

21 August 2017

IFRS Interpretations Committee  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
United Kingdom

**Comments on the Tentative Agenda Decision Relating to  
IAS 37 Provisions, Contingent Liabilities and Contingent Assets—Costs considered  
in assessing whether a contract is onerous**

1. The Accounting Standards Board of Japan (the “ASBJ”) welcomes the opportunity to comment on the IFRS Interpretation Committee’s (the “Committee”) tentative agenda decision relating to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* — Costs considered in assessing whether a contract is onerous in the June 2017 IFRIC Update.
2. We agree with the view in the Committee’s tentative agenda decision that the interpretation on unavoidable costs in the paragraph 68 of IAS 37 is not necessarily clear.
3. In our discussions, regarding whether to add this project to the Committee’s standard-setting agenda, some were sympathetic with the Committee’s tentative agenda decision stating that this project could not be solved without conducting a comprehensive review of the requirements in IAS 37 (including the various issues related to onerous contracts, for example, the definition of *onerous contracts* and *economic benefits*, and the unit of account), although providing further clarification regarding unavoidable costs may reduce diversity in practice.
4. At the same time, most were of the view that allowing two different interpretations regarding unavoidable costs would impair comparability. Assuming that the

tentative agenda decision were finalised as proposed, the following issues were raised as deep concerns:

- (a) The two interpretations regarding unavoidable costs may have existed prior to the issuance of the IFRS 15, but the difference between the two interpretations may not have been as significant as that compared with the situation where IAS 37 is applied to all contracts within the scope of IFRS 15<sup>1</sup>. The consequences of allowing two interpretations (especially in the case where an entity chooses to adopt the incremental cost approach for contracts that were previously within the scope of IAS 11, and the magnitude of the diversity arising from different interpretations) need to be carefully considered when IAS 37 is applied to all contracts within the scope of IFRS 15 in assessing whether they are onerous.
  - (b) Allowing two different interpretations and providing entities a free choice regarding the costs to be included in unavoidable costs may result in significant diversity among industries and among entities that may be affected significantly.
  - (c) There may be confusion in practice if the amount of the costs to be included in unavoidable costs would differ depending on whether the entity utilises its own employees to do the work or chooses to outsource the work to fulfill the contract.
5. Accordingly, we do not support the Committee's decision to allow two interpretations regarding unavoidable costs.
6. In our discussions, we could not reach a consensus regarding how to avoid allowing two interpretations. Nevertheless we would like to share with you the following views for the Committee's future consideration:
- (a) One approach we considered was whether to include full cost (for example, contract costs for construction contracts under IAS 11) included in unavoidable costs for all contracts within the scope of IAS 37, with the aim of achieving consistency with contracts that have been in the scope of IAS 11. However,

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<sup>1</sup> Prior to the issuance of IFRS 15, the transactions that were required to be assessed whether they were onerous in accordance with IAS 37 might have been limited (for example, firm sales contracts in excess of inventory quantities held or firm purchase contracts (paragraph 31 of IAS 2) and sub-lease contracts that are probable to incur losses) when compared to all long-term service contracts such as construction contracts. Furthermore, because the difference between the two interpretations in the tentative agenda decision relates to whether to include indirect overhead costs in the unavoidable costs, the transactions that are significantly affected by the two interpretations are those that require the calculation of manufacturing costs and that have firm sales contracts, as described above.

there was little support for this approach because the number of the contracts that are determined to be onerous is likely to increase.

- (b) Because this issue has arisen by expanding the contracts that are within the scope of IAS 37 as a result of the issuance of IFRS 15 (which replaces IAS 11), another approach we discussed was to limit the scope of clarification regarding this issue to transactions that are within the scope of IFRS 15. One advantage of this approach would be that most transactions that have been within the scope of IAS 37 prior to the issuance of IFRS 15 would not be affected.
  - (c) Yet another approach we discussed was to clarify that unavoidable costs is limited to “direct expenditure” as stated in paragraph 80 of IAS 37. One advantage of this approach would be that all contracts within the scope of IAS 37 would be treated consistently.
7. Whichever approach the Committee may choose to take, any action may change practice, depending on the nature of the entity’s transactions or the entity’s previous interpretation of unavoidable costs. Accordingly, instead of issuing an agenda decision, we believe this issue should be added to the standard-setting agenda and the Committee should issue a standard with appropriate effective dates and transition guidance.
8. We hope our comments are helpful for the Committee’s and the IASB’s consideration in the future. If you have any questions, please feel free to contact us.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Yukio Ono', with a stylized flourish at the end.

Yukio Ono  
Chairman of the Accounting Standards Board of Japan