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Review

Is the firm's business model related to segment reporting?

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ABSTRACT

In the academic literature, several definitions of the term *business model* have been put forward since the 1990s. This article considers the business model to be the translation of certain strategic choices. Our article intentionally restricts choices to financial decisions, such as those conveyed by cash flow statement (CFS) indicators. Segment reporting standards IAS 14 and IFRS 8 should be helpful in explaining a company's business model, translated into its IAS 7 cash flow statement. The article derives a major finding from a study of 101 financial statements published by industrial and commercial companies listed on the Euronext stock index between 2005 and 2010. Segment reporting disclosure contained in the notes to these companies' financial statements does not improve our understanding of their business models, which were assessed on the basis of CFS indicators.

Contents

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1. Introduction

The term *business model* has become so popular in recent years that it now constitutes a full-fledged research topic studied in all management sciences (Gartner, 1995). The term itself is coming under greater scrutiny from the academic community (Shi and Manning, 2009), with authors agreeing that apart from a few notable exceptions, the term *business model* lacks both a theoretical foundation (Zott and Amit, 2007, 2008) and a homogenous definition (Eden and Ackermann, 2000; George and Bock, 2011). Few studies – with the exception of Chesbrough and Rosenbloom (2002), Malone et al. (2006), and Zott and Amit (2007) – have dealt with its influence on company performance (George and Bock, 2011). Some try to ascertain how easy it is to apprehend and formalize this concept (Tracey and Jarvis, 2007), whether it adapts to the characteristics of a company's external environment (Hurt and Hurt, 2005) or if it is specific to a particular model of entrepreneurship (Morris et al., 2005). In addition, most research into the business model has focused on specific industrial sectors such as biotechnology (Bigliardi et al., 2005; Nosella et al., 2005) or dot-coms (Fay, 2004; Lechner and Hummel, 2002).

Value constitutes a central aspect of business model objectives. Questions about this construct's relevance and usefulness in enhancing our understanding of a company's financial situation and performance have turned it into a priority research theme for a number of accounting regulators, starting with France's Authority for Accounting Standards. This notion of value creation is deeply embedded in the business model and is widely employed throughout economic circles. Indeed, business model literature refers very frequently to the notion of value creation or to neighboring constructs such as the ability to make money sustainably (Afuah and Tucci, 2003) or generate income (Afuah, 2004).

From a strictly financial perspective, the value generated by companies' financial choices (investment decisions, efforts to optimize their operating cash flows, etc.) can be proxied by the income that they hope to derive from future cash flows (Damodaran, 2004). Many executives rely on wealth creation measurements as analytical tools helping them to make operating decisions as well as strategic choices. Financial analysts often measure financial performance using two disclosures of the annual report or registration document: the cash flow statement and segment information, also known as segment disclosure. IAS 7 paragraph 4 emphasizes the CFS's objectivity (i.e., the fact that it is not influenced by accounting policy choices) and specifies that cash flow-related disclosure "allows comparison of information about the performance of the operation of different companies as it eliminates the effects of using different accounting treatments for the same transactions and economic events." This paragraph contains a clear reference to the fact that cash remains the best variable for comprehending the business model of a company (Cormier and Magnan, 2002).

Segment reporting standards enhance understanding of the origins of this performance by breaking it down into different zones of activity or geographic locations. Despite the fact that accounting and financial information has become increasingly detailed and constrained, firms still benefit from a certain freedom in terms of the substance of the information they can publish in the notes to their financial statements. Until accounting periods beginning on January 1, 2009, firms had to apply a fairly structured standard determining what segment disclosures were to be provided and how these were to be measured. This was IAS 14 (segment reporting), whose definition of a segment started with the application of a risk and reward approach and mandated the presentation of two types of segment analysis (primary and secondary). As IFRS converged with US GAAP and with firms given the possibility of adopting the new standard early – IFRS 8 (operating segments) was adopted and was similar to SFAS 131. There was a profound change, with the definition of segments now being driven