

STAFF PAPER

July 2019

IASB® meeting

Project	Management Commentary		
Paper topic	Approach to guidance on qualitative characteristics		
CONTACT(S)	Jelena Voilo	jvoilo@ifrs.org	+44 (0)20 7246 6914
	Yulia Feygina	yfeygina@ifrs.org	+44 (0)20 7332 2743

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Purpose of this paper

1. This paper provides an overview of the staff's approach to developing guidance on considering the qualitative characteristics of useful financial information in preparing management commentary. That guidance would be for inclusion in the revised IFRS Practice Statement 1 *Management Commentary* (Practice Statement).
2. The paper is for information only and does not ask the Board for decisions. Staff recommendations for guidance on particular qualitative characteristics will be presented in separate papers. However, the staff would welcome any comments the Board may have on the overall approach.

Structure of this paper

3. This paper is structured as follows:
 - (a) background (paragraphs 4–6);
 - (b) why more guidance is needed (paragraphs 7–9);
 - (c) developing guidance (paragraphs 10–19):
 - (i) the *Conceptual Framework for Financial Reporting* (*Conceptual Framework*) (paragraph 11);
 - (ii) the *Materiality Practice Statement* (paragraph 12);
 - (iii) guidance issued by other standard-setters (paragraphs 13–18); and

- (iv) input from the Board’s consultative groups (paragraph 19); and
- (d) next steps (paragraphs 20–21).

Background

4. In November 2018, the Board discussed the objective of management commentary. The Board did not formally vote at that meeting but agreed in broad terms that the objective of management commentary should be to give context for the financial statements by providing primary users with the historical financial and operational information and analysis that is useful in assessing the prospects for the entity’s future net cash inflows, and in assessing management’s stewardship of the entity’s economic resources.
5. The proposed objective focuses on provision of *useful* information to primary users of financial reports. Chapter 2 of the *Conceptual Framework* identifies qualitative characteristics that financial information must possess for that information to be useful to primary users of financial reports. Management commentary is a form of financial reporting.¹ Hence, information in management commentary must possess the qualitative characteristics identified in the *Conceptual Framework* in order for management commentary to meet its proposed objective.
6. The existing Practice Statement already includes a requirement for management commentary to include information that possesses the qualitative characteristics described in the *Conceptual Framework*.² However, the Practice Statement just lists the qualitative characteristics and says that they are used in the Practice Statement with the meanings specified in the *Conceptual Framework*. It does not provide any guidance on how to consider the qualitative characteristics in preparing management commentary.

Why more guidance is needed

7. Staff’s research and discussions with the Management Commentary Consultative Group, the Capital Markets Advisory Committee, the Global Preparers Forum and the

¹ See paragraph IN4 of the Practice Statement.

² See paragraphs 13(b) and 20 of the Practice Statement.

Accounting Standards Advisory Forum (the Board’s consultative groups) indicating that currently information in management commentary does not always possess the qualitative characteristics of useful financial information. In particular, identified gaps in reporting practice include:

- (a) lack of focus on matters specific to the entity that could affect the entity’s long-term success;
- (b) incomplete or fragmented discussion that fails to ‘tell the whole story’;
- (c) lack of neutrality in selecting and presenting information in management commentary, with a tendency towards positive bias;
- (d) lack of comparability, either between entities, or for the same entity over time (for example, due to providing different performance measures in different periods); and
- (e) lack of conciseness due to duplication of content or including immaterial or ‘boilerplate’ information.

8. In the staff’s view, those gaps may in part result from lack of guidance in the existing Practice Statement on what makes information in management commentary useful to primary users. Just listing the qualitative characteristics and cross-referencing to the *Conceptual Framework* may not be sufficient because:

- (a) as noted by some members of the Management Commentary Consultative Group, management commentaries are often prepared by a wider group of individuals than those involved in preparing financial statements. Some of those people may not be familiar with the principles and language in the *Conceptual Framework* and IFRS Standards and may not find cross-references to the *Conceptual Framework* helpful.
- (b) the nature of information in management commentary differs from the nature of information in financial statements and other financial reports. The *Conceptual Framework* discusses the qualitative characteristics of useful financial information. However, that financial information includes various types of information, for example, quantitative (both monetary and non-monetary) and qualitative (narrative), and historical and forward-looking. The *Conceptual Framework* states that the considerations in applying the

qualitative characteristics may be different for different types of information.³ Management commentary is likely to contain more narrative explanatory information or forward-looking information than financial statements do, so preparers may need additional guidance on considering the qualitative characteristics in preparing management commentary.

9. The staff think that it is important to provide more guidance on the qualitative characteristics in the revised Practice Statement to improve preparers' understanding of what makes information in management commentary useful and help address gaps in practice identified in paragraph 7.

Developing guidance

10. In developing guidance on considering the qualitative characteristics of useful financial information in preparing management commentary, the staff consider:
 - (a) the discussion of the qualitative characteristics of useful financial information in the *Conceptual Framework* (paragraph 11);
 - (b) the guidance on making materiality judgements in IFRS Practice Statement 2 *Making Materiality Judgements* (Materiality Practice Statement) (paragraph 12);
 - (c) guidance issued by other standard-setters on management commentary or on similar reports (paragraphs 13–18); and
 - (d) input received from the Board's consultative groups (paragraph 19).

The Conceptual Framework

11. The staff used the discussion of the qualitative characteristics of useful financial information in the *Conceptual Framework* as the starting point for developing guidance for the revised Practice Statement on the qualitative characteristics. In addition, in developing recommendations for each qualitative characteristic, the staff consider whether any additional guidance on that characteristic would be needed because of the nature of information likely to be include in management commentary (see paragraph 8(b)).

³ See paragraph 2.3 of the *Conceptual Framework*.

The Materiality Practice Statement

12. The Materiality Practice Statement was issued by the Board in 2017, that is, after the issue of the Management Commentary Practice Statement. The staff considered the guidance in the Materiality Practice Statement in developing guidance on relevance and making materiality judgements in preparing management commentary (see Agenda Paper 15B *Making relevance and materiality judgements*).

Guidance issued by other standard-setters

13. In developing guidance on the qualitative characteristics, the staff have reviewed guidance issued by other standard-setters on management commentary or on similar reports. The staff's review covered responses from 24 national standard-setters to the staff's request for information about the requirements and commonly applied non-mandatory guidance on management commentary in their jurisdiction.⁴ The staff also reviewed the EU Non-financial Reporting Directive (2014/95/EU) and the related European Commission Guidelines on non-financial reporting, and the International Integrated Reporting <IR> Framework.
14. Most of those standard-setters set out overarching considerations in preparing management commentary often labelled as 'principles' or 'communication principles'. In essence, those principles are designed to make information in management commentary or similar reports useful to users of those reports. The principles listed most commonly included:
- (a) materiality;
 - (b) management's view or management's perspective or presenting information 'through the eyes of management';
 - (c) balanced or unbiased view;
 - (d) completeness or comprehensiveness;
 - (e) strategic or forward-looking orientation;
 - (f) understandability, clarity or conciseness;
 - (g) connectivity or linkage of information;

⁴ See Appendix A of November 2018 Agenda Paper 15B *Summary of research on the objective of management commentary* for details of the respondents and the survey questions.

- (h) comparability;
 - (i) reliability, accuracy or verifiability; and
 - (j) entity-specific information.
15. Some of these principles—materiality, completeness, accuracy, balance, clarity, comparability and reliability—have been identified in July 2019 paper *Understanding the value of transparency and accountability* issued by the participants in the Corporate Reporting Dialogue⁵ (an initiative bringing together the major international reporting frameworks, including those covering wider corporate reporting) as principles fundamental to corporate reporting.⁶
16. The level of guidance provided by other standard-setters on those principles varies. The staff intend to include in Board papers analysis of the guidance in other frameworks where it has helped in developing staff recommendations for particular qualitative characteristics.
17. Most of the principles mentioned in paragraphs 14–15, except for ‘management’s view’ and ‘strategic or forward-looking orientation’, can be viewed as consistent to a greater or lesser extent with the qualitative characteristics of useful financial information identified in the *Conceptual Framework*.
18. The staff do not plan to discuss management’s view and strategic or forward-looking orientation as part of the discussion on the qualitative characteristics of useful financial information. The November 2018 Agenda Paper 15A *The objective of management commentary* already discussed the notion of management’s view and suggested that management’s view should be discussed as part of the guidance on the objective of management commentary.⁷ As requested by the Board, the staff plan to bring a paper clarifying particular aspects of the objective of management commentary to a future meeting. As part of that analysis, the staff will also consider whether the guidance on the objective of management commentary should cover strategic or forward-looking orientation of management commentary.

⁵ The Board is a member in the Corporate Reporting Dialogue alongside CDP, Climate Disclosure Standards Board, Global Reporting Initiative, International Integrated Reporting Council, International Organization for Standardization and Sustainability Accounting Standards Board.

⁶ See <https://corporatereportingdialogue.com/wp-content/uploads/2019/07/Understanding-the-value-of-transparency-and-accountability-paper-1.pdf>

⁷ See paragraph 24(a) of the November 2018 Agenda Paper 15A *The objective of management commentary*.

Input from the Board's consultative groups

19. The staff discussed with the Board's consultative groups the staff's suggestions for including in the revised Practice Statement guidance on particular qualitative characteristics. The groups discussed suggestions for materiality, neutrality, completeness and comparability. Input from the groups has been considered in developing recommendations for the Board.

Next steps

20. The staff anticipate that the revised Practice Statement should:
- (a) include a brief description of each qualitative characteristic based on its description in the *Conceptual Framework*, instead of just listing them and referring to the *Conceptual Framework*. Because some preparers of management commentary may not be familiar with the concepts and principles in the *Conceptual Framework*, including such brief descriptions would help those preparers understand how these qualitative characteristics make information in management commentary useful to primary users, without needing to look at additional guidance in other documents.
 - (b) provide specific guidance on considering particular qualitative characteristics where such guidance is needed due to the nature of information included in management commentary.
21. At this meeting, the staff present their recommendations for guidance on considering the qualitative characteristic of relevance, and specifically on making materiality judgements, in preparing management commentary (see Agenda Paper 15B). At a future meeting, the staff will present their recommendations for guidance on the fundamental qualitative characteristic of faithful representation and the enhancing qualitative characteristics.

Question

Do you have any comments or suggestions on the discussion and analysis in this paper?
