



THE POWER OF BEING UNDERSTOOD

U.S. GAAP VS. IFRS: CONTINGENCIES AND PROVISIONS AT-A-GLANCE

Increasing globalization coupled with related regulations continues to put pressure on moving towards a common global accounting framework – International Financial Reporting Standards (IFRS). Currently, more than 100 countries use IFRS, so if your business goals include global expansion, it is critical to educate yourself now about the impact of IFRS on your financial reporting processes and business. To gain a better understanding of what IFRS means for your organization, we have prepared a series of comparisons dedicated to highlighting significant differences between IFRS and U.S. generally accepted accounting principles (GAAP). This particular comparison focuses on the significant differences between U.S. GAAP and IFRS related to accounting for contingencies and provisions. For other comparisons available in this series, refer to our [U.S. GAAP vs. IFRS comparisons at-a-glance series](#).

A discussion about U.S. GAAP and IFRS would not be complete without mentioning the status of the Securities and Exchange Commission's (SEC) activities focused on determining whether the application of IFRS by U.S. registrants should be required or allowed. The tone at the SEC on this matter changed recently when they indicated in their draft [Strategic Plan for Fiscal Years 2014–2018](#) that they will "consider...whether a single set of high-quality global accounting standards is achievable." As a result, it is not clear what the SEC's next steps and timetable are with respect to making a decision about the application of IFRS by U.S. registrants. For more information, refer to our [IFRS Resource Center](#).

The guidance related to contingencies in U.S. GAAP is included in several topics of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). The general

guidance on accounting for contingencies is contained in Topic 450, *Contingencies*, and guidance on accounting for specific types of contingencies is contained in other ASC topics, such as Topic 410, *Asset Retirement and Environmental Obligations*, and Topic 420, *Exit or Disposal Cost Obligations*. For U.S. GAAP purposes, the term "general loss contingency" is used in this comparison to refer to those contingencies that fall within the scope of ASC 450. In IFRS, the guidance related to contingencies and provisions is contained in International Accounting Standard (IAS) 37, *Provisions, Contingent Liabilities and Contingent Assets*.

One of the similarities between U.S. GAAP and IFRS with respect to contingent liabilities and provisions is that both require recognition of a loss based, in part, on whether it is probable that one or more future events will occur confirming that a loss event has occurred. However, as discussed further in the table included in this comparison, "probable" is defined differently under U.S. GAAP and IFRS. Other similarities are that both prohibit recognition of costs associated with operating activities expected to occur in the future and both require disclosures related to contingent liabilities that are not recognized, but that have a likelihood of occurrence that is more than remote. In addition, the accounting for gain contingencies under U.S. GAAP and contingent assets under IFRS are generally similar because gain contingencies are not recognized under U.S. GAAP until they are realized and contingent assets cannot be recognized under IFRS. While there are some similarities related to accounting for contingencies and provisions under U.S. GAAP and IFRS, there are also some significant differences, which are summarized in the following table.

	U.S. GAAP	IFRS
Relevant guidance	ASC 410, 420 and 450	IAS 37
Definitions	The Master Glossary of the ASC defines a contingency as follows: "An existing condition, situation, or set of circumstances involving uncertainty as to possible gain (gain contingency) or loss (loss contingency) to an entity that will ultimately be resolved when one or more future events occur or fail to occur."	<p>Paragraph 10 of IAS 37 defines a provision as "a liability of uncertain timing or amount."</p> <p>Paragraph 10 of IAS 37 defines a contingent liability or asset as a possible obligation or 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."</p> <p>Paragraph 10 of IAS 37 also includes in the definition of a contingent liability "a present obligation that arises from past events, but is not recognised because:</p> <ul style="list-style-type: none"> i. it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or ii. the amount of the obligation cannot be measured with sufficient reliability."
Recognition threshold	To recognize a general loss contingency, the loss must be probable. Probable is generally interpreted as "likely" and is not defined by reference to a single percentage threshold. The intent is that probable be interpreted as a high likelihood.	A loss must be probable to be recognized. Probable is interpreted as more likely than not (i.e., a probability of greater than 50 percent).
Measurement	General loss contingencies are only recognized when they are reasonably estimable. When there is a range of possible outcomes for a general loss contingency, the amount accrued should be the most likely outcome within the range. If no single outcome within the range is more likely than the others, the minimum amount in the range should be accrued.	Provisions must be reliably estimable to be recognized. When there is a range of possible outcomes for a provision, the amount accrued should be the best estimate of the obligation. If no single outcome within the range represents the best estimate, the midpoint of the range should be accrued
Discounting	Typically, a general loss contingency is not discounted unless the aggregate amount of the liability and the timing of cash payments for the liability are fixed or determinable. However, even in such circumstances, discounting is an accounting policy choice, rather than a requirement.	The anticipated cash flows to settle an obligation are discounted using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the liability, if the effect is material.
Onerous contracts	Unless specifically required by other U.S. GAAP, obligations arising from onerous contracts generally are not recognized.	An onerous contract is defined as a contract in which the unavoidable costs of meeting the obligations under the contract exceed the expected economic benefits. If such a contract exists, the reporting entity should recognize the present obligation as a provision.

	U.S. GAAP	IFRS
Asset retirement obligations (ARO)	A liability for an ARO is initially recognized when a legal obligation arises in connection with the acquisition, construction or development of a long-lived asset. The liability is measured at its fair value. If the expected cash flow approach is used to estimate the fair value of the ARO, a credit-adjusted, risk-free rate is used for discounting.	A liability for dismantling and removing an item, or for restoring the site, is recorded when a present obligation exists. The liability is recorded at management's best estimate of the costs to be incurred. A pre-tax discount rate that reflects the current assessment of the risks specific to the liability is used to discount the liability.
Restructuring costs	<p>A restructuring liability is only recognized if it represents a present obligation. An attribute of a present obligation is that the entity has little or no discretion to avoid settlement of the liability by transferring or using assets. An entity's commitment to an exit plan or disposal plan is required to recognize a restructuring liability. In addition, one-time employee termination benefits, must meet certain criteria prior to recognition of a related liability, including communication of the details of the plan to employees who could be affected.</p> <p>In general, a restructuring liability is measured at its fair value.</p>	<p>A provision for restructuring costs is required to be recognized if the general requirements for recognition of a provision are met. One of those criteria is that a present legal or constructive obligation exists. A constructive obligation exists when an entity has done both of the following:</p> <ul style="list-style-type: none"> · Prepared a detailed formal plan for the restructuring. · Raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing the main features to those affected by it. <p>A restructuring liability is measured at the best estimate of the direct expenditures related to the restructuring.</p>

These are the significant differences between U.S. GAAP and IFRS related to contingencies and provisions. Refer to ASC 410, 420 and 450 and IAS 37 for all of the specific requirements applicable to contingencies and provisions. Refer to our [U.S. GAAP vs. IFRS comparisons at-a-glance series](#) for more comparisons highlighting other significant differences between U.S. GAAP and IFRS.

Contact:

Richard Stuart, Partner
National Accounting Standards Group, RSM US LLP
+1203 905 5027
richard.stuart@rsmus.com

+1 800 274 3978
www.rsmus.com

This document contains general information, may be based on authorities that are subject to change, and is not a substitute for professional advice or services. This document does not constitute audit, tax, consulting, business, financial, investment, legal or other professional advice, and you should consult a qualified professional advisor before taking any action based on the information herein. RSM US LLP, its affiliates and related entities are not responsible for any loss resulting from or relating to reliance on this document by any person. RSM US LLP is a limited liability partnership and the U.S. member firm of RSM International, a global network of independent audit, tax and consulting firms. The member firms of RSM International collaborate to provide services to global clients, but are separate and distinct legal entities that cannot obligate each other. Each member firm is responsible only for its own acts and omissions, and not those of any other party. Visit rsmus.com/aboutus for more information regarding RSM US LLP and RSM International. RSM® and the RSM logo are registered trademarks of RSM International Association. *The power of being understood®* is a registered trademark of RSM US LLP.