31 Lecture - MGT401

Important Subjective

1. **What is a provision? Provide examples of situations where provisions might be created.**
Answer: A provision is a liability of uncertain timing or amount that a company expects to incur in the future. Examples of situations where provisions might be created include warranty claims, legal settlements, environmental cleanup costs, restructuring costs, and employee benefits.

2. **What is the difference between a provision and a contingent liability?**
Answer: A provision is a liability of uncertain timing or amount that a company expects to incur in the future, while a contingent liability is a possible obligation that arises from past events but whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.

3. **How are provisions measured and recognized in financial statements?**
Answer: Provisions are measured at the best estimate of the expenditure required to settle the present obligation at the end of the reporting period and recognized as a liability in the statement of financial position, with a corresponding charge to the statement of comprehensive income.

4. **What is the difference between a restructuring provision and an onerous contract provision?**
Answer: A restructuring provision is created when a company decides to restructure its operations, such as closing down a plant or laying off employees. An onerous contract provision is created when a company has a contract that is no longer profitable and is expected to result in a future net cash outflow.

5. **What is a contingent asset? Provide examples of situations where a contingent asset might arise.**
Answer: 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 entity. Examples of situations where a contingent asset might arise include legal claims against third parties, insurance claims, and tax refunds.

6. **What is the accounting treatment for a contingent asset?**
Answer: A contingent asset is not recognized in the financial statements because its existence is uncertain. However, if it is virtually certain that the asset will be received, then it may be disclosed in the notes to the financial statements.

7. **How are contingent liabilities disclosed in the financial statements?**
Answer: Contingent liabilities are disclosed in the notes to the financial statements unless the possibility of an outflow of resources is remote.

8. **What is the difference between a legal claim and a constructive obligation?**
Answer: A legal claim arises when a third party makes a claim against the company that is legally enforceable. A constructive obligation arises from past events that give rise to a moral

obligation to pay or perform but where there is no legal obligation.

9. **How is the likelihood of a contingent liability assessed?**
   Answer: The likelihood of a contingent liability is assessed by considering the available evidence and the possibility of future events.

10. **What is the difference between a provision and a reserve?**
    Answer: A provision is a liability of uncertain timing or amount that a company expects to incur in the future, while a reserve is a portion of retained earnings that has been set aside for a specific purpose, such as future expansion or dividend payments. Reserves are not recognized as liabilities in the statement of financial position.