and
  - (b) what guidance the Practice Statement should provide to help management meet the objective of management commentary.
2. This paper builds on Agenda Paper 15A *The objective of management commentary* discussed with the Board in November 2018.

**Structure of this paper**

3. This paper is structured as follows:
  - (a) Summary of staff recommendations (paragraph 4);
  - (b) Recap of the November 2018 discussion on the objective of management commentary (paragraphs 5–9);
  - (c) Objective of management commentary, including:

- (i) the link to assessments made by primary users (paragraphs 10–13); and
- (ii) the difference from the objective of financial statements (paragraphs 14–22);
- (d) Primary users and assumed knowledge (paragraphs 23–28);
- (e) Guidance supporting the objective of management commentary, including:
  - (i) management’s view (paragraphs 30–32); and
  - (ii) types of information included in management commentary (paragraphs 33–41);
- (f) Appendix A—Comparison of descriptions of objectives;
- (g) Appendix B—Extracts from the existing Practice Statement;
- (h) Appendix C—Overview of the feedback on the objective of management commentary received from the Management Commentary Consultative Group (Consultative Group);
- (i) Appendix D—Themes identified in other standard-setters’ descriptions of the objective of management commentary; and
- (j) Appendix E—Extracts from other standard-setters’ guidance on the description of the objective of management commentary.

## Summary of staff recommendations

4. The staff recommend that the revised Practice Statement:
  - (a) describes the objective of management commentary as follows:
 

The objective of management commentary is to support primary users in assessing an entity’s prospects for future cash flows and assessing management’s stewardship of the entity’s economic resources by providing useful information and analysis which:

    - (i) enhance the primary users’ understanding of the entity’s performance and position as depicted in the related financial statements; and
    - (ii) give insight into factors that could affect the entity’s prospects.

- (b) retains the statement that management commentary is prepared for existing and potential investors, lenders and other creditors and refers to them as ‘primary users’; and
- (c) explains that primary users are expected to have a reasonable knowledge of business and economic activities and to review and analyse the information diligently, but are not expected to have knowledge of the entity.

### Recap of November 2018 discussion on the objective

5. In [November 2018 Agenda Paper 15A](#) *The objective of management commentary*, the staff presented their analysis and recommendations on the objective of management commentary, and the guidance supporting the objective. In developing those recommendations, the staff sought to:
  - (a) consolidate the guidance related to the objective spread out across different sections of the existing Practice Statement (see Appendix B);
  - (b) align the description of the objective of management commentary with the description of the objective of general purpose financial reporting<sup>1</sup> set out in the *Conceptual Framework for Financial Reporting (Conceptual Framework)*; and
  - (c) make it easier for preparers to understand and apply the objective and for assurers and regulators to enforce compliance with it.
  
6. In November 2018, the staff recommended the following objective of management commentary:
 

The objective of management commentary is to give context for the financial statements by providing primary users of the management commentary with historical financial and operational information and analysis that is useful in assessing the prospects for the entity’s future net cash inflows, and management’s stewardship of the entity’s economic resources.
  
7. The Board broadly agreed with the recommendation but did not formally vote at that meeting. The Board asked the staff to consider providing further clarity on:

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<sup>1</sup> For brevity, in this Agenda Paper ‘general purpose financial reporting’ is referred to as ‘financial reporting’.

- (a) the difference between the objective of management commentary and the objective of financial statements; and
  - (b) the roles of historical information and forward-looking information in management commentary.
8. The Board also encouraged the staff to describe the objective of management commentary using simple language that can be understood by preparers of management commentary who might not be accountants.
  9. Since the November 2018 meeting, the staff have consulted the Consultative Group on the objective of management commentary. Appendix C summarises the Consultative Group’s feedback and explains how the staff considered the feedback in updating the recommendation for the objective.

**Objective of management commentary**

***Link to assessments made by primary users<sup>2</sup>***

10. In November 2018, the staff recommended that the objective of management commentary should explicitly refer to primary users’ assessments of the prospects for future net cash inflows and of management’s stewardship of the entity’s economic resources.
11. The explicit reference to information useful for primary users’ assessments was recommended to align the objective of management commentary with the objective of financial reporting. This is because management commentary is part of financial reporting and so should provide information that contributes to meeting the objective of financial reporting.<sup>3</sup> In addition, in the staff’s view, emphasising the role of management commentary in supporting primary users’ assessments of the entity’s prospects for future cash flows and of management’s stewardship of the entity’s economic resources would make the objective easier to implement. The staff also argued that the reference to those assessments would:

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<sup>2</sup> See paragraphs 23–28 for the staff’s recommendation on describing primary users in the revised Practice Statement.

<sup>3</sup> Appendix A compares the descriptions of the objective of financial reporting, the objective of financial statements and the recommended objective of management commentary.

- (a) help preparers in making materiality judgements;<sup>4</sup>
  - (b) make it clearer that management is responsible for the information that is useful for primary users’ assessments, not for the assessments themselves; and
  - (c) promote a long-term view in management commentary.
12. The staff think that this logic remains valid. In addition, the staff note that a reference to the assessments of prospects for cash flows and of management’s stewardship is a common feature in the description of both the objective of financial reporting and the objective of financial statements (see Appendix A), and the role of management commentary is to support the related financial statements. Finally, as noted in paragraph 7, in discussing the objective of management commentary at the November 2018 meeting, the Board broadly agreed with the staff recommendation and did not raise questions about the proposed reference to the assessments of prospects for cash flows and of stewardship.
13. For the reasons discussed in paragraphs 11–12, the staff recommend including in the description of the objective of management commentary an explicit reference to primary users’ assessment of the entity’s prospects for future cash flows and assessment of management’s stewardship of the entity’s economic resources.

***Note on terminology – ‘cash flows’***

The *Conceptual Framework* and IFRS Standards use the phrase ‘net cash inflows to the entity’ to refer to the cash flows resulting from gross cash inflows to the entity and gross cash outflows from the entity. This technical phrase is rarely used by stakeholders in discussing management commentary, who more commonly refer to ‘cash flows’ or ‘future cash flows’. The staff think that using the simpler phrase ‘future cash flows’ would not confuse the readers of the revised Practice Statement and we plan to use this simpler term in developing recommendations on the project.

The staff will consider in drafting how to introduce the simpler phrase in the exposure draft of the revised Practice Statement and to explain that those cash flows

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<sup>4</sup> See Appendix A of Agenda Paper 15 for this meeting for a summary of the Board’s tentative decisions on materiality.

can be both positive and negative and that the reference to ‘prospects for future cash flows’ is intended to capture the amount, timing and uncertainty of those future cash flows.

### ***Difference from the objective of financial statements***

14. The *Conceptual Framework* states that the objective of financial statements is:
  - ...to provide financial information about the reporting entity’s assets, liabilities, equity, income and expenses that is useful to users of financial statements in assessing the prospects for future net cash inflows to the reporting entity and in assessing management’s stewardship of the entity’s economic resources.
15. As noted in paragraphs 12–13, both financial statements and management commentary seek to provide information useful to primary users in assessing the prospects for future cash flows and in assessing management’s stewardship, so it would be helpful to set out the objective of management commentary in a way that makes it clear how it differs from the objective of financial statements.
16. Financial statements focus on financial information about the entity’s assets, liabilities, equity, income and expenses. Management commentary is intended to support primary users’ understanding of information included in the related financial statements. The existing Practice Statement describes the role of management commentary as ‘providing context for’ and ‘complementing and supplementing’ the related financial statements.<sup>5</sup>
17. The staff think that the basic principle in the existing Practice Statement about management commentary providing context for and supplementing the related financial statement is valid. However, the phrases used in the Practice Statement may be difficult to interpret. For example, it may not be clear what ‘supplemental’ or ‘contextual’ information must be provided. In the staff’s view, it would be helpful to be clarify the role of management commentary in providing useful information in addition to information already provided in financial statements, and how that role is achieved.
18. To clarify this, the staff recommend that the objective of management commentary in the revised Practice Statement states that the role of management commentary is to support

<sup>5</sup> See paragraphs 9, 10 and 16 of the Practice Statement in Appendix B.

primary users' assessments of prospects for future cash flows and of stewardship by providing useful information and analysis which:

- (a) enhance primary users' understanding of the entity's performance and position as depicted in the related financial statements; and
- (b) give insights into factors that could affect the entity's prospects.

19. This proposed clarification of the objective of management commentary—notably the references to 'analysis', 'enhancing understanding' and 'giving insights'—is intended to reflect that management commentary should not simply depict *what* has happened but should also explain *why* it has happened and provide information to help users better understand the *implications* of the transactions, events and conditions in the reporting period for the future. Such information, explanations and analysis:

- (a) provide management's view of the entity's performance, position and prospects; and
- (b) typically include set of information that differs from the information in the financial statements, specifically:
  - (i) more discussion, analysis, descriptions and other qualitative information than financial statements (see paragraph 34);
  - (ii) more information about possible future transactions and events and other forward-looking information than financial statements (see paragraphs 35–39);<sup>6</sup> and
  - (iii) more broad contextual and other non-financial information than financial statements (see paragraphs 40–41).

20. To help preparers apply the objective, the revised Practice Statement could provide supporting guidance on the concept of management's view and on types of information that is included in management commentary to meet its objective (see paragraphs 30–41).

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<sup>6</sup> Forward-looking information may also be included in financial statements but in limited circumstances. Specifically, paragraph 3.6 of the *Conceptual Framework* explains that such information is included in financial statements if both of the following conditions are met:

- (a) the information relates to the entity's assets or liabilities (including unrecognised) or equity, to income or expenses; and
- (b) the information is useful to users of financial statements.

In addition, the staff expect that the revised Practice Statement will set out disclosure objectives for types of content expected to be included of management commentary. Those disclosure objectives will build on and support the objective of management commentary as a whole (see Agenda Paper 15B *Disclosure objectives*).

21. The staff’s proposed clarifications of the objective—in particular, the references to ‘analysis’, ‘understanding of the entity’s performance and position’ and ‘insights into factors that could affect the entity’s prospects’—also feature in descriptions of the objective of management commentary (or a similar report) in reporting frameworks issued by other standard-setters. Appendix D summarises how themes identified by the staff in other standard-setters’ descriptions of the objective may feature in the revised Practice Statement. In addition, Appendix E includes selected extracts from guidance reviewed by the staff that provide a description of the objective of management commentary or a similar report.

***Note on terminology – ‘prospects for future cash flows’ and ‘value creation’***

One theme identified by the staff when reviewing how other standard-setters describe the objective of management commentary or a similar report was the reference to ‘value creation’. In this paper, the staff recommend that the description of the objective of management commentary explicitly refers to the entity’s prospects for future cash flows.

The question may arise how the entity’s prospects for future cash flows relate to the notion of value creation. This question was also raised by some of the members of the Consultative Group.<sup>7</sup>

In developing the guidance on business model, the Board tentatively decided to make it clear that the notion of value created for an entity is closely related to the entity’s ability to generate cash flows. In making that decision, the Board noted that

<sup>7</sup> See paragraph 11 of the [meeting summary](#) of the Consultative Group’s September 2018 meeting. The link between value creation and future cash flows was also discussed by the Consultative Group at its April 2019 meeting (see paragraphs 3 and 21 of the [meeting summary](#))



incorporating the notion of value creation into the guidance on business model would help to promote descriptions of a longer-term view of the entity's business model. As discussed in May 2019 Agenda Paper 15 *Overview of the staff's approach to revision*, supporting the provision of a long-term view in management commentary is one focus area in the Management Commentary project. The staff will also consider whether to refer to value creation in developing the disclosure objective for business model.

November 2019 Agenda Paper 15A *What is business model* noted that the revised Practice Statement would need to focus on the value created by the entity for itself because that value affects returns to primary users. Some see 'value' as wider than value for the entity, and suggest it should cover value created for a wide range of stakeholders other than the primary users, for example, for customers, employees, or society at large. This wider view of value creation is only partly consistent with the Board's focus on primary users. Primary users need information about the impacts of the entity's operations on other parties if those impacts could affect the entity's ability to generate cash flows—and value—in the future.

Given the importance of the notion of value creation to some stakeholders, its common interpretation as relating to a long-term view and the use of that notion in other frameworks, the staff think that the revised Practice Statement should comment on the interaction between the entity's prospects for cash flows that feature in the proposed description of the objective of management commentary and value creation. Specifically, the revised Practice Statement could explain that the notion of value that the entity creates for itself and its shareholders reflects the entity's ability to generate positive net cash inflows after taking into consideration not only the amount but also timing and uncertainty of those cash flows.

22. To conclude, bringing together staff's recommendations in paragraphs 13 and 18, the staff recommend that the revised Practice Statement describes the objective of management commentary as follows:

The objective of management commentary is to support primary users in assessing an entity’s prospects for future cash flows and assessing management’s stewardship of the entity’s economic resources by providing useful information and analysis which:

- (i) enhance the primary users’ understanding of the entity’s performance and position as depicted in the related financial statements; and
- (ii) give insight into factors that could affect the entity’s prospects.

**Question 1 for the Board**

Do you agree with the staff recommendation for the objective of management commentary as set out in paragraph 22?

**Primary users and assumed knowledge**

- 23. The existing Practice Statement states that management commentary is prepared for the primary users of financial reports and identifies them as ‘existing and potential investors, lenders and other creditors’, consistent with the definition of primary users set out in the *Conceptual Framework*. For clarity, the staff recommend retaining that description of primary users of management commentary in the revised Practice Statement.
- 24. Some standard-setters specify a broader range of users for their narrative reports. To explain whether management commentary may also serve information needs of parties other than the primary users, the revised Practice Statement could include a statement based on paragraph 1.10 of the *Conceptual Framework*:
  - Other parties, such as regulators and members of the public other than investors, lenders and other creditors, may also find management commentary useful. However, management commentary is not primarily directed to these other groups.
- 25. In discussing information needs of the primary users of management commentary, some members of the Consultative Group asked about the knowledge of the entity that the primary users are expected to have. Specifically, this question arose in discussing whether management commentary should focus on changes and developments since the previous reporting period, or whether it should also provide information about the entity that didn’t

change (some members referred to such information as ‘standing information about the entity’).<sup>8</sup> A question may also arise whether primary users are expected to have knowledge of the entity from sources other than the entity’s financial reports (for example, from the entity’s website, analysis briefings or the entity’s foundation documents).

26. The staff note that the *Conceptual Framework* explains that primary users ‘are expected to have a reasonable knowledge of business and economic activities and to review and analyse the information diligently’.<sup>9</sup> However, the *Conceptual Framework* does not suggest that primary users are expected to have knowledge of the entity itself either from previous financial reports or from other sources of information about the entity.
27. Accordingly, in the light of the questions raised by the Consultative Group, the staff recommend including in the revised Practice Statement the description of the assumed knowledge of primary users based on the existing description in the *Conceptual Framework* but clarifying that primary users are not expected to have knowledge of the entity.
28. This would mean that management commentary would need to include standing information about the entity in addition to information about what has happened or changed during the reporting period. For example, management commentary for the reporting period would need to include information about the entity’s long-term objectives even if the objectives have not changed during the reporting period and information about those long-term objectives was provided in management commentary for the previous period or in other sources such as the entity’s website.

**Question 2 for the Board**

The staff recommend that the revised Practice Statement:

- (a) retains the statement that management commentary is prepared for existing and potential investors, lenders and other creditors and refers to them as ‘primary users’; and

<sup>8</sup> See paragraph 25 of the [meeting summary](#) of the Consultative Group’s April 2019 meeting.

<sup>9</sup> See paragraph 2.36 of the *Conceptual Framework*.

- (b) explains that primary users are expected to have a reasonable knowledge of business and economic activities and to review and analyse the information diligently, but are not expected to have knowledge of the entity.

Do you agree with the staff's recommendation?

**Guidance supporting the objective of management commentary**

29. As noted in paragraph 20, including in the revised Practice Statement supporting guidance on the objective of management commentary would help preparers apply that objective.

The staff considered what guidance could be included on:

- (a) management's view (paragraphs 30–32); and
- (b) types of information in management commentary (paragraphs 33–41).

***Management's view***

30. The existing Practice Statement states that management commentary should provide management's perspective of the entity's performance, position and progress.<sup>10</sup> That is, management should explain how and why the performance of the entity falls short of, meets or exceeds previous expectations. It should also include management's assessment of the entity's prospects in the light of current period results. The staff think that this description of management's view is consistent with and integral to the objective of management commentary recommended by the staff in paragraph 22 and should be retained in the revised Practice Statement.

31. The existing Practice Statement also states that management commentary should derive from the information that is important to management in managing the business.<sup>11</sup> The Basis for Conclusions explains that the Board considered such information to be a suitable basis for preparing management commentary because it is the same information that is important to capital providers in assessing the entity's performance and prospects. Consistent with that logic, in discussing materiality judgements in this project, the Board tentatively decided that information used by management in managing the business is one source of identifying material information for inclusion in management commentary.

<sup>10</sup> See paragraph 15 of the Practice Statement in Appendix B.

<sup>11</sup> See paragraph 15 of the Practice Statement in Appendix B.

Using this information in preparing management commentary would help preparers meet the objective of management commentary.

32. This topic has been discussed with the Consultative Group and with the ASAF.<sup>12</sup> The members of the Consultative Group generally agreed that management is best placed to know what information is important to the business and that such information provides a suitable basis for preparing management commentary that meets users' information needs. The ASAF members also generally supported the notion of management's view.

***Types of information included in management commentary***

33. The staff think that guidance supporting the objective of management commentary in the revised Practice Statement should explain what types of information will typically be included in management commentary to meet its objective and when that information would be useful to primary users of management commentary.

***Qualitative and quantitative information***

34. Management commentary is often referred to as a narrative report. Some stakeholders expressed a concern that the term 'narrative' may imply that the report only includes qualitative information without financial analysis. To address that concern, the staff think it is important to state in the revised Practice Statement that management commentary includes both qualitative and quantitative information, as well as management's analysis and explanations.

***Historical and forward-looking information***

35. As noted in paragraph 19, management commentary is more future-orientated than the related financial statements. However, it also includes historical information. The staff think it would be helpful to acknowledge in the revised Practice Statement the need for both historical and forward-looking information and to comment on the role and the scope of forward-looking information in management commentary.

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<sup>12</sup> The Consultative Group discussed management's view at its [December 2019 meeting](#) (see paragraphs 30-35 of the [meeting summary](#)). ASAF discussed management's view at its April 2019 (see paragraphs 22–26 of [meeting summary](#)).

36. Historical information relates to past transactions, events and conditions, and is particularly useful in understanding financial performance and position reflected in the financial statements. Historical information in management commentary may also include non-financial information, for example non-financial key performance indicators (KPIs) related to employee satisfaction or retention (see paragraphs 40–41 and note on terminology on page 15).
  
37. Forward-looking information is described in the *Conceptual Framework* as information about possible future events or conditions that could affect the entity’s prospects. The staff suggest using that description in the revised Practice Statement as the basis for explaining forward-looking information, potentially emphasising that forward-looking information includes information about events and conditions that could affect the entity over the long term.
  
38. The existing Practice Statement states that the extent to which management commentary looks forward will be influenced by the regulatory and legal environment within which the entity operates. The staff think that this guidance may be helpful for some preparers, for example in preparing projections and forecasts if such projections and forecasts are included in management commentary.
  
39. The revised Practice Statement could also provide examples of forward-looking information such as information about management’s strategy and expectations, and information about opportunities and risks. Such forward-looking information is intended to help primary users make their own assessments, in particular, the assessment of the entity’s prospects for future cash flows. Other examples of forward-looking information include management’s projections, forecasts and targets. The staff expect to provide guidance on including projections, forecasts and targets in management commentary and will provide analysis and recommendations on this topic in a future paper.

***Note on terminology – ‘forward-looking information’***

During consultations on the project, the staff heard that the term ‘forward-looking information’ may be interpreted differently in different jurisdictions. This term is

used in the existing Practice Statement and in the *Conceptual Framework*, so the staff have used it in this paper and suggested describing it in the revised Practice Statement to reduce the risk of misinterpretation. The staff will consider in drafting whether another term, for example ‘future-orientated information’, is more appropriate and more easily understood.

***Financial and non-financial information***

40. In providing information that is useful for assessing an entity’s prospects for future cash flows and of management’s stewardship, financial statements focus on financial information about the entity’s assets, liabilities, equity, income and expenses. Management commentary is more contextual and explanatory in nature and for that reason it would need to include both financial and non-financial information. The staff think it would be helpful for the revised Practice Statement to spell out that both financial and non-financial information are included in management commentary. The Practice Statement should also explain that non-financial information is included in management commentary when it:
- (a) helps explain financial information for the reporting period; or
  - (b) provides insights into the factors that have already affected the entity or could affect the entity’s ability to generate cash flows in the future.
41. The revised Practice Statement could also provide examples of non-financial information such as production or sales volumes, statistical information about employees, narrative on business locations, and environmental, social and governance metrics such as water usage or health and safety.

***Note on terminology – ‘non-financial information’***

During consultations on the project, the staff have heard that the term ‘non-financial’ might not work well for information that is included in financial reporting and relates to factors or events that could have a financial impact on the entity in the future.

However, this term is used widely in narrative reporting frameworks as well as the existing Practice Statement to refer to non-financial factors, resources, performance and metrics. Some organisations, for example the Global Reporting Initiative and the Chartered Institute of Management Accountants (CIMA), have used alternative terms such as ‘extra-financial’ and ‘pre-financial’ information. ‘Pre-financial’ was used by CIMA to refer to those factors that do not affect an entity’s financial performance in the short-term, but will inevitably have a financial effect over time. In CIMA’s view, using ‘non-financial’ to describe those factors gives the false impression that there will be no medium or long-term financial effect.

The staff have used the term ‘operational’ as an alternative to ‘non-financial’ in previous discussions but feedback from the Consultative Group suggested that this term was confusing and could be interpreted narrowly.

The staff will consider in drafting whether there is a more suitable term than ‘non-financial’.

**Question 3 for the Board**

Paragraphs 29–41 provide staff’s discussion of the supporting guidance on the objective of management commentary that could be included in the revised Practice Statement. Does you have any questions or comments on that discussion?



## Appendix A— Comparison of descriptions of objective

The staff have added emphasis for ease of comparison.

Objective of general purpose financial reporting in the <i>Conceptual Framework</i>	Objective of financial statements in the <i>Conceptual Framework</i>	Recommended objective of management commentary for the revised Practice Statement
<p>1.2 The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity. ...</p> <p>1.3 ... The decisions described in paragraph 1.2 depend on the returns that existing and potential investors, lenders and other creditors expect, for example, dividends, principal and interest payments or market price increases. Investors', lenders' and other creditors' expectations about</p>	<p>3.2 The objective of financial statements is to provide financial information about the reporting entity's assets, liabilities, equity, income and expenses that is useful to users of financial statements in <b>assessing the prospects for future net cash inflows to the reporting entity and in assessing management's stewardship of the entity's economic resources.</b></p>	<p>The objective of management commentary is to support primary users in <b>assessing the entity's prospects for future cash flows and in assessing management's stewardship of the entity's economic resources</b> by providing information and analysis which:</p> <ul style="list-style-type: none"> <li>• enhances the primary users' understanding of the entity's performance and position as depicted in the related financial statements; and</li> <li>• gives insight into factors that could affect the entity's prospects.</li> </ul>

<p>returns depend on their <b>assessment of</b> the amount, timing and uncertainty of <b>(the prospects for) future net cash inflows to the entity and on their assessment of management’s stewardship of the entity’s economic resources</b>. Existing and potential investors, lenders and other creditors need information to help them make those assessments.</p>		
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## Appendix B—Extracts from the existing Practice Statement

### Introduction

#### *What is management commentary*

IN 3. Management commentary is a narrative report that provides a context within which to interpret the financial position, financial performance and cash flows of an entity. It also provides management with an opportunity to explain its objectives and its strategies for achieving those objectives. Users routinely use the type of information provided in management commentary to help them evaluate an entity's prospects and its general risks, as well as the success of management's strategies for achieving its stated objectives. For many entities, management commentary is already an important element of their communication with the capital markets, supplementing as well as complementing the financial statements.

[...]

#### **Users of management commentary**

8. Management should determine the information to include in management commentary considering the needs of the primary users of financial reports. Those users are existing and potential investors, lenders and other creditors.

#### **Purpose**

9. Management commentary should provide users of financial statements with integrated information that provides a context for the related financial statements. Such information explains management's view not only about what has happened, including both positive and negative circumstances, but also why it has happened and what the implications are for the entity's future.

10. Management commentary complements and supplements the financial statements by communicating integrated information about the entity's resources and the claims against the entity and its resources, and the transactions and other events that change them.

11. Management commentary should also explain the main trends and factors that are likely to affect the entity's future performance, position and progress. Consequently, management commentary looks not only at the present, but also at the past and the future.

#### **Principles**

12. Management should present commentary that is consistent with the following principles:

- (a) to provide management's view of the entity's performance, position and progress; and

- (b) to supplement and complement information presented in the financial statements.

[...]

14. Management commentary should provide information to help users of the financial reports to assess the performance of the entity and the actions of its management relative to stated strategies and plans for progress. That type of commentary will help users of the financial reports to understand, for example:

- (a) the entity's risk exposures, its strategies for managing risks and the effectiveness of those strategies;
- (b) how resources that are not presented in the financial statements could affect the entity's operations; and
- (c) how non-financial factors have influenced the information presented in the financial statements.

**Management's view**

15. Management commentary should provide management's perspective of the entity's performance, position and progress. Management commentary should derive from the information that is important to management in managing the business.

**Supplement and complement the financial statement information**

16. Management commentary should supplement and complement the financial statements with explanations of the amounts presented in the financial statements and the conditions and events that shaped that information. Management commentary should also include information about the entity and its performance that is not presented in the financial statements but is important to the management of the entity.

**Forward-looking information**

17. Management commentary should communicate management's perspective of the entity's direction. Such information does not predict the future, but instead sets out management's objectives for the entity and its strategies for achieving those objectives. The extent to which management commentary looks forward will be influenced by the regulatory and legal environment within which the entity operates.

18. Management should include forward-looking information when it is aware of trends, uncertainties or other factors that could affect the entity's liquidity, capital resources, revenues and the results of its operations. Such information should focus on the extent to which the entity's financial position, liquidity and performance may change in the future and why, and include management's assessment of the entity's prospects in the light of current period results. Management should provide forward-looking information through narrative explanations or

through quantified data, which may—but are not required to—include projections or forecasts. Management should disclose the assumptions used in providing forward-looking information.

19. Management should explain how and why the performance of the entity is short of, meets or exceeds forward-looking disclosures made in the prior period management commentary. For example, if management stated targets for future performance in previous reporting periods, it should report the entity’s actual performance in the current reporting period and analyse and explain significant variances from its previously stated targets as well as the implications of those variances for management’s expectations for the entity’s future performance.

**Appendix C—Overview of the feedback on the objective of management commentary received from the Management Commentary Consultative Group (Consultative Group)**

In December 2019, the Consultative Group discussed the objective of management commentary as part of the overall proposals for the revised Practice Statement. The objective discussed at that meeting was: *‘[The objective is to] provide 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 management’s stewardship of the entity’s economic resources as context for the financial statements’*. That wording was based on the description of the objective discussed in November 2018 with the Board.

The following table summarises the feedback received from members of the Consultative Group on that objective and explains how the feedback has been considered in the staff’s revised proposals for the objective.

<b>Feedback</b>	<b>Staff’s response</b>
Suggestion that the description of the objective of management commentary should refer providing context for the financial statements and to fair presentation	<p>As discussed in paragraph 17, the staff agree with the idea of management commentary providing context to the related financial statements. However, in the staff’s view, it may not be clear what type of information is meant by the term ‘context’ or ‘contextual’. Paragraph 18 explains how the staff recommend clarifying what is meant by management commentary providing context to the related financial statements.</p> <p>The notion of ‘fair presentation’ relates to relevance and faithful representation, ie the qualitative characteristics of useful information. The Board already discussed guidance on the qualitative characteristics of useful information in the September and October 2019 Board meetings (see the appendix to Agenda Paper 15).</p>
Query on why the objective of management commentary refers to future cash flows but not to performance and position	The revised objective includes a reference to ‘understanding of an entity’s performance and position’ in addition to the reference to future cash flows.

<p>Suggestion not to use the term ‘operational’ because it could result in too much detail</p>	<p>The staff no longer recommend referring to ‘operational information’ in the description of the objective of management commentary. However, in the guidance supporting the objective the staff suggest:</p> <p>(a) clarifying that management commentary includes both financial and non-financial information (in this paper the term ‘non-financial’ is used instead of ‘operational’ – see the note on terminology on page 15); and</p> <p>(b) explaining when non-financial information is included in management commentary.</p>
<p>Caution on including in the description of the objective a reference to ‘historical information’ without also referring to forward-looking information</p>	<p>The staff no longer recommend referring to ‘historical information’ in the proposed description of the objective of management commentary. The staff suggest that the guidance supporting the objective should discuss the types of information included in management commentary, including both historical and forward-looking information. See paragraphs 35–39.</p>
<p>Suggestion to explain what is meant by the term ‘economic resources’, for example, whether it captures intangible resources not recognised in financial statements or resources not controlled by the entity.</p>	<p>The use of the term ‘economic resources’ in the objective is aligned with the <i>Conceptual Framework</i>. The staff will consider in drafting whether to provide an explanation of the term ‘economic’ resources.</p>

## Appendix D – Themes identified in other standard-setters’ descriptions of the objective of management commentary

In developing proposals for the objective of management commentary, the staff reviewed guidance issued by other standard-setters to identify themes reflected in their descriptions of the objective of management commentary or a similar report (see November 2018 Agenda Paper 15A *The objective of management commentary*).

The staff’s review covered responses from 24 national standard-setters to the staff’s request for information about requirements and commonly applied non-mandatory guidance on management commentary in their jurisdictions.<sup>13</sup> The staff also reviewed EU Non-financial Reporting Directive (2014/95/EU) and the related European Commission Guidelines on non-financial reporting, and the International Integrated Reporting <IR> Framework because some of the respondent jurisdictions either require or encourage management to use them in preparing management commentary.

The following table summarises how themes identified by the staff may feature in the revised Practice Statement.

<i>Theme is other standard-setters’ descriptions</i>	<i>How the theme may feature in the description of the objective in the revised Practice Statement</i>
Context for the financial statements	Paragraphs 17–18 explain that the revised objective will not use the word ‘context’ but will explain that information in management commentary should enhance the primary users’ understanding of the entity’s performance and position as depicted in the related financial statements and give insight into factors that could affect the entity’s prospects.
Management perspective	In paragraphs 30–32, the staff suggest retaining the idea that management commentary should provide ‘management’s view’ and explaining what is meant by the notion in the guidance supporting the objective.

<sup>13</sup> See Appendix A of November 2018 Agenda Paper 15B *Summary of research into the objective of management commentary* for details of the respondents and the survey questions.



<i>Theme is other standard-setters' descriptions</i>	<i>How the theme may feature in the description of the objective in the revised Practice Statement</i>
Information about development, performance and position	The description of the objective clarifies that information is included in management commentary if it enhances the primary users' understanding of the entity's performance and position as depicted in the related financial statements.
Insight into prospects	The description of the objective clarifies that information is included in management commentary if it gives insight into factors that could affect the entity's prospects.
Quality of earnings	The description of the objective of management commentary does not refer to quality of earnings. Provision of information about the quality of earnings is expected to be covered by guidance on performance, position and progress (to be covered in a future paper).
Strategy and risks	The description of the objective of management commentary does not explicitly refer to strategy and risks but the staff suggest that strategy and risks should be listed as examples in the supporting guidance on providing forward-looking information in management commentary.
Resource stewardship <i>(Note: some jurisdictions and the EU Non-Financial Reporting Directive refer to resources outside the entity and to the entity's impact on stakeholders)</i>	<p>The objective of management commentary explicitly refers to providing information for primary users' assessment of management's stewardship of the entity's economic resources.</p> <p>The objective of management commentary is not intended to capture the entity's impacts on the entity's stakeholders' resources, unless those impacts could affect the entity's ability to generate cash flows in the future (see note on terminology on page 8)</p>
Value creation	The staff explain in the note on terminology on page 8 how the notion of 'value creation' will be explained in the guidance supporting the objective.

## Appendix E—Extracts from other standard-setters’ guidance on the description of the objective of management commentary

This appendix includes extracts from other standard-setters’ guidance that provides more detailed descriptions of the objective, as identified from the survey of national standard-setters referred to in Appendix D, as well as extracts from the EU Non-Financial Reporting Directive and the International Integrated Reporting <IR> Framework.

<b>Extracts related to the objective of management commentary</b>
<p><b><i>Australian Securities &amp; Investments Commission Regulatory Guide 247 Operating and Financial Review (OFR)</i></b></p> <p>RG 247.6 An OFR is an important document in meeting the information needs of shareholders. While an entity’s financial report provides useful information about the entity’s financial position and performance, it will rarely provide all of the information needed to readily assess the entity’s financial position and to appreciate the underlying reasons for the entity’s results. It will also provide little, if any, information about business strategies and prospects relevant to future financial performance.</p> <p>RG 247.8 (a) the OFR supplements and complements the financial report in the manner described in RG 247.6;</p> <p>(b) together with the financial report, the OFR allows shareholders to find relevant information on the entity in a single location, rather than having to piece together information from various past continuous disclosure announcements that shareholders may not have necessarily read;</p> <p>(c) depending on the specific circumstances of an entity, the OFR may contain a more or less detailed explanation and analysis of information provided in other formats, such as investor presentations and briefings to analysts.</p> <p>RG247.28 ...b) provide a narrative overview that enables shareholders to understand an entity’s business performance and the factors underlying its results and financial position.</p> <p>RG 247.30 An OFR should present: (a) <i>a narrative</i>—providing tailored information about an entity’s results and financial position. Information in the OFR should be consistent with and complement the financial report; and</p> <p>(b) <i>an analysis</i>—providing a reasoned and meaningful description of the underlying drivers of, and the reasons for, an entity’s performance, rather than simply restating information that may be readily determined from the financial statements.</p>
<p><b><i>Canada’s Form 51-102F1 Management’s Discussion &amp; Analysis (MD&amp;A)</i></b></p> <p>MD&amp;A is a narrative explanation, through the eyes of management, of how your company performed during the period covered by the financial statements, and of your company’s financial condition and future prospects. MD&amp;A complements and supplements your financial statements, but does not form part of your financial statements.</p>

<p><b>Extracts related to the objective of management commentary</b></p> <p>Your objective when preparing the MD&amp;A should be to improve your company’s overall financial disclosure by giving a balanced discussion of your company’s financial performance and financial condition including, without limitation, such considerations as liquidity and capital resources - openly reporting bad news as well as good news. Your MD&amp;A should:</p> <ol style="list-style-type: none"> <li>a. help current and prospective investors understand what the financial statements show and do not show;</li> <li>b. discuss material information that may not be fully reflected in the financial statements, such as contingent liabilities, defaults under debt, off-balance sheet financing arrangements, or other contractual obligations;</li> <li>c. discuss important trends and risks that have affected the financial statements, and trends and risks that are reasonably likely to affect them in the future; and</li> <li>d. provide information about the quality, and potential variability, of your company’s profit or loss and cash flow, to assist investors in determining if past performance is indicative of future performance.</li> </ol>	
<p><b><i>EU Non-Financial Reporting Directive</i></b>  <b>Article 19 a Non-financial statement:</b></p> <p>Large undertakings which are public-interest entities exceeding on their balance sheet dates the criterion of the average number of 500 employees during the financial year shall include in the management report a non-financial statement containing information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters, including: (a) a brief description of the undertaking's business model; (b) a description of the policies pursued by the undertaking in relation to those matters, including due diligence processes implemented; (c) the outcome of those policies; (d) the principal risks related to those matters linked to the undertaking's operations including, where relevant and proportionate, its business relationships, products or services which are likely to cause adverse impacts in those areas, and how the undertaking manages those risks; (e) non-financial key performance indicators relevant to the particular business.</p>	
<p><b><i>German Accounting Standard (GAS) 20 – Group Management Report</i></b></p> <p>The objective of group management reporting under this Standard is to report on the use of the group’s resources by management during the reporting period and to provide information that enables a knowledgeable user to obtain a suitable understanding of the course of business, the position and the expected development of the group, and of the opportunities and risks associated with this development.</p>	
<p><b><i>IIRC Integrated Reporting Framework Purpose</i></b></p> <p>1.7 The primary purpose of an integrated report is to explain to providers of financial capital how an organization creates value</p>	<p><b><i>IIRC Integrated Reporting Framework – proposed 2020 revision</i></b></p> <p>1.7 The primary purpose of an integrated report is to explain to providers of <del>financial</del> capital<sup>1</sup> how an organization creates value</p>

<b>Extracts related to the objective of management commentary</b>	
<p>over time. It therefore contains relevant information, both financial and other.</p>	<p>over time.  <sup>1.</sup> [new footnote] Including financial, manufactured, intellectual, human, social and relationship, and natural capital</p>
<p><b><i>UK Financial Reporting Council – Guidance on the Strategic Report</i></b></p> <p><b>Purpose</b></p> <p>4.1 The strategic report should provide shareholders of the company with information that will enable them to assess how the directors have performed their duty to promote the success of the company for the benefit of shareholders as a whole, while having regard to the matters set out in section 172.22</p> <p>4.2 Directors should apply judgement in determining the level of information that is disclosed, which may require the inclusion of information additional to that specifically listed in the Act.</p> <p>4.3 The strategic report has five main content-related objectives:            (a) to provide insight into the entity’s business model and its main strategy and objectives;            (b) to describe the principal risks the entity faces and how they might affect its future prospects;            (c) to provide relevant non-financial information;            (d) to provide an analysis of the entity’s past performance; and            (e) to provide information to enable shareholders to assess how directors have had regard to stakeholders and other matters when performing their duty under section 172.</p> <p>4.4 The strategic report should provide essential context to the financial statements to support an understanding of developments in the year and the future financial performance and position of the entity.</p> <p>4.5 The strategic report should provide additional explanations of amounts recognised in the financial statements and explain the conditions and events that shaped the information contained in the financial statements. The strategic report should also include information relating to sources of value that have not been recognised in the financial statements and how those sources of value are managed, sustained and developed, for example a highly trained or experienced workforce, natural capital, intellectual property or intangible assets, as these are relevant to an understanding of the entity’s development, performance, position or future prospects.</p> <p>4.6 The success of a company is dependent on its ability to generate and preserve value over the longer term. Companies do not exist in isolation; they need to build and maintain relationships with a range of stakeholders in order to generate and preserve value.</p> <p>4.7 There should be consistency between the strategic report and the information presented in</p>	

<b>Extracts related to the objective of management commentary</b>	
<p>the financial statements.</p> <p>4.8 The strategic report should reflect the collective view of the board.</p> <p>4.9 The strategic report should also provide signposting to show the location of complementary information.</p>	
<p><b>US SEC Financial Reporting Manual – current requirements on objective of Management Discussion &amp; Analysis (MD&amp;A)</b></p> <p><i>9110 Overall Objectives</i></p> <p>9110.1 MD&amp;A is a narrative explanation of the financial statements and other statistical data that the registrant believes will enhance a readers' understanding of its financial condition, changes in financial condition and results of operation.</p> <p>The objectives of MD&amp;A are:</p> <ol style="list-style-type: none"> <li>1. To provide a narrative explanation of a company's financial statements that enables investors to see the company through the eyes of management;</li> <li>2. To enhance the overall financial disclosure and provide the context within which financial information should be analyzed; and</li> <li>3. To provide information about the quality of, and potential variability of, a company's earnings and cash flow so that investors can ascertain the likelihood that past performance is indicative of future performance.</li> </ol>	<p><b>US SEC Proposed rule – objective of MD&amp;A</b></p> <p><b>§ 229.303 (Item 303) Management’s discussion and analysis of financial condition and results of operations</b></p> <p>(a) Objective. The objective of the discussion and analysis is to provide material information relevant to an assessment of the financial condition and results of operations of the registrant including an evaluation of the amounts and certainty of cash flows from operations and from outside sources. This discussion and analysis must provide a narrative explanation of the registrant’s financial statements that allows investors to view the registrant from management’s perspective. The discussion and analysis must focus specifically on material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition. This includes descriptions and amounts of matters that are reasonably expected to have a material impact on future operations and have not had a material impact on past operations, and matters that have had a material impact on reported operations and are not reasonably expected to have a material impact upon future operations. The discussion and analysis must be of the financial statements and other statistical data that the registrant believes will enhance a reader's understanding of the registrant’s financial condition, changes in financial condition and results of operations.</p>