

EFRAG
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B-1000 Brussels
Belgium

commentletters@efrag.org

30 May 2014

Dear Sir or Madam,

EFRAG/ ANC/ FRC consultation - The Role of the Business Model in Financial Statements Research Paper

Introduction

We are the Quoted Companies Alliance, the independent membership organisation that champions the interests of small to mid-size quoted companies. Their individual market capitalisations tend to be below £500m.

The Quoted Companies Alliance is a founder member of European **Issuers**, which represents over 9,000 quoted companies in fourteen European countries.

The Quoted Companies Alliance Financial Reporting Expert Group has examined your proposals and advised on this response. A list of members of the Expert Group is at Appendix A.

Response

We welcome the opportunity to respond to this consultation.

We agree that the use of the business model could play a useful role in financial reporting, allowing for greater openness which should improve the relationship between investors and management. We note that criteria should be included in the IASB's Conceptual Framework to provide a more understandable and consistent approach for accounting standard setters to consider the business model and to allow preparers to prepare comparable statements which users can understand at a general level and formulate decisions thereon. We also note that clear guidelines are necessary regarding the reporting of the attributes of the cash conversion cycle. Any application of this approach should only be introduced after a detailed cost-benefit analysis has been conducted bearing in mind the impact on small and mid-size quoted companies.

Please find below our responses to the specific questions.

Responses to specific questions

Question 1 – Implicit use of the Business Model

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

The Quoted Companies Alliance is the independent membership organisation that champions the interests of small to mid-size quoted companies.

Overall we support the analysis of the implicit examples in IFRS. The examples highlight where differing “business models” require the adoption of differing accounting policies over certain areas of the financial statements in order to present fairly to users the substance of the transactions undertaken so that they can then make informed judgments concerning the financial position and performance of the business and the impact that management have had, through their decisions, on them. For example, IFRS 8 allows users to understand how the decision makers of the business identify the key business segments within a business and allocate resources in order to maximise returns. This is important as it provides users with an understanding of the management’s aims and also highlights areas of underperformance, therefore challenging management as to whether certain components of the overall business model are not operating effectively.

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

We are not aware of any additional implicit examples in IFRS.

Question 2 – Cash conversion cycle

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

Overall we agree with the analysis of the cash conversion cycle and the six attributes included appear to cover the core components of a cash conversion cycle. However, we note that there would need to be clear guidelines as how these attributes would be reported to ensure consistency amongst preparers, otherwise comparability will be lost.

b) Are there any other attributes to add?

We consider that it would be useful to identify within the cash conversion cycle those costs that are fixed and variable in nature. This would allow users to compare cost bases between entities and also, on a period by period basis, assess how these costs are managed to maximise returns.

Question 3.1 – Banking Example

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

We consider that the examples describe different business models. They represent different ways of generating cash for the same core asset base which have arisen from decisions management have made concerning what process they consider best to generate returns.

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

Overall we support View A, as different business models would require differing accounting treatments in order to reflect the differing methods adopted. This would then allow for clear comparability amongst entities who have adopted the same approach. We do note that this may hinder comparability between entities who have adopted a differing model but consider that an investor would be able to make an informed decision about which method they considered most appropriate.

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?

Overall, we consider that our view would be consistent with that stated above. We believe that the two differing approaches would be managed separately within the bank and reported separately, and therefore represent differing business models that management are implementing. We do note that this may increase disclosure with the differing approaches requiring explanation, but consider that it would provide enhanced disclosure for users and make it easier for them to make their investment decisions.

Question 3.2 – Mobile network operator example

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

We consider that the examples describe different business models. They represent different ways of generating cash for the same core asset base which have arisen from decisions management have made concerning what process they consider best to generate returns.

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

Overall we support View A, as different business models would require differing accounting treatments in order to reflect the differing methods adopted. This would then allow for clear comparability amongst entities who have adopted the same approach. We do note that this may hinder comparability between entities who have adopted a differing model but consider that an investor would be able to make an informed decision about which method they considered most appropriate.

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?

Overall, we consider that our view would be consistent with that stated above. We believe that the two differing approaches would be managed separately within the mobile operator and reported separately, and therefore represent differing business models that management are implementing. We do note that this may increase disclosure with the differing approaches requiring explanation, but consider that it would provide enhanced disclosure for users and make it easier for them to make their investment decisions.

Question 3.3 – Insurance example

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

We consider that the examples describe different business models. They represent different ways of generating cash for the same core asset base which have arisen from decisions management have made concerning what process they consider best to generate returns.

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

Overall we support View A, as different business models would require differing accounting treatments in order to reflect the differing methods adopted. This would then allow for clear comparability amongst entities who have adopted the same approach. We do note that this may hinder comparability between entities who have adopted a differing model but consider that an investor would be able to make an informed decision about which method they considered most appropriate.

- 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?*

Overall, we consider that our view would be consistent with that stated above. We believe that the two differing approaches would be managed separately within the insurance provider and reported separately, and therefore represent differing business models that management are implementing. We do note that this may increase disclosure with the differing approaches requiring explanation, but consider that it would provide enhanced disclosure for users and make it easier for them to make their investment decisions.

Question 4 – Playing a role in financial reporting

- a) *Do you have any additional comments?*

We consider that, if appropriately defined, the use of the business model would play a useful role in financial reporting. It would allow greater clarity on management performance and allow investors to evaluate management to a greater degree. Investors would therefore be able to challenge management more regarding how the decisions they have made concerning how to run the business have been beneficial to it and to generate returns. This should allow for greater openness which should improve the relationship between investors and management.

Question 5 – Criteria for use of the business model

- 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?*

We agree that criteria should be included within the Conceptual Framework. This approach is required for consistency and to allow preparers to prepare comparable statements which users can understand at a general level and formulate decisions thereon. In addition, criteria will allow for ease of stewardship as guidelines will be in place for preparers to follow. Without criteria there runs the risk of there being too many permutations which confuse all stakeholders and reduce relevancy.

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

We agree with the suggested criteria.

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

We believe that criteria for when a business model is changed should play a role and be considered by accounting standard setters. This is important as it will then allow for improved assessment by users as to how successful changes in management (both in terms of personnel and direction) have had an impact on a business.

Question 6 – Implications of the business model

- a) *Do you have any additional comments?*

Overall we support the implications to the IFRS literature and welcome the various practical solutions suggested for managing the identified issues. Our comment in relation to the matter is the requirement to define the term “business model”, which we believe is required to ensure comprehensibility and

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comparability. Without a clear definition, stewardship becomes increasingly difficult and there is an increased risk of manipulation which would reduce the effectiveness of the proposals.

If you would like to discuss our response in more detail, we would be happy to attend a meeting.

Yours faithfully,

A handwritten signature in blue ink, appearing to read 'TW', with a horizontal line extending to the right.

Tim Ward

Chief Executive

Quoted Companies Alliance Financial Reporting Expert Group

Matthew Stallabrass (Chairman)	Crowe Clark Whitehill LLP
Joseph Archer	Crowe Clark Whitehill LLP
Edward Beale	Western Selection Plc
Anthony Carey	Mazars LLP
Ian Davies	Vislink PLC
Jack Easton	UHY Hacker Young
Bill Farren/Ian Smith	Deloitte LLP
David Gray	DHG Management
Matthew Howells	Smith & Williamson Limited
Shalini Kashyap	EY
Jonathan Lowe/Paul Watts/Nick Winters	Baker Tilly
Niraj Patel	Saffery Champness
Nigel Smethers	One Media IP Group plc
Chris Smith	Grant Thornton UK LLP