



*FAR is the institute for the accountancy profession in Sweden*

Sir David Tweedie  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
England

14 November 2002

Dear Sir David,

## **Exposure Draft of Proposed Improvements to International Accounting Standards – Response Addendum**

FAR submitted a response dated 30 September 2002 to the Exposure Draft of Proposed Improvements to International Accounting Standards. Recent developments in Sweden, prompted by the issuance of a revised Swedish standard on Accounting for Inventories based entirely on IAS 2 (revised 1993), have induced us to revert to the Exposure Draft of a revised IAS 2 included in the Improvements project.

The old Swedish standard was based on E38 rather than the finalised IAS 2 (revised 1993) and, therefore, did not in all respects mirror the final IAS. Among other things, the earlier standard did not include paragraph 16 dealing with “Cost of Inventories of a Service Provider”, nor the last sentence of paragraph 5 also stating that a service provider should include with inventories costs for the service as described in paragraph 16 for which the enterprise had not yet recognised the related revenue (with a reference to IAS 18, Revenue).

The Swedish standard setter, *Redovisningsrådet* (The Swedish Financial Accounting Standards Council), is in the process of revising the Swedish standard in full compliance with IAS 2 (revised 1993), incorporating said paragraphs 5 and 16.

The Exposure Draft of a revised IAS 2 in paragraph 1 states the scope restrictions. There is no scope restriction relating to IAS 18. To FAR this seemed logical, since service contracts under IAS 18 would not generate any inventory balances. Rather, the application of the percentage of completion method set out in IAS 18 would generate, as under IAS 11, a gross amount due from customers including costs incurred plus recognised profits (disregarding, for the purpose of discussion, recognised losses and progress billings). Even if, for some reason, an enterprise cannot apply the percentage of completion method, IAS 18 in its paragraph 26 states that revenue shall then be recognised to the extent of expenses recognised that are recoverable, i.e. giving rise to a potential accrued income (receivable) rather than an inventory item, and accumulated expenses would then be charged to the P&L.

Since IAS 18 would always seem to give rise to a receivable item in the balance sheet, paragraph 16 of IAS 2 (and the last sentence of paragraph 5) should be deleted, since the two

standards would otherwise be incompatible unless one with the inventory item in paragraph 16 of IAS 2 should see the accumulation of costs of a tangible nature; if so, this should be clarified. Further, an inventory item would always as a starting point be based on cost. It would not include any unrealised profits, which a service provider applying the percentage of completion method is required to do under IAS 18. FAR does not subscribe to the revised wording of paragraph 16 in the Improvements project, i.e. the added statement that “When revenues related to services provided have not been recognised, a service provider has inventories”. As discussed above, a service provider may at best have a receivable, either including a portion of the expected profit on the contract or to the extent of recoverable costs.

If the IASB with its statements in paragraphs 5 and 16 (including the added text in the Exposure Draft included in Improvements Project) only refers to the accumulation of costs and expenses (salaries and overheads, etc) in the accounting records between two balance sheet dates, we believe that paragraph 16 should make this clear, e.g. by adding a sentence to the following effect:

”At each balance sheet date, the accumulated costs and expenses should be evaluated and charged to expense in accordance with the revenue recognition criteria set out in IAS 18, Revenue (paragraphs 20–28).”

Yours sincerely,

Carl-Eric Bohlin  
Chairman, Accounting Practices Committee of FAR

Björn Markland  
Secretary General