



The role of the business model in financial statements  
European Financial Reporting Advisory Group  
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Dear Sir/Madam,

In the present letter ICAC answers the questions raised on EFRAG, ANC and FRC document: "The role of the business model in financial statements".

**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.

ICAC mostly agrees with the implicit examples identified in the paper.

We agree with the implementation of the business model in IAS 17, it allows to distinguish business models consisting on financing and operating leases, and to apply different and appropriated accounting treatments. Another solution would not provide the true picture of economic reality.

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

Activation of research and development expenses and plant, equipment and investment in progress are manifestations of capital investment and long-term business models where costs incurred in the performance are prior to profits and requires a singular accounting treatment.

**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.



In our view, the definition of the business model must meet all the variables related to the usefulness of financial information for investors i.e. the aspects that really affect the relevance and reliability of information. In this sense, the basic information the investor needs to know refers to the risk and return on his investment.

Any specific accounting treatment to improve the relevance and reliability of financial information, providing the true and fair view of the entity, in terms of profitability and risk exposure, is justified enough to be applied.

The justification of a specific accounting treatment in a standard should be based on criteria set out in the Framework and address to determine:

- Which variables affect the profitability and investment risk of economic operation. That is the same as to determine the basic characteristics of the concept of business model, and
- When to enter that specific accounting treatment, i.e., which elements, criteria for recognition, measurement and presentation must be applied to obtain a more relevant and reliable financial information. This issue is addressed in the response 5.

The variables declared in the document as the basic concept of business model are appropriate in our opinion, and we think that it is necessary to include in the conceptual framework.

**(b) Are there any other attributes to add?**

The information required by the investor, effectively deals with the profitability and risk of their investment. However, it is also of interest to check that, once invested their money in a particular business model, it is managed according to the risk and return preferences expressed by them. It is well understood that the business model should encompass a broad vision to collect what is called management intent i.e., how to manage can also vary the profitability and risk of a business model. That is why the investor needs to know also the effectiveness and efficiency of management.

**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.**



In ICAC's view, the examples may refer to two different business models since the economic realities of the two entities are not equal. Resources are used in different ways to generate cash flow and profitability and investment risks are influenced.

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

The question of the appropriate accounting treatment, justified by the existence of different business models, must be used consistently with this document by analysis to be performed by the application of the indicators proposed to be included in the conceptual framework. Therefore, it is understood that this analysis is beyond the scope of this document.

**(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.

**Question 3.2 - Mobile network operator example**

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

The example presented can portrait, in principle, different business models since the use of resources is different to produce cash flows. However, as it is said before, that can or cannot justify the inclusion of a specific accounting treatment so that the analysis should not be limited to that, performed so briefly in the document of EFRAG.

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

The question of the appropriate accounting treatment, justified by the existence of different business models, must be analyzed, consistent with what is proposed in the paper, by applying the indicators to be included in the conceptual framework. Therefore, it is understood that this analysis is beyond the scope of this document.

**(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.**

In ICAC's view, the example shows completely different business models which, however, may not require different accounting treatments. Everything will depend on the implications of these business models in economic reality and what would be the best way to represent it in financial reports. This analysis should be the subject of a separate document.

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

The question of the appropriate accounting treatment, justified by the existence of different business models, must be analyzed, consistent with what is proposed in the paper, by applying the indicators to be included in the conceptual framework. Therefore, it is understood that this analysis is beyond the scope of this document.

**(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.

#### **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?**

In ICAC's view, the business model is a concept which plays an important role in the economic reality and therefore, it should be included in the financial statements with appropriate accounting treatment to increase the relevance and reliability of financial information.

#### **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?**



As mentioned in the answer 3, regarding the question of the business model, the scope of the conceptual framework should include:

- What variables affect the economic operation profitability and investment risk? That is, to determine the basic characteristics of the concept of business model, issue addressed in Question 3
- When to enter a specific accounting treatment and which treatment would be i.e. which elements, recognition criteria, measurement and presentation must be applied to obtain a more relevant and reliable financial information.

On this issue, our view coincides generally with the criteria set out in section 5.7 of the document, as indicators of what the accounting treatment to be reflected in a specific standard for financial information to shape the fair representation of economic reality of the business model.

However, the ICAC preferred that the indicators to be included in the Conceptual Framework would be referred to the relevance and reliability of financial reporting and its features of comprehensiveness, neutral and free from error. Thus, the specific rule must submit justification of the chosen accounting treatment and its influence on these characteristics of the information gained from the implementation of the standard.

Madrid, June 4<sup>th</sup> 2014

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Chairman of ICAC