

International Accounting Standards Board
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Submitted electronically through the IASB Internet site (www.iasb.org)

Exposure Draft ED/2010/1 *Measurement of Liabilities in IAS 37*

Grant Thornton International is pleased to comment on the International Accounting Standards Board's (the Board) Exposure Draft ED/2010/1 *Measurement of Liabilities in IAS 37* (the ED). We have considered the ED as well as the accompanying draft Basis for Conclusions.

Taken as a whole we do not support the proposals in the ED. We generally support the underlying measurement objective set out in paragraphs 36A and B of the ED, but have concerns as to the proposed requirements on its implementation. Consequently, we do not believe that the proposals (and the related Working Draft of IAS 37 published on the Board's website) would achieve an overall improvement in financial reporting.

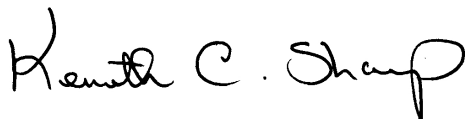
In particular, the proposals do not clearly articulate or support the requirement that the 'present value of the resources required to fulfil an obligation' should include a profit margin in all cases when the entity will provide the goods or services required to fulfil the obligation. We believe that where the entity will fulfil the obligation by supplying goods or rendering services, the resources expended should be measured by reference to cost.

Also, we disagree with the proposals relating to obligations to be fulfilled by providing a service (the proposals in B8). We are not convinced that a requirement to use contractor prices (if available) is consistent with the basic measurement objective (the amount the entity would rationally pay to be relieved of the obligation). If the entity intends to perform the service itself, it has presumably concluded rationally that this will involve a lower outflow of resources. Consequently, this should be reflected in the measurement of the liability.

We expand on these remarks and make a number of other comments and suggestions in our responses to the Invitation to Comment, set out in the Appendix to this letter.

If you have any questions on our response, or wish us to amplify our comments, please contact our Executive Director of International Financial Reporting, Andrew Watchman (andrew.watchman@gtuk.com or telephone + 44 207 391 9510).

Yours sincerely,

A handwritten signature in black ink that reads "Kenneth C. Sharp". The signature is written in a cursive style with a large initial 'K' and a distinct 'S'.

Kenneth C Sharp
Global Leader - Assurance Services
Grant Thornton International

Responses to invitation to comment questions

Question 1 - Overall requirements

The proposed measurement requirements are set out in paragraphs 36A–36F. Paragraphs BC2–BC11 of the Basis for Conclusions explain the Board’s reasons for these proposals.

Do you support the requirements proposed in paragraphs 36A–36F? If not, with which paragraphs do you disagree, and why?

In our October 2005 comment letter on the earlier ED, we supported retaining 'most likely outcome' in paragraph 40 of existing IAS 37, on practicality grounds. However, the arguments in BC1 to 18 of the ED are persuasive and we agree that the use of 'expected value' is more consistent with other IFRSs. Consequently we support the proposed requirements in paragraphs 36A-36F, except for the measurement requirements relating to the phrase 'the present value of the resources required to fulfil the obligation' (paragraph 36B(a) and paragraph 36C). We do not agree that this should include a notional profit margin (see our response to question 2 below).

Question 2 - Obligations fulfilled by undertaking a service

Some obligations within the scope of IAS 37 will be fulfilled by undertaking a service at a future date. Paragraph B8 of Appendix B specifies how entities should measure the future outflows required to fulfil such obligations. It proposes that the relevant outflows are the amounts that the entity would rationally pay a contractor at the future date to undertake the service on its behalf.

Paragraphs BC19–BC22 of the Basis for Conclusions explain the Board’s rationale for this proposal.

Do you support the proposal in paragraph B8? If not, why not?

No - we do not agree with the proposals in paragraph B8. Nor do we support the consequential argument that the present value of resources required to fulfil the obligation should include a notional profit margin whenever the entity itself provides goods and/or services to fulfil the obligation.

We are not convinced that a requirement to use contractor prices (if available) is consistent with the basic measurement objective (the amount the entity would rationally pay to be relieved of the obligation). If it is rational to use a contractor, most entities will do so and it then seems appropriate to measure the obligation on that basis. If the entity intends to perform the service itself, then it has presumably concluded that this will involve a lower outflow of resources and, in turn, this should be reflected in the measurement.

We are sympathetic to the alternative views expressed in AV2-AV4 and are not convinced by the Board’s reasoning in BC19-BC22, which seems confused. In BC21(a) the Board argues that the use of contractor prices will ensure greater discipline in using observable market prices. Although we can accept that point, we do not think this justifies a conceptually questionable rule. The general requirement to use the 'lower of' amount achieves the same objective.

We do not agree with the assertion in BC21(d) that the contractor price is effectively the amount the entity would rationally pay. This assertion is based on the argument that this contractor price represents 'the value' (rather than the cost) of the resources the entity would have to sacrifice to fulfil the obligation.

We disagree with this principle and believe that where the entity will fulfil the obligation through the supply of goods or rendering of services, the resources expended should be measured by reference to cost. We do not accept the assertion in BC21(e) that the fulfilment of an obligation is a revenue generating activity and so should result in the recognition of a profit if fulfilled internally rather than paying an external contractor.

Although we accept that there are practical issues in determining which costs should be included in measurement of the liability, as we noted earlier, we do not believe this justifies a conceptually questionable rule because it is an 'easier' option (BC21(b)). Also, B8(b) acknowledges that where there is no market, the entity estimates the value based on cost plus a margin. Consequently, guidance on costs is still needed.

Question 3 - Exception for onerous sales and insurance contracts

Paragraph B9 of Appendix B proposes a limited exception for onerous contracts arising from transactions within the scope of IAS 18 Revenue or IFRS 4 Insurance Contracts. The relevant future outflows would be the costs the entity expects to incur to fulfil its contractual obligations, rather than the amounts the entity would pay a contractor to fulfil them on its behalf.

Paragraphs BC23–BC27 of the Basis for Conclusions explain the reason for this exception.

Do you support the exception? If not, what would you propose instead and why?

We agree with the limited exception for the reasons given by the Board in BC23-27. However, such reasons are equally applicable to the treatment of other revenue-related items currently being reviewed within the Revenue project such as those warranty obligations that are currently recognised on a cost basis within existing IAS 37. The current Discussion Paper relating to *Revenue Recognition* proposes a treatment that differs from both existing IAS 37 and the proposals in the ED. Consequently, if the Board continues with the proposed revision to IAS 37 at this time, we agree with the alternative recommendation in paragraph AV3 and suggest a similar temporary exemption for warranty obligations and other revenue-related items until the new revenue standard is issued.

Other comments

Reliability of measurement

For single obligations, determination of an expected value can be especially problematic. Such obligations are subject to substantial uncertainty as to both possible outcomes and associated probabilities. These are often unique situations, and it is difficult to determine what a third party would rationally pay in the absence of a market. Consequently, it would be helpful if the Board could acknowledge this and provide some application guidance or illustrative examples.
