Date

19 April 2006

Le Président

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Sir David Tweedie
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Dear Sir David,

Re: IASB Discussion Paper on Management Commentary

1. FEE (Fédération des Experts Comptables Européens, European Federation of Accountants) is pleased to submit its comments on IASB Discussion Paper on Management Commentary. FEE as a founding organisation of EFRAG has also contributed to the EFRAG consultation process by submitting our views on their preliminary comments. We refer to the EFRAG preliminary comments (draft letter of 10 January 2006) where we are in agreement with their comments; where we are in disagreement our own views are put forward. However, we have not considered the final EFRAG submission to IASB in our own response.

2. We welcome the publication of the Discussion Paper on Management Commentary. It will be a very useful guidance for the preparation of such reports. We agree that Management Commentary is an important part of financial reports. The Discussion Paper provides a good analysis of the differences between existing requirements, and it could be a useful means of harmonizing practices in and outside of Europe.

3. Notwithstanding our answers to the questions raised we, like EFRAG, broadly agree with the objectives and principles and the qualitative characteristics developed in the Discussion Paper.

4. We prefer the issuance of an optional standard that would be available for use by entities or by national jurisdictions. It is not realistic to issue a mandatory standard in the short-term. We would prefer the conclusion of IASB to provide for optional adoption by jurisdictions or entities, in the short term at least, given the various systems of corporate governance and the responsibilities to prepare and review financial statements by reporting entities as well as the related audit implications.

5. Similarly, we see it as essential that Management Commentary remains outside of the scope of compliance with IFRSs. A separate compliance statement for Management Commentary would permit separate assurance on it, perhaps at a different level from the financial statements. Currently the responsibility of auditors towards the annual (directors') report is very different from country to country ranging from a consistency check to full audit requirement. Usually, the assurance on Management Commentary is of a different type than that of financial statements because the information is more qualitative and subjective in nature and may encompass elements that are not objectively verifiable. An auditor can assess the consistency of Management Commentary with the financial statements but will have more difficulty in applying the true and fair concept on it.

6. We agree with the view in the Discussion Paper that the preparation costs may be low because management already has the information and processes in place to prepare the Management

Commentary. However, compliance costs may be high if Management Commentary were required by a mandatory standard. Compliance costs could include lawyers fees, and other legal and liability costs, publication costs and audit fees. We support the concern expressed in paragraph 207 that increasing compliance costs and the burden of complying with a Management Commentary standard may discourage entities from adopting IFRSs.

7. We have some observations on what should be the content of Management Commentary. We agree with EFRAG's draft comment that the text of Appendix A could be less prescriptive, by suggesting examples instead of requiring elements for disclosure. The difference between grey and black paragraphs is not obvious. Moreover, the standard should stay at the principle level and so permit entities to include in Management Commentary information required by local legislation.

8. We have the following comments on the answers to the questions raised in the Discussion Paper.

Requirements for MC

The project team concluded that an entity's financial report should be viewed as a package comprising the primary financial statements, accompanying notes and MC (section 1). They also concluded that the quality of MC was likely to be enhanced if the IASB issued requirements relating to MC (section 6).

Question 1: Do you agree that MC should be considered as an integral part of financial reports? If not, why not?

We agree with EFRAG's draft comment that Management Commentary is an integral part of financial reports but clearly distinct from the financial statements. Under EU legislation the annual (director's) report is already part of the financial reports of companies. Financial statements should be understandable on their own for accounting purposes without a Management Commentary. We believe Management Commentary is not part of the financial statements. Making Management Commentary an integral part of financial statements would have severe consequences for the audit.

The principles included in the Framework such as qualitative characteristics and user identification would equally apply to selecting information for the Management Commentary. However we see no need to extend the Framework as suggested by EFRAG.

We suggest that IASB also addresses in the project the link between Management Commentary and other information communicated by management (in a press release, prospectus, etc.), and more in particular the consistency between the various types of financial information.

Question 2: Should the development of requirements for MC be a priority for the IASB? If not, why not? If yes, what form should any requirements take?

Considering that finalisation of the project would not take that much IASB Board and staff time we are of the opinion that it would be useful to finalise the guidance as it is a promising area for improving financial reporting. However if it takes substantial resources there should be further discussion of the priority the IASB should give to the project, there are clearly other projects that would rank higher in priority from a European perspective, notably the revision of the Framework and the development of accounting standards for SMEs.

Question 3: Should entities be required to include MC in their financial report in order to assert compliance with IFRSs? Please explain why or why not.

Although we would support a voluntary standard, similar to IAS 34, we would not support a mandatory standard.

We would prefer that an entity be required to provide a separate compliance assertion on the Management Commentary rather than to include Management Commentary in their compliance assertion on the IFRS financial statements.

We support optional adoption by national jurisdictions or entities of a voluntary Management Commentary statement or standard. Paragraph 221 is in line with our views; if an entity elects to prepare Management Commentary and complies with the statement or standard it would be required to assert compliance with it in a separate compliance assertion.

IASB could also address how Management Commentary could be prepared for interim financial statements. A condensed version could be used if the entity applies IAS 34. This would in particular be helpful for Europe where under the Transparency Directive this type of information is required to be disclosed from 2007 onwards.

Purpose of MC

The project team concluded that, rather than having one dominant objective, MC has three principal objectives (section 2). The project team also concluded that the primary focus of MC is to meet the information requirements of investors.

Question 4: Do you agree with the objectives suggested by the project team or, if not, how should they be changed? Is the focus on investors appropriate?

We agree with the objectives in paragraph 34. We consider the term "the most important issues facing the entity" vague. Instead of just referring to issues, it could be enhanced by addressing strengths, weaknesses, opportunities and risks within the entity's operational environment.

Although we believe that ideally financial reports should address the information needs of all users, we acknowledge that the primary focus of Management Commentary would be the investors. If the objective of Management Commentary were broader, there is a risk that the amount of information disclosed would be excessive. There are other types of reporting which meet the needs of users other than investors. Management Commentary should not replace other forms of reporting, and we therefore, agree with the assertion that if the needs of investors are satisfied, most of the needs of other users are also satisfied. We thus support EFRAG's draft comment.

Management Commentary can include information that may affect the financial position of a company, without replacing other forms of reporting. It is preferable that an international standard does not deal in detail with corporate governance because this depends on the legislative framework of jurisdictions and any material addressing corporate governance should only be at principle level. Regarding environmental and social responsibility issues, given their potential significance, we believe that if they are not addressed in the Management Commentary, there could be an encouragement for an explanation of why they are not deemed relevant. The Discussion Paper does not sufficiently address CSR or sustainability matters eventhough such issues under the EU Modernisation Directive are to be included in the annual report.

Principles, qualitative characteristics and content of MC

The project team concluded that it is not appropriate to specify the precise information that must be disclosed within MC, or how it is presented. Rather, they believe that any requirements for MC should set out the principles and qualitative characteristics, as well as the essential areas of MC, necessary to make the information useful to investors. It is up to management to determine what information is required to meet these requirements, and to determine how the information is presented. The project team has also suggested that it is appropriate consider ways to limit the amount of information management is allowed to disclose, as a way of

ensuring that it is the most important information which is presented to investors. (See sections 3 and 4)

Question 5: Do you agree with the principles and qualitative characteristics that the project team believes are essential in the preparation of MC? If not, what additional principles or characteristics are required, or which ones suggested by the project team would you change?

We broadly agree with the characteristics developed. However, we are not convinced of the need to invent new characteristics (such as supportability and balance) instead of using the existing Framework terms. The characteristics should also mention the balance between forward-looking information and past information.

It needs an absolute requirement that Management Commentary should be consistent with the financial statements. Auditors need to check as a minimum this consistency. It is essential that the financial information in Management Commentary be clearly linked to the financial statements. Although consistency is mentioned in paragraph 44 and A13, it should be highlighted more clearly.

Whilst Management Commentary should be consistent with financial statements, it should not duplicate information that is already in the financial statements. It should be possible to refer to the notes. However, the financial statements should not refer to Management Commentary for disclosure of information because they should be understandable on their own without reference to the Management Commentary.

Question 6: The DP outlines the essential content areas that MC should cover. Do you agree with these? If not, what additional areas would you recommend or which ones suggested by the project team would you change?

We support EFRAG's draft comment that it should be clarified that paragraph 100 is not a comprehensive list. Companies should be allowed to include other information if relevant or required by legislation.

We suggest Management Commentary include an assertion on who is responsible to prepare and approve, if applicable, this report.

The entity's objectives and strategies may constitute useful information for investors for their assessment of the entity's development. We suggest the Board clearly state that management should focus on the key elements of the entity's strategy and the main objectives that have been decided by the responsible bodies, as well as any important changes therein.

We also support EFRAG's comments that paragraph 100c) should include more information about on risk management. The text should put more emphasis on the management discussion on risks relevant to the business by expanding paragraph A41. We refer you to the FEE Discussion Paper on Risk Management and Internal Control in the EU of March 2005. Types of risks are distinguished between those relating to financial reporting objectives, those relating to compliance with laws and regulations and those relating to operations and strategy.

The FEE Discussion paper states that, in improving risk management and internal control, companies should follow an evolutionary approach to the management, disclosure and conclusions on risk management and internal control. Within this evolutionary approach, we broadly support disclosure by companies of their overall process of risk management including internal control over financial reporting, although in this respect there are a number of issues to be addressed. Whilst there are some requirements in financial reporting standards (for example IFRS 7) to disclose how specific financial risks are managed, the extension of disclosures related to the management of specific risks raise major concern, related to the commercial sensitivity and potential liability and reputational damage for directors.

We welcome that some examples of CSR information are included in the appendices. For example A40 refers to reputation and E15 to social strategy, training and education. We are of the opinion that further examples of CSR would be helpful. There is an indirect financial impact through reputation risk. The examples provided as non-financial information are not sufficiently specific to CSR.

Question 7: Do you think it is appropriate to provide guidance or requirements to limit the amount of information disclosed within MC, or at least ensure that the most important information is highlighted? If not, why not? If yes, how would you suggest this is best achieved?

We support EFRAG's draft response stating that Management Commentary should focus on issues relevant to investors and should be balanced. Furthermore, we believe it is not appropriate to limit the information disclosed within Management Commentary. The standard should stay at principle level, stressing the qualitative characteristics, the principles and the requirements to allow sufficient management discretion as to determine the contents in the specific context of the entity. We appreciate that the requirements should be sufficient to enable the auditor to assess if the respective requirements are fulfilled in jurisdictions where Management Commentary is subject to audit. Furthermore, management should be allowed to include in the Management Commentary additional information required to be disclosed by national legislation.

Question 8: Does your jurisdiction already have requirements for some entities to provide MC? If yes, are your local requirements consistent with the model the project team has set out? If they are not consistent, what would the major areas of conflict or difference be?

Although the Fourth and Seventh Directives do not seem to be in contradiction with the proposed Management Commentary Standard from the IASB, we disagree with EFRAG's draft comment that the annual report is very similar to the proposed Management Commentary. The Directives are very general and do not prescribe the contents of the report the way IASB proposes it. Also the Directives require discussion of specific issues even if not material (for example information on environmental and employee's responsibilities) whereas the proposed standard focuses on relevant issues. As illustrated in Appendix B, the transposition of the Directives into national legislation may create differences between EU countries (see Germany and the UK).

Placement principles

The project team concluded that it would be helpful to establish principles to guide the IASB in determining whether information it requires entities to disclose within financial reports should be placed in MC, on the face of the primary financial statements or in the notes to the financial statements. The project team has suggested some principles (section 5).

Question 9: Are the placement principles suggested by the project team helpful and, if applied, are they likely to lead to more consistent and appropriate placement of information within financial reports? If not, what is a more appropriate model?

The placement criteria are more useful as guidance to the Board than to preparers, not just related to Management Commentary but to all disclosures. IASB should develop general criteria for the whole scope of financial reports. They should work to develop high quality criteria, at principle-based level. Placement criteria are helpful to differentiate whether the information is related to the financial position or not. However, it is too simple to summarise in two criteria the placement of information which is also a matter of judgment. The placement of information in Management Commentary could be by deduction: anything that is not captured by a disclosure requirement in IFRSs should go into the Management Commentary.

We would be pleased to discuss any aspect of this letter with you.

Yours sincerely,

David Devlin
President