Think Ahead ACCA

Practice Statement on Management Commentary

Exposure draft issued by IASB in May 2021

Comments from ACCA
November 2021

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GENERAL COMMENTS

ACCA welcomes the opportunity to provide views in response to the exposure draft of the Practice Statement on Management Commentary. This has been done with the assistance of ACCA's Global Forum for Corporate Reporting.

We support the revision of the Practice Statement as it is needed not only to address the current deficiencies in management commentary (as identified in para IN8), but also to reflect current developments in sustainability reporting standard-setting. Connectivity between financial information and sustainability information is vital, and the Practice Statement is central to providing this connectivity.

Given the significant interactions between this Practice Statement and the standards that the ISSB will produce, we would recommend that the IASB pauses further work on the Practice Statement until such time as when the ISSB is firmly established. In our view, it is appropriate to develop the Practice Statement in close collaboration with the ISSB, so that it can reflect and be informed by the development of future ISSB standards.

The objectives-focused approach adopted in the PS revision mirrors the proposals set out in *Disclosure Requirements in IFRS Standards—A Pilot Approach*. While this approach should help to better address investors' information needs, it will require a shift in preparers' mindset as more judgement is required. Delaying the finalisation of the Practice Statement will thus also enable the IASB to learn from the implementation of the *Pilot Approach* before adopting it in the PS.

We note that the Basis for Conclusions (BC140) states that there is little evidence of entities applying the current Practice Statement. ACCA's own engagement with stakeholders in jurisdictions around the world shows little evidence of national regulators intending to either directly mandate reporting in line with the revised Practice Statement or set reporting requirements aligned to it. Nevertheless, this ED seems to adopt an approach which assumes that the Practice Statement would become mandatory – with a focus on enforceability and the requirement for an explicit statement of compliance. This would not seem appropriate if there is little appetite from national regulators to mandate reporting in line with the Practice Statement.

An alternative approach, which is not predicated on mandation, could see the ED providing more aspirational guidance. In our view, this would better align with both existing best practice and the mandate for the ISSB. For example, the Practice Statement could explicitly reference the International <IR> Framework (the <IR> Framework) and build upon the full concept of multi-capital value creation that lies at its core.

In ACCA's *Principles for Connected Corporate Reporting*[1], we emphasised that corporate reporting standards should highlight the interactions between the value that organisations create for themselves, and the impact that they have on society and planet. This is crucial for the Practice Statement in our view. An understanding of the interdependencies between the entity and its external environment, from the entity's board and management, should fundamentally inform the basis on which management commentary is prepared.

While we support the objectives-focused approach, the length and complex structure of the ED will make it very challenging for preparers to apply it. A more concise document, with a simpler structure will ensure operationality. This could include presenting guiding principles or attributes of useful information first, and grouping requirements for each area of content together with examples of material information for easier reference. The <IR> Framework is a helpful example of a clear guidance provided through a relatively concise and simple structure.

We understand that for the purposes of the management commentary, the term 'management' is intended to cover all those responsible for the decision-making and oversight of an entity, including executive management and the board. It would be helpful to explicitly state this, by defining the term 'management' in the practice statement.

In our detailed response below, we highlight the following recommendations for the IASB to consider:

- Consider removing 'financial performance and position' and 'resources and relationships' from the areas of content, and adding 'governance', 'stakeholder relationships' and 'basis of preparation' as areas of content.
- Include forward-looking items and natural capital-related issues more prominently in key matters
- Provide clearer guidance on how to make materiality judgements
- Align the language and terminology around attributes of useful information with the Conceptual Framework

We provide our answers to the specific questions raised below.

RESPONSES TO THE SPECIFIC QUESTIONS ASKED

Part A: General requirements

Question 1 – The financial statement to which management commentary relates

[1] https://www.accaglobal.com/gb/en/technical-activities/technical-resources-search/2021/november/acca-principles-connected-corporate-reporting-policy.html

Paragraph 2.2 proposes that management commentary identify the financial statements to which it relates. That paragraph further proposes that, if the related financial statements are not prepared in accordance with IFRS Standards, the management commentary would disclose the basis on which the financial statements are prepared.

The Exposure Draft does not propose any restrictions on the basis of preparation of the related financial statements (for example, it does not propose a requirement that financial statements be prepared applying concepts similar to those underpinning IFRS Standards).

Paragraphs BC34–BC38 explain the Board's reasoning for these proposals.

(a) Do you agree that entities should be permitted to state compliance with the revised Practice Statement even if their financial statements are not prepared in accordance with IFRS Standards? Why or why not?

(b) Do you agree that no restrictions should be set on the basis of preparation of such financial statements? Why or why not? If you disagree, what restrictions do you suggest, and why?

(a) Yes, we agree with the rationale provided.
(b) Yes, we agree.

Question 2 – Statement of compliance

(a) Paragraph 2.5 proposes that management commentary that complies with all of the requirements of the Practice Statement include an explicit and unqualified statement of compliance.

a. Paragraphs BC30–BC32 explain the Board's reasoning for this proposal.

b. Do you agree? Why or why not?

(b) Paragraph 2.6 proposes that management commentary that complies with some, but not all, of the requirements of the Practice Statement may include a statement of compliance. However, that statement would be qualified, identifying the departures from the requirements of the Practice Statement and giving the reasons for those departures.

Paragraph BC33 explains the Board's reasoning for this proposal.

Do you agree? Why or why not?

We do not support the proposal to require an unqualified statement of compliance based upon the ED as it stands.

Given the non-authoritative nature of the Practice Statement, and the uncertainty around the adoption of the Practice Statement by national regulators, drawing too strict a distinction between management commentary and non-management commentary content (para 2.1) could be problematic. For example, it would not be helpful to have a qualified statement of compliance, where an entity's integrated report includes information that its Board considers is relevant for the entity's value creation, but is not strictly covered by this practice statement.

What an unqualified statement of compliance entails would also require clarification: the fact that the practice statement is structured around disclosure objectives and examples of information needed to meet these disclosure objectives means that assessing 'compliance' will involve a high level of judgement.

Question 3 – Objective of management commentary

Paragraph 3.1 proposes that an entity's management commentary provide information that:

(a) enhances investors and creditors' understanding of the entity's financial performance and financial position reported in its financial statements; and

(b) provides insight into factors that could affect the entity's ability to create value and generate cash flows across all time horizons, including in the long term.

Paragraph 3.2 proposes that the information required by paragraph 3.1 be provided if it is material. Paragraph 3.2 states that, in the context of management commentary, information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that investors and creditors make on the basis of that management commentary and of the related financial statements.

Paragraphs 3.5–3.19 explain aspects of the objective, including the meaning of 'ability to create value'.

Paragraphs BC42–BC61 explain the Board's reasoning for these proposals.

Do you agree with the proposed objective of management commentary? Why or why not? If you disagree, what do you suggest instead, and why?

<u>Objective</u>

While we generally support the view that the primary users of management commentary should be the same as those for the financial statements, (i.e., existing and potential investors, lenders and other creditors), we are concerned that drawing too clear a distinction between the information needs of investors and those of other stakeholders is unhelpful. An overly narrow interpretation of materiality could run counter to the second objective of the management commentary: providing insight over the wide range of factors that could affect an entity’s ability to create value over the short, medium and long term.

We would encourage the IASB to revise paragraph 3.8 to align the wording with that of the <IR> Framework, by explicitly acknowledging that management commentary can ‘benefit all stakeholders interested in an organization’s ability to create value over time, including employees, customers, suppliers, business partners, local communities, legislators, regulators and policy-makers.’

Paras 3.11-3.12 introduces an interpretation of ‘enterprise value’ that seems overly narrow, and at odds with the integrated reporting concept of value creation, preservation and erosion. We understand the term ‘enterprise value’ to denote the market value that investors and creditors attribute to an entity, based on the information available to them. It is, therefore, not the role of the management commentary to determine enterprise value.

In our view, the purpose of the management commentary should instead be to give a holistic and balanced account of how an entity creates, preserves and erodes value for itself – a process inextricably linked to the way the entity creates, preserves and erodes value for other stakeholders.

Paragraph 3.13 as it currently stands is simplistic and ignores the entity's interactions with the external environment. The inter-dependencies of value for other parties and value for the entity itself needs to be better articulated, through direct reference to the <IR> Framework. Matters that are important to customers, suppliers, employees and society are also likely to be of interest to investors as they assess the risks and returns associated with the entity.

We note that while the bulk of the practice statement refers to ‘value creation’ paragraph 3.11 refers to ‘enterprise value.’ This inconsistency in terminology is not helpful. We would urge the IASB to adopt the same term consistently throughout, and to define this term in the practice statement, consistently with the definition in the ISSB standards (see below).

<u>Terminology</u>

Our engagement with stakeholders’ jurisdictions around the world suggests that there is currently no common understanding of the term ‘enterprise value’. Given the importance of this concept to the work of the ISSB, a clear and commonly-accepted definition of the term should be developed by the ISSB in consultation with regulators and standard-setters around the world.

We understand that for the purposes of the management commentary, the term ‘management’ is intended to cover all those responsible for the decision-making and oversight of an entity, including executive management and the board. It would be helpful to explicitly state this, by defining the term ‘management’ in the practice statement.

Future-orientated information

We agree that circumstances where the disclosure of information could seriously prejudice the entity are very rare. However, we understand that the reporting of forward-looking information, in particular forecasts and targets, can give rise to concerns around litigation. The IASB may wish to consider introducing similar wording as that included in IAS 37 (as noted in BC113) to provide exceptions in extremely rare cases. Further guidance to illustrate the disclosure of material information where there are such concerns.

Finally, it would be helpful for the IASB to clarify what time horizons are intended to be covered by the reference to 'long term' throughout the exposure draft. While appropriate long-term horizons may differ from one entity to another, illustrative examples in this respect would be helpful.

Part B and Appendix B: Areas of content

Question 4 – Overall approach

The Exposure Draft proposes an objectives-based approach that:

(a) specifies an objective for management commentary (see Chapter 3);

(b) specifies six areas of content for management commentary and, for each area of content, disclosure objectives that information provided in management commentary is required to meet (see Chapters 5–10);

(c) gives examples of information that management commentary might need to provide to meet the disclosure objectives (see Chapter 15); but

(d) does not provide a detailed and prescriptive list of information that management commentary must provide.

Paragraphs BC69–BC71 explain the Board's reasoning for proposing this approach.

Do you expect that the Board's proposed approach would be:

(a) capable of being operationalised - providing a suitable and sufficient basis for management to identify information that investors and creditors need; and

(b) enforceable - providing a suitable and sufficient basis for auditors and regulators to determine whether an entity has complied with the requirements of the Practice Statement?

If not, what approach do you suggest and why?

We broadly support the Board's objectives-based approach. Generally, this should render the practice statement capable of being operationalised. However, we note that this objectives-focused approach marks a new approach to standard-setting, reflecting the proposals set out in *Disclosure Requirements in IFRS Standards—A Pilot Approach*. While this should help to better address investors' information needs, it will require a shift in preparers' mindset as it demands a greater use of judgement.

It would seem unhelpful to have the examples of information that might be material in a separate chapter, and further examples relating to long-term prospects, intangible resources and relationships and environmental and social matters in the Appendix. These should feature in the main body of the practice statement, alongside the disclosure objectives and key matters for each area of content. Disclosure objectives are often interlinked: showing examples alongside the objectives would better illustrate the inter-connectedness of information meeting these objectives.

It is less clear to what extent the approach adopted would make the practice statement enforceable – we note it is also uncertain whether many regulators would seek to require compliance with the practice statement at this stage. 'Verifiability' – an attribute as described paragraphs 13.24–13.26 – would be a more suitable consideration than enforceability.

Question 5 – Design of disclosure objectives

The proposed disclosure objectives for the areas of content comprise three components—a headline objective, assessment objectives and specific objectives. Paragraph 4.3 explains the role of each component. Paragraphs 4.4–4.5 set out a process for identifying the information needed to meet the disclosure objectives for the areas of content and to meet the objective of management commentary.

Paragraphs BC72–BC76 explain the Board's reasoning for these proposals.

(a) Do you agree with the proposed design of the disclosure objectives? Why or why not? If you disagree, what do you suggest instead, and why?

(b) Do you have general comments on the proposed disclosure objectives that are not covered in your answers to Question 6?

(a) We broadly agree with the design of the disclosure objectives.

(b) Please see our response to Question 6 for specific concerns about areas of content and their related disclosure objectives.

Question 6 – Disclosure objectives for areas of content

Chapters 5–10 propose disclosure objectives for six areas of content. Do you agree with the proposed disclosure objectives for information about:

(a) the entity's business model;

(b) management's strategy for sustaining and developing that business model;

(c) the entity's resources and relationships;

(d) risks to which the entity is exposed;

(e) the entity's external environment; and

(f) the entity's financial performance and financial position?

Why or why not? If you disagree, what do you suggest instead, and why?

Although we agree broadly with the disclosure objectives for the six areas of content, we have some concerns regarding the proposed areas of content themselves.

<u>Financial performance and financial position</u>

We are concerned that featuring 'financial performance and financial position' as a content area may be interpreted by preparers to mean that information about financial capital should be prioritised over information about other capitals.

As it currently stands, the assessment objectives for this area of content would seem to duplicate assessment objectives for other areas: for example, 'drivers of the entity's financial performance and financial position' would seem to overlap with objectives in relation to the external environment; and 'the extent to which the financial performance and financial position reported in the entity's financial statements are indicative of the entity's ability to create value' seems to overlap with objectives in relation to the business model.

We agree that connectivity between financial and non-financial information is very important, including linkages between management commentary and the financial statements. However, this should feature more effectively as an underlying attribute – specifically, relating to coherence – rather than as a content area.

The attribute 'coherence' should be more broadly defined, to encompass the <IR> Framework guiding principles of connectivity and strategic focus. Please refer to our response to Question 9 for further discussion on this issue.

<u>Resources and relationships</u>

We also disagree with the inclusion of 'resources and relationships' (capitals) as a content area. In our view, this should instead be presented as a pervasive fundamental concept, running through the disclosure objectives, key matters and material information for all content areas.

We are particularly concerned with the presentation of 'resources and relationships' as involving only inputs and outputs, ignoring outcomes. While some outcomes appear to be included separately as 'social and environmental impact', in the content area 'business model', this is unsatisfactory. Presenting the capitals as inputs, outputs and ‘social and environmental impact’ would seem to misrepresent a key concept of integrated reporting: the inter-dependency between value created, preserved or eroded for the entity itself and value created, preserved or eroded for others. The light reference to this in para 5.7(c) seems inappropriate today, when entities’ wider social, natural and human capital outcomes are increasing influencing investment decisions as well as customer behaviour – thus affecting the entity’s ability to create value and generate cash flows more than ever before.

Further, we note that the examples provided in para 7.2 of resources and relationships see to cover only those which are owned/ controlled by the entity. This is at odds with the capitals concept in the <IR> Framework, which highlights that an entity’s ability to create value also depends upon resources and relationships outside of the entity’s reporting boundary: public infrastructure, or natural resources, for example.

We would recommend that ‘stakeholders relationships’ features as a defined content area, instead of ‘resources and relationships.’ This is because how the entity responds to key stakeholders’ legitimate needs and interests influences its strategy and risk management – and hence its ability to create value over time.

Governance

ACCA would strongly recommend the Board to consider including governance as a distinct area of content. We disagree with paragraphs B12 and BC83 (in the Basis for Conclusions), which suggest that governance is mainly concerned with compliance with local regulations. While local laws do regulate entities and the board’s duties, there is a broader range of governance issues that are universal and based on existing good governance principles and practices. An entity’s approach to governance has a strong influence on its strategy, risk management, business model and approach to social and environmental matters. As such, it should be a key content area for all entities.

Investors and stakeholders need information about how the governance structure and the composition and activities of the board itself influences entities' ability to create value. Key matters in this respect include board diversity, the board’s risk appetite and approach to risk management, the board’s role in influencing and monitoring the entity’s strategic direction, the quality of the board’s engagement and relationship with shareholders, and board remuneration.

Not having governance as a content area puts the practice statement at odds with the TCFD Recommendations which feature governance as a pillar. Alignment in this respect would be essential, material information climate-related financial disclosures should be included in management commentary.

Basis of preparation

In our view, an additional area of content should cover the basis of preparation for the management report. An entity’s process of determining material matters is a critical disclosure as it enables users to evaluate the appropriateness of the entity’s reporting process in areas that involve a significant degree of entity-specific judgement.

A description of the reporting boundary for the management report is also important in informing users about risks, opportunities and outcomes related to resources or relationships outside of the financial reporting boundary. This is particularly relevant, if entities are to incorporate disclosures in line with future ISSB standards within the management commentary.

Section 3D of the International Integrated Reporting Framework can serve as the basis for requirements in this area.

Question 7 – Key matters

Paragraphs 4.7–4.14 explain proposed requirements for management commentary to focus on key matters. Those paragraphs also propose guidance on identifying key matters. Chapters 5–10 propose examples of key matters for each area of content and examples of metrics that management might use to monitor key matters and to measure progress in managing those matters.

Paragraphs BC77–BC79 explain the Board's reasoning for these proposals.

(a) Do you agree that the Practice Statement should require management commentary to focus on key matters? Why or why not? If you disagree, what do you suggest instead, and why?

(b) Do you expect that the proposed guidance on identifying key matters, including the examples of key matters, would provide a suitable and sufficient basis for management to identify the key matters on which management commentary should focus? If not, what alternative or additional guidance do you suggest?

(c) Do you have any other comments on the proposed guidance?

(a) We agree broadly with the Board's proposed focus on key matters.

(b) The examples of key matters are at times too generic and based on too narrow an interpretation of the disclosure objectives to be useful to preparers. We note that references to natural capital is conspicuously missing in the examples of key matters provided. This is unhelpful.

Finally, as suggested in our response to Question 6 above, 'financial performance and position' should not feature as a separate area of content. Instead, we would recommend that the examples of metrics provided include financial metrics, to highlight the connectivity between financial capital and other capitals.

(c) Our specific comments about key matters are as follows:

- **Strategy**: Para 6.8 (c) refers to access to, and the quality of, resources and relationships in general. This contradicts paragraph 6.6 (e) which focuses only on financial resources. Consistency in this respect is paramount. In our view, investors require information about all key resources and relationships that are needed to implement an entity's strategy, not just financial resources.

- **Resources and relationships**: Para 7.9 (b) identifies exclusive supplier relationships and non-substitutable resources. While such business-critical resources and relationships will clearly constitute key matters, it seems important to highlight that key resources and relationships also comprise those which are necessary for an entity's continuous operation – for example, a pipeline of appropriately-trained employees.

  Para 7.10 makes an important point that key resources and relationships should be identified as precisely and specifically as possible. An illustration may help to bring this to life.

  Para 7.11 (a) and (b) identify the quantities of resources as examples of a relevant metric. This is insufficient. The quality and affordability of resources (for example, the quality of water for an entity producing beverages, and the amount of money that the entity would have to pay to obtain water at the level of quality required) are both relevant metrics. Such metrics are likely to be influenced by the ISSB's future standards.

- **External environment**: Para 9.10 notes 'Information about interrelated factors or trends may be clearer and more concise if those factors or trends and their effects are discussed collectively, rather than in isolation.' An example is needed here to make this applicable.

Question 8 – Long-term prospects, intangible resources and ESG matters

Requirements and guidance proposed in this Exposure Draft would apply to reporting on matters that could affect the entity's long-term prospects, on intangible resources and relationships, and on environmental and social matters. Appendix B provides an overview of requirements and guidance that management is likely to need to consider in deciding what information it needs to provide about such matters. Appendix B also provides examples showing how management might consider the requirements and guidance in identifying which matters are key and which information is material in the fact patterns described.

Paragraphs BC82–BC84 explain the Board's reasoning for this approach.

(a) Do you expect that the requirements and guidance proposed in the Exposure Draft would provide a suitable and sufficient basis for management to identify material information that investors and creditors need about:

(i) matters that could affect the entity's long-term prospects;

(ii) intangible resources and relationships; and

(iii) environmental and social matters?

(a) Why or why not? If you expect that the proposed requirements and guidance would not provide a suitable or sufficient basis for management to identify that information, what alternative or additional requirements or guidance do you suggest?

(b) Do you have any other comments on the proposed requirements and guidance that would apply to such matters?

We do not believe that the requirements and guidance set out in Appendix B provides a suitable basis for management to identify material information.

Despite the note that Appendix B constitutes an integral part of the practice statement, the positioning of requirements and guidance in an appendix still implies that it is of lesser importance than the content of the main chapters. There is therefore a risk that preparers would overlook the guidance when preparing management commentary, especially in a practice statement that runs over 100 pages. Such positioning is also unhelpful because it could be wrongly interpreted to signal that information about long-term prospects, intangible resources and relationships and environmental and social matters are somehow separate or marginal to other information covered in the PS.

Appendix B provides some helpful continuous examples that meet multiple disclosure objectives across different areas of content (ex. the pharmaceutical company example in B1.8 and B1.11). These demonstrate the connectivity and coherence between areas of content – an important point worth further emphasis in the Practice Statement. Equally, examples are needed to demonstrate the interdependencies between an entity's environmental and social impact and the availability, affordability and quality of key resources and relationships, and the connections between the considerations for short, medium and long-term timeframes. Besides the <IR> Framework, the UK Financial Reporting Council's Guidance on the Strategic Report[2] provides valuable linkage examples.

We would recommend the Board to include examples in the main body of the practice statement. These examples need not always be matched to specific disclosure objectives. Continuous examples, such as those discussed in the paragraph above, should be shown as one complete narrative, within the area of content to which they most relate.

Question 9 – Interaction with the IFRS Foundation Trustee's project on sustainability reporting

[2] https://www.frc.org.uk/getattachment/fb05dd7b-c76c-424e-9daf-4293c9fa2d6a/Guidance-on-the-Strategic-Report-31-7-18.pdf

Paragraphs BC13–BC14 explain that the Trustees of the IFRS Foundation have published proposals to amend the Foundation's constitution to enable the Foundation to establish a new board for setting sustainability reporting standards. In the future, entities might be able to apply standards issued by that new board to help them identify some information about environmental and social matters that is needed to comply with the Practice Statement.

Are there any matters relating to the Trustees' plans that you think the Board should consider in finalising the Practice Statement?

Although IN18 makes reference to the new board, the practice statement does not sufficiently prepare the ground for the inclusion of sustainability information in the management commentary. References to 'social and environmental impacts' in the practice statement are currently marginal and superficial. The Summary of the Technical Readiness Working Group's Programme of Work, published on 3 November, suggested that there are several possible locations for sustainability-related financial information, including the management commentary. Further clarity on this from the ISSB will be needed.

In our view, material sustainability information should be reported in the annual report alongside the financial statements – in management commentary. Given the close interactions between the practice statement and future ISSB standards, we would recommend that the IASB pauses further work on the practice statement for the time being. It would be appropriate to develop the practice statement in close collaboration with the ISSB, once it is up and running.

The Summary of the Technical Readiness Working Group's Programme of Work recommends that the new board sets a Conceptual Framework for Sustainability Reporting. We strongly support this and urge the ISSB to commence work on the Conceptual Framework without delay. In addition, ACCA has, in our submission to the IFRS Foundation in December 2020[3], highlighted the need for a Conceptual Framework for Corporate Reporting as a whole. Both potential Conceptual Frameworks may directly affect the attributes of useful information in the management.

Question 10—Making materiality judgements

Chapter 12 proposes guidance to help management identify material information.

Paragraphs BC103–BC113 explain the Board's reasoning in developing that proposed guidance.

[3] https://www.accaglobal.com/gb/en/technical-activities/technical-resources-search/2020/december/acca-reponse-ifrs-consultation-sustainability-reporting.html

Do you have any comments on the proposed guidance?

We agree that the receiving company should account for the combination from the date that it takes effect and there should be no restatement of results as if the entities had always been combined.

Disclosure requirements

Question 11

Paragraphs 5.5–5.12 discuss the Board's preliminary views that for business combinations under common control to which the acquisition method applies:

(a) the receiving company should be required to comply with the disclosure requirements in IFRS 3 Business Combinations, including any improvements to those requirements resulting from the Discussion Paper Business Combinations—Disclosures, Goodwill and Impairment; and

(b) the Board should provide application guidance on how to apply those disclosure requirements together with the disclosure requirements in IAS 24 Related Party Disclosures when providing information about these combinations, particularly information about the terms of the combination.

Do you agree with the Board's preliminary views? Why or why not? If you disagree, what approach do you suggest and why?

The introduction of materiality as being linked to key matters, rather than as an attribute of information, makes application difficult. Because of the way that materiality is introduced in the practice statement, the distinction between key matters and material information is not clear. While BC78 provides some explanation, it does not provide a suitable basis for application.

The presentation of materiality as a characteristic of key matters is unhelpful as this seems to be a circular argument. As noted in our answer to Question 9, we believe that relevance should remain the overarching attribute, instead of materiality. Starting with relevance would enable the guidance to emphasise that it is crucial for materiality determination to be entity-specific.

The guidance in Chapter 12 is currently too vague to be helpful to preparers. The factors to be considered when assessing whether information is material – especially under the notes in paragraphs 12.7 and 12.8 – require further expansion and illustration to avoid misinterpretation.

it would be beneficial to outline the process that management should follow to identify material information, with direct reference to *Practice Statement 2: Making Materiality*

Judgements. The <IR> Framework (paragraphs 3.21 – 3.29) also provides useful guidance in this respect.

Question 11—Completeness, balance, accuracy and other attributes

(a) Chapter 13 proposes to require information in management commentary to be complete, balanced and accurate and discusses other attributes that can make that information more useful. Chapter 13 also proposes guidance to help management ensure that information in management commentary possesses the required attributes.

Paragraphs BC97–BC102 and BC114–BC116 explain the Board's reasoning for these proposals.

Do you agree with these proposals? Why or why not? If not, what do you suggest instead and why?

(b) Paragraphs 13.19–13.21 discuss inclusion of information in management commentary by cross-reference to information in other reports published by the entity.

Paragraphs BC117–BC124 explain the Board's reasoning for these proposals.

Do you agree with these proposals?

(a) In our view, instead of proposing attributes of management commentary information, the Practice Statement should refer directly to the qualitative characteristics as set out in the existing and future Conceptual Frameworks. Aspects of the Conceptual Framework for Financial Reporting are directly relevant to the application of the PS – for example paragraph 2.21 of Conceptual Framework setting out the process for applying the fundamental qualitative characteristics. This should be explicitly referenced.

It is crucial that the IASB and the new Board use terminology and language that is consistent, with the Conceptual Framework acting as a point of reference. In this context, for example, we recommend that the PS refers to the qualitative characteristics using the same terms as currently employed in the Conceptual Framework for Financial Reporting. In our view, the terminology in the Conceptual Framework is more precise, and no less comprehensible, than the attributes proposed in this PS. By the same token, the PS should also ensure consistency of language elsewhere: for example, when referring to investors, creditors, and lenders (sometimes only investors are referred to, sometimes investors and creditors).

We have further specific comments in relation to the attributes as follows:

Materiality

Materiality seems less clearly understood than relevance. We would suggest that the PS refers to relevance, with an emphasis on the importance of entity-specific information. Clear step-by-step guidance on the process that management and preparers should follow to report material information would be beneficial. This can come through a direct reference to Practice Statement 2: Making Materiality Judgements, and the <IR> Framework.

Coherence

While we welcome and agree the inclusion of coherence as an additional characteristic of useful information, it is currently narrowly defined. We would recommend that the Board expands this characteristic to cover consistency in discussing strategic objectives and in connecting information about key resources and relationships – thus encompassing the <IR> Framework guiding principles of strategic focus and connectivity. We consider these two guiding principles to be essential to good corporate reporting.

As noted above, the qualitative characteristics for corporate reporting as a whole may need to be developed as a joint effort between the IASB and the new board. This should consequently inform the Practice Statement on Management Commentary.

Accuracy

In our view, 'accuracy' should not replace the original term, 'freedom from error'. Paragraph 13.12 refers to 'freedom from material error.' Without the fuller context from the Conceptual Framework for Financial Reporting, and in the absence of a definition for 'material error', this is unhelpful.

Clarity and conciseness

In line with our comment above, we would recommend that the PS refers to the qualitative characteristic of understandability. The Conceptual Framework for Financial Reporting provides useful guidance, which the replacement of 'understandability' with 'clarity and conciseness' would seem to omit. CF paragraph 2.35 would seem important in the context of MC, for example: 'some phenomena are inherently complex and cannot be made easy to understand. Excluding information about those phenomena from financial reports might make the information in those financial reports easier to understand. However, those reports would be incomplete and therefore possibly misleading.'

(b) In our view, information that is material to an entity's ability to create value should be presented in management commentary, even if more extensive discussion is provided in another report. While cross-referencing helps to reduce duplication, it should not be seen as a substitute for the presentation of material information. This should be made clearer in the note under paragraph 13.19.

Conversely, more clarity over how to determine which part of a cross-referenced report would be considered to be part of the management commentary would also be important, as this has implications for audit and assurance.

We are concerned that Para 13.17 (c) may be wrongly interpreted as suggesting that information already covered in the FS should not feature in MC. Preparers should not be dissuaded from providing further context about the climate-related risks facing the entity in the MC, just because they are mentioned in a note in the financial statements. On the contrary, consistency between the financial statements and the MC is crucial.

We agree with paragraph 13.20(c), in that the board should take the same level of responsibility over information that is crossed referenced, as over the management report.

Question 12—Metrics

Chapter 14 proposes requirements that would apply to metrics included in management commentary.

Paragraphs BC125–BC134 explain the Board's reasoning for these proposals.

Do you agree with these proposals? Why or why not? If not, what do you suggest instead and why?

We agree with the proposed requirements in relation to metrics.

The requirement under paragraph 14.15 to compare current period performance against previously published forecasts or targets will be particularly helpful in rendering reporting against targets more reliable and consistent. However, given the concerns around the competitive information and market perceptions if the entity fails to meet its initial expectations, further guidance may be needed to encourage entities to publish forecasts and targets.

Question 13—Examples of information that might be material

Material information needed to meet the disclosure objectives set out in Chapters 5–10 will depend on the entity and its circumstances. Chapter 15 proposes examples of information that might be material.

Paragraphs BC80–BC81 explain the Board's reasoning for these proposals.

Do you expect that the proposed examples would help management to identify material information that management commentary might need to provide to meet disclosure objectives for information about:

(a) the entity's business model;

(b) management's strategy for sustaining and developing that business model;

(c) the entity's resources and relationships;

(d) risks to which the entity is exposed;

(e) the entity's external environment; and

(f) the entity's financial performance and financial position?

If not, what alternative or additional examples do you suggest? Do you have any other comments on the proposed examples?

As noted in our response to Q4, it is unhelpful to have the examples of information that might be material in a separate chapter, rather than in the main body of the requirements alongside the disclosure objectives and key matters for each area of content.

Although we understand the rationale behind the Board's decision not to be prescriptive about the information that management commentary must provide, many key matter examples given in Chapter 15 are quite generic. As such, they can arguably be presented as requirements rather than as examples, while still allowing sufficient scope for preparers to exercise judgement in identifying relevant entity-specific information.

Many of the 'material information' examples are narrowly scoped, focusing primarily on connections between financial capital and other capitals in a restricted sense. There is a missed opportunity to highlight connections around natural capital. This seems problematic especially given the documents published by the IFRS Foundation on 2 November, which highlighted that the management commentary is a likely location of information reported applying the new sustainability reporting standards.

Most of the 'material information' examples provided are also backward-looking, which would seem to run counter to the Board's stated intention to emphasise matters fundamental to entities' ability to create value in the long-term.

Question 14—Effective date

Paragraph 1.6 proposes that the Practice Statement would supersede IFRS Practice Statement 1 Management Commentary (issued in 2010) for annual reporting periods beginning on or after the date of its issue. This means that the Practice Statement would be effective for annual reporting periods ending at least one year after the date of its issue.

Paragraphs BC135–BC137 explain the Board's reasoning for this proposal.

Do you agree with the proposed effective date? Why or why not? If not, what effective date do you suggest and why?

The effective date is perhaps less relevant for the practice statement than it is for IFRS standards, as we are not aware any national authorities intending to mandate the use of the practice statement.

As a source of best practice guidance for preparers, entities should be encouraged to adopt the practice statement as early as possible, once it is finalised.

Question 15—Effects analysis

(a) Paragraphs BC139–BC177 of the Basis for Conclusions accompanying the Exposure Draft analyse the expected effects of the proposals in this Exposure Draft.

Do you have any comments on that analysis?

(b) Paragraphs BC18–BC22 discuss the status of the Practice Statement. They note that it would be for local lawmakers and regulators to decide whether to require entities within their jurisdiction to comply with the Practice Statement.

Are you aware of any local legal or regulatory obstacles that would make it difficult for entities to comply with the Practice Statement?

a) We believe that the revised Practice Statement could drive improvements in reporting quality, in jurisdictions where there are currently no requirements for reporting outside of the financial statements.

However, as noted in BC140, we also see little evidence currently of entities applying the 2010 practice statement. The expected effects set out in the Basis for Conclusions can only come to pass if more entities around the world adopt the revised practice statement. To achieve this, we would recommend that the practice statement makes a direct reference to the International <IR> Framework, and aligns the revisions further with the underlying concepts, guiding principles and content elements of the <IR> Framework. Thus, the companies applying the <IR> Framework around the world can serve as a base to drive greater adoption for the practice statement.

b) As noted in our covering letter, we have seen limited evidence of lawmakers and regulators' intention to directly mandate the practice statement. On this basis, we would argue that local legal or regulatory obstacles may be a secondary consideration. The practice statement can therefore be more aspirational in terms of driving best practice in management commentary, by aligning with existing voluntary frameworks such as the International <IR> Framework.