

STAFF PAPER

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IASB® meeting

Project	Management Commentary		
Paper topic	Feedback summary—Identification, authorisation and statement of compliance		
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Purpose of paper

- 1 The papers for this meeting summarise feedback on the International Accounting Standards Board (IASB)'s proposals for a revised Practice Statement on management commentary (Practice Statement), as set out in the Exposure Draft *Management Commentary* (Exposure Draft).
- 2 This paper summarises feedback on:
 - (a) identifying management commentary and the related financial statements;
 - (b) definition of management and authorisation of management commentary; and
 - (c) statements of compliance.
- 3 This paper should be read in the context of Agenda Paper 15 *Feedback summary—Overview*, which discusses the sources of feedback reported in this paper, and explains some of the terminology used and how we have quantified feedback.

- 4 This paper does not ask the IASB to make decisions but invites IASB members' questions and comments on the feedback.

Structure of paper

- 5 This paper includes:
- (a) a recap of the Exposure Draft proposals (paragraphs 6–12);
 - (b) an overview of the key messages in the feedback (paragraphs 13–17);
 - (c) summaries of the feedback on:
 - (i) identifying management commentary and the related financial statements (paragraphs 19–26);
 - (ii) definition of management and authorisation of management commentary (paragraphs 27–28); and
 - (iii) statements of compliance (paragraphs 29–44).

Exposure Draft proposals

Identifying management commentary and the related financial statements

- 6 The Exposure Draft proposed that an entity should clearly identify management commentary and distinguish it from other information provided in the same report or in other reports published by the entity.
- 7 The Exposure Draft further proposed that management commentary should identify the financial statements to which it relates.
- 8 The Exposure Draft did not propose any restrictions on the basis of preparation of the related financial statements (for example, it did not propose a requirement that financial statements should be prepared in accordance with IFRS Standards or applying concepts similar to those underpinning IFRS Standards).

- 9 However, the Exposure Draft proposed that if the related financial statements are not prepared in accordance with IFRS Standards, management commentary should disclose the basis on which the financial statements are prepared.

Definition of management and authorisation of management commentary

- 10 The Exposure Draft did not define the term ‘management’. Paragraph BC61 of the Basis for Conclusions on the Exposure Draft referenced the description of ‘management’ in the introduction to the 2010 Practice Statement as ‘the persons responsible for the decision-making and oversight of the entity. They may include executive employees, key management personnel and members of a governing body.’ Paragraph BC61 further explained that the IASB did not propose to provide a specific description of management, because jurisdictional requirements determine who prepares and approves management commentary.
- 11 The Exposure Draft did not propose which body or individual should be responsible for authorising management commentary, but proposed that an entity should state the date on which management commentary was authorised for issue and identify the body(s) or individual(s) who gave that authorisation.

Statements of compliances

- 12 The Exposure Draft proposed that an entity should be:
- (a) *required* to make an explicit and unqualified statement of compliance if its management commentary complies with all of the requirements of the Practice Statement.
 - (b) *permitted* to make a qualified statement of compliance if its management commentary complies with some, but not all, of the requirements of the Practice Statement. Such a qualified statement of compliance should identify the departures from the requirements of the Practice Statement and give the reasons for those departures.

Key messages in feedback

- 13 Most of the respondents commenting supported the proposal that entities should be permitted to state compliance with the Practice Statement even if their financial statements are not prepared in accordance with IFRS Standards. Some of those respondents argued that such an approach may encourage wider application of the Practice Statement.
- 14 Some respondents suggested that without a definition of ‘management’, it is unclear whether the term is meant to include both executive management personnel and members of a governing body. Most of these respondents suggested separately defining the terms ‘management’ and ‘those charged with governance’ and clarifying the role of those charged with governance in authorising management commentary.
- 15 Most of the respondents commenting supported the proposals on unqualified and qualified statements of compliance.
- 16 However, some respondents argued that due to the non-mandatory status of the Practice Statement, it should be for local regulators to require or permit a statement of compliance.
- 17 A few respondents were concerned that permitting a qualified statement of compliance could result in management commentary being unbalanced and potentially misleading to investors.

Identifying management commentary and the related financial statements

Identifying management commentary

- 18 The Exposure Draft did not specifically ask respondents to comment on the proposal to clearly identify management commentary and distinguish it from other information provided by the entity. However, a few respondents commented that more guidance is needed on where to publish management commentary.

We think that to eliminate the current disparity of reports among entities, guidance should be provided on where to publish the management commentary. The current free-standing format approach makes it difficult for investors to identify the management commentary section. *CL63 European Federation of Financial Analysts Societies*

Financial statements to which management commentary relates

Financial statements not prepared in accordance with IFRS Standards

19 Many respondents commented on the proposal to permit entities to state compliance with the Practice Statement even if their financial statements are not prepared in accordance with IFRS Standards. Almost all of these respondents supported the proposal, stating that such an approach would:

- (a) encourage wider application of the Practice Statement, which would benefit investors:

Permitting a broader group of entities to apply the revised Practice Statement would improve the information communicated to users of management commentary. While a consistent underlying accounting framework would enhance the comparability of management commentary information, we believe the benefits of broadening the application of the practice statement outweighs the benefits of restricting the application. *CL57 BDO*

- (b) enhance the comparability of management commentaries across different entities and jurisdictions.

- (c) be both practical and helpful for preparers:

In our view, the Practice Statement will provide high quality guidance for management commentary reporting that does not rely on the use of IFRS concepts of recognition, measurement, presentation or disclosure. As such it can be decoupled from the basis of preparation used for the financial statements. *CL10 UK Financial Reporting Council*

- (d) be appropriate in the context of broader corporate reporting developments and consistent with the approach taken in other reporting frameworks:

We also see this position [as] relevant in the context of the IFRS Foundation's move to sustainability reporting standards under the International Sustainability Standards Board (ISSB). It would be important that policy makers, regulators or other bodies charged with endorsing standards, or entities who may adopt those standards on a voluntary basis, do not perceive that those standards could only be used with IFRS Foundation financial reporting standards.

In addition, such an approach would be consistent with that adopted in integrated reporting, which can be applied with all accounting frameworks. *CL68 Deloitte*

- 20 A few respondents did not support the proposal, mainly because they were concerned about the risk of creating the impression that the related financial statements have been prepared in accordance with IFRS Standards even if they have been prepared on a different basis.

We understand that this type of permission may not be properly understood by the market. The revised statement of practice may convey the idea that the financial statement has been prepared in accordance with IFRS standards, even if this is not the case. *CL60 Brazilian Development Bank (BNDES)*

No restrictions on the basis of preparation of financial statements

- 21 Most of the respondents who supported the proposal to permit entities to state compliance with the Practice Statement even if their financial statements are not prepared in accordance with IFRS Standards also agreed that no restrictions should be placed on the basis of preparation of their financial statements. A few of these respondents argued that placing restrictions on the basis of preparation could introduce unnecessary barriers to wider application of the Practice Statement (see paragraph 20(a)).

- 22 A few respondents suggested specifying that the Practice Statement is meant to apply to management commentary related to general purpose financial statements and not to special purpose financial statements. An accounting firm argued that entities should not be permitted to state compliance with the Practice Statement if the related financial statements are prepared for a limited or specific purpose.
- 23 A few respondents commented that entities which prepare financial statements applying concepts that are very different from the ones underlying IFRS Standards are unlikely to apply the Practice Statement.

Information about the basis of preparation of financial statements

- 24 A few respondents argued that management commentary should always clearly state the basis on which the related financial statements have been prepared, regardless of whether they have been prepared in accordance with IFRS Standards or another accounting framework.
- 25 A few standard-setters suggested that the IASB should specify the types of information entities should provide about the basis of preparation of the related financial statements if they are not prepared in accordance with IFRS Standards.

Other comments

- 26 An academic association suggested that the Practice Statement should specify whether:
- (a) the reporting entity of management commentary should be the same as for the related financial statements;
 - (b) a ‘combined’ management commentary can be prepared to accompany both the financial statements of the parent company as a standalone entity and the consolidated financial statements of the group; and
 - (c) the Practice Statement is applicable to management commentary relating to interim financial statements.

Definition of management and authorisation of management commentary

Definition of management

- 27 Some respondents suggested that without a definition of ‘management’ in the Practice Statement, it is unclear whether the term is meant to include both executive management personnel and those charged with governance, such as a board of directors. Most of these respondents suggested that the terms ‘management’ and ‘those charged with governance’ should be separately defined. A few others suggested defining the term ‘management’ in a manner that is broadly consistent with IAS 24 *Related Party Disclosures*.

Our concern is the title ‘Management Commentary’ suggests the contents of the report prepared has not been authorised and approved for issuance by directors (ie those charged with governance). They could mistakenly assume from a literal reading the [Exposure Draft]’s title this is a report that has been prepared solely by senior management of the reporting entity without any input from those charged with its governance (eg directors). In the definitions set out in IAS 24 ‘Related Party Disclosures’ there is a definition of ‘key management personnel’ (KMP) that explicitly states that both senior management and those charged with governance are KMP. We would like this [Exposure Draft] to reinforce that management commentary is a document that has been prepared and then reviewed thoroughly by the reporting entity’s KMP. *CL59 Grant Thornton*

Authorisation of management commentary

- 28 Respondents advocating a distinction between ‘executive management personnel’ and ‘those charged with governance’ expressed various views on the role that those charged with governance should play in the preparation and authorisation of management commentary, including:
- (a) those charged with governance should assume responsibility for setting the direction for the preparation of management commentary:

In so far as reporting is concerned, the *King Report on Corporate Governance* in South Africa 2016 (King IV), for example, firmly entrenches this responsibility on the board. It includes the practice recommendation that: “*The governing body should assume responsibility for the organisation’s reporting by setting the direction for how it should be approached and conducted.*” *CL17 Integrated Reporting Committee of South Africa*

- (b) management commentary should be prepared from the perspective of executive management personnel and those charged with governance should explain what procedures they have followed to ensure the credibility of the reported information:

... we propose that the IASB consider adding the requirement for Those Charged with Governance to explain what procedures they have followed from the perspective of ensuring the credibility of corporate reporting, while maintaining the positioning of Management Commentary as a document to present management’s views. *CL35 Japanese Institute of Certified Public Accountants*

- (c) those charged with governance should not have a responsibility over management commentary, but should articulate their perspective in a separate report:

Requiring an overarching report adding the board’s perspective (potentially as a component of today’s ‘*corporate governance statements*’) to ‘*management’s perspective*’ in management commentary. *CL5 Value Reporting Foundation*

Statements of compliance

Unqualified statement of compliance

Support for requiring an unqualified statement compliance

- 29 Most respondents commented on the proposal to require an unqualified statement of compliance if an entity complies with all of the requirements of the Practice Statement. Most of these respondents, including most of the standard-setters, most of the accountancy bodies and all investors commenting, supported the proposal. Respondents supporting the proposal argued that an unqualified statement of compliance would:
- (a) provide investors with useful information about the basis of preparation of management commentary;
 - (b) increase focus of management on the quality of information provided in management commentary; and
 - (c) provide the basis for assurance of management commentary.
- 30 A few respondents who broadly supported the proposal for an unqualified statement of compliance suggested refinements. An individual suggested that the IASB should specify that immaterial departures from the Practice Statement would not prevent the entity from stating full compliance and would not need to be identified and explained in management commentary.

Concerns about requiring an unqualified statement of compliance

- 31 Some respondents did not support the proposal, arguing that it is not appropriate to require a statement of compliance with a non-mandatory Practice Statement.

Our concern is that the introduction of statements of compliance dilutes the conceptual difference between authoritative guidance (standards) and non-authoritative guidance (practice statements). *CL9 EY*

The Practice Statement is a non-mandatory disclosure guideline, so it is debatable whether a compliance statement should be issued. *CL13 Accounting Regulatory Department of the Ministry of Finance and China Accounting Standards Committee*

- 32 Some respondents expressed the view that it should be for local regulators to determine whether to require a statement of compliance. A few respondents suggested that the Practice Statement should encourage, rather than require, a statement of compliance.
- 33 A few respondents provided further reasons for not supporting the proposed requirement for an unqualified statement of compliance, including:
- (a) the condition for issuing an unqualified statement of compliance (needing to comply with all the requirements of the Practice Statement) is too strict;
 - (b) requiring an unqualified statement of compliance may discourage entities from applying the Practice Statement; and
 - (c) requiring a statement of compliance is premature at this time as the role of the Practice Statement could evolve as a result of the future work of the International Sustainability Standards Board (ISSB).

Qualified statement of compliance

Support for permitting a qualified statement of compliance

- 34 Most respondents commented on the proposal to permit an entity to make a qualified statement of compliance with the Practice Statement if it complies with some, but not all, of the requirements of the Practice Statement. Most of these respondents, including most of the accountancy bodies, many of the standard-setters and all investors, preparers and regulators commenting, supported the proposal.
- 35 In support of this view, some respondents argued that permitting entities to make a qualified statement of compliance could encourage wider adoption of the Practice Statement and assist entities in moving towards full compliance over time.

... we support the flexibility provided in the proposals to allow a partial/modular application of the Practice Statement and we believe that as best practice develops over time, it may encourage entities to fully comply with the requirements of the Practice Statement. *CL21 KPMG*

- 36 A few respondents suggested that a qualified statement of compliance should be required rather than just permitted.

Concerns about permitting a qualified statement of compliance

- 37 Some of the respondents who argued that it is not appropriate to require an unqualified statement of compliance because of the non-mandatory status of the Practice Statement (see paragraph 32) also argued that it is not appropriate to permit a qualified statement of compliance. In addition, some of the respondents who stated that it should be for local regulators to decide whether to require an unqualified statement of compliance (see paragraph 33) also stated that local regulators should decide whether to permit a qualified statement of compliance. Some respondents expressed other concerns about permitting a qualified statement of compliance, including that such an approach could:

- (a) result in misleading information provided in management commentary if entities are biased in selecting which requirements of the Practice Statement to apply.
- (b) create confusion about the extent of compliance with the Practice Statement:

We note that there are no parameters regarding a partial statement of compliance. Therefore, this statement could technically cover only a very small portion of the management commentary or could exclude critical aspects of the Practice Statement. In these cases, the level of compliance could be misconstrued by users. From our outreach with users on various projects, we know that some users currently misunderstand the level of assurance over information outside the financial statements. We think it will be important to ensure users of management commentary have a thorough understanding of what is meant by partial and full compliance, so that the proposal doesn't add

to the confusion in this area. *CL22 Accounting Standards Board (AcSB) [Canada]*

- (c) pose assurance challenges:

A partial statement of compliance may create confusion, pose audit challenges, increase costs in understanding which elements of the report adhere to which parts of the Practice Statement, and for what reasons other parts are not complied with. *CL79 European Financial Reporting Advisory Group*

- (d) bring into question the appropriateness of the requirements in the Practice Statement and discourage its application:

A qualified statement conveys that the framework is either not suitable for its purpose or that the management commentary is not compliant with the Practice Statement. There is no benefit in voluntarily adopting a Practice Statement which is not fit for purpose. If it is not a regulatory requirement to comply with the Practice Statement, it is probable that such a statement of compliance would be omitted altogether. *CL37 CPA Australia and Chartered Accountants Australia and New Zealand*

Identification of departures from the Practice Statement

- 38 A few respondents expressed the view that information about departures from the requirements of the Practice Statement and the reasons for these departures would be useful to investors.
- 39 However, a few other respondents argued that the requirement to provide information about reasons for departures may discourage application of the Practice Statement as entities may be reluctant to include such statements.
- 40 A standard-setter suggested that the IASB should specify how entities should clearly indicate the level of adherence to the Practice Statement.

- 41 Another standard-setter suggested an alternative approach to communicating to investors which parts of the Practice Statement the entity has complied with.

Instead of a statement identifying the departures from the requirements of the revised Practice Statement, we consider it would be useful for entities to describe the aspects of the revised Practice Statement it has complied with. We consider this would provide readers with more clarity than allowing an entity to claim qualified compliance with the revised Practice Statement and is also consistent with the proportionate application of the revised Practice Statement. *CL47 Malaysian Accounting Standards Board*

Other comments

Identifying the requirements that need to be complied with

- 42 A few respondents stated that it may be difficult for entities to judge whether they have fully complied with the requirements of the Practice Statement.

We believe that the proposals in the [Exposure Draft] are too high level to be operationalised, making a statement of compliance challenging for preparers. Preparers need to understand which requirements they need to meet to be able to assert compliance. To this end, we suggest amending the language in the [Exposure Draft] so that there is a clear set of requirements underpinned by distinct principles and objectives. This would also be helpful from an assurance perspective. *CL 14 Accountancy Europe*

- 43 Furthermore, a few respondents suggested ways to make it easier for entities to identify the requirements they must comply with in order to state compliance with the Practice Statement, including:

- (a) clearly distinguishing between requirements and guidance; and
- (b) moving the list of requirements that preparers must comply with from paragraph BC32 of the Basis of Conclusions to the section of the Practice Statement that sets out the requirements for an unqualified statement of compliance.

Terminology

- 44 A few respondents argued that the terms ‘qualified’ and ‘unqualified’ are generally associated with auditing standards and should not be used in the context of a statement of compliance with the Practice Statement.

... we suggest reconsidering using the labels ‘qualified’ and ‘unqualified’ for the statement of compliance to avoid confusion with the level of assurance provided. A ‘comply or explain’ terminology could be used to evidence whether the report fully complies with the Practice Statement, evidence any areas of non-compliance (if any) and explain the reason for diverging from the Practice Statement. *CL14 Accountancy Europe*

Question for IASB members

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Do you have any questions or comments on the feedback reported in this paper?