

United Nations

Corporate Guidance

for

**International Public Sector Accounting
Standards**

Provisions and Contingent liabilities

8 June 2013

Final Draft



Corporate Guidance to Support the Adoption of International Public Sector Accounting Standards (IPSAS) by the United Nations

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Corporate Guidance # 7 – Provisions and (contingent) liabilities (IPSAS 19)

This corporate guidance will cover the following topics with respect to provisions and (contingent) liabilities:

- Guidance for recognition and measurement of provisions and contingent liabilities in the United Nations: **see captions 5 and 6;**
- Guidance on recognition of constructive obligations. What are steps taken to deal with constructive obligations in peacekeeping missions? What are possible scenarios of constructive obligations? Template to identify constructive obligations in UN; **see caption 5.1;**
- How to recognise a provision or contingent liability in following cases:
 - Litigation and legal claims; **see caption 10.1;**
 - Third party claims; **see caption 10.2;**
 - Restoration costs and other contractual obligations; **see caption 10.3;**
 - Restructuring costs: **see caption 10.4;**
 - Death and disability claims; **see caption 10.5;**
 - Claims under defacto lease arrangements *; **see caption 10.6;**
 - Claims submitted to United Nations Compensation Commission; **see caption 10.7;**
 - Insurance claims (covered in employee benefit paper); **see caption 10.8;**
 - Guarantees and warranties; **see caption 10.9.**
- Guidance on accounting and identification of adjustment of provisions and movements from contingent liabilities to provisions. Template to record the movements and adjustments: **see caption 7;**
- Guidance on presentation and disclosure requirements of provisions and contingent liabilities in financial statements of UN Secretariat entities: **see captions 8 and 9.**

* De facto leases *refer to situations where no formal agreements have been signed between the parties*

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1 Introduction

The objective of this paper is to provide guidance on when to recognise provisions in the statement of financial position or disclose contingent liabilities and contingent assets, how to measure such entries, and which disclosures are necessary for these items. Key to this is the clarification of how provisions differ from other liabilities, such as payables and accruals through the level of uncertainty associated with each class of liability.

In the course of its operations and activities throughout the world, the United Nations Secretariat (“United Nations”) will take actions which will invariably result in future payments or outflows of resources.

Under IPSAS, such actions and events may require the United Nations to recognise provisions in addition to the more traditional liabilities recognised during the course of a financial year, even where “obligations” may have not been raised under UNSAS. Provisions appear as short and/or long-term liabilities on the statement of financial position and are defined as “liabilities of uncertain timing or amount”. Where provisions are not recognised, disclosures regarding contingent liabilities may still be required.

For example, the United Nations may be involved in a legal case as a result of its past activities, which may result in a payment of damages to a third party. Even if the case is not settled by the year-end, it may be necessary for the United Nations to “provide” for anticipated damages in its financial statements if it is probable (more than 50% probability) that the United Nations will have to make a payment and a reliable estimate can be made. If it is less probable that a payment will be made, a contingent liability may still need to be disclosed in the notes to the financial statements.

The likelihood or probability of outflows occurring is therefore a key factor in determining whether a provision should be recognised, or whether a note disclosure as a contingent liability is instead necessary. In addition, recognition of a provision will also depend on whether the actions of the United Nations have led to an “obligation” to pay future costs – this may not always be a legal obligation, but can also include cases where past behaviour and precedents create a “constructive” obligation for the United Nations to pay costs.

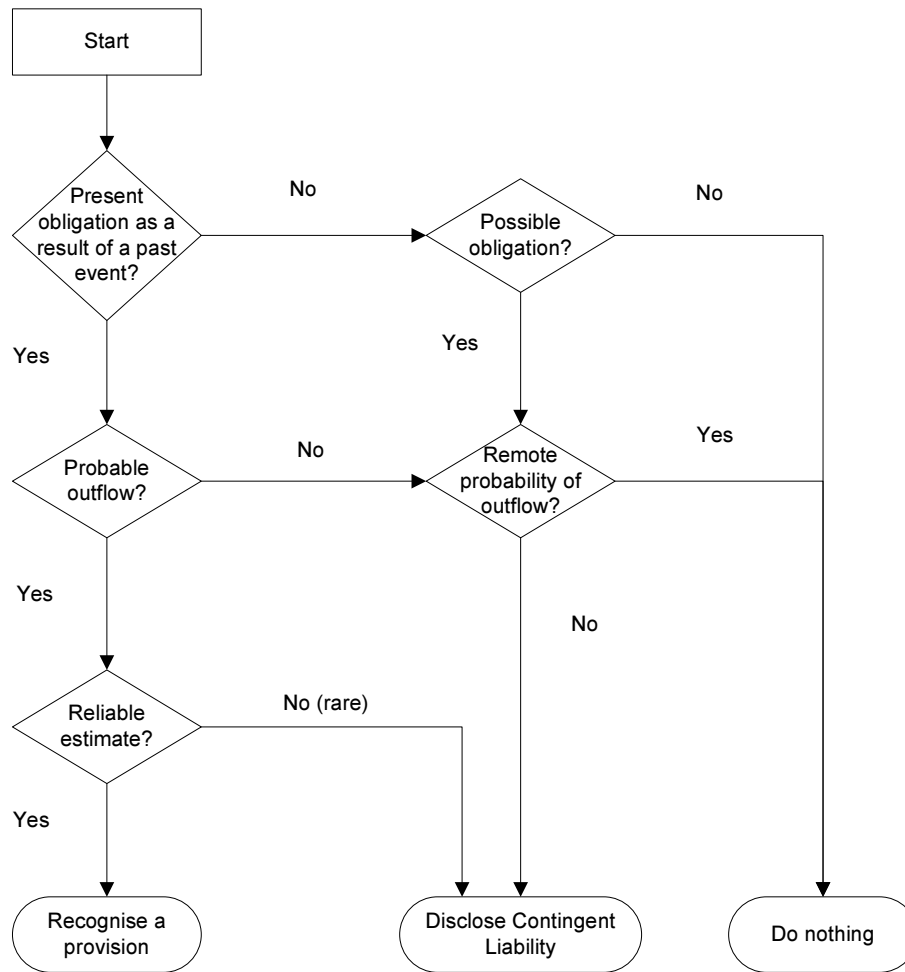
Specifically, the United Nations should recognise a provision when all of the following three key criteria have been met:

- a) The United Nations has a present obligation (legal or constructive) as a result of a past event;
- b) It is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; **and**
- c) A reliable estimate can be made of the amount of the obligation.

These criteria are examined in more detail in section 5 below, however it is important to note that in many cases the criteria will need to be applied with professional judgement dependent on the overall substance of actions and events – not all cases will have an immediate, definitive answer and expert advice may be required, such as the input of the Office of Legal Affairs (“OLA”). Under IPSAS, it is therefore likely that increased communication and collaboration will be required between finance teams and experts such as the OLA.

The flowing decision tree may be used to assist in the decision making process:

Flowchart – Decision tree for recognition of provisions or disclosure of contingent liabilities



Other typical examples where provisions may need to be considered include future clean up and decontamination costs, refurbishing of buildings at the end of leases, restructuring plans, and onerous contracts.

There are some notable exclusions to the scope of IPSAS 19, where other standards take precedence and which are therefore outside the scope of this Corporate Guidance paper. These include but are not limited to:

- Employee benefits (apart from restructuring) – see Corporate Guidance #8 – Employee Benefits;
- Executory contracts (apart from onerous executory contracts) (see definitions, e.g. operating lease contracts); and
- Other topics where specific IPSASs deal with specific provisions’ guidance (e.g. Construction contracts, etc).

Note: “Provisions” for doubtful debts are also outside the scope of this Corporate Guidance.

2 Definitions

2.1 IPSAS

Provisions and contingent liabilities

A **liability** is a **present obligation** of the United Nations arising from past events, the settlement of which is expected to result in an outflow from the United Nations of resources embodying economic benefits or service potential.

Payables are **liabilities** to pay for goods or services that have been received or supplied, and have been invoiced or formally agreed with the supplier.

Accruals are **liabilities** to pay for goods or services that have been received or supplied, but have not been paid, invoiced, or formally agreed with the supplier, including amounts due to employees (for example, amounts relating to accrued vacation pay). Although it is sometimes necessary to estimate the amount or timing of accruals, the uncertainty is generally much less than for provisions.

A **provision** is a **liability** of uncertain timing or amount.

An **obligating event** is an event that creates a legal or constructive obligation that results in the United Nations having no realistic alternative to settling that obligation.

A **legal obligation** is an obligation that derives from:

- a) A contract (through its explicit or implicit terms);
- b) Legislation; or
- c) Other operation of law.

A **constructive obligation** is an obligation that derives the United Nations' actions where:

- a) By an established pattern of past practice, published policies, or a sufficiently specific current statement, the United Nations has indicated to other parties that it will accept certain responsibilities; **and**
- b) As a result, the United Nations has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

A **contingent liability** is

- a) 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 United Nations; **or**
- b) a present obligation that arises from past events, but is not recognized because:
 - i. It is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; **or**

- ii. The amount of the obligation cannot be measured with sufficient reliability.

Executory contracts (e.g. an operating lease contract) are contracts under which neither party has performed any of its obligations, or both parties have partially performed their obligations to an equal extent.

An **onerous contract** is a contract for the exchange of assets or services in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits or service potential expected to be received under it.

A **restructuring** is a program that is planned and controlled by management, and materially changes either:

- (a) The scope of the United Nations' activities; or
- (b) The manner in which those activities are carried out.

Assets and contingent assets

An **asset** is a resource controlled by the United Nations as a result of past events and from which future economic benefits or service potential are expected to flow to the United Nations.

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 events not wholly within the control of the United Nations.

2.2 UNSAS

Note – UNSAS definitions are shown for illustrative purposes, however for IPSAS accounting, the IPSAS definitions above should be used.

Obligations are amounts of orders placed, contracts awarded, services received and other transactions which involve a charge against the resources of the current financial period under UNSAS and which would require payment during the same or a future financial period.

Unliquidated obligations (“ULO”s) are obligations which remain unpaid.

2.3 Note on the term “obligation”

The term “**obligation**” is a key component in the recognition of provisions or other liabilities under IPSAS, and should not be confused with the same term under UNSAS. Not all “obligations” defined under IPSAS will meet the definition of an “obligation” under UNSAS.

For example, under IPSAS the United Nations may have a legal or constructive “obligation” to restore the site of a Peacekeeping base to its original condition at the end of an operation, even though an UNSAS “obligation” may not yet have been raised for the anticipated costs.

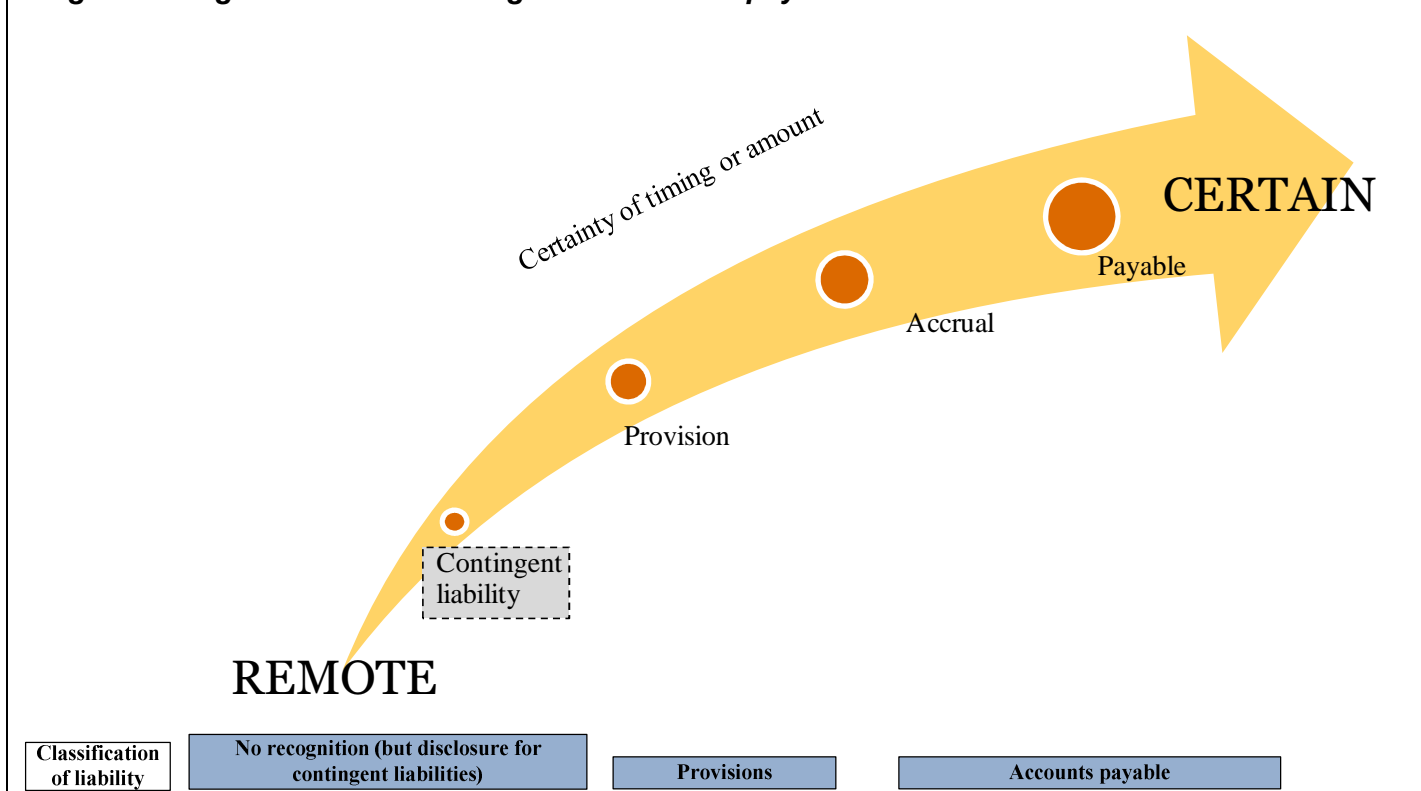
It is critical to understand this difference when considering the activities of the United Nations under IPSAS, as additional “obligations” may be present under IPSAS that are not recorded as UNSAS “obligations”.

Equally, an UNSAS obligation may be raised for an item to be paid in the future where the United Nations does not yet have a legal or constructive obligation to pay under IPSAS. For example, the United Nations may raise an UNSAS “obligation” in December 20X3 for a restructuring programme which will be planned and announced in June 20X4. At 31 December 20X3, the United Nations will therefore not have a “legal” or “constructive” obligation to carry out the restructuring under IPSAS and hence no provision will be recognised. Further details regarding “restructuring” may be found in section 10.4 below.

3 Differentiation between payables, accruals, provisions and contingent liabilities

The classification of liabilities between provisions, accruals and payables will depend on the degree of certainty of the timing or amount of the future settlement of an obligation. As per the definitions in section 2 above, payables have the greatest degree of certainty, as they are based on invoices received, or where final amounts have been agreed with suppliers. For those goods and services received but not yet invoiced, or formally agreed, accruals are recognised within accounts payable. Accruals may therefore be considered as similar to provisions, as final amounts may not have yet been agreed.

The key difference between accruals and provisions however is the degree of certainty of timing or amount of the outflow. Although it is sometimes necessary to estimate the amount or timing of accruals, the uncertainty is generally much less than for provisions.

Diagram - Progression from contingent liabilities to payables

Accruals and payables are presented together within “accounts payable” on the statement of financial position, whereas provisions are presented separately.

The term contingent liability is used for liabilities that do not meet the recognition criteria (see section 5 below). Such a distinction is very important as contingent liabilities are not recognised as liabilities in the statement of financial position, but disclosed in the notes to the financial statements.

4 Opening statement of financial position – practical considerations

It should be noted the opening statement of financial position should include provisions that reflect conditions that existed at the date of transition to IPSAS besides other accruals and payables recognized in the opening statement of financial position. Such provisions should be based on the information which was available at the date of transition to IPSAS; hindsight should not be used.

5 Recognition

As noted in the introduction, there are three key recognition criteria for provisions:

- The United Nations has a present obligation (legal or constructive) as a result of a past event;
- It is probable that an outflow of resources embodying 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.

In order for a provision to be recognised, **all** of these conditions must be satisfied. In some cases, it is easy to determine this, however in others, significant judgement may be required by United Nations staff and, if necessary, independent external advisors. This section will examine each of these criteria in turn, and provide examples of how they can be considered and applied in the context of the United Nations.

5.1 Present obligation from a past event

In order to recognise a provision, the United Nations must have a **legal or constructive obligation** which results from an event in the past – in other words, the United Nations must have done something in the past for which it is now responsible for.

For this reason, any provision should relate to the financial position of the United Nations at the end of the financial year, and not its possible position in the future. Costs that need to be incurred to continue United Nations ongoing activities in the future should not be provided for. Provisions are therefore only recognised for obligations resulting from past events existing independently from the United Nations' future actions. In other words, if the United Nations ceased operations on the last day of the financial year, it would still need to pay the costs provided for, independent of future activities.

The obligation thus effectively represents the “reason” for an outflow of resources from the United Nations. Obligations may be either **legal** or **constructive** in nature. Whilst legal obligations may be easier to identify through contractual or legal terms, constructive obligations may be more difficult to determine and may require a more judgemental assessment.

Finally, it should be noted that provisions should not be raised for future losses or deficits occurring from future operations. These do not meet the definition of a liability, as in these cases there is no “present obligation” from a “past event”.

Future operating losses however may indicate that any asset used in the relevant operations may be impaired. In this case, an impairment review may need to be considered as discussed in Corporate Guidance #3 – Impairment of Property, Plant and Equipment.

***Note:** As noted in section 2.3 above, the term “obligation” under IPSAS should not be confused with “obligations” under UNSAS.*

5.1.1 Legal obligations

Legal obligations will derive from a contract, legislation or another operation of law. In essence, there is a document signed by the United Nations, governed by law, which holds the United Nations responsible for certain actions undertaken.

For example, the United Nations may sign a lease for a building in which the building is to be restored to its original condition at the end of the lease (e.g. any leasehold improvements made by the United Nations must be removed). In this case, the United Nations has a legal obligation to “make good” the building through the clause in the lease relating to restoration.

Example – Pollution of Peacekeeping bases

The United Nations has two Peacekeeping missions in operation, one located in Southern Lebanon (UNIFIL) and the other in Italy (Brindisi depot). In the bases for both, the storage of military equipment and general use of the base over time has led to environmental contamination of the site and surrounding area.

In Lebanon, there is no relevant or applicable environmental legislation covering the damage in question. Conversely, the Brindisi base falls under European Union environmental legislation where the United Nations can be fined for polluting and ordered to pay clean-up costs. Both positions are confirmed by legal advice received from the OLA.

Brindisi base:

For the pollution caused at Brindisi, there is a clear legal obligation for the United Nations to clean-up the pollution, and possibly pay a fine, through the requirements of the EU legislation. This is supported through the legal advice received.

Lebanon base:

In the case of the Lebanon base pollution, no such environmental legislation exists and as such there is no legal obligation for the United Nations to clean up the pollution (as supported through the legal advice obtained).

Note – these are simplified cases and the precise determination of a legal obligation will depend on the specific legislation. Legal advice is recommended where it is unclear whether the United Nations has a legal obligation.

In some cases, legislation in a country may change, whereby the United Nations may incur a legal obligation where one did not previously exist. Using the above example regarding decontamination costs, a change in environmental legislation in a certain country may make it obligatory for the United Nations to clean up each munitions storage site after use, where in the past this was not legally required. In such cases, a legal obligation is created at the point in which the legislation came into force, or when the legislation is virtually certain to be enacted as drafted.

It may be difficult in some cases to determine whether the United Nations has a legal obligation, particularly in lawsuits against the United Nations where a formal judgement has not been made by the court in question by the date of the preparation of the financial statements. In such examples, the OLA should be consulted - and external independent experts where appropriate - to assist in judging whether a legal obligation exists for the purposes of preparing the financial statements.

Note: discretion should be used when employing the services of experts to avoid incurring unnecessary costs and time – experts will not be needed in every case of a provision and judgement should be used to determine whether the potential complexity and value of the provision require such advice.

5.1.2 Constructive obligations

In addition to **legal obligations**, the United Nations may have an obligation even where there is no “legal” basis for the obligation. Instead, an obligation will arise from the past pattern of behaviour of, or communication from, the United Nations which raises valid expectations with the counterparty that the United Nations will accept and discharge the related responsibilities. This is known as a “**constructive obligation**”. The essence of a constructive obligation is the United Nations’ commitment to a third party.

For instance, the United Nations may have a past record of dismantling temporary buildings at the end of a mission and thus the United Nations will have a constructive obligation if the countries have a valid expectation that the United Nations will deconstruct these properties. This expectation will usually be based upon the behaviour of the United Nations in similar situations in the past, or through communications made by the United Nations in relation to the “event” in question (e.g. through a press statement or published policy on the United Nations website).

As noted above, the existence of a constructive obligation may not be straight-forward in some cases and will require professional judgement in terms of whether past behaviour or certain communications have raised a valid expectation with the counterparty that the United Nations will discharge its responsibilities. The United Nations may, for example, establish different expectations in different territories relating for similar types of actions; voluntary decontamination of Peacekeeping bases may be commonplace in urban areas but not in remote rural regions. Such historic behaviour is key in determining whether a constructive obligation arises.

One further example of a constructive obligation is the case of a restructuring, where a plan may have been agreed by United Nations management and communicated to the staff concerned. Even though the United Nations may not yet have signed a contractual agreement directly with any member of staff to leave the United Nations, the staff will have a valid expectation that the plan will be implemented, and as such the United Nations will have a “constructive obligation” towards the employee. Equally, a constructive obligation will not exist if the plan has not been communicated to the impacted employees or started by the end of the financial year.

Owing to their potential impact upon financial statements, restructuring plans are addressed explicitly in IPSAS 19, and further details regarding accounting for the plans may be found in section 10.4 below.

Example – Pollution of Peacekeeping base

The United Nations has a Peacekeeping mission - MONUSCO (formerly MONUC) - located near Kinshasa, Democratic Republic of Congo (DRC), where the storage of military equipment and general use of the base over time has led to environmental contamination of the site and surrounding area.

There is no relevant or applicable environmental legislation covering the damage in question and no legal obligation to pay for the decontamination of the site. The United Nations has however paid for the past costs of decontamination of previous MONUC and MONUSCO bases as part of its commitment to minimising its environmental impact in the region detailed in its environmental policy published on the United Nations website.

The United Nations must now review the contamination at the end of the year to determine whether it has a constructive obligation at the end of the financial year to decontaminate the site.

Given that the United Nations has a track record of decontaminating MONUC and MONUSCO sites (over and above local legislative requirements), and that there is a published decontamination policy upon its website, it is reasonable to assume that the Congolese authorities would have a valid expectation that the United Nations would pay for the decontamination of the Kinshasa site at the end of the mission.

The United Nations therefore has a “constructive obligation” to decontaminate the site, as a result of a past event (the contamination of the land) and should raise a provision for the anticipated decontamination cost if the other provision criteria are met. The provision should be recognised as the pollution occurs and the anticipated costs of decontamination develop.

Example – Dismantling of temporary offices

The United Nations has two bases for overseas missions in Port-au-Prince (Haiti) and in Monrovia (Liberia) where it has constructed a number of temporary office buildings on land owned by the local Government. There is no legal obligation in either country to dismantle these buildings (either under the local law or any contractual arrangements).

There are however different precedents set by the United Nations in the two locations regarding the dismantling of buildings constructed. In Haiti, the local Government has in the past successfully requested that the United Nations leaves the buildings at the end of the missions for use by the local population.

Conversely, the United Nations has in the past dismantled buildings in Liberia so that the areas in question can be developed by private investors.

The United Nations needs to consider whether it has a constructive obligation to dismantle existing buildings in each country. This should be considered from the point at which the building is originally constructed and reassessed annually.

Buildings in Port-au-Prince (Haiti)

In Haiti, the United Nations does not have not have a constructive obligation to dismantle the offices it has built, as the Government does not have a valid expectation that the buildings will be dismantled. This is because the United Nations has not dismantled buildings in the past in the country. A provision for the dismantling of the building should therefore not be recognised.

Buildings in Monrovia (Liberia)

In Monrovia, the United Nations does have a constructive obligation to dismantle the buildings, as its past practice of dismantling buildings has raised a valid expectation with the Liberian Government that any new temporary buildings will be dismantled in the future. The United Nations therefore has a “present obligation as a result of a past event” and should raise a provision for the anticipated dismantling cost if the other provision criteria are met. The provision should be recognised at the point of construction of the buildings as it is at this point that the United Nations knows that it has an obligation to dismantle in the future.

Example – Evacuation of staff

A United Nations office is located in an area which is experiencing significant social disturbances. In mid-December 20X4, the security situation quickly deteriorates. On 23 December 20X4 the United Nations office receives notice from the United Nations Department of Safety and Security (UNDSS) to stay alert and get ready for an emergency evacuation plan in case security situation continues to get worse. In case such evacuation notice is officially released, international staff and contractors are to be evacuated immediately and no more than 3 weeks from the notice date.

On 25 Dec 20X4, the UNDSS officially notifies United Nations office to start the evacuation. Full information was available relating to the number of staff, their dependants, and contractors whom United Nations needed to evacuate. At the date of notification, the costs related to the evacuation were estimated at \$2,400,000.

At 31 December 20X4, only initial evacuation steps had been taken, with costs incurred of \$100,000. The full evacuation was completed on 12 January 20X5, costing the United Nations a total of \$2,500,000 in associated expenses (including the \$100,000 incurred in 20X4). These costs are captured after 31 December 20X4 but before the date of preparation of the 20X4 financial statements.

Accounting in year-end 31 December 20X4:

At 31 December 20X4, no provision should be recognized nor contingent liability disclosed for the foreseen evacuation costs. This is because the United Nations does not have a present obligation resulting from a past event, as the evacuation “event” has not yet occurred. Even though an evacuation plan was in place and announced to the office in question, this does not qualify as a “restructuring” (as per Section 10.4 below), but is instead considered as a future operating cost. Expenses should only be recognized for the actual costs incurred in relation to the evacuation in 20X4 (i.e. the \$100,000 incurred).

The following accounting entries should be made in 20X4 to recognize these expenses:

Dr. Expenses (evacuation)	\$ 100,000
Cr. Accounts payable / cash	\$ 100,000

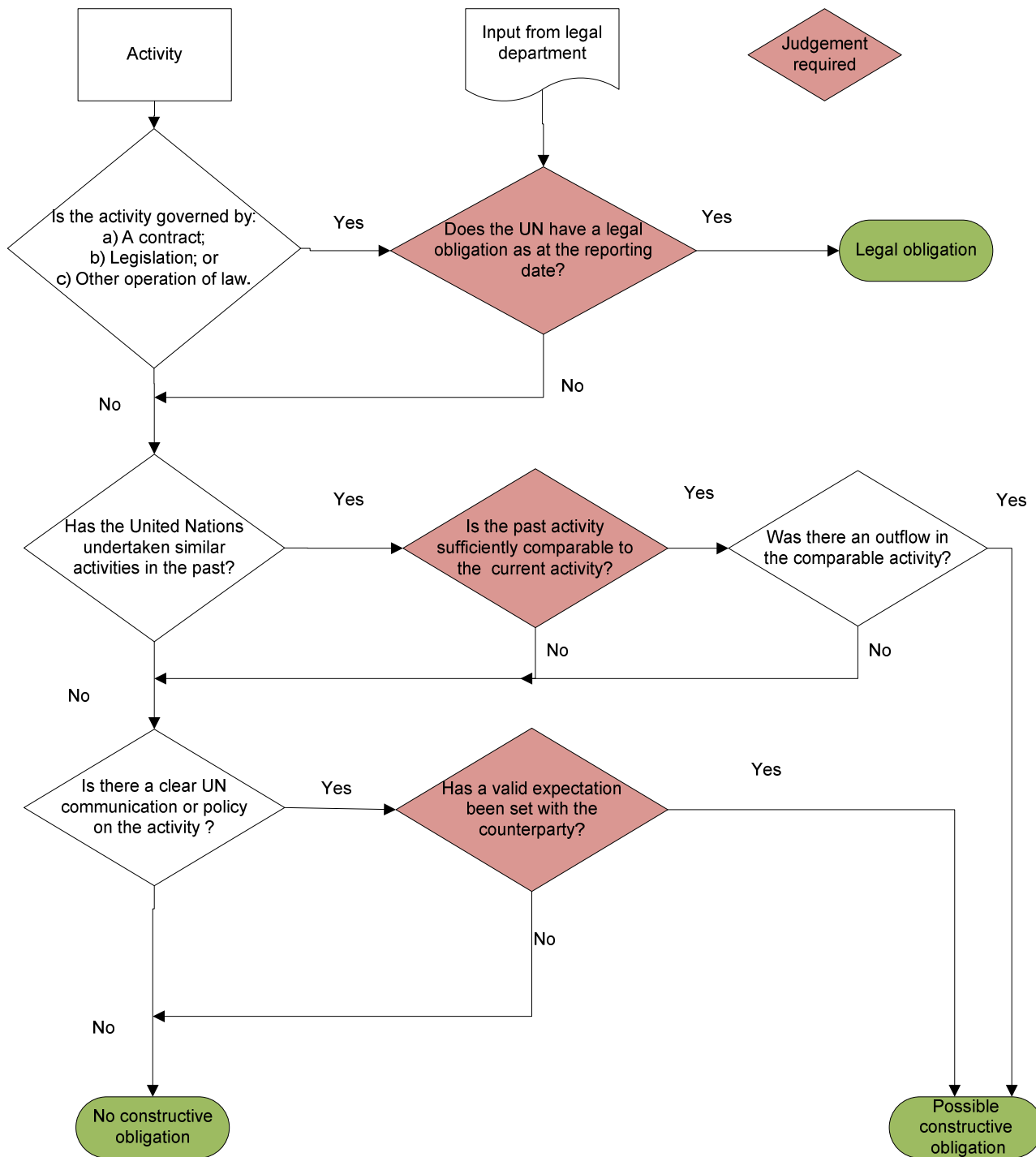
Accounting in year-end 31 December 20X5:

In 20X5, the United Nations should recognize an expense for the remaining costs incurred in 20X5 (i.e. \$ 2,400,000).

The following accounting entries should be made in 20X5 to recognize these expenses:

Dr. Expenses (evacuation)	\$ 2,400,000
Cr. Accounts payable / cash	\$ 2,400,000

Flowchart – Decision tree to assist the determination of legal and constructive obligations



Note – the above flowchart should be used as a starting point for guidance to inform the overall thought process for considering legal and constructive obligations. Precise classification will be a matter of judgement based on the individual facts and circumstances of the case in question.

5.2 Probable outflow of resources embodying economic benefits or service potential

The second recognition criterion is that there should be a probable outflow of resources embodying economic benefits or service potential to settle the **obligation**. This means that in order for a **provision to be recognised**, it should be more probable than not that the outflow of resources will occur. Whilst IPSAS does not specify a precise numerical threshold, this is generally accepted as having a probability of greater than 50% of occurring.

Should the probability of the outflow be less probable, a **contingent liability** should be disclosed in the notes to the financial statements by the United Nations (but not recognised in the statement of financial position). If the probability is considered **remote** (i.e. highly unlikely), no entries or disclosures should be made (see example in section 5.4 below).

Again, in some cases the probability of an outflow may be relatively straight-forward to determine; for an onerous lease it is probable that the United Nations is contractually (and therefore legally) committed to future outflows. The condition for probable outflow of resources is therefore met.

In many cases, however, the probability of the outflow of resources may not be clear-cut, and may therefore require an element of judgement to determine. Legal cases are good examples of this, where the cases may be in early stages, and it can be unclear whether the United Nations will be found liable or not. Where the probability is not clear, the United Nations should, where possible, make use of independent experts (such as OLA) to assist the determination of the probability of the outflow. In many cases, such experts can also assist with the determination of the other recognition criteria for provisions at the same time (i.e. whether obligations exist and whether costs can be measured reliably). For legal cases, the relevant lawyers should be consulted, whilst for environmental contamination, an environmental consultant may be required.

Where several similar obligations exist (e.g. compensation claims from inhabitants of a village impacted by a Peacekeeping mission), the probability of outflow may be determined by considering the class of the obligation as a whole.

5.3 Reliable estimate

Finally, a reliable estimate of the value of the obligation is necessary in order to recognise a provision. In most cases, the United Nations should be able to determine a range of possible values and thus form a reliable estimate. The use of accounting estimates to determine the value of the obligation is permitted and encouraged where precise values are not available. Further details concerning the use of estimates may be found in section 6.1 below, where the measurement of provisions is examined.

In the very rare cases where an obligation cannot be reliably measured, a contingent liability should be disclosed.

5.4 Contingent liabilities

As noted above, **contingent liabilities** are (a) a possible obligation that arises from past events, or (b) a present obligation that arises from past events, where outflow of resources is not probable or where the amount of the obligation cannot be measured with sufficient reliability.

Contingent liabilities should not be recognised by the United Nations. This means that no entries should be made in the statements of financial position or performance, cash flow statement or statement of changes in net assets for contingent liabilities. This is critical, as the uncertainty of one or more component of contingent liabilities means that no impact on the net liabilities of the United Nations should be recognised for such items.

Instead, a contingent liability should only be disclosed in the notes to the financial statements, in line with the disclosures set out in section 9 below.

It should be noted however that circumstances may change such that a contingent liability may meet the recognition criteria for provisions in later periods. Fresh consideration of the criteria should therefore be given at the end of each reporting period in order that any new events are taken into account each year. Section 7 below provides further details regarding changes in provisions.

Contingent liabilities may also be disclosed in cases where the United Nations is jointly and severally liable for an obligation. The amount disclosed as a contingent liability would be the component of the obligation that is to be settled by other parties, with a provision recognised for the component that the United Nations must settle (if this meets the provision recognition criteria).

Examples of contingent liabilities include legal cases or environmental contamination where there is more than a remote chance that the United Nations will be found liable, but where the likelihood is not “probable”.

Note – contingent liabilities are only disclosed where significant; the United Nations should not disclose every possible item that meets the above criteria, but instead use judgement to determine which information would be of significant importance to the users of the financial statements (i.e. material by value or nature).

Example – Legal case for serious road traffic incident in Nairobi, Kenya

In September 20X1, a United Nations lorry carrying explosives and personnel collides with a government school bus in the centre of Nairobi, Kenya, on its way to the OAH in the city. There are several injuries and fatalities in both vehicles.

In December 20X1, the families of children travelling in the school bus who were involved in the incident take the United Nations to court for fixed damages and the case is in progress at the 31 December 20X1. At this point in time, the legal advice provided by the OLA is that the driver of school bus was negligent and that there is a low (but not remote) probability that the United Nations will be found liable for the crash and therefore damages. A reliable estimate of the potential costs of damages can be made.

In May 20X2, the court rules in favour of the United Nations and all charges are dropped. No payments are made by the United Nations for damages and no further claims are expected. The financial year end is 31 December.

Assessment at 31 December 20X1:

Based on the legal advice received from OLA, a **contingent liability should be disclosed** in the financial statements for the potential damages payable from the legal case, but **no provision recognised**. Although one of the recognition criteria for provisions has been met based on the amount sued for (reliable measurement), the **probability of the outflow of resources embodying economic benefits or service potential is unlikely** (i.e. less than 50%) as it is likely that the court will rule in favour of the United Nations and

based on the legal advice there is no legal obligation as a result of past events. However, there is more than a remote possibility of an outflow and therefore disclosure of a contingent liability is appropriate.

Assessment at 31 December 20X2:

No contingent liability will be disclosed or provision recognised at 31 December 20X2 as the case has been concluded and charges dropped. There is only a very remote chance of further charges being raised and therefore no entries should be made for this case.

5.5 Contingent assets

As noted above, **contingent assets** are possible assets that arise 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 United Nations.

Contingent assets should not be recognised by the United Nations. This is critical, as the uncertainty of one or more component of contingent assets means that no impact on the net assets of the United Nations should be recognised for such items.

Instead, a contingent asset should only be disclosed in the notes to the financial statements, in line with the disclosures set out in section 9 below. However, the point at which the United Nations should disclose a **contingent asset** in the financial statements is different to the one at which a **contingent liability** is disclosed.

Contingent assets are only disclosed when it is “more probable than not” that economic benefits or service potential will flow to the United Nations. An asset will only be recognised when the inflow of economic benefits or service potential to the United Nations is “virtually certain”. No disclosure is required if the inflow is not “probable”.

Examples of contingent assets include legal cases which are likely to conclude in payment of compensation to the United Nations, or claims to land where it is more probable than not that the United Nations will be able to gain title to the land. For a contingent asset to be disclosed there is usually an element that will be outside of the United Nations’ control which prevents the recognition of an asset on the statement of financial position.

As with contingent liabilities, circumstances will change and therefore contingent assets should be continually reassessed at the end of each reporting period in order to determine the correct accounting treatment for the reporting period in question.

Note – contingent assets are only disclosed where significant; the United Nations should not disclose every possible item that meets the above criteria, but instead use judgement to determine which information would be of significant importance to the users of the financial statements (i.e. material by value or nature).

Example – Legal case for serious road traffic incident in Nairobi, Kenya

Using the above example, in September 20X1 a United Nations lorry carrying explosives and personnel collides with a government school bus in the centre of Nairobi, Kenya, on its way to the OAH in the city. There are several injuries and fatalities in both vehicles and in addition, the explosives contained in the lorries are irreparably damaged.

In November 20X1, the United Nations takes the Kenyan Government to court for compensation and damages relating to the fatalities and injuries resulting from the incident and the damaged inventory.

At 31 December 20X1, the case is ongoing. Following legal advice from OLA, it is understood that it is more likely than not that the Kenyan Government (through its employee) will be found liable for causing the incident and that compensation is likely to be payable to the United Nations for the staff fatalities and injuries.

However, the OLA estimates that it is unlikely that the United Nations will be able to recover costs from the Kenyan Government for the damage to the United Nations lorry and the inventory.

After prolonged legal proceedings, in November 20X2 the court rules in favour of the United Nations for all of the charges, including the fatalities and injury claim and also the damage to the lorry and the inventory. The court orders the Kenyan Government to pay \$3,000,000 to the United Nations to settle the entire case. This remained unpaid at 31 December 20X2 but was paid in full in January 20X3.

Assessment at 31 December 20X1

The United Nations should disclose a contingent asset in the financial statements relating to the fatalities and injuries to staff given that it is more likely than not that the Kenyan Government will have to pay damages to the United Nations. However, as there is still a degree of uncertainty around the outcome of the case, an asset for the potential amount receivable should not be recognised.

No contingent asset should be disclosed for the amounts recoverable for the lorry and inventory as it is less than 50% likely that the United Nations will win this part of the lawsuit.

Assessment at 31 December 20X2

The United Nations should now recognise an asset (receivable) in its financial statements as the case has completed and the inflow of the damages and compensation from the Kenyan Government is virtually certain at the end of the financial year, given the court's decision in favour of the United Nations and precise value of the amounts of damages awarded. In addition, payment of the amount in the next financial year (but during the preparation of the 20X2 financial statements) adds a further degree of certainty that the inflow will take place as at the year end.

5.6 *Summary of recognition of provisions and contingent liabilities*

Where, as a result of past events, there may be an outflow of resources embodying future economic benefits or service potential in settlement of: (a) a present obligation , or (b) a possible obligation whose existence will be confirmed only by the occurrence or non-occurrence of <u>one or more uncertain future events</u> not wholly within the control of the United Nations.		
There is a present obligation that probably requires an outflow of resources.	There is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources.	There is a possible obligation or a present obligation where the likelihood of an outflow of resources is remote.
A provision is recognized	No provision is recognized	No provision is recognized
Disclosures are required for the provision	Disclosures are required for the contingent liability	No disclosure is required

A contingent liability also arises in the extremely rare case where there is a liability that cannot be recognized because it cannot be measured reliably. Disclosures are required for the contingent liability.

5.7 *Summary of recognition of assets and contingent assets*

Where, as a result of past events, there is a <u>possible asset</u> whose existence will be confirmed only by the occurrence or non-occurrence of <u>one or more uncertain future events</u> not wholly within the control of the United Nations.		
The inflow of economic benefits or service potential is virtually certain	The inflow of economic benefits or service potential is probable, but not virtually certain.	The inflow of economic benefits or service potential is not probable.
The asset is not contingent and recognized in the financial statements.	No asset is recognized.	No asset is recognized.
Disclosures in line with specific IPSAS disclosure requirements for asset (s) contained in relevant Standard.	Disclosures are required.	No disclosure is required.

6 Measurement

The measurement of a provision is critical in determining the financial impact upon the United Nations in a reporting period. Measurement should be based upon the best estimate the United Nations can make, taking into account the risks and uncertainties of the outflow and the effect of the time value of money (for long-term provisions), in addition to consideration of future events which may inform the measurement of a provision.

6.1 Best estimate

A best estimate should be made based on the amount required to settle the obligation as at the reporting date (i.e. the financial year-end), and should represent what the United Nations would rationally pay to settle the obligation or transfer the obligation to a third party.

Management judgement is an integral component of forming a best estimate. An estimation, by its very nature, may not be 100% accurate when compared to the final settlement of the obligation in the future, however for the purposes of provision measurement, the best estimate should be as accurate as possible given the potential information available. For recognition in the financial statements, an estimate should always be materially accurate.

Whilst in some cases, an estimate may be simple to establish, such as fixed amounts stipulated in an onerous lease, other estimates may be difficult to determine and may therefore require independent expert advice to establish an accurate value. United Nations staff should use their judgement in determining their own capacity to form a best estimate given their experience, and consult experts where appropriate. Experts should only be consulted where the United Nations does not have the in-house capacity to obtain a best estimate.

For large populations of similar obligations, a weighted outcome should be used, by weighing all possible outcomes and probabilities to determine an “expected value”. Should there be a continuous range of values of equal possibility, the mid-point should be used.

For single obligations, there may be several possible outcomes. Whilst the individually most likely outcome may also often form the best estimate, other outcomes should also be considered as these may also impact the overall measurement of the provision. For instance, if the other possible outcomes will result in a higher cost to the United Nations than the individually most likely one, these should also be taken into account when forming the best estimate.

Note – any assumptions used in forming a best estimate need to be reliable and auditable.

Example – Weighted “expected value”

The United Nations is forced to change terms and conditions for its entire staff such that all staff are able to apply individually for an additional benefit dependant on their personal circumstances, payable retrospectively.

It is expected that for 1,000 members of staff:

- 20% of staff may be paid \$10,000 each;

- 30% of staff may be paid \$15,000 each; and
- The remaining 50% will paid \$nil each.

The expected value will be calculated as follows:

$$\begin{aligned}
 \text{Expected value} &= (20\% * 1,000 * \$ 10,000) + (30\% * 1,000 * \$ 15,000) \\
 &= \$ 2,000,000 + \$ 4,500,000 \\
 &= \mathbf{\$ 6,500,000}
 \end{aligned}$$

Accounting entries:

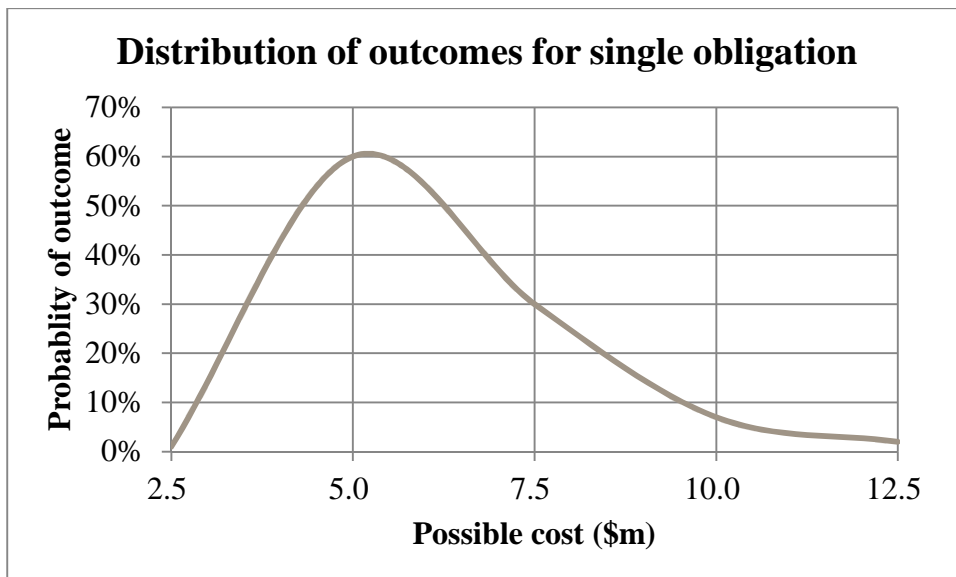
Dr. Staff expenses	\$ 6,500,000
Cr. Provisions	\$ 6,500,000

Example – Distribution of outcomes for single obligation

The United Nations employs an environmental consultant to estimate possible decontamination costs for a Peacekeeping site based on the current level of pollution at the site.

The consultant estimates costs for five possible outcomes, and indicates that the costs for the most likely outcome will be \$5,000,000. However, this value is at the low end of the range of outcomes and greater costs may be possible (although less likely):

Outcome	1	2	3	4	5
Possible cost (\$m)	2.5	5.0	7.5	10.0	12.5
Probability of outcome	1%	60%	30%	7%	2%



The best estimate should therefore take into account not just the most likely outcome (\$5m) but also include consideration of the other outcomes:

Outcome	1	2	3	4	5	Total
Possible cost (\$m)	2.50	5.00	7.50	10.00	12.50	
Probability of outcome	1%	60%	30%	7%	2%	
Expected value (\$m)	0.025	3.000	2.250	0.700	0.250	6.225

The expected value of the provision would therefore be approximately \$6.225m.

6.2 Risk and uncertainty

The risk and certainty of an obligation (or potential asset) should be considered with a degree of caution. Certain outcomes relating to a provision or contingent asset may represent very high or low potential inflow or outflows for the United Nations. However, if they are very uncertain, this should be taken into account for the measurement of the provision or contingent asset. The key reason for this is to avoid excessive or exaggerated provisions where they are not necessary.

For example, in the above decontamination example, there may also be a sixth outcome where the United Nations may have to pay \$50m for pollution of the surrounding area. The environmental expert has stated that the likelihood of this is virtually zero and thus the United Nations should not include this amount when forming the best estimate as it would increase the provision unnecessarily.

6.3 Present value – discounting

Provisions should be discounted to the present value of the outflows required to settle the obligation where the effect of the time value of money is material.

In other words, the measurement of an obligation will vary depending on when the amount in question will be settled; \$1m payable four weeks from the reporting date will be worth more in present terms than \$1m payable four years after the reporting date.

Where discounting of a provision occurs over a number of years, the present value of the provision will increase at the end of each year as the settlement date approaches, with the increase in the provision due to the movement of time recognised as an interest expense. This is known as the “unwinding” of the discount rate and such interest expenses should be disclosed separately in the note to the provision.

The discount rate used for the provisions should be the pre-tax rate which reflects the current market assessment of risks specific to the liability. However, the rate should not reflect risks for which future cash flows have already been adjusted in the calculation of the provision. The discount rate will be based on the opportunity cost which is the rate of return that could have been earned from investments held in Cash Pools. This will be provided by UN Treasury every 6 months.

For further details on setting appropriate discount rates, we refer to Corporate Guidance #8 - Employee Benefits.

Note – discounting is not often applied in practice, mainly due to the uncertainty regarding timing and amount of cash flows. Discounting should only be applied where the effect of the time value of money is material; small provisions (e.g. \$10,000) do not require discounting.

Example – Dismantling costs payable four years after construction

The United Nations completes construction of a temporary office on 1 January 20X1 and is due to dismantle a building upon the end of a mission on 31 December 20X4 and receives a quote from a local firm that it will cost \$5,000,000 (at 31 December 20X4) to fully dismantle the building and restore the site. This estimate does not change over the life of the building.

The pre-tax discount rate used by the United Nations is 5%. The financial year-end is 31 December and 20X1 is the first year where the costs meet the provisions recognition criteria.

Present value at 31 December 20X1:

The cost of the potential dismantling at the year-end must take into account the present value of the anticipated outflow. The present value (PV) of the outflow is using the relevant discount factor:

$$\text{Discount factor} = \frac{1}{(1 + \text{discount rate})^{(\text{years to payment})}}$$

$$\begin{aligned} \text{PV} &= \$ 5,000,000 * (1 / [1.05]^3) && \text{(3 years until payment)} \\ &= \$ 5,000,000 * 0.864 \end{aligned}$$

= **\$ 4,319,188** **at 31 December 20X1**

Accounting entries:

Dr. Assets (building)	\$ 4,319,188	
Cr. Provisions		\$ 4,319,188

Present value at 31 December 20X2

At the end of the next financial year, the present value of the outflow should be recalculated, as there are now only two years to the expected outflow date. This will result in a higher value provision, with the increase in the provision recognised as an interest expense:

PV	= \$ 5,000,000 * (1 / [1.05] ²)	(2 years until payment)
	= \$ 5,000,000 * 0.907	
	= \$ 4,535,147	at 31 December 20X2

Movement in provision = \$ 4,535,147 - \$ 4,319,188 = **\$ 215,959**

Accounting entries:

Dr. Interest expense	\$ 215,959	
Cr. Provisions		\$ 215,959

Note – accounting entries for the asset recognised above should be made in line with IPSAS 17.

Remaining years:

The following table can be used to calculate the present value of the obligation and interest expense at each year end:

Anticipated costs (\$)	5,000,000
Date of settlement	31/12/X4
Discount rate "D"	5%

Year ended	Years to payment "Y"	Discount factor = 1 / ([1 + "D"] ^ "Y")	PV	DR Interest expense CR Provision
31/12/X1	3	0.864	4,319,188	-
31/12/X2	2	0.907	4,535,147	215,959
31/12/X3	1	0.952	4,761,905	226,757
31/12/X4	0	1.000	5,000,000	238,095

If the obligation is settled at 31 December 20X4, the provision is fully “utilised” and the value of the provision at the year-end is zero.

A further example of the calculation of present values for multiple payments is included in section 10.3.2 below.

6.4 Future events

The determination of a best estimate should take into account any relevant future events, to the extent that they are able to inform United Nations management about the potential future costs or outflows resulting from the obligation present at the reporting date.

Thus, while the recognition of a present obligation requires a “past event”, the measurement of the obligation may make use of future events related to the “past event” to form a more accurate view of the true value of the obligation.

For example, the United Nations may take into account future advances in decontamination technology or experience when measuring a decontamination provision, where it is anticipated that the technology or experience will be available when decontamination takes place. Equally, if a future obligation is index-linked, the rate of inflation should be used in determining the future costs of settlement.

Such future events should however only be reflected where there is sufficient evidence and certainty that they will occur. Equally, any future legislation which may apply to costs of settling the obligation in question should only be considered in the measurement of an obligation when it is virtually certain to be passed.

Note – where a significant event occurs after the reporting date but before the date that the financial statements were authorised for issue, the impact upon the financial statements should be considered in line with Corporate Guidance #16 – Events after the reporting date.

6.5 Disposal of assets

Any proceeds anticipated from the disposal of assets to be used in settlement of the obligations should not be taken into account when measuring a provision, even if the disposal is closely linked to the obligating event. Instead, such gains or losses on disposal should be recognised and measured in line with the Standard relevant for the asset.

For example, if the United Nations plans to sell storage facilities which are owned near a rented office subject to an onerous lease, the anticipated proceeds of the storage facility should not be used in determining the amount required to settle the onerous lease obligation.

6.6 Reimbursements related to provisions

In the case of some provisions, the United Nations may receive reimbursement from a third party (e.g. a contractor or Government) for full or partial settlement of an obligation. Where such reimbursements meet the definition of an asset:

- a) A separate asset should be recognised on the statement of financial position - the “debit” entry is not offset against the provision (i.e. balances are shown gross on statement of financial position); and

- b) The corresponding “credit” entry of the reimbursement may be offset against (i.e. deducted from) the expense recognised for the provision (i.e. “revenue” and expense are shown net on statement of financial performance). This means that no revenue is shown for the reimbursement, but instead reduced or zero expense.

The amount of reimbursement recognised should not exceed the amount of the provision.

Example – Reimbursement for settlement of an obligation

Following an incident involving the injury of private sector contractors by United Nations troops, the United Nations is taken to court by the private contractor. Legal advice received from OLA indicates that the contractor will win the case and that \$20m of damages and compensation are anticipated.

The OLA has also been in discussion with the troops’ national Government and has agreed that the Government will pay the United Nations up to \$30m due to its role in the incident, depending on the damages to be paid by the United Nations. The receipt of the cash meets the recognition criteria for an asset, and it is virtually certain to be received from the Government if the United Nations settles the case with the contractor.

The United Nations should therefore recognise a provision of \$20m relating to the obligation to compensate the contractors, as the provision recognition criteria have been met. The United Nations should also recognise a separate asset of \$20m on the statement of financial position to reflect the portion of the Government’s reimbursement up to the value of the United Nations’ obligation to the contractor. The additional \$10m potential reimbursement is not recognised as it is in excess of the amount of the provision.

On the statement of financial performance, a net expense of zero should be recognised. This is because the expense recognised with the provision is offset by the reimbursement from the Government.

The accounting entries would therefore be:

To recognise the provision:

Dr. Compensation expense	\$ 20,000,000
Cr. Provision for compensation (liabilities)	\$20,000,000

To recognise the reimbursement:

Dr. Reimbursement due from Government (assets)	\$ 20,000,000
Cr. Compensation expense	\$ 20,000,000

The net impact on the statement of financial performance is therefore zero. A separate asset and provision are presented in the statement of financial position.

7 Changes in provisions

As circumstances surrounding provisions and contingent liabilities rarely remain the same over the course of time, provisions and contingent liabilities should be reviewed at the end of each financial year, to ensure that the initial recognition and measurement is still appropriate, and also that the disclosures made are still relevant.

7.1 Changes in recognition and reversal of provisions

Firstly, provisions and contingent liabilities may interchange, depending on whether the circumstances relating to the “event” meet the necessary recognition criteria at the end of the financial year in question. It is possible for example that the outcome of a legal case may become more or less certain from one year to the next. The judgement of the OLA regarding the likelihood of an outflow of resources embodying economic benefits or service potential may also change from one year to the next depending on legal circumstances at the end of each financial year.

A provision recognised in one financial year may therefore be reversed and instead disclosed as a contingent liability in the next financial year. Equally, a contingent liability disclosed in one year may be recognised as a provision in later years if it meets the provision recognition criteria in later years.

Where a provision is no longer required (i.e. where the provision recognition criteria are no longer met), it should be reversed. A provision can be fully or partially reversed depending on the specific circumstances.

For example, new information may be available on a legal case which significantly raises the probability of an outflow and which may therefore result in the recognition of a provision where a contingent liability had been disclosed in previous periods. Equally, a case against the United Nations which was provided for in one year may be dropped in the next year, meaning that the provision should be reversed. In such cases of the partial or full reversal of a provision, the following accounting entries should be made:

Dr. Provision	[value of reversal]
Cr. Reversal of provisions (expense)	[value of reversal]

***Note:** the reversal of a provision results in a credit “expense” entry as “reversal of provisions” and should not be recognised as “revenue” in the statement of financial performance.*

7.2 Changes in measurement

Secondly, whilst the recognition criteria may still be met, the best estimate of the settlement of the obligation may change between financial years on receipt of more information or new events relating to the obligation. For example, new technologies may have been developed in the financial year which significantly reduce the cost of environmental decontamination and therefore revise the measurement of the provision from the previous financial year.

The best estimate of the provision should therefore be reviewed annually.

Should any new legislation be introduced that may influence the provision, it should also be taken into consideration in the recognition and measurement of provisions. This should not be done retrospectively, but instead from the point at which the legislation came into force.

7.3 Utilisation of provisions

Finally, provisions may be “utilised” in the financial year, meaning that part of the obligation may be settled in the financial year. This will reduce the value of the provision at the end of the financial year, although the remaining portion of the obligation may change in value depending on events. The utilisation of a provision is disclosed in the notes to the financial statements.

For example, the United Nations may recognise a \$10m provision for two potential future payments of approximately \$4m and \$6m over two years. When the first \$4m payment is made, \$4m of the provision is “utilised”, leaving \$6m remaining.

Note: Only relevant expenditure should be offset against a provision. In other words, only those costs for which the provision was originally intended can result in the “utilisation” of the provision. For example, the lease payments for an onerous lease previously provided for may be offset against that provision. Lease payments for other (non-onerous) leases should not however be offset against the onerous lease provision.

As noted in section 6.3 above, the present value of provisions will also increase at the end of each financial year if they are discounted, even if all other factors remain equal. This is due to the change in the time value of money, and the increase in the provision is recognised as an interest expense in the financial year. The impact of the “unwinding” of the discount rate should therefore be calculated annually.

Example – Changes in a provision over time

In September 20X2, the United Nations pollutes the site of a base and meets the recognition criteria for a provision at that point. The pollution is estimated to cost \$2m to decontaminate. This estimate remains the same at 31 December 20X2.

At 31 December 20X3, the United Nations is still at the site, however the costs of decontaminating the site are reassessed as \$1.5m due to new technologies available.

In 20X4, the United Nations leaves the site, and incurs costs of \$400,000 in August 20X4 towards the initial decontamination; these were paid in September 20X4. At 31 December 20X4, the United Nations estimates that the remaining decontamination costs will be \$1.1m.

On 25 February 20X5, the United Nations completes the decontamination work and pays the final costs of \$1.1m to a decontamination team. As a result of a site inspection on the date of the final payment, it is determined that there is no further obligation for the United Nations to pay decontamination costs in relation to the pollution.

Accounting treatment in year-ended 31 December 20X2:

The United Nations should recognise a provision for the best estimate of the decontamination costs of \$2m in September 20X2, which remains unchanged at 31 December 20X2 (in practice, this may be recognised at 31 December 20X2). The following accounting entries should be made:

Dr. Expenses (decontamination)	\$ 2,000,000
Cr. Provisions for decontamination	\$ 2,000,000

Accounting treatment in year-ended 31 December 20X3:

In 20X3, the United Nations still retains an obligation to settle the decontamination costs, and therefore a provision should be maintained in the statement of financial position at 31 December 20X3. The best estimate of the provision has however now changed and the provision should therefore be measured at \$1.5m. The reduction of \$500,000 should be recognised as a “credit” to expenses and not recognised as revenue.

Such an adjustment should be made at the point at which the change in estimate is known in 20X3, however, it is likely that this will be a year-end adjustment as it is likely that the value of the decontamination costs will be reviewed at the end of the financial year.

The following accounting entries should be made:

Dr. Provisions for decontamination	\$ 500,000
Cr. Reversal of provisions (expenses)	\$ 500,000

Accounting treatment in year-ended 31 December 20X4:

In the year, the United Nations incurs eligible costs of \$400,000 and pays cash a month later. This is considered to be “utilisation” of the provision, as the costs incurred related to the purpose for which the provision was originally intended. No reversal or increase to the remaining provision is required as the estimated costs of settlement at 31 December 20X3 (\$1.1m) are equal to the opening provision (\$1.5m) less the “utilised” component (\$400,000).

The following accounting entries should therefore be made in the financial year:

On incurring eligible decontamination costs:

Dr. Provisions for decontamination	\$ 400,000
Cr. Accounts payable	\$ 400,000

On subsequent payment:

Dr. Accounts payable	\$ 400,000
Cr. Cash	\$ 400,000

No further accounting entries are made in the financial year relating to the decontamination provision.

Accounting treatment in year-ended 31 December 20X5:

In the financial year, the United Nations fully settles the obligation at the same amount estimated at 31 December 20X4 (i.e. \$1.1m), thus the provision is considered to be fully “utilised”, with no further “reversals” made.

The following accounting entries should therefore be made in the financial year:

On incurring and paying eligible decontamination costs:

Dr. Provisions for decontamination	\$ 1,100,000
Cr. Cash	\$ 1,100,000

No further accounting entries are made in the financial year relating to the decontamination provision.

There is subsequently no remaining provision for the decontamination costs, as the outstanding provision is fully “utilised” in 20X5 and no further costs or remaining obligation exist after February 20X5.

8 Presentation considerations

Provisions should be presented as one line on the face of the statement of financial position. In the supporting notes to the financial statements, provisions may be classed together (i.e. aggregated) when the narrative disclosures can cover all of the relevant provisions in a single statement.

The following classes of provisions should be used by the United Nations*:

- a) Death and disability claims from Troop and Police Contributing Countries;
- b) Restoration costs;
- c) Restructuring;
- d) Onerous contracts;
- e) Legal cases;
- f) Claims submitted to the United Nations Compensation Commission;
- g) Self-insurance¹; and
- h) Other

* A new class of provision should only be used where a material provision is recognised for an obligation which cannot be covered by narratives for the classes (a) to (g) above.

Provisions should be split between their long- and short-term components on the face of the statement of financial position and also in the related notes in line with IPSAS 1. The long-term component should represent amounts which are due to be settled in more than 12 months from the end of the reporting date.

9 Disclosure requirements

Given the uncertain nature of provisions, contingent liabilities and contingent assets, disclosures are important to assist the user of the financial statements in understanding the nature and circumstances of the events concerned. This is particularly relevant for contingent liabilities and contingent assets, where liabilities and assets are disclosed but not recognised.

9.1 Disclosures for provisions

For each class of provision, the United Nations should disclose the following figures:

- a) The carrying amount at the beginning and end of the period (in line with section 6 above);
- b) Additional provisions made in the period, including increases to existing provisions;

¹ The United Nations recognizes various payables with regards to its self-insurance scheme. Please refer to Corporate Guidance #8 Employee benefits for further information.

- c) Amounts used (i.e. incurred and charged against the provision) during the period (section 7.3 above);
- d) Unused amounts reversed during the period; and
- e) The increase during the period in the discounted amount arising from the passage of time and the effect of any change in the discount rate (the “unwinding” of the discount rate, section 6.3 above).

This is normally disclosed through a reconciliation of movements between the opening and closing balances.

In addition, the following narrative disclosures should be made for each class of provision:

- a) A brief description of the nature of the obligation and the expected timing of any resulting outflows;
- b) An indication of the uncertainties about the amount or timing of those outflows. Where necessary to provide adequate information, the United Nations should disclose the major assumptions made concerning future events (as per section 6.4 above); and
- c) The amount of any expected reimbursement, stating the amount of any asset that has been recognized for that expected reimbursement.

If any of the above information is unavailable, or if publication of the information would prejudice a legal case, this fact should be disclosed in the notes.

Example - Note disclosures for provisions

\$m	Environmental restoration	Legal cases	Onerous leases	Death and disability claims	Restructuring	Total
At 1 January 20X1	30.0	22.0	4.2	3.0	26.0	85.2
Charged / (credited) to the statement of financial performance:						
Additional provisions in the period	12.0	1.0	1.2	30.0	2.0	46.2
Amounts used in the year	(4.0)	(2.0)	(3.0)	(10.0)	0.0	(19.0)
Reversal of unused amounts	(1.0)	(2.0)	(0.5)	(6.0)	0.0	(9.5)
Unwinding of discount and changes in discount rate	0.5	0.2	2.0	0.0	3.0	5.7
At 31 December 20X1	37.5	19.2	3.9	17.0	31.0	108.6

Analysis of total provisions:

	20X0	20X1
Non-current	45.0	60.0
Current	40.2	48.6
Total	85.2	108.6

(a) Environmental restoration:

The United Nations is responsible for the future decontamination costs of certain sites used during the course of its Peacekeeping operations. A provision is recognised for the present value of costs to be incurred for the restoration of these sites, totalling \$37.5m at 31 December 20X1. It is expected that \$10m will be used in 20X2 and \$27.5m in future years. During 20X1, restoration of sites in Afghanistan, Haiti and Kashmir was undertaken, and additional provisions for future decontamination recognised for contamination in Darfur and Ivory Coast.

(b) Legal cases:

The provision of \$19.2m represents claims from United Nations employees and third parties for a number of separate cases which the United Nations is currently defending. The information usually required under IPSAS 19 Provisions, Contingent Liabilities and Contingent Assets is not disclosed on the grounds that it can be expected to prejudice seriously the outcome of the litigation.

(c) Onerous leases:

The United Nations has a provision of \$3.9m for the present value of the future of the lease payments for land in New York which has not been used by the United Nations since 20X0 but where the lease cannot be exited until 20X7. In addition, due to the early termination of two Peacekeeping missions in 20X1, the United Nations has moved out of several office buildings in the relevant countries before the expiry of the leases covering those properties. A provision for \$1.2m has been recognised for these leases, which is net of any recoveries and sub-leasing foreseen at the sites.

(d) Death and disability claims:

The United Nations has a provision of \$17m resulting from incidents in which United Nations troops, police and staff have been killed or disabled whilst in service and where claims have yet to be finalised. Following attacks at three United Nations bases in 20X1, \$30m of claims were recognised in the financial year.

(e) Restructuring:

Following the closure of the United Nations Office Away from Headquarters in Country X in 20X0, a number of staff retired early. The United Nations must pay a lump sum to staff at their statutory retirement date. The lump sums will be paid between 20X5 and 20X8. In 20X1, an additional 10 members of staff were included in this scheme. The present value of the payments to be made relating to the restructuring was \$31.0m at 31 December 20X1.

9.2 Disclosures for contingent liabilities

A brief description of each class of contingent liability should be given, and in addition the following disclosures should be made where possible:

- a) An estimate of its financial effect, measured on the same basis as provisions in section 6 above;
- b) An indication of the uncertainties relating to the amount or timing of any outflow; and

- c) The possibility of any reimbursement.

Should the contingent liability relate to a provision recognised by the United Nations in the same financial statements, the narrative disclosures should show the link between the two.

Example – Note disclosure for contingent liability (at 30 June 20X2)

The United Nations is currently defending a court action from the families of three individuals who were shot and killed by United Nations Peacekeeping troops during a demonstration in Kosovo in August 20X1. The United Nations Office of Legal Affairs believes that the case can be successfully defended by the United Nations. The amount of any potential cannot be disclosed at this point in time as it may prejudice the outcome of the legal case. A verdict is expected in October 20X2.

9.3 Disclosures for contingent assets

A brief description of each class of contingent asset should be given, and where possible the financial effect, measuring the value of the contingent asset in line with section 6 above.

Prudence should be used in disclosures - unrealistic expectations should not be set with the user of the financial statements where the likelihood of the United Nations recognising an asset in the future is very limited.

Example – Note disclosure for contingent asset (at 31 December 20X1)

In 20X1 United Nations disclosed a contingent asset of \$500,000 for a portion of a grant paid to a beneficiary where the project expenditure was found to be ineligible following an ex-post grant audit. The grant audit was in the last stages of finalisation at 31 December 20X1 and it is probable that the United Nations will recover the funding from the beneficiary in 20X2.

Note – contingent liabilities and assets are only disclosed where significant; the United Nations should not disclose every possible item that meets the criteria in section 5 above, but instead use judgement to determine which information would be of significant importance to the users of the financial statements (i.e. material by value or nature).

10 Specific scenarios

10.1 Litigation and legal claims

During the course of its operations, the United Nations may be the subject of legal claims or litigation. Consideration of whether a provision should be recognised for such legal claims or litigation should cover the key recognition criteria (i.e. a present obligation from a past event, a probable outflow of resources embodying economic benefits or service potential and an amount reliably estimated). Whilst it is in only very rare cases that a reliable estimate cannot be made, the other two criteria will warrant particular focus:

Present obligation from past events

Often in a legal case the events might be disputed by the parties. Because of the uncertainty concerning the past event it will be unclear whether a present obligation exists.

In this type of situation, it may be necessary for the United Nations to obtain an expert's opinion (such as the OLA) in order to determine, after taking into account all the available evidence, whether or not a present obligation arises for which provision is required. On the basis of such information:

1. Where it is more likely than not that a present obligation exists at the reporting date, the United Nations should recognise a provision (if the other recognition criteria are met).
2. Where it is is not likely that a present obligation exists at the reporting date, the United Nations should disclose a contingent liability, unless the possibility of an outflow of resources or service potential embodying economic benefit is remote, in which case no disclosure is required

Outflow of economic benefits or service potential

With litigation, there will not only be a need to assess whether or not the evidence supports the fact that a past event has occurred (that is, that there is a case to answer), but there will also be a need to consider whether or not it is probable that an outflow of economic benefits or service potential will be required to settle the obligation. Again, it might be necessary to seek an expert's advice (such as the OLA) to estimate the probability of the case ending with judgement against the United Nations and the amount that might have to be paid to settle the case.

Where the provisions recognition criteria are not met, a contingent liability should be disclosed, unless the possibility of an outflow of resources embodying economic benefit is remote, in which case no disclosure is required. Contingent liabilities are usually disclosed when the United Nations has been taken to court for material amounts but where the probability of the United Nations losing the case is not probable (i.e. less than 50%).

Example – Staff challenging employment status

In September 20X3, the United Nations receives a claim from a number of staff challenging their “temporary” employment status and requesting compensation to align their employment conditions to those of “permanent” staff.

At 31 December 20X3, the case is in progress in the United Nations Dispute Tribunal and due to legal complications, a verdict had not been reached by the time of the preparation of the financial statements. The advice provided by the OLA however suggests that it is more probable than not that the United Nations has a legal obligation to the employees under employment law, and that it is highly probable that the case will be won by the employees, with compensation to be paid. The OLA is able to provide an estimate of the anticipated compensation due.

In June 20X4, the case is concluded in favour of the employees, and compensation paid by the United Nations to the employees.

Assessment at 31 December 20X3

Based on the advice provided by OLA, a provision for the legal case should be recognised in the financial statements for the year ended 31 December 20X3, as all three recognition criteria regarding the legal case have been met. The United Nations has a legal obligation towards the employees, an outflow of resources is more probable than not, and a reliable estimated of the outflow can be made.

10.2 Third party claims

Third party claims should be recognised in line with litigation and legal claims as per the guidance in section 10.1 above.

10.3 Restoration costs and other contractual obligations

10.3.1 Restoration costs

Clauses of a lease may require the United Nations to restore leased land or buildings to their original condition at the end of a lease term. Therefore, if the United Nations has modified the leased land or building during its use (for example through leasehold improvements in a leased building or by constructing a building on leased land), it may need to pay for restoration costs at the end of the lease.

Such restoration costs may include:

- (a) Dismantling of leasehold improvements; and
- (b) Dismantling of buildings at the end of a lease term (when built on leased land).

Where a contractual requirement to restore the leased land or buildings to their original condition exists:

1. The United Nations should recognise a provision for the anticipated dismantling costs at the point at which the leasehold improvements or buildings are constructed; and
2. The debit entry for these costs should be capitalised as part the cost of the leasehold improvement or building asset recognised on construction of the improvement or building, and included in the annual depreciation expense for the asset over its useful economic life.

A provision is recognised because the United Nations has a legal obligation to dismantle the leasehold improvements or buildings under the terms of the lease, and the probability of a future outflow of resources (i.e. payment of the dismantling costs) is probable. A reliable estimate of dismantling costs is also possible.

In some cases, the terms of the lease may not clearly define what actions the United Nations must take at the end of a lease. In addition, in the case of leases where liability is shared with a Government, there may be uncertainty regarding which restoration costs are due to be payable by each party concerned. In such cases, the lease should be worded (using OLA input where required) to clearly define these points. Where the wording cannot be edited and remains inconclusive, the United Nations should use judgement to determine whether a provision (based on a legal or constructive obligation) should be recognised by reviewing the provisions recognition criteria, consulting OLA where necessary.

Should a claim for restoration costs from landlord arise where no provision has previously been recognised, the claim should be treated in line with section 10.6 below (Claims under defacto lease arrangements).

Example – Restoration costs for leased warehouse in Lebanon (UNIFIL)

The United Nations has entered into a lease for a warehouse in Lebanon from a Lebanese landowner. The United Nations wishes to use the warehouse for office accommodation. It has planning permission to build a mezzanine floor and partition the building for offices at a cost of \$1.5m. The lease is for a period of 40 years and the property must be returned to the Lebanese landlord in its original condition as this is clearly specified in the lease. The United Nations estimates that it will cost \$500,000 in today's money to remove the improvements.

The United Nations should capitalise leasehold improvements of \$1.5m and depreciate them over the term of the lease. The United Nations also has an obligation under the lease to remove the improvements at the end of the lease term. The obligation arises as the United Nations completes the improvements and this represents a past event.

Therefore, if the improvements have been made by the financial year end, a provision for \$500,000 should be made for their eventual removal. In addition, an asset of the same amount should be recognised which will be recovered from the benefits generated by the business over the term of the lease. The asset should then be depreciated in line with the leasehold improvements capitalized above.

The accounting entries on construction of the leasehold improvements are as follows:

For the leasehold improvements:

Dr Assets (leasehold improvements)	\$ 1,500,000
Cr Payables / cash	\$ 1,500,000

For the restoration costs:

Dr Assets (leasehold improvements)	\$ 500,000
Cr Provisions	\$ 500,000

Note – the effect of the time value of the payment for the removal of the leasehold improvements is excluded from this example.

10.3.2 Other contractual obligations – onerous contracts

Under IPSAS 19, if an entity has a contract that is onerous, the present obligation under the contract should be recognised and measured as a provision. An onerous contract is defined as a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

A typical example of an onerous contract is an operating property lease which has been abandoned by the United Nations following the liquidation of a mission and cannot be sub-let. While an operating lease would be regarded as an executory contract, and executory contracts are generally outside the scope of IPSAS 19, an exception exists where such contracts are onerous. In this example it can be seen that the contract is onerous as the United Nations expects to receive no further benefit under the contract but it is still committed to pay the landlord the future rentals.

An onerous contract is no different to any other provision and must be recognised and measured in the same way as any other provision. In considering the scope of IPSAS 19, in respect of onerous contracts it is important to note that the standard does not apply to other provisions where a more specific standard exists, for example construction contracts.

When measuring a provision for onerous contracts, the best estimate should be the lower of

- a) The present value of future lease payments (up to the first point that it may exit the lease), net of any recoveries (i.e. sub-lease revenue); and
- b) Any penalty fee payable for early termination of the lease.

Example – Onerous contract in Sudan

In January 20X1, the United Nations starts a 25-year operating lease in Sudan for a new OAH building at \$500,000 per annum payable at the start of each year (i.e. in advance). The lease contains an exit clause whereby the United Nations may exit the lease without penalty after 10 years (i.e. 1 January 20Y1) or 20 years (1 January 20Z1). The penalty clause to exit the lease is otherwise \$5m.

In December 20X3, there is significant civil unrest in Sudan and the United Nations takes the decision to abandon the building due to security concerns. There is no possibility to sublet the building. The financial year end is 31 December and the United Nations discount rate is 5% per annum.

Accounting for the lease in 20X1 and 20X2

Following commencement of the lease in January 20X1, there are no foreseen issues with the operations in Sudan, and the United Nations expects to obtain future economic benefits and service potential from the use the building over the 25 years of the lease. The lease expense should therefore be recognised as a standard operating lease expense in 20X1 and 20X2 in line with Corporate Guidance #1 - Leasing.

Accounting for the lease at 31 December 20X3

The lease expense should be recognised as above until December 20X3. In December 20X3, the United Nations abandons the building and does not expect to obtain future economic benefit or service potential from the building after this time, as it can neither use nor sub-let the building. The lease is therefore considered to be onerous from December 20X3.

The United Nations should recognise a provision for the lower of the present value of the future lease payments up to the first break clause, and the lease exit penalty, as:

1. The United Nations has a present (legal) obligation as a result of a past event;
2. It is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; **and**
3. A reliable estimate can be made of the amount of the obligation.

The exit clause in the lease is \$5m, whilst the present value of the minimum lease payments may be calculated as follows:

Variable	Value
Annual lease payment (\$)	500,000
Payable on	1 January
First break clause	1 January 20Y1
Date of provision	December 20X3
Discount rate	5%

Payment date	Time from year-end (years)	Amount payable (\$)	Discount factor	Present value (\$)
01/01/20X4	0	500,000	1.000	500,000
01/01/20X5	1	500,000	0.952	476,190
01/01/20X6	2	500,000	0.907	453,515
01/01/20X7	3	500,000	0.864	431,919
01/01/20X8	4	500,000	0.823	411,351
01/01/20X9	5	500,000	0.784	391,763
01/01/20Y0	6	500,000	0.746	373,108
Total		3,500,000		3,037,846

The provision should therefore be measured at the present value of the minimum lease payments (\$3.038m), as this is lower than the exit penalty of \$5m.

The provision should be recognised using the following accounting entries:

Dr. Onerous lease expense	\$3.038m
Cr. Provisions	\$3.038m

Note – discounting is not often applied in practice, mainly due to the uncertainty regarding timing and amount of cash flows. Discounting should only be applied where the effect of the time value of money is material; small provisions (e.g. \$10,000) do not require discounting.

In this example, discounting has been applied to explain possible considerations, however at 31 December 20X3 the difference between the undiscounted provision (\$3,500,000) and the discounted provision (\$3,037,846) is \$462,154, which is likely to be immaterial. Discounting is therefore unlikely to be necessary in this example.

Accounting at 31 December 20X4

In 20X4, the United Nations makes the annual lease payment of \$500,000, which “utilises” part of the provision. In addition, at 31 December 20X4 the remaining payments are one year closer to the reporting date and their present value should be increased to reflect this. The increase in value of the present value of the future payments is recognised as an interest expense for the unwinding of the discount.

The tables below summarises the calculation of the present value of the minimum lease payments at 31 December 20X4, and the movement of the provision over the course of the year.

Payment date	Time from year-end (years)	Amount payable (\$)	Discount factor	Present value (\$)
01/01/20X5	0	500,000	1.000	500,000
01/01/20X6	1	500,000	0.952	476,190
01/01/20X7	2	500,000	0.907	453,515
01/01/20X8	3	500,000	0.864	431,919
01/01/20X9	4	500,000	0.823	411,351
01/01/20Y0	5	500,000	0.784	391,763
Total		3,000,000		2,664,738

Opening provision 1 January 20X4	3,037,846
Utilisation of provision	(500,000)
Unwinding of discount (balancing figure)	126,892
Closing provision 31 December 20X4	2,664,738

The transactions in the year should be recognised through the following accounting entries:

For payment of the annual lease payment:

Dr . Provision	\$ 500,000	
Cr. Cash		\$500,000

For the unwinding of the discount:

Dr. Interest expense	\$ 126,892	(Statement of financial performance)
Cr. Provision	\$ 126,892	

10.4 Restructuring

IPSAS 19 defines restructuring as “a program that is planned and controlled by management, and materially changes either: (a) the scope [of the United Nations’] activities or (b) the manner in which those activities are carried out”.

Examples of restructuring events may include the termination of an activity or service, the closure of an office or terminations of activities in a certain region, the relocation of activities from one region to another, a change in management structure (such as removing a layer of management), or fundamental reorganisations that have a material effect on the nature and focus of the United Nations’ operations.

10.4.1 Recognition of restructuring plans

The recognition of restructuring provisions is conducted in line with the same provisions recognition criteria set out in section 5 above (i.e. a present obligation resulting from a past event where an outflow of service potential or economic benefit is probable, and which can be reliably measured). Key to the recognition of restructuring provisions is the determination of when an obligation arises.

In order to recognise a restructuring provision, the following criteria must be met:

1. There must be a formal plan (containing minimum requirements) for the restructuring; **and**
2. A valid expectation must have been raised with those affected that the plan will be implemented.

The raising of valid expectation is critical in determining whether a provision should be recognised.

10.4.1.1 Requirement for formal plan

Restructuring plans must identify:

- a) The activity or part of activity affected;
- b) The main locations affected;
- c) The location, function and approximate number of United Nations staff to be compensated;
- d) The costs that are anticipated to be incurred in the plan (i.e. the expenditures); **and**
- e) The timing of the plan’s implementation (i.e. when it will take place).

All criteria must be met in order to have a valid plan which may be recognised as a provision.

10.4.1.2 Valid expectation raised

In the context of restructuring provisions, a “valid expectation” is raised when the affected parties (usually staff) are informed of the plan, either individually, or more commonly through a general (but sufficiently detailed) announcement.

A provision should not be recognised where a valid expectation has not been raised. This means that even if the United Nations senior management has developed and agreed a restructuring plan, it cannot recognise a provision for the plan until the staff affected have been informed. Should the plan be communicated after year end, it may be considered as an event after the reporting date and disclosed in the notes to the financial statements if material.

In order to raise a valid expectation, the restructuring plan should also be planned to be implemented as soon as possible. This is because plans which will be implemented only after a long delay in the future may be subject to change and a higher degree of uncertainty, which may mean that staff involved will no longer have a valid expectation that the plan will go ahead.

Clearly this is an area where there will be considerable debate concerning whether or not a plan is detailed enough and firm enough to create a valid expectation in others that it will be carried through. Any plan that is over one year in length is unlikely to be sufficiently detailed on initial announcement to permit provision in full for all costs, and for major restructuring programmes this is likely to lead to costs being charged to surplus or deficit over a number of financial years.

Example – Valid expectation of a restructuring

In July 20X9, the United Nations finalises a plan to merge two departments into one as part of a cost-savings plan. The new department is due to start operations in July 20Y2 and will involve a significant reduction in the number of staff.

It is anticipated that there will be significant restructuring costs, and a restructuring plan is well developed, meeting the criteria for plans' contents stipulated in IPSAS 19. The restructuring plan is foreseen in two phases; phase one will be implemented in February 20Y1 at the latest, whereas phase two will not take place until July 20Y2.

Due to administrative delays, it is not until December 20Y0 that the United Nations General Assembly takes the decision to formally adopt the plan. The staff involved are informed of the plan on the same day. The implementation plan remains unchanged.

Assessment of restructuring for year ended 31 December 20X9

At 31 December 20X9, the United Nations does not have a constructive obligation to restructure, as although a plan had been agreed by the year-end, it had not yet been formally communicated to staff and therefore no valid expectation had been raised with the staff concerned. In addition, as the plan was not due to start until 14 months after the end of the financial year, it may be possible to argue that the timeframe allows the United Nations to change its plans.

Assessment of restructuring for year ended 31 December 20Y0

The United Nations has a constructive obligation for restructuring relating to phase one of the restructuring, but not for phase two. In both cases, a detailed plan exists, whose contents meet the IPSAS 19 criteria for a restructuring plan. The plans have also been communicated to staff for both phases, however the staff concerned will only have a valid expectation that the first phase will be implemented, as this is planned two

months after the year-end. Again, for the second phase, it may be possible to argue that the timeframe allows the United Nations to change its plans as its implementation is planned for 18 months after the year-end. A provision should therefore only be recognised for the eligible costs foreseen for phase one of the restructuring.

Note – this is a fictional example for illustrative purposes only.

10.4.1.3 Sale or transfer of operations

Where operations are sold or transferred, an obligation only arises at the point where there is binding agreement for the United Nations to sell or transfer the operation.

10.4.2 Measurement of restructuring provisions

When measuring the amount required to settle the restructuring obligation, the criteria in section 6 above should be followed; best estimates should be used, which take into account the timing and uncertainty of the plan, the present value of the obligation, and future events.

Only costs that are directly attributable to the restructuring plan should be included in the provision. Such costs should be necessarily entailed as part of the plan and should not be associated with the ongoing activities of the United Nations.

Costs such as retraining of staff, marketing, and investment in new systems should also be excluded as these relate to future operational activities (i.e. development of the new activity rather than the restructuring of the old one).

Table – Examples of costs that are included and excluded from restructuring provisions

Description of costs	Included	Excluded	Reason for exclusion
Voluntary redundancies.	✓		
Compulsory redundancies, if the targets for voluntary redundancies are not met.	✓		
Lease cancellation fees for an office that will no longer be used.	✓		
Relocation of employees and related equipment from an office (to be closed) to an office that will continue to be used.		✓	Costs associated with ongoing activities.
Retraining of remaining employees.		✓	Costs associated with ongoing activities.
Recruitment costs for a new manager.		✓	Costs associated with ongoing activities.
Marketing costs to promote awareness of new office.		✓	Costs associated with ongoing activities.

Investments in a new delivery network to new office.		✓	Costs associated with ongoing activities.
Future identifiable operating losses up to the date of a restructuring.		✓	Costs associated with ongoing activities.
Impairment write-down of certain property, plant and equipment.		✓	The impairment should be accounted for in accordance with IPSAS 21 or IPSAS 26.
Costs of the remaining non-cancellable term of an operating lease after operations cease (i.e. an onerous lease).	✓		
Rental costs under the lease contract for the period after the provisions criteria were met but before the operation ceased.		✓	Operations continued to be used.
Consulting fees to identify future corporate strategies and organisational structures.		✓	Costs associated with ongoing activities.
Costs of relocating inventory and equipment that will be used at another location.		✓	Costs associated with ongoing activities.
Merger costs, for example, integrating computer systems following merger of two Chapters' functions.		✓	Costs associated with ongoing activities.

10.5 Death and disability claims

Note – this section relates specifically to cases of death or disability where claims are submitted to the United Nations. Where the United Nations is taken to court by a Government or individual (s) in connection with a death or disability, the United Nations should account for this as a legal case as per section 10.1 above.

During the course of its peacekeeping and administrative operations, United Nations troops, police and administrative staff may suffer injuries that lead to their death or disability. Under its terms of employment with staff, and under the General Assembly resolution for troops and police from Contributing Countries, the United Nations may be liable for death and disability payments where certain conditions have been met.

Claims for death and disability payments are split into two principle categories:

1. Claims relating to United Nations staff received directly from the staff themselves or their representatives; and
2. Claims relating to troops and police received from the Governments of Contributing Countries.

10.5.1 Claims relating to United Nations staff

Claims for death and disability for United Nations staff are paid from the United Nations' own self-insurance fund. Compensation and insurance for both staff death and disability form part of employee's

employment contract are classified as **post-employment benefits**. We refer to Corporate Guidance #8 – Employee Benefits, where further guidance around the recognition of provisions for claims may be obtained.

10.5.2 Claims relating to troops and police

The United Nations is usually made aware of the death or disability of troops and police very quickly and will inform the relevant Government within 24 hours via a NOTICAS (Notification of Casualty) form. The United Nations will then receive a claim from the Government in question requesting compensation for the death or disability.

On receipt of these claims, the United Nations will perform a claim assessment and pay those claims which meet the necessary criteria. It is important to note that not all claims are paid in full, and in some instances the full claims are rejected (e.g. for deaths caused by pre-existing medical conditions or injuries caused by negligence by the individual).

Whilst the United Nations receives internal notification of such incidents and individuals concerned very quickly, formal claims may be received much later – years later in some instances. Furthermore, once claims have been submitted to the United Nations, the claim review process (usually involving a Board of Inquiry) may take several months or even years to finalise.

Where claims are agreed and finalised with the Governments concerned, the probability of outflow is almost certain and an accrual or payable should be recognised by the United Nations. However, at the end of the financial year, the United Nations may be aware of a number of incidents or events causing death or potential disability which had taken place before the end of the financial year, where a claim has not yet been received, or where the assessment process is in progress. In such cases, a degree of uncertainty will exist around the eventual outcome of the claim procedure, and the United Nations will need to consider whether it will need to recognise a provision for potential results.

In both cases, the triggering event for the recognition of a provision is the incident or event itself (i.e. that which causes the death or disability), and not the later receipt of a claim. In other words, the United Nations should provide for potential claims as soon as it is aware of the incident, if the incident meets the provisions recognition criteria.

10.5.2.1 Death of troops and police

In the case of the death of United Nations troops or police, the United Nations should recognise a provision at the point at which the death occurs, unless - on an exception basis only - there are indisputable reasons where the United Nations is not liable (e.g. clear staff negligence or pre-existing medical conditions). A provision is recognised because the United Nations has a legal obligation through the General Assembly resolution to pay compensation in the event of the death of a troop or member of the police, and it is probable that a claim will be received that will be paid by the United Nations. A reliable estimate of the outflow is also possible as the amounts payable are fixed in the event of a death.

Any provisions should be measured at the best estimate based on the fixed amount specified in the General Assembly resolution (2013: \$70,000).

For those cases where a provision is not recognised (anticipated as a low proportion of incidents), a contingent liability should be disclosed for the estimated value of payment (if any), unless the probability of the claim being paid is remote.

10.5.2.2 Disability of troops and police

Disability claims require a medical review process and the value payable by the United Nations to a Government is capped at the amount payable in the event of a death (2013: \$70,000). The precise amount is dependent on nature of the disability agreed with the Government, which is then converted to a percentage of full disability listed in the American Medical Guide. This percentage is multiplied by the amount payable in the event of a death to determine the amount payable to the Government by the United Nations. For example, a 50% disability when the maximum rate for death is \$70,000 will result in a \$35,000 payment to the Government.

The initial receipt of a claim from a Government may take several months or years and equally the medical review may take a long time to complete. At the financial year-end, the United Nations will therefore be aware of a number of incidents where:

- a) Claims for disability have either not yet been received; or
- b) Claims for disability have been received but not yet finalised by the year-end.

In such cases, the United Nations will not know the final outcome of the claim and hence there will be uncertainty surrounding the probability, timing and value of payment. The application of the provisions recognition and measurement criteria will however be the same in both cases.

Where the United Nations has issued a NOTICAS form prior to the financial year-end, it should recognise a provision for those claims not yet received and in progress, as it has a legal obligation to the Governments as a result of a past event (the injury to the troops and police), it is probable that there will be an outflow and a reliable estimate of the costs can be made.

When measuring the provision, the best estimate should be formed by reviewing historic data on similar completed claims, such as the proportion of claims that are successful, and the average percentage disability determined from those successful claims. Such data may be obtained from the United Nations medical database and UNPKO Situations Centre. The provision should be reviewed annually and adjusted for those claims paid, those rejected and any new incidents where no claim has been received.

Example – Measurement of provision for claims not yet received or finalised

At the end of the financial year, the United Nations is aware of several incidents involving the injury of 100 troops and police occurring during the financial year for which no claims have been received yet from any Governments or where finalisation has not been completed. Historic data shows that 95% of cases produce valid claims, and of those valid claims, the average disability is approximately 60%. The amount payable for 100% disability is \$70,000.

The provision for claims not yet received should be calculated as follows:

$$\begin{aligned} \text{Provision} &= 100 * 95\% * 60 * \$ 70,000 \\ &= \$ 3,990,000 \end{aligned}$$

Accounting entries at year-end:

Dr.	Disability claim expense (police and troops)	\$ 3,990,000
Cr.	Provisions (death and disability claims)	\$ 3,990,000

10.6 Claims under defacto lease arrangements

Situations where the United Nations enters into an implied lease agreement, but no formal supporting documents of the arrangement are in place, are referred to as defacto leases. The lease classification recognition, and measurement is based on the available facts and circumstances. Further details relating to defacto leases can be found in Corporate Guidance #1 – Leasing.

In a Peacekeeping context, host Governments may give the United Nations “permission” to use land and buildings, even though that Government may not be the legal owner. At a later stage, the UN may receive unexpected claims for lease payments by the true legal owners of the land and buildings. These will require review by the United Nations and may result in payment of additional lease expenses if approved by OLA.

The United Nations should recognise provisions for claims under defacto leases when the claims meet the provisions recognition criteria on a case-by-case basis. The trigger for this review will normally be on receipt of the claims, as this will be the first point at which the United Nations is aware of the claim. On receipt of a claim, an assessment should be performed of whether it is likely that the claim will be paid. Legal advice may be required to determine the probability of payment.

The past practice of the United Nations regarding the settlement of such claims should also be examined to inform whether the United Nations has a constructive obligation to settle the claim. A provision should be recognized for those claims which are judged to be more probable than not to be paid by the United Nations.

Example – Receipt of a defacto lease claim

The United Nations occupies land in Southern Lebanon and sets up a base for Peacekeeping Operations there which it uses over a period of several years for no charge.

After 6 years, a claim for rental payments is received from a Lebanese landowner who claims ownership of the land. The United Nations had no previous knowledge of this individual’s claim to the title of the land and had not recognised any defacto lease expense for the rental of the land in the past. The case is not yet in court and the United Nations has sought legal advice from the OLA.

The OLA advice concludes that, on the basis of the information at the financial year-end, the Lebanese landowner cannot prove title to the land, and that is unlikely that the United Nations will have to make any payments to the individual. The United Nations has a firm, published policy of not paying defacto lease claims unless genuine title can be proved by the claimant.

On the basis of this legal advice, and its published policy, the United Nations should not recognise a provision, as it does not have a legal or constructive obligation to the individual, nor is it probable that there will be an outflow. Instead, a contingent liability should be disclosed.

10.7 Claims submitted to United Nations Compensation Commission

10.7.1 Background

The United Nations Compensation Commission (UNCC) is a subsidiary organ of the Security Council. It was established in accordance with Security Council resolutions to process claims and pay compensation for direct losses and damage suffered by individuals, corporations, Governments and international organizations as a direct result of the invasion and occupation of Kuwait by Iraq.

Funds to pay compensation are drawn from the United Nations Compensation Fund (UNCF), which receives a percentage of the proceeds generated by the export sales of Iraqi petroleum and petroleum products. This percentage has been set at 5 per cent since its reduction from 25 per cent under a Security Council resolution. In a further resolution, the Council reaffirmed the 5 per cent and also decided to apply it to non-monetary payments.

In addition to the payment of successful claims, the main ongoing activity of the Secretariat includes overseeing the Follow-up Programme for Environmental Awards established in December 2005 by Governing Council decision 258 to monitor the technical and financial implementation of approximately \$4.3 billion of environmental remediation and restoration projects being undertaken with funds awarded in the “F4” (environmental) category of claims. The programme is funded by the participating Governments (namely, the Islamic Republic of Iran, Jordan, Kuwait and Saudi Arabia) through contributions proportional to the value of their awards.

At the date of the issuing of this Corporate Guidance, the UNCC was in the final stages of its mandate. Claims processing concluded in 2005 and all but one of the more than 1.5 million successful claims have been paid in full. The remaining claim has an outstanding award balance of approximately \$11.2 billion remaining to be paid. In accordance with relevant Governing Council decisions, payments are made on a quarterly basis. Based on recent funding to the UNCF and projections, this balance is expected to be paid in full in early 2015. With regard to the Follow-up Programme for Environmental Awards, while the awards were paid in full by January 2010, Governing Council decisions 258 (2005) and 266 (2009) provide for a certain percentage of the awards to be withheld. In this regard, approximately \$1bn is currently held in an escrow account by the United Nations. At its seventy-fifth session in May 2013, the Governing Council determined that the mandate in the cases of Iran and Saudi Arabia had been fulfilled and authorized the release of their respective funds currently being withheld in the escrow account. It is expected that the mandate in the cases of Jordan and Kuwait will be concluded by the end of 2013, and following that, their withheld funds will also be released.

The main limiting factor in the payment of the remaining compensation claim is the level of funding from Iraqi petroleum revenue; the balance in the UNCF is always lower than the total value of the outstanding claim and thus the claim can only be paid when the funding is received from the Government of Iraq.

As per legal advice from the OLA, UNCC does not have a direct legal obligation to the claimants to settle the claims it receives; this obligation instead lies with the Government of Iraq. The United Nations is only legally obliged to make payment for eligible claims when the funds are made available by the Government of Iraq.

Equally, should there be excess funds remaining in the UNCF after the settlement of all claims (unlikely in practice due to the payment mechanisms in place), this excess will be returned to the Government of Iraq; the United Nations does therefore not benefit from any surplus funds.

Administrative expenses incurred by the United Nations relating to the UNCC are deducted from the UNCF where incurred.

10.7.2 Accounting for claims

Given the mature stage of the claims process, with all claims processed and final payment to the remaining claimant being one of the remaining key items of business for the UNCC, there are fewer factors subject to change than in some of the other cases described in the “Provisions” Corporate Guidance paper. However, owing to the highly material nature of the remaining outflows, the correct accounting treatment under IPSAS is still critical.

Before examining the accounting entries for the recognition of outstanding claims and payments, the role that the United Nations plays in administering the fund should be considered, as its position as either “agent” or “principal” in the arrangements is key to determining the accounting entries required.

10.7.2.1 Determination of “agent” or “principal”

The concepts behind the determination of “agent” or “principal” are explained in detail in Corporate Guidance #5 – Funding Agreements. Key to this determination is whether the United Nations is exposed to the risks and rewards associated with the rendering of the claims management service; if exposed, the United Nations should be considered as “principal”. However, if the Government of Iraq takes the exposure for these risks, then the United Nations is likely to be an “agent”.

In other words, in this context, the question is whether the United Nations is exposed to an obligation to claimants should the Iraqi fail to provide funds, and whether the United Nations is able to retain any surplus funds remaining at the end of its mandate. Both would be indicators that the UNCC is acting as principal.

The legal analysis provided suggests instead that the Government of Iraq takes responsibility for the risks and rewards of the arrangements, and hence the United Nations may be considered as an “agent”, responsible for administration of the fund only.

Indeed, were the United Nations to be principal in the relationship, it would effectively need to underwrite the liability of the Government of Iraq towards the remaining claimant, which is clearly not the case in this arrangement and also not part of the wider operations or mandate of the United Nations. The accounting treatment for the United Nations as principal is therefore inapplicable and will not be considered in this guidance.

10.7.2.2 Impact on accounting treatment - agent accounting

Should the United Nations act as an “agent” in these arrangements, the UNCC should not recognise a provision or liability for the full amount of the claims, as the United Nations itself is not liable to settle them, and the settlement of the liability will not lead to a decrease in economic benefits or service potential of the UNCC. Instead, a liability should be recognised only for the amount of funds received by the United Nations from the Government of Iraq which are yet to be disbursed to the claimant. Such a liability should be recognised at point at which the funding is received.

A liability is recognised as cash has been received in a bank account which is held in the name of the United Nations; the UNCF is not a separate legal entity from the UNCC and therefore the cash contained within the fund falls under the consolidation boundary for the United Nations. In addition, the mandate to establish the UNCC was given by the United Nations Security Council, and not a third party, and thus it is the United Nations itself which has established the UNCF.

Note: The accounting treatment may be different for other “funds” managed by the United Nations, were the mandate to be given by an individual member state (e.g. the UK or USA) or third party (e.g. private enterprise to manage a fund on their behalf). Any determination of consolidation boundaries for such funds should be made using all of the relevant facts and circumstances available.

As the processing of all claims has concluded, and the limiting factor for payment rests with funding from Iraqi petroleum revenues, it can be assumed that all cash and investments held by the UNCC will be disbursed to the remaining claimant (less any administrative deductions). The accounting entry upon receipt of the funding from the Government of Iraq is therefore credited directly as a liability towards the claimant.

On the statement of financial position, as noted in IPSAS 9 [12], only the “*amount of any commission received or receivable for the collection or handling of the gross fees*” should be recognised as revenue by the UNCC. “*The amounts collected on behalf of the principal [i.e. the Government of Iraq] are not revenue*”. This means that the funding received from the Government of Iraq should not be recognised as revenue, but instead as a liability as described above.

Administrative expenses incurred by the UNCC in carrying out its mandate should however be deducted from the liability to the claimant and an equal amount of revenue recognised for these expenses, as the management of claims by the UNCC is viewed as an “exchange transaction” under IPSAS 9.

Narrative disclosures may however be made regarding the nature of the fund and the gross amounts of claims awaiting payment. This will assist the user of the accounts to understand the wider context of the claims and payments.

Accounting entries:

On receipt of funding from Government of Iraq:

Dr. Cash	[value of funding]
Cr. Liabilities to remaining claimants	[value of funding]

To recognise administration expenses:

Dr. Administration costs	[value of administration costs]
Cr. Cash / payables	[value of administration costs]
Dr. Liabilities to remaining claimants	[value of administration costs]
Cr. Revenue	[value of administration costs]

Note: Revenue is recognised for the UNCC as it is providing a “service” for the management of the fund and claims process, providing that the recognition criteria described in IPSAS 9 (Revenue from Exchange Transactions) are met.

On payment of claim instalments:

Dr. Liabilities to remaining claimants	[value of instalment]
Cr. Cash	[value of instalment]

Example – Agent accounting for UNCC Claims

In 20X3, the UNCC is in the final stages of its mandate and is in the process of paying down one final claim for compensation and releasing withheld funds under the Follow-up Programme for Environmental Awards to two of the participating Governments. In all cases, the amounts due to the claimant in question are fixed.

At the start of the financial year, the UNCC held \$1bn of funding from Iraqi petroleum revenues in a pooled United Nations bank account and \$1bn in a separate escrow account due to be released for the Environmental Programme. The outstanding award balance to the remaining claimant was \$11.2bn and the withheld funds under the Environmental Programme total \$1bn, however the two countries in question have not yet been released from the Programme*.

During the year, the UNCC:

- Receives a further \$4bn in funding from the Government of Iraq;
- Incurs administrative expenses of \$3m (of which £200,000 remains unpaid at the reporting date);
- Pays a \$4bn instalment for the claim for compensation; and
- Releases the remaining \$1bn of withheld funds from the escrow account.

The position at the 31 December 20X3 is thus as follows:

- Cash balance of \$997.2m (= \$2bn + \$4bn - \$4bn - \$1bn - \$3m + \$200,000).
- Compensation claims of \$8.2bn remaining.

Accounting treatment for year-end 31 December 20X3:**Statement of financial position at start of financial year (1 January 20X3) - extract:**

At the start of the financial year (i.e. as part of its opening balances), the United Nations should present the following on its statement of financial position:

Assets*:

Cash and cash equivalents	\$ 2,000,000,000
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Liabilities**:

Liabilities to remaining claimants	\$ 2,000,000,000
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The full value of the claims (i.e. \$11.2bn + \$1bn = \$12.2bn) is not recognised, as the United Nations is not the Principal in the transactions.

Upon receipt of funding:

Dr. Cash	\$ 4,000,000,000
Cr. Liabilities to remaining claimants	\$ 4,000,000,000

The cash received is recognised as a liability towards the claimants as the United Nations has an obligation to pay this to the claimants under the various Security Council resolutions, as the claims in question have been accepted as valid and payment is only dependent on availability of cash from the Government of Iraq.

Upon incurring administrative expenses:

Dr. Administrative expenses	\$ 3,000,000
Cr. Cash	\$ 2,800,000
Cr. Payables (administrative)	\$ 200,000
Dr. Liabilities to remaining claimants	\$ 3,000,000
Cr. Revenue	\$ 3,000,000

The liability to remaining claimants is reduced on incurring administrative expenditure as the UNCC is entitled to deduct its administration costs from the UNCF, reducing the funds available to pay claimants in that period.

Payment of compensation instalment and Environmental Claims:

Dr. Liabilities to remaining claimants	\$ 5,000,000,000
Cr. Cash *	\$ 5,000,000,000

Statement of financial position at end of financial year (31 December 20X3) - extract:

At the end of the financial year, the United Nations should present the following on its statement of financial position:

Assets:

Cash and cash equivalents	\$ 997,200,000
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Liabilities**:

Liabilities to remaining claimants	\$ 997,000,000
Payables (administrative)	\$ 200,000

The full value of the remaining compensation claim (i.e. \$11.2bn - \$4bn= \$7.2bn) is not recognised, as the United Nations is not the Principal in the transaction.

Statement of financial performance for the financial year (year ended 31 December 20X3) – extract:Revenue:

Management fee for administrative costs of UNCC	\$ 3,000,000
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Expenses:

Administrative expenses	\$ 3,000,000
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(n.b. this will be split between staff costs, rent, etc)

Note: For the purposes of this example, the UNCC is deemed to be a going concern at the date of authorisation for issue of the financial statements, and is also deemed to be an “agent” in the claims management arrangements.

* Includes cash present in the escrow account relating to Environmental Programme totalling \$1bn. In line with IPSAS 2 – Cash Flow Statements – any restrictions upon cash should be disclosed in the notes to the financial statements.

**Any liabilities for future administration payments (e.g. pension provisions) are excluded from the scope of this example, as is any interest generated on the funds held in the UNCF.

10.8 Insurance claims

Most of the United Nations' health insurance plans are **self-insured plans** and the United Nations relies on external insurance companies for the administrative process of receiving and processing claims. The actual costs to cover employees' claims are however borne by the United Nations.

The accounting treatment for such claims is covered in Corporate Guidance #8 – Employee Benefits.

10.9 Guarantees and warranties

10.9.1 Guarantees

The United Nations may act as guarantor of borrowings made by certain beneficiaries or projects run by third parties. Where this occurs, the United Nations should recognise and measure guarantees as detailed under IPSAS 29 – we refer to Corporate Guidance #9 – Financial Instruments for further information.

Example – United Nations acting as guarantor for bank loan to a Non-Governmental Organisation (NGO)

Note – this example reviews the treatment of a guarantee under IPSAS 29 (Financial Instruments: Recognition and Measurement)

The United Nations funds a project which is managed by a Non-Governmental Organisation (NGO). The NGO takes out a bank loan in September 20X2 and the United Nations acts as the guarantor on the loan should the NGO default on the loan repayments. The contract meets the definition of a financial guarantee in IPSAS 29.

During the remaining part of 20X2, the financial condition of the NGO is sound, however in June 20X3 the NGO's financial condition deteriorates and in November 20X3 the NGO is declared bankrupt. The year-end of the United Nations is 31 December.

Accounting treatment at 31 December 20X2

At the end of the financial year, the United Nations has a present obligation as a result of a past event, resulting from the giving of the financial guarantee.

However, an outflow of resources is not probable at the year-end, as the financial condition of the NGO is sound. The guarantee should therefore be recognised at fair value.

Accounting treatment at 31 December 20X3

Again, the United Nations has a present obligation as a result of a past event resulting from the giving of the guarantee. However, the bankruptcy of the NGO also indicates that that an outflow of resources is probable. The guarantee is therefore subsequently measured at the higher of the best estimate of the obligation and the amount initially recognised (as per IPSAS 29) less any cumulative amortisation (which may be recognised as revenue in line with IPSAS 9).

10.9.2 Warranties

A warranty is often provided in conjunction with the sale of goods. Warranty costs represent additional costs that the United Nations (as the seller) may have to incur to rectify defects in, or to replace, the product it has sold. The warranty obligation can arise either through the operation of the law (contract or statute) or through an entity's stated policies or practices. Although warranty contracts meet the definition of an insurance contract, they are scoped out of IFRS 4 (Insurance Contracts, no IPSAS equivalent) and are, therefore, within IPSAS 19's scope.

When The United Nations sells a product subject to warranty, it must first determine whether the warranty represents a separable component of the transaction. If an item sold proves to have been defective at the time of sale (usually based on evidence coming to light within a standard period), the purchaser may have the right to require the United Nations to rectify the defect or replace the faulty item. Such a warranty is considered to be a 'standard warranty' that relates to the condition of the item sold at the date of sale. It is not usually considered separable from the sale of goods.

When the warranty is not a separate element and represents an insignificant part of the sale transaction, generally the full consideration received is recognised as revenue on the sale and a provision is recognised for the expected future cost to be incurred relating to the warranty. An example of such an arrangement is a standard manufacturing warranty given under the normal terms and conditions of sale. Warranties that are not separate elements are dealt with in IPSAS 19.

Provisions for warranties should be recognised in line with sections 5 and 6 above.

Example – Product repairs or replacement

The United Nations sells radios to Governments. On some of its products it warrants at the time the sale is made that it will make good by repair or replacement manufacturing defects that become apparent within one year from the date of sale. Its past experience shows that it does receive warranty claims on these products.

A provision should be made for the best estimate of the obligation for the following reasons:

- A legal obligation exists which is more likely than not to arise;
- The obligating event is the sale of the product and the normal one-year warranty can be legally enforced;
- The related costs of repair do not relate to the United Nations' future operations;
- From past experience, it is more likely than not that the obligation will result in an outflow of economic benefits or service potential; and
- A reliable estimate of the obligation can be made from the entity's previous claims experience.

Using the simple year end test, if the United Nations stopped trading at its year end, it would still be liable for the obligations arising from warranties it has already given. Hence provision is required. The entity should use past experience to estimate reliably the amount of potential claims.

Note - given the nature of the activities of the United Nations, it is not expected that many provisions for warranties, if any, will be recognised.

11 Case study – Serious incident in United Nations depot

11.1 Background

The United Nations has a large Peacekeeping depot and offices based near the port of City A, the capital city of Country X. It employs 500 staff and the site comprises several administration buildings and warehouses which the United Nations has adapted over many years since it first moved to the city in 19X1.

In May 20X4, there is a sudden explosion inside the United Nations complex perimeter during the loading of munitions from a ship onto a transportation lorry. There are several fatalities of which 35 are Peacekeeping troops and four private contractors, in addition to multiple injuries. Extensive toxic pollution is released in the local environment.

Initial investigations indicate a fault with the manner in which the munitions were handled by United Nations troops. As a result, the insurance company for the private contractors takes the United Nations to court for the death and injuries to its employees and at 30 June 20X4, the case was in court. Under terms of the service contract with the private contractor, the United Nations has a legal obligation to pay compensation to the company and the families of the victims in the event of the death or injury of a contractor where the United Nations is negligent. At that point in time, the OLA advises that the insurance company has a very strong case and is likely to win the compensation and damages requested which total \$80m.

In addition, the environmental law of Country X requires that the tenants must pay for the decontamination of any sites occupied in the Country. For the area polluted by the incident, these costs are estimated at \$15m at 30 June 20X4. OLA advice indicates that this is unlikely to be enforceable as the law specifically excludes International Organisations such as the United Nations. No such examples of pollution have been identified in the past and the United Nations has no public policy on decontamination of pollution in such cases.

Several claims for death and disability compensation are received by 30 June 20X4 relating to the United Nations Peacekeeping troops, and many more are expected based on the injuries reported in the days following the explosion and discussions with the Governments in question. In total, out of injuries to 100 troops, 11 claims had been received from Governments. None of the claims had been finalised by the time of the preparation of the accounts.

In October 20X4, a terrorist group in Country X admits responsibility for the attack and deliberately sabotaging the munitions. Owing to these additional complexities, the insurance company's case is still ongoing at 30 June 20X5. As a result of the developments, the OLA determines that the case is significantly weakened to the extent that it is probable that the United Nations will successfully defend it. In May 20X4 the environmental pollution charges are also dropped by the Government of Country X with no amounts payable by the United Nations.

By December 20X4, the United Nations has received, approved and paid death and disability claims from all the relevant Governments. The total payments made were \$6.2m, with no further claims expected.

As the next calendar year progresses, the security situation in City A and Country X deteriorates rapidly and, unable to guarantee the safety of its staff, the United Nations formulates a plan to relocate its

Peacekeeping offices and depot to City B in Country Z, a neighbouring but stable country. As at 30 June 20X5 a detailed plan had been established and agreed internally by United Nations management, however a public announcement of the plan was only made on 8 July 20X5, with the staff concerned informed the day before. The plan is due to start immediately, with the move beginning on 1 August 20X5. Several staff do not wish to transfer to the new site and are instead offered termination payments. Total estimated costs are \$100m (excluding onerous leases below).

As part of the move, the United Nations must continue to make lease payments for the leases on three buildings, which end on 30 June 20Y5. The rental is \$150,000 per year per property, payable annually in arrears on 30 June. Due to the security situation, the United Nations is unable to sublease these buildings to a third party and has no remaining exit clauses in the leases. It is not required to restore the buildings to their original condition under the terms of the lease, and in the past in the region has left the leasehold improvements for the landlord. In September 20X5 the contents of the site are evacuated to Country Z.

In July 20X5 the United Nations signs new leases for four sites of land in Country Z, on which it constructs its own temporary warehouses and buildings in August and September 20X5. The land leases require the restoration of the land to its original condition at the end of the leases. The present value of the anticipated cost of dismantling the buildings in 5 years time is \$500,000.

In September 20X5, the legal case against the United Nations ends in favour of the United Nations and no compensation is payable to the insurance company.

For the purposes of these examples, the tax-free discount rate used by the United Nations is 5% and the year end is 30 June.

11.2 Accounting treatment for year ended 30 June 20X4

At the end of the financial year; the United Nations will need to consider whether provisions should be recognised for the following items:

- Death and disability of Peacekeeping troops;
- The costs of compensation for death and injury to the private contractors; and
- The costs of decontamination.

Death and disability of Peacekeeping troops;

Following the deaths of the 35 Peacekeeping Troops, the United Nations should recognise a provision for the anticipated costs of the claims to be received from the Governments, as it has a legal obligation through the General Assembly resolution to pay compensation in the event of the death of a troop or member of the police, and it is probable that a claim will be received that will be paid by the United Nations. A reliable estimate of the outflow is also possible as the amounts payable are fixed in the event of a death.

Death of Peacekeeping troops

Assuming an amount payable for each death of \$ 70,000 in the event of a successful claim, the provision should be measured as:

Provision	=	\$ 70,000 * 35
	=	\$ 2,450,000

The provision should be recognised with the following accounting entry:

Dr. Death and disability expenses (troops and police)	\$ 2,450,000
Cr. Provisions for death and disability claims	\$2,450,000

Note – it is assumed that all the deaths were due to the explosion and not pre-existing medical conditions.

The United Nations should also provide for the anticipated costs of the payment due to Governments for the disability of troops resulting from the accident. Even though only 11 out of 100 potential claims have been made and their potential final value is unknown, the United Nations has a legal obligation through the General Assembly resolution to pay compensation in the event of the disability of a troop or member of the police, and it is probable that a claim will be received that will be paid by the United Nations. A reliable estimate of the outflow is also possible. A provision should therefore be made for all 100 injuries as they may lead to disability.

Disability of Peacekeeping troops

Given that no claims have been received by the end of the financial year, the amount to provide will have to be calculated based on the number of injured troops, with an estimate made of the likely success of the claims and the percentage disability agreed by the medical review.

Such data should be taken from historic data of similar incidents, or if this is unavailable, the overall rates for all incidents over the recent past. Assuming a claim success rate of 95%, an average percentage disability of 60%, and a maximum amount payable of \$70,000 in the event of 100% disability, the provision should be calculated as:

Provision	=	95% * 100 troops * 60% * \$ 70,000
	=	\$ 3,990,000

The provision should be recognised with the following accounting entry:

Dr. Death and disability expenses (troops and police)	\$ 3,990,000
Cr. Provisions for death and disability claims	\$ 3,990,000

The compensation for the death and injury of private contractors

A provision should also be recognised for the legal case brought by the insurance company regarding the death of the four contractors, based on the legal advice provided by OLA. The legal advice indicates that the United Nations has a present (legal) obligation as a result of a past event (the explosion), and that it is probable that the insurance company will win the case. The amount claimed is known to be \$80m, thus a reliable estimate is possible.

The United Nations should therefore recognise a provision through the following accounting entries:

Dr. Third party compensation expense	\$ 80m
Cr. Provisions for legal cases	\$ 80m

The costs of decontamination

Based on the legal advice received from the OLA, a provision should not be recognised by the United Nations in respect to the environmental pollution, as the OLA has advised that the United Nations does not have a legal obligation to decontaminate the land under the law of Country X, and that it is improbable that the legal case launched by the Government will be successful. Given there is no past practice or policy relating to the situation by which the United Nations could have raised a valid expectation to clear the pollution, it is unlikely to have constructive obligation to decontaminate the land.

The United Nations should instead disclose a contingent liability, containing a brief description of the incident, the value of the claim, and the timing of any possible payment.

11.3 Accounting treatment for year ended 30 June 20X5

At the end of the financial year; the United Nations will need review the status of any existing provisions or contingent liabilities relating to:

- Death and disability of Peacekeeping troops;
- Compensation for the death and injury of private contractors; and
- Costs of decontamination.

The United Nations will also need to consider whether provisions should be recognised for the following items:

- Restructuring (relating to the move from Country X to Country Z);
- Onerous leases (relating to the vacated buildings); and
- Restoration costs (for the buildings constructed in Country Z).

Death and disability of Peacekeeping troops

In the financial year, all expected claims relating to the explosion were received and finalised, and therefore no provision as is required at the financial year-end as the liability relating to the claims has been extinguished.

Accounting entries for changes in death and disability provision

Of the provision recognised at 30 June 20X4 for \$6.45m (\$2.45m for death + \$3.99m for disability):

- \$6.2m has been “utilised” through approval and payment; and
- The remaining \$250,000 of the provision is “reversed” as it was not required to settle the obligation.

The following accounting entries should be made in the year:

On settlement of the claims:

Dr. Provisions for death and disability claims	\$ [value of claim] (up to total of \$6.2m)
Cr. Payables / Cash	\$ [value of claim] (up to total of \$6.2m)

On reversal of remaining unused provision:

Dr. Provisions for death and disability claims	\$ 250,000
Cr. Death and disability expenses (troops and police)	\$ 250,000

Compensation for the death and injury of private contractors

Following the changes in circumstances of the legal case, and based on the advice of the OLA, the event no longer meets the recognition criteria for a provision, as it is no longer probable that there will be an outflow embodying economic benefits from the United Nations. The provision recognised in the financial year ended 30 June 20X4 should therefore be reversed as at 30 June 20X5.

A contingent liability should instead be disclosed, as the probability of the insurance company winning in the case is still more than remote.

Accounting entries for changes in provision for compensation for the death and injury of private contractors

The following accounting entries should be made to reverse the provision:

Dr. Provisions for legal cases	\$80m
Cr. Third party compensation expense	\$ 80m

Note – the credit entry may need to be disclosed individually in the statement of financial performance if material.

Costs of decontamination

Following the end of the legal case, and a result in favour of the United Nations, there is no further obligation requiring settlement. A provision should not therefore be recognised and no contingent liability disclosed regarding the case in the financial statements.

Move to Country Z - restructuring plan

Given the scale of the relocation, the move may be viewed as meeting the definition of a “restructuring”, namely “the relocation of business activities from country or region to another”. In addition, a valid and detailed plan had been prepared by management.

A provision should not however be recognised at 30 June 20X5 for the anticipated restructuring costs of \$100m, as the staff and third parties had not been made aware of the plan until after this date. A valid expectation had therefore not been raised with those affected by the plan, and as such there is no obligating event.

Vacated offices and new leasehold improvements

No provision should be recognised for leases relating to the vacated offices at 30 June 20X5, as the buildings were still occupied at the end of the financial year and the decision to vacate them was not announced until after the financial year-end. Equally, no provision should be recognised for the future cost of dismantling the buildings on the new leased land, as the lease was not signed, nor had the construction of the buildings started prior to the financial year-end.

11.4 Accounting treatment for year ended 30 June 20X6

At the end of the financial year; the United Nations will need review the status of any existing provisions or contingent liabilities relating to:

- Death and disability of Peacekeeping troops;
- Compensation for the death and injury of private contractors; and
- Costs of decontamination.

The United Nations will also need to consider whether provisions should be recognised for the following items:

- Restructuring (relating to the move from Country X to Country Z);
- Onerous leases (relating to the vacated offices); and
- Restoration costs (for the buildings constructed in Country Z).

Death and disability of Peacekeeping troops

No further provisions should be recognised for these costs as all claims were settled by the end of the previous financial year and no further claims are expected.

Compensation for the death and injury of private contractors

Following the verdict on the legal case in the United Nations' favour, the United Nations has no legal or constructive obligation to pay the insurance company for the deaths of or injuries to the contractors. It is also remote that any future outflow embodying economic benefits or service potential will occur in relation to the case. No provision should be recognised nor any contingent liability disclosed.

Costs of decontamination

As in the previous financial year, there is no further obligation requiring settlement. A provision should not therefore be recognised and no contingent liability disclosed regarding the case in the financial statements.

Restructuring (relating to the move from Country X to Country Z)

Upon announcement of the plan to the affected parties, the United Nations should recognise a provision for the future restructuring costs (i.e. in July 20X5), as it is at this point that a valid expectation is raised that the plan will be implemented. A formal plan exists which meets the requirements of IPSAS 19, and the plan is expected to be implemented soon after announcement.

The provision should only include costs which arise directly from the restructuring (i.e., which are necessarily entailed and not associated with the ongoing activities of the United Nations. This includes onerous leases (discussed separately below for the purposes of this example) and redundancy costs. The provision should however exclude those costs which are associated with the ongoing United Nations activity (in this case the operation of the new depot). The costs of transporting equipment and staff to the new depot, leases expenses at the new site, and the construction costs of the new buildings should therefore be excluded from the restructuring provision. The provision recognised may thus be much lower than the \$100m costs anticipated in the plan.

Any costs incurred in the financial year should be deducted from the initial provision raised and the measurement of the provision re-assessed on 30 June 20X6 to determine which eligible costs remain to be paid in the coming years.

Accounting entries to recognise restructuring provision

The provision for restructuring should be recognised through the following accounting entries:

Dr. Restructuring expense	\$ [value of total eligible costs]
Cr. Provision for restructuring	\$ [value of total eligible costs]

Eligible costs should then be deducted from the provision as they are incurred:

Dr. Provision for restructuring	\$ [value of eligible cost incurred]
Cr. Payables / cash	\$ [value of eligible cost incurred]

Onerous leases (relating to the vacated offices)

Upon departure from the leased buildings in Country X, the United Nations should recognise a provision for the three onerous contracts. This is because having vacated the buildings, the United Nations can reasonably expect that obligations under the contract are greater than any future economic benefits or service potential which may be gained from the lease of the buildings. This is supported by the fact that the United Nations cannot even sublet the buildings, and is unable to exit the lease at any cost.

As the United Nations has a present (legal) obligation from a past event (the signing of the lease), a probable future outflow embodying economic benefits or service potential (the lease payments) and a reliable estimate of the amount may be made, the criteria for the recognition of a provision are met.

Measurement of present value of onerous lease provision at 30 June 20X6

The best estimate of the present value of the onerous lease provision should be calculated using the discounted future lease payments until the end of the lease. As at the 30 June 20X6, the next lease payment will be on 30 June 20X7 and the lease payments will end on 30 June 20Y5. Nine payments will thus be made, the first one exactly one year after the year end. The total annual lease payments are \$450,000 (3 * \$150,000).

The present value of the obligation may therefore be calculated using the following table:

Variable	Value
Annual lease payment (\$)	450,000
Payable on	30 June
First break clause	N/A
Date of provision	30 June 20X6
Discount rate	5%

Payment date	Time from year-end (years)	Amount payable (\$)	Discount factor	Present value (\$)
30/06/20X7	1	450,000	0.952	428,571
30/06/20X8	2	450,000	0.907	408,163
30/06/20X9	3	450,000	0.864	388,727
30/06/20Y0	4	450,000	0.823	370,216
30/06/20Y1	5	450,000	0.784	352,587
30/06/20Y2	6	450,000	0.746	335,797
30/06/20Y3	7	450,000	0.711	319,807
30/06/20Y4	8	450,000	0.677	304,578
30/06/20Y5	9	450,000	0.645	290,074
Total		4,050,000		3,198,520

A provision should therefore be recognised for \$3,198,520 through the following accounting entries at the end of the financial year:

Dr.	Onerous lease expenses (restructuring)	\$3,198,520
Cr.	Provisions (onerous leases / restructuring)	\$3,198,520

Note – *discounting is not often applied in practice, mainly due to the uncertainty regarding timing and amount of cash flows. Discounting should only be applied where the effect of the time value of money is material; small provisions (e.g. \$10,000) do not require discounting.*

In this example, discounting has been applied to explain possible considerations, however at 30 June 20X6 the difference between the undiscounted provision (\$4,050,000) and the discounted provision (\$3,198,520) is \$851,480, which is likely to be immaterial. Discounting is therefore unlikely to be necessary in this example.

Restoration costs (for the dismantling of temporary buildings constructed on leased land)

On construction of the temporary buildings in Country Z, the United Nations should capitalise the costs of construction in line with IPSAS 17 and depreciate these over the life of the buildings. Furthermore, the United Nations should also recognise a provision for the anticipated costs of dismantling the buildings at the end of the lease. The obligation arises as the United Nations constructs the buildings and this represents a past event.

An asset for the same value should also be recognised, which will be recovered from the economic benefits and service potential generated by the building over its life. This asset should then be depreciated over the life of the building.

Accounting entries to recognise provision for land restoration costs

The following accounting entries should therefore be made to record the provision:

Dr. Buildings (temporary)	\$ 500,000	(statement of financial position)
Cr. Provisions for restoration of land	\$ 500,000	

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