THE
INSTITUTE OF
CHARTERED
ACCOUNTANTS
OF SCOTLAND

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Email: commentletter@efrag.com

19 March 2010

Dear Mr Enevoldsen

EFRAG DRAFT COMMENT LETTER: IASB EXPOSURE DRAFT 2010/1: MEASUREMENT OF LIABILITIES IN IAS 37

The Institute's Accounting Standards Committee has considered the above exposure draft and I am pleased to forward the comments we will be submitting to the IASB.

The Institute is the first incorporated professional accountancy body in the world. The Institute's Charter requires the Accounting Standards Committee to act primarily in the public interest, and our responses to consultations are therefore intended to place the general public interest first. Our Charter also requires us to represent our members' views and protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount.

The Committee does not agree with the proposals contained within this exposure draft. We believe that the use of the "best estimate" of a liability results in the most appropriate measurement. The estimate is a matter of professional judgement and may not always result in consistency between entities but this is a result of the inherent uncertainty in these liabilities. The use of probability calculations results in the creation of a fictional figure within the financial statements and does not improve the usefulness of the information. The proposal appears to be counter-intuitive and seems to be moving away from the exercise of professional judgement which is fundamental to a principles-based accounting standard.

We disagree with the decision not to re-expose the proposed standard in its entirety. The original exposure draft was issued in 2005 and since then there have been significant developments in IFRS. The exposure draft proposes fundamentally changing the measurement criteria for a liability, moving the uncertainty from recognition into the measurement. As measurement and recognition are inextricably linked it is not possible to comment properly on one without understanding the proposals for the other.

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We agree with the dissenting views of Messrs Danjou and Engström and consider that the Board should re-expose proposals which were opposed by a large number of respondents to the 2005 exposure draft.

We have chosen to respond to the specific questions posed in the exposure draft and our comments can be found in the Appendix to this letter. However, we do not consider that the Board has followed due process in this instance.

I hope our comments are useful to you. If you wish to discuss anything further please do not hesitate to contact me.

Yours sincerely

Karen Shaw

KAREN SHAW
Assistant Director, Accounting and Auditing
Secretary to the Accounting Standards Committee

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ANNEX A: RESPONSES TO SPECIFIC QUESTIONS

Question One: Overall requirements
Do you support the requirements proposed in paragraphs 36A-36F? If not, with which paragraphs do you disagree, and why?

The Committee does not support the use of an expected value approach to measurement. The use of probabilities is statistically valid over a large population of possible outcomes but liabilities under the proposed standard may have only a small number of possible outcomes. The use of expected values essentially results in the creation of a fictional number in the financial statements. It creates a false sense of accuracy and ultimately provides less relevant information for the user.

We do not agree with the proposal to add a risk margin into the calculation. The use of an expected value approach takes into account risk and therefore adding a risk margin to the provision appears to be overstating the liability.

Finally, the Committee is also concerned that these proposals offer greater scope for manipulation than the existing IAS 37. Increased measurement complexity offers more opportunity to deliberately misstate liabilities and could prove particularly difficult for auditors.

Question Two: Obligations fulfilled by undertaking a service
Do you support the proposal in paragraph B8? If not, why not?

We do not agree with the proposal in paragraph B8. If the preparer is providing the service themselves, the amount they would rationally pay to relieve themselves of the obligation would not include a profit margin. This provision assumes that the preparer is already providing the service and therefore will be able to easily estimate the profit margin - this may not always be the case.

Question Three: Exception for onerous sales and insurance contracts
Do you support the exception? If not, what would you propose instead and why?

We believe that there would be no need for an exception if the measurement of a liability is always the best estimate of the costs expected to be incurred – this is the rational approach for the measurement of all liabilities under this proposed standard and not just onerous sales and insurance contracts.

If the proposals are to be adopted, we would support the inclusion of clear application guidance on what costs should be included within the liability. One example of where problems could arise is the cost of an in-house legal department. It could be very difficult to allocate the costs of the department to individual liabilities.

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