

**CORRELATION AND IMPLICATIONS RELATING TO
PROVISIONS AND IDENTIFICATION
OF RISKS WHICH DETERMINE THEIR CONSTITUTION**

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Abstract

In order to optimize costs and ensure the sustainability of businesses less affected by the COVID pandemic crisis 19, the restructuring of activities in accordance with the provisions of IAS 37 - Provisions, contingent liabilities and contingent assets may be a viable solution. In this context, this article aims to provide the necessary clarifications in order to provide a basis for assessing the appropriate recognition criteria applied to provisions, contingent liabilities and contingent assets, to ensure full information support in the explanatory notes to the financial statements, necessary for users. accounting information in substantiating decisions.

The results of the present study emphasize that, now more than ever, in a pandemic context, professional judgment is crucial in determining when the conditions for recognizing a provision in the financial statements are met and in accounting for amounts that can be recognized as part of this. provision, in accordance with IAS 37. We believe that this study can be particularly useful, in this pandemic context, to professional accountants engaged in financial reporting work, but also to regulatory bodies that can provide solutions to revise this standard.

Keywords: current obligation; contingent assets; contingent liabilities; provision.

1. Introduction

In April 2001, the International Accounting Standards Board adopted IAS 37 “Provisions, Contingent Liabilities and Contingent Assets”, originally issued by the International Accounting Standards Committee in September 1998. This standard was intended to partially replace IAS 10 “Quotas”. and events subsequent to the balance sheet date ”which was issued in 1978.

There are also standards that include minor amendments to IAS 37. These are IFRS 9 Financial Instruments (Hedge Accounting and Amendments to IFRS 9, IFRS 7 and IAS 39) issued in November 2013, Annual Improvements to IFRSs, 2010-2012 cycle issued in December 2013, IFRS 15 Revenues from customer contracts issued in May 2014), IFRS 9 Financial instruments issued in July 2014 and IFRS 16 Leases issued in January 2016 (CECCAR, 2017).

Starting from the way of defining, recognizing and presenting in the financial statements the provision as an uncertain liability item, the international accounting standard (IAS 37 - Provisions, contingent liabilities and contingent assets) has the means to ensure the most used criteria and methods. to deal with provisions and to identify contingent liabilities and assets. Provisions and quotas must be recognized as a result of obvious risks or threats to the activities of an entity, which is why it is determined to make up those provisions. Basically, their establishment is directly highlighted by the fundamental policy of the company, with the role of avoiding possible differences or impossible situations to deal with future expenses or debts, with uncertain value. In this respect, one of the mandatory requirements provides in the explanatory notes clear and relevant (credible) information on the nature of these provisions, the estimated duration of the verification and very importantly their nature or destination. However, there are exceptions to the application of IAS 37:

- liabilities arising from transactions in financial instruments recorded at fair value;
- obligations arising from enforceable contracts, less those for consideration;
- obligations arising under insurance contracts;
- obligations under other IASs.

Provisions are created by including in the company's operating expenses, with effects on reducing the taxable result, which creates a tax advantage for the entity. As the entity uses the provisions, there is an increase in revenue, which will be taxed.

2. Provisions

A provision "shall be charged to expenses and are intended to cover certain losses or expenses the cause of which is precise and for which there is uncertainty as to the size or date of their occurrence. Funds created on account of expenses, intended to cover exchange rate fluctuations, price increases and to cover losses and latent expenses that incurred or ongoing events make probable (eg for litigation, customer guarantees, etc.). Being created by including in the exceptional expenses of the company, they influence, by reduction, the taxable profit, temporarily creating a tax advantage for the company. Subsequently, as the provisions are used, the benefits increase and will be taxed. " (<http://www.contabilitateafirmei.ro>, 2021).

IAS 37 provides useful references for deciding whether a debt is a provision or a contingent liability." A contingent liability also arises very rarely if there is a debt that cannot be recognized due to the fact that it cannot be measured reliably. In that case, provision shall be made for information on the contingent liability." (CECCAR, 2017)

Table no. 1 shows the settlement of the provision provided that part or all of the amount required to be reimbursed by a third party.

<p>The entity has no obligation to pay part of the amount to be repaid by a third party.</p>	<p>The liability for the amount expected to be reimbursed remains with the entity and it is almost certain that the reimbursement will be received if the entity settles the provision.</p>	<p>The obligation for the amount expected to be reimbursed remains with the entity, and if the entity settles the provision, the receipt of the reimbursement is not nearly certain.</p>
<p>The entity has no liability for the amount to be repaid * paragraph 57</p>	<p>Reimbursement is recognized in the statement of financial position as a separate asset and may be offset against expenses in the statement of comprehensive income. The amount recognized for the expected repayment does not exceed the debt * points 53 and 54</p>	<p>Expected repayment is not recorded as an asset * paragraph 53</p>
<p>It is not necessary to present information</p>	<p>Reimbursement is presented together with the related amount recognized for reimbursement * point 85, letter c</p>	<p>The expected reimbursement is present * point 85, letter c</p>

Table no. 1 Settlement provisions

Source: International Financial Reporting Standards (2017). IAS - IAS 37 - Provisions, liabilities and contingent assets, p. 4136, ed. CECCAR (CECCAR, 2017)

An important chapter in the accounting of the organization of the capital of an entity is the provisions, fulfilling the role of some reserves that generate, however, certain expenses that influence the financial result in a negative way. They are represented by shares of the results that were reserved to finance a reversible depreciation or loss of an asset, as well as expenses that are not yet effective but were considered probable at the end of the financial year.

3. Active Contingent

Contingent assets "are defined in the economic dictionary as a potential asset that arises from events prior to the balance sheet date and whose existence is to be confirmed only by the occurrence / non-occurrence of one or more uncertain future events that are not controlled by entity as a whole " (Mihai, 2004).

"These contingent assets arise as a result of events that have not been taken into account, but which in the end may generate inflows of economic benefits for the entity. Contingent assets will not be recognized in the balance sheet (the reason being that they are not certain economic inflows, and their recognition could lead to an incorrect transposition in the financial statements of the entity's situation, due to which it may appear as unrealized income) , but must be disclosed in the explanatory notes if there are probable economic benefits inputs for the entity. " (www.contzilla.ro, 2021)

If the realization of an income is secure, the related asset is not a contingent asset and must be recognized in the balance sheet. "According to IAS 37, a contingent asset is defined as that potential asset that arises as a result of past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events that cannot be fully under control of the undertaking " (M.A. Ștefan, 2021).

The main provisions of the standard are presented in the Table no. 2.

Inputs of economic benefits are secure.	Entry benefits are likely, but not certain.	Entries are unlikely.
The asset is not a contingent asset * item 33	No assets recognized * item 31	No assets recognized * item 31
	Information required * paragraph 89	No disclosure required * paragraph 89

Table nr. 2 – Active contingent

Source: : International Financial Reporting Standards (2017). IAS - IAS 37 - Provisions, liabilities and contingent assets, p. 4135, ed. CECCAR (CECCAR, 2017)

Contingent assets should not be recognized as income or assets, they should be disclosed if there is likely to be an inflow of economic benefits. Table 3 presents a summary of the requirements that contingent assets must meet.

The probability of receiving an income	Almost sure	Probably, but not nearly for sure	Unlikely
Presentation required	No - the asset is no longer contingent	Introduces himself	Presentation is not required

Tabel nr. 3 Rezumat al cerințelor legate de activele contingente

Source: <http://contabilitate-primara.blogspot.com>

4. Contingent Debts

A contingent liability is defined as a potential obligation, arising from past events, prior to the balance sheet date and the existence of which will be confirmed only by the occurrence / non-occurrence of at least one uncertain future event, but which the entity cannot control. fully. The entity will not recognize a contingent liability in the balance sheet, which is present in the explanatory notes.

Where an entity has a jointly and severally liable obligation with other parties, the part assumed by the other parties is presented as a contingent liability. Contingent liabilities will be continuously assessed by the entity in order to be able to correctly determine in the financial statements of the period any outflow of resources that incorporates economic benefits. "If there are several similar obligations (example: guarantees for similar products or contracts), the probability that an outflow of resources will be required to settle the obligation is determined by taking into account the entire class of obligations. Although the probability of a resource outflow for an individual item may be reduced, a resource outflow may be required to settle the entire class of obligations. In such cases a provision is recognized (if the other conditions of recognition are met)" (CECCAR, 2017).

In table no. 4 summarizes the requirements for the existence of a contingent liability that must be presented in the financial statements where there is a possible obligation, or there is a present obligation but it is not possible to reasonably estimate the loss or the probability of a distant loss.

Type of obligation	Possible	Present	Possible	Present
The probability of the benefits coming out is	Possible, but not	Possible, but not probable	Removed	Removed

necessary	probable			
Presentation required	Introduces himself	Introduces himself	Presentation is not required	Presentation is not required

Table nr. 4 – Summary of contingent debt requirements

Source: <http://contabilitate-primara.blogspot.com/2011/02/ias-37-provizioane-datorii-si-active.html> (contabilitate-primara.blogspot.com, 2021)

5. The difference between provisions and contingent liabilities

Contingent liabilities are distinguished from provisions by the fact that:

- a. *the provisions* will be recognized as liabilities, as they constitute current liabilities at the balance sheet date and it is likely that outflows of resources will be required in order to settle the liabilities;

and

- b. *contingent liabilities* will not be recognized as liabilities because:
 - there are possible obligations (for which it must be confirmed whether the entity has a current obligation that can generate an outflow of resources);

or

- are current liabilities that do not meet the recognition criteria in the balance sheet.

In table no. 5 summarizes the main provisions of the standard. Contingent debt that arises, in very rare cases where there is a debt that cannot be recognized due to the fact that it cannot be measured reliably.

<p>Where, as a result of previous events, an outflow of resources incorporating economic benefits may be recorded to settle: (a) a current obligation; or (b) a possible obligation whose existence will be confirmed only by the occurrence or absence of one or more uncertain future events that are not fully under the control of the entity.</p>		
<p>There is a current obligation that probably requires an outflow of resources.</p>	<p>There is a possible obligation or a current obligation that may require an outflow of resources, but it is likely that this will not happen.</p>	<p>There is a possible obligation or a current obligation, but the probability of an outflow of resources is removed.</p>
<p>A provision is recognized * point 14</p>	<p>No provision is recognized * point 27</p>	<p>No provision is recognized * point 27</p>
<p>It is necessary to present information on the provision * points 84 and 85</p>	<p>It is necessary to provide information on the contingent liability * paragraph 86</p>	<p>No information required * paragraph 86</p>

Table nr. 5 Provisions and contingent liabilities

Source: : International Financial Reporting Standards (2017). IAS - IAS 37 - Provisions, liabilities and contingent assets, p. 4135, ed. CECCAR (CECCAR, 2017)

“Information on items recorded in off-balance sheet accounts must be provided in the notes to the annual financial statements. The off-balance sheet items also include contingent assets (account 807 “Contingent assets”), respectively contingent liabilities (account 808 “Contingent liabilities”)” (Ionescu, 2016).

6. The decision tree

Figure no. 1 summarizes the main provisions for recognizing the standard for contingent provisions and liabilities.

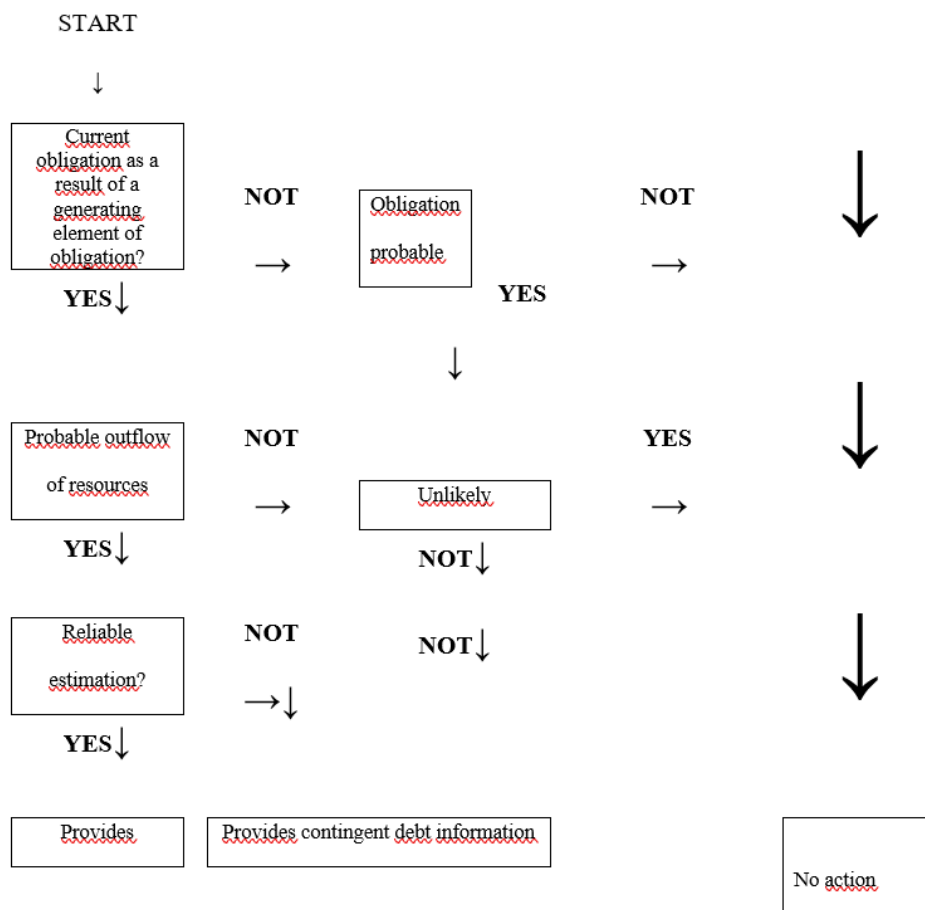


Figure nr. 1. The main provisions for recognizing the standard
Source: : International Financial Reporting Standards (2017). IAS - IAS 37 – Provisions, liabilities and contingent assets, p. 4137, ed. CECCAR

Practical application (STRATON, 2018)

A. Establishment of provisions

(a) as part of the cost of the period:

6812	=	151
Operating expenses on provisions		Provisions

(b) as part of the cost of the asset, for example, provision for the estimated costs of dismantling and moving the assets, respectively the costs of restoring the sites:

2xx	=	151
Tangible fixed assets		Provisions

B. Changes and cancellations of provisions

Provisions are reviewed at each balance sheet date and adjusted to reflect the best current valuation. If it is no longer probable, in order to settle an obligation, that an outflow of resources materialized in economic benefits will be required, the provision must be canceled. Also, if the update is used, the carrying amount of the provision increases with each period to reflect the passage of time. This increase is recognized as an interest expense.

The types of accounting records are:

(a) if the carrying amount of the provision has increased:

6812	=	151
Operating expenses on provisions		Provisions

or:

2xx	=	151
Tangible fixed assets		Provisions

(b) if the carrying amount of the provision has decreased:

(b1) if the initial provision has been spent:

151	=	7812
Provisions		Income from provisions

(b2) dacă provizionul inițial a fost inclus în costul activului:

151	=	2xx
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Provisions

Tabgible fixed assets

*taking into account the accumulated depreciation and depreciation.

C. Use of provisions

The provision is used only for the purpose for which it was originally recognized. Under these conditions, only the expenses corresponding to the original purpose for which the provision was established are settled with it.

Adjusting the provisioning expenses hides the impact of two different events, respectively:

(a) recognition of expenses that have become due:

6xx x lei	=	3xx x lei
		4xx x lei
Expenditure accounts by nature		5xx x lei
		Balance sheet accounts of resources used

(b) resumption of the established provision:

151 y lei	=	7812 y lei
Provisions		Income from provisions

It is specified that the operations of setting up and using provisions may affect the result of the enterprise by the differences between x (amounts actually committed) and y (amounts foreseen).

D. Reimbursement of provisions

If it is estimated that part or all of the expenses necessary to extinguish a provision will be reimbursed by a third party, the reimbursement should only be recognized when it is certain

that the reimbursement will be received if the company honors its obligation. Repayment must be considered a separate asset. The amount recognized for reimbursement must not exceed the value of the provision.

From an accounting point of view, the company will record a provision for the full amount of the debt:

6812	=	151
Operating expenses on provisions		Provisions

Once the company is sure that the refund will be received, an asset will be recognized, the registration being:

512x	=	7xx
Current bank accounts		Revenue from the reimbursement of the provision

and at the same time the provision established is partially or totally canceled, as the case may be:

151	=	7812
Provisions		Income from provisions

Conclusions

The objective of the treated standard is to ensure the correct application of recognition criteria and valuation bases appropriate to provisions, contingent liabilities and contingent assets, as well as the presentation of sufficient information in the notes so as to enable users to understand the nature, retention over time. as well as their value.

Provisions are distinguished from other liabilities such as trade payables or accounting commitments because there is uncertainty about the timing or amount of future expenses

required to settle them, with commitments often relating to trade payables and other liabilities, while provisions are reported separately.

IAS 37 uses the term “contingent” which is used for unrecognized liabilities and assets, as their existence will be confirmed only by the occurrence or absence of one or more uncertain future events that are not fully controlled by the entity. also, the term "contingent liability" is used for debts that do not meet the recognition criteria.

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*** <http://www.iasplus.com>

***Active contingente, <https://www.contzilla.ro/ce-sunt-actiunile-contingente/>