IFRS AT A GLANCE

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*

As at 1 January 2016

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*

Also refer:
IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*
IFRIC 5 *Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds*

Effective Date
Periods beginning on or after 1 July 1999

SCOPE

Excludes provisions, contingent liabilities and contingent assets arising from:

- Non-onerous executory contracts
- Those covered by other IFRSs:
  - IAS 11 *Construction Contracts*
  - IAS 12 *Income Taxes*
  - IAS 17 *Leases*
  - IAS 19 *Employee Benefits*
  - IFRS 4 *Insurance Contracts*.

DEFINITIONS

- Provision – a liability of uncertain timing or amount.
- Contingent liability
  - A possible obligation that arises from past events, whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly in the control of the entity; or
  - A present obligation that arises from past events that is not recognised because:
    -it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or
    -the amount of the obligation cannot be measured with sufficient reliability.
- 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.

RECOGNITION

PROVISIONS

Provisions are recognised when all the following conditions are met:

- The entity has a present legal or constructive obligation as a result of a past event
- It is probable that an outflow or economic benefits will be required to settle the obligation; and
- A reliable estimate can be made of the amount of the obligation.

CONTINGENT LIABILITIES

Contingent liabilities are not recognised.

CONTINGENT ASSETS

Contingent assets are not recognised.

MEASUREMENT

- Provisions are measured at the best estimate of the expenditure required to settle the present obligation at reporting date
- Where the provision being measured involves a large population of items (i.e. goods' warranties), the obligation is estimated by weighting all possible outcomes by their associated probabilities.
- In determining the best estimate, the related risks and uncertainties are taken into account
- Where the effect of the time value of money is material, the amount of the provision is the present value of the expenditures expected to be required to settle the obligation. The discount rate used is a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the liability
  - The discount rate does not reflect risks for which future cash flow estimates have been adjusted.
- Future events that may affect the amount required to settle the obligation are reflected in the amount of the provision where there is sufficient objective evidence that they will occur
- Gains from the expected disposal of assets are not taken into account in measuring the provision
- Reimbursements from third parties for some or all expenditure required to settle a provision are recognised only when it is virtually certain that the reimbursement will be received. The reimbursement is treated as a separate asset, which cannot exceed the amount of the provision
- Provisions are reviewed at each reporting date and adjusted to reflect the current best estimate
- If it is no longer probable that an outflow of economic benefits will be required to settle the obligation, the provision is released
- Provisions are not recognised for future operating losses

ONEROUS CONTRACTS

- Onerous contract – one where the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it
- For onerous contract, the provision is recognised and measured at the lower of:
  - The cost of fulfilling the contract
  - The costs/penalties incurred in cancelling the contract.
- Before a separate provision for an onerous contract is recognised, an entity recognises any impairment loss (IAS 36 *Impairment of Assets*) that has occurred on assets dedicated to that contract.

RESTRUCTURING

Restructuring provisions are only permitted to be recognised when an entity has:

- A detailed formal plan for the restructuring identifying:
  - The business or part of business concerned; principal locations affected; location, function, approximate number of employees to be compensated for termination of their services; expenditures that will be undertaken and when the plan will be implemented.
- Has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing (e.g. by a public announcement) its main features to those affected before the end of the reporting period
- Restructuring provisions only include the direct expenditures arising from the restructuring – i.e. those that are both necessarily entailed by the restructuring and not associated with the entity's on-going activities.

For further information about how BDO can assist you and your organisation, please get in touch with one of our key contacts listed below. Alternatively, please visit www.bdointernational.com/Services/Audit/IFRS/IFRS Country Leaders where you can find full lists of regional and country contacts.

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