

EFRAG  
35 Square de Meeûs  
B-1000 Brussels  
Belgium

Secretariaat:  
Antonio Vivaldistraat 2-8, 1083 GR Amsterdam  
Postbus 7984, 1008 AD Amsterdam

T +31(0)20 301 02 35  
F +31(0)20 301 03 02  
rj@rjnet.nl  
www.rjnet.nl

**Our ref :** EFRAG-571 C

**Direct dial :** Tel.: (+31) 20 301 0391

**Date :** Amsterdam, 30 May 2014

**Re :** Comment Letter on Research Paper ‘The role of the business model in financial statements’

Dear members of EFRAG,

The Dutch Accounting Standards Board (DASB) appreciates the opportunity to respond to your Research Paper ‘The role of the business model in financial reporting’ published in December 2013.

In general, we support your view that the business model should play a role in financial reporting and therefore be addressed in the conceptual framework. In many cases, the existing concepts in the framework should be sufficient for standard setting. However, adding the notion of the business model in the framework as one of the concepts may be helpful in those cases where different business models should result in different accounting outcomes. Including the business model concept in the framework guarantees that, if relevant, this concept is considered explicitly and systematically by the IASB when addressing a specific accounting issue in the standard-setting process. The IASB should explain in the basis for conclusions how they have considered the business model concept when developing a standard. We believe that including the business model concept in financial reporting will generally result in more useful information that represents faithfully the economic reality and increases comparability.

In the appendix we respond to the questions raised in the Research Paper.

We recommend to use the feedback received on this Research Paper to draft a position paper which can be addressed to the IASB.

If you wish to discuss our comments further, please do not hesitate to contact me.

Yours sincerely,



Hans de Munnik  
Chairman Dutch Accounting Standards Board

Enclosed: Response to questions in EFRAG’s Research Paper ‘The role of the business model in financial statements’

## Appendix

### Question 1 - Implicit use of the business model

Chapter 2 discusses the explicit use of the term ‘business model’ in IFRS. The chapter also includes implicit examples of earlier use of the business model.

(a) Do you support the analysis of the implicit examples in IFRS? Please explain.

*No, we believe that the examples relating to IAS 17 and IFRIC 13 are not very good examples of the business model implicitly used in financial reporting. Regarding these examples we agree that there is some relationship between the accounting to be applied and a business model. In these examples the accounting is based primarily on the specific facts and circumstances of a transaction. We agree with the analysis relating to commodity broker-traders (IAS 2), investment property (IAS 40) and operating segments (IFRS 8).*

(b) Are you aware of additional implicit examples in IFRS?

*Yes. We believe that the provisions in IFRS 10 relating to investment entities are implicitly based on the business model of investment entities. We also believe that the classification of assets as current or non-current is partly based on the business model (‘it expects to realise the asset, or intends to sell or consume it, in its normal operating cycle, it holds the asset primarily for the purpose of trading’). In addition, the presentation of cash flows in the cash flow statement is also based implicitly on the business model (‘An entity presents its cash flows from operating, investing and financing activities in a manner which is most appropriate to its business’).*

### Question 2 - Cash conversion cycle

Chapter 3 discusses the assumed meaning of the business model, including an analysis of the cash conversion cycle.

(a) Do you agree with the analysis of the cash conversion cycle? Please explain.

*We believe that the business model is a broader concept than the cash conversion cycle. The meaning of business models should focus on the manner how an entity creates value (‘value creation’). However, we agree that the cash conversion cycle could help to understand the value creation. As a result it can help to determine a business model and the links of the different attributes of a business model. We also refer to the business model guidance included in the International Integrated Reporting Framework. We believe that using the same concepts of a business model could help to improve the linkage between financial reporting and other forms of reporting.*

(b) Are there any other attributes to add?

*We also suggest to consider the definition of a business in IFRS 3 Business Combinations. In addition, we believe that the following attributes of a business model could help to differentiate one business model from another to justify different accounting:*

- *manner of value creation;*
- *the types of markets and customers for the outputs;*
- *the risks and rewards related to the business;*
- *the key resources and their configuration;*
- *the operational processes;*
- *how management monitors the entity's operations;*
- *the policies;*
- *the way the business is organised (organisational form); and*
- *how an entity will be competitive.*

### **Question 3 – Examples**

Chapter 3 also includes examples of business models and raises recognition and measurement issues for each example with alternative views.

#### **Question 3.1 - Banking example**

(a) Do you think the example describes different business models? Please explain.

*Yes. Entity A creates value by providing loans to customers and holding these loans to collect the cash flows. Entity B creates value by providing loans to customers and subsequently selling these loans to other financial institutions.*

(b) Do you support View A or View B? Please explain.

*View A. We believe that the accounting in the financial statements should align with the different business models. The accounting by entity B should focus on the fair value of the loans provided to customers. Fair value of these loans provides relevant information about the value creation and future cash flows. This is completely different for entity A. Entity A should not measure the loans provided to customers at fair value because entity A holds these loans and will not sell these loans. Therefore, the accounting for fair value movements of these loans results in less relevant information because entity A will not sell these loans to realise these fair value movements.*

(c) If the different activities of Entity A and Entity B were both conducted in the same entity, would your answer to the above question be different? If so, why?

*No, provided that these different activities ('business models') can be clearly separated within the entity.*

### **Question 3.2 - Mobile network operator example**

(a) Do you think the example describes different business models? Please explain.

*No. We do not believe that entity A and entity B have substantially different business models. Although they use different distribution channels, we believe that both entities create value in a similar way. We expect that the following attributes will be more or less similar:*

- *manner of value creation and cash conversion;*
- *the types of markets and customers for the outputs;*
- *the risks and rewards related to the business;*
- *the key resources and their configuration;*
- *the operational processes;*
- *how management monitors the entity's operations;*
- *the policies; and*
- *how the entities will be competitive.*

(b) Do you support View A or View B? Please explain.

*View B. The similarities between these entities should make it possible that both entities recognise an intangible asset (for the right to recover acquisition costs) and amortise it on a systematic basis consistent with the pattern of expected subscription cash flows.*

(c) If the different sales channels of Entity A and Entity B were both conducted in the same entity, would your answer to the above question be different? If so, why?

*No.*

### **Question 3.3 - Insurance example**

(a) Do you think the example describes different business models? Please explain.

*Yes. We do believe that entity A and entity B have substantially different business models. We expect that the following attributes will be different:*

- *manner of value creation and cash conversion;*
- *the types of markets and customers for the outputs;*
- *the risks and rewards related to the business;*
- *how management monitors the entity's operations; and*
- *how the entities will be competitive.*

(b) Do you support View A or View B? Please explain.

*View A. The accounting should be aligned to the different business models. Accounting by these entities based on the business model should give insights in the way an entity generates or preserves value over the longer term.*

- (c) If both insurance products of Entity A and Entity B were provided by the same entity, would your answer to the above question be different? If so, why?

*No, provided that these different activities can be clearly separated within the entity.*

#### **Question 4 - Playing a role in financial reporting**

Chapter 4 discusses the conceptual debate as to whether the business model should play a role in financial statements. The Bulletin includes a tentative view that the business model should play a role in financial reporting, including financial statements, and asked whether constituents support that view.

Do you have any additional comments?

*We support the view that the business model should play a role in financial reporting. Although we believe that in some situations it will be difficult to make a clear distinction between the business model and management intent, we believe that in general it will be possible to make a distinction between these notions. The business model has a strong relationship with the business objectives and strategy of an entity i.e. how an entity is creating added value for customers resulting in cash flows. The business model gives insights in the way an entity generates or preserves value over the longer term. The business models tend to focus on the bigger (more stable) picture and require less documentation to make them verifiable. Therefore, it will be possible to verify the business model as a real economic phenomenon.*

*We have the following additional comments:*

- *We support your view that the business model should be addressed in the conceptual framework. In many cases, the existing concepts in the framework should be sufficient for standard setting, however adding the notion of the business model as one of the concepts in the framework may be helpful in those cases where different business models should result in different accounting outcomes. Including the business model concept in the framework guarantees that, if relevant, this concept is considered explicitly and systematically by the IASB when addressing a specific accounting issue in the standard-setting process. We would like to emphasize that the IASB should explain in the basis for conclusions how they have considered the business model concept when developing a standard.*
- *The Research Paper states that ‘verifiability is important, but is, in our view a precondition to be met when the conclusion would be there is a role for the business model in financial reporting, and is therefore not further considered here’. Arguments against a role for the business model in financial reporting focus on difficulties to verify the distinction between business model and management intent resulting in a lack of comparability and misuse by management. Addressing verifiability more prominently could help to address these counterarguments.*
- *More attention should be paid to address situations in which more than one business model exists within one entity. The manner of presentation and accompanied disclosures should explain clearly what these different business models are and why the accounting is different*

*for these business models. These narrative disclosures should help users of financial statements to understand the different business models within an entity and the performance of the related activities.*

- *We recommend to place more emphasis on non-financial institutions by including more examples of business models within non-financials.*
- *We recommend to use the feedback received on this Research Paper to draft a position paper which can be addressed to the IASB.*

## **Question 5 - Criteria for use of the business model**

Chapter 5 discusses the implications of the business model in IFRS and proposes criteria to be used in the *Conceptual Framework* to identify when the business model might be used in accounting standards. The chapter also proposes principles for identifying business models in those accounting standards.

- (a) Do you agree that criteria should be included in the Framework to provide a more systematic approach for accounting standard setters to consider the business model?

*Yes. We believe that the Framework should include criteria to provide a more systematic approach for accounting standard setters to consider the business model. Not including such criteria results in an inherent risk that the role of the business model is not always considered.*

- (b) If so, do you agree with the suggested criteria?

*Yes. We believe that the key characteristics mentioned in the Research Paper can help to identify business models within an entity ('activities of a business, cash flow generation and value creation, configuration of assets, customers of the products and services, role of risk'). We agree that the cash flow generation and value creation are the most relevant characteristics of a business model.*

- (c) Are there additional criteria that should be included? Please explain.

*Yes. We believe that verifiability should also be a criterion in deciding if the business model should play a role in financial reporting. We believe that a discussion about the role of the business model in financial reporting should explicitly address verifiability.*

## **Question 6 - Implications of the business model**

The Bulletin proposes some implications to IFRS and asks whether constituents support the implications to the IFRS literature.

Do you have any additional comments?

*We believe that the notion of the business model as basis for reporting financial information should be incorporated in the Conceptual Framework. Understanding different business models could help the IASB to choose the measurement basis for items in the balance sheet. It also could help the IASB to address issues relating to recognition and derecognition, presentation and disclosures.*