

6 March 2019

By email: commentletters@hkicpa.org.hk and By post

Ms. Christine Ng
Director
Standard Setting Department
Hong Kong Institute of Certified Public Accountants
37th Floor, Wu Chung House
213 Queen's Road East
Wanchai Hong Kong

Dear Ms. Ng

Consultation on IASB Exposure Draft ED/2018/2 Onerous Contracts - Cost of Fulfilling a Contract (Proposed Amendments to IAS 37)

Thank you for your letter of 2 January 2019 and the related Exposure Draft attached. Our comments on the specific questions raised in the Exposure Draft are set out in the enclosed annex for your consideration.

We hope you find our comments useful. Should you have any questions, please contact our Manager, Ms Emily Ngan, at 2526 6080 or our Officer, Ms. Seiki Kwok, at 2567 1363.

Yours sincerely



Boey Wong
Secretary

HKAB’s Comments on IASB Exposure Draft ED/2018/2 Onerous Contracts - Cost of Fulfilling a Contract (Proposed Amendments to IAS 37)

Seq.	Relevant Extracts	HKAB Comments
<p><u>Question 1</u></p> <p>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.</p> <p>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?</p>		
1.	<p><u>Para 68 (page 7)</u></p> <p>This Standard defines an onerous contract as a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. The cost of fulfilling a contract comprises the costs that relate directly to the contract.</p> <p><u>Para BC16 (page 13)</u></p> <p>The Board considered two approaches to determining the cost of fulfilling a contract:</p> <p>(a) the incremental cost approach—includes only the costs an entity would avoid if it did not have the contract, ie the incremental costs of the contract.</p> <p>(b) the directly related cost approach—includes all the costs an entity cannot avoid because it has the contract. Such costs include both the</p>	<p>As the terms “direct cost”, “directly attributable cost” and “incremental cost” are extensively used throughout IFRS Standards for the measurement of both financial and non-financial assets. For the sake of clarity, we recommend further defining the “directly related costs” in the IFRS Standard than the Basis for Conclusion (BC16). Hence, we suggest revising para 68 as follows:</p> <p>“[...] The cost of fulfilling a contract comprises the costs that relate directly to the contract, <u>which include both incremental costs of the contract and an allocation of other costs incurred on activities required to fulfill the contract.</u>”</p>

Seq.	Relevant Extracts	HKAB Comments
	incremental costs of the contract and an allocation of other costs incurred on activities required to fulfil the contract.	
<p><u>Question 2</u></p> <p>The Board proposes to add paragraphs 68A–68B which would list costs that do, and do not, relate directly to a contract.</p> <p>Do you have any comments on the items listed?</p> <p>Are there other examples that you think the Board should consider adding to those paragraphs? If so, please provide those examples.</p>		
		We do not have comments on the proposal.
<p><u>Question 3</u></p> <p>Do you have any other comments on the proposed amendments?</p>		
2.	<p><u>BC 25</u></p> <p>Several IFRS Standards specify the types of costs to include in the measurement of a non-monetary asset. These Standards require an entity to include both the incremental costs of purchasing or constructing the asset and any other directly related or directly attributable costs. For example:</p> <p>(a) IFRS 15 states that an entity recognises as an asset costs incurred in fulfilling a contract if they ‘relate directly’ to the contract;</p> <p>(b) IAS 2 <i>Inventories</i> states that an entity includes in the cost of inventories costs ‘directly attributable’ to the acquisition of finished goods, material and services, and costs ‘directly related’ to units of production; and</p> <p>(c) IAS 16 <i>Property, Plant and Equipment</i>, IAS 38 <i>Intangible Assets</i> and IAS 40 <i>Investment Property</i> all state that an entity includes ‘directly</p>	<p>In relation to cost of fulfilling a contract, we acknowledge that BC25 lists out several IFRS Standards which specify the types of costs to include in the measurement of a non-monetary asset, as examples to illustrate the consistency of including both the incremental costs of purchasing or constructing the asset and any other directly related or directly attributable costs in the proposed IAS 37 amendments with these Standards. However, the explanation in BC25(b) may not be precise, since para 12 of IAS 2 describes “production overheads” as “indirect” costs of production, which is also included in the measurement of inventory via systematic allocation. Please clarify.</p>

Seq.	Relevant Extracts	HKAB Comments
	attributable' costs in the cost of an item of property, plant and equipment, intangible assets and investment property.”	