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Things Your CFO Wishes You Knew

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450 Contingencies
20 Loss Contingencies
25 Recognition

General Note: The Recognition Section provides guidance on the required criteria, timing, and location (within the financial statements) for recording a particular item in the financial statements. Disclosure is not recognition.

General

> General Rule

450-20-25-1 When a loss contingency exists, the likelihood that the future event or events will confirm the loss or impairment of an asset or the incurrence of a liability can range from probable to remote. As indicated in the definition of contingency, the term is used for convenience to include many charges against income that are commonly referred to as expenses and others that are commonly referred to as losses. The Contingencies Topic uses the terms *probable,* reasonably possible, and *remote* to identify three areas within that range.

450-20-25-2 An estimated loss from a loss contingency shall be accrued by a charge to income if both of the following conditions are met:

a. **Information available before the financial statements are issued or are available to be issued (as discussed in Section 855-10-251 indicates that it is probable that an asset had been impaired or a liability had been incurred at the date of the financial statements. Date of the financial statements means the end of the most recent accounting period for which financial statements are being presented. It is implicit in this condition that it must be probable that one or more future events will occur confirming the fact of the loss.**

b. **The amount of loss can be reasonably estimated.**

The purpose of those conditions is to require accrual of losses when they are reasonably estimable and relate to the current or a prior period. Paragraphs 450-20-55-1 through 55-17 and Examples 1-2 (see paragraphs 450-20-55-18 through 55-351 illustrate the application of the conditions. As discussed in paragraph 450-20-50-5. disclosure is preferable to accrual when a reasonable estimate of loss cannot be made. Further, even losses that are reasonably estimable shall not be accrued if it is not probable that an asset has been impaired or a liability has been incurred at the date of an entity's financial statements because those losses relate to a future period rather than the current or a prior period. Attribution of a loss to events or activities of the current or prior periods is an element of asset impairment or liability incurrence.

> Assessing Probability of Incurrence of a Loss

450-20-25-3 The conditions in the preceding paragraph are not intended to be so rigid that they require virtual certainty before a loss is accrued. Instead, the condition in (a) in the preceding paragraph is intended to proscribe accrual of losses that relate to future periods.

> Assessing Whether a Loss Is Reasonably Estimable

450-20-25-4 The condition in paragraph 450-20-25-2(b) is intended to prevent accrual in the financial statements of amounts so uncertain as to impair the integrity of those statements.

450-20-25-5 That requirement shall not delay accrual of a loss until only a single amount can be reasonably estimated. To the contrary, when the condition in paragraph 450-20-25-2(a) is met and information available indicates that the estimated amount of loss is within a range of amounts, it follows that some amount of loss has occurred and can be reasonably estimated. Thus, when the condition in paragraph 450-20-25-2(a) is met with respect to a particular loss contingency and the reasonable estimate of the loss is a range, the condition in paragraph 450-20-25-2(b) is met and an amount shall be accrued for the loss.

> Events After the Date of the Financial Statements

450-20-25-6 After the date of an entity's financial statements but before those financial statements are issued or are available to be issued (as discussed in Section 855-10-25) information may become available indicating that an asset was impaired or a liability was incurred after the date of the financial statements or that there is at least a reasonable possibility that an asset was impaired or a liability was incurred after that date. The information may relate to a loss contingency that existed at the date of the financial statements, for example, an asset that was not insured at the date of the financial statements. On the other hand, the information may relate to a loss contingency that did not exist at the date of the financial statements, for example, threat of expropriation of assets after the date of the financial statements or the filing for bankruptcy by an entity whose debt was guaranteed after the date of the financial statements. In none of the cases cited in this paragraph was an asset impaired or a liability incurred at the date of the financial statements, and the condition for accrual in paragraph 450-20-25-2(a) is, therefore, not met.

450-20-25-7 If a loss cannot be accrued in the period when it is probable that an asset had been impaired or a liability had been incurred because the amount of loss cannot be reasonably estimated, the loss shall be charged to the income of the period in which the loss can be reasonably estimated and shall not be charged retroactively to an earlier period. All estimated losses for loss contingencies shall be charged to income rather than charging some to income and others to retained earnings as prior period adjustments.

> Business Risks

Securities and Exchange Commission (SEC)

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> Accounting for Legal Costs

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