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February 28, 2010

International Accounting Standards Board
30 Cannon Street, London EC4M 6XH, United Kingdom

RE: IASB Exposure Draft ED/2009/6 *Management Commentary*

To Whom it May Concern:

The World Intellectual Capital Initiative (“WICI”) respectfully submits the following written comments on the June 2009 International Accounting Standards Board (“IASB”) Exposure Draft (“ED”) on Management Commentary (“MC”). WICI is a private/public sector collaboration aimed at improving corporate information - with a focus on non/extra financial information - for more effective decision making and capital allocation from a value creation perspective.

WICI believes that the development of a common framework for business reporting with the objective of effectively encouraging communication and sharing of appropriate information between companies and stakeholders would significantly enhance the relevance and transparency of the existing financial reporting model. In moving toward this goal, WICI hopes that IASB will consider facilitating a dialogue among a wide range of stakeholders on the broader reporting package, taking into account the fact that the range of information dealt with by MC has a far wider scope than that in the present financial information based system (including, for example, industry-specific KPIs, intangibles, intellectual capital and sustainability reporting, governance and risk-related disclosure).

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The following comments are presented in the context of selected related questions set out in the discussion paper.

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

Given the nature of the content of MC related disclosures, which will likely vary significantly by company, industry and geography, it would be difficult and perhaps counterproductive to establish a rigidly binding standard on its contents. Accordingly, we agree that a guidance document for the preparation and presentation of Management Commentary would be a useful first step in the right direction.

However, WICI perceives a risk related to the status of the document: the nature of the document (being only guidance, a non binding document) may induce in fact limited implementation (Management Commentaries developed only by the "best-in-class" companies).

In addition, WICI would like to suggest IASB to include some review process and procedures to step up to more solid status in order to raise the status of MC in the future. This process will also contribute to improve the quality of the information and make MC more diffuse, through reviewing 1) whether actual MC disclosed is relevant to decision-making, 2) whether MC is compatible with, supplementary to and complementary to financial information, and making available the result of this review.

If this process is too burdensome, it could be done by some external organizations commissioned by IASB, which have a specific know-how on reporting of non-financial information.

Furthermore, it is recommended that IASB would encourage each country's government to establish either guidelines or regulation based on its guidance.

Moreover, Management Commentary disclosure should be evaluated in cooperation with appropriate regional bodies on whether it satisfies the principles and content elements of the voluntary guidance that IASB proposes to issue.

A final point relates to the need that information disclosed is not misleading and is subject to a certain level of assurance (by undergoing an audit process). In consideration of sections 6 and 7, it is unclear whether the management commentary should be audited or not and how the criteria mentioned in section 20 (i.e. relevance, faithful representation, comparability, verifiability, and materiality) are to be assessed.

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

We found the paragraphs 24-39 well designed and relevant on most aspects addressed. We particularly appreciate the 24 (c) on "the entity's most significant resources, risks and relationships", which could be the starting point for Management Commentary about Intangibles/Intellectual Assets. Paragraph 20 is useful as well, putting to the fore MC characteristics such as relevance, faithful representation, comparability, materiality, verifiability. Materiality is of course the key element to us and should be even more stressed.

If there is one element missing in the overall discussion about MC that we could suggest, it is the reference to shareholder value and more generally to stakeholder value. The MC is the most natural and legitimate reporting space to discuss how the architecture for shareholder/stakeholder sustainable value creation is designed. Since the users of financial statements are strictly connected to the capital providers, it should only be obvious that the MC tackles here the complex issue of how they plan to create value for their shareholders, while keeping due respect and fairness to creditors, employees, clients, suppliers, communities and the likes. A well articulated description of the shareholder/stakeholder value creation process can offer great disclosure opportunities about: how the company positions itself within its own value chain; what are the key business drivers that it sees critical in this process; how the company manages those key business drivers and how those drivers have evolved over time through some kind of quantitative or qualitative measurement. For instance, an invitation to discuss how management encourages and leverages the innovation capability of the company to strengthen competitive advantages could be a very decision-useful information. These discussions tend to lead to a consideration of various intangibles (cf. sections 27 through to 39, with an emphasis on sections 29 and 32 in particular).

Talking about "Resources, Risks and Relationships", it should be stressed that intangibles and ESG (Environmental, Social, Governance) issues should be addressed in the same MC, as both fall under the extra-financial umbrella and both ESG & intellectual capital[1] are

[1] Intellectual Capital (IC) can be defined as the internal (competencies, skills, leadership, internal procedures and routines, know-how, research capacities, organizational capabilities, etc.) and external (image, reputation, brands, alliances, customer relationships and satisfaction, etc.) stock of intangibles recognized by and "available" to an

interlinked and to some extent overlapping. The IASB document should be used as a platform to voice the vision of an informational relevant and effective convergence between IC and ESG. Unfortunately, intangibles are currently only quoted in a note on page 20 of the ED.

Further, we recommend that IASB moves further toward the establishment of a common, broader framework for business reporting in cooperation with other organizations that have already or are working on publishing open standard frameworks for business reporting.

In particular, we believe the suggested content elements by IASB are appropriate and are consistent with the high-level elements of the WICI framework. WICI also recommends that IASB continues efforts to encourage more companies to disclose these elements using quantitative financial and non-financial information (e.g. Key Performance Indicators or "KPIs"), and including definitions and calculation formulas where appropriate, to foster the persuasiveness of accompanying narrative descriptions.

In order to raise the reliability of the description, we suggest adopting what can be termed as a "sequential explanatory approach". The description of each element with an explanation of the relationship or logical combination with the others may have different meaning when it refers to forward-looking aspects or past issues. Therefore, WICI recommends that IASB would also encourage companies to explain both aspects (from the past to present and from the present to the future) by referring to each element in the MC. This would result in 1) a self-evaluation by a company in the current year of what was described in the previous year as the future prospect; 2) an improvement in the accountability and soundness of the explanation, and 3) making it easier for users of the information to understand it. For example, WICI business reporting framework proposes to use this approach for explaining company's business activities from past to the present and from present to the future.

Another issue is how, as far as possible, to improve the comparability of management commentary disclosures. The use of XBRL format would help on this issue, by raising the capability of users to compare not only disclosed elements of information, but also the context around that information, including the underlying definition, calculation where appropriate, and other relevant contextual information. A common framework for MC

organization, which can be transformed by the entity into a corporate performance affecting sustainable stakeholder's value through the pursuit of sustainable competitive advantages. Intangibles become IC only when they are durably and effectively internalized and/or appropriated by an organization.

disclosures would enable the development of a corresponding XBRL taxonomy, which would in turn enable enhanced transparency and comparability of MC disclosures.

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

It is clearly stated that this is essentially a Framework of Guidance, and as such it should not be seen as an IFRS. Being the IASB document presented as an option, and then WICI recommends not to be far too specific or exact on what companies could/should elaborate on, since many may balk at starting any new endeavors if it looks like a big and complex investment that is not required to comply with IFRS. Indeed, the presentation of <u>detailed</u> examples may <u>not</u> be advisable as they could bias the content of company disclosures related to strategy, plans, and value creation potential.

Nonetheless, since the philosophy of the ED is to let companies choose their objectives and KPIs according to their own circumstances, some broad and general domains should be at the very least suggested for comments like: "How does the company generate and anticipate demand?", "How does the company rapidly and efficiently align supply with demand?", "What factors can explain the divergence between one's performances and the performances of one's competitors?".

In particular, hinting at some examples of possible disclosures about specific intangibles could provide momentum for some to follow suit as they can feel it making sense for themselves without the need to unleash their imagination about what to do.

Therefore, the IASB document is certainly general, but it also risks being too generic. A clear indication that Intangibles/Intellectual Assets as well as ESG aspects are relevant to value creation processes should be pointed out therein.

Furthermore, it might be helpful to launch some pilot studies in order to invite more companies to create illustrative management commentary disclosures. WICI recommends that in this initial phase of the above proposed exercise, IASB would lead by organizing a group consisting of various stakeholders, including companies (on a voluntary basis, representing various industries and business scale), standards setters/regulators, investors/analysts, accountants, academics, etc., to discuss practical implementation issues, taking into account the possibility of electronic linking of data, for example through the use of XBRL.

We also would like to provide more specific comments on the ED.

- Section 26: nature of the business. Reference to the innovativeness character of the environment in which the organization operates may be useful to depict the nature of the business and how the organization positions itself. This could be added in point c) (for general understanding of the context) and in point d) in terms of company's strategy on innovation (both product/service innovation and organizational innovation).

- Section 29: although it is clearly mentioned that this document does not aim to produce illustrative examples and application guidance, introducing only the distinction between financial and non-financial resources may not provide enough indication on what to disclose/comment. It may be useful to introduce basic categories of non-financial resources (Human Capital, Structural Capital/Organizational Capital and Relational Capital or broad categories such as individual resources, organizational resources, market-oriented resources, etc.). This would also be consistent with the level of detail provided in article 31 about risks, where several types of risks (financial, commercial, and strategic) are mentioned. Resources, as defined in section 29, seem to restrict Management Commentary to "stocks" (static aspects) and to neglect dynamic aspects. Introducing the concept of capabilities or at least mentioning the activities that sustain the ongoing development of resources may broaden the scope.

- Section 31: risks should not only be described, but the way the principal risks are faced should be elaborated (e.g. risk analysis, assessment, treatment, etc.). In a similar way, if opportunities are mentioned, how they are to be addressed should be delineated.

- Section 32: there is a strong emphasis on the "customers" to the detriment of other stakeholders and more specifically, partnerships, agreements, alliances or any other stakeholder that may significantly affect the future performance (in either ways) of the organization.

- Section 37: reference to industry-specific KPIs that may support comparability purposes. Also an "inverted pyramid" approach should be suggested (a reduced number of general and common KPIs, and a more expanded number of sector specific KPIs).

- There is no reference at all to IT "resources", which are increasingly critical in many sectors.

Presentation of detailed examples may not be advisable as they could bias the content of company disclosures related to strategy, plans, and value creation potential.

A further risk is the lack of more detailed guidance with some examples: the document is certainly general, but it also risks being too generic. A clear indication that Intangibles/Intellectual Assets as well as ESG aspects relevant to value creation processes should be required.

On the other hand, it might be helpful to launch some pilot studies in order to invite more companies to create illustrative management commentary disclosures. WICI recommends that in the initial phase of the study, IASB would lead by organizing a group consisting of various stakeholders including; companies (voluntary basis, various industries and business scale), standards setters/regulators, investors/analysts, accountants, academia, etc., to discuss practical implementation issues, taking into account the possibility of electronic linking of data, for example through the use of XBRL.

In conclusion, we applaud the efforts of IASB in undertaking this project and we would like to thank you for the opportunity to share our views on Management Commentary. We would be pleased to meet with IASB staff and partner standard-setters and organizations to discuss our comments. If you have any questions, please contact Takayuki Sumita , Chairman for WICI Global (tel: +32-2-230-6992, e-mail: sumita@jmceu.org).

Sincerely,

The Members of the World Intellectual Capital Initiative Network:

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