

Deutsches Rechnungslegungs Standards Committee e.V.

Accounting Standards Committee of Germany



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IFRS Technical Committee

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Berlin, [date] 2019

Mr Hans Hoogervorst
Chairman of the
International Accounting Standards Board
Columbus Building
7 Westferry Circus / Canary Wharf
London E14 4HD

Dear Hans,

**IASB Exposure Draft ED/2018/2 *Onerous Contracts – Cost of Fulfilling a Contract*
(Proposed amendments to IAS 37)**

On behalf of the Accounting Standards Committee of Germany (ASCG) I am writing to comment on the Exposure Draft ED/2018/2 *Onerous Contracts – Cost of Fulfilling a Contract* (Proposed amendments to IAS 37) issued by the IASB on 13 December 2018 (herein referred to as 'ED'). We appreciate the opportunity to comment on the ED.

The IASB proposes specifying the "cost of fulfilling a contract" to comprise costs that directly relate to the contract, rather than to comprise incremental costs only. We welcome the IASB's efforts to clarify the requirements in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and agree that the proposed clarification sets the basis for a common understanding of the term "cost of fulfilling a contract" and thereby counters diversity in accounting practice. Also, we agree that the directly related cost approach is preferable and provides a more faithful representation of the cost of fulfilling a contract than the incremental cost approach.

[...]

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Our detailed comments in response to the ED questions are laid out in the appendix to this letter. If you would like to discuss our comments further, please do not hesitate to contact Kristina Schwedler (schwedler@drsc.de) or me.

Yours sincerely,

Andreas Barckow
President

DRAFT

Appendix – Answers to the questions in the DP

Question 1

The IASB proposes to specify in paragraph 68 of IAS 37 that the cost of fulfilling a contract comprises the costs that relate directly to the contract (rather than only the incremental costs of the contract). The reasons for the IASB's decisions are explained in paragraphs BC16 – BC28.

Do you agree that paragraph 68 of IAS 37 should specify that the cost of fulfilling a contract comprises the costs that relate directly to the contract? If not, why not, and what alternative do you propose?

We agree. Against the backdrop that IAS 11 has been withdrawn, the application of the requirements in IFRS 15 and IAS 37 allow for different interpretations as to which cost to include in estimating the cost of fulfilling a contract. The proposed clarification encourages a common understanding of the term “cost of fulfilling a contract” and, hence, improves financial reporting by preventing diversity in accounting practice.

We also agree that in assessing whether a contract is onerous, the cost of fulfilling the contract includes both incremental costs and an allocation of other costs that relate directly to contract activities. We support the reasoning provided in paragraphs BC18 to BC23 of the ED stating that the directly related cost approach provides a more faithful representation of the cost of fulfilling a contract. Further, we do not expect that the proposed clarification will lead to significant changes in the German accounting practice as the prevailing view supports an interpretation that goes beyond the incremental costs but excludes general costs.

Notwithstanding our directional support, we recommend complementing the reasoning by a reference to the general principle of income recognition (comparison of revenue and related expenses). Accordingly, the accounting for acquisition transactions and production processes as well as construction contracts result in capitalised costs. The identification of onerous contracts should follow this principle and should, therefore, refer to the costs that are able of being capitalised.

Further, we note that the terms “directly related costs” as well as “incremental costs” are universally known and commonly used. However, in our view, the descriptions of the incremental cost approach (“includes only the costs an entity would avoid if it did not have the contract”) and the directly related cost approach (“includes all the costs an entity cannot avoid because it has the contract”) in BC16 do not make the differences between these two approaches sufficiently clear.

[...]

Question 2

The IASB proposes to add paragraphs 68A–68B which would list costs that do, and do not, relate directly to a contract.

Do you have any comments on the items listed?

Are there other examples that you think the Board should consider adding to those paragraphs? If so, please provide those examples.

We welcome that guidance be provided, and we find it helpful that examples of costs that do and do not relate directly to a contract be included. We also acknowledge that other standards (e.g. IFRS 15, IFRS 17, IAS 2, IAS 16, IAS 38 and IAS 40) contain examples of costs that are included in or excluded from the cost of an asset and that the examples now proposed are based on those in paragraphs 97-98 of IFRS 15. However, we have difficulty in seeing a coherent principle that is being followed in the examples in paragraph 68A: They overlap and leave room for further interpretation. As this is already the case when applying IFRS 15 and as we support a timely clarification of the onerous contract requirements, we encourage the IASB to consider this within a future project (e.g. the research project to review IAS 37 might be a good candidate).

[...]

Kommentar [s1]: tbd –alternativ konkrete Anmerkungen zur Anpassung des Beispielkatalogs

Question 3

Do you have any other comments on the proposed amendments?

The transitional provisions specify that an entity shall not restate comparative information. Instead, the entity shall recognise the cumulative effect of initially applying the amendments as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the date of initial application. We appreciate the IASB's objective to balance the cost an entity would incur in first applying the amendments with the usefulness of the information provided on initial application to users of financial statements. However, since a full retrospective application is the preferred method per IAS 8, we wonder why the IASB ruled out its application. We would advocate permitting a full retrospective application as an alternative, provided the necessary information is available to the entity without the use of hindsight.

[...]