

STAFF PAPER

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Project	Management Commentary
Paper topic	Sweep issues—Status of the Practice Statement

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Introduction

1. At its October 2020 meeting, the International Accounting Standards Board (Board) gave the staff permission to begin the balloting process for an Exposure Draft of a revised IFRS Practice Statement 1 *Management Commentary* (Practice Statement). In December 2020, the staff circulated a pre-ballot draft of the Exposure Draft to Board members and external reviewers.
2. Some reviewers raised questions or comments about the status of the Practice Statement. In this paper, the staff analyse those comments and questions, and suggest an approach to clarifying the status of the Practice Statement. The paper does not ask the Board to make any decisions but invites Board members to comment on the staff analysis and suggestions.

Background

3. In September 2020, the Board discussed the status of the Practice Statement, and statements of compliance with the Practice Statement. The Board tentatively decided:
 - (a) to retain the existing status of the Practice Statement.

- (b) to require an entity to include in its management commentary an unqualified statement of compliance with the Practice Statement if the management commentary complies with all the requirements in the Practice Statement.
 - (c) to permit an entity to include in its management commentary a statement of partial compliance with the Practice Statement. In this case, the management commentary would need to explain which requirements of the Practice Statement the management commentary does not comply with.
4. In making those decisions, the Board noted that entities would be able to make an unqualified statement of compliance only if their management commentary meets all the requirements in the Practice Statement, including requirements relating to:
- (a) the objective of management commentary;
 - (b) the attributes of information in management commentary;
 - (c) metrics in management commentary; and
 - (d) the disclosure objectives for all areas of content.
5. The introduction to the existing Practice Statement describes it as a ‘non-binding framework’. The pre-ballot draft of the Exposure Draft did not use this term. It proposed to explain the status of the Practice Statement as follows:

This [draft] Practice Statement applies to management commentary relating to general purpose financial statements. It sets out requirements for that management commentary and explains how those requirements can be met.

This [draft] Practice Statement does not specify which entities are required to prepare management commentary, how frequently an entity should do so, or the level of assurance to which management commentary should be subjected. Local laws or regulations might require some entities to publish management commentary that complies with this [draft] Practice Statement, and other entities might choose to do so.

This [draft] Practice Statement is not an IFRS Standard. Financial statements can comply with IFRS Standards even if they are not

accompanied by management commentary, or if they are accompanied by management commentary that does not comply with this [draft] Practice Statement.

6. The pre-ballot draft of the Exposure Draft included the following requirements for the statement of compliance:

An entity whose management commentary complies with all the requirements of this [draft] Practice Statement shall include in the management commentary an explicit and unqualified statement of compliance.

An entity whose management commentary complies with some, but not all, the requirements of this [draft] Practice Statement may include in the management commentary a qualified statement of compliance. That qualified statement shall identify the departures and give the reasons for them.

7. The draft Basis for Conclusions described the Board's rationale for those proposals, building on the Basis for Conclusions on the existing Practice Statement.

Questions arising in developing the Exposure Draft

8. In reviewing the drafts of the Exposure Draft, some reviewers raised questions and comments related to the status of the Practice Statement. Reviewers suggested:
- (a) it is unclear how a non-binding Practice Statement can include requirements;
 - (b) references to requirements should be replaced by references to principles, guidance or similar;
 - (c) the descriptions of the status and applicability of the Practice Statement should be aligned with those used in IFRS Practice Statement 2 *Making Materiality Judgements* (Materiality Practice Statement); and

- (d) even after the effective date of the revised Practice Statement, its application would be permitted rather than required, and that needs to be made clear in the transition provisions.

Staff analysis and conclusions

9. This section considers:
 - (a) what is meant by describing the Practice Statement as non-binding or non-mandatory (paragraphs 10–12);
 - (b) whether the status of the Practice Statement is the same as the status of the Materiality Practice Statement (paragraphs 13–15); and
 - (c) whether and how the status of the Practice Statement could be made clearer (paragraphs 16–17).

10. The staff think the use of the words ‘non-binding framework’ in discussing the status of the existing Practice Statement has created confusion. Specifically:
 - (a) the Practice Statement is indeed non-mandatory in the sense that an entity is not required to prepare a management commentary applying the Practice Statement in order for the entity’s financial statements to comply with IFRS Standards; but
 - (b) the Practice Statement is mandatory in the sense that if an entity is required by its local laws or regulations (or chooses) to apply it and wishes to state compliance with the Practice Statement, the entity must comply with its requirements.

11. The staff consider that the status of the Practice Statement is similar to, for example, the status of IAS 34 *Interim Financial Reporting*. That Standard does not mandate which entities should be required to publish interim financial reports, or how frequently, or how soon after the end of an interim period. Entities need not apply IAS 34 in order for their annual financial statements to comply with IFRS Standards. However, if an entity is required (or chooses) to publish an interim

financial report in accordance with IAS 34, it must apply all the requirements of that Standard.

12. Similarly, December 2020 Agenda Paper 20 *Disclosure Initiative: Accounting Policies Sweep Issues* (December 2020 Agenda Paper) argued that:

The purpose of IFRS Practice Statement 1 *Management Commentary* is similar to the purpose of an IFRS Standard—an entity may be required or choose to prepare management commentary that complies with IFRS Practice Statement 1, just as it may be required or choose to prepare financial statements that comply with IFRS Standards. ...

13. The staff further notes that the status of the Practice Statement is different from the status of the Materiality Practice Statement. Specifically, as December 2020 Agenda Paper also argued:

In contrast, similar to agenda decisions and educational material, the purpose of IFRS Practice Statement 2 *Making Materiality Judgements* is to improve the consistent application of the Standards. In particular, IFRS Practice Statement 2 seeks to improve the consistent application of the definition of material in paragraph 7 of IAS 1 and does not add or change the requirements in the Standards. ...

14. In other words, the Materiality Practice Statement provides guidance on applying IFRS Standards. In contrast, the Practice Statement provides requirements for entities that are required (or choose) to prepare management commentary that complies with the Practice Statement.

15. In addition, unlike the Materiality Practice Statement, the Practice Statement on management commentary is not linked to IFRS Standards and does not apply to preparing IFRS financial statements. Furthermore, in November 2020, the Board tentatively confirmed that an entity would be able to apply the Practice Statement in preparing a management commentary on non-IFRS financial statements.

16. For the reasons discussed above, the staff think it is both appropriate and necessary for the Practice Statement to refer to requirements. Likewise, it is also both

appropriate and necessary for the Practice Statement to use language that is different from the language used in the Materiality Practice Statement.

17. The staff think that:
- (a) the status of the Practice Statement and the requirements for the statement of compliance are appropriately described in the pre-ballot draft of the Exposure Draft (see paragraphs 5–6). The staff will consider in drafting whether these descriptions need further clarification.
 - (b) the Basis for Conclusions should explain why the Exposure Draft does not use the terms ‘non-binding’, ‘non-mandatory’ or similar, reflecting the analysis set out in this paper. Specifically, it should explain:
 - (i) that the use of the term ‘non-binding’ in the existing Practice Statement has caused confusion;
 - (ii) how the status of the Practice Statement compares to the status of IFRS Standards; and
 - (iii) how the status of the Practice Statement compares to the status of the Materiality Practice Statement.

Question for the Board

Question 1—Status of the Practice Statement

Do you have any comments or questions on the staff’s analysis and suggested approach to clarifying the status of the Practice Statement?

