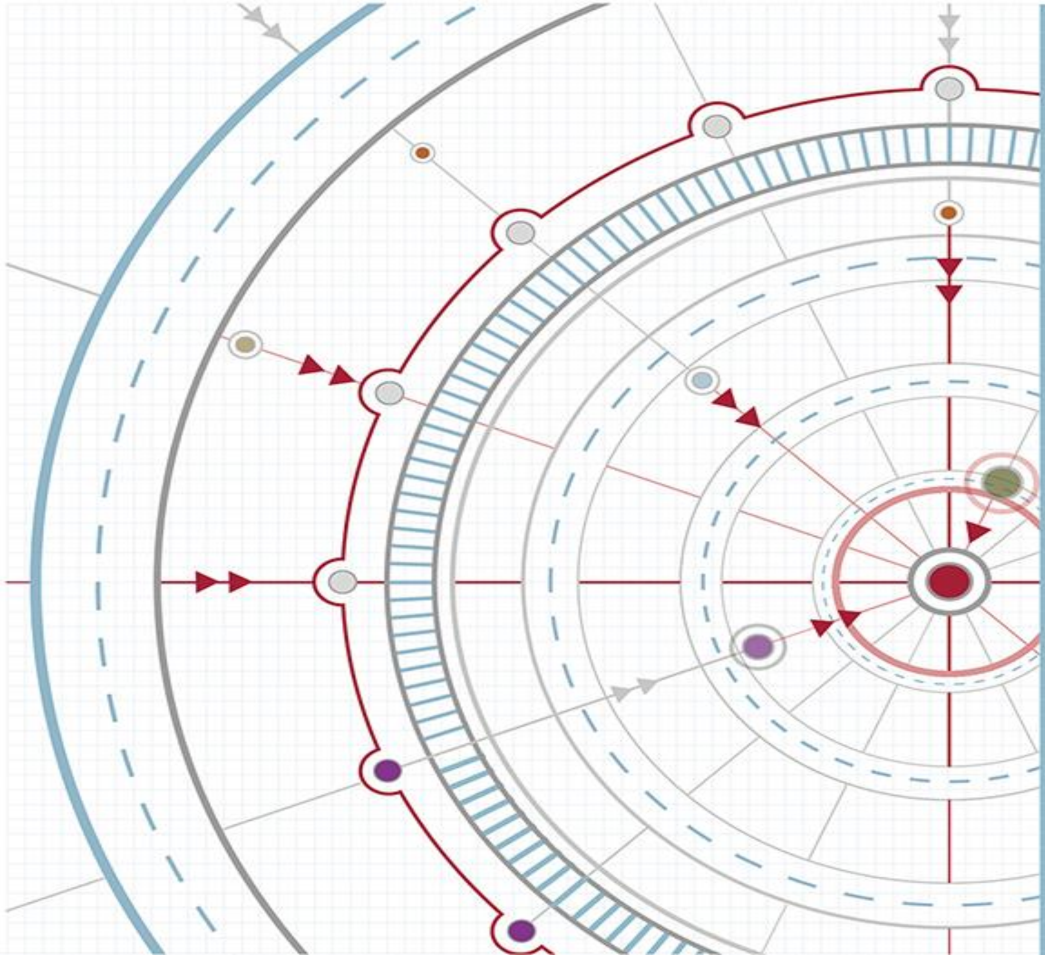
IFRS® Foundation



Management Commentary

Stream 3 *Business Model, Strategy, Operating Environment and Risks*

Slide Deck 1 *Overall Approach*

Consultative group meeting – 3 April 2019

The views expressed in this presentation are those of the presenter, not necessarily those of the International Accounting Standards Board or the IFRS Foundation.

Overall approach
Contents

Staff's proposed approach to Stream 3

Challenges with current reporting practice

The staff identified the following challenges with current reporting practice that are applicable to today's discussion:

Area	Challenges	Illustration of problematic reporting
Business model	• Key resources or relationships not addressed in management commentary	Dependency on water-stressed sites is only discussed in management commentary if there is a failure which negatively affected performance
	• Key features of how the business operates are either not described in management commentary or are over-generalised	A key part of the customer base is controlled by a reseller, but this is not described in management commentary
Strategy	• Strategy discussion focuses on operational tactics without addressing long-term drivers of success	Strategy discussion focuses on revenue increments or efficiency programmes without responding to the threat posed by a potential new class of market entrant
Operating environment and risks	• Narrow view of the operating environment	Discussion focuses on year-on-year changes in market size without addressing a threat of market disruption
	• Lack of focus resulting in key risks hidden by disclosure of other risks which are less important, and varied approaches to identification of key risks	Generic disclosure of a particular type of risk faced by all or most entities in a country without focusing on the key risks the entity faces
Narrative coherence	• Issues raised in management commentary without the detail to help users understand implications of the issues on the prospects for the future net cash inflows to the entity and the progress in managing the issues	Employees are identified as the key resource the entity depends on for its success, but no detail is provided to help users evaluate how the entity is managing this resource

During today's discussion, we would like to ask the Consultative Group whether the staff's proposals address the challenges identified above, and whether there are other challenges we need to consider.

Extracts from the 2010 Practice Statement (1/2)

Extracts from the 2010 Practice Statement are provided below and on the next slide as an overview of our starting point. We will discuss each of these in detail in slide decks 2-4.

[Content elements]
24 Although the particular focus of management commentary will depend on the facts and circumstances of the entity, management commentary should include information that is essential to an understanding of:

a) the nature of the business;
b) management's objectives and its strategies for meeting those objectives;
c) the entity's most significant resources, risks and relationships;
d) the results of operations and prospects; and
e) the critical performance measures and indicators that management uses to evaluate the entity's performance against stated objectives.

25 The elements are not listed in a specific order. They are, however, related and should not be presented in isolation. Management should provide its perspective on the business and its analysis of the interaction of the elements to help users to understand the entity's financial statements and to understand management's objectives and strategies for achieving those objectives.

[Description of the business]
26 Management should provide a description of the business to help users of the financial reports to gain an understanding of the entity and of the external environment in which it operates. That information serves as a starting point for assessing and understanding an entity's performance, strategic options and prospects. Depending on the nature of the business, management commentary may include an integrated discussion of the following types of information:

a) the industries in which the entity operates;
b) the entity's main markets and competitive position within those markets;
c) significant features of the legal, regulatory and macro-economic environments that influence the entity and the markets in which the entity operates;
d) the entity's main products, services, business processes and distribution methods; and
e) the entity's structure and how it creates value.

[Objectives and strategies]
27 Management should disclose its objectives and strategies in a way that enables users of the financial reports to understand the priorities for action as well as to identify the resources that must be managed to deliver results. For example, information about how management intends to address market trends and the threats and opportunities those market trends represent provides users of the financial reports with insight that may shape their expectations about the entity's future performance. Management should also explain how success will be measured and over what period of time it should be assessed.

28 Management should discuss significant changes in an entity's objectives and strategies from the previous period or periods. Discussion of the relationship between objectives, strategy, management actions and executive remuneration is also helpful.

Note: Subtitles in bold added for clarity

Extracts from the 2010 Practice Statement (2/2)

[Resources, risks and relationships]

29 Management commentary should include a clear description of the most important resources, risks and relationships that management believes can affect the entity's value and how those resources, risks and relationships are managed.

30 Management commentary should set out the critical financial and non-financial resources available to the entity and how those resources are used in meeting management's stated objectives for the entity. Disclosure about resources depends on the nature of the entity and on the industries in which the entity operates. Analysis of the adequacy of the entity's capital structure, financial arrangements (whether or not recognised in the statement of financial position), liquidity and cash flows, and human and intellectual capital resources, as well as plans to address any surplus resources or identified and expected inadequacies, are examples of disclosures that can provide useful information.

31 Management should disclose an entity's principal risk exposures and changes in those risks, together with its plans and strategies for bearing or mitigating those risks, as well as disclosure of the effectiveness of its risk management strategies. This disclosure helps users to evaluate the entity's risks as well as its expected outcomes. Management should distinguish the principal risks and uncertainties facing the entity, rather than listing all possible risks and uncertainties.

32 Management should disclose its principal strategic, commercial, operational and financial risks, which are those that may significantly affect the entity's strategies and progress of the entity's value. The description of the principal risks facing the entity should cover both exposures to negative consequences and potential opportunities. Management commentary provides useful information when it discusses the principal risks and uncertainties necessary to understand management's objectives and strategies for the entity. The principal risks and uncertainties can constitute either a significant external or internal risk to the entity.

33 Management should identify the significant relationships that the entity has with stakeholders, how those relationships are likely to affect the performance and value of the entity, and how those relationships are managed. This type of disclosure helps users of the financial reports to understand how an entity's relationships influence the nature of its business and whether an entity's relationships expose the business to substantial risk.

Note: Subtitles in bold added for clarity

How we propose to revise the 2010 Practice Statement (1/2)

The 2010 Practice Statement already covers the main topics for today's discussion. However, it does so at a high level. An underlying theme with today's staff's proposals is to support more effective application of the Practice Statement, whilst maintaining a principles-based approach. We think it is particularly important that the Practice Statement is not perceived to be telling entities what their strategically important issues are.

To support this approach, we are proposing a restructuring of the content elements in the 2010 Practice Statement, and additional guidance on each, outlined on slide 8. The Practice Statement will not prescribe the way in which an entity should structure its management commentary. The purpose of the guidance on the content elements is to act as a base for determining what information should be provided, rather than how to structure and order those content elements.

The 2010 Practice Statement:

Description of the business
- Nature of the business
- External environment

Resources, risks and relationships
- Critical financial and non-financial resources
- Principal strategic, commercial, operational and financial risks

Objectives and strategies
- Objectives and strategies

'What we do today'

'What could affect our ability to do it'

'How we are responding'

Staff's proposed approach:

Business model

(a) Structure of the entity
(b) Business activities:
  (i) inputs (including resources and relationships)
  (ii) processes
  (iii) outputs and impacts

Operating environment and risks

(a) Trends and factors in the operating environment
(b) Risks to the prospects for future net cash inflows to the entity

Strategy

(a) Purpose
(b) Objectives
(c) Plans
(d) Culture
(e) Funding strategy

How we propose to revise the 2010 Practice Statement (2/2)

Proposed approach:

Summary of the key changes proposed:

Business model
(a) Structure of the entity
(b) Business activities:
- (i) inputs (including resources and relationships)
- (ii) processes
- (iii) outputs and impacts

Covered in Slide deck 2

- We are proposing two components of the business model description, with one of the components addressing three different areas on the basis that (i) all areas are needed to interpret the other information in management commentary; and (ii) the information required to support each area is different.
- *Resources & relationships* is covered as a separate content element in the 2010 Practice Statement. We are proposing that it should be an integral (but discrete) part of the business model description.
- We are proposing more guidance on what to cover in each component. The aim of the additional proposed guidance is to help preparers identify what information to include in management commentary.

Operating environment and risks
(a) Trends and factors in the operating environment
(b) Risks to the prospects for future net cash inflows to the entity

Covered in Slide deck 4

- *External environment* forms part of the *description of the business* in the 2010 Practice Statement, and *risks* are covered alongside *resources and relationships*. We recognise that there is a strong interaction between (i) external environment and risks and (ii) resources and relationships. However, there is also a strong interaction between resources and relationships and both business model and strategy. We think that these links should be reflected in the discussion of the content elements in management commentary. Therefore, we propose to make operating environment and risks a separate content element (rather than embedding those topics within one of the other elements).
- We are proposing a more explicit link between the identification of risks to be discussed in management commentary and the effect of those risks on the prospects for future net cash inflows to the entity. The approach also makes the likelihood of a particular outcome an explicit consideration in identifying those risks as we are concerned that reporting many risks whose likelihood is remote, rather than the key risks, could undermine the overall clarity of management commentary.
- We are proposing specific guidance on the information to be reported for each identified risk.

Strategy
(a) Purpose
(b) Objectives
(c) Plans
(d) Culture
(e) Funding strategy

Covered in Slide deck 3

- We are concerned that descriptions of strategy may focus on the short term, and are therefore proposing a structured approach that builds from the entity's *purpose*, the *objectives* management has set in pursuit of the purpose, through to its *plans* to deliver these objectives in pursuit of the entity's purpose.
- We are also proposing an explicit reference to the entity's culture in the Practice Statement, recognising the role it plays in pursuit of the entity's purpose.
- We are proposing that the Practice Statement also provides guidance on discussion of strategy for a particular item–funding strategy–that addresses the entity's ability to finance its strategy whilst meeting expectations on liquidity and dividend levels.

Management commentary architecture
How the content elements fit together

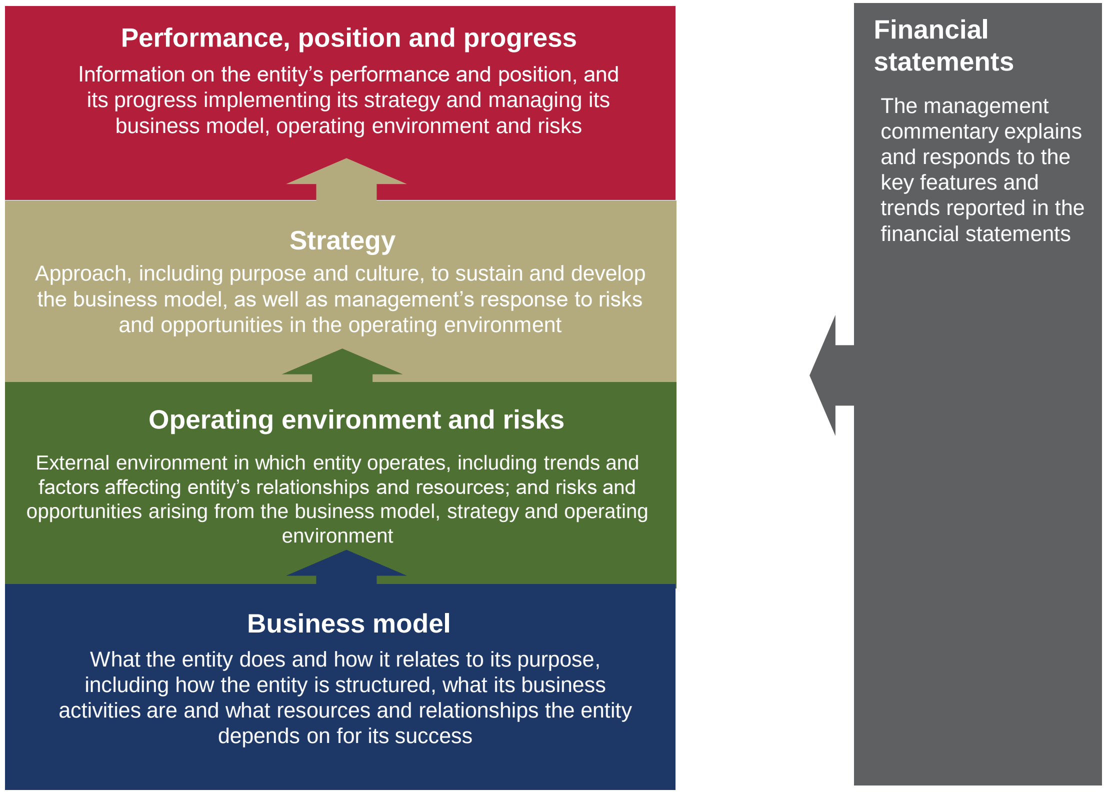
The diagram illustrates how the proposed content elements of management commentary fit together in the Practice Statement, which will provide guidance on each content element to support entities in meeting the overall objective of the management commentary.

As a result, management commentary is built up from a description of the entity's business model through a description of its operating environment and risks, and its strategy in order to provide focused information about the entity's performance, position, and progress.

The principle of *narrative coherence* applies across all content elements in management commentary and is addressed in Slide Decks 2, 3 and 4.

> ***Illustration:***
>
> An entity identifies that its business model is heavily reliant on a constant stream of innovation from its design team. Its discussion of operating environment identifies the market shortage of design talent, and the consequent risk to the entity's competitive advantage. The entity explains its strategy for developing and maintaining the right skill set in the face of market conditions, and the entity reports on its performance in retaining skilled design staff.

Management commentary
Financial and operational information and analysis to help users assess the prospects for future net cash inflows to the entity and assess management's stewardship of the entity's economic resources.



Terminology

There is considerable diversity and overlap in the use of terminology for each of the three content elements being discussed today. In particular, features that some would consider to be 'business model' may be considered by others to be 'strategy' and vice-versa. The following conventions have been followed in today's slide decks:

Term	*Includes*	*Simple illustration*
Business model	A description of how the entity is structured and its business activities, including inputs, in particular resources and relationships the entity depends on for its success, processes, outputs and impacts	We design, make and sell widgets to retail customers in Europe and Asia
Operating environment	The external environment in which the entity operates, including trends and factors affecting the entity's access to the resources and relationships the depends on for its success	Africa's widget needs are not being met
Strategy	Management's approach to sustaining and developing the entity's business model, including the entity's purpose and culture, and management's response to risks and opportunities in the entity's operating environment	We will open a sales office in Africa to meet the demand for widgets

Purpose and *culture* have been included in the discussion of strategy because of the role they play in sustaining and developing the entity's business model. We think it is helpful to emphasise this link in order to support a longer-term perspective of the reporting on the selection and execution of strategy. However, we recognise that *purpose* and *culture* could instead be regarded as features of the entity's business model, and management commentaries may be structured accordingly.

We note that the translation of terminology may result in additional challenges that we will consider in drafting.

Cross-cutting issues

Cross-cutting issues
Commercial sensitivity – issue

Background

- The topic of sensitive information has come up in previous Consultative Group discussions.
- The Board has also heard concerns over disclosure of sensitive information in its other projects focused on presentation and disclosure, such as Disclosure Initiative and Primary Financial Statements.
- As a result, the Board is seeking advice from the IFRS Foundation Advisory Council (Advisory Council) on how best to balance:
  - (a) our focus:
    - (i) the IFRS Foundation's mission to develop IFRS Standards that bring transparency, accountability and efficiency to financial markets around the world; and
    - (ii) the objective of general purpose financial reporting 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; and
  - (b) concerns over disclosure of sensitive information.
- The Advisory Council is discussing this topic at its March 2019 meeting.
- The material on sensitive information in this slide deck is based on the agenda paper presented to the Advisory Council https://www.ifrs.org/-/media/feature/meetings/2019/march/advisory-council/ap3-disclosure-of-sensitive-information.pdf. Staff's proposed approach presented on slide 13 may change depending on the input received from the Advisory Council.

What is sensitive information?

- As discussed in the agenda paper for the Advisory Council, types of information that could result in commercial loss to the reporting entity include:

Type of sensitive information	Example and perceived effect
Negotiating position	Information on revenue contribution by major customer—key customers, knowing their importance to the entity, may have the upper hand in negotiation
Strategic plan	Description of intangible asset—may reveal details of R&D, prompting competitors to step in
Confidentiality	Disclosures of items subject to confidentiality required by agreement—may result in legal disputes for breach of agreement
Uncertain positions	Uncertainty relating to going concern—may cause further negative impact to entity's financial position; effects of 'self-fulfilling prophecy'
Regulatory scrutiny and reputational risks	Disclosure of information that is reputationally harmful—may damage brand image resulting in adverse financial effects

- Sensitive information is generally entity and fact-specific, with its prejudicial effect being hypothetical and difficult to prove.

Cross-cutting issues
Commercial sensitivity – staff's proposed approach

Possible standard-setting approaches to sensitive information

(1) ***No accommodation for sensitivity* concerns** approach

- avoids providing basis for broad non-compliance with IFRS Standards
- IFRS Standards should not be seen as tools to facilitate avoidance of stakeholder and regulatory scrutiny

(2) '***Comply or explain***' approach

- creates incentive for disclosing required information
- allows for exemption where entity determines that costs exceed benefits
- effectiveness depends on market and regulatory environments

(2a) ***'Comply or explain'*** approach ***with constraints***

- similar to 'comply or explain' approach but:
  - temporary disclosure exemption if criteria specified by the IFRS Standard are satisfied;
  - requires disclosure when potential cost of disclosures reduces;
  - audit committee or board or directors could be required to take explicit responsibility for non-disclosure;
- provides auditors and regulators basis for enforcement to avoid abuse
- criteria difficult to articulate because of fact-specific sensitivities

(3) ***Tailor disclosure*** requirements to reflect concerns

- seeks to provide relevant information indirectly via inference where possible
- compromise between needs of users and preparers

(4) ***Voluntary disclosure*** approach

- relies on market to penalise poor disclosure
- creates a burden for investors to obtain information
- market may not function effectively in penalising poor disclosure due to transparency
- may be subject to abuse

Staff's proposed approach for the Practice Statement (subject to change depending on the input received from the Advisory Council)

We consider proposing ***'comply or explain' approach with constraints***

- Information provided in management commentary will ordinarily be at a higher level than is useful to the entity's competitors.
- If management considers that the disclosure of detailed information about impending developments or matters in the course of negotiation would be seriously prejudicial to the interests of the entity, the management:

(a) provides summarised information about the developments or matters that is as detailed as possible but without being seriously prejudicial to the interests of the entity;

(b) considers whether information in the management commentary may be misleading without the context of the excluded information, and if so, management adapts the content and tone of the management commentary accordingly; and

(c) describes the process undertaken to determine that it was appropriate to exclude material information from the management commentary.

- The exclusion of material information is:

(a) applicable only if permitted by the entity's legal and regulatory environment; and

(b) limited to situations when providing that information would cause serious prejudice to the entity's interests in impending developments or in ongoing negotiations which are not in the public domain, for example when the entity is in negotiations to acquire another entity.

Cross-cutting issues
Overlap with corporate governance reporting – issue

- Corporate Governance codes and reporting have attracted increased attention in recent years. In an analysis of annual report's components, the UK's Financial Reporting Council (FRC) describes the objective of a corporate governance report to be "*To provide information necessary to explain how the composition and organisation of the entity's governance structures supports the achievement of the entity's objectives*". We see some correlation with the objective of management commentary related to providing information to help users assess management's **stewardship** of the entity's economic resources. We reviewed the following Corporate Governance codes to identify whether and how the reporting requirements set by those codes could overlap with those for management commentary:
  (a) The UK Corporate Governance Code (issued by the FRC in 2018)
  (b) Corporate Governance Principles and Recommendations (4th edition issued by the Australian Securities Exchange (ASX) Corporate Governance Council in 2019)
  (c) Japan's Corporate Governance Code (issued by the Tokyo Stock Exchange (JPX) in 2018)

  In addition, we note that South Africa's King IV Corporate Governance Code endorses the use of the International Integrated Reporting Framework.

- While the UK Corporate Governance Code sets requirements for reporting in accordance with the code's principles and provisions, the Japanese and Australian codes also contain general principles on reporting which could relate to management commentary:

> ***ASX Corporate Governance Principles and Recommendations***
>
> Principle 5: A listed entity should make timely and balanced disclosure of all matters concerning it that a reasonable person would expect to have a material effect on the price or value of its securities.

> ***Japan's Corporate Governance Code***
>
> Principle 3 - Ensuring Appropriate Information Disclosure and Transparency: The board should actively commit to ensure that disclosed information, including non-financial information, is as valuable and useful as possible [avoiding boiler-plate].

- The three codes all require reporting on:
  (a) the board's (and related committees') responsibilities and attendance at meetings
  (b) nomination/selection policies and succession planning
  (c) identification of independent directors and independence policies
  (d) process of evaluating board effectiveness
  (e) exposure to risks and actions taken to mitigate them
  (f) remuneration policies for board and senior management
  (g) entity's diversity policy and related objectives

- Other reporting requirements in these codes include:
  (a) explaining board's corrective actions where board is not satisfied that policy, practices or behaviour are aligned with entity's purpose, values and strategy (FRC)
  (b) discussing strategy and business plans, presenting targets for profitability and capital efficiency and explaining clearly allocation of resources (JPX)
  (c) articulating the entity's values (ASX)
  (d) describing the sustainability of the entity's business model and how the board's governance contributes to the delivery of its strategy (FRC)
  (e) disclosing a board skills matrix of the skills it has and those the board is looking to achieve, to show it has the necessary skills to fulfil its obligations and meet business needs (ASX)
  (f) describing the policies aimed at promoting constructive dialogue with shareholders (JPX)

Cross-cutting issues
Overlap with corporate governance reporting – staff's proposed approach

We note that many of the areas covered in this Stream have a potential overlap with corporate governance disclosures; for example:

(a) the entity's plans and actions in pursuit of the entity's purpose and objectives, including the setting of its purpose and objectives, and the establishment of culture to support them;

(b) the entity's funding strategy;

(c) the entity's policies, monitoring and management in relation to resources and relationships that the entity depends on for its success and the entity's impacts on those resources and relationships;

(d) the entity's risk monitoring, mitigation, and response procedures; and

(e) the entity's operating environment and the process for monitoring it.

The question of where to draw the line between information to be included in management commentary and information on corporate governance is a subjective one. An entity's governance processes may be important for understanding management's stewardship of the entity's economic resources, but a requirement to report on them could extend the scope of the Practice Statement which does not currently refer to *corporate governance*. We also highlight that the setting of national corporate governance reporting requirements may be undertaken by a different body to that which is responsible for national management commentary requirements.

Whilst the structure of and information to be included in management commentary could potentially provide a basis for developing corporate governance reporting requirements, we are not suggesting that the Practice Statement should be used to develop those disclosures. We propose that the Practice Statement should *not* make an explicit reference to corporate governance disclosures, but recognise that information about corporate governance may need to be included in management commentary, either directly or by cross-referencing to other reports (see slides 16-17) if such information could influence users' assessments of the prospects for the future net cash inflows to the entity and of management's stewardship of the entity's economic resources.

Cross-cutting issues
Cross-referencing (1/2)

Issue

- At the previous Consultative Group meetings we have heard concerns about duplication of information (1) between management commentary and financial statements and (2) between management commentary and other reports. Some topics covered by this Stream overlap with other reports. Therefore, we would like to discuss how cross-referencing could be used to avoid duplication.

The 2010 Practice Statement

- The 2010 Practice Statement discusses management commentary as being supplementary to financial statements. The 2010 Practice Statement does not explicitly refer to cross-referencing but discusses the need to avoid duplication.

> 23(b) When practicable, management should avoid duplicating in its management commentary the disclosures made in the notes to its financial statements.

- The 2010 Practice Statement does not discuss the link between management commentary and other reports provided by the entity.

Staff's proposed approach

- We propose including in the Practice Statement guidance on incorporating information into management commentary by cross-referencing. The aim of this guidance would be:

(a) on the one hand, to avoid duplication and encourage coherent and understandable discussion in management commentary; and

(b) on the other hand, to avoid excessive cross-referencing that may lead to fragmentation of information.

- We propose introducing:

(a) a principles-based approach to the interaction between management commentary and financial statements and incorporation of information by cross-referencing (see slide 17). We propose that similar principles should also apply when incorporating information in management commentary by cross-referencing to other reports.

(b) restrictions on providing cross-references from management commentary to financial statements and to other reports (see slide 17).

(c) a requirement that where information is included by cross-referencing to other reports, the specific section being referenced will be considered to form part of management commentary and will be subject to all the requirements of the Practice Statement.

In developing this approach, we have considered proposals on location of information in the Board's 2017 Discussion Paper *Disclosure Initiative—Principles of Disclosure* and feedback received on those proposals.

Cross-cutting issues
Cross-referencing (2/2)

Principles-based approach to incorporation of information by cross-referencing (to avoid duplication and encourage coherent and understandable discussion)

(a) management commentary should include ***all relevant information*** needed to meet the objective of management commentary, either directly or by cross-referencing;
(b) information provided, either directly or by cross-referencing, should ***faithfully represent the substance*** of the relevant matter;
(c) management commentary can incorporate information by cross-referencing to financial statements or other reports to provide a ***coherent discussion*** and ***avoid duplication*** of information in these reports;
(d) incorporation of information by cross-referencing should not be done in a way that hinders ***understandability*** and ***neutrality*** of management commentary.

Restrictions on providing cross-references (to avoid excessive cross-referencing that may lead to fragmentation of information)

(a) the reference should be to a ***precisely specified part*** of the document;
(b) the referenced document should be available:
(i) at the same (or approximately the same) ***time*** as management commentary;
(ii) on the same ***terms**** as management commentary; and
(iii) ***for as long as*** the management commentary is available.
(c) the referenced information is ***current*** at the date the management commentary is approved and ***cannot be changed*** after the management commentary has been approved (unless the change is highlighted in an updated management commentary).

* Ie, users should have access to the referenced material on the same basis as they have for accessing management commentary

Example 1—cross-reference to notes to financial statements

IFRS 7 *Financial Instruments: Disclosures* requires entities to disclose breaches of loan agreements during the reporting period.
If information about a breach is material to understanding the entity's financial position, management commentary should include information about the breach and its implications.
Such information could be provided by identifying the issue (ie the breach of a loan agreement) and cross-referencing the specific note in the financial statements. However, it would not be sufficient to simply include a general cross-reference saying 'Note X to financial statements discusses the entity's loan agreements' because that would not help users understand the substance of the issue.

Example 2—cross-reference to other reports required in local jurisdiction

Local regulation might require an entity to provide a risk report. If the report discusses issues that may materially affect the entity's future performance and position, management commentary should inform the users that such issues exist and may provide the further information that users need through a cross-reference to the precisely specified part of the risk report.

Example 3—cross-reference to other published reports

Management may decide to provide in management commentary information about customer satisfaction based on a survey. In this case, management commentary may include directly a summary, comprising the material information, of the results and methodology, but include a more detailed breakdown of the survey results by cross-referencing to the publicly available report on the survey (for example, when published on the entity's website).

Questions

Questions for the Consultative Group

1. Have we correctly identified the challenges with current reporting practice (slide 4)? Are there additional challenges that we should consider?
2. Do you agree with the staff’s proposed overall approach to Stream 3 (slide 7) and the related discussion of management commentary architecture (slide 9)? If not, why and what do you propose instead?
3. Do you agree with the staff’s proposed approach to commercially sensitive information in management commentary (slide 13)? If not, why and what do you propose instead?
4. Do you agree with the staff’s conclusions on overlap between corporate governance reporting and management commentary (slide 15)? If not, why and what do you propose instead?
5. Do you agree with staff’s proposed approach to incorporation of information by cross-referencing and the restrictions on providing cross-references (slides 16–17)? If not, why and what do you propose instead?

Appendix

Appendix
Alignment with common themes in narrative reporting (1/4)

- At the September 2018 meeting of the Consultative Group, we discussed eight common themes in the development of narrative reporting:
    1. Long-term value creation
    2. Resources and relationships
    3. Business model focus
    4. Narrative coherence
    5. Application of materiality
    6. Operational information
    7. Sustainability reporting
    8. Stewardship and culture
- Staff's proposed approach to each theme in Stream 3 is summarised on the following slides to show how each theme is being considered.
- Consultative Group members also stressed the importance of addressing the entity's purpose, which we propose to include in the discussion of the entity's strategy (see Slide Deck 3).

Alignment with common themes in narrative reporting (2/4)

What we said in September 2018:

	Why it matters	*How the staff plan to address it*	*Staff's proposed approach for Stream 3:*
Long-term value creation	There is a widespread concern that corporate reporting does not address the full range of matters related to an entity's long-term prospects	• Link the objective of management commentary to assessment of the prospects for future net cash inflows and to providing insight into the entity's strategy, including over long term	• Focus discussion of the entity's strategy around the pursuit of the entity's purpose (see Slide Deck 3).
Resources & relationships	Users need information about an entity's key resources and relationships irrespective of whether it is appropriate to discuss those resources and relationships in the financial statements	• Information on resources and relationships is a possible area of content of a management commentary • Emphasise the role that reporting on business impacts can play in providing insight into the ongoing health of the entity's relationships	• Integrate discussion of resources and relationships into the business model description, and provide guidance on how to identify resources and relationships for discussion in management commentary. Include an explicit reference to the development of resources and relationships in the strategy content element (see Slide Deck 2), and to their continuous availability in the operating environment and risks content element (see Slide Deck 4). • Recognise the role that the entity's impacts could have on resources and relationships by requiring discussion of impacts in the description of business activities (see Slide Deck 2).
Business model focus	The specific issues and opportunities faced by an entity will be unique to each entity's business model and strategy, even across the same sector	• Retain a principles-based approach to business model reporting with onus on management to identify what is important in the entity's circumstances	• The discussion of business model provides the foundation for applying the principle of narrative coherence in management commentary (see slide 9 and Slide Deck 2 for a summary of how the principle of narrative coherence applies).

IFRS

Alignment with common themes in narrative reporting (3/4)

What we said in September 2018:

	Why it matters	*How the staff plan to address it*
Coherence	The management commentary needs to tell a joined-up story of the business across the content elements without leaving unanswered questions	• An approach which builds the report out from the entity's business model • Coherence identified as a distinct principle that supports the build of a complete 'story' of the business
Application of materiality	Preparers struggle with the application of materiality to narrative and operational performance information	• Provide guidance on the application of materiality judgements eg by making the link between the entity's future net cash inflows and stewardship • Draw a distinction between matters and material information about those matters building on the four-step approach in Materiality Practice Statement
Operational information	Users need operational information to support their assessments of the entity's prospects for future net cash inflows and of stewardship	• Application guidance on the objective of management commentary will explicitly refer to both financial and operational information • The revised Practice Statement will discuss operational performance as a separate content element of management commentary

Staff's proposed approach for Stream 3:

- Narrative coherence is a principle in the staff's proposed approach to the management commentary as a whole – we have summarised how the principle of narrative coherence applies in relation to each of the content elements being discussed today in the relevant decks.

- We seek to emphasise that the entity considers materiality in identifying information to provided in each content element to support the objective of the management commentary. We seek to avoid the use of qualifiers such as '*critical*', '*principal*', and '*key*' as these may be seen as implying alternative levels of materiality.

- Operational performance information was covered in Stream 2 *Performance, position and progress*. The application of principle of *narrative coherence* provides a basis for reporting operational performance information that links to the content elements discussed in Stream 3.

Alignment with common themes in narrative reporting (4/4)

What we said in September 2018:

	Why it matters	*How the staff plan to address it*
Sustainability reporting	Users need relevant ESG information to support their assessment of an entity's prospects for cash flows	• Relevant ESG information will form a part of operational performance discussion and will be subject to same materiality considerations • Reporting on 'resources and relationships' provides useful inputs for assessments of business sustainability
Stewardship & culture	Users use information about the stewardship of an entity's economic resources in assessing the relationship between the risks being taken and expected returns	• Link to stewardship in the objective of management commentary • Consideration of the potential consequences for the entity of its external impacts to be incorporated into discussion of completeness • Recognise the potential linkages between management commentary and governance reporting

Staff's proposed approach for Stream 3:

- Environmental and social considerations to the extent they relate to the objective of management commentary are covered in the discussion of the business model, in particular in the proposed guidance on the entity's *resources and relationships*, and *impacts* (see Slide Deck 2).
- We propose to elevate operating environment and risks as a separate content element, and explicitly refer to long-term factors and risks (see Slide Deck 4).
- We are not proposing to include governance disclosures in management commentary except when some such information is necessary for meeting the objective of management commentary (see slides 14-15).

- We propose explicit reference to stewardship in relation to the entity's business model, recognising the need for information that helps users assess the management's stewardship of the entity's resources.
- We propose to include specific reference to culture in relation to its role in pursuit of the entity's purpose. We are not proposing further guidance on what should be covered on culture in management commentary beyond this, or that culture should be a specific section in management commentary.

Keep up to date

www.ifrs.org

@IFRSFoundation

IFRS Foundation
International Accounting Standards Board

IFRS Foundation

IFRS Foundation