



Enhancing financial reporting: The contribution of business models



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ABSTRACT

The term business model has recently entered discussions on how it might be possible to improve the information content of financial statements. It has done so as part of the rejuvenation of an earlier debate about moving from a corporate reporting to a business reporting model of external reporting. Despite a flurry of interest and exploration about how financial reporting might be enhanced following the publication of the Jenkins Report, the accountancy profession found itself confronted with other, more pressing problems. Current interest in business models marks a return to these earlier concerns. The paper provides further background to the business model concept, as well identifying a number of examples of frameworks capable of illustrating the dynamics of a business model, emphasising their links with the visualisation of value creation and delivery within organisations, viewed as the basis for enhancing financial reporting.

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1. Introduction

In a recent paper in this journal Beattie and Smith draw together the greater part of the literature that has emerged during the past few years considering the contribution that business models might make to the development of business reporting (Beattie & Smith, 2013). The link Beattie and Smith make with current interest in integrated reporting is evidence that there is valuable mileage in exploring a wide ranging literature on business models, much of which remains outwith the purview of financial reporting, something also acknowledged by Beattie and Smith. Their decision to argue for particular attention to be afforded the relationship between intellectual capital, value creation and business models is useful to progressing the debate. It is also significant that the previous debate about business reporting, to which Beattie was an influential contributor (ICAS, 1999), in some part focused attention on both intellectual capital, sometimes in the guise of intangibles, and value creation, although this may have been forgotten to some degree in the interim.

The purpose of the present paper is to respond to a growing number of calls from accounting bodies such as the IASB and EFRAG to explore the business model literature, initially by means of a more detailed discussion of the business model concept as a preface to a review of several examples of frameworks for visualising business model frameworks that appear to hold out promise for progressing business reporting. In contrast to Beattie and Smith, the principal focus here is on value creation and value delivery, rather than intellectual capital. This said, intellectual capital is never far away from the actual

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discussion, since as Beattie and Smith report, intellectual capital is now regarded in some quarters, including OECD and the World Bank, as the most important type of capital (Beattie & Smith, 2013: 244). One of the most interesting observations contained in the paper is that three of the examples of business models that are identified and discussed already have a presence within the accounting and finance literature, as well as the management literature. That their locus might be more within the tradition of managerial accounting rather than financial reporting is not without significance. Overall this paper reinforces the view that business model thinking should be enrolled in promoting integrated reporting or more radical approaches to business reporting, as an enhanced approach to financial reporting.

The paper is organised as follows. In the following section the main elements of the value creation perspective are discussed in order to establish how the successful value creation for and delivery to customers provides the focal point for business model thinking. Section 3 begins by discussing a number of the meanings associated with business model concept before briefly identifying the Business Model Canvas as a widely employed example of business model thinking. The remainder of the section provides brief overviews of three further examples of frameworks capable of representing business models, all of which have some presence within the accounting and finance literature. The fourth section explores several of the issues associated with combining business models and financial reporting. In the concluding section the focus shifts to the difficulties that some of those who presently commend the exploration and incorporation of business model thinking face from wide sections of a profession weaned on the primacy of shareholder value and jurisdictional exclusivity.

2. The value creation perspective

The generic process of creating value is very familiar within accounting and finance, in contrast to the concept of value creation, which has only relatively recently become part of the accounting and finance vocabulary. The concept originates outside of accounting and finance as part of the conceptual framework associated with Porter's competitive advantage theory of strategic management (Porter, 1980, 1985, 1996). For Porter the challenge of accomplishing value creation is what calls into existence the value chain, in the form of unique configurations of value adding activities that organisations assemble in the pursuit of sustained competitive advantage. Organisations are required to continuously ensure the efficient and effective use of their stocks of resources, *inter alia* by addressing or ultimately removing any non value adding activities from their value chains. Insights on how this might be pursued are provided in Porter's strategic cost analysis technique (Porter, 1985, chapter 6).

This very brief description of value creation is probably better known within managerial accounting, particularly in the context of Shank and Govindarajan's strategic cost management framework (Shank, 1989; Shank & Govindarajan, 1992, 1993), with strong resonances also evident in connection with activity-based management (Kaplan & Cooper, 1998) and target costing/cost management (Cooper & Slagmulder, 1997). All three contributions to managerial accounting can be characterised as attempting to develop a form of managerial accounting that merits the designation 'strategic'. Parallel and subsequent developments within strategic management accounting, e.g. by Bromwich and Bhimani (1989, 1994) and Roslender and Hart (2002a,b, 2003) are similarly heavily informed by the value creation concept, as a result of which they qualify as attempts to account for value creation. Linking value creation with managerial accounting in this way is important because managerial accounting's defining attribute is its future orientation. This ought to be immediately evident in all of the developments identified in this paragraph. As a consequence, it would be more accurate to talk of accounting for future value creation, or continued or sustained value creation.

A second, equally important aspect of linking value creation and managerial accounting in this way can be identified. From the middle 1990s there has been a growing tendency to talk of value creation *and delivery* in both the managerial accounting and strategic management literature. A major reason for this is evident in contemporary marketing theory, which draws attention to the purpose of value creation – the delivery of value *to customers*. Unless it is possible to sell a product, i.e., deliver something that customers wish to buy or consume, there is no point in seeking to create value, or more specifically superior value. The emergence of market orientation (Kohli & Jaworski, 1990; Narver & Slater, 1990) and relational marketing (Gronroos, 1994; Sheth & Parvatiyar, 1995) theories from the early 1990s took as axiomatic that customers now wanted what they wanted and could no longer readily be persuaded to buy what organisations sought to sell to them (McKitterick, 1957; Webster, 1988). As a consequence, accounting for value creation is actually focused on how it might be possible to successfully and continuously create *and deliver* value to customers, whose empowerment should only be disregarded as a last resort. Porter's early distinction between cost leadership and product differentiation strategies is relevant here. Creation and delivery of value is equally applicable in the case of a value for money product or a product that is more expensive but is in line with the values of the customer. Subsequent focus on the co-creation of value reinforces the centrality of the customer within the value creation perspective (Cova & Dallı, 2009; Vargo, Maglio, & Akaka, 2008).

Embracing the value creation narrative should not be interpreted as a section of the managerial accounting sub discipline 'going native'. Initially there is no foundation to the view that the pursuit of profit has been forgotten. What is now being emphasised is that the accomplishment of profitable activity is increasingly reliant on delivering value to customers. Unless customers are prepared to buy the product, the pursuit of cost management initiatives becomes a futile exercise. This position was made explicit in the early discussions of target costing (Hiromoto, 1988, 1991; Monden & Hamada, 1991) that drew attention to how Japanese businesses adopted a very different, externally-driven logic to activity-based costing, which restricted attention to the identification of cost reductions within the organisation.

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