

STAFF PAPER

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IASB Meeting

Project	Conceptual Framework		
Paper topic	Feedback investment	summary—Business activities	and long-term
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Purpose of paper

1. This paper summarises the feedback received on the discussion of business activities and long-term investment in the Exposure Draft *Conceptual Framework for Financial Reporting*.
2. This paper provides a high-level summary of the comments received. Where appropriate, we will provide a more detailed breakdown of the comments for future meetings.

Summary of key messages

3. In summary:

Business activities

- (a) Almost all of those respondents who commented on the proposals agreed that the way in which an entity conducts its business has a role to play in financial reporting. However, those respondents expressed different views on how overarching that role should be and how much guidance should be included in the *Conceptual Framework*. Roughly one-half of the respondents who commented on the topic broadly agreed with the proposals

in the Exposure Draft. Others asked the Board to give more prominence to the notions of business activities or business model in the *Conceptual Framework*.

- (b) Many respondents did not seem to make a distinction between the terms ‘business model’ and ‘business activities’. Others expressed a preference for a particular term or asked the Board to clarify whether it intended to ascribe different meanings to those terms.

Long-term investment

- (c) Many of those respondents who commented on long-term investment broadly agreed with the Board’s approach in the *Conceptual Framework*, ie that the *Conceptual Framework* contains sufficient discussion for the Board:
 - (i) to make appropriate Standard-setting decisions on measurement and presentation of long-term investments; and
 - (ii) to address appropriately the needs of long-term investors.
- (d) Some respondents agreed with the general direction of the Board’s approach, but suggested that particular areas of the *Conceptual Framework* should be developed further.
- (e) Some respondents did not think that the *Conceptual Framework* as proposed contains sufficient and appropriate discussion to address the information needs of long-term investors and/or to assist the Board in making appropriate Standard-setting decisions on long-term investment (or financing).

Structure of paper

- 4. This paper is structured as follows:
 - (a) Business activities (paragraphs 5-12)
 - (b) Long-term investment (paragraphs 13-24)

Business activities

Exposure Draft proposals

5. In developing the Exposure Draft, the Board formed the view that the nature of an entity's business activities plays different roles in different aspects of financial reporting. Accordingly, the Exposure Draft did not include a general discussion on the role of a business model in financial reporting, but discussed how the way in which an entity conducts its business activities may affect:
 - (a) the unit of account;
 - (b) measurement; and
 - (c) presentation and disclosure, including how to classify assets, liabilities and items of equity, income and expenses. Classification of items of income and expenses includes determining whether to include them in other comprehensive income (OCI) instead of in the statement of profit or loss.
6. The Board did not identify any situations in which consideration of an entity's business activities would be relevant to the recognition of assets and liabilities and noted that it is performing further research on the distinction between liabilities and equity.
7. The Exposure Draft did not use the term 'business model' because this term is used with different meanings by various organisations.

Summary of feedback

Terminology

8. Many respondents who commented on the proposals did not make comments about the terminology. However, they used different terms in their responses. Some respondents used the term 'business activities', while others used the term 'business model'. Some respondents used the terms 'business model' and 'business activities' interchangeably.
9. Some respondents commented on the terms 'business model' and 'business activities'. Of those respondents:

- (a) Some respondents preferred the term ‘business model’. Those respondents also tended to think that the *Conceptual Framework* should provide more guidance on the role of the business model in financial reporting.
- (b) A few respondents supported the use of the term ‘business activities’ in the *Conceptual Framework*. Those respondents tended to agree with the proposals in the Exposure Draft.
- (c) A few respondents asked the Board to clarify whether it ascribes different meanings to the terms ‘business model’ and ‘business activities’ and recommended that the Board should use consistent terminology to avoid confusion. In particular, they noted that IFRS 9 *Financial Instruments* uses the term ‘business model’ and were not clear whether the Board means something different by the term ‘business activities’ in the Exposure Draft.

Role of business activities in financial reporting

10. Almost all respondents of those who commented on the proposals agreed that the way in which an entity conducts its business has a role to play in financial reporting. However, a few respondents did not support including a discussion of business activities in the revised *Conceptual Framework*. Those respondents expressed the following views:

- (a) Consideration of business activities in Standard-setting may impair the comparability of financial statements. Identical transactions should be treated in the same way, irrespective of the entity type or its business model. Although entity-specific information is of great interest to users of financial statements, such information is best placed outside financial statements, for example, in management commentary.
- (b) Consideration of business activities is a Standards-level detail and should not be included in the *Conceptual Framework*.
- (c) Interested parties have diverse views on what ‘business model’ or ‘business activities’ mean and how these notions should be reflected in Standard-setting. It is therefore necessary to conduct further research on those topics and it is premature to include a discussion about business activities in the *Conceptual Framework* at this stage.

11. Roughly one-half of the respondents broadly agreed that business activities should be considered in some, but not all, aspects of Standard-setting and broadly supported the proposals in the Exposure Draft. Some of those respondents also provided the following comments:
- (a) Business activities is one factor that should be considered by the Board in setting Standards and other factors are equally or more important.
 - (b) Business activities have a greater role to play in particular aspects of Standard-setting such as measurement (in particular, avoiding accounting mismatches) or presentation of income or expenses in the statement of profit or loss or other comprehensive income.
 - (c) The way in which an entity conducts its business has implications for both relevance and faithful representation of information in financial statements.
 - (d) It would be useful to include in the *Conceptual Framework* additional guidance on how business activities or business model should be taken into account in Standard-setting.
 - (e) Consideration of business activities in Standard-setting is consistent with the notion of stewardship being a part of the objective of financial reporting.
 - (f) Research and debate around the notions of business activities and business model should continue.
12. Other respondents generally thought that the *Conceptual Framework* should give more prominence to the notions of business model or business activities. In particular, they provided the following comments:
- (a) The *Conceptual Framework* should include a general discussion of the business model and provide guidance on how an entity's business model should be considered in Standard-setting.
 - (b) The business model should be considered in all aspects of Standard-setting and should be embedded in the *Conceptual Framework* as an overarching principle.

- (c) Consideration of the business model is essential in providing useful information and achieving the objective of financial reporting, notably providing information that is useful in assessing stewardship. Accordingly, a discussion of the business model should be included in Chapters 1 and 2 of the *Conceptual Framework*.
- (d) The business model does not only affect Standard-setting decisions on unit of account, measurement and presentation. It also has a role to play in other areas such as recognition and the distinction between liabilities and equity.
- (e) The business model should play a greater role in Standard-setting than other considerations such as the characteristics of an asset or liability.

Long-term investment

Exposure Draft proposals (BCIN.35-BCIN.44)

- 13. The Exposure Draft did not include a specific discussion about:
 - (a) long-term investment (or financing) *by* the reporting entity, or
 - (b) the information needs of long-term investors *in* the reporting entity.
- 14. However, the Basis for Conclusions on the Exposure Draft included a discussion of the implications of long-term investment for Standard-setting. That discussion stated that:
 - (a) the proposals in the Exposure Draft provide sufficient tools for the Board to make appropriate Standard-setting decisions if future projects consider:
 - (i) how to measure the long-term investments (or liabilities) of entities whose business activities include long-term investment; or
 - (ii) whether such entities should report changes in the carrying amount of those investments (or liabilities) in the statement of profit or loss or other comprehensive income.
 - (b) the *Conceptual Framework* contains sufficient and appropriate discussion of primary users and their information needs, and the objective of general

purpose financial reporting, to address appropriately the needs of long-term investors.

15. The Board noted that:
 - (a) referring explicitly to any particular business activity would, inappropriately, embed Standards-level detail in the *Conceptual Framework*;
 - (b) the proposed changes to the objective of financial reporting clarify the need to provide information that helps investors to assess management's stewardship of the entity's resources;
 - (c) the Board's decisions (including decisions on measurement) are driven by an assessment of what information would be useful to all investors; and
 - (d) it is not the role of accounting Standards to encourage or discourage investments that have particular characteristics.

16. The Invitation to Comment on the Exposure Draft asked respondents whether they agree with the Board's conclusions on long-term investment.

Summary of feedback

17. Just under one-half of respondents commented on long-term investment. Many of them agreed with the Board's proposed approach. In particular, most standard-setters, accounting firms, accountancy bodies and regulators who commented on long-term investment agreed with the Board's proposed approach. Some of them commented on, and specifically stated their support for, both aspects of the discussion, ie that the *Conceptual Framework* contains sufficient discussion for the Board:
 - (a) to make appropriate standard-setting decisions on measurement and presentation of long-term investments; and
 - (b) to address appropriately the needs of long-term investors.

18. Other respondents focussed their comments on one of those aspects of the discussion.

19. Respondents who supported the Board's proposed approach provided the following comments about investors' information needs:

- (a) as long as the objective of financial reporting is met, the needs of both long-term and short-term investors will be met. There is no bias in the *Conceptual Framework* towards the needs of short-term investors.
 - (b) there is no evidence to suggest that information needs of long-term investors are different from information needs of short-term investors. Any additional information needs of long-term investors can be met via providing additional disclosure.
20. Respondents who supported the Board’s proposed approach provided the following comments about a long-term investment business model:
- (a) the *Conceptual Framework* should not identify any particular type of business activity or business model. That would be embedding Standards-level detail in the *Conceptual Framework*. Besides, long-term investments can be undertaken with different objectives and the Board should be careful not to identify long-term investment as a business model or business activity in its own right.
 - (b) it is very difficult, if not impossible, to determine which entities are more long-term- and which are more short-term-oriented. Allowing management to deem some activities as long-term and account for them differently would create an opportunity for potential manipulation.
 - (c) it is not the case that current value measurement, or reporting changes in current values of assets and liabilities in the statement of profit or loss, is not appropriate for long-term investments. On the contrary, current value provides better information about the asset’s capacity to generate cash flows and a better indication of the return on investment and assists in assessing stewardship. If historical cost is permitted for long-term investments, disclosure of current values should be required.
21. A few of those respondents also emphasised that it is not the role of accounting Standards to facilitate any particular type of investment. Accounting Standards play their role by facilitating transparent financial reporting.
22. Some respondents supported the general direction of the Board’s approach but provided the following comments:

- (a) it is not appropriate or necessary for the *Conceptual Framework* to specifically discuss long-term investments. However, to assist the Board in making Standard-setting decisions on long-term investments:
 - (i) particular areas of the *Conceptual Framework* should be developed further, for example recognition, measurement or presentation of information about financial performance, or
 - (ii) stewardship or the business model should be given more prominence in the *Conceptual Framework*.
 - (b) The Board should consider setting out accounting requirements for long-term investments (and financing) using the guidance provided in the revised *Conceptual Framework*. In particular, the Board should revisit the appropriateness of:
 - (i) using current values for measurement of long-term investments (or financing), in particular those that are subject to significant foreign currency exchange rate fluctuations, or
 - (ii) reporting changes in current values of such long-term investments (or financing) in the statement of profit or loss.
 - (c) It would be helpful to acknowledge in the *Conceptual Framework* that long-term investment may warrant special consideration by the Board in setting Standards—even though that would probably result in a different accounting outcome in only a limited number of cases.
23. Some respondents did not support the Board’s approach. They provided the following comments:
- (a) the *Conceptual Framework* should discuss the long-term investment business model or at least establish a more explicit commitment for the Board to consider such a business model in setting Standards. The *Conceptual Framework* as proposed does not contain sufficient guidance to address the needs of the long-term investment business model.
 - (b) Current value measurement, and in particular reporting changes in current values in the statement of profit or loss, do not provide relevant information about long-term investment (or financing). Where current value measurement is required for such items, changes in current values should be

included in OCI and subsequently recycled to the statement of profit or loss. The *Conceptual Framework* as proposed could result in long-term investments being measured at fair value through profit or loss.

- (c) The information needs of long-term investors are different from the information needs of short-term investors. For example, long-term investors are more interested in assessing stewardship and less interested in short-term market fluctuations. They need information that is as free from measurement and outcome uncertainty as possible. The *Conceptual Framework* should at least acknowledge the different information needs of different categories of investors.
24. A few respondents expressed support for one aspect of the Board’s approach but not the other. For example:
- (a) one respondent, a standard-setter, agreed that as long as the objective of financial reporting is met, information needs of all types of users will be met. However, they did not think that the *Conceptual Framework* as proposed would provide sufficient guidance on how to reflect long-term investment business models.
 - (b) one respondent, an accounting firm, agreed that the *Conceptual Framework* provides sufficient tools to enable the Board to make appropriate Standard-setting decisions, including for the long-term investment business model. However, they did not agree that the *Conceptual Framework* contains sufficient and appropriate discussion of primary users and their information needs to address appropriately the needs of long-term investors. They suggested that long-term equity investors (as opposed to short-term ‘speculators’) need information on a ‘per share’ basis for the elements of financial statements.