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Message from the CEO: What the financial statements say – or not – about fraud and corruption

There is a view that the financial statements report on fraud and corruption and that there will be a line item in the financial statements or notes saying “Fraudulent and/or corrupt activities”. There is also a view that the disclosure of items such as “irregular expenditure” always equates to fraudulent or corrupt activities.

Can financial statements aid in the fight against fraud and corruption?

To respond to the first idea that the financial statements will highlight fraud and corruption in a well labelled line item or disclosure, the answer is probably “no”. There is no specific Standard of GRAP that deals with the reporting of fraud and corrupt activities, transactions or balances.

The requirements of the Standards of GRAP are designed to report information to a wide range of users - those who provide resources to the entity, and those who rely on an entity’s services - to enable them to hold entities accountable and to make decisions. While the financial statements do not actively seek to identify fraud and corruption, the information in the financial statements can be used to identify trends and to predict certain outcomes. If there are anomalies or inconsistencies in the information based on users’ expectations, this allows users an opportunity to interrogate and investigate the underlying information. While not all inconsistencies and anomalies are related to fraud and corruption, they may warrant more attention.

It is also possible that accounting policy choices, along with the presentation and disclosure of information, can be used to hide fraud and corruption. Preparers and users should be vigilant and interrogate changes to accounting policies along with what information is disclosed and how it is presented. As an example, a person in an organisation may recommend changes to the accounting policy on provisions to reduce liabilities in the financial statements. This could be to achieve an individual/organisational performance target to reduce liabilities. Using accounting to achieve a specific outcome is always worth interrogating.

GRAP 1 on *Presentation of Financial Statements* indicates that information not specifically required by the Standards of GRAP should be disclosed to enable users to understand the impact of particular transactions, other events and conditions on the entity’s financial position and financial performance. Judgement should be exercised by preparers to assess whether or what information related to fraud and corruption is required in the financial statements, and/or whether presentation elsewhere in the annual report may be more appropriate.

Does irregular expenditure always mean fraud and corruption?

Irregular expenditure, what it means and its disclosure in the financial statements, is governed by the requirements of the Municipal Finance Management Act and the Public Finance Management Act and their respective Regulations. Irregular expenditure does not always equate to fraud and corruption as

irregular expenditure relates to non-compliance with the procurement requirements, which could result for various reasons. Irregular expenditure also does not mean that the financial statements were not prepared in compliance with the Standards of GRAP.

While preparers may be well versed with what irregular expenditure means and how it arises, users of the financial statements may not. It is important to educate users each year on what irregular expenditure and other legal disclosures mean – particularly in the context of fraud and corruption.

As a professional accountant, what is your role?

Professional accountants subscribe to a Code of Ethics and Conduct. This means that when professional accountants prepare financial statements, they are required to apply the same ethical principles and conduct as with any other decision. When financial statements are prepared by professional accountants, by applying professional ethics, financial statements go a long way to producing credible, transparent information, that can aid anti-corruption and anti-fraud initiatives.

ISSB issues IFRS Sustainability Disclosure Standards

The International Sustainability Standards Board (ISSB) issued its first two global sustainability disclosure standards on 26 June 2023. The Standards, namely IFRS S1 and IFRS S2, aim to improve trust and confidence in company disclosures about sustainability to inform investment decisions.

The ISSB Standards are designed so that companies provide sustainability related information alongside financial statements. The Standards are built on the concepts that underpin the IFRS Accounting Standards, but they can be used in conjunction with any accounting requirements. The ISSB Standards create a global baseline that is suitable for application around the world, with any additional jurisdictional requirements being built on top of this global baseline.

[IFRS S1 - General Requirements for Disclosure of Sustainability-related Financial Information](#)

IFRS S1 requires the disclosure of information about an organisation's sustainability related risks and opportunities over the short, medium and long term. It prescribes how an entity prepares and reports its sustainability related financial disclosures by setting out the general requirements for the content and presentation of those disclosures.

[IFRS S2 - Climate-related Disclosures](#)

IFRS S2 sets out requirements for disclosing information about an organisation's climate related risks and opportunities that could reasonably be expected to affect the entity's prospects. The objective of the Standard is for an entity to disclose information about its climate related risks and opportunities that is useful to users in making decisions relating to providing resources to the entity.

Transition and adoption

The Standards are effective for annual reporting periods beginning on or after 1 January 2024, with earlier application permitted. The ISSB plans to work with jurisdictions and companies to support their adoption and implementation of the Standards. A Transition Implementation Group and capacity-building initiatives are some types of support that companies can look out for from the ISSB.

Click [here](#) to watch two high level webcasts on IFRS S1 and IFRS S2, hosted by the ISSB Vice-Chair.

Cash flows in a principal-agent arrangement: is sufficient information disclosed in the financial statements?

A previous article on [Identifying principal-agent arrangements – the nature of transactions with third parties](#) explained the nature of transactions with third parties in a principal-agent arrangement. Where the transactions with third parties are financial transactions, it is likely that cash needs to be transferred from the agent to the principal and vice versa. The disclosures required by GRAP 109 on *Accounting by Principals and Agents* on a principal's resources that are in the custody of an agent at the reporting date may be particularly relevant in these instances.

GRAP 2 on *Cash Flow Statements* requires entities to present information on the gross cash inflows and gross cash outflows in the cash flow statement. There are limited circumstances when GRAP 2

permits an entity to present cash flows on a net basis. These circumstances include cash receipts collected and payments made on behalf of customers, taxpayers or beneficiaries when the cash flows reflect the activities of the other party rather than those of the entity. The allowance refers only to transactions where the resulting cash balances are controlled by the reporting entity. It is therefore likely that an agent may conclude that it is permitted by GRAP 2 to present cash flows from agency activities on the net basis in the cash flow statement.

The post-implementation review of GRAP 109 seeks to establish whether the information required by GRAP 2 and GRAP 109 on cash flows from a principal-agent arrangement is useful to hold both the principal and agent accountable, and for making decisions.

Comment to the Board on ED 200

The ASB published [ED 200](#) on its post-implementation review of GRAP 109 with a comment deadline of 15 September 2023. The Board welcomes comment from all stakeholders on any aspect of GRAP 109.

Comment may be provided in writing through questionnaires (available on the ED 200 webpage on the ASB website) or in any other written form to info@asb.co.za. Comment may also be provided through roundtable discussions. Contact elizna@asb.co.za to be invited to a roundtable discussion.

The Board commenced a Post-implementation Review of GRAP 108 on Statutory Receivables

As part of its 2024-2026 work programme, the Accounting Standards Board (the Board) is undertaking a Post-implementation Review (hereafter “PIR”) of the Standard of GRAP on *Statutory Receivables* (GRAP 108).

What transactions are addressed in GRAP 108?

GRAP 108 sets out the recognition, measurement, presentation and disclosure requirements for statutory receivables. A statutory receivable is a receivable that arises from legislation, supporting regulations or similar means (hereafter “legislation or similar means”). A statutory receivable is required to be settled by another entity in cash or another financial asset.

Statutory receivables differ from contractual receivables. Contractual receivables arise from transactions that are entered into voluntarily, for example where an entity provides goods and services in return for a cash payment (receivable). These receivables are accounted for using GRAP 104 on *Financial Instruments*. Statutory receivables arise from compulsory transactions based on legislative requirements. Examples include receivables for taxes, fines, penalties, appropriations, grants and fees charged in terms of legislation or similar means.

Issues identified to date

The PIR commenced with research to understand how entities apply the principles in GRAP 108, and what information is presented and disclosed in the financial statements on statutory receivables.

General issues

The review noted two general issues with the preparation of financial statements using GRAP 108, namely:

- the accounting policy and/or the note on statutory receivables do not provide information specific to the entity’s circumstances. Entities often use boilerplate information from templates and wording from the definitions and principles in GRAP 108, instead of explaining how the principles in GRAP 108 apply to the entity’s circumstances. For example, the definition of a statutory receivable is used as the accounting policy without explaining how the receivable arises with reference to legislation or similar means; and
- information presented in the financial statements is inconsistent. For example, entities sometimes do not include an accounting policy for statutory receivables, but the financial statements and notes present information on statutory receivables.

Specific issues

Among others, some of the specific issues with the application of GRAP 108 noted from the review include:

- Entities are unsure about the distinction between a statutory receivable and a contractual receivable.
- Where statutory receivables are presented as a separate line item on the face of the statement of financial position, the relevant policy and/or note does not always indicate whether the statutory receivable arises from an exchange or non-exchange transaction. In other instances, receivables are classified on the face of the statement of financial position as either exchange or non-exchange, but the note does not indicate which of the exchange and non-exchange receivables are statutory or contractual in nature.
- Entities' accounting policies incorrectly indicate that statutory receivables are initially recognised at fair value and subsequently measured at amortised cost that approximates fair value.
- Some of the information required to be presented and disclosed on statutory receivables is omitted from either the accounting policy or note. Examples include explaining:
 - (i) how the statutory receivable's transaction amount is determined with reference to the applicable legislation or similar means;
 - (ii) how accrued interest and other charges (i.e. fines and penalties) are levied;
 - (iii) the basis and rate used to recognise interest and other charges levied on the statutory receivable; and
 - (iv) how and when a statutory receivable is derecognised.

These results will be used to identify the specific issues on which the Board needs respondents' views.

The next phase of the PIR

The Board will next seek comment from stakeholders to understand:

- (a) the challenges experienced with the application of GRAP 108; and
- (b) if the disclosure requirements in GRAP 108 provide relevant and useful information to hold entities accountable and for decision-making.

If you are interested to participate in the PIR of GRAP 108, subscribe to the ASB's Newsletter, follow us on social media, or contact Amanda Botha on amandab@asb.co.za for updates on this project.



Contact us

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