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Project	Management Commentary		
Paper topic	Overview of guidance on matters affecting long-term prospects, on intangible resources and relationships and on ESG matters		
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Purpose of this paper

1. This paper provides an overview of the Board’s proposals intended to promote provision of information in management commentary on the following interrelated matters of particular interest to investors and creditors:
 - (a) matters that could affect the entity’s long-term prospects;
 - (b) intangible resources and relationships; and
 - (c) environmental, social and governance (ESG) matters.

Note on terminology – ‘ESG matters’

- In this project, the term ‘ESG matters’ has been used to refer to environmental, social and governance matters that could affect the entity’s long-term prospects. ESG matters (some or all of which are sometimes called ‘sustainability-related matters’) are often considered to be the subject of ‘sustainability reporting’, although there are various interpretations of the scope of ESG reporting and sustainability reporting and their target audiences.

- In September 2020, the Trustees of the IFRS Foundation published *Consultation Paper on Sustainability Reporting* seeking stakeholder input on the need for global sustainability standards and gauging support for the Foundation to play a role in the development of such standards.¹

2. This paper does not ask the Board to make decisions but asks the Board for comments.

Structure of this paper

3. This paper is structured as follows:
- (a) investors' and creditors' requests for information (paragraphs 4–6);
 - (b) approach to developing guidance (paragraphs 7–11);
 - (c) feedback from consultative groups (paragraphs 12–13);
 - (d) overview of draft guidance on matters that could affect the entity's long-term prospects (paragraph 14);
 - (e) overview of draft guidance on intangible resources and relationships (paragraphs 15–16);
 - (f) overview of draft guidance on ESG matters (paragraph 17–19); and
 - (g) considerations for the future (paragraphs 20–21).

Investors' and creditors' requests for information

4. As noted in Agenda Paper 15 *Cover paper*, short term focus has been identified as a gap in current narrative reporting practice. Investors and creditors increasingly request information about matters that could affect the entity's long-term prospects. Particular demand is for information about intangible resources and relationships and about ESG matters. For example, the Chartered Financial Analyst (CFA) Institute states that:

..more thorough consideration of ESG factors by financial professional can improve the fundamental analysis they undertake and ultimately the investment choices they make..²

¹ See the full Consultation Paper [here](#).

² See <https://www.cfainstitute.org/en/research/esg-investing>.

5. The changing information needs of investors and creditors—and in some cases the needs of wider audiences—have led to multiple developments in the field of narrative, and in particular sustainability, reporting. This has led to calls and initiatives to harmonise the multiple frameworks, standards and guidelines, including the following recent developments:

- (a) the International Organization of Securities Commission (IOSCO) setting out its intention to accelerate the harmonisation of sustainability standards and establishing a Task Force on Sustainable Finance with the aim of improving sustainability-related disclosures made by issuers and asset managers; to work in collaboration with other international organizations and regulators to avoid duplicative efforts and to enhance coordination of relevant regulatory and supervisory approaches;³
- (b) the International Federation of Accountants calling for creation of an International Sustainability Standards Board to sit alongside the IASB under the auspices of the IFRS Foundation;⁴
- (c) five organisations active in sustainability or narrative reporting—CDP, the Climate Disclosure Standards Board (CDSB), the Global Reporting Initiative (GRI), the International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB)—issuing the *Statement of Intent to Work Together Towards Comprehensive Corporate Reporting*;⁵
- (d) the World Economic Forum, in collaboration with Deloitte, EY, KPMG and PwC, publishing a white paper *Measuring Stakeholder Capitalism: Towards Common Metrics and Consistent Reporting of Sustainable Value Creation*

³ For more information see <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD652.pdf>.

⁴ For more information see <https://www.ifac.org/news-events/2020-09/ifac-calls-creation-international-sustainability-standards-board-alongside-international-accounting>.

⁵ See the full Statement of Intent [here](#). Those five organisations participate in the Corporate Reporting Dialogue, together with the International Accounting Standards Board and the International Organization for Standardization.

seeking to identify metrics that can support effective long-term sustainable value creation;⁶ and

- (e) the European Commission starting a revision of its Non-Financial Reporting Directive and preparatory work on non-financial reporting standards.⁷

6. There have also been recent developments in research into better information on intangible resources and relationships, including:

- (a) the European Financial Reporting Advisory Group's (EFRAG) research project on better information on intangibles, which aims to provide suggestions on how information on creating, maintaining and/or improving value can be provided in financial reports in a manner that is useful for decisions on providing resources to the entity. In February 2020, EFRAG published a literature review on the reporting of intangibles.⁸
- (b) the Korea Accounting Standards Board's (KASB) research project on accounting for intangible assets, including their proposal for Statement of Core Intangibles, which was presented at December 2019 Accounting Standards Advisory Forum (ASAF) meeting.⁹
- (c) the UK Financial Reporting Council's (FRC) research project *Intangibles: How Can Business Reporting Do Better?* In February 2019, FRC issued a Discussion Paper *Business Reporting on Intangibles: Realistic Proposals* which was presented at July 2019 ASAF meeting.¹⁰

Approach to developing guidance

7. Because of the growing demand for information on matters that can affect the entity's long-term prospects, and in particular, on intangible resources and relationships and ESG

⁶ See the full white paper [here](#).

⁷ For more information see <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12129-Revision-of-Non-Financial-Reporting-Directive/public-consultation>.

⁸ See more information on the EFRAG research project [here](#).

⁹ See the KASB papers presented at December 2019 ASAF meeting [here](#).

¹⁰ See the FRC Discussion Paper [here](#) and the paper presented at July 2019 ASAF meeting [here](#).

matters, promotion of information on these topics in management commentary has been one of the focus areas of the Management Commentary project.

8. In this project, the Board is not seeking to identify specific matters that need to be explained or information or metrics that need to be provided by all entities in relation to those matters because the range of matters that may need to be addressed is very wide and the information that would be required in relation to each matter would be unique to the entity. Asking all entities to provide specified information on a defined set of matters may lead to entities reporting immaterial information. It may also lead to a ‘checklist’ approach and discourage preparers from applying judgement in identifying all entity-specific matters for which information about the matter would be material to investors and creditors.

9. Nevertheless, the Board has acknowledged that information about matters that could affect the entity’s long-term prospects, including information about intangible resources and relationships and ESG matters may be necessary to meet the objective of management commentary. Accordingly, the Board is seeking to promote management commentary as a ‘home’ for all material information about key matters that fundamentally affect or could fundamentally affect the entity’s ability to create value and generate cash flows, including matters that could fundamentally affect the entity’s long-term prospects. Matters that could fundamentally affect the entity’s long-term prospects could include intangible resources and relationships, and ESG matters. This approach based on the principle of materiality would allow preparers to:
 - (a) focus in management commentary on key matters specific to the entity—that is on matters that could fundamentally affect the entity’s ability to create value and generate cash flows. Because they could have such a fundamental effect, such matters are typically monitored and managed by management.
 - (b) use other standard-setters’ frameworks, standards and guidance to help identify key matters and material information specific to their entity, about those key matters.

- (c) reassess what information needs to be provided as the entity’s circumstances and investors’ and creditors’ information needs evolve.
10. The Board’s proposals for the provision of information on matters of particular interest to investors and creditors—including information on matters that could fundamentally affect the entity’s long-term prospects, such as intangible resources and relationships and ESG matters—are expected to be included throughout the draft guidance rather than separately. This is because:
- (a) these matters may affect various aspects of the entity and its operations and so may need to be described throughout management commentary. For example, an ESG matter may affect one or more key processes in the entity’s business model, or its key relationship with a supplier, or a key aspect of the entity’s strategy.
 - (b) there is an overlap between these matters, for example, a relationship with the entity’s key employees could be viewed as a key intangible relationship, a key social matter and a key matter affecting the entity’s long-term prospects.
11. Paragraphs 12–13 discuss feedback received from consultative groups on the materiality-based approach to reporting on matters of particular interest to investors and creditors, and on the staff’s initial suggestions for the related guidance. The following sections summarise the draft guidance intended to promote the provision of information in management commentary on matters that could fundamentally affect the entity’s long-term prospects (paragraph 14), and specifically, to encourage provision of information on intangible resources and relationships (paragraphs 15–16) and on ESG matters (paragraphs 17–19). The summary is based on the working draft of the Exposure Draft that has been reviewed by the Board and by members of the Management Commentary Consultative Group (Consultative Group).

Feedback from consultative groups

12. The staff discussed the proposed principle-based approach to guidance on information about intangible resources and relationships and ESG matters with the Management Consultative Group and the International Forum of Accounting Standard-setters

(IFASS).¹¹ Members of these groups supported the proposal that identification of intangible resources and relationships and ESG matters should be based on materiality to investors and creditors. Many also agreed that the discussion of these matters should be an integral part of management commentary and need not be separated from other information in management commentary. These members said that there is no need to present separately specific guidance on intangible resources and relationships and ESG matters, although some members suggested that more prominence should be given to guidance on intangible resources and relationships, for example by providing that guidance in a separate section.

13. The staff also discussed with the ASAF the staff's initial suggestions for identifying and reporting matters that could affect the entity's long-term prospects, including intangible resources and relationships. Members agreed with the proposed principle-based approach. They also commented that guidance to promote the provision of information that gives insight into long-term prospects is needed throughout the revised Practice Statement, as suggested by the staff. Some members highlighted that emphasis is needed on providing information about intangible resources and relationships.

Overview of draft guidance on matters that could affect the entity's long-term prospects

14. Table 1 summarises proposals throughout the working draft of the Exposure Draft that ask management to provide information about matters that could fundamentally affect the entity's long-term prospects. Such information is needed to help investors and creditors assess the entity's prospects for future cash flows and assess how efficiently and effectively management has used and protected the entity's resources.

¹¹ IFASS is an independent grouping on national standard-setters from around the world, plus other organisations that have a close involvement in financial reporting issues.

Table 1. Overview of draft guidance on provision of information about matters that could fundamentally affect the entity’s long-term prospects

Area of the draft guidance	Draft guidance to promote provision of information includes:
Guidance on the overall objective of management commentary	<p>(a) specifying that the objective of management commentary is not only to provide information that enhances investors’ and creditors’ understanding of an entity’s performance and position depicted in its financial statements, but also information that provides insight into factors that could affect the entity’s prospects for future cash flows. The guidance explains that:</p> <ul style="list-style-type: none"> (i) future cash flows will be assessed by investors and creditors over the short, medium and long term; (ii) for their assessments, investors and creditors need to understand factors that could affect the amount or timing of the entity’s future cash flows, or that affect the uncertainty in their amount or timing; and (iii) management commentary includes forward-looking information that relates to possible future transactions, other events or conditions that could affect the entity’s prospects, including its long-term prospects. <p><i>Note: Some reviewers of the working draft of the Exposure Draft commented that the objective of management commentary could have a stronger emphasis on the long term, for example, by referring not just to cash flows but also to value creation. The staff will consider these comments in drafting the Exposure Draft.</i></p>
Guidance on materiality	<p>(b) linking the identification of key matters in all areas of content to the entity’s ability to create value and generate cash flows and explaining that value creation covers the short, medium and long term. Some of those key matters may relate to uncertain future events, so the proposals explain that in assessing materiality of information about such an event, management needs to consider the effects of that event on the amount, timing and uncertainty of the entity’s future cash flows, including in the long term, taking account of the time value of money of the future cash flows and</p>

	<p>the degree of uncertainty associated with them. The proposals would require management to provide information that is material to investors’ and creditors’ assessments of uncertain future events, but would not require management to make predictions or forecasts about those events.</p>
<p>Guidance on business model</p>	<p>(c) specifying the headline disclosure objective as providing information to help investors and creditors understand how the entity’s business model creates value and generates cash flows. The disclosure objective also specifies that information about an entity’s business model should help investors and creditors not only assess how effective the entity’s business model is, but also whether it has potential to grow and whether it is resilient, adaptable and durable¹². In addition, the guidance on business model:</p> <ul style="list-style-type: none"> (i) states that examples of key features of business model that are fundamental to the entity’s ability to create value and generate cash flows are features that underpin the entity’s value proposition, provide the entity with a competitive advantage or create uncertainty about the entity’s ability to create value and generate cash flows in the future; (ii) asks management to provide information about the entity’s business model in a way that helps investors and creditors understand how the entity’s long-term purpose is operationalised and assess how closely the entity’s business model is aligned with the stated purpose, if the entity has issued a public statement of its purpose; (iii) asks management to describe the entity’s processes involved in obtaining its key resources, maintaining its key relationships or enhancing those resources and relationships, for example processes relating to research and development, staff training or customer loyalty programmes if they can fundamentally affect the entity’s future ability to create value and generate cash flows; and (iv) asks management to describe wider consequences (impacts) of the entity’s operations that have fundamentally affected,

¹² April 2020 [Agenda Paper 15B Business model](#) explains that resilience, adaptability and durability are intended to capture the idea of a ‘sustainable’ business model as a business model that can continue creating value and generating cash flows both in normal circumstances and when circumstances change (paragraph 36).

	<p>or could fundamentally affect, the entity’s ability to create value and generate cash flows, including over the long term.</p>
<p>Guidance on strategy</p>	<p>(d) specifying that management needs to describe its strategy for sustaining and developing the entity’s business model in the short, medium and long term. In particular, the proposals ask for description of the drivers of the strategy (including the opportunities management has chosen to pursue), the long-term aims of the strategy, intermediate milestones on the path towards achieving the long-term aims and plans for reaching the intermediate milestones and for achieving the long-term aims. Because the following matters are important for assessing the potential effect of the strategy and whether the strategy is achievable, the proposals also ask management to discuss:</p> <ul style="list-style-type: none"> (i) progress in implementing strategy; and (ii) management’s plans for funding the strategy and its plans for capital allocation.
<p>Guidance on resources and relationships</p>	<p>(e) specifying that management commentary needs to describe the key resources and relationships on which the entity’s business model and management’s strategy for sustaining and developing that business model depend, including providing information about factors that could affect the availability of those resources and the strength of those relationships.</p>
<p>Guidance on risks</p>	<p>(f) specifying that management commentary needs to focus on key risks that could severely disrupt the entity’s ability to create value and generate cash flows in the short, medium or long term. In addition, the draft guidance on risks:</p> <ul style="list-style-type: none"> (i) states that examples of key risks are risks that threaten the entity’s existence, risks that could severely disrupt the entity’s business model, risks that could severely disrupt management’s strategy, or risks that could severely disrupt access to a key resource or severely damage a key relationship; (ii) specifies that if a risk has the potential to cause severe disruption, information about that risk might be material even if the likelihood of the risk materialising is low, or if the risk could materialise only in the long term; and

	(iii) asks management to discuss how it monitors and manages the risks and would mitigate the disruption if it occurs, as well as to discuss progress in managing risks.
Guidance on external environment	(g) specifying that key factors and trends in the external environment include factors and trends that have fundamentally affected, or could fundamentally affect in the short, medium or long term: <ul style="list-style-type: none"> (i) the entity’s business model; (ii) management’s strategy for sustaining and developing that business model; (iii) the entity’s resources or relationships; or (iv) the risks to which the entity is exposed.
Guidance on performance and position	(h) specifying that management commentary needs to cover not only the factors that have fundamentally affected the entity’s performance for the period or position at the end of the reporting period but also the factors that could fundamentally affect them in the future, including in the long term. In particular, the draft guidance: <ul style="list-style-type: none"> (i) asks for information about capital allocation decisions during the reporting period, including any changes from the previous decisions, and for an analysis of future expenditure to which the entity has committed itself; and (ii) asks for an analysis of the entity’s ability to meet its obligations, including over the long term, for example, an analysis of the entity’s liquidity and leverage measures and indicators, and analysis of mitigating actions management has taken to address any liquidity issues that arose in the reporting period or could arise in the next period.

Overview of draft guidance on intangible resources and relationships

15. As noted in paragraph 4, investors and creditors increasingly request information about intangible resources and relationships, in particular about those not recognised in the entity’s financial statements. The working draft of the Exposure Draft includes the following guidance to promote provision of information on intangible resources and relationships in management commentary:

- (a) draft guidance on resources and relationships that asks for information to help investors and creditors understand the entity’s key resources and relationships that are fundamental to the entity’s ability to create value and generate cash flows and specifies that resources and relationships include intangible resources and relationships. Key intangible resources and relationships should be described irrespective of whether they are recognised in financial statements. Sometimes, only a particular intangible resource or relationship, or only a particular category of intangible resource or relationship, is key—for example a group of employees with specialist know-how. If that is the case, information in management commentary should focus on that particular resource, relationship or category. The disclosure objective specifies the following types of information that need to be provided about key resources (including key intangible resources) and key relationships:
- (i) the nature of those resources and relationships;
 - (ii) how the entity accesses and deploys them;
 - (iii) factors that could affect the availability of the resources and the strength of the relationships; and
 - (iv) progress in managing the resources and relationships.
- (b) draft guidance on strategy that explains that one aspect of management’s strategy may relate to preserving or enhancing the entity’s access to key resources and relationships (including intangible ones), or the quality of those resources and relationships; if information about that aspect is material, management commentary needs to provide that information.
- (c) draft guidance on risks that asks management to consider risks that could severely disrupt access to the entity’s key resources and relationships (including intangible ones) in identifying key risks for the entity.
- (d) draft guidance on performance and position that suggests that, in explaining how the entity has allocated capital in the reporting period, management should provide an analysis of expenditure on enhancing the entity’s ability to create

value and generate cash flows, for example, expenditure on research and development. This is because some expenditure on intangible resources and relationships may be recognised in the entity's financial statements as an expense rather than included in the measurement of a recognised intangible asset.

16. Some reviewers of the working draft of the Exposure Draft suggested that a more in-depth discussion of intangible resources and relationships is needed because of their unique contribution to value creation or that guidance on intangible resources and relationships should be more prominent. The staff will consider in drafting how to make the guidance on intangible resources and relationships more visible.

Overview of draft guidance on ESG matters

17. As mentioned in paragraph 4, investors and creditors increasingly ask for information about ESG matters because those matters can affect entities' ability to create value and generate cash flows, especially in the long term.
18. The Board noted that environmental matters, social matters and governance matters can affect the entity differently and so information that needs to be provided about them in management commentary would differ. In particular, the Board is not proposing guidance specific to governance matters because governance requirements as well as governance-related reporting are typically set by local law and regulations and may vary between jurisdictions. Nevertheless, information in management commentary is likely to provide an insight into some governance matters, for example, through description of management's strategy, information on how management monitors and manages key matters or information on progress in achieving strategy or managing key matters.
19. The working draft of the Exposure Draft includes the following draft guidance seeking to promote provision of information related to environmental and social matters:
 - (a) the draft guidance on resources and relationships (see paragraph 15(a)). This guidance would apply to some ESG matters because there is an overlap between intangible resources and relationships and ESG matters (see paragraph 10(b)). In particular, the guidance on resources and relationships would apply to the

entity's key natural resources and to the entity's key relationships, including those with its employees, customers or suppliers or its wider relationships such as those with regulators or local communities. The guidance would ask for information on progress in managing those key natural resources and key relationships, including measures and indicators management uses to monitor the effectiveness of its actions, for example, employee retention or engagement scores, or to monitor the usage and the available quantity of the key natural resource.

- (b) the draft guidance on the external environment. This guidance asks for information about factors and trends in an entity's external environment that fundamentally affect the entity, including social and environmental factors and trends. In particular, the guidance asks for an explanation of how those factors and trends have affected or could affect the entity's business model, management's strategy for sustaining and developing that model, the entity's resources and relationships and the risks to which the entity is exposed. Examples of social and environmental factors and trends that might affect an entity include those relating to society, such as demographic changes, or to the natural environment, such as new regulation (or possible new regulation) on carbon emissions. In explaining factors and trends that fundamentally affect the entity, including social and environmental factors and trends, management commentary would need to cover:
 - (i) the nature of the key factors and trends;
 - (ii) how those factors and trends have affected, or could affect, the entity; and
 - (iii) how management has responded, or plans to respond, to the factors.
- (c) the draft guidance on business model. This guidance asks for information about wider consequences (impacts) of the entity's operations on for example, the natural environment, the economies of the regions in which the entity operates, particular groups of people or society at large. To be useful for investors' and creditors' economic decisions, information about such impacts would need to be

provided if they have fundamentally affected, or could fundamentally affect, the entity's ability to create value and generate cash flows. Information would not be needed about impacts that have not fundamentally affected, and could not fundamentally affect, the entity's ability to create value and generate cash flows. The draft guidance discusses what types of information about impacts may need to be provided.

Considerations for the future

20. Developing a revised Practice Statement to promote management commentary as a 'home' for material information about matters that could fundamentally affect the entity's long-term prospects, about intangible resources and relationships and about ESG matters is the Board's response to investors' and creditors' growing demand for this information.
21. Following the calls for harmonisation in sustainability reporting (see paragraph 5), in September 2020 the Trustees of the IFRS Foundation issued a *Consultation Paper on Sustainability Reporting* to seek stakeholder input on the need for global sustainability standards and gauge support for the Foundation to play a role in the development of such standards.¹³

Question for the Board

Do you have any comments or questions on the overview of draft guidance intended to promote provision of information about matters of particular interest to investors and creditors?

¹³ See the full Consultation Paper [here](#).