

Comment Letters  
IASB  
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Canary Wharf  
London E14 4HD  
United Kingdom

Paris, 15<sup>th</sup> April 2019

## Exposure Draft ED-2018-2: Onerous Contracts – Cost of Fulfilling a Contract

Dear Hans,

Mazars welcomes the opportunity to comment on the International Accounting Standards Board's Exposure Draft (hereafter ED) Onerous Contracts – Cost of Fulfilling a Contract, issued in December 2018.

Mazars agrees that IAS 37 requires clarifications regarding how to assess whether a contract has become onerous and especially regarding which costs should be considered in determining the cost of fulfilling a contract. The removal of IAS 11 on construction contracts and the coming into force of IFRS 15 have increased the number of contracts to which IAS 37 provisions regarding onerous contracts apply, leading to greater diversity in practice than the one previously observed. We thus believe it is necessary to amend IAS 37 as soon as possible and we therefore welcome the Board's initiative in that regard. Besides, we overall agree with the proposed amendments, which we believe provide the right answer on which costs to consider when assessing whether a contract is onerous.

Nevertheless, topics at least as important in the case of loss-making contracts, especially how to identify the "economic benefits expected to be received under the contract", are not dealt with by the above-mentioned Exposure Draft. Consequently, we support the research project on Provisions currently conducted by the IASB and encourage the Board to turn this research project into a standard-setting one to amend other aspects of IAS 37.



Our detailed comments to the questions raised in the Exposure Draft are set out in the Appendix.

Please do not hesitate to contact us should you want to discuss any aspect of our comment letter.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'M. Barbet-Massin', followed by a right-pointing arrow.

Michel Barbet-Massin  
*Head of Financial Reporting Technical Support*

## Appendix

### **Question 1:**

*The Board 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 Board'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?*

Yes we agree with the proposed amendment of paragraph 68 of IAS 37 since we believe taking into account the costs that relate directly to the contract in order to assess whether a contract is onerous provides a more faithful representation of the cost of fulfilling a contract than the incremental cost approach.

As mentioned in our comment letter in response to the June 2017 tentative agenda decision, we do not believe that taking into account only the incremental costs of the contract is relevant since there are costs beyond incremental costs which are however unavoidable if the entity has to fulfil its obligations as stated in the contract. In addition, we note that the Board's proposal is consistent with the definition of the costs of fulfilling a contract in IFRS 15, and we believe it is important to have a consistent definition for a similar wording throughout the standards.

Having said that, we understand that the amendment has been made necessary especially because of the recent replacement of IAS 11 on construction contracts (notably) by IFRS 15 on revenue recognition which does not include any guidance regarding onerous contracts and refers systematically to IAS 37. However, IAS 37 is applicable to other contracts than contracts with customers. For instance, it may not always be clear how to assess whether a supply contract is onerous especially when the buyer is engaged in a long-term supply contract and it is committed to purchase minimum quantities per year of contract above its operational needs.

In such a situation, we wonder if referring to the "costs that relate directly to the contract" provides sufficient guidance in order to assess whether a contract – other than a contract with a customer – is onerous.

**Question 2:**

*The Board 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 agree with the examples of costs that relate directly to a contract to provide goods or services listed under paragraph 68A, and with the guidance given under paragraph 68B relating to general and administrative costs.

We understand that the examples provided do not form an exhaustive list to which refer to. In particular, it is clearly stated that the examples only relate to contracts with customers that are within the scope of IFRS 15. Nevertheless, we are not sure that adding other examples illustrating the costs to be included in the onerous contract assessment for non-IFRS 15 contracts would add clarity to the standard.

**Question 3:**

*Do you have any other comments on the proposed amendments?*

Though we acknowledge that the proposed amendments will permit, on a timely basis considering the recent coming into force of IFRS 15, to avoid diversity in practice for contracts previously falling under the scope of IAS 11, and to solve diversity in practice observed until now for contracts previously falling under IAS 18, we note that the definition of the cost of fulfilling a contract is not the only issue in practice when it comes to assessing whether a contract is onerous.

As mentioned in our cover letter, the practical application of the onerous contract requirements in IAS 37 raises other questions that are as important as the one addressed by the above-mentioned Exposure Draft. In particular, regarding the “economic benefits expected to be received under the contract”, we wonder if they include “anticipated contracts that the entity can specifically identify” (as per IFRS 15). More broadly, the key question is how to deal with “loss leaders” contracts in certain industries such as aerospace, where an initial loss-making contract is necessary to obtain – and will generate – in the future other highly profitable contracts.

We encourage the Board to address such issue in the frame of the current research project on IAS 37 while hoping such project will be completed as soon as possible.

Besides, we agree with the transitional provisions proposed under paragraph 94A according to which a “simplified” retrospective method will have to be applied (i.e. no restatement of comparative information).