### IAS 37 Provisions, Contingent Liabilities and Contingent Assets

**SCOPE AND DEFINITIONS**

<table>
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<th>Apply to all:</th>
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<td>• Provisions = liability of uncertain timing or amount.</td>
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<td>• Contingent liabilities = possible obligation arising from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; OR</td>
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<td>• Present obligations arising from past events but is not recognized because:</td>
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<td>o An outflow of economic benefits is not probable; OR</td>
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<td>o Amount of the obligation cannot be measured with sufficient reliability.</td>
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<tr>
<td>• Contingent asset = possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.</td>
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**DO NOT apply to:**

- Exeuctive contracts, except where the contracts are onerous;
- Provisions, contingent liabilities/assets covered by other standards:
  - E.g. construction contracts, income taxes, leases, employee benefits, insurance contracts, financial instruments and contingent considerations of an acquirer in a business combination (IFRS 3).

**MEASUREMENT**

The amount recognised as a provision shall be the **best estimate** of expenditure required to settle the **present obligation** at the **end** of the reporting period. 

**Best estimate** = amount would rationally pay to settle/transfer the obligation.

- Use weighted average probability of possible outcomes, if appropriate.
- Involves judgment, experience, evidence from events after the reporting period and, in some cases, use of independent experts.

**Risk and uncertainties:**
- Those that inevitably surround many events and circumstances are taken into account in best estimate.
- Risk describes, variability of outcomes.
- Avoid excessive prudence and duplication of risk adjustments.

**Present value (PV):**
- Use PV if effect of time value of money is material. 
- Discount rate:
  - Pre-tax rate.
  - Reflect current market and risks of the liability. 
  - Excludes risks included in cash flow estimates. 
  - Recognize borrowing cost over time.

**Future events:**
- Reflect if sufficient objective evidence of occurrence. 
- E.g. possible new legislation when virtually certain of enactment, future site restoration costs reduced by future changes in technology, etc.

**Expected disposal of assets:**
- Gains from expected disposal of assets are not reflected in provision.

**Change in provisions:**
- Reviewed at each reporting period to reflect current best estimate.

**RECOGNITION**

**PROVISIONS**

Recognize only when:
- Entity has a **present obligation** (legal or constructive) as a result of a past event (i.e., obligating event);
- It is **probable** that an outflow of resources will be required to settle the obligation; AND
- A **reliable estimate** can be made of the amount.

**CONTINGENT**

Do not recognize!
- For each class, disclose the following (unless outflow in settlement is remote):
  - Description of the nature;
  - Estimate of financial effect;
  - Uncertainties relating to amount or timing of any outflow;
  - Possibility of reimbursement;
  - Impracticality to disclose the above (if applicable).

Reassess continually:
- Recognize as a provision when outflow becomes **probable** (more likely than not [i.e., >50% probability]).

**CONTINGENT ASSETS**

Do not recognize!
- If inflow of economic benefits probable, **disclose**:
  - Description of the nature;
  - Estimate of financial effect;
  - Impracticality to disclose the above (if applicable).
  - E.g. claim legally pursued but outcome is uncertain.

Reassess continually:
- **Recognize** when inflow becomes virtually certain.
- **Disclose** when inflow becomes **probable**.

**OBLIGATING EVENT IN PAST**

No realistic alternative to settling the obligation created by the past event:
- Settlement enforceable by law (legal obligation).
- The event creates valid expectations in other parties that the entity will discharge the obligation (constructive obligation).

**PRESENT OBLIGATION**

A past event is deemed to give rise to a **present obligation** if, taking account of all available evidence, it is more likely than not that a present obligation exists at the end of the reporting period.

When more likely that no present obligation exist = **contingent liability**.

**PROBABLE OUTFLOW**

- **Probable** = more likely than not (i.e., >50% probability) that there will be an outflow of resources embodying economic benefits.
- Consider the class of obligations as a whole (e.g. product warranties or similar controls).

When more likely that no outflow of resources = **contingent liability**.

When obligation amount not reliably estimated = **contingent liability**.

**RELIABLE ESTIMATE**

Except in extremely rare cases, an entity will be able to determine a range of possible outcomes and can therefore make an estimate of the obligation that is sufficiently reliable to use in recognizing a provision.

**OTHER POINTS**

- Reimbursements recognized as separate assets if virtually certain to be received and amount recognized shall not exceed provision.
- Provisions are not recognized for future operating losses.
- No restructuring obligation arises for the sale of an operation without restructuring.
- Provisions include only direct expenditure arising from the restructuring.

This communication contains a general overview of the topic and is current as of March 31, 2017. The application of the principles addressed will depend upon the particular facts and circumstances of each individual case. Accordingly, this publication is not a substitute for professional advice and we recommend that any decisions you take about the application or not of any of the information presented be made in consultation with a qualified professional, who can address any variance that may be required to reflect your circumstances. Please contact your local MNP representative for customized assistance with the application of this material. MNP LLP accepts no responsibility or liability for any loss related to any person's use of or reliance upon this material. © MNP LLP 2017. All rights reserved.