

STAFF PAPER

October 2019

IASB® Meeting

Project	Onerous Contracts—Cost of Fulfilling a Contract (Proposed amendments to IAS 37)		
Paper topic	Cover paper		
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Introduction and purpose

1. The International Accounting Standards Board (Board) published Exposure Draft *Onerous Contracts—Cost of Fulfilling a Contract* (Exposure Draft) in December 2018.
2. At its meeting in [September 2019](#)¹, the Board decided to proceed with its project to make a narrow-scope amendment to IAS 37 to clarify which costs an entity includes in determining the ‘cost of fulfilling’ a contract for the purpose of assessing whether that contract is onerous. The Board also decided to specify, as proposed in the Exposure Draft, that such costs comprise those that relate directly to the contract.
3. At this meeting the Board will discuss:
 - (a) Agenda Paper 12C—responses to Question 2 in the Exposure Draft. Question 2 invited comments on the proposed list of costs that do, and do not, relate directly to a contract.
 - (b) Agenda Paper 12D—other comments on the Exposure Draft proposals.
4. This paper includes background information on the development of the Exposure Draft proposals.

¹ See also [Agenda Paper 12](#) to that meeting.

Background information

5. IAS 37 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. IAS 37 also states that 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. However, IAS 37 does not specify which costs to include in determining the cost of fulfilling a contract.
6. The IFRS Interpretations Committee (Committee) received a request to clarify which costs to include in determining the cost of fulfilling a contract. In particular, the request referred to construction contracts. These contracts were previously within the scope of IAS 11 *Construction Contracts*, which included requirements for onerous construction contracts. IAS 11 has now been withdrawn and, for annual reporting periods beginning on or after 1 January 2018, an entity applies IAS 37 to assess whether such contracts are onerous. Accordingly, the Committee considered this matter urgent.
7. Research conducted by the Committee indicated that differing views on which costs to include applying IAS 37 could lead to material differences in the financial statements of entities that enter into some types of contracts.
8. In response, the Board developed proposals to clarify which costs to include and published an Exposure Draft.
9. The Exposure Draft proposed adding a sentence to paragraph 68 of IAS 37 that would state:

The cost of fulfilling a contract comprises the costs that relate directly to the contract.
10. The Exposure Draft also proposed to add a list of costs that relate directly to a contract to provide goods or services, to clarify that such costs include both:
 - (a) the incremental costs of fulfilling that particular contract; and
 - (b) an allocation of other costs that relate directly to contract activities.