



Management commentary

Slide Deck 4 *Supporting adoption of the Practice Statement*

Consultative Group meeting – 13 December 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.

Supporting adoption of the Practice Statement

Purpose of this session

In this session the staff would like to discuss practical aspects that would support adoption and application of the Practice Statement.

The staff would like the Consultative Group members' views on the staff's analysis of:

- whether a Statement of Compliance with the Practice Statement should be required
- how the principles-based approach of the Practice Statement enables its enforcement by regulators and that it results in an assurable management commentary
- how the Practice Statement interacts with other reporting frameworks
- how to support preparers through use of application guidance

Contents:

- Statement of compliance (slides 3–10)
- Enforceability of the Practice Statement and assurability of management commentary (slides 11–20)
- Interaction of the Practice Statement with other reporting frameworks (slides 21–28)
- Supporting application by preparers (slides 29–35)



Statement of compliance

Statement of Compliance

Purpose of this section

This section focuses on whether the Practice Statement should require the management commentary to include a statement of compliance. The staff see three broad reasons why this might be desirable:

1. Clarity over date of authorisation

The date of authorisation is important as some components of a management commentary may need to be presented as at the date of authorisation, rather than the period end.

2. Clarity over basis of preparation

It should be clear when a document has been prepared in accordance with the Practice Statement.

3. Acknowledgement of responsibility for complying with the Practice Statement

A statement of responsibility could encourage preparers to apply a similar level of due diligence to the preparation and review of the management commentary as for the financial statements. The implications of a responsibility statement compared to an approval statement will be considered.

Consultative Group members are asked for their views on the merits of requiring a compliance statement, what it should cover, and whether they anticipate that such a requirement could give rise to practical difficulties.

Contents:

- Date of authorisation (slide 5)
- Basis of preparation (slide 6)
- Acknowledgement of responsibility (slides 7–9)
- Question for the Consultative Group (slide 10)

Statement of Compliance

Date of authorisation

IAS 10 includes a requirement for the date of authorisation of the financial statements to be stated. The staff think the reason for requiring a date cited in IAS10 applies equally to management commentary. Furthermore, it cannot be assumed that the date of approval of the management commentary is the same as that for the financial statements.

Staff proposal

For the reasons above, the staff think requiring a date of authorisation would be helpful for users.

IAS10 §17-18

Date of authorisation for issue

An entity shall disclose the date when the financial statements were authorised for issue and who gave that authorisation. If the entity's owners or others have the power to amend the financial statements after issue, the entity shall disclose that fact.

It is important for users to know when the financial statements were authorised for issue, because the financial statements do not reflect events after this date.

Statement of Compliance

Basis of preparation

Circumstances in which the Practice Statement might be applied

Because compliance with the Practice Statement is not required in order to state compliance with IFRS Standards, there are a number of situations in which the Practice Statement might be applied:

- The Practice Statement may be mandated by the standard setter or regulator in a jurisdiction
- The Practice Statement may be applied voluntarily by an entity
- The Practice Statement may be applied as a means of meeting a high-level regulatory requirement where the entity / regulator has concluded that the requirement is aligned with the Practice Statement

It is also possible that parts of the Practice Statement may be applied on an ad hoc basis, for example because guidance is needed on a particular area of content, or because guidance is absorbed into *best practice*.

The staff therefore think it is important that users can distinguish between situations in which the Practice Statement has been applied in its entirety rather than in part.

Use of other frameworks in a management commentary

As discussed in a later section of this session, preparers may use other frameworks to identify information that is useful to users on a particular topic, or to provide a basis for calculating a particular KPI. The staff are supportive of this approach, but think it is important that all information in a management commentary should nevertheless be prepared in accordance with the requirements of the Practice Statement. For example, it would not be appropriate to only include information on a matter as specified by another framework without considering whether the objective of management commentary and the requirements of the Practice Statement are being met.

The staff think that a basis of preparation statement would reduce the risk that preparers ‘blend’ the requirements of the Practice Statement with those of other frameworks.

Staff proposal

The staff think that the factors described above mean that there may be ambiguity over whether the Practice Statement has been applied in full in preparing the whole management commentary. Therefore, a statement that the management commentary has been prepared in accordance with the Practice Statement would provide useful clarity.

Types of statements that acknowledge responsibility

Staff observe that it is common for national regulations to require a statement approving the management commentary, which would also identify the body responsible for it. However, some frameworks go further by asking for statements that:

- Explicitly acknowledge responsibility (rather than just provide a statement of approval)
- Acknowledge or describe the process applied in preparing the management commentary
- Conclude that the management commentary meets certain objectives

Process-based statements

Process-based statements address the diligence with which the management commentary has been prepared. The Integrated Reporting Framework is one example which covers responsibility for ensuring the integrity of the report and the role of those charged with governance in addressing both preparation and presentation of the report. However, staff think the findings of limited uptake in the subsequent Implementation Review illustrate the difficulty of requiring such a statement without the backing of a legal or regulatory requirement.

Integrated Reporting Framework §1.20

Responsibility for an integrated report

An integrated report should include a statement from those charged with governance that includes:

- An acknowledgement of their responsibility to ensure the integrity of the integrated report
- An acknowledgement that they have applied their collective mind to the preparation and presentation of the integrated report
- Their opinion or conclusion about whether the integrated report is presented in accordance with this Framework or, if it does not include such a statement, it should explain:
 - What role those charged with governance played in its preparation and presentation
 - What steps are being taken to include such a statement in future reports
 - The time frame for doing so, which should be no later than the organization's third integrated report that references this Framework.

Integrated Reporting Implementation Review, October 2017

'There was general consensus about the role of those charged with governance vis-à-vis Integrated Reporting, which was seen as crucial to successful adoption of the Framework.... Governance statements of the type described by Paragraph 1.20 are not often seen in practice. Respondents cited various reasons for limited uptake.'

Objectives-based statements

The UK and German frameworks are two examples where the approver of the management commentary is required to include a statement as to its fairness.

The staff think that were the Practice Statement to follow a similar approach, it could align with the objective of management commentary – i.e. that it addresses the *matters that could reasonably be expected to influence assessments by primary users of the amount, timing and uncertainty of the entity's future net cash inflows, and their assessments of management's stewardship of economic resources*^(*)

Germany: GAS20 §234

Statement required on the group management report

'To the best of our knowledge, the group management report includes a fair review of the development and performance of the business and the position of the group, together with a description of the material opportunities and risks associated with the expected development of the group.'

UK Corporate Governance Code §27

The directors should explain in the annual report their responsibility for preparing the annual report and accounts, and state that they consider the annual report and accounts, taken as a whole, is fair, balanced and understandable, and provides the information necessary for shareholders to assess the company's position, performance, business model and strategy.

^(*) Text provided for illustration, based on the illustrative drafting for the objective of management commentary that the Board discussed in November 2018

Interaction with legal and other requirements

The staff think that the significance of a statement of responsibility may be interpreted differently in different legal jurisdictions and this may result in unintended legal consequences. Furthermore, such a statement may overlap with existing regulatory or corporate governance requirements

Staff proposal

Taking account of the above, the staff think the Practice Statement should require the identification of the body approving the management commentary as this may vary by jurisdiction and users need to understand this in order to make use of the document.

Whilst acknowledgements of responsibility would be desirable, the staff think that this question is best dealt with at a jurisdictional level, and therefore do not propose to include further requirements in the Practice Statement

Question 1

Do you agree with the staff proposal that the Practice Statement:

- a) Should require the management commentary to state the date of authorisation;
- b) Should require a statement that the management commentary has been prepared in accordance with the Practice Statement;
- c) Should require the management commentary to identify the body that has approved its issue; and
- d) Should NOT require a statement of the process followed in preparing it or a statement that the management commentary meets a particular objective (e.g. that it is fairly presented)?



Enforceability of the Practice Statement and assurability of management commentary

Purpose of this section

In this section the staff are seeking the Consultative Group's views on whether the requirements and guidance that the staff's propose to include in the revised Practice Statement would be enforceable and whether they would provide a suitable basis for external and internal assurance of management commentaries prepared in accordance with the Practice Statement.

Contents:

- How the Practice Statement can contribute to assurability and enforceability? (slide 13)
- IAASB analysis of the characteristics of a 'sound' framework (slide 14)
- Staff's proposals that should support assurability (slides 15–19)
- Question for the Consultative Group (slide 20)

How the Practice Statement can contribute to enforceability and assurability?

The staff think that the uptake of the revised Practice Statement is likely to depend not only on how well it helps preparers prepare management commentary but also on whether the Practice Statement provides a suitable basis for:

- enforcement if it has been mandated by regulators;
- external assurance of management commentaries if required; and
- internal assurance and due process on behalf of audit committees and others charged with governance.

In October 2019, the Board tentatively decided that the revised Practice Statement should retain the statement that it does not mandate the level of assurance to which management commentary should be subjected. (Similarly, IFRS Standards do not mandate whether financial statements prepared in accordance with the Standards should be assured.)

The Board also tentatively decided that the Practice Statement should include a description of verifiability based in paragraphs 2.30 and 2.32 of the *Conceptual Framework* and requirements intended to promote provision of information in management commentary that is verifiable (see also a summary of the Board's tentative decisions to date in Slide Deck 1).

2.30 Verifiability helps assure users that information faithfully represents the economic phenomena it purports to represent. Verifiability means that different knowledgeable and independent observers could reach consensus, although not necessarily complete agreement, that a particular depiction is a faithful representation. Quantified information need not be a single point estimate to be verifiable. A range of possible amounts and the related probabilities can also be verified.

2.32 It may not be possible to verify some explanations and forward-looking financial information until a future period, if at all. To help users decide whether they want to use that information, it would normally be necessary to disclose the underlying assumptions, the methods of compiling the information and other factors and circumstances that support the information.

Guidance on verifiability is only part of the guidance in the revised Practice Statement that could help regulators, assurers and audit committees enforce the Practice Statement and assure or review management commentary.

In this section the staff have provided an overview of the staff's proposed principles-based guidance and requirements for the Practice Statement that would promote enforceability and assurability. The overview is based on how the proposals could help in assurance of management commentary because the staff think that if the Practice Statement provides a suitable basis for external assurance, it would also provide a suitable basis for enforcement and internal assurance.

IAASB analysis of the characteristics of a ‘sound’ framework

The staff have considered how the staff’s proposals for the Practice Statement correspond to the International Auditing and Assurance Standards Board (IAASB)’s proposed description of a ‘sound’ extended external reporting (EER) framework*

Characteristics of an EER framework that are likely to engender credible reporting*	IAASB characteristics of suitable criteria*	IASB staff’s comment on the corresponding proposals for the revised Practice Statement (detailed proposals are summarised on slides 15–19)
Has an objective that reflects the users’ expectations as to the scope, intended users and intended use of the EER report	Relevance	1. The Practice Statement is intended to provide an objective basis for determining the content of a management commentary that reflects users’ needs and can be consistently applied (ie different parties would reach the same conclusion on the content required for an entity) – slide 15
Consistently includes and reliably depicts all relevant reportable content elements that are material to the intended users in the context of the intended purpose of the EER report	Relevance, completeness, reliability	2. The Practice Statement is intended to provide an objective basis for determining whether the <u>range of matters</u> addressed is complete – slide 16 3. The Practice Statement is intended to provide an objective basis for determining whether the <u>information provided on each matter</u> is complete – slide 17
Recognizes areas of uncertainty, ambiguity and judgment that give rise to inherently greater susceptibility to preparer bias risk and establishes adequate disclosure and neutrality principles to counter this	Neutrality, completeness	4. The Practice Statement is intended to provide guidance on the basis for preparing a management commentary that can be objectively and consistently applied – slides 18–19
Promotes transparent (open), clear (unambiguous) and concise (readily understandable) reporting of these matters, and enables effective comparability both with other pertinent entities and over time	Relevance, reliability, understandability	

* See IAASB Extended External Reporting Consultation Paper, page 79; February 2019

How staff's proposals correspond to the IAASB description of a 'sound' EER framework	Related staff proposals
<p>1. The Practice Statement is intended to provide an objective basis for determining the content of a management commentary that can be consistently applied (i.e. different parties would reach the same conclusion on the content required for an entity).</p>	<p>Set a clear overarching objective that a management commentary must meet The Board broadly agreed that the objective of management commentary would focus on providing primary users with information useful for their assessments of prospects for the entity's future net cash inflows and of management's stewardship of the entity's resources. The Board also tentatively decided to make an explicit link between identification of material information and the objective of management commentary – that is in making materiality judgements management would need to consider what information would be useful for users' assessments. This approach will require both management and an assurer to have a clear understanding of the basis on which the entity's future net cash inflows would be expected to be modelled, and the assumptions that would drive this.</p>
	<p>Set a 'test of success' for each area of content in a management commentary The staff intend to propose a disclosure objective for each content element that provides an overall 'test of success'. Each disclosure objective is defined in terms of the user needs that the information must meet (see Slide Deck 3).</p>
	<p>Ensure the requirements of the Practice Statement are unambiguous The staff anticipate proposing directive language wherever possible. However, there may be alternative approaches to a particular disclosure that would satisfy the disclosure objective of each content element, therefore some components of the Practice Statement are expected to be set out as guidance (for achieving the disclosure objective).</p>

How staff's proposals correspond to the IAASB description of a 'sound' EER framework	Related staff proposals
<p>2. The Practice Statement is intended to provide an objective basis for determining whether the range of matters addressed is complete</p>	<p>Determining the matters to be covered in a management commentary The staff think proposed guidance on the application of materiality that (i) identifies practical sources for identifying matters that need to be discussed (for example, information used in managing the business), and (ii) explains the application of narrative coherence would provide an objective basis for determining the matters to be covered in a management commentary. The staff anticipate that an assurance practitioner might then apply their knowledge of the entity to determine whether the management commentary included all relevant matters based on (i) their understanding of the business, its transactions and relationships; (ii) their understanding of the entity's strategy (for example, based on what the board and management committees have discussed); (iii) the outcome of the entity's own risk and opportunity management processes; and (iv) their understanding of the causes of trends and factors that have emerged in the entity's historical financial or operational performance.</p> <p>Determining whether to include an uncertain matter in a management commentary The staff think that the question of when to address a matter whose outcome is uncertain is particularly important in determining the matters to be addressed. The staff propose that the Practice Statement should provide guidance to deal with the question of when an uncertain matter should be addressed, specifically that:</p> <ul style="list-style-type: none"> a) uncertain matters are addressed based on consideration of whether knowledge of the matter could reasonably be expected to affect a user's assessment of future cash flows; b) time value, likelihood and magnitude of the potential effects of a matter on the entity's future cash flows should be taken into account; c) matters arising from systemic factors should be addressed where applicable; and d) uncertain matters that could affect the entity's future cash flows should be described regardless of whether the management's strategy mitigates those risks (see also slide 17 of Slide Deck 3).

How staff's proposals correspond to the IAASB description of a 'sound' EER framework	Related staff proposals
3. The Practice Statement is intended to provide an objective basis for determining whether the information provided on each matter is complete	Introduce guidance on narrative coherence (see Slide Deck 2) to promote provision of information on a matter across all content elements.
	Provide guidance on the information expected to be provided for each content element , but do not make assumptions over the matters that the information needs to address. Slide Deck 3 summarises the staff's proposals for guidance on: <ul style="list-style-type: none">a) strategy (slides 11–12);b) business model (14–15);c) risks and operating environment (slides 17–19);d) performance, position and progress (slides 21 – 24).

How the staff's proposals correspond to the IAASB description of a 'sound' EER framework	Related staff proposals
<p>4. The Practice Statement is intended to provide guidance on the basis for preparing a management commentary that can be objectively and consistently applied</p>	<p>Neutrality: The Board has tentatively decided that the Practice Statement should:</p> <ul style="list-style-type: none"> a) explain that for a depiction of a matter to be neutral, information about it cannot be omitted, obscured, given undue prominence or otherwise manipulated to influence primary users' view of the matter favourably or unfavourably; b) explain that neutrality of management commentary as a whole depends on: (i) how prominently matters are reported and (ii) overall tone and language; and c) introduce requirements for describing ranges of uncertain outcomes, to avoid misleading descriptions.
	<p>Relevance / materiality: The staff have previously highlighted the perception that materiality is difficult to apply to qualitative information and matters affecting the longer term. The staff believe these challenges are addressed by the Board's recent tentative decisions in relation to materiality, in particular that the Practice Statement should:</p> <ul style="list-style-type: none"> a) include an explicit link between the identification of material information and the objective of the management commentary of providing information useful in assessing the entity's future net cash inflows and management's stewardship of its economic resources; and b) identify practical sources that indicate a matter should be addressed in the management commentary, including whether information on the matter is used in managing the business, and whether the matter is addressed in the entity's capital market communications.
	<p>Completeness: The Board has tentatively decided that completeness should be based on meeting primary users' information needs and requires material information about the nature of the matter and the facts and circumstances that might affect it.</p>

How staff's proposals correspond to the IAASB description of a 'sound' EER framework	Related staff proposals
<p>4. The Practice Statement is intended to provide guidance on the basis for preparing a management commentary that can be objectively and consistently applied <i>(continued)</i></p>	<p>Comparability</p> <p>The Board tentatively decided that the Practice Statement should require management to:</p> <ul style="list-style-type: none"> a) consider that users need to make comparisons with information provided by other entities, by the entity in previous periods and with other information published by the entity; and b) explain assumptions, methods of calculations and any changes (including reasons for) from the previous year, highlight where new information is provided on a matter previously reported, provide comparative information to allow emergence of trends and consider whether information is consistent with information in the financial statements and other information.
	<p>Information based on judgement in a management commentary</p> <p>Where information in management commentary is based on judgement, the Board tentatively decided to require management to 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. This is intended to help (i) users make an informed determination of the extent of reliance they are prepared to place on the information; and (ii) assurers consider the underlying assumptions and basis of preparation without taking responsibility for the application of management's judgement.</p>
	<p>Forward-looking information</p> <p>It is not proposed that the Practice Statement would require management to prepare forecasts or targets for inclusion in management commentary. However, if management has published elsewhere forecasts or targets, it is anticipated that they should be included in management commentary. The following proposals would help in assuring forecasts and targets if they are included in management commentary:</p> <ul style="list-style-type: none"> a) requirement to describe the basis of preparation of the information; b) requirement to identify risks and assumptions; c) requirement to explain the extent to which risks and assumptions take account of matters identified elsewhere in the management commentary.

Question 2

Have the staff achieved the right balance in developing proposals for guidance and requirements that would promote enforceability of the Practice Statement and assurability of management commentaries prepared in compliance with the Practice Statement?



Interaction of the Practice Statement with other reporting frameworks

Interaction of the Practice Statement with other reporting frameworks

Purpose of the section

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The Practice Statement is designed to guide entities in meeting the objective of management commentary of providing useful information to primary users.

However, other reporting frameworks can also play an important role in developing an entity's management commentary.

The staff seek input from the Consultative Group on the interaction of the Practice Statement with other reporting frameworks.

Proposed components of the Practice Statement

OBJECTIVE

- Establishes focus on providing information useful to primary users in assessing future cash flows and management's stewardship as a context for the financial statements.

BASIS OF PREPARING

- Based on the concepts for providing useful financial reporting in the *Conceptual Framework for Financial Reporting (Conceptual Framework)*.
- Provides practical guidance to address key gaps in reporting practice, in particular guidance on materiality, neutrality and completeness.

CONTENT ELEMENTS

- Provides principles-based guidance for building a coherent narrative across topics (content elements) that are expected to be discussed in management commentary to meet primary users' information needs:
 - business model;
 - strategy;
 - risks and operating environment; and
 - performance, position and progress.
- Provides basis for determining entity-specific content that is aligned with the entity's strategic priorities.

Specifically, the staff seek input on:

- including information identified applying other reporting frameworks in management commentary (slides 23–25); and
- using management commentary in meeting other reporting objectives or meeting information needs of other stakeholders (slides 26–27).

The question for the Consultative Group is on slide 28.

The staff do not seek to address whether and how the Practice Statement might be used in applying other reporting frameworks (for example, in making materiality judgements).

ROLE OF OTHER FRAMEWORKS

Other frameworks may help to identify relevant, comparable information on a matter but are not part of the Practice Statement

Industry guidance

Topic guidance

Information identified applying other reporting frameworks may be useful for the primary users of a management commentary

As previously discussed, the Practice Statement cannot identify all information that may need to be provided in a management commentary. Attempting to do so could create the following risks:

- (i) relevant information may be omitted if the matter is not explicitly identified in the Practice Statement and the preparer applies a 'checklist approach' to disclosure; and
- (ii) irrelevant information may be provided simply because the matter is identified in the Practice Statement.

The staff see benefits in applying other reporting frameworks that identify information to be provided on a particular subject in preparing management commentary. Doing that would:

- (i) support comparability of management commentaries; and
- (ii) help preparers identify relevant information.

For this reason, the staff think that the Practice Statement should acknowledge that preparers may use other reporting frameworks in preparing management commentary.

The staff note that other reporting frameworks may either set out specific requirements for presenting information (for example, on how to calculate 'scope 3' carbon emissions) or provide broad requirements for information that must be provided on the subject (for example, describe the scope of information that may need to be provided on a topic). The staff think that either type of framework may help in preparing a management commentary. The staff further note that many frameworks that address ESG factors can help in preparing management commentary, as well as frameworks that cover other topics (such as natural resources, intellectual capital, market share).

However, the staff do not propose identifying in the Practice Statement specific frameworks that may be used in preparing a management commentary. This is because the content of reporting frameworks may change over time. Besides, identifying any specific frameworks may be misinterpreted as endorsement.

The staff identified concerns about using other reporting frameworks in preparing management commentary:

1. **The information required by other reporting frameworks may not meet the objective of management commentary. This is because:**
 - a) information may be required to be presented at a level that obscures a trend that would be important for a user of a management commentary.

Some frameworks appear to prioritise comparability over relevance by requiring entity-wide information. However, users of the management commentary may need more granular information. For example, an entity may have a positive water consumption trend that is required to be disclosed by another framework. However, consumption for its key water-stressed site may show a negative trend.

- b) information may not be sufficient to help users assess the effect of the matter on the entity's prospects for future cash flows.

For example, a preparer may assume that information required by another framework is sufficient for users of management commentary whereas those users need different or additional information.

- c) information may not be relevant for users of management commentary.

For example, a preparer may be reluctant to exclude immaterial information that is required by another framework, and may include a block of information without explaining the links to related content in the management commentary, instead of focusing on the specific matter that needs to be addressed in the management commentary.

2. **Other reporting frameworks might use a different basis for preparing reports.**

The basis of preparation specified in other reporting frameworks may differ from the basis in the Practice Statement. However, in some cases, information prepared on a different basis may still be useful for users of a management commentary.

The staff think that information included in a management commentary, including information identified applying other reporting frameworks, must meet the requirements of the Practice Statement, including the objective of and the basis for preparing a management commentary.

Specifically, with respect to the concerns identified on slide 24:

- The staff have previously discussed guidance on the level at which information should be aggregated in a management commentary. That guidance would equally apply to information identified applying other reporting frameworks regardless of the basis of preparation specified in those frameworks.
- The staff have previously discussed guidance on materiality and completeness of information in management commentary as well as guidance on narrative coherence. That guidance would equally apply to information identified applying other reporting frameworks regardless of the basis of preparation specified in those frameworks.

Accordingly, the staff think that there is not need to provide guidance on including in a management commentary information identified applying other reporting frameworks. However, the staff think it would be helpful to explain in the Practice Statement that:

- a) information identified applying other reporting frameworks must meet the requirements of the Practice Statement (eg it must be material); and
- b) management commentary prepared applying other reporting frameworks in addition to applying the Practice Statement must meet the requirements of the Practice Statement (eg it must be complete).

The staff think that in principle it may be desirable to include in a management commentary information that supports other reporting objectives or meets information needs of other stakeholders.

Consultative Group members have previously highlighted that a management commentary may be useful to a broader set of stakeholders than the primary users.

The staff recognise that some information included in a management commentary, such as information about the entity's business model and strategy, may provide a useful foundation for understanding the entity for a broad range of users of information. Furthermore, different users may have a common interest in particular performance measures. Finally, using one document to support multiple reporting objectives or various users' needs helps to avoid duplication of information and reduces the risk that inconsistent information is presented to different audiences.

From a primary users' perspective, such an approach may be desirable as it provides confidence that they are receiving the same 'story' through the management commentary as the entity is presenting to its other stakeholders.

In particular, the staff think some might wish to use the management commentary as the 'core' in a 'core and more' type reporting model. The staff use 'core and more' terminology loosely here to cover reporting models which supplement a central 'core' of information with more specific information to address particular reporting objectives. The term is used by Accountancy Europe, but other terms such as 'hub and spoke' are also used to represent a similar notion.

The staff are seeking the Consultative Group's views on whether such an approach is desirable, and if so, what the Practice Statement should and should not do to support this.

Ways in which the Practice Statement could support a 'core and more' type approach:

The staff identified two areas in which the Practice Statement might support such an approach:

1. The Practice Statement could permit 'signposting' to immaterial information in other documents.

The staff use the term 'signposting' to refer to information that is provided outside management commentary which is not material to distinguish it from material information included in other reports that is incorporated in a management commentary by cross-referencing.

The staff think that permitting 'signposting' to other information should not be problematic provided that it is clear in the management commentary that such additional information does not form part of the management commentary and is not material.

2. The Practice Statement could permit the inclusion in a management commentary of information that is immaterial if that is required by laws and regulations in the entity's jurisdiction and both of the conditions set out below are met.

The staff anticipate this may be helpful to other users of the report but think that if it were to be permitted, the Practice Statement should include requirements to ensure that the *other information* is not confusing for primary users. Specifically, (i) such information should be separately identified in order to preserve the conciseness of the information presented to primary users; and (ii) management should explain any differences in trends reported in the *other information* to those presented to primary users (for example, because the information is presented on a more aggregated basis).

Question 3

Do you agree with the staff's proposed approach for:

- a) including information in a management commentary identified applying other reporting frameworks (see slides 23–25); and
- b) the use of management commentary to meet other reporting objectives or information needs of other users (see slides 26–27)?



Supporting application by preparers

Supporting application by preparers

Purpose of this section

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In the 'Overview of the staff's current proposals' slide deck the staff provided an overview of proposed requirements and guidance intended to help management prepare management commentaries that meet primary users' information needs. In this section, the staff would like to discuss whether, and how, further application guidance (through illustrations and examples) may need to be provided to support management in meeting the requirements of the Practice Statement in preparing management commentaries. Such application guidance may be particularly desirable in areas which are considered challenging in practice, for example the application of materiality.

There are different options of how such guidance can be provided, whether within the Practice Statement itself or in separate publications as supplementary guidance. The staff would like to obtain the Consultative Group's views on how helpful the different options would be for preparers.

Contents:

- Options for providing application guidance (slides 31–33)
- Considerations in providing application guidance (slide 34)
- Question for the Consultative Group (slide 35)

The existing Practice Statement does not contain any application guidance or examples.

The options presented are based on the staff's analysis of how application guidance is provided in:

- IFRS Standards;
- IFRS Practice Statement 2 *Making materiality judgements* (Materiality Practice Statement);
- IFRS *Disclosure Initiative* Case Studies – Better communication: Making disclosures more meaningful;
- Other reporting frameworks:
 - FRC Guidance on Strategic Report;
 - European Commission Guidelines on non-financial reporting (EU NFR Guidelines);
 - US SEC Interpretation – Interpretation: *Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations* (SEC Interpretation);
 - International Integrated Reporting Framework;
- Other guidance:
 - Financial Reporting Lab reports;
 - Accountancy firms' guidance.

Options for guidance within the Practice Statement

The staff have identified the following examples of different formats of application guidance which could be incorporated within the Practice Statement:

- **Appendices:** IFRS Standards sometimes include an appendix with application guidance on specific paragraphs within that Standard. This guidance is typically narrative text, and occasionally includes application examples and decision trees. Such appendices are an integral part of the Standard. These appendices sometimes refer to **accompanying guidance** which includes illustrative examples or implementation guidance. This accompanying guidance is not an integral part of the Standard, and the Standard can be applied without the accompanying material.
- **Examples within text:** The International Integrated Reporting Framework explains some of its requirements by including an example within the related paragraph.
- **Footnotes:** The SEC Interpretation includes examples and explanations in footnotes. The footnotes also include external references to other SEC regulations and Interpretive Releases.

Options for guidance within the Practice Statement (continued)

- **Call-out boxes:** The Materiality Practice Statement, the FRC's Strategic Report Guidance, and the EU NFR Guidelines, highlight examples in a box, usually following the related requirement. The staff include some examples below:

Example L—prior-period information not previously provided

Background

In the prior period, an entity had a very small amount of debt outstanding. Information about this debt was appropriately assessed as immaterial in the prior period, and so the entity did not disclose any maturity analysis showing the remaining contractual maturities or other information that would otherwise be required by paragraph 39(a) of IFRS 7 *Financial Instruments: Disclosures*.

In the current period, the entity issued a large amount of debt. The entity concluded that information about debt maturity was material information and disclosed it, in the form of a table, in the current-period financial statements.

Application

The entity might conclude that including a prior-period debt maturity analysis in the financial statements would be necessary for primary users to understand the current-period financial statements. In these circumstances, a narrative description of the maturity of the prior-period balances of the outstanding debt might be sufficient.

Source: Materiality Practice Statement



Example

An entity in the extractive industry may include its total proven and probable reserves within the strategic report as one of its non-financial **key performance indicators (KPIs)**. The provision of the disaggregation of these totals is an example of complementary information that is not required to meet the objectives of a strategic report. Some companies may include this complementary information as part of their annual report within a separate, non-statutory component of the annual report.

Linkage example

For instance, where an entity is reliant on technological innovation, this is likely to be reflected in the disclosed KPIs, the review of the business and the principal risks and uncertainties.

Similarly, where the entity is reliant on a highly trained and engaged workforce, or other stakeholder relationships, this should be apparent in different elements of the strategic report which should set out how the entity manages, measures and nurtures those relationships.

Source: FRC Guidance on Strategic Report

Example and KPIs

A bank may consider that its own water consumption in offices and branches is not a material issue to be included in its management report. In contrast, the bank may assess that the social and environmental impacts of projects that it funds and its role in supporting the real economy of a city, a region or a country are material information.

Source: EU NFR Guidelines

Options for guidance supplementary to the Practice Statement

- As referred to on slide 31, IFRS Standards have accompanying guidance which includes **illustrative examples** for different scenarios. If similar supplementary illustrative examples were to be provided for the Practice Statement, the Board would need to consider whether to provide:
 - examples which illustrate the process of what to consider in identifying and presenting information; and/or
 - examples of what the expected content should be.
- In 2017, the Board published *Better communication: Making disclosures more meaningful*, a report which contained 6 case studies of public companies' reporting. The **case studies** illustrated disclosures before and after the companies implemented a change in the way they communicated information. A case study report could be prepared based on what is identified as 'best practice' in existing management commentary practice, and would illustrate what is intended by the requirements of the Practice Statement. Alternatively, such a report could include **pilot case studies** of companies which apply the proposed Practice Statement, and compares to previous reporting, to illustrate desired changes in reporting practice.
- The FRC's Financial Reporting Lab undertakes projects on different aspects of narrative reporting and the resulting reports provide **investor perspectives** and examples or case studies of company reporting on that particular aspect of reporting, highlighting what is considered useful by investors.
- The alternative to real-life case studies is the development of a **fictitious company** and scenarios to illustrate what a complete (or main sections of a) management commentary would include if the requirements of the Practice Statement were met. Some accountancy firms have developed **illustrative annual reports**.
- Accountancy firms have also produced **practical guides** for implementing narrative reporting requirements. These practical guides tend to include presentation of key concepts of the guidance or requirements in table format, key questions to ask (to assess if requirements are met) and some examples.

Considerations in providing application guidance

Level of detail of application guidance

Whether the application guidance is an integral part of the Practice Statement or is supplemental, the Board would need to consider the type of, as well as level of detail, of the illustrations or examples. Considerations would include whether:

- different scenarios (companies) are considered for each example illustrating a particular requirement, or whether one scenario (company) is considered across different examples, ie create a story or one narrative;
- illustrations are provided for different industries/sectors; and
- examples are provided for specific trends or risks.

Examples or illustrations would need to be presented in such a way that is not interpreted as providing a template or disclosure checklist which results in boilerplate descriptions. Furthermore, examples or illustrations cannot cover every eventuality and would only be indicative of the desired level of reporting.

Other considerations

Other considerations on which type of application guidance to provide would include:

- costs and resources needed to develop the illustrations and examples which could affect the timing of issuing the guidance; and
- challenges (eg compliance approval) and potential risks (eg subsequent reporting malpractice) involved in identifying corporate case studies.

The staff have not selected a proposed course of action, but would like to use this analysis of options and considerations as prompts for discussion, to gather the Consultative Group's views on application guidance.

Question 4

- a) Are there specific areas of the Practice Statement which you think would benefit from application guidance (including illustrations and examples)?
- b) Do you think that the application guidance (including illustrations and examples) should be provided within the Practice Statement or could it be published separately as a supplement to the Practice Statement?
- c) What type of application guidance from the ones illustrated in this section do you think would be most helpful to preparers without resulting in boilerplate descriptions? Is there any other guidance that could be helpful?

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