



M A Z A R S

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

25 April 2010

Dear Sir / Madam,

Re: Comments on IASB Exposure Draft Measurement of Liabilities in IAS 37

Mazars welcomes the opportunity to comment on the Exposure Draft Measurement of Liabilities in IAS 37.

We understand that the Board is not inviting comments on aspects of the new standard that were included in the 2005 exposure draft.

However, even though we understand the Board's intent, we want to stress the fact that we have not been convinced by the Board's comments and we do not believe that the Board has properly addressed our concerns.

More specifically, in our response letter to the 2005 exposure draft, we did express our strong disagreement with the removal of the probability of outflow criteria.

We justified our disagreement by explaining that the proposal was in contradiction with the framework, that this would not provide users of financial statements with useful information, and that this would require preparers to incur additional costs for no apparent benefit.

In practice, under current IAS 37, and even though the guidance provided in this respect could be improved, it was frequent to assess globally the existence of an obligation and the probability of outflows in order to determine whether a provision should be recognized.

The working draft ("WD") posted on the IASB's website does not provide additional guidance to help preparers assess whether an obligation exists at a given date, and even suppressed the more likely than not reference existing in IAS 37 (§ 16) regarding the present obligation.

The deletion of the probability of outflow criteria puts more stress on the existence of the obligation. As a consequence, the lack of additional guidance regarding the existence of an obligation in the WD reinforced our fears.

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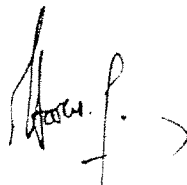
In practice, much will depend on whether the entity has an obligation. In case of lawsuits, it will require to obtain quantified information from lawyers, which may be difficult to obtain (depending on the legal environment) and which will be costly.

We also note that the working draft is not clear as to what types of provisions are in the scope of IAS 18 and what other provisions should be measured based on the guidance included in the WD. In effect, § 3 of the WD excludes liabilities whose treatment is specified by another IFRS, including IAS 18, whereas § 4 states that onerous contracts within the scope of IAS 18 should be measured according to the WD. This should be clarified before the final standard is issued.

Overall, we believe that the exposure draft, as completed by the Working Draft, will not result in better information for the users of financial statements whereas it will impose an additional burden, as well as associated costs, on preparers.

We would be pleased to discuss our comments with you and remain at your disposal should you require further clarification or additional information. Would you have any request regarding the above comments, please do not hesitate to contact Michel Barbet-Massin (+33 1 49 97 62 27).

Yours faithfully

A handwritten signature in black ink, appearing to read 'Michel Barbet-Massin', followed by a small flourish or checkmark.

Michel Barbet-Massin
Head of Accounting Principles Department

Question 1 – Overall requirements

The proposed measurement requirements are set out in paragraphs 36A–36F. Paragraphs BC2–BC11 of the Basis for Conclusions explain the Board’s reasons for these proposals. Do you support the requirements proposed in paragraphs 36A–36F? If not, with which paragraphs do you disagree, and why?

We note that the general measurement requirement set out in paragraph 36A is largely in line with the current standards (§ 36-37 of IAS 37).

However, we believe that, in the general case where the obligation will be settled by the obligation being fulfilled, whether by the entity or by a third party, the provision should be estimated at the present cost of the resources required, rather than at the present value of those resources.

Furthermore, the intense discussions within the Board itself, evidenced by the number of dissenting views, lead us to question the need for adding measurement guidance in the new standard on provisions since it appears to work reasonably well in practice.

- Risk adjustment

We are also not convinced by the rationale put forward by the Board regarding the need to take into account a risk margin when the provision is measured based on the present value of the resources required to fulfil the obligation (fulfilment value).

According to § B15, the risk adjustment measures the amount (if any) that the entity would rationally pay in excess of the expected value of the outflows to be relieved of this risk.

Given the overall measurement objective, that is the amount that an entity would rationally pay to be relieved of the present obligation, it is hard to see how the risk adjustment fits.

In effect, one could wonder if this is truly rational to somehow “overpay” to be relieved of the obligation since the entity would have to forego any positive variation.

According to the Board, the provision should be based upon a “lower of” method (§ 36B). The same logic would exclude the risk margin, since an entity would rationally decide to fulfil the obligation itself at a lower cost rather than transferring it for an amount that would include both the contractor’s margin and an adjustment for risk.

- Inclusion of additional costs

In addition, the notion of costs of cancellation or transfer should be detailed (§ 36D), and compared to the associated costs referred to in paragraph B7b. It is not clear what these costs are, and whether these costs differ from directly attributable costs.

Question 2 – Obligations fulfilled by undertaking a service

Some obligations within the scope of IAS 37 will be fulfilled by undertaking a service at a future date. Paragraph B8 of Appendix B specifies how entities should measure the future outflows required to fulfil such obligations. It proposes that the relevant outflows are the amounts that the entity would rationally pay a contractor at the future date to undertake the service on its behalf.

Paragraphs BC19–BC22 of the Basis for Conclusions explain the Board's rationale for this proposal.

Do you support the proposal in paragraph B8? If not, why not?

We disagree with the Board's proposal to measure a provision based on the present value of the resources required to fulfil the obligation when the entity does not intend to outsource the service or when no market exists for the service.

- Profit margin

We agree with the dissenting views, explaining that this would result in the entity recognizing a gain in the period where the service is provided.

We believe that a gain should only be recognized on transactions with customers, and the fulfilment of an obligation is not equivalent to an income generating transaction.

Based upon the oil production example (in § BC21), an entity would include a margin (internal hypothetical margin) not only for the dismantling obligation but also when constructing an asset for itself. This margin would correspond to the cost saved by the company by carrying out the work itself rather than employing a contractor.

Carrying this logic to its extreme, it would even be possible to include a margin relating to the production of goods. This approach would be similar to measuring inventory at fair value in the context of business combinations (purchase price allocation).

We believe that these changes to the standard will mean that provisions will henceforth be measured at an amount close to fair value and we strongly believe that this is not a faithful representation of the economic reality.

- Risk adjustment

The exposure draft requires that a risk adjustment is made when the entity cannot cancel or transfer the obligation.

As already indicated, we do not believe that a risk adjustment is justified as a principle.

In addition, in practice, no guidance is provided in the exposure draft as to how this risk adjustment should be measured.

In the illustrative example, it is assumed that “the entity estimates that it would rationally pay an additional 5 per cent to be relieved of this risk”, but no explanation is given to justify the level of this risk adjustment.



- Expected value

In the general case of obligations which are measured on the basis of the present value of the resources required to fulfil the obligation, the exposure draft requires entities to take into account the relative probabilities of the various possible outcomes.

We are not convinced that this is appropriate for single event obligations and that it provides better information than the use of a most likely outcome approach.

Also, in case of litigation, the proposed approach will require that the entity asks its lawyers for details of the various possible outcomes, even in cases where the risk is low and the entity does not expect to have to make any payment.

In practice, an entity's ability to obtain the information necessary to measure these liabilities from the lawyers in charge of the various cases will also be affected by its geographical location as obtaining this type of information may be more difficult in certain regulatory environments (starting with the US environment).

Thus, in addition to the impact on the amount of provisions recognised, this will have significant impacts at the operational level and will impose additional costs to preparers.

Overall, determining the amount of provisions is judgmental, and imposing an expected value approach in all instances will increase costs without leading to less judgment. As a consequence, we are not convinced that this will improve financial reporting.

Question 3 – Exception for onerous sales and insurance contracts

Paragraph B9 of Appendix B proposes a limited exception for onerous contracts arising from transactions within the scope of IAS 18 *Revenue* or IFRS 4 *Insurance Contracts*. The relevant future outflows would be the costs the entity expects to incur to fulfil its contractual obligations, rather than the amounts the entity would pay a contractor to fulfil them on its behalf.

Paragraphs BC23–BC27 of the Basis for Conclusions explain the reason for this exception.
Do you support the exception? If not, what would you propose instead and why?

We agree with the Board's proposal to exclude onerous contracts arising from transactions within the scope of IAS 18 or IFRS 4, pending the completion of the ongoing projects on revenue and insurance.

This limited exception would provide relief and would avoid the risk of imposing changes for a limited time, should the final decision on these projects require entities to use cost as the basis for measuring onerous contracts.

In addition, several questions related to onerous contracts could be dealt with by the Board.

For example, what costs should be taken into account ? More specifically, what level (if any) of overhead costs should / could be included ? Should all costs be included when a structure is used to run-off the contracts (without attempting to gain any new customers) ?

Another practical question relates to the level at which onerous contracts should be combined.