



Mr. Stig Enevoldsen
Chairman
Technical Expert Group
EFRAG
Square de Meeûs 35
B-1000 BRUXELLES

E-mail: commentletter@efrag.org

12 February 2010

Ref.: ACC/HvD/LF/ID

Dear Mr. Enevoldsen,

**Re: FEE Comments on EFRAG's Draft Comment Letter on IASB Exposure Draft
*Management Commentary***

- (1) FEE (the Federation of European Accountants) is pleased to provide you below with its comments on the EFRAG Draft Comment Letter on the IASB Exposure Draft *Management Commentary* (the "ED").
- (2) In summary:
 - We support like EFRAG the IASB's decision to develop high-level, principles-based, non-mandatory guidance on the Management Commentary (MC);
 - Like EFRAG, we broadly support the proposals of the ED;
 - Like EFRAG, we do not support the IASB's decision to pursue the MC project while deferring the development of placement principles to Phase E of the conceptual framework. We consider the issue of placement as being essential in establishing the boundaries of financial statements. Accordingly, we believe that it is difficult to establish guidelines for the MC without a clear understanding of what information should be included in the financial statements (the information required to comply with IFRSs) vs. the information that belongs in the MC (information that explains the performance of the entity from the eyes of management). To ensure that the MC is clearly non-mandatory, we believe that it is necessary that the IASB clearly establishes what constitutes a complete set of financial statements under IFRS and reaffirms the principle that complete financial statements under IFRSs must be self-supporting. We believe that clarity on the boundary between financial statements and the MC would contribute to making financial information more understandable and would avoid misinterpretation of the level of assurance given on this information;

- Given that the MC is meant to provide decision-useful information to users, it may be appropriate to include in the MC certain information that by nature does not belong in the financial statements (e.g. certain information on sustainability matters) if this is relevant to understanding the overall performance and outlook of an entity. Accordingly, even though the outcome of the ED is non-mandatory guidance, we believe that reference to Environmental Social and Governance (ESG) matters - in a sustainability context often referred to as CSR (Corporate Social Responsibility) - in the final management commentary guidance document would be helpful;

- We have some concerns regarding two aspects of the desirable characteristics that the ED proposes the MC should have. In particular, we support EFRAG's comments that it might not be realistic to expect the MC to be both comparable between entities and also be able to show the entity's performance with an emphasis on what management views as important. In addition, we are not sure that the notion of verifiability could be applied effectively to the MC, particularly given the basis of the information that is expected to be provided in the MC which could include future oriented information.

Our responses to the questions in the Invitation to comment of the ED are included as an Appendix to this letter.

For further information on this letter, please contact Leyre Fuertes, Project Manager.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Hans van Damme', is written over a horizontal line.

Hans van Damme
President

Status of the final work product

Question 1

Do you agree with the Board's decision to develop a guidance document for the preparation and presentation of management commentary instead of an IFRS? If not, why?

- (3) We agree with EFRAG and support the IASB in carrying out work on the MC. We believe the MC is vital for users to understand an entity's performance. In that respect we believe that the ED, in general, establishes appropriate principles to assist management in preparing the MC that meets the needs of users.
- (4) We note that the principles proposed in the ED are consistent with the existing requirements for the MC in several jurisdictions. Accordingly, in Europe, the ED would have little impact on entities.
- (5) Like EFRAG, we agree that developing non-mandatory guidance with the high level principles of the information to be presented in the MC is the most appropriate approach at this time. This will ensure that the guidance produced by the IASB does not result in contradictions with requirements in many jurisdictions and at the same time contributes to improvement in financial reporting in jurisdictions where such requirements do not exist.
- (6) Paragraph 3 of the EFRAG draft letter notes that the IASB project on the subject ought to assist with the global convergence of the MC reporting requirements. We question whether such convergence would be achieved in the absence of mandatory detailed guidance. We nevertheless believe that the issuance of the MC guidance would contribute to improving financial reporting by providing a useful framework in jurisdictions where the MC is not regulated.
- (7) As a drafting point, we note that in several instances the ED is using the word "should" (several paragraphs such as par. 8, 18-20, 22-23, 31, 33, 35 and others). This word conveys the idea that management must necessarily provide certain information. This may be seen as contradictory with the proposal that the guidance is non-mandatory. Accordingly, we suggest that the IASB considers avoiding using "should" and other similar words.
- (8) Nevertheless, the IASB should consider indicating that, even though the guidance is non-mandatory, an entity cannot claim to have prepared its MC in accordance with the guidance published by the IASB without having fully complied with all of the principles established in this guidance. If the IASB were to follow this route, we nonetheless believe that the presentation of future oriented quantitative information should be recommended but remain voluntary. In Europe, future oriented information is already regulated and subject to a specific attestation by auditors (such as is the case with respect to forecasts). Further, in several jurisdictions where safe harbour provisions do not exist in respect to future oriented information, presenting future oriented quantitative information may have unintended consequences in terms of management responsibilities.

Content elements of a decision-useful management commentary

Question 2

Do you agree that the content elements described in paragraphs 24–39 are necessary for the preparation of a decision-useful management commentary? If not, how should those content elements be changed to provide decision-useful information to users of financial reports?

- (9) Overall, we agree with EFRAG and support the high-level, principles-based approach that the IASB is proposing to adopt.
- (10) Further, we agree with EFRAG and are also broadly supportive of the content elements described in the proposals. However, like EFRAG, we would favour a greater focus on the information objectives and the need to develop the MC with care and less on a list of information to be provided.
- (11) As a drafting point, we note that paragraph 39 indicates that “if financial performance measures that are not required or defined by IFRSs are included within management commentary, those measures should be defined and explained and, **when possible**, reconciled to measures presented in the financial statements.” We question the reason why management would not always be in a position to reconcile measures used in the MC to the measures used in the financial statements. Accordingly, we suggest that the words “when possible” be deleted from this sentence.

Suggestions for references to ESG matters in the final management commentary guidance

- (12) Given that the MC is meant to provide decision-useful information to users, it may be appropriate to include in the MC certain information that by nature does not belong in the financial statements (e.g. certain information on sustainability matters) if this is relevant to understanding the overall performance and outlook of an entity. Accordingly, even though the outcome of the ED is non-mandatory guidance, we believe that reference to ESG matters in the final management commentary guidance document would be helpful. We present below some suggestions of where specific references to ESG could be covered:

- ***Objective (paragraphs 2 and 3 of the ED)***

A reference to ESG issues could be made in paragraph 2 of the Guidance since ESG performance is highly relevant for the corporate strategy and cannot be ignored in presenting a holistic view of the organisation.

- ***Time frame (paragraph 10 of the ED)***

A specific mention of non-financial information could be added in paragraph 10 - where it is indicated that the MC should explain the main trends and factors that are likely to affect the entity’s future performance, position and development - to refer to “financial and non-financial” trends and factors. In our view, an entity needs to demonstrate the current and future relevance of ESG for its business activities and

Appendix - Comments on the EFRAG draft comment letter including the responses to the questions in the Invitation to comment of the IASB Exposure Draft *Management Commentary*

how the entity takes ESG aspects into account in implementing its business strategy. The MC should enhance transparency regarding the risk exposures.

- ***Supplement and complement the financial statement information***

We are of the opinion that it would be helpful if the MC would include a reference to additional reports relevant for the corporate strategy, for example to sustainability reports that are separately published by the organisation.

Application guidance and illustrative examples

Question 3

Do you agree with the Board's decision not to include detailed application guidance and illustrative examples in the final management commentary guidance document? If not, what specific guidance would you include and why?

- (13) We agree with EFRAG and support the IASB's approach not to include detailed application guidance and illustrative examples in the final management commentary guidance document. We believe that this is most consistent with our view that the guidance should not be mandatory.

Additional observations

Objective of the MC

- (14) We agree with EFRAG and support the proposal that the information objective of the MC is the same as the information objective of all other general purpose financial reports as set out in Framework ED: to provide decision-useful information to the primary user group. Financial statements must remain a comprehensive and stand-alone set of information. The MC can offer separate and additional decision-useful information.
- (15) We agree with EFRAG's comment that the first sentence of paragraph 10 of the ED does not fully reflect what we see as the essence of the MC. However, instead of suggesting the deletion of the sentence, we believe that the idea expressed should be clarified. Indeed we do not believe that the MC should "communicate information about an entity's economic resources, claims on those resources and the transactions and other events and circumstances that change them". It is the purpose of the financial statements to communicate this information. The MC should "comment" or "put in context" this information. We believe that making this clarification is important in order to clearly distinguish the different purpose of the financial statements vs. that of the MC.

The users of the MC

- (16) We agree with EFRAG that users of the MC are the same as users of general purpose financial reports as described in the Framework ED.

Appendix - Comments on the EFRAG draft comment letter including the responses to the questions in the Invitation to comment of the IASB Exposure Draft *Management Commentary*

- (17) In addition, we support EFRAG's observation that general purpose financial reports (such as the MC) should not focus exclusively on the information needs of existing and potential capital providers. Therefore, we agree that the reference to existing and potential capital providers as sole users of the information (in paragraph 11 of the ED) might not be appropriate. We agree with EFRAG that it would be more appropriate to use the reference to the description of "Users" as detailed in paragraph 9 of the ED, i.e. existing and capital providers, as the primary users.
- (18) Therefore, we support EFRAG's suggestion (in paragraph 12 of its draft comment letter) to use the term "users" throughout the ED and to make it clear in the description under "Users" in paragraph 9 of the ED that the term is intended to refer to users as described in that paragraph.

Desirable qualitative characteristics of the MC

- (19) We note that EFRAG does not believe it reasonable to expect all MC to be comparable between entities, and be neutral and verifiable (as detailed in paragraph 14 of EFRAG's draft comment letter).
- (20) We support EFRAG's observations regarding the verifiability of the MC as a desirable characteristic. Like EFRAG, we are not sure that the notion of verifiability could be applied effectively to the MC, particularly given the basis of the information that is expected to be provided in the MC and which could include future oriented information. As noted by EFRAG, "supportability" would be a more appropriate characteristic in relation to the MC.
- (21) We also support EFRAG's comments that it might not be realistic to expect the MC to be both comparable between entities and also be able to show the entity's performance with an emphasis on what management views as important. It is difficult to expect that high-level principles included in non-mandatory guidance can result in comparability between entities.
- (22) On the other hand, we are not convinced by EFRAG's arguments with respect to the neutrality of the MC. In our view, if neutrality is defined as "the absence of bias, intended to attain a predetermined result or to induce a particular behaviour", it would be difficult not to agree that the MC should be neutral in the sense that it should be balanced, presenting both positive and negative events that affected (or are expected to affect) the entity.
- (23) We support EFRAG's observation that the meaning of paragraph 23 of the ED ("management should avoid duplicating in its MC the disclosures made in the notes to its financial statements. Doing so may create an obstacle for users to identify and understand the most significant matters facing the entity") is unclear.

PLACEMENT PRINCIPLES

- (24) Like EFRAG, we do not support the IASB's decision to pursue the MC project while deferring the development of placement principles to Phase E of the conceptual framework. We consider the issue of placement as being essential in establishing the boundaries of financial statements. Accordingly, we believe that it is difficult to establish guidelines for the MC without a clear understanding of what information should be included in the financial statements (the information required to comply with IFRSs) vs. the information that belongs in the MC (information that explains the performance of the entity from the eyes of management). To ensure that the MC is clearly non-mandatory, we believe that it is necessary that the IASB clearly establishes what constitutes a complete set of financial statements under IFRS and reaffirms the principle that complete financial statements under IFRSs must be self-supporting. We believe that clarity on the boundary between financial statements and the MC would contribute to making financial information more understandable and would avoid misinterpretation of the level of assurance given on this information.
- (25) In relation to the question of placement, paragraph BC46 of the ED notes that "the Board determined it was important to establish management commentary as a disclosure tool within IFRSs". This brings the question of whether financial information could be considered as being presented in accordance with IFRSs if the financial statements were not accompanied by the MC that complies with the ED. This ambiguity further highlights to importance of resolving the placement principles issue before finalising the MC project.

OTHER COMMENTS

- (26) Management often comments outside the annual financial reports, for example through press releases, interim financial statements, discussions with analyst. Accordingly, we believe that it would be important to clarify that the principles established in the ED relate to the MC presented with the financial statements.

Principles for the preparation of management commentary

- (27) We question whether paragraphs 12 (a), 12 (b) and 12 (c) cover all key aspects. While we note that these are given by way of examples, we note that the list of items in paragraph 24, in our view better articulates all of what is covered in paragraph 12.