



**INTERNATIONAL FEDERATION  
OF ACCOUNTANTS**

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## Agenda Item

# 7

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**DATE:** February 22, 2011  
**MEMO TO:** Members of the IPSASB  
**FROM:** Joy Keenan  
**SUBJECT:** Narrative Reporting – Discuss Issues

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### OBJECTIVE OF THIS SESSION

To **discuss** a draft Issues Paper on *Narrative Reporting*

### AGENDA MATERIAL

#### 7.0 Covering Memo

Appendix 1 – Approved Project Brief (for information)

Appendix 2 – Excerpt from Minutes on Narrative Reporting session from March 2008 IPSASB meeting

#### 7.1 Issues Paper – *Narrative Reporting*

#### 7.2 Summary of Requirements in Standards and Guidance

#### 7.3 Research Details by Jurisdiction

### ACTION REQUIRED

The IPSASB is asked to provide staff with comments and suggestions for further development of the Issues Paper – *Narrative Reporting*.

### BACKGROUND

1. The Project Brief for narrative reporting was approved in March 2008. Due to the IPSASB's decision to complete its convergence initiative throughout 2008-2009, work on this project was deferred. A copy of the approved Project Brief is appended to this paper.

2. The topic of narrative reporting has been addressed in a number of jurisdictions internationally within English and non-English speaking jurisdictions. There are a variety of terms applied to it, including Management Discussion and Analysis (MD&A), Management Commentary (MC), Financial Statement Discussion and Analysis (FSD&A), Operating and Financial Review (OFR), Rapport de gestion, and Business Report.
3. While the terms used for this type of reporting vary widely, all center on providing narrative explanation by management to enhance the usefulness of financial information. The detail of what is required, however, also varies by jurisdiction to some degree.
4. Material on narrative reporting varies from accounting standards to recommended practices to requirements by regulators, legislatures and government agencies that specify form and content of public sector financial information to be included. In undertaking this project, the work of national standard setters both in the public and private sectors, regulatory guidance, and current practice will be considered.
5. The research undertaken to date is included in agenda papers 7.2 and 7.3. The information reflects material provided by Members and TAs to staff. Members are encouraged to provide staff with additional relevant sources of information to consider as the project progresses.

## **SCOPE**

6. The Project Brief notes that: “This project will evaluate how a narrative explanation (termed Narrative Reporting for this project) by management should be used to enhance the usefulness of financial information provided by general purpose financial statements (GPFS).”
7. Because narrative reporting on financial statements is linked to the financial statements, this project is closely linked to Phase 1 of the IPSASB’s Conceptual Framework project (currently subject to public exposure), which sets out the objectives, users and qualitative characteristics of general purpose financial reports (GPFRs), which include the financial statements. This project will assume the same direction as the project on service performance reporting to be consistent with the users, user needs, and qualitative characteristics identified in the Conceptual Framework ED 1.
8. It may also need to consider the work currently under way in Phase 4 of the Conceptual Framework, dealing with presentation. This project deals with presentation of all GPFRs,

and may have an impact on how narrative reports on financial information are presented within a GPFR.

9. At this stage the point of this paper is not to reach any conclusions but to have a preliminary discussion of some of the issues inherent in the project and provide feedback to staff to further develop the Issues Paper.

10. A task-based group (TBG) has been established to develop this project. The TBG members are:

Hong Lou  
Bharti Prasad  
Ron Salole  
Frans van Schaik

11. The TBG met briefly in Jakarta to discuss the project. One of the issues they identified, on which the IPSASB's views are sought, pertains to the relationship of this project with the project on service performance reporting. This issue is discussed in agenda paper 7.1.



## **INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS BOARD**

### **PROJECT BRIEF AND OUTLINE**

#### **1. Subject – Narrative Reporting (NR)**

This project will evaluate how a narrative explanation (termed Narrative Reporting for this project) by management should be used to enhance the usefulness of financial information provided by general purpose financial *statements* (GPFS).

#### **2. Project Rationale and Objectives**

In the private sector and in many governmental jurisdictions, it is reasonably widely accepted that NR enhances the usefulness of financial information. The focus of the project will be to identify and standardize the unique aspects of NR and how they “add value” in a public sector financial reporting context.

NR provides stakeholders with a narrative description of various matters, such as the major factors underlying the performance of the entity during the reporting period or the known factors which are likely to influence its performance in the future. This description can assist in placing aspects of the financial statements in context. NR can also enhance the value of financial information for decision making and to make assessments of the entity’s discharge of accountability.

As the appropriate scope of NR for the public sector is considered, the project will examine the current International Accounting Standards Boards (IASB) active project on Management Commentary (MC), as well as existing national standards and guidance on NR (or its equivalent) in the public and private sectors, where standards, guidance, and regulatory requirements for NR have a long history. In addition, NR approaches of other public sector bodies interested in making comparative fiscal information, such as Eurostat, IMF, World Bank and the United Nations will be considered.

##### **a) Issues Identification**

The main issues to be considered in the NR project are:

- What are the objectives of NR?
- What are the main attributes of high quality narrative explanations?
- Are there essential content elements to include in NR?
- What type of guidance is appropriate?

## **b) Objectives to be achieved**

The objective of the project is to provide guidance for NR.

The initial objective is to produce a Consultation Paper - “Narrative Reporting: Exploring the Issues for Standardization and Use in Public Sector General Purpose Financial Reporting.” The Consultation Paper will highlight and analyze existing approaches by the IASB and in jurisdictions where NR is a feature of governmental financial management.

Preliminary research conducted that indicates NR is used by various groups to enhance GPFR in current practice. Unlike traditional financial statements, NR often includes non-financial information coupled with financial information to explain the current status and potential future financial status while introducing the idea of prospective or future looking financial data. The project will consider whether the standardization of this process will improve financial reporting within the public sector.

### *i. Target Audience*

The definition of the users and objectives of NR should correspond closely with the Conceptual Framework work as it develops.

In considering how NR will be developed for the public sector, a consideration of those who currently define the form and content of public sector narrative explanations will be undertaken. In establishing guidance we must be cognizant of regulators and/or the equivalent government agencies that currently set the form and content (i.e. US Office of Management & Budget, European Commission, FReM) of certain types of reporting.

### *ii. Project Deliverables*

The next step in this project would be to develop a draft Consultation Paper to be presented at the June Moscow IPSASB meeting. Once approved, this Consultation Paper would be issued for comment and eventually lead to guidance or standards as necessary.

### *iii. Content of IPSAS*

This is not a project directly related to the general purpose financial statements. Therefore, it is not feasible or appropriate to provide definitive final outputs at the initiation stage. Dependent upon decisions following analysis of submissions on a Consultation Paper, an Exposure Draft of a Standard and/or detailed Guidance will be developed.

### **c) Link to IFAC/IPSASB Strategic Plans**

#### *i. Link to IPSASB Strategy*

In the IPSASB Strategy and Operating Plan MD&A (NR) is listed as a potential project that is public sector specific and is identified as important. At the March 2007 meeting in Accra, the IPSASB approved the initiation of this project in 2008. The NR project was linked to the #2 IPSASB Strategic Theme of Public Sector specific project. High quality NR will enhance the quality and transparency of public sector financial reporting by providing better information for public sector financial management and decision making.

#### *ii. Link to IFAC Strategic Plan*

The alignment of the IPSASB Strategic theme concerning NR results in a direct impact on the IFAC Strategic Theme of “Recognition as the International Standard Setter” as well as a direct impact on the “Enhancement of collaborative efforts.”

## **3. Outline of the Project**

### **a) Project Scope**

The scope of the project is to determine how a narrative explanation by management in the public sector should be used to enhance the usefulness of financial information within general purpose financial *statements* (GPFS) and how it should be included within general purpose financial *reporting* (GPFR).

The NR guidance would apply to all public sector entities other than Government Business Enterprises.

Note that there are linkages with the Conceptual Framework, Long-Term Fiscal Sustainability and Performance Reporting projects.

### **b) Major Problems and Key Issues that Should be Addressed**

#### *Key Issue #1 - What are the objectives of NR?*

The first issue will be to consider the objectives of narrative reporting since this will ultimately lead to developing the guidance needed to meet those objectives. The work of the IASB and national standard setters will be considered and evaluated in this context.

#### *Key Issue #2 - What are the main attributes of high quality narrative explanations?*

In establishing the main attributes that make narrative explanations useful and of high quality, the needs of the public sector GPFR user will be important. Certain definitions like “supplement and complement” will be explored. In addition, the term “through the eyes of management” will be assessed to determine if it is

appropriate in the public sector and, if so what it means. The use of prospective forward looking information will also be considered.

*Key Issue #3 - Are there essential content elements to include in NR?*

There are a variety of approaches to the format and elements of NR prescribed by standard setters and regulators. It will be important to consider the approach that will yield the highest quality NR that allows comparison to other entities and periods.

*Key Issue #4 – What type of Guidance is appropriate?*

There are a number of potential ways that guidance could be developed, including:

- Recognizing best practices;
- Issuing specific non-mandatory guidance;
- Issuing a standard that applies when certain conditions exist  
(IPSAS 24, “Presentation of Budget Information in Financial Statements); and
- Issuing a standard (revised or new) that is mandatory.

While the IPSASB has primarily issued standards, as the first project addressing reporting outside of GPFS, there may be other appropriate vehicles. In considering the type of guidance, audit and assurance aspects of NR will also be addressed.

#### **4. Describe the Implications for any Specific Persons or Groups**

##### **a) Relationship to IASB**

As noted, the IASB project on MC will be followed closely for points of convergence where possible.

##### **b) Relationship to other projects in process or planned**

There are close linkages with the Conceptual Framework project, Long Term Fiscal Sustainability, and Performance Reporting.

##### **c) Other**

This project has implications for the following:

- Assurance and verifiability (IAASB/INTOSAI); and
- Budget and statistical groups involved with public sector financial statements.

## **5. Development Process, Project Timetable and Project Output**

### **a) Development process**

The development of outputs will be subject to the IPSASB's formal due process. The issuance of documents for public comment will be subject to the usual IPSASB voting rules. As the project progresses, regular assessments will be made to confirm the proposed path in the project timetable remains the most appropriate.

The initial output will be a Consultation Paper. Following analysis of submissions on the Consultation Paper, a decision will be made on whether to develop an Exposure Draft of Reporting Requirements and/or Guidance. An Exposure Draft and/or Guidance will also be subject to formal due process, including a consultation period of at least four months.

### **b) Project timetable**

The project timetable should identify the major project milestones and the expected timeline for achieving the objectives.

<b>Major Project Milestones</b>	<b>Expected Completion</b>
Present Project Brief & Draft Issues Paper	March 2008
Approve Consultation Paper	October 2008 Response date March 31, 2009
Analysis & ED	October 2009 Response date March 31, 2010
Analysis of ED responses	May/June 2010
Present and Approve Final IPSAS or Guidance as required	October 2010

### **c) Project output**

The nature of the output will depend on the results of IPSASB process.

## **6. Resources Required**

### **a) Task Force**

A full Task Force is unlikely to be required; however, members may need to assist the Technical Staff with a broad understanding of current practices in both English and non-English speaking countries.

This project has significant interplay with the current IASB project on Management Commentary and other projects by National Standard Setters in both the Public and Private Sectors.

The project would benefit from input from government agencies that set form and content of existing NR reports. Staff will reach out to groups like (FReM – FRAC, European Commission, US Office of Management and Budget, etc) for input.

**b) Staff**

One staff member will be required on this project for the period of the review (March 2008 – October 2010). It is anticipated that approximately one-third of an FTE would be needed.

**c) Factors that might add to complexity or length**

- Nature of Product;
- Interaction with other projects at the IPSASB (Conceptual Framework, Fiscal Sustainability, etc);
- Developments/Decisions with the IASB Management Commentary project;
- The IPSASB position of prospective forward looking information; and
- Implication to the Audit and Assurance community. Verifiability of NR.

## **7. Important Sources of Information that Address the Matter being Proposed**

### **IASB MC Project:**

*IASB Project Page Management Commentary* [Click here for MC Project Page](#)

### **IPSAS Standards & Projects:**

*IPSAS 01 Presentation of Financial Statements* [Click here for IPSAS 01](#)

*IPSAS 24 Presentation of Budget information in Financial Statements*

[Click here for IPSAS 24](#)

*Fiscal Sustainability (current project)*

[Click here for FISCAL SUSTAINABILITY project page](#)

*IPSAS Conceptual Framework (current project)*

[Click here for CONCEPTUAL FRAMEWORK project page](#)

*IPSAS 18 - Segment Reporting* [Ctrl + Click here for IPSAS 18](#)

*IPSAS 22 - Disclosure of Financial Information General Government Sector*

[Click here for IPSAS 22](#)

*IPSAS Glossary of Defined Terms (as of December 31, 2006)*

[Click here for GLOSSARY](#)

### **Public Sector Standard Setters:**

*Canada PSAB* [http://www.cica.ca/index.cfm/ci\\_id/225/la\\_id/1.htm](http://www.cica.ca/index.cfm/ci_id/225/la_id/1.htm)

*FReM - Financial Reporting Manual* with consultation with the Financial Reporting Advisory Board and is issued by the relevant authorities in England and Wales, Scotland and Northern Ireland <http://www.financial-reporting.gov.uk/default.htm>

*French websites* [www.comptes-publics.gouv.fr](http://www.comptes-publics.gouv.fr) or *Conseil National de la comptabilite*

*USA GASB* <http://www.gasb.org/>

*USA FASAB* <http://www.fasab.gov/>

*Private Sector Standard Setters:*

Prepared by \_\_\_\_\_ Date \_\_\_\_\_

(Technical Manager IPSASB)

The following should be completed after board or committee approval and after revising the project proposal form to reflect any changes by the board or committee.

Approved by \_\_\_\_\_ Date \_\_\_\_\_

(Chair IPSASB)

## **COMMENTS BY TECHNICAL MANAGERS**

The comments of Technical Manager from each technical area are required before this Project Proposal is considered by the board or committee proposing to undertake the project.

### **Technical Manager to the Compliance Advisory Panel**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

### **Technical Manager to the DNC**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

### **Technical Manager to the SMPC**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

### **Technical Manager to the IESBA**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

**Technical Manager to the IAASB**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

**Technical Manager to the PAIB Committee**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

**Technical Manager to the IAESB**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

**Technical Manager to the Transnational Auditors Committee**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

## **Appendix 2 – Excerpt from Minutes on Narrative Reporting session from March 2008 IPSASB meeting**

### **7. NARRATIVE REPORTING**

A draft project brief was presented in preparation for the initiation of a project on Narrative Reporting in 2009. Staff had undertaken an initial analysis of issues to be considered, including considering the project in the context of “Rules of the Road”.

Members expressed initial agreement with the scope of the coverage proposed by Staff. They agreed that the project should be initiated only once responses to the Consultation Paper on Conceptual Framework (CF) have been considered. In addition they discussed using an incremental approach towards the evolution of this project with the initial step being focused on financial statement discussion and analysis and further steps going beyond to other aspects of performance reporting.

Staff was also directed to update the Project Brief and draft Issues Paper as follows:

- Emphasis that this will not necessarily be an IPSAS but may be in the form of guidance;
- Revise the project scope to start to draw a boundary/distinction between performance reporting, budgetary reporting and narrative reporting, recognizing that there will be overlap and crossover issues that will need to be dealt with;
- Revise the brief to indicate a step-by-step approach to implementation, starting with NR on financial statements but leading to other steps that will correlate with the CF and more public sector specific focus (actual performance against budget, accountability in government, budget modifications, etc);
- Review and revise the public sector justification by further strengthening the accountability to stakeholders;
- Revise language such as “likelihood,” and consider more appropriate terms such as “risk.”
- Recognize the need to explore forward looking information, in a fact based way;
- Review and enhance the discussion of the whole-of-government versus entity level-of-government, as well as consideration of a wide variety of other public sector entities, such as the United Nations;
- Explain the need to define “management” in a public sector context, including avoiding political connotations;
- Highlight a number of factors such as the relevance of qualitative characteristics, the need to avoid “boiler plating,” and concerns over the length of NR.
- Recognize that this project will consider the IASB Management Commentary project. However, the IASB project is not the driving force behind IPSASB’s NR project. NR should not be viewed as a convergence project because the different user base in the public sector makes the public sector specific needs quite clear. It is anticipated that there will be fewer correlations to private sector standards as the project moves beyond the financial statement phase; and
- Various editorial suggestions to improve the general readability.

A further version of the project brief will be distributed to Members for comment out of session.

## NARRATIVE REPORTING – ISSUES PAPER

### Introduction

#### Background

1. At present, there is no internationally generally accepted form or content for narrative reports and the practice of narrative reporting varies across jurisdictions. For example, in some jurisdictions, the requirement to provide such reports is in legislation or regulation, while in others it is strictly voluntary. In some jurisdictions, there is a standard for narrative reporting issued by a standard-setting body specifically for public sector entities, while in other jurisdictions, the form and content of such reports may be left to management's discretion. See agenda papers 6.2 and 6.3 for the research results.
2. This project was initiated to provide a framework for providing narrative reports. It is recognized that the form and content of such reports may, and should, vary among entities and across jurisdictions. Narrative reports are intended to provide insight into an entity's specific circumstances, including the legal and economic circumstances of the jurisdiction in which an entity operates. A flexible approach, such as that adopted in the jurisdictions that have either issued standards on, or have a legal or regulatory requirement for, narrative reporting, will permit entities to discuss and analyze the trends, events, and factors that are most relevant to their particular circumstances.

#### March 2008 Approved Project Brief

3. The Project Brief identified the scope of the project as follows:

The scope of the project is to determine how a narrative explanation by management in the public sector should be used to enhance the usefulness of financial information within general purpose financial statements (GPFSS) and how it should be included within general purpose financial reports (GPFRRs).

The guidance developed would apply to all public sector entities other than Government Business Enterprises.

4. The Project Brief identified the main issues to be considered in the narrative reporting project as follows:
  - What are the objectives of narrative reporting?
  - What are the main attributes of high quality narrative explanations?
  - Are there essential content elements to include in narrative reporting?

- What type of guidance is appropriate?

This paper will explore these issues as well as others identified by the TBG.

5. This project has linkages with the following active IPSASB projects:
  - The Conceptual Framework (especially Phase 1 and Phase 4);
  - Reporting on the Long-Term Sustainability of Public Finances (“long-term fiscal sustainability”); and
  - Service Performance Reporting.
6. These other IPSASB projects will be considered as this project is developed. As discussed below, the objectives and users of general purpose financial reports (GPFRs) set out in the Conceptual Framework Phase 1 exposure draft are considered to be an appropriate basis for narrative reporting. In addition, the Phase 4 project on presentation may also contain guidance relevant to narrative reporting.
7. For example, as discussed below, some jurisdictions consider both long-term fiscal sustainability reporting and service performance reporting to be included in narrative reporting. In addition, the IPSASB may determine that those two projects, as well as narrative reporting, should have the same level of authoritative status.
8. In addition, the IASB issued the IFRS Practice Statement, *Management Commentary: A Framework for Presentation* in December 2010, which will also be considered to the extent that the Practice Statement is relevant to the public sector. Note that the approved Project Brief indicated this is not a convergence project.

**Questions for the IPSASB:**

- Do you agree that the project should provide a definition of “narrative reporting”?
- Are there any other issues this project should address in addition to those identified in the approved Project Brief?

## Definition of Narrative Reporting

9. The March 2008 Project Brief did not discuss a definition of narrative reporting. The IPSASB had decided to use the term instead of one involving the term “management”. Many of the existing standards refer to management’s involvement.
10. The TBG is of the view that a definition is required to clearly distinguish the scope of this project from others that might be considered to fall under the umbrella of “narrative

reporting” in some jurisdictions. Accordingly, this paper contains a discussion of elements of such a definition.

11. However, additional research on legislation and regulation governing such reports in the public sector and the development of other guidance and proposed pronouncements since the time the Project Brief was prepared have tended to use the term “narrative reporting” in a broader sense. For example, certain jurisdictions include service performance reporting and comparisons with budget within the scope or understanding of narrative reporting (e.g., FASAB, South African Treasury and Municipal Finance Act, New Zealand Public Finance Act 1989 and Local Government Act 2002 Schedule 10 Part 3). These are the subject of existing IPSASs or projects under way. There may also be requirements to report on compliance (e.g., New Zealand Local Government Act 2002 Schedule 10 Part 3).
12. In addition, the December 2010 Exposure Draft, *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Role, Authority and Scope; Objectives and Users; Qualitative Characteristics; and Reporting Entity* (Conceptual Framework ED 1), notes under the caption of “Narrative Reports”:

2.25 In some cases, quantitative measures of the outputs and outcomes of the entity’s service delivery activities during the period and anticipated activities in future periods will provide relevant information about the achievement of these service delivery objectives—for example, information about the cost, volume, and frequency of service delivery, and the relationship of services provided to the resource base of the entity. In other cases, the achievement of service delivery objectives may need to be communicated by an explanation of the quality of particular services provided or the outcome of certain programs.

This reference to the communication of an explanation of service delivery quality could imply that such an explanation would be part of the narrative report. However, the approved project brief excludes service performance reporting from the scope of this project.

13. The Israel Government Accounting Standards Board has issued draft guidance, *Narrative Information Attached to the Financial Statements of a Public Sector Entity*, which “... defines the preparation and presentation requirements of narrative information attached to financial statements of a public sector entity (here and after - "a management report"), which shall be attached to the annual financial statements of a public sector entity (here and after – "the entity") and be prepared by the entity's management.” It clearly links the term “narrative information” to the GPFS.

14. On the other hand, the December 2010 IFRS Practice Statement defines management commentary as follows:

IN3. Management commentary is a narrative report that provides a context within which to interpret the financial position, financial performance and cash flows of an entity. It also provides management with an opportunity to explain its objectives and its strategies for achieving those objectives. Users routinely use the type of information provided in management commentary to help them evaluate an entity's prospects and its general risks, as well as the success of management's strategies for achieving its stated objectives. ...

This definition implies there are other types of narrative reports than those specifically related to the financial statements, and clearly distinguishes such reports from other types of narrative reports.

15. The TBG is seeking the IPSASB's confirmation that narrative reporting should not include or subsume service performance reporting, or other types of reports that may form part of the GPFR, but that it should deal strictly with the narrative analysis of the information contained in the GPFs. This was the intended scope of the project as described in the March 2008 approved Project Brief.
16. The TBG is of the view that retaining the term used in the Project Brief will cause confusion, and that a more descriptive and specific term should be used. The covering memo accompanying the Project Brief indicated that "At this stage, staff proposes to use the term Narrative Reporting for operational purposes, with a view to determining the most appropriate title once the project has progressed." The TBG seeks the IPSASB's views on whether to use a different term to describe this specific type of financial reporting, and if so, what the term should be.
17. In doing so, it is necessary to consider whether to change the name from "narrative reporting" to avoid any potential confusion or overlap with the service performance reporting project. For example, the US public sector standards issued by the GASB and FASB term "management discussion and analysis", and the private sector term "management commentary" are well understood. Canada's public sector standard terms this type of reporting "financial statement discussion and analysis". As noted above, Israel's draft guidance uses the term "narrative information attached to financial statements" which is appealing because it clearly links to the financial statements without limiting the term "narrative reporting" which is used more broadly in some jurisdictions and pronouncements. The TBG suggests the term "narrative reporting on financial statements" to help reduce potential confusion on the scope of this project relative to the IPSASB project on service performance reporting. The remainder of this paper adopts that approach.

18. Based on existing elements of definitions of narrative reporting on financial statements, a possible definition (subject to change, as noted above) follows:

A **narrative report on financial statements** is a report by management included in the GPF of the entity that complements and supplements the GFS of the entity. It includes qualitative as well as quantitative analysis and discussion that provides a context within which users can interpret the entity's financial position, results of operations and cash flows for the period.

19. However, if the IPSASB prefers a term referring to “management” in the definition, as is done in certain existing pronouncements, it is proposed that the starting point would be “key management personnel” IPSAS 20, *Related Party Disclosures*. Key management personnel would generally be those responsible for preparing a narrative report on financial statements.

**Key Management Personnel**

6. Key management personnel include all directors or members of the governing body of the reporting entity, where that body has the authority and responsibility for planning, directing, and controlling the activities of the entity. At the whole-of-government level, the governing body may consist of elected or appointed representatives (for example, a president or governor, ministers, councilors and aldermen or their nominees).
7. Where an entity is subject to the oversight of an elected or appointed representative of the governing body of the government to which the entity belongs, that person is included in key management personnel, if the oversight function includes the authority and responsibility for planning, directing, and controlling the activities of the entity. In many jurisdictions, key advisors of that person may not possess sufficient authority, legal or otherwise, to satisfy the definition of key management personnel. In other jurisdictions, key advisors of that person may be deemed to be key management personnel because they have a special working relationship with an individual who has control over an entity. They therefore have access to privileged information, and may also be able to exercise control or significant influence over an entity. Judgment is required in assessing whether an individual is a key advisor, and whether that advisor satisfies the definition of key management personnel, or is a related party.
8. The governing body, together with the chief executive and senior management group, has the authority and responsibility to plan and control the activities of the entity, to manage the resources of the entity and for the overall achievement of entity objectives. Therefore, key management personnel will include the chief executive and senior management group of the reporting entity. In some jurisdictions, civil servants will not have sufficient authority and responsibility to qualify as key management personnel (as defined by this Standard) of the whole-of-government reporting entity. In these cases, key management personnel will consist only of those elected members of the governing body who have the greatest responsibility for the government; often these persons are referred to as Cabinet Ministers.

9. The senior management group of an economic entity may comprise individuals from both the controlling entity and other entities that collectively make up the economic entity.
  
20. The definition will be supplemented by identifying qualitative characteristics of such reports that will best meet users' needs (discussed later in this paper).

**Questions for the IPSASB:**

- Do you agree that the scope of the project should be limited to information reported in the GPFS?
- Should the term used for such reports be changed to something more reflective of the specific type of information presented (e.g., “narrative report on financial statements” as indicated above)?
- Are there any other elements that need to be included in the definition?

## Objectives and Users of Narrative Reports on Financial Statements

21. This project will assume the same direction as the project on service performance reporting to be consistent with the users, user needs, and qualitative characteristics identified in the Conceptual Framework ED 1.

### Objectives of GPFRs

22. The objectives of narrative reporting on financial statements derive from those of GPFRs. Conceptual Framework ED 1 states:
  - 2.1 The objectives of financial reporting by public sector entities are to provide information about the entity that is useful to users of GPFRs for accountability purposes and for decision-making purposes (hereafter referred to as “useful for accountability and decision-making purposes”).
  - 2.2 Financial reporting is not an end in itself. Its purpose is to provide information useful to users of GPFRs. The objectives of financial reporting are therefore determined by reference to the users of GPFRs, and their information needs.
23. Accountability and decision making are the primary objectives of GPFRs of public sector entities. Information provided in GPFRs for accountability purposes will contribute to, and inform, decision making.
24. Accountability and decision making are likewise the overarching objectives of narrative reporting on financial statements. Accountability is the relationship between those who

control or manage an entity and those who possess formal power over them. Financial reporting is intended to provide information that helps a public sector entity fulfill its duty to be publicly accountable. However, public sector entities' financial statements alone do not provide all of the information users of those statements need to make informed decisions. Additional quantitative and qualitative information may be required to provide a better context for understanding, interpreting, and assessing public sector GPFS.

### Objectives of Narrative Reporting on Financial Statements

25. Transactions entered into by public sector entities are increasingly complex and the GPFSs that report on such transactions are consequently increasingly complex and detailed. Narrative reporting on financial statements assists users in understanding and interpreting GPFS by providing more user-friendly descriptions of the entity's financial operations than the financial statements alone, and in ways that users can readily understand. It may also demonstrate linkages and dependencies among financial statement items that users may not otherwise be able to discern.
26. Narrative reporting on financial statements may encourage better analysis of an entity's current operations. For example, identification of the main events, trends, and factors influencing the current reporting period, provides useful information for decision making regarding the use of scarce resources. It may also help identify potential impacts on future reporting periods. Some pronouncements on narrative reporting require a forward-looking point of view (see Agenda Paper 7.2).
27. Frameworks for pronouncements (standards or guidance) developed by standard setters generally adopt an approach of linking the objectives pertaining to narrative reporting on financial statements to their financial reporting frameworks. Agenda Paper 7.2 summarizes the main objectives contained the various existing standards.
28. For example, the Israel Government Accounting Standards Board's proposed guidance indicates the objective of such information is to "...provide to the users information about the entity's objectives and activities, including information about factors that affect the entity." This is consistent with Conceptual Framework ED 1.
29. In jurisdictions for which narrative reporting on financial statements is required by legislation or regulation, the objectives may not be specifically stated or may be stated in more general terms. Most legislation or regulation pertaining to narrative reporting on financial statements sets out requirements only. Agenda Paper 7.2.1 includes the summaries of legislative and regulatory requirements provided to staff by Members and TAs to date.

30. For example, the South African Municipal Finance Act indicates the following purpose of the annual report (of which the narrative report on financial statements is a part):

- (a) To provide a record of the activities of the municipality or municipal entity during the financial year to which the report relates;
- (b) To provide a report on performance against the budget of the municipality or municipal entity for that year; and
- (c) To promote accountability to the local community for the decisions made throughout the year by the municipality or municipal entity.

Item (c) relates directly to the IPSASB GPFR objective of accountability.

31. The New Zealand annual report must provide the information that is necessary to enable an informed assessment to be made of the department's performance during the financial year (including an assessment against the intentions, measures and standards set out at the start of the financial year in the information on the department's future operating intentions in accordance with sections 40 and 41). This objective is consistent with the IPSASB GPFR objective of decision making.

32. In addition to the overall objectives of GPFRs, the main specific objectives of narrative reports on financial statements, identified from existing and proposed pronouncements and legislative and regulatory requirements (see agenda paper 7.2), include:

- (a) Enhance user understanding and usefulness of GPFRs;
- (b) Expand and explain financial statement information (e.g., what has happened, why, and implications);
- (c) Provide context for the related financial statements; and
- (d) Aid in understanding operations, successes, and challenges in present and future.

**Questions for the IPSASB:**

- Do you agree with the identified objectives of narrative reporting on financial statements identified in paragraph 32 above?
- Are there objectives that should be added, deleted, or amended?

## Users and their Needs

33. Conceptual Framework ED 1 identifies two groups primary users of GPFs of public sector entities:

- (a) Service recipients (taxpayers and other members of the community that benefit from the services provided by the government or other public sector entity, whether as a result of exchange or non-exchange transactions); and
- (b) Resource providers (“involuntary resource providers” such as taxpayers, and “voluntary resource providers” such as lenders, donors, suppliers, fee-for-service consumers and employees).

These two groups of users are also the identified users of narrative reports on financial statements. Narrative reporting on financial statements assists these users by providing information beyond that contained in the financial statements. It complements and supplements the financial statements by expanding on and explaining information contained in the financial statements.

34. As noted in Conceptual Framework ED 1, for accountability and decision-making purposes, service recipients and their representatives require information as input to assessments of such matters as whether the range, volume and cost of services provided during the reporting period, and the amounts and sources of their cost recoveries, are appropriate and whether current levels of taxes or other charges are sufficient to maintain the volume and quality of services currently provided. They will also require information about the entity’s anticipated future objectives, and the amounts and sources of cost recoveries necessary to support those activities.

35. Resource providers require information as input to assessments of such matters as whether the entity is achieving the objectives established as the justification for the resources raised during the reporting period; funded current operations from funds raised in the current period from taxpayers or from borrowings or other sources; and is likely to need additional (or less) resources in the future, and the likely sources of those resources. Lenders and creditors require information as input to assessments of the liquidity of the entity and to confirm that the amount and timing of repayment will be as agreed.

36. Conceptual Framework ED 1 specifically discusses the usefulness of narrative reports in providing the information required by service recipients and their representatives and resource providers and their representatives:

2.24 Narrative reports can provide additional information about the major factors underlying the financial and service delivery performance of the entity during the reporting period. They can also outline the assumptions that underpin expectations about, and factors that are likely to influence, the entity's future performance. This will assist users to better understand and place in context the financial and non-financial information included in GPFRs, and enhance the role of GPFRs in providing information useful for accountability and decision-making purposes.

37. Narrative reporting on financial statements may include quantitative analysis of significant variances between the prior year and current year, including assets, liabilities, revenues, and expenses. This allows users to assess the results of past events, and identify future prospects. It also assists in understanding and assessing trends in the entity's financial position and changes in financial position.
38. In some cases, a significant change may have occurred during the reporting period, but the financial statements and quantitative analyses may not illustrate a significant variance because of offsetting factors. Narrative explanations may identify and explain significant variances between the current year and prior year such as variances due to changes in how a service is delivered, changes in programs and services provided, and changes due to the level of revenues raised or costs incurred. Some of these may be within the control of the entity (e.g., taxation rates, new or discontinued programs or services, restructuring operations, or changing the method of service delivery), while others may be due to external factors (e.g., a decreased tax base, wage contracts, and unexpected events such as a natural disaster). Such explanations may assist users in assessing future services and commitments of the entity.
39. An analysis of financial assets provides information regarding the amount of resources available to be converted to cash if necessary. In addition, specific ratios and analysis of cash flows may be useful to highlight liquidity.
40. Analyses of revenues by major source may indicate trends and dependencies on specific revenue sources (e.g., government business enterprises (GBEs), transfers, or royalties).
41. Analyses of expenses may demonstrate the entity's allocation and use of resources, provide insight into the cost of programs and services, and assist in evaluating the cost of borrowing to finance spending.
42. Discussion of significant commitments, contingencies, and subsequent events assists users in assessing future revenue requirements of the entity.

**Questions for the IPSASB:**

- Do you agree that the user needs identified above related to narrative reports on financial statements are also appropriate for narrative reporting?

## Qualitative Characteristics of, and Constraints on, Information included in Narrative Reports

### Qualitative Characteristics of Information Contained in GPFRs

43. Narrative reports on financial statements are part of GPFRs because they are intended to complement and supplement the GPFSs. Conceptual Framework ED 1 notes that “...the qualitative characteristics of information included in GPFRs are the attributes that make that information useful to users and support the achievement of the objectives of financial reporting.” As noted earlier, the objectives of financial reporting are to provide information useful for accountability and decision-making purposes.
44. Conceptual Framework ED 1 proposes the qualitative characteristics of information contained in GPFRs are:
- Relevance;
  - Faithful representation;
  - Understandability;
  - Timeliness;
  - Comparability; and
  - Verifiability.
45. Conceptual Framework ED 1 proposes the constraints are:
- Materiality;
  - Cost-benefit; and
  - Balance between the qualitative characteristics.
46. These qualitative characteristics are discussed below in relation to narrative reporting. In addition, specific attributes of narrative reports on financial statements identified from the research, will be considered.

### **Relevance**

47. Conceptual Framework ED 1 proposes that financial and nonfinancial information is relevant if it is capable of making a difference in achieving the objectives of financial reporting. For narrative reports on financial information to be relevant they must pertain to the specific circumstances of the entity and add management’s insights. Management of an entity has the detailed knowledge of the transactions, events, and conditions reflected in the entity’s financial report and of the policies that govern the entity’s operations.

Management also possess informed expectations regarding the future based on that knowledge. For example, some pronouncements on narrative reporting require a summary or overview of the entity's objectives, significant events and conditions that affected the financial statements (e.g., significant changes, unplanned events), which provides the starting point for assessing the entity's financial performance and trends.

48. Generic disclosures that do not relate to the specific operations, practices and circumstances of the entity would not be relevant. Likewise, information that simply repeats financial statement information or note disclosures in the financial statements without analysis or presenting discussions that do not provide insight into the entity's past performance or prospects is unlikely to be relevant to users and may make it more difficult for them to understand the most significant matters the entity faces. For example, a discussion of the risks the entity faces would provide relevant information to users about exposure or vulnerability to concentrations (e.g., significant loans to particular regions or industries) or dependence on a particular source of revenue as noted above.

#### **Faithful representation**

49. Conceptual Framework ED 1 proposes that faithful representation is attained when the depiction of the phenomenon is complete, neutral, and free from material error. Narrative reports on financial information that faithfully represent the information would be:
- (a) based on currently-known facts, decisions, or conditions;
  - (b) consistent with the financial statements; and
  - (c) balanced in discussing both positive and negative facts and views of management.

Information that excludes certain facts (e.g., negative) is incomplete and thus could be biased (not neutral). In cases when a narrative report on financial information presents ratios, tables, or charts, they should not distort the information in the financial statements by, for example, using a scale that exaggerates a positive or negative trend.

50. Although some jurisdictions require or permit future-looking information to be presented, such information must also meet the conditions noted above.

#### **Understandability**

51. Conceptual Framework ED 1 proposes that understandability is the quality of information that enables users to comprehend its meaning. Narrative reports on financial statements complement and supplement the financial statements. They are intended to help users of the financial statements by explaining the complex events and transactions in the financial

statements in a readable, clear, and simple manner. Reports are not understandable when they use descriptions that are too technical, or provide excessive detail or are too vague in describing those events and transactions.

#### **Timeliness**

52. Conceptual Framework ED 1 proposes that timeliness means having information available for users before it loses its capacity to be useful for accountability and decision-making purposes. Narrative reports on financial statements discuss and analyze the current financial statements. In doing so, they may be useful in predicting future results by explaining significant changes and highlighting trends. They may, for example, include an analysis of trends in financial performance that provides information that is useful beyond the date of the narrative report.

#### **Comparability**

53. Conceptual Framework ED 1 proposes that comparability is the quality of information that enables users to identify similarities in, and differences between, two sets of phenomena. It is not a quality of an individual item of information, but rather a quality of the relationship between two or more items of information. In some jurisdictions, comparisons with prior years' results are required. Comparability would be enhanced when the same principles and practices are used for each period for such items as determining ratios and preparation of tables and charts included in a narrative report on financial statements. In addition, disclosure of those principles and practices, including underlying assumptions and formulae, may be useful in interpreting the analyses.

#### **Verifiability**

54. Conceptual Framework ED 1 proposes that verifiability is the quality of information that helps assure users that information in GPRFs faithfully represents the phenomena that it purports to represent. In some cases it may not be possible to verify the accuracy of all qualitative and quantitative explanations of such information until a future period, if at all. For example, if the entity's strategy (long-term and risk management) are included in a narrative report on financial statements, such information would be less verifiable than, for example, a ratio calculated from information provided in the financial statements. Verifiability is enhanced when the underlying assumptions and formulae used in the analyses are disclosed. In addition, the methodologies adopted in compiling it, and the factors and circumstances that support any opinions expressed or disclosures made, should be transparent.

#### **Materiality**

55. Conceptual Framework ED 1 proposes that information is material if its omission or misstatement could influence the discharge of accountability by the entity, or the decisions

that users make on the basis of the entity's GPFRs prepared for that reporting period. Narrative reports on financial statements must be concise to be useful, therefore management must select the most important matters to discuss. This means that some items that are material to the financial statements, notes, and other sections of the GPFR may not be discussed in the narrative report on financial statements. For example, a line-by-line analysis of the financial statements is not generally appropriate. Instead, MD&A should summarize the most important items, explain the relevant causes and effects, and place them in context. Inclusion of immaterial disclosures could make the more important information difficult to find.

56. When dealing with qualitative or future-looking information (e.g., expectations about financial results in the future), it is not generally possible to specify a uniform quantitative threshold above which a particular type of information becomes material.

#### **Cost-benefit**

57. Conceptual Framework ED 1 notes that the benefits of financial reporting should justify the costs it imposes. The benefit to users of a narrative report on financial statements that presents a clear and understandable analysis of the complex information contained in the financial statements must be weighed against such costs as collecting and processing the information used in the analysis, and presenting underlying assumptions and methodologies that support such analysis.

#### **Balance between the qualitative characteristics**

58. Conceptual Framework ED 1 notes that in some cases, a balancing or trade-off between qualitative characteristics may be necessary to achieve the objectives of financial reporting. For example, there is often a trade-off between the timeliness of information and its reliability. Narrative reports on financial statements should aim to achieve a balance among the qualitative characteristics to meet the objectives of providing the information. In some cases, depending on the circumstances of the entity, the relative importance of a particular qualitative characteristic may be greater than in others.

#### **Questions for the IPSASB:**

- Are there additional factors that should be considered in discussing the qualitative characteristics of narrative reports on financial information to those identified above?

#### **Main Attributes of High-quality Narrative Explanations**

59. In addition to the overall objectives of GPFRs, the specific attributes of narrative reports on financial statements, identified from existing and proposed pronouncements and legislative and regulatory requirements (see agenda paper 6.2), include:

- (a) Provide management perspective and insights, which is linked to relevance;
- (b) Complement and supplement financial statements, which is linked to understandability;
- (c) Describe positive and negative circumstances (“balance”), which is linked to faithful representation;
- (d) Interpret and assess financial statement information (e.g., whether the entity’s financial position has improved or deteriorated during the period), which is linked to relevance and faithful representation; and
- (e) Identify main trends, events, and factors (both for current financial reporting period and likely to affect future performance, position and progress), which is linked to relevance and timeliness.

**Questions for the IPSASB:**

- Do you agree with the specific attributes of narrative reports on financial statements identified above?
- Are there additional items that should be considered?
- Should these specific attributes be considered as part of the qualitative characteristics?

## Essential Content Elements of Narrative Reports on Financial Statements

### Overview

60. There are a variety of approaches to the format and essential elements of narrative reports on financial statements in material issued by standard setters and regulators. It is important to consider the approach that will yield the highest quality narrative reports on financial statements that allow comparisons to other entities and periods.

### Standards and Guidance issued by Standard Setters

61. Standard setters identified some similar elements of narrative reports on financial statements:
- a. Overview or summary;
  - b. Nature of the entity’s operations;

- c. Risks and uncertainties;
- d. Strategy (long-term and risk management);
- e. Changes from prior year; and
- f. Analysis of significant trends.

These elements were identified in the discussion of the qualitative characteristics, above, and are consistent with those underlying characteristics.

62. In addition to containing similar elements to those noted above, the Israel draft guidance contains the following essential elements for the Management Report (the term used for narrative information attached to financial statements of a public sector entity), which are more specific to that country:

A Management Report shall include an overview of the data from the entity's financial statements, in accordance with its operations, as follows:

- (a) The financial position of the entity;
- (b) The operating results;
- (c) Special events;
- (d) Contingent liabilities;
- (e) Critical accounting estimates.

In addition, significant detailed guidance is provided for each of these items. These requirements are similar to those found in legislative or regulatory requirements for narrative reporting on financial statements in other jurisdictions (see below).

### Legislative and Regulatory Requirements

63. Legislative or regulatory requirements tend to reflect the specific needs of the jurisdiction, and may not, therefore, provide relevant information to users in other jurisdictions.
64. Article 58(1) of the Central Government of the Netherlands Government Accounting Act 2001 requires that:
- (a) The financial information includes information on obligations, expenditures, income, revenues, expenses, capital expenditures, capital income and balance sheet items, as stated in the accounting records and the accompanying notes.

- (b) The financial information presented in the annual report can be clearly distinguished from the non-financial information.

65. The Netherlands' *Besluit begroting en verantwoording provincies en gemeenten* for local governments requires the budget<sup>1</sup> to at least contain the following paragraphs, unless the aspect concerned is irrelevant for the respective province or municipality:

- (a) local taxes;
- (b) financial strength;
- (c) maintenance of capital assets;
- (d) financing;
- (e) management;
- (f) related parties; and
- (g) land use policy.

Certain of these aspects would be within the scope of narrative reports on financial statements, while others are specific requirements of the jurisdiction's regulatory framework.

66. Japanese agencies of central government, which are called "Incorporated Administrative Agencies", and national universities must prepare for their annual reports including "business report", which is considered similar to "narrative reporting". The annual report is required to include:

Financial Information

- (1) Overview of Financial Statements;
- (2) Overview of Investments (e.g., facilities);
- (3) Overview of Budgeted Amounts and Actual Amounts; and
- (4) The Relationship between Reduction of Expenses and the Target of Efficiency.

There are also some practices in Japan where national and local governments prepare narrative explanations regarding particularly changes in financial statements items. There are no prescribed standards or guidelines.

**Questions for the IPSASB:**

- Do you agree with the main common elements of narrative reports on financial statements identified in paragraph 61?

<sup>1</sup> The annual report should contain the paragraphs that are included in the budget in accordance with Article 9. These contain the justification of that which is included in the respective paragraphs in the budget.

- Should guidance be provided at the level of detailed requirements in legislation and regulation identified above (paragraphs 63–66), or should it be more broadly based?
- Are there additional items that should be considered as essential content elements (e.g., the entity’s objectives, specific financial statement items such as contingencies and estimates), or should the essential content elements be limited to identification of “significant financial statement items” and examples of such items be provided (e.g., assets, liabilities, revenues, expenses, contingent liabilities, accounting estimates)?

## Type of Guidance

67. While the IPSASB supports the need for narrative reports on financial statements as a means of improving public sector entities’ accountability and decision making, it acknowledges that the current state of such reporting is still in its early stages of its evolution and development, and that the form and content of narrative reports on financial statements are expected to develop in the future. For example based on the research done, it was found that in some jurisdictions, narrative reporting:

- g. is required with detailed requirements set out in legislation or regulation;
- h. is required with detailed requirements set out in standards (e.g., GASB and FASAB in the US, and the UK FReM);
- i. is voluntary, and there may or may not be standards in place; or
- j. is not required.

68. Paragraph BC 1.7 of Conceptual Framework ED 1 points out that a more comprehensive scope for financial reporting, such as narrative reports on financial statements, does not mean that it is inevitable that authoritative requirements will be developed.

69. The Project Brief indicated that the decision on the type of pronouncement to be issued by the IPSASB ranges from:

- k. Recognizing best practices;
- l. Issuing specific non-mandatory guidance;
- m. Issuing a standard that applies when certain conditions exist (e.g., IPSAS 24, *Presentation of Budget Information in Financial Statements*); and

- n. Issuing a mandatory IPSAS.
70. Given the state of current practice, it is not expected that this project would mandate which entities should be required to publish narrative reports, how frequently an entity should do so, or the level of assurance to which narrative reports should be subjected. Accordingly, it is proposed that this project develop guidance that is non-authoritative. Such guidance would provide a framework for the preparation of high-quality narrative reports on financial statements in jurisdictions in which such reports are required, that helps achieve the objectives of GPFRs by improving accountability and decision making in the public sector. The guidance would be used by public sector entities that do present narrative reports that relates to financial statements prepared in accordance with IPSASs.
71. However, the nature of the guidance developed and its authoritative status will ultimately depend on the IPSASB's decisions on this issue in the current IPSASB projects on service performance reporting and long-term fiscal sustainability.

## Appendix A – EXISTING PRONOUNCEMENTS SUMMARIZED

Examples of Standards and Guidance on Narrative Reporting on Financial Statements (for public sector unless noted otherwise)

	<b>Federal Accounting Standards Advisory Board (United States of America)</b>	<b>Financial Reporting Manual (FReM) (UK – HM Treasury)</b>	<b>Governmental Accounting Standards Board (United States of America)</b>	<b>International Accounting Standards Board (Private Sector)</b>	<b>Israel Government Accounting Standards Board</b>	<b>Public Sector Accounting Standards Board (CICA, Canada)</b>
<b>Term used for this type of report</b>	Management Discussion and Analysis (MD&A)	Operating and Financial Review (OFR)	Management Discussion and Analysis (MD&A)	Management Commentary	Narrative Information Attached to the Financial Statements of a Public Sector Entity	Financial Statement Discussion and Analysis (FSD&A)
<b>Type of Pronouncement</b>	Standard /Concepts SSFASC 3 is not “prescribed guideline for required supplementary information (RSI)” SSFAS 15 is required		Standards Statement No. 3,4 deals with State and Local Governments Statement No. 3,5 deals with Public Colleges and Universities	Non-mandatory guidance	Mandatory guidance (for an entity that prepares and presents financial statements under the accrual basis of accounting)	Non-mandatory guidance – Statement of Recommended Practice (SORP)
<b>Objectives</b>	MD&A is an important vehicle for (1) communicating managers’ insights about the reporting entity, (2) increasing the understandability and usefulness of the GPFFR, and (3) providing accessible information about the entity and its operations.		Assist users in assessing whether the financial position has improved or deteriorated as a result of the year’s activities	<ul style="list-style-type: none"> <li>Management commentary is a narrative report that provides a context within which to interpret the financial position, financial performance and cash flows of an entity. It also provides management with an opportunity to explain</li> </ul>	To provide to the users information about the entity’s objectives and activities, including information about factors that affect the entity.  A Management Report should be used as an addition and as a completion of a public	

<sup>1</sup> The FReM is the technical accounting guide that complements guidance on the handling of public funds published separately by the relevant authorities. The Manual is prepared following consultation with the Financial Reporting Advisory Board and is issued by the relevant authorities in England and Wales, Scotland and Northern Ireland.

	<p>Federal Accounting Standards Advisory Board (United States of America)</p> <p>service levels, successes, challenges, and future. Some federal agencies also refer to MD&amp;A as the “overview.”</p>	<p>Financial Reporting Manual (FRM) (UK – HM Treasury<sup>1</sup>)</p>	<p>Governmental Accounting Standards Board (United States of America)</p>	<p>International Accounting Standards Board (Private Sector)</p> <p>its objectives and its strategies for achieving those objectives. Users routinely use the type of information provided in management commentary to help them evaluate an entity’s prospects and its general risks, as well as the success of management’s strategies for achieving its stated objectives. For many entities, management commentary is already an important element of their communication with the capital markets, supplementing as well as complementing the financial statements.</p> <ul style="list-style-type: none"> <li>• Management commentary should provide information to help users of the financial reports to assess the performance of the entity and the actions of its management relative to stated strategies and</li> </ul>	<p>Israel Government Accounting Standards Board</p> <p>sector entity’s financial statements, through presentation of non-monetary information about the entity’s operations and analysis of the entity’s operation from point of management’s view, and through reference to forecasts and forward-looking information.</p>	<p>Public Sector Accounting Standards Board (CICA, Canada)</p>
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	Federal Accounting Standards Advisory Board (United States of America)	Financial Reporting Manual (FRM) (UK – HM Treasury <sup>1</sup> )	Governmental Accounting Standards Board (United States of America)	International Accounting Standards Board (Private Sector)	Israel Government Accounting Standards Board	Public Sector Accounting Standards Board (CICA, Canada)
<p><b>Specific Attributes</b></p> <ul style="list-style-type: none"> <li>• Supplement &amp; complement GPFS</li> <li>• Mgmt insights</li> <li>• Balanced (positive and negative)</li> <li>• “Vital few” matters addressed (materiality)</li> <li>• Forward-looking information regarding the possible future effects of the most important <u>existing</u>, currently-known demands, risks, uncertainties, events, conditions and trends</li> <li>• May also include forward-looking information about the possible effects of <u>anticipated</u> future demands, events, conditions, and trends</li> </ul>	<ul style="list-style-type: none"> <li>• Introduce the financial statements and provide an analytical overview of the government’s financial activities</li> <li>• Supplement &amp; complement</li> <li>• Objective</li> <li>• Easily readable</li> <li>• Based on currently-known facts, decisions, or conditions that are expected to have a significant effect on financial position and results of operations (fwd-looking)</li> <li>• Provide an analysis of the entity’s overall financial position and results of operations</li> <li>• Fact based</li> <li>• Focus on primary government not component units</li> <li>• Discuss current year results compared with prior year (focus on</li> </ul>	<p>plans for progress.</p> <ul style="list-style-type: none"> <li>• Integrated information that provides a context for the related financial statements</li> <li>• Management’s view determine the information to include in Management commentary considering the needs of the primary users of financial reports. Those users are existing and potential investors, lenders and other creditors.</li> <li>• Explains management’s view not only about what has happened, including both positive and negative circumstances, but also why it has happened and what the implications are for the entity’s future</li> <li>• Complements and supplements the financial statements by communicating</li> </ul>	<ul style="list-style-type: none"> <li>• Data included in the Management Report in accordance with the management’s judgment about the importance of those data to the understanding of the entity’s financial position and operations by a reasonable user</li> <li>• Supplement &amp; complement GPFS</li> <li>• Management’s view</li> <li>• Forward looking</li> <li>• Objective analysis of the entity’s operations, including a discussion of the positive and negative views of its operations and the effects of various events</li> </ul>			



	Federal Accounting Standards Advisory Board (United States of America)	Financial Reporting Manual (FRM) (UK – HM Treasury) <sup>1</sup>	Governmental Accounting Standards Board (United States of America)	International Accounting Standards Board (Private Sector)	Israel Government Accounting Standards Board	Public Sector Accounting Standards Board (CICA, Canada)
<p><b>Essential Content</b></p> <ul style="list-style-type: none"> <li>• the entity's mission and organizational structure;</li> <li>• the entity's performance goals and results;</li> <li>• the entity's financial statements;</li> <li>• the entity's systems, controls, and legal compliance; and</li> <li>• the possible future effects on the entity of existing, currently-known demands, risks, uncertainties, events, conditions and trends.</li> </ul> <p>MD&amp;A should also address the reporting entity's actions taken or planned to address problems and significant</p>			<p>Should provide an analysis of significant changes that occur in funds and significant budget variances. Should describe capital asset and I-t debt activity during the year. Should conclude with a description of currently known facts, decisions, or conditions that are expected to have a significant effect on financial position or results of operations.</p>	<p>account materiality Should taken into account qualitative characteristics of <i>relevance</i> and <i>faithful representation</i>, <i>comparability</i>, <i>timeliness</i> and <i>understandability</i> Forward looking Although the particular focus of management commentary will depend on the facts and circumstances of the entity, management commentary should include information that is essential to an understanding of: (a) the nature of the business; (b) management's objectives and its strategies for meeting those objectives; (c) the entity's most significant resources, risks and relationships; (d) the results of operations and prospects; and</p>	<p>The Management Report shall refer and provide explanations about the key data in the financial statements within a description of entity's segments. The Management Report shall also include information about non-monetary data, including data used by the entity for its segment analysis and goals achievement. A Management Report shall include an overview of the data from the entity's financial statements, in accordance with its operations, as follows: (a) The financial position of the</p>	



	Federal Accounting Standards Advisory Board (United States of America)	Financial Reporting Manual (FRM) (UK – HM Treasury <sup>1</sup> )	Governmental Accounting Standards Board (United States of America)	International Accounting Standards Board (Private Sector)	Israel Government Accounting Standards Board	Public Sector Accounting Standards Board (CICA, Canada)
<b>Subject to Audit?</b>	Yes – required supplemental information (RSI)		Yes – required supplemental information (RSI)		above. Yes – an integral part of the financial statements	No – not part of GPFS

Narrative Reporting – Research Summary

<b>Jurisdiction</b>	Japan
<b>Body issuing pronouncement</b>	Ministry of Internal Affairs and Communications (see below)
<b>Nature and description of Pronouncement</b>	Ministry of Internal Affairs and Communications developed the mandatory guideline for annual reports prepared by agencies of central government. There are no prescribed standards or guidelines for local governments. There are no prescribed standards or guidelines for narrative reporting issued by a standard-setting body.
<b>Type of organizations in scope</b>	Japanese agencies of central government, which is called “Incorporated Administrative Agencies”, and national universities must prepare for their annual reports including “business report”, which is considered similar to “Narrative Reporting”.
<b>Main requirements of Standard</b>	For central government annual reports, the guideline states the minimum requirements of annual reports as follows: <ol style="list-style-type: none"> <li>1. Executive Summary</li> <li>2. Basic Information</li> <li>3. The Summary of Financial Statements</li> <li>4. Financial Information <ol style="list-style-type: none"> <li>(a) Overview of Financial Statements</li> <li>(b) Overview of Investments (e.g. facilities)</li> <li>(c) Overview of Budgeted Amounts and Actual Amounts</li> <li>(d) The Relationship between Reduction of Expenses and the Target of Efficiency</li> </ol> </li> <li>5. The Explanation of Outputs and Outcomes <ol style="list-style-type: none"> <li>(a) The structure of Revenues</li> <li>(b) The Explanation of Outputs and Outcomes related to the Financial Data</li> </ol> </li> </ol>
<b>Other information</b>	There are some practices where national and local governments prepare narrative explanation regarding particularly change in financial statements items. There are no prescribed standards or guidelines. Therefore, practices of local governments vary.

Narrative Reporting – Research Summary

Jurisdiction	The Netherlands
Body issuing pronouncement	Government
Nature and description of pronouncement	Provinces and Municipalities Budgets and Accounts Decree <sup>1</sup> – Section about narrative reporting
Type of organizations in scope	Provinces and municipalities
Main requirements of Standard	<p>Article 9</p> <p>1. Separate paragraphs of the budget should lay down the policies relating to relevant administrative aspects and local taxes.</p> <p>2. The budget should at least contain the following paragraphs, unless the aspect concerned is irrelevant for the respective province or municipality:</p> <ul style="list-style-type: none"> <li>(a) local taxes;</li> <li>(b) financial strength;</li> <li>(c) maintenance of capital assets;</li> <li>(d) financing;</li> <li>(e) management;</li> <li>(f) related parties;</li> <li>(g) land use policy.</li> </ul> <p>Article 10</p> <p>The paragraph on local taxes should at least contain:</p> <ul style="list-style-type: none"> <li>(a) the estimated income;</li> <li>(b) the policy with respect to local taxes;</li> <li>(c) a headline overview of the different taxes;</li> <li>(d) an indication of the local tax burden;</li> <li>(e) a description of the remission policy.</li> </ul> <p>Article 11</p> <p>1. The financial strength is determined by the relationship between:</p> <ul style="list-style-type: none"> <li>(a) the financial strength, i.e., the assets and opportunities available to the respective province or municipality to cover extrabudgetary costs;</li> </ul>

<sup>1</sup> Besluit begroting en verantwoording provincies en gemeenten

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	<p>(b) all risks that have not been provided for and that can be material in relation to the financial position.</p> <p>2. The paragraph on financial strength should at least contain: (a) an assessment of the financial strength; (b) an assessment of the risks; (c) the policy regarding the financial strength and the risks.</p> <p>Article 12</p> <p>1. The paragraph on the maintenance of capital assets should at least cover the following capital assets: (a) road; (b) sewerage; (c) water; (d) green space; (e) buildings.</p> <p>2. The following should be described in respect of the capital assets mentioned in the first paragraph: (a) the policy framework; (b) the financial consequences resulting from the policy framework; (c) the incorporation of the financial consequences in the budget.</p> <p>Article 13</p> <p>The paragraph on financing should at least describe the policy intentions regarding risk management of the financing portfolio.</p> <p>Article 14</p> <p>The paragraph on management should at least provide an insight into the current situation and the policy intentions regarding the management.</p> <p>Article 15</p> <p>The paragraph on related parties should at least contain: (a) the vision on related parties in relation to the realisation of the objectives included in the budget;</p>
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	<p>(b) the policy intentions concerning related parties.</p> <p>Article 16 The paragraph on the land policy should at least contain:</p> <ul style="list-style-type: none"><li>(a) a vision of the land policy in relation to the realisation of the objectives of the programs included in the budget;</li><li>(b) an indication of the manner in which the respective province or municipality is implementing the land use policy;</li><li>(c) a current forecast of the expected results of the total land exploitation;</li><li>(d) a substantiation of the estimated profit-taking;</li><li>(e) the policy principles regarding the reserves for land use in relation to the risks of the land use.</li></ul> <p>Article 26 The annual report should contain the paragraphs that are included in the budget in accordance with Article 9. These contain the justification of that which is included in the respective paragraphs in the budget.</p>
Other information	

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Jurisdiction	The Netherlands
Body issuing pronouncement	Government
Nature and description of pronouncement	Government Accounting Act 2001 – Central government (the Netherlands)
Type of organizations in scope	Central Government
Main requirements of Standard	Chapter V: The accountability of the State  Article 54 1. The notes to the accountability statement in any case offer insight into the following policy related issues, for each of the policy articles: a. general and if applicable more detailed operationalised goals that have been endeavoured and the extent to which they have been realised; b. instruments used to achieve the goals; ... 3. ... An annual report includes the achievement data, for each of the policy articles, which includes data on effectiveness, data on the policy efficiency, both obtained from policy evaluation surveys or not, and the efficiency data on the system expenditures, comparing this data with the estimates included in the draft budget. Remarkable differences are explained. ... Article 56 1. The notes to the accountability statement in a departmental annual report contain information on the operating procedures in the financial year of the ministry involved. ... Article 58 1. An annual report otherwise fulfils the following requirements: (a) the included financial information is reliably reflected and lawfully obtained; (b) the included information on the policy implemented and the operating procedures is reliably obtained; (c) the included information on the policy implemented and the operating procedures fulfils the related quality standards. 2. The financial information includes information on obligations, expenditures, income, revenues,

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	<p>expenses, capital expenditures, capital income and balance sheet items, as stated in the accounting records and the accompanying notes.</p> <p>3. The financial information presented in the annual report can be clearly distinguished from the non-financial information.</p> <p>... Article 61</p> <p>... 2. In any case, the Financial annual report of the State includes: <b>(a)</b> considerations about the budgetary significance of the policy implemented for the State and for other parts of the collective sector, which is considered to form the budget discipline sector; <b>(b)</b> a consideration about the operating procedures of the State;</p>
Other information	

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**Sections of New Zealand Acts which contain requirements which may be considered narrative reporting requirements:**

Central Government – Public Finance Act 1989: Sections 32A, 38 and 40 and 45

Local Government – Local Government Act 2002: Schedule 10, Part 3, Sections 15, 16 and 21

Education sector – Education Act 1989: Sections 87 and 220

Crown Entities Act 2004: Section 151

Energy Companies Act 1992: Section 44

Port Companies Act 1988: Section 16

Also: Paragraphs 38 and 40 of NZ IAS 1 (which applies to both public and private sector entities)

The wording of these sections and a link to the relevant document is included in the table below.

Item	Requirements	Comment	Link
Public Finance Act 1989	<p>Statutory Requirement: Section 38 and 40 of the PFA</p> <p>38 Departments must provide information on <b>future operating intentions</b></p> <ul style="list-style-type: none"> <li>(1) A department must, before the start of each financial year and not later than the date specified by its Responsible Minister, provide information on the department's future operating intentions.</li> <li>(2) The information must relate to the forthcoming financial year and, for the purposes of <a href="#">section 40</a>, to at least the next 2 financial years.</li> </ul>	<p>Not a financial reporting requirement but requires a narrative of the entity's <b>future</b> operations.</p> <p>The information is</p>	<p><a href="http://www.legislation.govt.nz/act/public/1989/0044/latest/DLM162408.html?search=ts_act_public+finance+act_rese&amp;page=1">http://www.legislation.govt.nz/act/public/1989/0044/latest/DLM162408.html?search=ts_act_public+finance+act_rese&amp;page=1</a></p>

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Item	Requirements	Comment	Link
	<p>40 Requirements for information on <b>future operating intentions</b></p> <ul style="list-style-type: none"> <li>• The information required under <a href="#">section 38</a> must set out and explain for the period to which it relates— <ul style="list-style-type: none"> <li>○ (a) the nature and scope of the department's functions and intended operations; and</li> <li>○ (b) the specific impacts, outcomes, or objectives that the department seeks to achieve or to contribute to through its operations; and</li> <li>○ (c) how the department intends to— <ul style="list-style-type: none"> <li>▪ (i) perform its functions and conduct its operations to achieve those impacts, outcomes, or objectives; and</li> <li>▪ (ii) effectively manage those functions and operations within a changeable operating environment; and</li> </ul> </li> <li>○ (d) the main measures and standards that the department intends to use to assess and report on matters relating to the department's future performance, including, without limitation, the following matters: <ul style="list-style-type: none"> <li>▪ (i) the impacts, outcomes, or objectives achieved or contributed to by the department (including possible unintended impacts or negative outcomes);</li> <li>▪ (ii) the cost-effectiveness of the interventions that the department delivers or administers;</li> <li>▪ (iii) the department's organisational health and capability to perform its functions and conduct its operations effectively; and</li> </ul> </li> <li>○ (e) any other matters that— <ul style="list-style-type: none"> <li>▪ (i) are reasonably necessary to achieve an</li> </ul> </li> </ul> </li> </ul>	<p>provided in a Statement of Intent” that is published with the <b>Budget</b> (this usually occurs prior to the start of the financial year).</p> <p>Treasury guidance for this report and the narrative information it contains can be found at this link <a href="http://www.treasury.govt.nz/publications/guidance/strategy/soi/content-production">http://www.treasury.govt.nz/publications/guidance/strategy/soi/content-production</a></p>	

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Item	Requirements	Comment	Link
Public Finance Act 1989	<p>understanding of the department's operating intentions and direction; or</p> <ul style="list-style-type: none"> <li>▪ (ii) may be specified by the Minister or the Responsible Minister for the purposes of subparagraph (i).</li> </ul> <p>Statutory requirement: Section 45 (2) of the PFA -</p> <p>The <b>annual report</b> must provide the information that is necessary to enable an informed assessment to be made of the department's performance during the financial year (including an assessment against the intentions, measures and standards set out at the start of the financial year in the information on the department's future operating intentions in accordance with sections 40 and 41)</p>	<p>Represents a legislative narrative reporting requirement.</p> <p>Link is to Treasury guidance for this report (including narrative requirements)</p>	<p><a href="http://www.treasury.govt.nz/publications/guidance/reporting/annualreports">http://www.treasury.govt.nz/publications/guidance/reporting/annualreports</a></p>
Public Finance Act 1989	<p>Statutory requirement: Section 32A (2) of the PFA -</p> <p>The Minister responsible for each appropriation or class of outputs must, within 3 months of the end of that financial year, prepare and present to the House of Representatives a report that complies with subsection (3).</p> <ul style="list-style-type: none"> <li>• (3) The report must include— <ul style="list-style-type: none"> <li>○ (a) a statement of service performance prepared in accordance with generally accepted accounting practice in relation to that appropriation or class of outputs that compares the service performance that was achieved with the service performance that was forecast to be achieved; or</li> </ul> </li> </ul>	<p>Represents a separate service performance reporting requirement where the <b>service is purchased by the Government, but is not delivered by a Government agency.</b></p> <p>Links are to PFA and Treasury</p>	<p><a href="http://www.legislation.govt.nz/act/public/1989/0044/latest/DLM162073.html?search=ts_act_public+finance+act_resel&amp;p=1">http://www.legislation.govt.nz/act/public/1989/0044/latest/DLM162073.html?search=ts_act_public+finance+act_resel&amp;p=1</a></p> <p><a href="http://www.treasury.govt.nz/publications/guidance/reporting/s32areports/s32a-guidance10.pdf">http://www.treasury.govt.nz/publications/guidance/reporting/s32areports/s32a-guidance10.pdf</a></p>

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Item	Requirements	Comment	Link
Local Government Act 2002 Schedule 10 Part 3	<ul style="list-style-type: none"> <li>○ (b) if the type and scope of the appropriation is such that a statement of service performance is inappropriate, a statement of the results produced or achieved in relation to that appropriation that compares those results with the results that were forecast to be produced or achieved from the expenses or capital expenditure.</li> </ul> <p>15 Group of activities</p> <ul style="list-style-type: none"> <li>• An annual report must, in relation to each group of activities of the local authority,— <ul style="list-style-type: none"> <li>○ (a) identify the activities within the group of activities; and</li> <li>○ (b) identify the community outcomes to which the group of activities primarily contributes; and</li> <li>○ (c) report the results of any measurement undertaken during the year of progress towards the achievement of those outcomes; and</li> <li>○ (d) describe any identified effects that any activity within the group of activities has had on the social, economic, environmental, or cultural well-being of the community; and</li> <li>○ (e) include an audited statement— <ul style="list-style-type: none"> <li>▪ (i) setting out a comparison between the actual levels of service provision of that group of activities and the intended levels of service provision (as set out in the long-term council community plan in respect of that year) of that group of activities; and</li> <li>▪ (ii) giving the reasons for any significant variance between the actual service provision and the expected service provision; and</li> </ul> </li> <li>○ (f) include an audited statement— <ul style="list-style-type: none"> <li>▪ (i) describing any significant acquisitions or</li> </ul> </li> </ul> </li> </ul>	<p>guidance for this report</p>	
		<p>Some parts may be more in the nature of service performance reporting</p>	<p><a href="http://www.legislation.govt.nz/act/public/2002/0084/latest/DLM176046.html?search=ts_act_local+government+act_resel&amp;page=1">http://www.legislation.govt.nz/act/public/2002/0084/latest/DLM176046.html?search=ts_act_local+government+act_resel&amp;page=1</a></p>

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	<p>replacements of assets undertaken by the local authority in the year to which the report relates; and</p> <ul style="list-style-type: none"> <li>▪ (ii) giving the reasons why the local authority acquired or replaced those assets; and</li> <li>▪ (iii) giving the reasons for any significant variation between the acquisitions and replacements projected in the long-term council community plan and those actually made.</li> </ul> <p>16 Council-controlled organisations</p> <ul style="list-style-type: none"> <li>• An annual report must include, in relation to each council-controlled organisation, – <ul style="list-style-type: none"> <li>○ (a) a report on the extent to which the local authority's significant policies and objectives in regard to ownership and control of the organisation (as set out in the relevant long-term council community plan or annual plan) have been implemented or attained in the year to which the report relates; and</li> <li>○ (b) a comparison between the nature and scope of the activities intended to be provided by the organisation in the year to which the report relates (as set out in the relevant long-term council community plan or annual plan) and the nature and scope of the activities actually provided by the organisation in that year; and</li> <li>○ (c) a comparison between actual performance and the key performance targets and other measures set out in the relevant long-term council community plan or annual plan.</li> </ul> </li> </ul> <p>Schedule 10 clause 16: amended, on 7 July 2004, by <a href="#">section 27(2)</a> of the Local Government Act 2002 Amendment Act 2004 (2004 No 63).</p>		

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Item	Requirements	Comment	Link
Education Act 1989	<p><b>21 General</b></p> <ul style="list-style-type: none"> <li>• An annual report must include a report on the activities that the local authority has undertaken in the year to establish and maintain processes to provide for opportunities for Māori to contribute to the decision-making processes of the local authority.</li> </ul> <p><b>87 Annual reports</b></p> <ul style="list-style-type: none"> <li>• (1) As soon as is practicable after the end of every financial year, and in any event no later than a day fixed by the Secretary, every board shall give the Secretary an annual report in accordance with this section.</li> <li>(2) A report given under subsection (1) must include— <ul style="list-style-type: none"> <li>○ (a) the names of all the board's elected trustees, appointed trustees, and co-opted trustees; and</li> <li>○ (b) the date on which each trustee goes out of office; and</li> <li>○ (c) the auditor's report in accordance with <a href="#">section 87A</a>; and</li> <li>○ (ca) in respect of the board or, in the case of a Crown entity group, for each Crown entity in the group,— <ul style="list-style-type: none"> <li>▪ (i) the total value of the remuneration (other than compensation and other benefits referred to in subparagraph (v)) paid or payable to the trustees in their capacity as trustees from the board (or entities in the group, as the case may be), during that financial year; and</li> <li>▪ (ii) the total value of the remuneration (other than compensation, and other benefits referred to in subparagraph (v)) paid or payable to the committee members in their capacity as committee members from the board (or entities in the group, as the case</li> </ul> </li> </ul> </li> </ul>		

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	<p>may be) during that financial year (except that this paragraph does not apply to trustees whose remuneration is disclosed under subparagraph (i)); and</p> <ul style="list-style-type: none"> <li>▪ (iii) the number of employees (other than principals of the school) to whom, during the financial year, remuneration (other than compensation and other benefits referred to in subparagraph (v)) was paid or payable in their capacity as employees, the total value of which is or exceeds \$100,000 per annum, and the number of those employees in brackets of \$10,000; and</li> <li>▪ (iv) a report, presented in the manner required by the Minister by notice in the <i>Gazette</i>, on the total remuneration (including benefits, any compensation, ex gratia payments, any other payments, and any other consideration paid or payable in the school principal's capacity as an employee) paid to a principal of the school; and</li> <li>▪ (v) the total value of any compensation or other benefits paid or payable to persons who ceased to be trustees, committee members, or employees during the financial year in relation to that cessation and the number of persons to whom all or part of that total was payable; and</li> </ul> <ul style="list-style-type: none"> <li>○ (d) the board's annual financial statements; and</li> <li>○ (e) a statement in which schools provide an analysis of any variance between the school's performance and the relevant aims, objectives, directions, priorities, or targets set out in the school charter:</li> </ul>		

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	<p>(3) The annual financial statements must be prepared in accordance with generally accepted accounting practice, audited as required by <a href="#">section 87A</a>, and include all of the following:</p> <ul style="list-style-type: none"> <li>○ (a) a statement of the financial position of the board as at its balance date;</li> <li>○ (b) a statement of financial performance reflecting the revenue and expenses of the board for the financial year;</li> <li>○ (c) if required by generally accepted accounting practice, a statement of cash flows reflecting cash flows of the board for the financial year;</li> <li>○ (d) a statement of the commitments of the board as at the balance date;</li> <li>○ (e) a statement of the contingent liabilities of the board as at the balance date;</li> <li>○ (f) a statement of accounting policies;</li> <li>○ (g) such other statements as are necessary to fairly reflect the financial operations of the board for the financial year and its financial position at the end of the financial year;</li> <li>○ (h) any other statements that the Secretary determines in consultation with the Auditor-General;</li> <li>○ (i) in relation to each statement required by paragraphs (a) to (c) and, if appropriate, by paragraph (g), budgeted figures for the financial year;</li> <li>○ (j) in relation to each statement required by paragraphs (a) to (c), paragraph (d), and paragraph (e) and, if appropriate, by paragraph (g), comparative actual figures for the previous financial year.</li> </ul> <p>(3A) In addition, a board that is a parent in a Crown entity group must, to the extent required to do so by generally accepted accounting practice, prepare consolidated financial statements in</p>		

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Item	Requirements	Comment	Link
	<p>relation to the group for that financial year.</p> <p>(4) The annual financial statements must be accompanied by a statement of responsibility that complies with <a href="#">section 155</a> of the Crown Entities Act 2004 but that is signed by the chair of the board and principal instead of 2 members.</p> <p>(5) In subsection (2), <b>trustee</b> and <b>employee</b> include a person who was a trustee or employee at any time during the applicable financial year but who is no longer a trustee or employee.</p> <p>(6) The requirements of this section and <a href="#">section 87A</a> as to annual financial statements also apply to a Crown entity subsidiary of a board as if the subsidiary were a board and with all necessary modifications.</p> <p>(7) Subsection (2)(ca)(iv) and (v) applies in respect of each financial year that ends on or after 31 December 2004.</p> <p><b>87B Report on performance of schools' sector</b></p> <ul style="list-style-type: none"> <li>• (1) The Minister of Education must in each year, not later than 30 September, prepare and present to the House of Representatives a report on the performance of the schools' sector in the immediately preceding financial year ending on 31 December.</li> <li>(2) The report must include information on —             <ul style="list-style-type: none"> <li>○ (a) the performance of the schools' sector in the supply of outputs;</li> <li>○ (b) the management performance in the schools' sector, including the quality of the management systems and practices in the schools' sector and the management of all the assets used in the schools' sector;</li> <li>○ (c) the effectiveness of the schools' sector in terms of educational achievement.</li> </ul> </li> <li>(3) The report—</li> </ul>		

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Item	Requirements	Comment	Link
Education Act 1989	<p><b>Requirements</b></p> <ul style="list-style-type: none"> <li>○ (a) must relate to all of the schools owned by the Crown; and</li> <li>○ (b) may relate to other schools</li> </ul> <p><b>Tertiary Institutions</b></p> <p><b>220 Annual report</b></p> <ul style="list-style-type: none"> <li>• (1) As soon as practicable after the end of each academic year of an institution ending after the commencement of this section the council of the institution shall give to the Minister a report on the operations of the institution during that year.</li> <li>(2) A council must include in every annual report of the council the financial statements prepared by the council, in accordance with <a href="#">section 154</a> of the Crown Entities Act 2004, in respect of the academic year to which the report relates, together with the audit report and the statement of responsibility under <a href="#">section 155</a> of that Act relating to those financial statements.</li> <li>(2AA) A council must comply with <a href="#">sections 154 to 157</a> of the Crown Entities Act 2004 except that, despite <a href="#">section 155(d)</a> of that Act, the statement of responsibility must be signed by— <ul style="list-style-type: none"> <li>○ (a) the chairperson of the council and the chief executive of the institution; or</li> <li>○ (b) if there is no chairperson, the chief executive of the institution and the chief financial officer.</li> </ul> </li> <li>(2A) A council shall include in every annual report— <ul style="list-style-type: none"> <li>○ (a) a summary of its equal employment opportunities programme for the year to which the report relates; and</li> <li>○ (b) an account of the extent to which the council was able,</li> </ul> </li> </ul>		<p><a href="http://www.legislation.govt.nz/act/public/1989/0080/latest/DLM184698.html?search=ts_act_education+act_rese&amp;p=1">http://www.legislation.govt.nz/act/public/1989/0080/latest/DLM184698.html?search=ts_act_education+act_rese&amp;p=1</a></p>

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	<p>during the year to which the report relates, to meet the equal employment opportunities programme for that year; and</p> <ul style="list-style-type: none"> <li>○ (c) an account of the extent to which the council has eliminated unnecessary barriers to the progress of students; and</li> <li>○ (d) an account of the extent to which the council has avoided the creation of unnecessary barriers to the progress of students; and</li> <li>○ (e) an account of the extent to which the council has developed programmes to attract students from groups in the community— <ul style="list-style-type: none"> <li>▪ (i) under-represented in the institution's student body; or</li> <li>▪ (ii) disadvantaged in terms of their ability to attend the institution; and</li> </ul> </li> <li>○ (f) in the case of an institution that has a plan, a statement of service performance for that financial year reporting on the performance of the institution as compared with the proposed outcomes described in that plan</li> </ul>		
<p>Crown Entities Act 2004</p>	<p>151 Form and content of annual report</p> <ul style="list-style-type: none"> <li>• (1) An annual report must contain the following information and reports in respect of the financial year to which it relates: <ul style="list-style-type: none"> <li>○ (a) information on operations that complies with subsection (2); and</li> <li>○ (b) a statement of service performance in accordance with <a href="#">section 153</a>; and</li> </ul> </li> </ul>	<p>Treasury Guidance setting out what is expected and/or required of Crown entities in preparing their annual reports</p>	<p><a href="http://www.legislation.govt.nz/act/public/2004/0115/latest/DLM330553.html?search=ts_act_crown+entities+act_resel&amp;p">http://www.legislation.govt.nz/act/public/2004/0115/latest/DLM330553.html?search=ts_act_crown+entities+act_resel&amp;p</a></p>

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Item	Requirements	Comment	Link
	<ul style="list-style-type: none"> <li>○ (c) the annual financial statements for the entity and, if the entity is the parent of a Crown entity group, the consolidated financial statements for the group in accordance with <a href="#">section 154</a>; and</li> <li>○ (d) a statement of responsibility in accordance with <a href="#">section 155</a>; and</li> <li>○ (e) the audit report in accordance with <a href="#">section 156</a>; and</li> <li>○ (f) any direction given to the entity by a Minister in writing under any enactment during that financial year; and</li> <li>○ (g) information on compliance with its obligation to be a good employer (including its equal employment opportunities programme); and</li> <li>○ (h) information required by <a href="#">section 152</a> (which relates to payments in respect of members, committee members, and employees during that financial year); and</li> <li>○ (i) information required by <a href="#">section 20(3)</a> (which relates to the enforcement of certain natural person transactions); and</li> <li>○ (j) information required by <a href="#">section 68(6)</a> (which relates to permission to act despite being interested in a matter); and</li> <li>○ (k) any matters that relate to or affect the entity's operations that the entity is otherwise required, or has undertaken, or wishes to report on in its annual report.</li> </ul> <p>(2) The annual report must provide the information that is necessary to enable an informed assessment to be made of the entity's operations and performance for that financial year, including an assessment against the intentions, measures, and standards set out in the statement of intent prepared at the beginning of the financial year.</p> <p>(3) An annual report must be in writing, be dated, and be signed on</p>	<p>in accordance with the Crown Entities Act 2004</p> <p><a href="http://www.treasury.govt.nz/publications/guidance/reporting/annualreports-early">http://www.treasury.govt.nz/publications/guidance/reporting/annualreports-early</a></p> <p>Guidance</p>	<p><a href="#">=1</a></p>

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Item	Requirements	Comment	Link
<p>Energy Companies Act 1992</p>	<p>behalf of the board by 2 members or, in the case of a corporation sole, by the sole member.</p> <p><b>44 Reports and accounts</b></p> <ul style="list-style-type: none"> <li>• (1) Within 3 months after the end of the first half of each financial year of an energy company, the directorate of the energy company shall deliver to the shareholders a report of the company's operations during that half-year.</li> <li>(2) Each report required by subsection (1) of this section shall include the information required by the statement of corporate intent to be included therein.</li> <li>(3) Within 3 months after the end of each financial year of an energy company, the directorate shall deliver to the shareholders— <ul style="list-style-type: none"> <li>○ (a) A report of the operations of the energy company and those of its subsidiaries (if any) during the financial year; and</li> <li>○ (b) Audited consolidated financial statements for that financial year in respect of the energy company and its subsidiaries (if any); and</li> <li>○ (c) The auditor's report on— <ul style="list-style-type: none"> <li>▪ (i) Those financial statements; and</li> <li>▪ (ii) The performance targets and other measures by which performance has been judged in relation to the objectives.</li> </ul> </li> </ul> </li> <li>(4) Every report under subsection (3)(a) of this section shall— <ul style="list-style-type: none"> <li>○ (a) Contain such information as is necessary to enable an informed assessment of the operations of the energy company and its subsidiaries (if any), including a comparison of the performance of the energy company and its subsidiaries (if any) with any relevant statement of corporate intent; and</li> </ul> </li> </ul>		<p><a href="http://www.legislation.govt.nz/act/public/1992/0056/latest/DLM267769.html?search=ts_act_energy+companies+act_rese&amp;p=1">http://www.legislation.govt.nz/act/public/1992/0056/latest/DLM267769.html?search=ts_act_energy+companies+act_rese&amp;p=1</a></p>

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Item	Requirements	Comment	Link
<p>Port Companies Act 1988</p>	<p>○ (b) State the maximum dividend (if any) recommended to be payable by the energy company in respect of its equity securities (other than fixed interest securities) for the financial year to which the report relates.</p> <p>16 Reports and accounts</p> <ul style="list-style-type: none"> <li>• (1) Within 2 months after the end of the first half of each financial year of a port company, the directorate of the port company shall deliver to the shareholders and the Minister a report of its operations during that half-year.</li> <li>(2) Each report required by subsection (1) of this section shall include the information required by the statement of corporate intent to be included therein.</li> <li>(3) Within 3 months after the end of each financial year of a port company or such longer period as the Minister may allow, the directorate of the port company shall deliver to the shareholders and the Minister— <ul style="list-style-type: none"> <li>○ (a) A report of the operations of the port company and those of its subsidiaries during that financial year; and</li> <li>○ (b) Audited consolidated financial statements for that financial year consisting of— <ul style="list-style-type: none"> <li>▪ (i) Statements of financial position, profit and loss, and cash flows; and</li> <li>▪ (ii) Such other statements as may be necessary to show the financial position of the port company and its subsidiaries and the financial results of their operations during that financial year; and</li> </ul> </li> <li>○ (c) The auditor's report on those financial statements.</li> </ul> </li> <li>(4) Every report under subsection (3)(a) of this section shall— <ul style="list-style-type: none"> <li>○ (a) Contain such information as is necessary to enable an</li> </ul> </li> </ul>		<p><a href="http://www.legislation.govt.nz/act/public/1988/0091/latest/DLM132162.html?search=ts+act+Port+companies+Act+reel&amp;p=1">http://www.legislation.govt.nz/act/public/1988/0091/latest/DLM132162.html?search=ts+act+Port+companies+Act+reel&amp;p=1</a></p>

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Item	Requirements	Comment	Link
<p>NZ IAS 1 <i>Presentation of Financial Statements</i></p>	<p>informed assessment of the operations of the port company and its subsidiaries, including a comparison of the performance of the port company and subsidiaries with any relevant statement of corporate intent; and</p> <ul style="list-style-type: none"> <li>○ (b) State the maximum dividend (if any) recommended to be payable by the port company in respect of its equity securities (other than fixed interest securities) for the financial year to which the report relates.</li> </ul> <p>Comparative information</p> <p>38 Except when NZ IFRSs permit or require otherwise, an entity shall disclose comparative information in respect of the previous period for all amounts reported in the current period's financial statements. An entity shall include comparative information for narrative and descriptive information when it is relevant to an understanding of the current period's financial statements.</p> <p>40 In some cases, narrative information provided in the financial statements for the previous period(s) continues to be relevant in the current period. For example, an entity discloses in the current period details of a legal dispute whose outcome was uncertain at the end of the immediately preceding reporting period and that is yet to be resolved. Users benefit from information that the uncertainty existed at the end of the immediately preceding reporting period, and about the steps that have been taken during the period to resolve the uncertainty.</p>	<p>This standard applies to both public and private sector entities</p>	<p><a href="http://www.nzica.co.nz/AM/Template.cfm?Section=NZEIFRS_2010_Volume_files&amp;Template=/CM/ContentDisplay.cfm&amp;ContentID=18650">http://www.nzica.co.nz/AM/Template.cfm?Section=NZEIFRS_2010_Volume_files&amp;Template=/CM/ContentDisplay.cfm&amp;ContentID=18650</a></p>
<p>New Zealand Institute</p>	<p>The Annual Report Awards are designed to encourage excellence in</p>	<p>Two links shown: the</p>	<p><a href="http://www.nzica.co">http://www.nzica.co</a></p>

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Item	Requirements	Comment	Link
<p>of Chartered Accountants Awards</p>	<p>the presentation of information in annual reporting.</p> <p>The Awards are open to every organisation that produces an annual report, with entrants ranging from multinational companies to small community groups. The judges take into account the size, complexity and sophistication of each entrant as well as the resources it has available.</p> <p>The Judges' comments on the 2009 awards discuss the criteria against which the reports were assessed.</p>	<p>first is for the judges' comments 2009.</p> <p>The second is for the reports of the 2008 award winners. Winners include a number of public sector entities. 2009 award winner reports are not in the NZICA website but can be obtained if required.</p>	<p><a href="http://www.nzica.co.nz/AM/Template.cfm?Section=Leadership_Awards&amp;Template=/CM/ContentDisplay.cfm&amp;ContentID=16806">m/AM/Template.cfm?Section=Leadership_Awards&amp;Template=/CM/ContentDisplay.cfm&amp;ContentID=16806</a></p> <p><a href="http://www.nzica.co.nz/AM/Template.cfm?Section=Awardsand_Scholarships&amp;Template=/CM/ContentDisplay.cfm&amp;ContentID=8313">http://www.nzica.co.nz/AM/Template.cfm?Section=Awardsand_Scholarships&amp;Template=/CM/ContentDisplay.cfm&amp;ContentID=8313</a></p>

## Narrative Reporting – Research Summary

### NARRATIVE REPORTING IN THE SOUTH AFRICAN PUBLIC SECTOR

#### Purpose and scope

The purpose of this document is to outline the requirements and practices of public sector entities in South Africa with regards to narrative reporting. “Public sector entities” include national and provincial departments, government entities/agencies and local government (including municipalities and municipal entities). Government business enterprises have been excluded from this document.

#### Background

Narrative reports have been prepared for a number of years either in accordance with:

- Legislation (or similar) such as the Public Finance Management Act (and its accompanying Regulations) or Municipal Finance Management Act (and its accompanying Regulations and Circulars) which requires the preparation of specific reports; or
- A “Code”, such as the King Code on Corporate Governance<sup>2</sup>, or practice that has evolved over time (for example, drawing on best practice reporting in the private sector).

While no formal standard or guideline exists regarding the form and contents of narrative reports, the National Treasury has issued some literature which broadly outlines the suggested contents of such reports at the various levels of government. This document outlines the requirement to prepare such reports at the various levels of government and whether any guidance exists.

#### National and provincial departments

National and provincial departments are required to prepare an annual report in accordance with section 40(1)(d) of the Public Finance Management Act (PFMA) (see attachment 1). Further to this, section 18.3 of the Treasury Regulations (see attachment 2) requires that the following information should be included in the annual report.

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<sup>2</sup> The King Code on Corporate Governance is issued by the Institute of Directors of South Africa ([www.iodesa.co.za](http://www.iodesa.co.za)).

The Code is not mandatory for any entities, but is widely applied in both the public and private sector. In the public sector, many government entities/agencies have adopted King II. It is expected that many will adopt the new revised Code (King III) in the future.

The Code deals with, for example, the reporting on assurance, remuneration and sustainability (economic and environmental).

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### S18.3 of the Treasury Regulations

In preparing the annual report of an institution, the accounting officer must –

- a. in the case of a department or trading entity, comply with the requirements prescribed in Chapter 1, Part III J of the *Public Service Regulations, 2001 (provided as attachment 3)*;
- b. include information about the institution's efficiency, economy and effectiveness in delivering programmes and achieving its objectives and outcomes against the measures and indicators set out in any strategic plan for the year under consideration;
- c. include information on transfers and subsidies per organisation for the entire financial year as well as a report on compliance with section 38(1)(j) of the Act;
- d. include all information required in terms of the annual Division of Revenue Act;
- e. include any additional information required by Parliament or the provincial legislature;
- f. report on the use of foreign aid assistance, detailing the source and intended use of the assistance (including the value of any aid-in-kind in rand), performance information on the institution's use of the assistance, and any pending applications for assistance;
- g. a report from the audit committee as required by paragraph 3.1.13; and
- h. include information on the management of PPP agreements as required by paragraph 16.7.1(f).

The Office of the Accountant-General at the National Treasury has issued specific guidelines regarding the annual report and the accounting officer's report (**see attachments 4 and 5**<sup>3</sup>). The guidance issued by the National Treasury forms part of Departmental Reporting Framework/Guide issued annually.

In general, the guidance issued by the National Treasury outlines that the following topics should be included in the Accounting Officer's Report (many of the requirements outlined in section 18.3 of the Treasury Regulations are discussed in the Accounting Officer's Report, with additional information being presented in separate reports):

- General review of the state of financial affairs.
- Services rendered by the Department.
- Capacity constraints or considerations.
- Utilisation of donor funds.
- Trading entities and public entities that have been established and report to the Department.
- Organisations to whom transfer payments made.
- Public Private Partnership arrangements.
- Corporate governance arrangements (further information often provided in a separate report, e.g. report from the audit committee).
- Discontinued or new activities.
- Asset management (including inventory management).

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<sup>3</sup> These documents are available on <http://oag.treasury.gov.za> (Click on Publications – Annual Financial Statements)

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- Events after the reporting date.
- Reporting against pre-determined objectives (performance reporting) (additional information provided in a separate report).
- Resolutions issued by the Standing Committee on Public Accounts (SCOPA).
- Modified audit opinions.

The annual report of the National Treasury has been included as an example of the reports prepared by departments ([see attachment 6](#)).

### Public entities

Similar to departments, public entities are also required by the PFMA to prepare annual reports (see section 55(1)(d)). Further to this, section 28.2.2 of the Treasury Regulations outlines certain information that should be included in the annual report.

#### Section 28.2.2 of the Treasury Regulations

Particulars of the public entity's strategic objectives and outcomes as identified and agreed on by the executive authority, the key performance measures and indicators for assessing the entity's performance in delivering the desired outcomes and objectives and the entity's actual performance against the strategic objectives and outcomes, must be disclosed in the annual report of the public entity.

Unlike with the departments, the National Treasury does not issue any guidelines on what information should be included in either the annual report or the report of the Accounting Authority (governing body, council or similar of the entity). Much of the reporting by public entities is driven by good practice, and is often influenced by the reporting in private sector entities (see the King Code on Corporate Governance II and III). As there is no clear guidance provided, the information included in the annual reports may vary from entity to entity. In general though, the annual report and/or accounting authority's report include a discussion of:

- Financial affairs
- Achievement of objectives (more specific information provided in a separate report)
- Operational issues (funding, human resource issues, compliance with legislation, including health and safety).
- Governance (including a report from the audit committee, environmental issues/sustainability which is relatively new, if done at all).

The annual report of the ASB has been included as an example of the type of information that is reported ([see attachment 7](#)).

### Local government (municipalities)

Section 121 of the Municipal Finance Management Act ([see attachment 8](#)) requires the preparation of annual report, and specifies the information that must be included in the annual report.

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#### Section 121 of the MFMA

- (1) Every municipality and every municipal entity must for each financial year prepare an annual report in accordance with this Chapter. The council of a municipality must within nine months after the end of a financial year deal with the annual report of the municipality and of any municipal entity under the municipality's sole or shared control in accordance with section 129.
- (2) The purpose of an annual report is—
  - (a) to provide a record of the activities of the municipality or municipal entity during the financial year to which the report relates;
  - (b) to provide a report on performance against the budget of the municipality or municipal entity for that financial year; and
  - (c) to promote accountability to the local community for the decisions made throughout the year by the municipality or municipal entity.
- (3) The annual report of a municipality must include—
  - (a) the annual financial statements of the municipality, and in addition, if section 122(2) applies, consolidated annual financial statements, as submitted to the Auditor-General for audit in terms of section 126(1);
  - (b) the Auditor-General's audit report in terms of section 126(3) on those financial statements;
  - (c) the annual performance report of the municipality prepared by the municipality in terms of section 46 of the Municipal Systems Act;
  - (d) the Auditor-General's audit report in terms of section 45(b) of the Municipal Systems Act;
  - (e) an assessment by the municipality's accounting officer of any arrears on municipal taxes and service charges;
  - (f) an assessment by the municipality's accounting officer of the municipality's performance against the measurable performance objectives referred to in section 17(3)(b) for revenue collection from each revenue source and for each vote in the municipality's approved budget for the relevant financial year;
  - (g) particulars of any corrective action taken or to be taken in response to issues raised in the audit reports referred to in paragraphs (b) and (d);
  - (h) any explanations that may be necessary to clarify issues in connection with the financial statements;
  - (i) any information as determined by the municipality;
  - (j) any recommendations of the municipality's audit committee; and
  - (k) any other information as may be prescribed.
- (4) The annual report of a municipal entity must include—
  - (a) the annual financial statements of the entity, as submitted to the Auditor-General for audit in terms of section 126(2);
  - (b) the Auditor-General's audit report in terms of section 126(3) on those financial statements;
  - (c) an assessment by the entity's accounting officer of any arrears on municipal taxes and service charges;
  - (d) an assessment by the entity's accounting officer of the entity's performance against any measurable performance objectives set in terms of the service delivery agreement or other agreement between the entity and its parent municipality;
  - (e) particulars of any corrective action taken or to be taken in response to issues raised in the audit report referred to in paragraph (b);
  - (f) any information as determined by the entity or its parent municipality;
  - (g) any recommendations of the audit committee of the entity or of its parent municipality; and
  - (h) any other information as may be prescribed.

Guidance has been issued by the National Treasury on certain aspects of the annual report in MFMA Circular 11 ([see attachment 9](#)).

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A link has been provided to the annual report of the City of Joburg for an example of the type of reports reproduced ([http://www.joburg.org.za/annual\\_report](http://www.joburg.org.za/annual_report)).