national treasury
Department: National Treasury
REPUBLIC OF SOUTH AFRICA

GRAP 19 – Provisions, Contingent Liabilities and Contingent Assets

Effective 1 April 2021

Principal:
Provisions should only be recognised when there is a liability. Thus, only genuine present obligations are recognised and not planned future expenditure

DEFINITIONS

A **provision** is a liability of uncertain timing or amount
A **contingent liability** is:
- A possible obligation 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, or
- A present obligation that arises from past events but is not recognised because it is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation or the amount of the obligation cannot be measured with sufficient reliability

A **contingent asset** is a 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 event not wholly within the control of the entity

RECOGNITION

Provisions are recognised when:
- The entity has a present legal or constructive obligation as a result of a past event
- It is probable ('more likely than not') that an outflow of economic benefits or service potential will be required to settle the obligation, and
- A reliable estimate can be made of the amount of the obligation

Contingent assets are not recognised but are disclosed where an inflow of economic benefits or service potential is probable

Contingent liabilities are not recognised but are disclosed unless the outflow of economic benefits or service potential is remote

ONEROUS CONTRACTS

- An onerous contract is one where the unavoidable costs of meeting the obligations under the contract exceed the economic benefits or service potential expected to be received under it
- For onerous contracts, the provision is recognised and measured at the lower of the cost of fulfilling the contract or the costs / penalties incurred in cancelling the contract
- Before a separate provision for onerous contract is recognised, an entity recognises an impairment loss that has occurred on assets dedicated to the contract

MEASUREMENT

The amount recognised should be the best estimate of the expenditure required to settle the present obligation at the reporting date. This means:
- Provisions for one-off events (environmental clean-up, settlement of lawsuit) are measured at the **most likely outcome**
- Provisions are large populations of events (warranties) are measured at a **probability-weighted expected value**
- Both measurements are discounted (where the effect is material) using a pre-tax discount rate that reflects the current market assessment of the time value of money **and** the risks specific to the liability

In reaching this best estimate, the entity takes into account the **risks** and uncertainties that surround the underlying events

In measuring provisions, consider future events as follows: forecast reasonable change in applying existing technology (cannot predict discovery of new technology); ignore possible gains on sale of assets; and consider changes in legislation only if it is virtually certain to be enacted

- Reimbursements from 3rd 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 reversed.