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Comments on IASB Exposure Draft on IFRS Practice Statement: *Management Commentary*

The Japanese Institute of Certified Public Accountants (hereinafter "JICPA") respects the continued efforts of the IASB and appreciates the opportunity to comment on Exposure Draft "IFRS Practice Statement Management Commentary" (hereinafter the "Exposure Draft").

The demand for non-financial information has increased in capital markets in recent years. The JICPA has recognized that it is highly important to provide financial and non-financial information in an integrated manner, thereby communicating to information users an entity's ability to sustainably create value and ultimately generate cash flows. The IFRS Foundation has been working toward setting standards for sustainability reporting, including reporting on climate change. We believe that sustainability information should be reported as part of more comprehensive non-financial information, which covers the entity's business model, strategy, risk, and governance, to address the fundamental needs of capital market participants, and that updating Practice Statement Management Commentary is also meaningful from the perspective of increasing the usefulness of sustainability reporting.

In the Exposure Draft, important proposals are made on various points. In particular, we strongly support the adoption of a purpose-based approach, the basic structure of the Areas of Content, and the method of ensuring the disclosure of important information through identification of Key Matters.

Meanwhile, in reviewing the Exposure Draft, we have become aware of the following issues and believe further improvements are necessary:

1. Positioning of Management Commentary in Corporate Reporting (Including Its Relationship with Financial Reporting)

We understand that in the Exposure Draft, the Practice Statement "Management Commentary" (hereinafter the "Practice Statement" or "Management Commentary") is positioned as narrative reporting on an entity's ability to create value. We also believe that sustainability information, for which the International Sustainability Standards Board (hereinafter the "ISSB") will develop standards in the future, can be positioned as part of Management Commentary or as the information complementing Management Commentary.

While we basically agree with such positioning of Management Commentary, we understand that it is controversial whether Management Commentary falls within the scope of financial reporting and also whether the Conceptual Framework of financial reporting applies to Management Commentary. For instance, the question remains whether the qualitative characteristics of useful information defined in the Conceptual Framework thoroughly apply to Management Commentary (refer to the answer to Question 11). Also, the elements of information to be disclosed in Management Commentary are not defined in the Conceptual Framework of financial reporting.

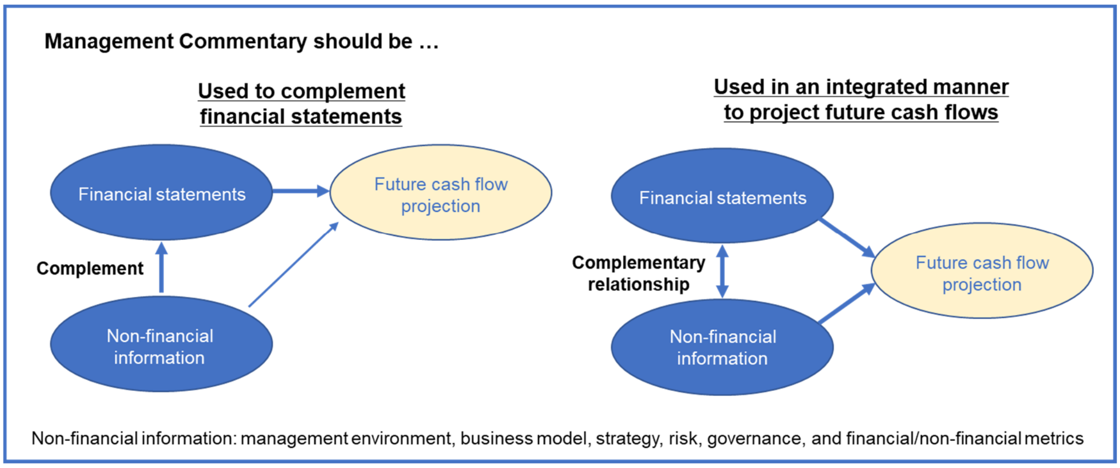
Given these circumstances, we have come to believe that it may be difficult to position Management Commentary within the scope of the Conceptual Framework of financial reporting. To address these issues, we have the following two potential approaches to choose from: i) positioning Management Commentary outside the scope of the Conceptual Framework of financial reporting, or ii) revising the Conceptual Framework so that it reflects the characteristics of Management Commentary. We believe, however, that we should not take approach ii) as it could undermine the stability of the financial reporting standards.

We believe it is important to develop a framework that enables desirable narrative reporting while ensuring the stability of the standards by adhering to accumulated knowledge and consensus on financial reporting. From this perspective, we also believe it is necessary to underscore that corporate reporting should consist of financial reporting and Management Commentary including sustainability information (narrative reporting). On top of this, from the perspective of maximizing the usefulness of Management Commentary while clarifying the relationship and connectivity between financial reporting and Management Commentary (narrative reporting), we are convinced that it is important to clearly define the objective of reporting, basic principles, content elements, presentation principles, etc.

2. Objective of Management Commentary

In IN3, it is noted "Management Commentary is a report that complements an entity's financial statements." We understand that the objective of Management Commentary has been expanding and evolving (i.e. has been updated) given that a term representing its relationship with financial statements has been replaced from "supplement" to "complement" in the Exposure Draft and it is mentioned that management insights, regarding the factors that may affect the entity's value creation ability and cash flow generation in the future, should be provided.

In our view, the ultimate objective of corporate reporting is to assist information users in economic decision making based on future cash flow prediction and risk assessment. In order to better achieve this objective, it is important that information users use financial and non-financial information (Management Commentary) in an integrated manner when assessing corporate value. Non-financial information (Management Commentary) is primarily intended for use by investors directly in their cash flow and risk assessment. We therefore propose making it clearer that the role of Management Commentary is to "help users assess corporate value in an integrated manner with financial statements" and also that Management Commentary is in a complementary relationship with financial statements (refer to Figure).



3. Roles of Those Charged with Governance

Leadership and oversight by the board of directors are critical to narrative reporting. It is also strongly required that business model, strategy, risk, governance, performance evaluation, etc. reflect the board of directors' collective views. Further, narrative reporting is focused on providing future-oriented information, including management strategies and risks. Such future-oriented information reflects the recognitions and assertions of corporate management, and thus, it is difficult to ensure verifiability, which results in a strong need for raising the credibility of disclosure information through reporting governance and process. Therefore, it is fundamental that the corporate reporting monitoring process of supervisory bodies, such as the board of directors including independent directors, functions effectively, and also that the governance and process related to corporate reporting are well explained to information users to enhance credibility.

However, regulations on the structure of corporate governance and the roles that the board of directors and other supervisory bodies should play in corporate reporting may vary from jurisdiction to jurisdiction. In view of the positioning of Management Commentary as a global standard, it is not desirable to make requirements that are applicable only to specific jurisdictions.

Based on the above, 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.

4. Required Normativity and Naming of This Document

We agree with the direction of developing this Practice Statement which is designed for adoption by reporting entities. Also, we agree with the Exposure Draft adopting the comply or explain approach. Given that the practice of narrative reporting is still evolving, we believe it is appropriate to explain the reasons for departures to users while allowing for limited compliance rather than requiring full compliance.

On the other hand, while the Exposure Draft assumes that the inclusion of requirements ensures compliance by preparers, the fact that the positioning (naming) of the document remains unchanged from IFRS Practice Statement may need to be reconsidered (including renaming the document to Standards).

5. Assurability

The Exposure Draft employs an objectives-based approach. We support the adoption of an approach in which preparers identify information to be disclosed from the perspective of achieving the reporting objective, while taking into account the needs of users.

Meanwhile, many of the requirements in this Exposure Draft (sentences containing “shall”) are related to objectives, which require high-level judgment. Since the fulfilment of these objectives is highly dependent on subjective judgment, it is difficult, if not impossible, to objectively verify and assess them from a third-party perspective. It is therefore assumed that there may be significant differences in the judgments of auditors and regulating authorities. Under such circumstances, if a third party assures compliance with this Practice Statement as a whole, this may result in users having doubts about the credibility of such assurances, and thus the value of assurance.

Based on our review concerning assurance, we recognize that currently there is no strong need for assurance that non-financial reporting as a whole is in compliance with comprehensive standards, but rather a strong need for third-party assurance on performance information, such as KPIs, and disclosure of the governance and processes related to reporting to enhance information credibility. With regard to KPIs, it is strongly expected that measurement standards for specific information to be considered by the ISSB will function to provide assurance. Regarding disclosure of the governance and processes, we request that information be added to this Exposure Draft from the perspective of enhancing the quality of Management Commentary disclosure based on objective-based standards.

Our answers to each of the questions in the Exposure Draft are as follows:

Question 1—The financial statements to which management commentary relates
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?

(Comment)

We agree with both (a) and (b).

We believe that the proposals in this Exposure Draft are generally effective as a framework for providing useful information, regardless of the basis on which the related financial statements are prepared.

On the other hand, it should be noted that the significance of management commentary as a complement to financial statements will be smaller for those prepared on a cash basis.

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

(Comment)

(a) We agree on the direction of developing a commentary that ensures compliance with the Practice Statement.

Since currently there is no internationally established standard for the disclosure of non-financial information, it would be useful for users wishing to assess the credibility of the information if the management commentary states that it complies with all the requirements of this Practice Statement and that it is unqualified.

(b) We agree with the adoption of the comply or explain approach.

Given that the practice of management commentary (narrative reporting) is still evolving, we believe that it is appropriate to explain the reasons for departures to users while allowing limited compliance rather than requiring full compliance.

On the other hand, the following points need to be carefully considered:

(1) Adequate due process to ensure the quality of this Practice Statement and to build consensus

(2) In relation to (1) above, sorting out the relationship with the standards to be developed by the ISSB

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 3.15–3.19 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?

(Comment)

We agree in principle to both objectives (a) and (b).

However, we think it is necessary to sort out the order in which the two objectives are stated and their relationship with the comprehensive objective of corporate reporting.

In our view, the ultimate objective of corporate reporting is to assist information users in economic decision making based on future cash flow prediction and risk assessment. In order to better achieve this objective, financial and non-financial information (management commentary) should be used in an integrated manner when information users assess corporate value.

In this regard, the primary objective of non-financial disclosure (management commentary), together with financial statements, is to directly help investors and others understand and assess the entity's ability to create value, and we recognize that its relationship with financial statements is more complementary than supplementary. Investors use information such as the strategies, business models and risks of an entity primarily to assess its value (and profitability, growth, and risk assessment for that purpose). If this is the case, objective (b) should be stated prior to (a).

On the other hand, it is also understandable that the IASB, whose primary role is to set standards for financial reporting, reviews management commentary with an emphasis on its effective use as a complement to financial statements. We can clearly see the IASB's view from how the board defines management commentary: "a report that complements an entity's financial statements" as described in IN3.

We expect that the IASB and ISSB will work together effectively to achieve the ultimate objective of corporate reporting in the IFRS Foundation's initiatives on non-financial disclosures, including sustainability reporting. Ideally, the guidance on management commentary should cover sustainability reporting, and from this perspective, it is important to describe its positioning and objectives.

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?

(Comment)

(a) Is the approach capable of being operationalised?

Yes (with limitations).

We agree with the adoption of an approach in which preparers identify disclosure information from the perspective of achieving the reporting objective while taking into account the needs of users.

However, because this approach depends on the subjective judgment of the preparer and the reporting governance process, there may be cases where it is not possible to provide the high-quality information that meets users' needs. In this sense, it has certain limitations. On the other hand, it may be premature at this stage to include the content exemplified in Chapter 15 in requirements. It is conceivable that these matters would be added as requirements in the future, when the practice becomes widespread.

For (b) areas of content, the following points need to be reviewed.

- We think that the matters identified as disclosure objectives in this Exposure Draft are more like requirements that should be taken into account when reporting than objectives, thus it feels inappropriate to call them reporting objectives.
- We believe that "risks", one of the areas of content, should be changed to "risks and opportunities". In recent years, there has been a growing need to report both the downside and the upside of uncertainty in the disclosure of non-financial information, and it is desirable that this Practice Statement reflect such need.
- We believe that metrics should be presented together with the relevant performance. This point is addressed in detail in our response to Question 6.

The Exposure Draft employs an objectives-based approach. We support the adoption of an approach in which preparers identify information to be disclosed from the perspective of achieving the reporting objective, while taking into account the needs of users.

(b) Is the approach enforceable?

No.

Many of the requirements in this Exposure Draft (sentences containing "shall") are those related to objectives, which require high-level judgment. Since the fulfilment of these objectives is highly dependent on subjective judgment, it is difficult, if not impossible, to objectively verify and assess it from a third-party perspective. It is therefore assumed that there may be significant differences in the judgments of auditors and regulating authorities. Under such circumstances, if a third party provides assurance of compliance with this Practice Statement as a whole, this may result in users having doubts about the credibility of such assurances, and thus their value.

If this Practice Statement aims to provide assurance concerning management commentary, it would be conceivable to set as requirements the points to be noted for disclosure by area of content in Chapter 15. Based on our review concerning assurance, we recognize that currently there is no strong need for assurance that non-financial reporting as a whole is in compliance with comprehensive standards, but rather a strong need for third-party assurance on performance information, such as KPIs, and disclosure of the governance and processes related to reporting to enhance information credibility. With regard to KPIs, it is strongly expected that measurement standards for specific information to be considered by the ISSB will function to provide assurance. For disclosure governance and processes, we request that information be added to this Exposure Draft from the perspective of enhancing the quality of Management Commentary disclosure based on objective-based standards.

We would also like to point out that this Exposure Draft mixes requirements and guidance when presenting them. This structural complexity makes it difficult to identify and understand the requirements.

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?

(Comment)

We disagree with the proposal.

There are three levels of objectives, which is (or looks) complicated. We believe that assessment objectives and specific objectives can be practically integrated.

Question 6—Disclosure objectives for the 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?

(Comment)

The following points should be revised.

<u>Governance</u>

- Governance matters is a key element of corporate reporting and is useful for investors and creditors to understand whether an entity is creating value and generating cash flows in a sound manner. There is a strong need for a globally consistent framework for this information.
- Institutional regulations in each country, including topics other than governance, are becoming more specific and it would be problematic in terms of consistency to not set global standards for governance reporting because of the existence of such regulations.
- Those in charge of governance reporting should be Those Charged with Governance, and its framework may be developed separately from that for management commentary. However, as the governing board's views on entity strategies, business model, risk, and performance are also given particular importance, and the integration of management commentary and governance reporting is required, we expect more in-depth review in this area.

Performance

- Performance can be addressed by expanding the scope of financial performance to include non-financial performance. Among metrics, those related to performance and position should be incorporated into performance information as performance indicators.

Resources and relationships

- Resources and relationships, the core of business models, should be reported as an integral part of business models. Relationships may be positioned as part of resources. If that is not the case, relationships should be addressed separately from resources to clarify details of each element. In addition, examples for an entity's resources should include technology resources.

Risks

- In general, risk disclosure should be combined with opportunity disclosure.

Business model

- This Practice Statement focuses on relatively limited business models for the present and near future only, and does not address business model transformations that reflect medium- to long-term environmental changes (megatrends) or innovative changes.
- In addition, Figure 1 could be further improved. In particular, the relationship between business model and strategy needs to be further clarified. There is also room for improvement in the order of areas; in particular, external environment should come first.

It is expected that standards to be developed by the ISSB will address information related to management commentary. Although the preparation of management commentary itself is not mandatory, the IASB should consider the consistency with standards to be issued by the ISSB, as it may be incorporated into the framework for disclosure of non-financial information in each jurisdiction (for example, in Japan, the Cabinet Office Order on Disclosure of Corporate Affairs).

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?

(Comment)

We strongly agree that management commentary should focus on key matters (Question (a)), and that this Practice Statement clearly states the guidance, including examples of key matters (Question (b)).

Paragraphs 3.15 to 3.17 distinguish between material information and key matters. Since the relationship between the two is very important, a diagram, for example, should be added to promote clear understanding.

We also make the following two comments on the identification of key matters:

<u>Presentation of key matters</u>

- Paragraph 4.10 lists the following as indications that a matter might be key, but (c) in particular may be too broad.
  - (a) discussed with the entity's board or other governing body;
  - (b) discussed in the entity's capital markets communications—for example, in presentations to investors and creditors; or
  - (c) raised by the entity's customers, suppliers, employees or other stakeholders.
- While we agree that stakeholder views should be taken into account, we suggest that it would be better to adopt a process to assess and identify the materiality of matters among those identified through systematic stakeholder engagement, for which knowledge has been accumulated in integrated reporting and the like.

<u>Layers of key matters</u>

- We agree with the approach of organizing key matters by area of content, but we think more specific guidance is needed on the relationship between the identification of "what are key matters" and the entity's ability to create value and generate cash flows at the top of Figure 2 (on page 33). For example, if the diversity of human resources is identified as a key matter, how does it relate to each content area? In integrated reporting practices, risks and opportunities are assessed with consideration of external environmental changes, business models, resources and relationships, and the results are reflected in key matters (generally materiality). These key matters are incorporated into strategies and are measured and monitored as KPIs (metrics). It is important that such a series of processes are logically connected, and this Practice Statement should explain such a process (flow).

Question 8—Long-term prospects, intangible resources and relationships 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?

   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?

(Comment)

While we believe that the requirements and guidance proposed in this Exposure Draft are useful for investors and creditors to understand (i) through (iii), they should be considered in light of their relevance to the sustainability reporting standards to be issued by the ISSB.

The ISSB is expected to publish standards for non-financial information, particularly on climate change issues, in the future, and thus it is necessary to consider consistency with those standards. For example, the disclosure items recommended by the TCFD are Governance, Strategy, Risk Management, and Metrics and Targets, but as mentioned in our response to Question 6 above, unless governance matters are included in the management commentary framework, this Practice Statement would be inconsistent with the TCFD recommendations.

In any case, reporting on long-term issues such as ESG is strongly related to sustainability reporting, which is being reviewed by the ISSB, and we do not think that the IASB should provide specific guidelines prior to the outcome of such review.

Question 9—Interaction with the IFRS Foundation Trustees' project on sustainability reporting

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?

(Comment)

As already mentioned, many of the matters proposed in this Exposure Draft are expected to overlap with standards to be issued by the ISSB. It is also envisaged that this Practice Statement may have an overall framework similar to that of the ISSB standards. In this regard, it is necessary to clarify the relationship and consistency between the two.

This Practice Statement should be positioned as a provisional one, and a joint committee of the IASB and the ISSB should be set up to develop a framework and/or standards for non-financial reporting when the review by the ISSB has progressed to a certain extent.

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. Do you have any comments on the proposed guidance?

(Comment)

Definition of "materiality"

The definition of "material" in this Exposure Draft is consistent with that of IFRS, and thus should be easy to understand for those who are familiar with IFRS. We strongly hope that the concepts of materiality and key matters will be applied consistently to the ISSB standards to be developed, while taking into account their consistency with financial reporting.

Relationship between material information and key matters

In the Exposure Draft, some considerations concerning material information and key matters overlap. Specifically, factors (b) and (c) of paragraph 12.4, which describe indications that information might be material, are already discussed in identifying key matters (in paragraph 4.10), and therefore it may not be clear to readers why this paragraph discusses the identification of material information.

In order to eliminate the complexity from this document, we suggest making the following revisions for improvement:

- Clearly state that in principle, all information related to key matters is material information.
- List factors that should be considered other than those related to key matters as well.

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

(Comment)

(a) No.

We believe that the attributes identified in Chapter 13 are organized in a manner that is intended to be consistent with the qualitative characteristics of useful financial information identified in the Conceptual Framework for financial reporting. However, as shown in the table below, there are differences in how to treat the terms “relevance”, “timeliness”, and “coherence”, as well as in how to use the terms “neutrality” and “free from error”. The table below compares the relationship between the qualitative characteristics of financial reporting described in the Conceptual Framework and the attributes identified in this Exposure Draft, based on our recognition.

Qualitative characteristics of financial reporting in the Conceptual Framework		Attributes identified in this Proposed Practice Statement
Fundamental	Relevance	
	− Materiality	
	Faithful Representation	
	− Completeness	Completeness
	− Neutrality	Balance
	− Free from error	Accuracy
Enhancing	Comparability	Comparability
	Verifiability	Verifiability
	Timeliness	
	Understandability	Clarity and Conciseness
		Coherence

The background behind the differences may be that the Conceptual Framework was developed primarily with IFRS, a financial reporting standard, in mind, and was not intended for non-financial information. Therefore, we believe that it would not be an essential solution that this Practice Statement sets attributes required for management commentary so that they completely match the qualitative characteristics described in the Conceptual Framework.

We consider it impractical to limit the scope of management commentary to financial reporting only. We propose that financial reporting be limited to financial accounting and related disclosure only, and that information such as strategy, business model, and risks be placed outside the scope of financial reporting. On this basis, it is important to build consensus on the fundamental principles that should be met in narrative reporting on sustainable value creation.

The following are additional comments on the attributes:

- The overall impression of the disclosure attributes for narrative reporting of sustainable value creation is static. From the perspective of satisfying the fundamental needs of users, the inclusion of attributes such as future orientation and value relevance should be considered.
- It is questionable whether it is appropriate to use the term “accuracy” for management commentaries that contain a lot of narrative information. It would be more appropriate to use the term “free from material error”.

- “Conciseness” has been identified as an attribute, but we are concerned about the risk that non-financial information may be general and abstract. Therefore, we suggest that the Practice Statement state that such information requires a certain level of granularity.
- We also regard “timeliness” very important.

(b) We agree with cross-referencing, provided that the inclusion of management commentary information is limited to a main annual report (single medium).

Cross-referencing is expected to enhance the usefulness of disclosure information by avoiding duplication of information and ensuring the comprehensiveness of disclosure.

On the other hand, the scope of inclusion of management commentary should not be extended to multiple media through cross-referencing. It should be made clear that management commentary should be reported in a single report in its entirety, and that references to other media, if any, are outside the scope of management commentary.

In particular, the public expectation for assurance of non-financial information is expected to increase in the future, and it is necessary to clarify the scope of information subject to assurance. We are opposed to cross-referencing to other reports if it expands the scope of management commentary, as it may obscure the scope of information subject to assurance.

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?

(Comment)

No.

We recognize that it is important that meaningful metrics are disclosed in an effective manner in order to ensure the usefulness of management commentary. On this basis, we recognize that the requirements in Chapter 14 need to be further improved in the following areas:

- Metrics are presented for all areas of content, but some of them, such as risk metrics, may be disclosed in too much detail. In integrated reporting and other non-financial reporting, metrics are generally used synonymously with KPIs and are understood as indicators of financial and non-financial performance. While it is important to use objective numbers to provide evidence-based disclosures about the external environment and risk perception, it seems unfitting to call them metrics, and we are concerned that defining metrics too broad may increase the complexity of this guidance.
- Taking into account its consistency with existing frameworks, guidance, and practices, non-financial information should be integrated into financial performance and financial position, to be referred to as performance and position. It is also important for management and the board of directors to present their analysis and views on performance, and this point should be clarified in the Practice Statement.

- Regarding the treatment of changes in metrics from the previous reporting period, the Exposure Draft requires that details of changes be described and the reasons for those changes be explained (Paragraph 14.8 (c)). From the perspective of comparability of periods, the need to disclose retrospectively revised metrics for the previous reporting period should be considered.

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?

(Comment)

We find that these examples will help to ensure the quality of disclosure.

However, we get the impression that examples with very different characteristics are listed randomly. We suggest that they be organized by grouping and explanations for them be provided in the form of guidance etc.

As stated in our response to question 4, it is considered difficult for a third party to objectively determine that the disclosure objectives have been met. Therefore, if the priority is to ensure "assurability" on disclosed information, an approach may be taken to determine required disclosure items in detail and then omit items that do not need to be disclosed in light of materiality and disclosure objectives.

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?

(Comment)

We have no comments.

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?

(Comment)

We have no comments.

Question 16—Other comments
Do you have any other comments on the proposals set out in the Exposure Draft?

(Comment)

As stated at the beginning of this document.

Yours faithfully,

Takako Fujimoto

Executive Board Member — Business Accounting Standards and Practice/Corporate Disclosure

The Japanese Institute of Certified Public Accountants