

STAFF PAPER

December 2018

IASB[®] Meeting

Project	Provisions
Paper topic	Project update
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Introduction

1. The International Accounting Standards Board (Board) has a pipeline of research projects it expects to become active before the next Agenda Consultation. In February 2018, the Board identified five projects that it would aim to make active first. Two of these projects—Extractive Activities and Pension Benefits that Depend on Asset Returns—became active earlier this year. A third project—Provisions—is also now active.
2. The Provisions research project is not a new project. The Board is reactivating a research project it decided in 2016 to hold in its research pipeline pending revisions to its *Conceptual Framework for Financial Reporting (Conceptual Framework)*. The Board issued the revised *Conceptual Framework* in March 2018.
3. This paper reminds the Board of the purpose of the Provisions research project and evidence already gathered on the project. The paper also informs the Board of the remaining activities planned for the project and the target timings for those activities.
4. The Board will not be asked to make any decisions at this meeting, but Board members will be invited to comment on and ask questions about the project.

Purpose of project

5. The expected output of a research project is not an Exposure Draft. The expected output is evidence to help the Board decide whether or not to add to its work plan a standard-setting project or maintenance project.
6. The purpose of the Provisions research project is to gather evidence to help the Board decide whether to add to its work plan a project to amend aspects of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

Evidence already gathered

7. The evidence already gathered in this project includes:
 - (a) an initial research summary, presented to the Board in July 2015 (see paragraphs 8–10);
 - (b) stakeholder feedback on matters discussed in the research summary, obtained in meetings during 2015 and 2016 (see paragraphs 11–13); and
 - (c) feedback from the 2015 Agenda Consultation, presented to the Board in April 2016 (see paragraphs 14–19).

Initial research summary

8. The staff presented an initial research summary to the Board at its meeting in July 2015—see [Agenda Papers 14-14C](#) for that meeting. The summary brought together staff analyses of:
 - (a) possible problems with IAS 37 identified by stakeholders and the Board; and
 - (b) ways in which concepts then being developed for the revised *Conceptual Framework* could help address these problems.
9. The main problems with IAS 37 identified in the summary included:

- (a) two different principles in IAS 37 for identifying liabilities. The staff noted that the principles appeared contradictory and had resulted in inconsistent and sometimes unsatisfactory requirements. In particular, IFRIC 21 *Levies*, an interpretation of IAS 37, had been criticised by a range of stakeholders, including users, preparers and auditors of financial statements and national standard-setters.
- (b) unclear guidance on measurement, which had resulted in diversity in practice. The staff noted diversity in:
 - (i) *the costs included in the measure of a provision*. IAS 37 does not specify whether a provision for an obligation should include only the incremental costs of fulfilling that obligation, or whether it should also include an allocation of directly related overheads. IAS 37 is also unclear about whether provisions should include costs payable to third parties, such as legal costs expected to be incurred in negotiating the settlement of a legal claim.
 - (ii) *discount rates*. IAS 37 does not specify whether the rate used to discount future cash flows should take into account the risk of non-performance by the entity, sometimes called the entity's own credit risk. Taking account of the risk of non-performance can substantially reduce the measure of long-term liabilities such as decommissioning and environmental rehabilitation obligations.

10. To identify ways in which the concepts being developed for the revised *Conceptual Framework* could help address these problems, the research summary analysed the implications for IAS 37 of the concepts proposed in the Exposure Draft *Conceptual Framework for Financial Reporting*. The staff concluded that:

- (a) the proposed concepts could be the basis of clearer general guidance on identifying liabilities. The guidance would reconcile, and could replace, seemingly contradictory statements in IAS 37. Application of the guidance could lead to requirements for levies that were different from those in IFRIC 21.

- (b) the proposed concepts could support retaining the existing recognition criteria in IAS 37.
- (c) the proposed concepts could help the Board if it decided to develop more specific measurement requirements for liabilities within the scope of IAS37. The proposed concepts suggested that the Board could:
 - (i) focus on ‘fulfilment value’ when developing measurement requirements for IAS 37; and
 - (ii) consider whether, and if so how, to customise fulfilment value to provide the most useful information about the liability and expenses, and to take into account the cost constraint. Previous stakeholder feedback suggested that if the Board were to take this approach, it might specify a measure that excluded the effects of non-performance risk (and possibly any risk adjustment) and required outflows of services to be measured at the cost of providing those services (without adding the service margin that the Board had proposed in a previous aborted project to amend IAS 37).

Stakeholder feedback on matters discussed in research summary

- 11. During 2015 and 2016, Board and staff members discussed the main points of the research summary with members of the Global Preparers Forum, Capital Markets Advisory Committee, Accounting Standards Advisory Forum and Emerging Economies Group, and with subject specialists at large accounting firms.
- 12. Meeting participants tended to say they did not have many problems applying IAS 37 in practice and so did not see a need for a fundamental review of the whole Standard. In particular, they were not in favour of changes to the existing recognition criteria, or more rigid requirements for measuring litigation liabilities.
- 13. However, some meeting participants identified specific aspects of IAS 37 (such as lack of clarity around discount rates and measurement of onerous contract provisions)

for which more guidance could improve application. And some supported changing the requirements for levies.

Feedback from 2015 Agenda Consultation

14. In August 2015, the Board published for comment the Request for Views: *2015 Agenda Consultation* (Request for Views). Among other things, the Request for Views asked for views on the relative importance and urgency of the Board’s research projects.

15. Approximately 60 of the 119 respondents to the Request for Views gave a view on the importance and urgency of the Provisions research project. Many of those respondents—including most of the users of financial statements, standard-setters, regulators and accountancy bodies expressing a view—identified the project as being of medium or high importance.

16. Of those respondents, the main suggestion was that IAS 37 should be updated to reflect the concepts then being developed for the revised *Conceptual Framework*. A few respondents specifically referred to a need to address an inconsistency between the concepts proposed for the revised *Conceptual Framework* and the requirements of IFRIC 21. A regulator argued that IFRIC 21 does not lead to relevant information in financial statements.

17. Some respondents identified the Provisions research project as being of low importance. These respondents included most of the preparers and accounting firms expressing views. They also included some (predominantly European) standard-setters and accountancy bodies. Some of the respondents said they had not encountered significant difficulties applying IAS 37 and expressed a view that IAS 37, even if not perfect, was operational in practice. There appeared to be a concern among some of those respondents, explicitly expressed by a few, that a project to amend IAS 37 could result in the removal of the ‘probable outflows’ recognition criterion.

18. A more detailed report of the feedback from the Request for Views is in [Agenda Paper 22 Research Project IAS 37 Provisions, Contingent Liabilities and Contingent Assets—Agenda Consultation Feedback](#) for the April 2016 IASB meeting.
19. Based on this feedback, the Board decided to hold the Provisions project in its research pipeline, with a view to restarting the project after it had finalised its revisions to the *Conceptual Framework*.

Planned activities

20. After the December 2018 Board meeting, the staff will update the IASB website to indicate that the Provisions research project is now active.
21. The first activity will be to update the research summary prepared in 2015. The summary needs to be updated to:
- (a) reflect the final wording of the revised *Conceptual Framework*.
 - (b) consider the possible implications of a narrow-scope maintenance project to amend the onerous contract requirements in IAS 37. Earlier this year, the IFRS Interpretations Committee identified an urgent need to specify in IAS 37 the types of costs an entity should include in assessing whether a contract is onerous. The Board is about to publish proposals for comment. There is more information about this project on the [Onerous Contracts—Cost of Fulfilling a Contract \(Amendments to IAS 37\)](#) project page on the IASB website.
 - (c) identify any possible problems with IAS 37 that have emerged or been resolved since 2015. The staff intend to consider matters referred to the IFRS Interpretations Committee in that period and seek assistance from members of the Board’s Accounting Standards Advisory Forum and subject specialists at large accounting firms.

22. The staff also intend to discuss the matters covered in the updated summary at meetings of the Global Preparers Forum and Capital Markets Advisory Committee, seeking participants’ feedback on which, if any, of these matters should be within the scope of a project to amend IAS 37.
23. The staff intend to use the updated research summary and feedback from meeting participants to develop recommendations on:
- (a) whether or not the Board should add to its work plan a standard-setting or maintenance project to amend any aspects of IAS 37;
 - (b) if so, which aspects of IAS 37 should be within the scope of the project; and
 - (c) if the Board reaches tentative decisions on these matters, whether and how the Board should consult further on these decisions—for example by publishing them in a Discussion Paper—before taking further action.

Target timings

Period	Activity
Quarter 1 2019	Updating project summary
Quarters 1–2 2019	Consulting stakeholders
Quarter 3 2019	Developing recommendations and presenting them to the Board

Question for the Board

Comments or questions
Do you have any comments or questions?