

STAFF PAPER

May 2020

IASB® meeting

Project	Management Commentary		
Paper topic	Cover paper		
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Purpose of this paper

1. This paper:
 - (a) recaps the discussions to date in the Management Commentary project (paragraph 2–3);
 - (b) introduces the papers to be discussed at this month’s meeting (paragraphs 4–6);
 - (c) explains the design of disclosure objectives and supporting guidance for individual areas of content in management commentary (paragraphs 7–11); and
 - (d) sets out next steps in the project (paragraph 12).

Recap

2. To date, the International Accounting Standards Board (Board) has discussed:
 - (a) the staff’s approach to revising IFRS Practice Statement 1 *Management Commentary* (Practice Statement);
 - (b) the objective of management commentary;

- (c) the characteristics of useful information in management commentary, including:
 - (i) relevance and materiality;
 - (ii) completeness and neutrality; and
 - (iii) comparability, verifiability and understandability;
 - (d) disclosure objectives and possible supporting guidance for three areas of content:
 - (i) business model;
 - (ii) strategy; and
 - (iii) resources and relationships.
3. Appendix B summarises the Board’s previous discussions and tentative decisions to date.

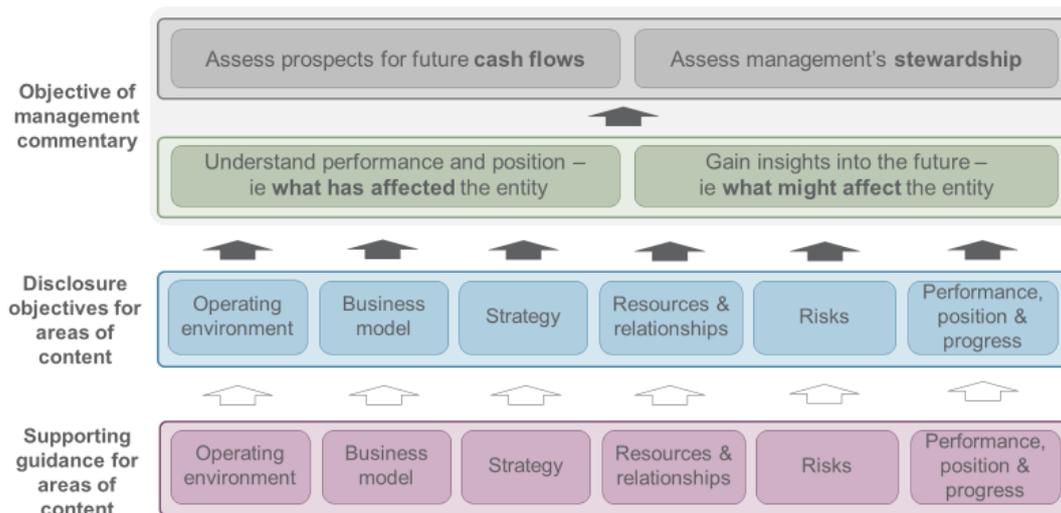
Papers for this month’s meeting

4. The papers for this month’s meeting discuss two further areas of content:
- (a) Agenda Paper 15A *Risks*; and
 - (b) Agenda Paper 15B *External environment*.
5. Each paper discusses:
- (a) the disclosure objective for the area of content; and
 - (b) possible supporting guidance, including on how to describe the key items that need to be discussed in a management commentary.
6. Each paper asks the Board for decisions on the disclosure objective and on describing the key items to be discussed in a management commentary. The papers do not ask the Board for decisions on other aspects of the supporting guidance but invite comments from Board members. The staff will consider those comments and will either address them in drafting the document or present further analysis to the Board at a future meeting.

The design of disclosure objectives and supporting guidance

7. As discussed in April 2020 Agenda Paper 15A *Introduction to disclosure objectives*, the disclosure objectives for the areas of content in management commentary are designed to:
- (a) support all four aspects of the overall objective of management commentary, as set out in Figure 1; and
 - (b) provide a link between that objective and the supporting guidance on the areas of content—as also illustrated in Figure 1.

Figure 1 Relationship between overall objective and disclosure objectives and supporting guidance for the areas of content



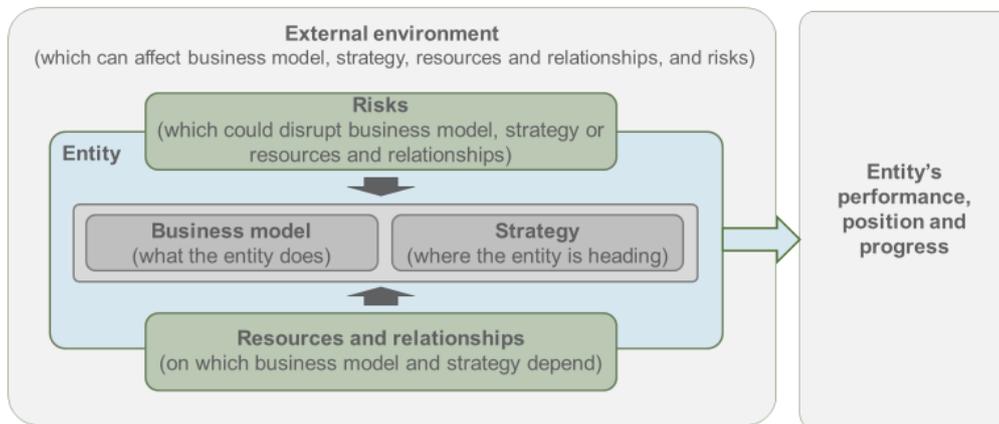
8. Disclosure objectives for the areas of content are intended to help:
- (a) management identify information and analysis that needs to be included in management commentary; and
 - (b) assurers and regulators assess whether information and analysis included in management commentary meet the overall objective of management commentary.

9. To fulfil that role, disclosure objectives must be based on clear principles, focus on investors' and creditors' information needs and contain enough detail. Accordingly, the disclosure objectives contain the following components:
 - (a) the headline objective—the main principle for information and analysis in the area of content.
 - (b) assessments—a description of the main assessments that investors and creditors typically make using information and analysis in that area of content. In some cases, investors and creditors would also need to use information from other areas of content to make those assessments. For example, to assess how effectively management identifies an entity's risks, investors and creditors may consider information and analysis management provides about trends and factors in the entity's external environment.
 - (c) information and analysis—a description of the types of information and analysis that need to be provided to help investors and creditors make their assessments, and a requirement to focus on key matters in providing that information. This component would also be helpful in updating IFRS Taxonomy.

10. Management commentary would be required to meet the disclosure objectives for each area of content to meet the overall objective specified in the revised Practice Statement. Entities would apply supporting guidance in determining what information to provide to meet the individual disclosure objectives. The specific information provided by entities as a result of applying the supporting guidance would depend on their specific circumstances.

11. Appendix A sets out side by side the disclosure objectives and descriptions of key items approved by the Board at its April 2020 meeting and recommended by the staff at this meeting. This side-by-side layout makes it easier to see the similarities in the structure of the disclosure objectives and descriptions of key items for each content area, and how the disclosure objectives form an integrated whole. These relationships can also be represented diagrammatically as show in Figure 2 below.

Figure 2 Relationships between disclosure objectives for areas of content

**Note on terminology – ‘key’**

- The existing Practice Statement uses the terms ‘main’, ‘critical’, ‘significant’, ‘most important’, ‘principal’ to refer to items that need to be described in management commentary in various areas of content. The staff use the term ‘key’ to consistently refer to all such items. The staff will consider in drafting whether this is the most appropriate label for this notion.

Next steps

12. The staff plan that the next Board discussion will cover management commentary on an entity’s performance, position and progress.

Appendix A—Disclosure objectives and descriptions of key items for areas of content discussed to date

	April 2020 IASB meeting—Board’s tentative decisions			May 2020 IASB meeting—staff recommendations	
	Business model	Strategy	Resources and relationships	Risks	External environment
Headline disclosure objective	Management commentary shall provide information and analysis to help investors and creditors understand...				
	how an entity’s business model creates value and generates cash flows.	management’s strategy for sustaining and developing the entity’s business model in the future.	the resources and relationships on which the entity’s business model and management’s strategy for sustaining and developing that model depend.	the risks that could disrupt: the entity’s business model; management’s strategy for developing and sustaining that model; or the entity’s resources and relationships.	how the environment in which the entity operates affects: the entity’s business model; management’s strategy for sustaining and developing that model; the entity’s resources and relationships; or its risks.
Assessments investors and creditors make	That information and analysis helps investors and creditors assess...				
	(a) how effective the entity’s business model is in creating value and generating cash flows; (b) how scalable it is; and (c) how resilient, adaptable and durable it is.	(a) the potential effect of the strategy on the entity’s ability to create value generate cash flows; and (b) the entity’s ability to execute the strategy.	(a) how much the entity depends on particular resources or relationships; and (b) whether those resources are likely to continue to be available and whether the relationships are likely to strengthen and continue.	(a) the magnitude and likelihood of potential future disruption to the entity’s ability to create value and generate cash flows; and (b) how effectively management identifies and manages risks.	(a) how factors and trends in the external environment affect the entity; and (b) how effectively management monitors and responds to factors and trends in the external environment.

	April 2020 IASB meeting—Board’s tentative decisions			May 2020 IASB meeting—staff recommendations	
	Business model	Strategy	Resources and relationships	Risks	External environment
Information required	That information and analysis shall...				
	<p>focus on the key features of the entity’s business model and cover:</p> <p>(a) the range, nature and scale of the entity’s operations;</p> <p>(b) the entity’s cycle for creating value and generating cash flows; and</p> <p>(c) indirect wider consequences or impacts of the entity’s operations if they could affect the entity’s ability to create value and generate cash flows.</p>	<p>focus on the key aspects of management’s strategy and cover:</p> <p>(a) what drives management’s strategy;</p> <p>(b) what management aims to achieve in the long term;</p> <p>(c) how management plans to achieve those aims; and</p> <p>(d) how management will monitor and measure success.</p>	<p>focus on the key resources and relationships and cover:</p> <p>(a) the nature of the resources and relationships;</p> <p>(b) how the resources and relationships are accessed;</p> <p>(c) how they are used;</p> <p>(d) what could affect the availability of the resources and the strength of the relationships; and</p> <p>(e) how the resources and relationships are managed.</p>	<p>focus on the key risks and cover:</p> <p>(a) a description of the risks and of the entity’s exposure to those risks;</p> <p>(b) how management monitors and manages the risks, and would mitigate disruption if it occurs.</p>	<p>focus on the key factors and trends and cover:</p> <p>(a) a description of factors and trends in the external environment;</p> <p>(b) how those factors and trends affect the entity; and</p> <p>(c) how management monitors and responds to those factors and trends.</p>
Description of key items	The key features of the entity’s business model are those that underpin the entity’s ability to create value and generate cash flows.	The key aspects of management’s strategy are those designed to sustain or develop the entity’s ability to create value and generate cash flows in the future.	An entity’s key resources and relationships are those on which the entity’s ability to create value and generate cash flows depend.	An entity’s key risks are those that could disrupt the entity’s ability to create value and generate cash flows.	The key factors and trends in an entity’s external environment are those that affect the entity’s ability to create value and generate cash flows.

Appendix B—Summary of the Board’s previous discussions and tentative decisions

Topic and discussion date	Board’s tentative decision(s)
<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>
<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.

Topic and discussion date	Board's tentative decision(s)
<p>The objective of management commentary (March 2020)</p>	<p>The Board tentatively decided that the revised Practice Statement should:</p> <ul style="list-style-type: none"> (a) retain the statement that management commentary is prepared for existing and potential investors, lenders and other creditors and refer to them as 'primary users'; and (b) explain that primary users are expected to have a reasonable knowledge of business and economic activities and to review and analyse the information diligently; but such users are not expected to have knowledge of the entity to which the management commentary relates. <p>The Board also tentatively decided that the revised Practice Statement should describe the objective of management commentary as supporting primary users in assessing an entity's prospects for future cash flows and management's stewardship of the entity's economic resources by providing useful information and analysis that:</p> <ul style="list-style-type: none"> (a) enhance the primary users' understanding of the entity's performance and position as depicted in the related financial statements; and (b) give insight into factors that could affect the entity's prospects. <p>The Board also discussed a working draft of guidance on the objective of management commentary to be included in the revised Practice Statement, including guidance on:</p> <ul style="list-style-type: none"> (a) the notion of 'management's view'; (b) types of information in management commentary; and (c) the link between the notions of 'an entity's prospects for future cash flows' and 'value creation'. <p>The Board discussed initial ideas on developing disclosure objectives for the types of content expected to be included in management commentary. The Board was not asked to make any decisions</p>
<p>Approach to guidance on qualitative characteristics (July 2019)</p>	<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>

Topic and discussion date	Board’s tentative decision(s)
<p>Making relevance and materiality judgements (July 2019)</p>	<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</i> (Materiality Practice Statement) 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, information management uses in managing the business and information identified through engagement with the entity’s key stakeholders; and (c) explain how management would consider what information to provide about such matters in each content element to deliver a coherent narrative. <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> <ul style="list-style-type: none"> (a) consider the likelihood of a matter occurring, not just the size of the impact, in assessing the quantitative factors when making materiality judgements; (b) consider the appropriate level of aggregation when assessing what information an entity needs to provide in management commentary; and (c) highlight the links between different pieces of information when organising the information within management commentary.

Topic and discussion date	Board's tentative decision(s)
<p>Faithful representation (September 2019)</p>	<p>The Board tentatively decided that the revised Practice Statement would:</p> <ul style="list-style-type: none"> (a) include guidance on the qualities that make up faithful representation—completeness, neutrality and freedom from error; and (b) explain that these qualities should be maximised to the extent possible. <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> <ul style="list-style-type: none"> (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. (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>The Board tentatively decided that the revised Practice Statement would:</p> <ul style="list-style-type: none"> (a) require that the management commentary be neutral. To facilitate that: <ul style="list-style-type: none"> (i) each matter that needs to be discussed in the management commentary should be given due prominence; and (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>

Topic and discussion date	Board's tentative decision(s)
<p>Enhancing qualitative characteristics (October 2019)</p>	<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; (iv) provide comparative information for each performance measure over a period that is long enough to show the emergence of trends; and (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>The Board tentatively decided that the revised Practice Statement would:</p> <ul style="list-style-type: none"> (a) include in its discussion of understandability the current guidance in the Practice Statement on presentation; (b) explain that making management commentary concise is an important part of making it understandable; (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: <ul style="list-style-type: none"> (i) on enhancing the understandability of management commentary when information is incorporated by cross-reference; and (ii) on conditions that must be met by a report when management commentary incorporates information by cross-reference to that report.

Topic and discussion date	Board’s tentative decision(s)
<p>/Continued</p> <p>Enhancing qualitative characteristics (October 2019)</p>	<p>The Board tentatively decided that the revised Practice Statement would:</p> <ul style="list-style-type: none"> (a) include a description of verifiability based on paragraphs 2.30 and 2.32 of the <i>Conceptual Framework</i>; (b) require management to: <ul style="list-style-type: none"> (i) distinguish information based on judgement from factual information; and (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 (c) retain the statement that it does not mandate the level of assurance to which management commentary should be subjected. <p>The Board tentatively decided that the revised Practice Statement would not include guidance on timeliness.</p>
<p>Business model (November 2019)</p>	<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>
<p>Business model Strategy Resources and relationships (April 2020)</p>	<p>The Board tentatively decided to specify the disclosure objectives and descriptions of key items set out in Appendix A to this paper. The Board also discussed possible supporting guidance but was not asked to make any decisions on that guidance.</p>