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International
Accounting Standards
Board

This observer note is provided as a convenience to observers at IFRIC meetings, to assist them in following the IFRIC's discussion. Views expressed in this document are identified by the staff as a basis for the discussion at the IFRIC meeting. This document does not represent an official position of the IFRIC. Decisions of the IFRIC are determined only after extensive deliberation and due process. IFRIC positions are set out in Interpretations.

Note: The observer note is based on the staff paper prepared for the IFRIC. Paragraph numbers correspond to paragraph numbers used in the IFRIC paper. However, because the observer note is less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

IFRIC meeting: 2 November 2006, London

Project: Review of published tentative agenda decisions

Subject: IAS 11 *Construction Contracts* – Allocation of profit in a single contract (Agenda Paper 7(xiv))

Tentative agenda decision published in September-2006 IFRIC Update

The IFRIC considered an issue identified in its deliberations of service concession arrangements, namely whether it is appropriate in a single contract to determine different profit margins for the different components of the contract.

Whilst IAS 11 *Construction Contracts* has specific criteria for contract segmentation, the guidance on segmenting in IAS 18 *Revenue* is expressed only at a general level. The IFRIC noted that in IAS 18:

- paragraph 4 states that services directly related to construction contracts are not dealt with in IAS 18 but are dealt with in IAS 11
- paragraph 13 states that in certain circumstances, it is necessary to apply the recognition criteria to the separately identifiable components of a single transaction in order to reflect the substance of the transaction.

The IFRIC noted that, whilst IAS 18 paragraph 21 refers to IAS 11, it does so only for the percentage of completion method for recognition of revenue and the associated expenses and does not refer to the combining, segmenting and disclosure requirements of IAS 11.

The IFRIC noted that, as part of its project on D20 *Customer Loyalty Programmes*, it has deliberated whether, in a single contract within the scope of IAS 18, it is appropriate to determine different profit margins for the different components of the contract. In D20, the IFRIC tentatively concluded that the requirements of IAS 18 paragraph 13 to account for separately identifiable components of a contract would require segmentation of contracts that have separately identifiable components potentially with different profit margins. D20 also proposes guidance on how to allocate the total contract revenue to the different components.

The IFRIC noted that, for a single contract for construction and other services not directly related to construction activities, IAS 18 paragraphs 4 and 13 require the contract to be separated into two components, a construction component within the scope of IAS 11 and a service component within the scope of IAS 18, in order to reflect the substance of the transaction. The IFRIC noted that the segmenting criteria of IAS 11 apply only to the progressive recognition of margin relating to the construction component and that the requirements of paragraph 13 of IAS 18 apply to the service component. The consequence is that different profit margins might be recognised on the different components of such a single contract.

The IFRIC believed that there is sufficient guidance in IAS 18, IAS 11 and D20 and [decided] not to take this item onto its agenda.



Association pour la participation des
entreprises françaises à l'harmonisation
comptable internationale



Mouvement
des Entreprises de France
MEDEF

IFRIC
30 Cannon Street
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Paris, October 18, 2006

Ref: IFRIC tentative wording for rejection “Allocation of profit in a single contract”

ACTEO & MEDEF welcome the opportunity to comment on the tentative wording for rejection issued after IFRIC’s September meeting.

The proposed motive for rejection is that the existing guidance would be sufficient to deal with the issue under consideration

We object to the proposed wording for rejection for two main reasons:

- 1- The wording for rejection takes the view that because, taken separately, different elements in the contract would meet the scope of IAS 11 while others would not, there is no economic interrelation between different components in the contract. We believe this requires judgement on a case by case basis and therefore might vary in some circumstances and not in others. Therefore the wording for rejection is likely to prevent preparers to report on their operations with the benefit of a principle based set of standards; we would favour a wording for rejection which would clearly state that the guidance provided only applies when grouping criteria detailed in IAS 11.9 or IAS 18.13 are not met. Indeed, we believe the wording for rejection is not relevant when construction and other goods or services “are so closely interrelated that they are, in effect, part of a single project with an overall profit margin” and/or they “are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole”.

- 2- The wording for rejection designates "D20", the draft interpretation on customer loyalty programmes as part of the existing IFRS literature. Draft interpretations have proven in the past to be, partially or totally, contradicted after comments received and re-deliberations. We therefore would kindly request from IFRIC that draft interpretations or standards not be considered as available references for the determination of appropriate accounting treatments; the IFRIC ought to determine whether, without D20, it believes that enough guidance is being provided by existing standards, namely by IAS 11 and IAS 18. If so, the reference to D20 should be dropped. If not, the IFRIC should let its tentative wording for rejection pending (once modified in order to take our first comment into consideration), until such time that D20 is transformed, if ever, into a final interpretation.

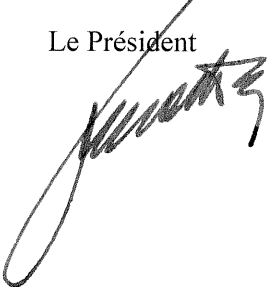
We remain at your disposal should you need further clarification or background information.

Yours sincerely,

ACTEO

Patrice MARTEAU

Le Président



MEDEF

Agnès LEPINAY

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20 October 2006

Robert Garnett, Chairman
International Financial Reporting Interpretations Committee
30 Cannon Street
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Email: ifric@iasb.org

Dear Bob,

Proposed agenda decision wording: IAS 11 *Construction Contracts* – Allocation of profit in a single contract

Deloitte Touche Tohmatsu is pleased to respond to the IFRIC's publication in the September 2006 *IFRIC Update* of the tentative decision not to take the above issue onto the IFRIC agenda with a view to developing an Interpretation.

We support the IFRIC's decision not to take this item to the agenda. We support the proposed wording for the Agenda Decision and believe that it draws out the accounting principles for a single contract that includes components for construction and other services not directly related to construction.

If you have any questions concerning our comments, please contact Ken Wild in London at +44 (0)20 7007 0907.

Sincerely,



Ken Wild
Global IFRS Leader
cc: Allan Cook, IFRIC