
IASB[®] meeting

Date **December 2025**
Project **Provisions—Targeted Improvements**
Topic **Recognition—Legal obligations**
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Purpose of paper

1. The International Accounting Standards Board (IASB) published Exposure Draft [*Provisions—Targeted Improvements*](#) (Exposure Draft) in November 2024, with a comment deadline of 12 March 2025. The Exposure Draft proposes amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.
2. The IASB discussed feedback on the Exposure Draft at its [June 2025 meeting](#), Members of the Accounting Standards Advisory Forum (ASAF) provided their views on how the IASB should move forward in the light of that feedback at their [July 2025 meeting](#).
3. At this meeting, we will ask the IASB to redeliberate aspects of the proposals in the light of the feedback received.
4. This paper asks for decisions on an aspect of the proposals relating to the recognition of a provision—the requirement for the entity to have a present obligation to transfer an economic resource as a result of a past event (present obligation criterion).

5. The present obligation criterion comprises three conditions—‘obligation’, ‘transfer’ and ‘past-event’ conditions. This paper asks for decisions on aspects of the **obligation** condition—aspects relating to **legal obligations**.

Staff recommendations

6. The staff recommend:
- (a) revising the criteria proposed in the Exposure Draft for identifying a legal obligation—that is, for concluding that an entity has no practical ability to avoid discharging a legal responsibility—to require that either:
 - (i) the responsibility is legally enforceable—the counterparty has a right to ask a court to force the entity to discharge the responsibility or to pay a penalty or compensation for failing to do so; or
 - (ii) the counterparty has a right to take another form of action against the entity for failing to discharge the responsibility and, as a result, the economic consequences for the entity of not discharging the responsibility are expected to be significantly worse than the costs of discharging it.
 - (b) adding no application guidance on how to assess the economic consequences of failing to discharge a responsibility.
 - (c) as proposed in the Exposure Draft, making no changes to existing requirements in IAS 37 for proposed new laws that have yet to be finalised.

Contents of this paper

7. This paper:
- (a) provides an overview of:
 - (i) the present obligation criterion proposed in the Exposure Draft and the obligation condition within that criterion (paragraphs 8–12); and
 - (ii) overall stakeholder feedback on the obligation condition (paragraphs 13–15); and
 - (b) discusses in more detail feedback on two aspects of the proposed obligation condition:
 - (i) the criteria for identifying a legal obligation (paragraphs 16–38); and
 - (ii) requirements for proposed new laws that have yet to be finalised (paragraphs 39–53).

Overview of the obligation condition

Exposure Draft proposals

8. The Exposure Draft proposes to update the wording of the present obligation criterion to align it with the definition of a liability in the IASB's *Conceptual Framework for Financial Reporting (Conceptual Framework)*. It also proposes to identify and explain three separate conditions within the present obligation criterion:
- (a) an obligation condition—the entity has an obligation;
 - (b) a transfer condition—the nature of the entity's obligation is to transfer an economic resource; and
 - (c) a past-event condition—the entity's obligation is a present obligation that exists as a result of a past event.

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9. Paragraph 14B of the Exposure Draft defines the obligation condition. It proposes that an entity has an obligation if:
- (a) a mechanism is in place that imposes a responsibility on the entity if it obtains specific economic benefits or takes a specific action;
 - (b) the entity owes that responsibility to another party; and
 - (c) the entity has no practical ability to avoid discharging the responsibility if it obtains the specific economic benefits or takes the specific action.
10. Using existing definitions of legal and constructive obligations in IAS 37, paragraph 14C of the Exposure Draft clarifies that the mechanism imposing a responsibility could be legal (deriving from an operation of law) or constructive (deriving from an entity's established pattern of past practice, policies or current statement).
11. Paragraph 14F of the Exposure Draft specifies criteria for identifying legal and constructive obligations—that is, for concluding that an entity has no practical ability to avoid discharging:
- (a) a legal responsibility; or
 - (b) a constructive responsibility.
12. Paragraph 14G carries forward an existing requirement in IAS 37 that specifies when an obligation arises if details of a proposed new law have yet to be finalised.

Stakeholder feedback

13. Many respondents—from all stakeholder groups and regions—expressed outright or broad agreement with the proposals to amend the requirements supporting the present obligation recognition criterion. Some of these respondents specifically welcomed the proposal to separate the obligation, transfer and past-event conditions within the present obligation criterion. They said that separating the conditions in this way would provide a clearer framework for analysing obligations.

14. However, even respondents who expressed broad agreement with the proposed requirements overall went on to express concerns about aspects of the requirements.
15. The main concerns expressed about the obligation condition related to:
 - (a) the criteria in paragraph 14F(a) for identifying a *legal* obligation (discussed in paragraphs 16–38);
 - (b) requirements in paragraph 14G relating to proposed new laws that have yet to be finalised (discussed in paragraphs 39–53); and
 - (c) the criterion in paragraph 14F(b) for identifying a *constructive* obligation (discussed in Agenda Paper 22B *Recognition condition—Constructive obligations* for this meeting).

Criteria for identifying a legal obligation

Exposure draft proposals (paragraph 14F(a))

16. Paragraph 14F(a) of the Exposure Draft proposes to change the criteria in IAS 37 for identifying a legal obligation—that is, the criteria for concluding that an entity has no practical ability to avoid discharging a legal responsibility:
 - (a) at present, paragraph 17 of IAS 37 requires that ‘settlement of the obligation can be enforced by law’; whereas
 - (b) paragraph 14F(a) of the Exposure Draft proposes that:
 - (i) the counterparty to the obligation has a legal right to act against the entity if the entity fails to discharge the responsibility—for example, to ask a court to enforce settlement, charge the entity a financial penalty or restrict the entity’s access to economic benefits; and
 - (ii) as a result of that right, the economic consequences for the entity of not discharging the responsibility are expected to be significantly worse than the costs of discharging it.

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17. The change is intended to clarify the treatment of increasingly-common ‘soft’ laws and regulations—those that are not enforceable through the courts but that give an entity a strong economic incentive to comply. The IFRS Interpretations Committee considered an example in reaching its conclusions in [Agenda Decision *Negative Low Emission Vehicle Credits \(IAS 37\)*](#). In that example, a government imposed climate-related regulations on vehicle manufacturers. The government had no legal right to force manufacturers to comply with the regulations, but had a legal right to withdraw market access from manufacturers that failed to comply.
18. The intention of paragraph 14F(a) in the Exposure Draft is to clarify that, for a legal responsibility to meet the obligation condition, it is not necessary for compliance to be legally enforceable—it is sufficient that economic incentives to comply are strong enough for the entity to have no practical ability to avoid complying.
19. The wording of the proposed requirement reflects wording in paragraph 4.34 of the *Conceptual Framework for Financial Reporting*, which states that:
- 4.34 The factors used to assess whether an entity has the practical ability to avoid transferring an economic resource may depend on the nature of the entity’s duty or responsibility. *For example, in some cases, an entity may have no practical ability to avoid a transfer if any action that it could take to avoid the transfer would have economic consequences significantly more adverse than the transfer itself. ...* (Emphasis added)

Feedback from respondents to the Exposure Draft

20. Many respondents commenting on the obligation condition raised concerns about the wording of the criteria in paragraph 14F(a)—specifically on the proposal in paragraph 14F(a)(ii) that the counterparty’s legal right to act against the entity must be such that the economic consequences of non-compliance are expected to be significantly worse than the costs of compliance.

The criteria would not capture all legal obligations

21. Respondents expressed concern that this requirement would not capture all legal obligations that should be captured (and that they think the IASB intends to capture). They argued that:

- (a) the requirement would fail to capture a legal obligation if the compensation payable for non-compliance is less than or similar to the cost of compliance.

Respondents expressed a view that, in these circumstances the question is not whether the entity has an obligation (it does) but the amount at which it should measure that obligation. Some respondents suggested that the entity should recognise the lower of the two amounts, consistent with the requirements for onerous contracts in paragraph 68 of IAS 37.

- (b) the requirement would fail to capture a legal obligation if the economic consequences of non-compliance are worse, but not *significantly* worse, than the cost of compliance.

Respondents asked why the consequences must be *significantly* worse.

- (c) by focusing on *economic* consequences, the requirement would fail to capture an obligation an entity might be unable to avoid for other reasons—for example, because non-compliance could lead to imprisonment of the entity's directors or protracted litigation.

- (d) by referring to *expected* consequences, the requirement would fail to capture legal obligations that the entity does not expect to be detected or stringently enforced.

A few respondents—mainly accounting firms—expressed a view that uncertainties over detection or enforcement should not affect conclusions on whether the entity *has* an obligation. Instead, they should be considered in applying one of the other recognition criteria in IAS 37—the requirement in paragraph 14(b) of IAS 37 that it is probable that an outflow of economic resources will be required to settle the obligation (the probable outflows criterion)—and in the measurement of the obligation.

Costs and complexity

22. Some respondents—including preparers of financial statements—also expressed concerns that the proposed criteria for identifying legal obligations would be difficult to apply in practice, so would increase the costs and complexity of applying IAS 37 and the risks of inconsistent application. Respondents noted that:

- (a) an entity would be required to evaluate the economic consequences of defaulting on every one of its legal responsibilities.

Predicting the economic consequences of failing to discharge some types of responsibilities could be difficult—for example, if the responsibilities are not due to be discharged until many years in the future.

- (b) the term ‘significantly worse’ is unclear and judgements would be subjective.
(c) the term ‘economic consequences’ is not defined.

There is a risk of the term being interpreted too narrowly, as encompassing only items recognised as expenses in financial statements and not, for example, reputational damage or enhancement.

- (d) it is unclear whether and how the term ‘expected’ differs in meaning from the term ‘probable’ used elsewhere in IAS 37.

Suggested solutions

23. Respondents suggested two alternative ways of capturing all the obligations they think should be captured:

- (a) a few respondents suggested retaining the existing criterion in IAS 37—that settlement can be enforced by law—but adding a statement that assessing whether the criterion is met would require the exercise of judgement in some cases (for example, those involving ‘soft’ law). One respondent noted that legal enforceability is a key concept underlying other IFRS Accounting Standards.

- (b) other respondents suggested revising the proposed criteria so that it is sufficient that a responsibility is legally enforceable—that is, that the counterparty has the right to ask a court to force the entity to discharge the responsibility or to pay a penalty or compensation for failing to do so.

The need to consider the economic consequences of non-compliance would then apply only in the absence of legal enforceability.

24. A few respondents asked for guidance (including illustrative examples) to help entities assess the economic consequences of non-compliance. They asked for guidance on:

- (a) the meaning of ‘economic consequences’.
- (b) the meaning of ‘significantly worse’. One respondent suggested adding the interpretation in paragraph BC4.55 of the Basis for Conclusions on the *Conceptual Framework*—the adverse economic consequences of not discharging the responsibility would be so severe that the entity has no practical ability to avoid discharging it.
- (c) how uncertainties around detection and enforcement should be treated in applying the obligation condition.

25. A few respondents suggested omitting the term ‘significantly’ or using a term other than ‘significant’, which a respondent said is already over-used in IFRS Standards and interpreted in different ways in different contexts.

Feedback from ASAF members

26. At their meeting in July 2025, a few ASAF members commented on how the IASB should respond to the feedback on this matter:

- (a) the Australian Accounting Standards Board (AASB) / External Reporting Board, New Zealand (XRB) representative expressed support for specifying that legal enforceability is sufficient; and
- (b) the Autorité des Normes Comptables, France (ANC) representative expressed support for removing the word ‘significantly’ from the description of a legal obligation.

Staff analysis

The proposed criteria would not capture all legal obligations

- 27. As explained in paragraph 18, the requirement proposed in the Exposure Draft is intended to clarify that the definition of a legal obligation includes *not only* responsibilities that can be enforced through the courts, but *also* responsibilities that an entity has no practical ability to avoid for other reasons.
- 28. However, the feedback from respondents indicates that the effect of the proposed requirement could be the opposite of that intended—it could serve to *narrow* the existing definition of a legal obligation to *exclude* some legal responsibilities that are enforceable through the courts.
- 29. As explained in paragraph 23, a few respondents suggested retaining the existing criterion in IAS 37—that is, that settlement of a legal responsibility can be enforced by law—while clarifying that whether the requirement is met would require the exercise of judgement in some cases (for example, in relation to soft law). However, such an approach would do nothing to clarify *how* to make the judgement in difficult cases, so would fail to meet one of the objectives of the proposed amendments.

30. Some other respondents instead suggested revising the proposed criteria so that it is sufficient that the obligation is legally enforceable—that is, that the counterparty has the right to ask a court to force the entity to discharge the responsibility or to pay a penalty or compensation for failing to do so. The need to consider the economic consequences of non-compliance would then apply only in the absence of legal enforceability.
31. To achieve this revision, criteria proposed in the Exposure Draft could be reworded along the following lines:

An entity has no practical ability to avoid discharging a responsibility:

- (a) in the case of a legal obligation, if either:
 - (i) the responsibility is legally enforceable—that is, the other party has a legal right to act against the entity if the entity fails to discharge the responsibility—for example, to ask a court to enforce settlement, charge the entity a financial penalty or restrict the entity's access to economic benefits; and ask a court to force the entity to discharge the responsibility or to pay a penalty or compensation for failing to do so; or
 - (ii) the other party has a right to take another form of action against the entity for failing to discharge the responsibility and, as a result of that right, the economic consequences for the entity of not discharging the responsibility are expected to be significantly worse than the costs of discharging it.

32. In favour of revising the proposed criteria in this way, it could be argued that:
- (a) the criteria would be clear and simple to apply in the majority of cases—any legal responsibility that is legally enforceable would meet the criteria.
 - (b) the criteria would provide a principle to apply in the minority of cases where a legal responsibility is not legally enforceable, thus meeting an objective of the proposed amendments.

The proposed criteria would be difficult to apply

33. As explained in paragraph 22, some respondents expressed concern that a requirement to assess the economic consequences of failing to discharge a responsibility would be difficult to apply in practice, increasing both the costs and complexity of applying IAS 37 and the risks of inconsistent application.
34. Revising the proposed criteria as described in paragraph 30 would help address this concern. A requirement to assess the economic consequences of failing to discharge a responsibility would be less burdensome if it an entity had to apply it only to ‘soft’ laws and regulations, which are much less common than legally enforceable obligations.

Requests for more guidance

35. As detailed in paragraph 24, a few respondents requested additional guidance on how to assess the economic consequences of failing to discharge a responsibility. However, assessing these economic consequences would require consideration of all the facts and circumstances, which could vary widely. Developing guidance would require further research and consultation and we do not have evidence of a widespread need for the guidance—only one or two respondents asked for guidance on each of the matters listed and none provided a view on what the guidance should be.

Removing or replacing the term ‘significantly’

36. As noted in paragraph 21(b), a few respondents asked why the economic consequences of failing to discharge a responsibility had to be ‘significantly’ worse than the costs of discharging it. And, as noted in paragraph 25, a few respondents suggested the term ‘significantly’ could be difficult to interpret. These respondents suggested either removing the term or replacing it with another term.
37. However, none of the respondents suggested an alternative term and, as explained in paragraph 19, the proposed use of the term ‘significantly’ is consistent with its use in the *Conceptual Framework*.

Staff recommendations

38. For the reasons set out in paragraphs 28, 32, 34, 35 and 37, we recommend:
- (a) revising the criteria proposed in the Exposure Draft for identifying a legal obligation—that is, for concluding that an entity has no practical ability to avoid discharging a legal responsibility—to require that either:
 - (i) the responsibility is legally enforceable—the counterparty has a right to ask a court to force the entity to discharge the responsibility or to pay a penalty or compensation for failing to do so; or
 - (ii) the counterparty has a right to take another form of action against the entity for failing to discharge the responsibility and, as a result, the economic consequences for the entity of not discharging the responsibility are expected to be significantly worse than the costs of discharging it.
 - (b) adding no application guidance on how to assess the economic consequences of failing to discharge a responsibility.

Questions for the IASB**Criteria for identifying a legal obligation**

1. Do you agree with the recommendation to revise the criteria for identifying a legal obligation as set out in paragraph 38(a)?
2. Do you agree with the recommendation in paragraph 38(b) to add no application guidance on how to assess the economic consequences of failing to discharge a responsibility?

Requirements for proposed new laws that have yet to be finalised

Exposure Draft proposals

- 39. Paragraph 14G of the Exposure Draft proposes to move but not change requirements currently in paragraph 22 of IAS 37.
- 40. These requirements state that if details of a proposed new law have yet to be finalised, an obligation arises only when the legislation is virtually certain to be enacted as drafted.
- 41. The proposed move is part of the reorganisation required to separate requirements supporting the obligation condition from those supporting the past-event condition.

Feedback from respondents to the Exposure Draft

- 42. Some respondents to the Exposure Draft asked the IASB to reconsider the ‘virtually-certain’ threshold.

Application difficulties

- 43. Some accounting firms, preparers of financial statements, accountancy bodies and standard-setters said that the political judgements required to conclude on whether legislation is virtually certain to be enacted as drafted are (increasingly) difficult and subjective, especially:
 - (a) in jurisdictions where changes can be made until late in the lawmaking process; and
 - (b) in energy industries, where new laws and regulations may be proposed for political reasons, with doubt as to whether or when they will be enacted.

44. These respondents said that reaching and documenting conclusions on this matter places a heavy burden on preparers and auditors and has led to diversity in practice:

The legal obligations that underpin asset retirement and environmental obligations may come from a number of different legislative authorities. Many of our operations and facilities are subject to a variety of environmental requirements under federal, provincial, state and local laws, regulations, permits and approvals, all of which vary depending on the specific operation and location. Licenses, permits, and approvals at sites are obtained in accordance with applicable laws and regulations, which may regulate land, water, and raw material use and management, waste storage and disposal, emissions and other discharges.

We must consider all of these legal requirements in determining our environmental remediation liability, and in more recent years, we have observed increased discussion on whether it is virtually certain that a law or change in law will be enacted.,

CL15 Nutrien Ltd

Inconsistencies with IAS 12

45. Some respondents referred to the requirements in IAS 12 *Income Taxes*:
- (a) paragraph 46 of IAS 12 requires entities to measure current tax assets and liabilities using tax rates and laws that have been ‘enacted or substantively enacted’;
 - (b) paragraph 48 of IAS 12 explains that in some jurisdictions, the announcement of a tax rate or law might have the substantive effect of actual enactment.
46. These respondents questioned the need for differences between IAS 37 and IAS 12, a national standard setter noting that some levies within the scope of IAS 37 are enacted via tax legislation.

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47. Two accountancy bodies suggested that determining the point of substantive enactment within a particular jurisdiction's legislative process is less subjective than judging when an individual piece of legislation is virtually certain to be enacted as drafted. They said views on the former are well-established.
48. Respondents suggested various alternatives:
- (a) some respondents, including most of the preparers commenting on this matter, suggested amending paragraph 14G to state that an obligation arises only when legislation has been enacted. They said this approach would improve comparability, reduce subjectivity and lower the risk of recognising provisions for obligations that may never arise.
 - (b) others suggested:
 - (i) aligning the threshold in IAS 37 with the substantively-enacted threshold in IAS 12 (and providing more guidance on interpreting the substantively-enacted threshold);
 - (ii) providing more guidance on interpreting the virtually-certain threshold, including on whether and how it differs from the substantively-enacted threshold in IAS 12; or
 - (iii) requiring entities to disclose management's judgements in reaching its conclusions on whether the virtually-certain threshold has been met.

Feedback from ASAF members

49. At their meeting in July 2025, a few ASAF members commented on how the IASB should respond to the feedback on this matter:

- (a) the AASB/XRB and Accounting Standards Board of Japan representatives expressed support for aligning the threshold in IAS 37 with the substantively-enacted threshold in IAS 12.
- (b) the Asian-Oceanian Standard-Setters Group representative noted split views among its members—some members would align the threshold in IAS 37 with the substantively-enacted threshold in IAS 12, but others would retain the existing virtually-certain threshold; and
- (c) the ANC representative expressed a view that no law is virtually certain to be enacted until it is enacted.

Staff analysis

- 50. Responses to the Exposure Draft provide evidence that the existing requirements for proposed new laws can be difficult to apply, and perhaps have become increasingly difficult to apply in recent years. However, these difficulties are not a consequence of amendments proposed in the Exposure Draft.
- 51. By proposing to move the existing requirement for proposed new laws (showing the deletion of one paragraph and the insertion of another), the Exposure Draft has drawn attention to this requirement, and perhaps given the impression that the scope of this project includes reviewing the requirement. However, reviewing the existing virtually-certain threshold would expand the scope of the project, requiring further research, analysis and consultation with stakeholders, and delaying completion of the project.
- 52. Furthermore, we have evidence to suggest that there is not a clear consensus among our stakeholders on whether and, if so, how the threshold should change—as explained in paragraphs 48 and 49, some stakeholders have said they would prefer to retain the existing virtually-certain threshold, some have suggested aligning IAS 37 with the substantively-enacted threshold in IAS 12, and others have suggested requiring actual enactment.

Staff recommendation

53. For the reasons explained in paragraphs 50–52, we recommend that, as proposed in the Exposure Draft, the IASB make no changes to existing requirements in IAS 37 for proposed new laws that have yet to be finalised.

Question for the IASB

Proposed new laws that have yet to be finalised

Do you agree with the recommendation in paragraph 53?