Deutsches Rechnungslegungs Standards Committee e.V.

Accounting Standards Committee of Germany

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Berlin, 22 November 2021

Mr Andreas Barckow
Chair of the
International Accounting Standards Board
Columbus Building
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London E14 4HD

Dear Andreas,

IASB Exposure Draft ED/2021/6 *Practice Statement Management Commentary*

On behalf of the Accounting Standards Committee of Germany (ASCG) we are writing to comment on the Exposure Draft ED/2021/6 Practice Statement Management Commentary issued for consultation by the IASB on 27 May 2021 (herein referred to as 'ED').

The IASB is certainly aware that the Management Report has been subject to detailed regulation in the European Union since 1978, and, in particular, in Germany since 1986, as regards the scope and the content of such reports. Articles 19 and 29 of the Directive 2013/34/EU (Accounting Directive) contain guidance on the Management Report and the Consolidated Management Report, respectively, setting out a baseline for EU member states to adhere to in their own legal framework. In Germany, the scope and the content of the Management Report is governed by the German Commercial Code (GCC).[1]

Furthermore, the ASCG has been addressing the topic since 2004 when German Accounting Standard No. 15 (GAS 15) *Management Reporting* was issued. Meanwhile, GAS 15 has been superseded by GAS 20 *Group Management Report* in 2012. Many of our comments on the questions raised by the IASB in the ED are based on our line of thinking underlying the content of GAS 20 as well as the experience made with the requirements in Germany. We further believe, this way of approaching the discussion in the ED on management commentary might be helpful for the IASB as well since we are aware that the Board is also revising the Practice Statement with the aim of enabling national legislators and regulators of certain jurisdictions, where no or no comparable guidelines exist, to require the application of PS 1 in these jurisdictions.

[1] For the purpose of this comment letter, the terms ‚Management Report' and ‚management reporting' are consistently used when referring to the EU / German reporting requirements.

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We support the IASB's rationale for revising the PS 1 as set out in para IN8 of the ED as we also consider the information needs of users of management reporting are subject to significant change that is not only driven by the evolving sustainable finance regulation in the EU. However, we believe that some of these emerging issues, in particular regarding the reporting on ESG topics are – although addressed in general – not elaborated in the ED in a sound and conceptual manner. This might be because the IASB does not want to pre-empt the ISSB in its approach to ESG-reporting. However, not only in this case, we believe the IASB should consider pausing the project on the revision of PS 1 until there is sufficient clarity on the ISSB's approach. An important aspect from our point of view is that it seems unclear at this point how the IFRS Foundation, i.e. IASB and ISSB, intend to address the matter of interconnectivity between financial reporting and sustainable reporting - a key issue for the further development of corporate reporting as a whole. Our view in this respect would also be supported by the discussion on the double materiality, in particular regarding the relevance of inside-out effects for the content of corporate reporting in general as set out in detail in our answer on the IASB's question 9 raised in the ED.

Finally, we would like to point out that PS 1 is not widely applied in Germany for the reasons mentioned above. There is some anecdotal evidence supporting that observation. A study published by KPMG in 2014[2] shows that only two of the 30 entities of the DAX30 segment declared their Management Reports prepared in accordance with the GCC and GAS 20 were also in line with PS 1. A quick revision by the ASCG staff of the Management Reports of the DAX40 for the financial year 2020 did not indicate a change in this conclusion.

In order to not only help the guidelines for management commentary to gain a broader application (possibly with the view of turning the PS 1 guidance into an IFRS Standard), but also to gain global acceptance for the IFRS Sustainability Standards (by means of a global baseline), the Foundation should strive for the highest possible level of compatibility of these sets of guidance with the current and upcoming requirements and political goals of at least the largest jurisdictions of the world. This includes, but is not limited to, keeping up with current aforementioned developments in the European Union with regard to the Management Report, which in the future will have to contain the sustainability reporting.

Our responses to the questions to constituents raised in the ED are laid out in the appendix to this letter. If you would like to discuss our comments further, please do not hesitate to contact Thomas Schmotz (schmotz@drsc.de) or us.

Yours sincerely,

Georg Lanfermann	*Sven Morich*
President	Vice President

[2] See KPMG, Accounting Insights, August 2014.

Appendix – Answers to the questions in the DP

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?

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

The EU legal framework contains a minimum requirement for listed parent companies in the scope of the Accounting Directive to prepare group financial statements according to IFRS Standards. According to the German legal framework, the requirements of the German Commercial Code (GCC) and the German Accounting Standard No 20 (GAS 20) governing the content of the Management Report or the Group Management Report accompanying the financial statements of an entity have to be adhered to in the same manner regardless of whether the financial statements of that entity were prepared in accordance with the GCC or IFRS Standards. Based on the experience gained from this practice, we think that a comparable rule for the revised PS 1, according to which entities should be permitted to state compliance with that Practice Statement in preparing the management commentary even if their financial statements are not prepared in accordance with IFRS Standards, might be meaningful and practicable by analogy.

We have further discussed whether or not PS 1 should contain a minimum condition as mentioned by the IASB. According to that condition, the financial statements of an entity would need to be based on concepts similar to those underpinning IFRS Standards (such as the accrual principle underlying many other standards and requirements including the GCC) to be complemented by management commentary prepared in compliance with the PS 1. However, we agree with the IASB's arguments brought forward in the ED's Basis for Conclusions, including the reasoning that entities preparing financial statements according to concepts very different from the accruals concept will unlikely apply the PS 1.

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?

We agree to question 2 (a) that management commentary that complies with all of the requirements of the Practice Statement shall include an explicit and unqualified statement of compliance. We refer to a similar requirement in the German literature, according to which a Management Report includes a *Responsibility Statement* by the legal representatives of an entity to give an assurance that, to the best of their knowledge, the Management Report includes a fair review on the development and performance of the business and the position of the group, together with a description of the material opportunities and risks associated with the expected development of the group.

However, we have some reservations with regard to question 2 (b). First, we think that users of management commentary need information on whether this commentary complies with all or with some of the requirements of the Practice Statement. Therefore, we do not consider the requirement set out in para. 2.6 of the ED ("Management commentary that complies with some, but not all, of the requirements of this [draft] Practice Statement ***may*** include a statement of compliance." emphasis added) as appropriate. In contrast, we believe a report complying with some of the requirements **shall,** in any case, include a qualified statement. Furthermore, the qualified statement should also contain information on which elements of the guidelines have not been complied with. In this (latter) respect, we agree with the IASB's view.

In addition, we take the view that a reporting entity shall indicate the level of adherence to the PS by using clear language. In other words, phrases like "used the PS 1 as basis" or "in orientation to the specifications" should be avoided. We believe the proposed guidance in the ED is not explicit enough in this regard, and, therefore, encourage the IASB to consider a slightly clearer wording.

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

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?

We agree since we note the overall objective of management commentary as worded in the ED is similar to our line of thinking with regard to the Management Report because the IASB's view involves many elements that are addressed in GAS 20 including stewardship. For example, according to para. 3 of GAS 20 the "objective of group management reporting […] is to report on the use of the group's resources by management during the reporting period and to provide information that enables a knowledgeable user to obtain a suitable understanding of the course of business, the position and the expected development of the group, and of the opportunities and risks associated with this development."

Although we agree that creditors and investors shall be deemed the primary users of management commentary, we are aware – and so does the IASB, obviously – that non-financial information is increasingly included in Management Reports, very often due to legal requirements such as Art. 19a and Art. 29a of the Accounting Directive. Against this background, the discussion on the composition of the stakeholder groups which information in Management Reports are addressed to and what perspective to be taken by the reporting entity has gained in intensity, driven further by the CSRD proposal by the European Commission as of 21 April 2021. We note that the IASB in the ED frames the discussion by reference to the sphere of an entity's ability of value creation considering not just what is recorded on the face of the financial statements but also considering further effects that will influence the entity's enterprise value, regardless of being already recognised in financial statements. We strongly support this view. (Please see also our response to question 9 in this respect.)

Furthermore, management commentary should be seen as a separate and self-contained report that complements the financial statements (including the notes), and, therefore, has to be consistent with these financial statements. It shall express group management's assessments and evaluations, and hence be, concluding, prepared on the basis of the management's perspective.

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?

Without going into too much detail at this stage of discussing the proposed requirements in the ED, we agree with the IASB's overall approach to the ED, including the definition of areas of content, the hierarchy of objectives, and the elaboration of key matters based on the objectives. Our reasoning is based on our core understanding of what the revised PS 1 is designed to constitute: A process-oriented guidance intended to serve as a signpost directing an entity's management on the road to the decision on what has to be reported in management commentary. As a result, the requirements proposed appear very abstract as regards their wording. Therefore, the numerous examples in the ED on almost all aspects of the ED seem very helpful, in our opinion. In other words, we do not see evidence to the contrary that the IASB's approach might be capable of providing a suitable and sufficient basis for an entity's management to identify information that investors and creditors need. However, some of the specifics the IASB elaborates in the ED based on its overall approach give rise to concerns as outlined in the succeeding section of this letter.

In addition, we would like to point to the highly tentative character of this aforementioned conclusion, given the early stage of the IASB project. In our opinion, the IASB should consider performing field tests to gain more profound findings in this respect. The same applies to part (b) of question 4: At this point, we cannot faithfully conclude, in an appropriate manner, on the enforceability of the requirements proposed in the ED.

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.

Basically, we agree with the design of the objectives, including the hierarchy underlying these objectives. In comparing the IASB proposals in the ED/2021/3 Disclosure Requirements in IFRS Standards – A Pilot Approach (Proposed Amendments to IFRS 13 and IAS 19), we noted that the Board's proposals on management commentary slightly vary from the Pilot approach. In particular, the Pilot Approach explicitly addresses two hierarchy levels with some elements of the “assessment” level included in the “specific” level, whereas the ED introduces the “assessment” level as a third level, explicitly. We do not consider this as a fatal problem. First, we understand that the objectives of management commentary on the one hand and of the Financial Statements (which the Pilot is designed for as regards disclosure) on the other hand may not be deemed identical. This fact may even justify such variances. Second, both the ED and the Pilot Approach, are in a very early stage of development, and it seems unclear at this point whether the Pilot Approach in its final stage is intended to serve as a conceptual basis for management commentary in addition. Nevertheless, we think the IASB should continue paying due consideration to this issue. This may include exploring whether or not the aforementioned variance is indeed intended or to what extent the PS 1 shall be deemed generally consistent with the Pilot Approach as noted in BC76 of the ED.

While we express our support to the IASB's overall approach in our answer on question 4 (see the preceding section of this letter), we would like to raise some reservations as regards the process that an entity's management has to perform in identifying the information needed to meet the disclosure objectives for the areas of content. This bottom-up process as outlined in para. 4.4 of the ED introduces a high level of complexity by requiring an entity's management to verify on each level of hierarchy whether the disclosures identified in applying the IASB's guidance are actually sufficient to meet the users' information needs. Basically, we agree with the IASB to clearly articulate the relevance of the users' perspective in identifying the information to be reported in management commentary. This is because the content of this report is stronger geared to entity specifics than the entity's financial statements are, and, compared to financial statements, management commentary involves a stronger management focus on the information needs of the entity-specific users. As a result, the level of specification regarding the disclosures to be made in management commentary will have to be lowered, while at the same time, the extent of management's discretion will have to be expanded. We understand the requirement in para. 4.4 to reflect this view in principle. However, the task of identifying the content to be reported by an entity should not be completely shifted from the

standard setter to the entity. Hence, we fail to find support for the process outlined in para. 4.4 of the ED.

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?

In our view, the IASB's deduction and specification of the objectives for the areas of content seem conclusive and logically coherent. However, we have got some reservations with respect to the area of content "resources and relationships". We note the IASB addresses relationships to suppliers as an element of this area of content. This element can well be distinguished from other resources and relationships, and, in addition, it forms a typical issue of intangible resources. Therefore, addressing that element seems appropriate in general. Furthermore, we understand that the area of content "resources and relationships" goes beyond just relationships to suppliers; however, the ED is silent on what elements are further involved, except for the examples proposed. Therefore, the specification of this area of content in the ED, including its dedicated disclosure objective, seems not clear enough, in our opinion.

Furthermore, we note that the ED does not address governance in the same detail as the (other) areas of content. In our view, governance should be considered as an additional area of content. Our line of thinking is based on the observation that governance is a so-called cross-cutting issue being likewise relevant for all other areas of content. In addition, we refer to the German practice where the Governance Statement is an element of reporting contained as a separate section within the Management Report. Therefore, governance should be addressed in PS 1 as a separate area of content, rather than addressing it area-of-content-wise. We further refer to our answer on question 8.

In addition, we note that the area of content "risk" is focused on risk while opportunities are dealt with rather marginally. In our view, risks and opportunities shall be treated in an equal manner. A similar requirement is contained in the GCC as well as in GAS 20. A biased focus on risks only will result in an incomplete depiction of the factors that could affect the entity's ability to create value and generate cash flows in the future. Therefore, we urge the IASB considering this reservation. Furthermore, we note that the notion "risk" is not included in the defined terms section. Although it can be assumed that the meaning of the terms "risk" and "opportunity" are widely known, an explicit definition seems helpful to create clarity in this respect in the context of management commentary. We may point to the definition used in GAS 20 involving potential future developments or events that could lead to a deviation

(negative of positive, for risks and opportunities, respectively) from the group's forecasts or objectives.

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?

We basically agree with the IASB's proposal to link the content of management commentary to issues that are important and to operationalise those issues further by applying the notion of key matters. Furthermore, we support the IASB in defining indicators through which preparers of management commentary can identify the "key characteristic" of a matter. Although the notion "key" is not unknown in the IFRS literature (e.g., key management personnel in IAS 24 Related Party Disclosures), we note that it is rather rarely used and, in those cases, explicitly defined. However, the ED does not contain such a definition, which in our view is necessary.

In addition, we have some concerns with respect to the meaning of the notion "key matters" in its interaction with the assessment of relevance and materiality on information about key matters. We acknowledge the IASB addresses this point by the wording in para. 4.8 of the ED ("*Because key matters are fundamental to the entity's ability to create value and generate cash flows, it is likely that much of the information that is material to investors and creditors will relate to key matters.*"). However, we fail to assess conclusively whether or not the linkage of management commentary's content to key matters is intended to form an upstream condition of the relevance/materiality criterion. In addition, we note that the notions "key matters" and "materiality" are addressed in the ED in a certain sequence indicating that "key characteristic" indeed forms an upstream condition of the relevance/materiality criterion. Also, we do believe that the IASB's statement contained in para. BC78 of the EDs Basis for Conclusions ("*materiality is an attribute of information, not an attribute of matters*") is neither convincing nor helpful in this regard.

In our view, an understanding of a matter's key characteristic as an upstream condition of materiality is neither conceptually sound nor practicable. Adding the 'key' feature as another condition in this context may result in relevant and material information not being disclosed in

management commentary, just because the information relates to a matter that is not considered 'key'. Therefore, we urge the IASB to explicitly advice in the revised PS 1 that the key matters notion is not meant to add a condition to be considered prior to materiality considerations. Such advice should be much clearer than the current wording in para. 4.8 of the ED.

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?

We support the IASB's intention – as expressed in the ED – to take greater account of the increased need of investors and creditors for forward-looking information, information on intangible resources, and ESG matters, through the revision of PS 1. However, we have the impression that these questions should be given more emphasis in the ED from a conceptual point of view. We acknowledge the ED contains three dedicated tables presenting numerous examples for information that might be provided in this context. We believe preparers will find these very helpful. Nevertheless, the conceptual basis following the headline "*Information about long-term prospects, intangible resources and relationships and ESG matters*" and involving the two paras. 4.16 and 4.17 of the ED seems far too short in our view. Furthermore, we note the IASB, firstly, has located this section of the ED within the chapter B "Areas of content" but separately from the actual areas of content, and, secondly, has addressed the issues repeatedly in almost all other sections of the ED, but to varying degrees in depth and granularity. Therefore, we fail to recognise the IASB's approach of considering and embedding the issue of information about long-term prospects etc. in PS 1 from a conceptual perspective.

In our view, the IASB should better structure these issues and address them in a much more focused and conceptually sound manner.

We further note the ED repeatedly contains the requirement for forward-looking information in management commentary to involve "*all time horizons including in the long term*". The IASB further elaborates on this by referring to "short, medium or long term". However, there is immanent diversity in practice on the meaning of how short-, medium-, and long-term periods (in years or months). In other words, different entities assume different time ranges to these time horizons as this definition is entity specific. In order to be useful for creditors and investors, forward-looking information should be accompanied by a disclosure of the time span in years or months assigned to the time horizons considered in management commentary. Therefore, we believe the IASB should consider such a requirement but without prescribing fixed time ranges for these time horizons.

Also, in discussing this section of the ED, we repeatedly note the issue "governance" not being addressed in the ED. Although we acknowledge the IASB is right in observing that "*governance is typically regulated by local laws, which may also require entities to provide specified information about governance*" (para. B12 of the ED), we do not think this reasoning justifies excluding governance from the guidance in PS 1. Firstly, there are many other financial reporting issues that are typically regulated by national laws, for example, the presentation of financial statements or revenue recognition. However, this fact does not form an obstacle for the IASB to develop standards on such topics as IAS 1 or IFRS 15. In contrast, IFRS Standards aim at a globally accepted and applied basis for financial reporting, thus, minimising effects from diversity in financial reporting due to differing national reporting requirements. For the same reason, the IASB might strive for a minimum harmonisation of management reporting as regards governance since the national laws quoted by IASB are varying across the world in the same manner. One could argue the specifics of management commentary do not allow an analogy to be drawn; however, there is no such discussion in the ED.

Secondly, based on the overall objective of management commentary, the IASB concludes in para. 3.3 of the ED that "*information in management commentary influences investors and creditors' decisions by influencing their assessments of* [amongst others] *management's stewardship of the entity's resources—how efficiently and effectively management has used and protected the entity's resources.*" In our view, reporting on management's stewardship of the entity's resources will not be complete without reporting on governance. In addition, empirical evidence indicates that disclosures on governance matters are deemed relevant by investors, in particular, if disclosures on specific institutionalised measures (such as Compliance-Management-Systems) are involved. Against the background of these observations, the IASB's tentative decision not to address governance in the ED in an equal manner as other relevant topics does not appear consistent.

Another argument in favour of including guidance on governance reporting in PS 1 might be that the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) contain corresponding disclosures. Since the TCFD guidelines are an essential basis of the IFRS Foundation's preparatory work for a standard prototype on climate reporting, we expect that governance topics will be taken up in this context by the International Sustainability Standards Board (ISSB). We further refer to our comments on question 9 in the succeeding section of this letter.

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?

In our view, the most prevalent issue in this respect is the level of compatibility of management commentary and the sustainability reporting addressed by the ISSB in the near future. In other words, may management commentary continue to be seen as the best location for the reporting according to the ISSB Standards from a conceptual view in light of the discussion on the European Commission's CSRD proposal?

As we understand, the IASB's concept on the set of information contained predominantly in the management commentary can be framed by what is called the sphere of enterprise value as described in the paper "*Reporting on enterprise value, illustrated with a prototype climate-related financial disclosure standard*" facilitated by the Impact Management Project, World Economic Forum and Deloitte in December 2020. The authors of this paper introduce the concept of Dynamic and nested materiality and note in this context that reporting on enterprise value typically addresses a narrower range of sustainability matters that are considered sufficiently likely to influence enterprise value. With this concept in mind, the information contained in management commentary according to the IASBs approach goes beyond (but does not exclude) elaborating on items that have or already had an effect on monetary amounts recognised in the financial statements (also referred to as the first layer). More precisely, management commentary would include impacts (inside-out-effects) resulting from an entity's business activities on the entity's environment (in a broader sense) as long as these impacts already had or have or will have a repercussive effect (outside-in-effects) on the reporting entity measurable in monetary terms (also referred to as the second layer). The aforementioned paper further introduces as the third layer the reporting on all significant impacts resulting from an entity's business activities on its environment, regardless of these impacts being expected to feed back to the entity. In other words, the impacts of this layer may or may not have a repercussive effect on the reporting entity and reporting on the latter is – according to the IASBs discussion (see in para. 3.13 of the ED as an example) – not the primary objective of the management commentary.

In our opinion, the content of sustainability reporting is far from being considered harmonised, yet, in particular, with respect to the layers defined relevant for identifying the information to be disclosed by entities. For example, the Global Reporting Initiative (GRI) is currently running a project on the revision of GRI 101 *Foundation* and other GRI Standards. According to the Exposure draft on the GRI Universal Standards: GRI 101, GRI 102, and GRI 103 the Global Sustainability Standards Board proposes for an item to be reported to refer to the impact feature primarily (see line 118 to 171). In other words, sustainability reporting according to GRI Standards aims at providing information about material inside-out effects and, therefore, is framed by the third layer described above. In contrast, we understand other concepts

addressing sustainability reporting, such as the Climate Disclosure Standards Board Framework, and the Recommendations of the Task force on Climate-related Financial Disclosures (TCFD), to refer to the second layer primarily, i.e., they focus on the sphere of enterprise value. This understanding is described by these organisations as follows: "*Better disclosure of the financial impacts of climate-related risks and opportunities on an organization is a key goal of the Task Force's work. In order to make more informed financial decisions, investors, lenders, and insurance underwriters need to understand how climate-related risks and opportunities are likely to impact an organization's future financial position[…]*" (TCFD 2017, p. 8), and, "*Organisations should focus on reporting those activities and outputs that are likely to cause changes to the balance, stock, flow, availability and quality of natural capital for the organisation itself and for others and/or where the impacts from those activities and outputs (in so far as the organisation can reasonably be expected to observe or anticipate them) are likely to affect the organisation's ability to operate its business model and execute its strategy.*" (CDSB Framework, p. 8).

In this context, the European Commission's proposals for its draft CSRD as of April 2021 contain clarifications on the concept of double materiality as a main principle for the content of the sustainability reporting that is proposed to form a part of a Management Report from 2023: According to the draft Article 19a of the Accounting Directive the "*management report* [shall contain] *information necessary to understand the undertaking's impacts on sustainability matters, and information necessary to understand how sustainability matters affect the undertaking's development, performance and position.*" In other words, entities will be required "*to report both on how various sustainability matters affect the undertaking, and on the impacts of the activities of the undertaking on people and the environment.*" (Recital 25). This gives rise to the conclusion that the Commission suggests the third layer to be relevant for what has to be disclosed in the Management Report.

However, there is an ongoing debate on whether the third layer exists at all. The arguments exchanged include whether every entity-made inside-out-effect will ultimately respond to the entity (as its originator) and whether expectation, recognition, and measurement might only be a matter of time horizon and/or materiality. We refrain from further reproduction of the discussion at this point but would like to narrow the debate down to the essential observation and question: Against the background of impact-related reporting and considering a long-term time horizon, are there inside-out effects that are not relevant or material for investors, and, if yes, to what extent?

From our point of view, it is even less certain which view the ISSB will adopt on the matters described in the preceding paragraphs, and in particular, what its position will be on the question raised in the preceding paragraph. We note that the Technical Readiness Working Group (TRWG) of the IFRS Foundation considers the second layer (enterprise value sphere) to be relevant for sustainability reporting (para IN3 of the *General Requirements for Disclosure of Sustainability-related Financial Information Prototype* issued by the TRWG on 4 November 2021). Notwithstanding this, and, from a merely technical point of view, we feel obliged to advise the IASB to put on hold the project on the revision of PS 1 until there is sufficient clarity on the approach to be taken by the ISSB itself and on the ultimate location of the information to be provided under the standards issued by that Board. We think that sufficient clarity might be available once the first Exposure drafts on these standards are issued in early 2022 for public consultation.

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?

We agree with the clarifications in the ED concerning materiality judgments to be taken by an entity's management in identifying the information to be provided in management commentary. In particular, we think the reference to the IASBs discussions in the Conceptual Framework and the IFRS Practice Statement 2" as a conceptual basis for this part of PS 1 will be helpful for preparers.

However, we think the IASB should keep in mind consistency in terms of terminology and definitions. In this regard, we would have expected in the ED a discussion on relevance prior to elaborating on materiality since relevance is understood as a feature superior to materiality. In our view, the relevance feature might be seen even more or at least equally important as for financial statements since an entity's management has to assess what information might influence investors' and creditors' decisions to a greater extent for purposes of management commentary than for purposes of financial statements, even if relevance and materiality assessments are often combined with those for financial statements. Our reasoning for that view is based on several discussions the IASB takes in the ED, including the definition of the IASB's aim to provide sufficient flexibility – for management commentary to focus on matters that are fundamental to the entity's ability to create value and generate cash flow, and on our understanding regarding the intended overall character of the PS 1, i.e., to serve as a signpost directing an entity's management on the road to the decision on what has to be reported on the face of management commentary.

Furthermore, we note the IASB assumes that an entity's management considers whether information provided in other entity's management would be material in the context of the entity's management commentary (para 12.5 of the ED). Although we concede this kind of peer-comparison is quite common in practice and helpful for preparers, we have concerns on the wording of this paragraph. According to the ED, the IASB strives for the PS 1 to be adopted by legislators or regulators, for example, in jurisdictions with no such guidance. However, the tone of the paragraph suggests a requirement for an entity's management to perform a peer review with regard to information provided in the peers' management commentary. We oppose such a requirement as it puts an undue burden on the entities in jurisdictions that have adopted the PS 1.

Lastly, we would like to refer to our concerns with respect to the nature of the notion of key matters as expressed in our answer on question 7.

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?

In our opinion, the characteristics addressed in chapter 13 of the ED are appropriate in terms of their substance. Furthermore, we support the IASB in referring to qualitative characteristics of information provided in financial statements as set out in the Conceptual Framework. However, we have some concerns with respect to the terminology the IASB applies for the ED in comparison to the Conceptual Framework, for example, "*clarity and conciseness*" vs. "*understandability*". We acknowledge the IASB's reasoning for these variances, including the observation noted in paragraph BC98 of the ED's Basis for Conclusion (other or larger group of individuals involved in preparing management commentary, information in such reports is broader than information in financial statements). In addition, we think the table in BC102 explaining these differences might be helpful for preparers. Nevertheless, we believe that any variance in terminology and a definition's wording could give rise to considering those variances as variances in meaning, which does not seem to be intended by the IASB. Therefore, we strongly prefer taking the opposite approach, i.e., sticking to the terminology used in the Conceptual Framework and explaining their (specific) meaning to management commentary in more detail, first, to provide a better understanding for individuals who may not be familiar with IFRS Standards and the Conceptual Framework, and, second, to consider the specifics of management commentary.

Apart from this, we support defining "coherence" as an additional characteristic of management commentary due to this report's nature. This is, furthermore, in line with the requirement set out in GAS 20 according to which the consolidated financial statements and the group Management Report shall be consistent.

We further agree to the IASB's guidance on cross-references addressed in chapter 13 of the ED, in particular its reservation on including extensive information by cross-reference. In line with the IASB we think management commentary should be seen as a separate and self-contained report that should not be fragmented by cross-references.

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?

The qualitative characteristics set out in the ED for metrics are widely appropriate in our view. In particular, we strongly support the broad scope the IASB defines for the notion "metrics" in para 14.1 of the ED. Our reasoning is based on the discussion around the IASB project Primary Financial Statements that revealed the widely shared concern on the too narrow scope of the term "key performance indicator".

In contrast, we do not agree with the IASB's views set out in para 14.10 of the ED with regard to the qualitative characteristic "comparability" related to metrics reported by other entities. The IASB proposes to require the management of an entity to describe the differences between the method the entity uses to calculate the metric, or the name management uses to label the metric and a different but commonly used method or name used by other entities. We concede such information might be helpful for users. However, it seems neither practicable nor conceptually appropriate to define a requirement in this respect. First, a requirement of this kind might force an entity's management to monitor both the terminology and methods used for metrics by other entities regularly. In our view, such regular monitoring with a view to label and calculate metrics in the same way other entities do seems impossible in most cases, but at least it places an undue burden to the management because of a wide variety of business models that may exist even within a given sector. This would be made more difficult by the fact that comparable entities are not subject to the same reporting standards as the reporting entity. Second, although we concede, a commonly used name for a single metric and a commonly used method for determining the metric ("commonly used name and method" are defined as a condition for this requirement) might be considered as indicating a consistent practice in this respect but cannot be regarded as consistent practice. This holds true for metrics that are not derived from information disclosed in the entity's financial statements, particularly as there is no defined target in place (like a standard) on which explanations on differences may be based. Third, we do not believe the requirement under discussion would accord to the principle of management's view, as it introduces another condition to this principle. The condition is that management may only present its own metrics without additional explanations if a sufficient number of other companies state the same metric and calculate it using the same methods. Introducing this condition does not seem appropriate in our view. Last but not least, the notion "commonly used" seems hardly feasible to operationalise as a relevant condition for a requirement in general. We acknowledge, by introducing the notion "commonly used" the IASB intends to link the requirement to a certain practice that should be seen as widely accepted. However, for a certain practice to be considered widely accepted or "commonly used" a high degree of judgment is needed as there is no common understanding of what "commonly used" in fact means, e.g., what is the proportion of entities determining and naming a particular metric in the same way, and what size does the population need to have? Against the background of our aforementioned reservations, we think the IASB should include in PS 1 a recommendation or advice rather than a requirement in this respect.

We support the qualitative characteristics as well as the reporting requirements described in the ED for 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?

We agree with the examples proposed by the IASB and believe these will help an entity's management identify material information that management commentary might need to provide to meet the disclosure objectives. However, we strongly recommend the IASB to address the issues of governance and opportunities (as part of the risk and opportunities area of content) as outlined and reasoned in our comments on question 6. The content and structure of chapter 15 should then be aligned accordingly.

In addition, we think the IASB should consider rewording the headline of chapter 15 as well as the headline following para. 15.2 in order to stronger indicate the non-binding and advisory nature of the examples.

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?

From our perspective, the effective date as proposed in the ED seems appropriate for jurisdictions as Germany that do not require entities to comply with PS 1 in preparing Management Reports. However, given there might be jurisdictions in which adherence to PS 1 is or will be required, a certain transition period might be considered.

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?

We refer to the second part of our answer on question 4.

Question 16—Other comments

Do you have any other comments on the proposals set out in the Exposure Draft?

We do not have further comments.