



ACCOUNTING STANDARDS BOARD

RESEARCH PAPER

APPLICATION OF STANDARDS OF GRAP BY SMALL ENTITIES



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Executive summary

Why did the Board do research and what was the research about?

Respondents to the Board's work programme consultation for 2017 to 2020 raised concerns with the ability of small entities to prepare financial statements in accordance with Standards of GRAP. Based on stakeholders' concerns, the Board agreed to research the financial reporting environment of small entities to establish what challenges these entities face, and to consider an appropriate response to assist these entities.

The Board's research focused on identifying:

- (a) The characteristics that could be used to classify entities as small.
- (b) The challenges experienced by small entities to prepare financial statements in accordance with Standards of GRAP.

What were the results of the research?

Characteristics to classify entities as small

There is no description or definition in the Standards of GRAP for "small entities". Several matters that could impact the classification of entities as small were identified, including when and how entities could be classified, the specific characteristics that may be used, and the circumstances under which entities may need to be classified.

Stakeholders favoured using a combination of quantitative and qualitative characteristics to classify entities for financial reporting purposes locally, including the following:

- The value of revenue, expenses and an entity's budget.
- The number of employees.
- The functions performed by an entity.

More information on the characteristics identified are included in Appendix B.

Small entity challenges

The challenges are categorised into those affecting (a) accounting, and (b) the broader small entity environment. Since these are interrelated, addressing accounting challenges could resolve one or more issues that are inherent to the broader small entity environment, and vice versa. The conclusion was that a holistic approach should be followed when assisting small entities.

Accounting challenges

The most prevalent accounting challenges, in order of prevalence, are:

- accounting for non-current assets, including measurement and applying judgement related to determining useful lives, residual values and componentisation of assets;
- the requirements in Standards of GRAP are often complex and difficult to interpret;
- accounting for and disclosure of financial instruments;
- keeping up to date with changes to the reporting framework; and



- applying materiality, including determining appropriate accounting policies.

Refer to Appendix C Table 1 for the detail of accounting challenges identified. These challenges are likely to contribute to entities doing unnecessary work when accounting for their transactions and preparing financial statements.

Broader small entity environment

Issues inherent to the environment that small entities operate in included:

- human resource and budget constraints;
- not having daily or monthly controls in place, including proper record keeping;
- placing undue reliance on consultants; and
- an inability to meet all legislated requirements.

Appendix C Table 2 contains more information on these issues.

What decisions did the Board take based on the findings?

The Board's conclusions on the research were based on a number of factors. These included the legislative environment, the impact that different reporting requirements could have on consolidations and other reporting requirements, stakeholder views, and the actions the Board could take to effectively address the challenges identified.

Based on these factors, the Board decided not to introduce any reporting requirements or guidance for small entities. The Board concluded that other initiatives could instead be taken, or have been taken, but the effectiveness of those initiatives could not yet be determined.

- A number of the Board's projects and related guidance could assist entities with the accounting challenges identified, including requirements in the Standards that are misunderstood and misapplied. Most notably, the Board's Guideline on *The Application of Materiality to Financial Statements* (materiality guideline), which was published in 2019, contains guidance that would be useful.
- The Board agreed to publish a Research Paper to communicate the results of the research and raise awareness of the resources available, as it could be useful to stakeholders.

The Board's mandate limits its ability to respond to all the challenges that were identified. These were discussed with those stakeholders that may be better placed to assist small entities.

More information on Board's considerations and conclusions are contained in Section 3 – Board's considerations and conclusions on the project.



Introduction

What is the history of the project?

The Board previously considered whether different reporting requirements should be developed for small entities. The outcome of this resulted in the publication of the Position Paper on *Differential Reporting in the South African Public Sector* in 2011, which can be accessed on the [ASB's website](#). The Board's position was that differential reporting requirements should not be introduced, because of the following:

➤ Users' information needs

Since users need the same information from financial statements for all entities in the public sector, differential reporting was considered inappropriate. It was also noted that it is important for oversight structures, such as Parliament, provincial legislatures and municipal councils, to receive the same information from entities for accountability purposes.

➤ Consolidated financial statements

While one set of consolidated financial statements for all levels of government (whole of government consolidation) was not prepared, it remained government's intention to move towards this position. Introducing another reporting framework would have conflicted with government's intention and would not support the preparation of whole-of-government consolidated financial statements. It was also noted that the PFMA requires the National Treasury and provincial treasuries to prepare consolidated financial statements nationally and provincially. Differential reporting would introduce further difficulty for treasuries to prepare these consolidations.

Respondents to the Board's work programme consultation for 2017 to 2020 noted concerns with the ability of small entities to prepare financial statements in accordance with Standards of GRAP. The main reason for their concerns was constrained resources, including the inability to employ competent staff. The Board agreed to assess how the financial reporting environment of small entities may have evolved since 2011 and to determine the current status.

What was the purpose of the research?

The Board agreed to research whether steps could be taken to address preparers' concerns on the preparation of financial statements using Standards of GRAP when an entity is small. In order to meet this objective, the research focussed on the following matters:

(a) The characteristics that could be used to classify entities as small.

Because no definition or description of "small entities" exists in Standards of GRAP, the Board needed to understand what makes an entity small.

(b) The challenges experienced by small entities to prepare financial statements using Standards of GRAP.

It was necessary for the Board to obtain a clear understanding of the problem, to determine the Board's possible actions.



The Research Paper is set out in three sections:

Section 1 – Research methodology

Section 2 – Results of the research

Section 3 – Board's considerations and conclusions on the project

The Secretariat of the ASB may be contacted on info@asb.co.za if more information is required on the research.

What is the authority of this Research Paper?

The Board publishes Research Papers to outline its research into issues such as the results of any reviews undertaken on the application of Standards of GRAP and/or current practice in applying the Standards or any other topic the Board may deem appropriate. This Research Paper is not authoritative.

Section 1 – Research methodology

The research was conducted during 2018/2019 and considered by the Board in the first quarter of 2019.

How was the research conducted?

The research was conducted using the following methods:

- (1) A *desktop review* of characteristics applied nationally and internationally to identify entities that are considered small. These characteristics enable authorities to prescribe different, less complex accounting and legislative requirements to some entities. The review included obtaining an understanding of the financial reporting frameworks for small entities in other jurisdictions. The results of the review are included in Appendix B – Small entity characteristics.
- (2) A *questionnaire* to stakeholders on the matters being researched.
- (3) A *desktop review* of the financial statements of entities that completed the questionnaire. The purpose of the desktop review was to:
 - confirm and contextualise the challenges entities identified; and
 - identify issues that may exist in these entities' financial statements.
- (4) Two rounds of *engagements with stakeholders* to discuss the matters researched and initial feedback received on the financial reporting environment of small entities.

Engagements with stakeholders – who participated in the project?

Stakeholders were consulted through large scale outreach activities such as a webinar with a live audience hosted by SAICA, a discussion at the PSAF, through a questionnaire, as well as targeted stakeholder engagements.

Stakeholders from all groups with an interest in the project were involved in the research. These stakeholders included preparers, users and auditors of financial statements, professional membership bodies, and consultants and technical specialists.

The specific stakeholders engaged are included in Appendix A.

The results of the research are summarised in Section 2 – Results of the research.

Section 2 – Results of the research

The results of the research are categorised into the following areas, and are presented in this section:

- Characteristics to classify entities as small.
- Challenges small entities have to prepare financial statements using Standards of GRAP.

What characteristics could be used to classify entities as small?

There is no description or definition in Standards of GRAP for “small entities”. Several matters that could impact on the classification of entities were identified, including the following:

- Considerations in classifying entities.
- Specific characteristics.
- The need for classification.

(a) Considerations in classifying entities

In classifying certain entities as small, a number of matters need consideration, including who should classify entities, when they should be classified, and the method used to classify entities.

Who should classify entities?

Stakeholders expressed concern about entities performing a self-assessment to determine if they are small, because small entities find it difficult to apply judgement (see challenges small entities have below). Stakeholders preferred that an oversight body, such as the National Treasury or specific Ministers for the entities within their portfolio, should be responsible to classify entities. If entities perform a self-assessment, stakeholders preferred that an oversight body reviews and approves entities’ assessments of whether they are small.

When should entities be classified?

Stakeholders noted that classifications should not change from one year to the next. Entities should be classified initially, and their classification only reconsidered when there has been a significant change in the nature and/or size of the entity’s business. The treatment of once-off transactions should be considered because they could distort the assessment and lead to inappropriate classifications.

What methods could be used to classify entities?

The research explored whether, as an alternative to applying characteristics, certain types of entities could be classified as small. For example, all district municipalities, or all public entities listed in schedule 3D of the PFMA. Stakeholders noted reservations about this approach, because within each type of entity, entities vary in size and complexity of their transactions.

Users of financial statements expressed concerns about types of entities being classified as small, even when meeting certain characteristics. They highlighted the need for:

- comparability among entities; and
- having the same information available for all entities to enable the preparation of consolidated financial statements.

Reservations were also expressed about classifying certain types of entities as small, for example municipalities and entities under their control, given their importance in delivering services. The same level of information would be required from these entities, to hold them accountable and for users to make decisions.

(b) Specific characteristics

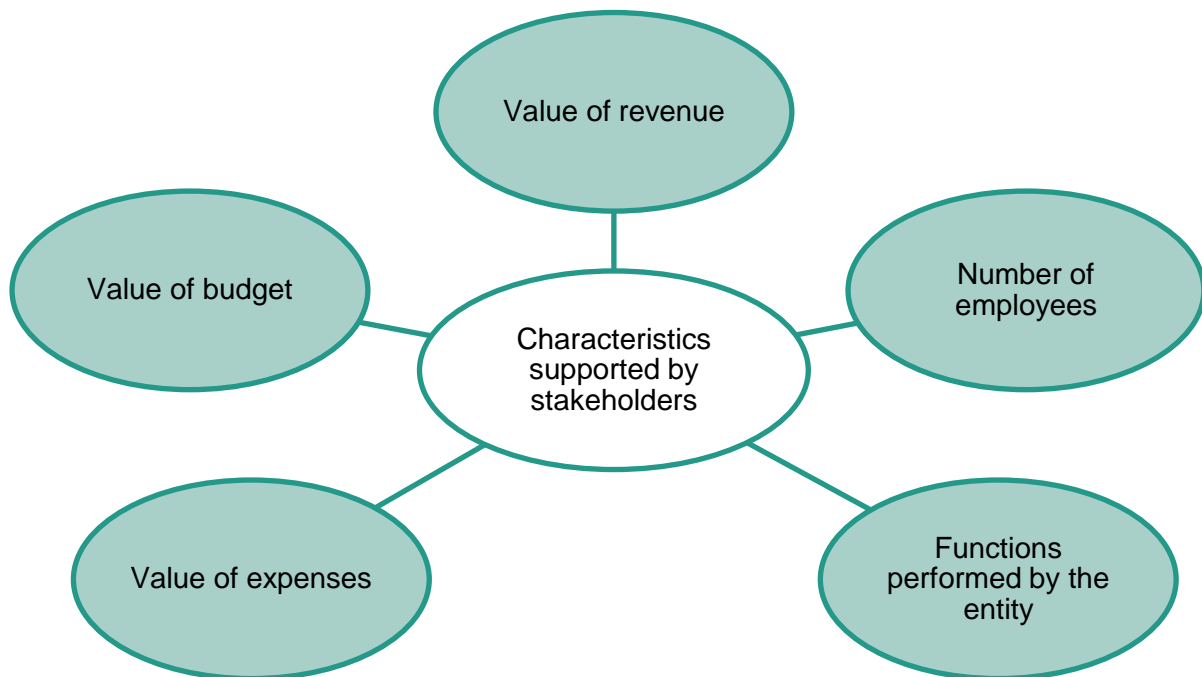
What is used in the national and international environment?

Characteristics that national and international organisations and bodies use to classify entities for various purposes were identified. Refer to Appendix B Table 1 for the detailed information.

What did stakeholders think?

Stakeholders supported the use of a combination of characteristics, both qualitative and quantitative. They were concerned that using only one characteristic could lead to inappropriate classifications. To promote consistency in the entities that are classified locally as small for accountability and reporting purposes by various structures, stakeholders supported an approach of considering existing, instead of identifying new, characteristics.

The following characteristics were mostly supported by stakeholders:



Refer to Appendix B Table 2 for the detailed information on the characteristics supported by stakeholders, with a description of how they proposed that they should be applied.

(c) The need for classification

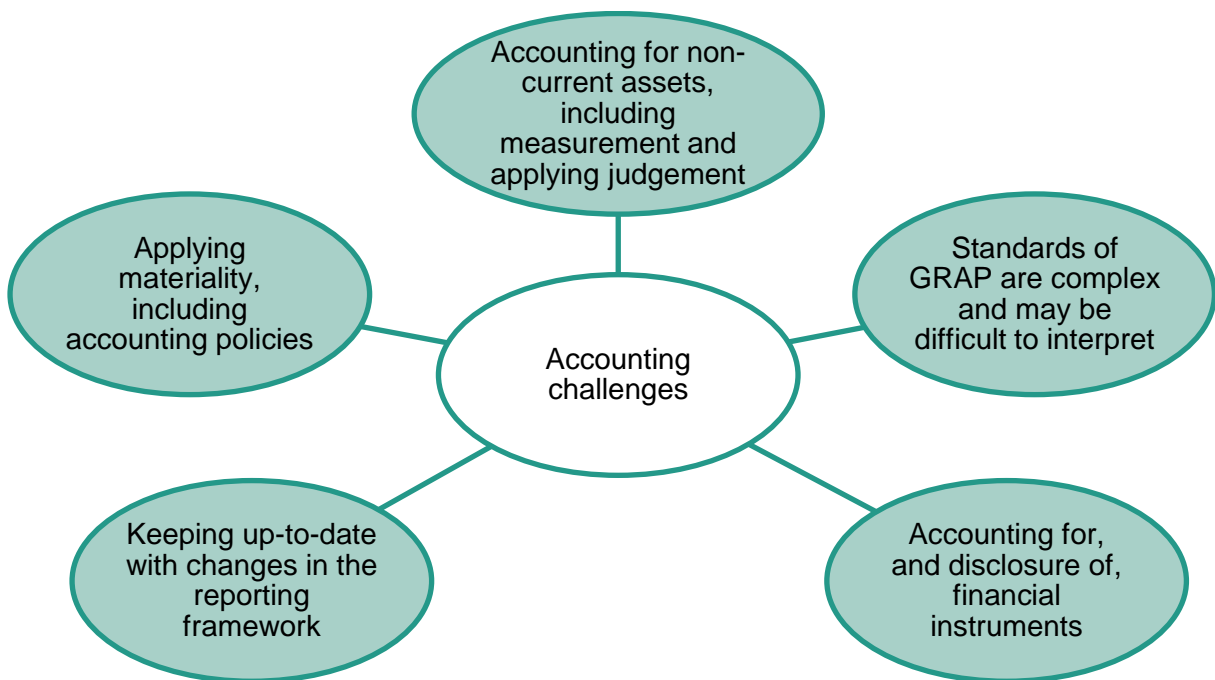
The classification of certain entities as small would have been necessary if the Board decided to prescribe reporting requirements or provide guidance to small entities. A classification is, however, not needed if guidance is provided that will assist all entities. For example, guidance on developing accounting policies that are appropriate for an entity’s size and complexity of transactions could be applied by any entity, irrespective of their size.

What challenges do small entities have to prepare financial statements using Standards of GRAP?

Based on the Board’s mandate and the role it could play to assist small entities to prepare financial statements using Standards of GRAP, the challenges were categorised as relating to (a) accounting, and (b) the broader small entity environment.

Accounting challenges

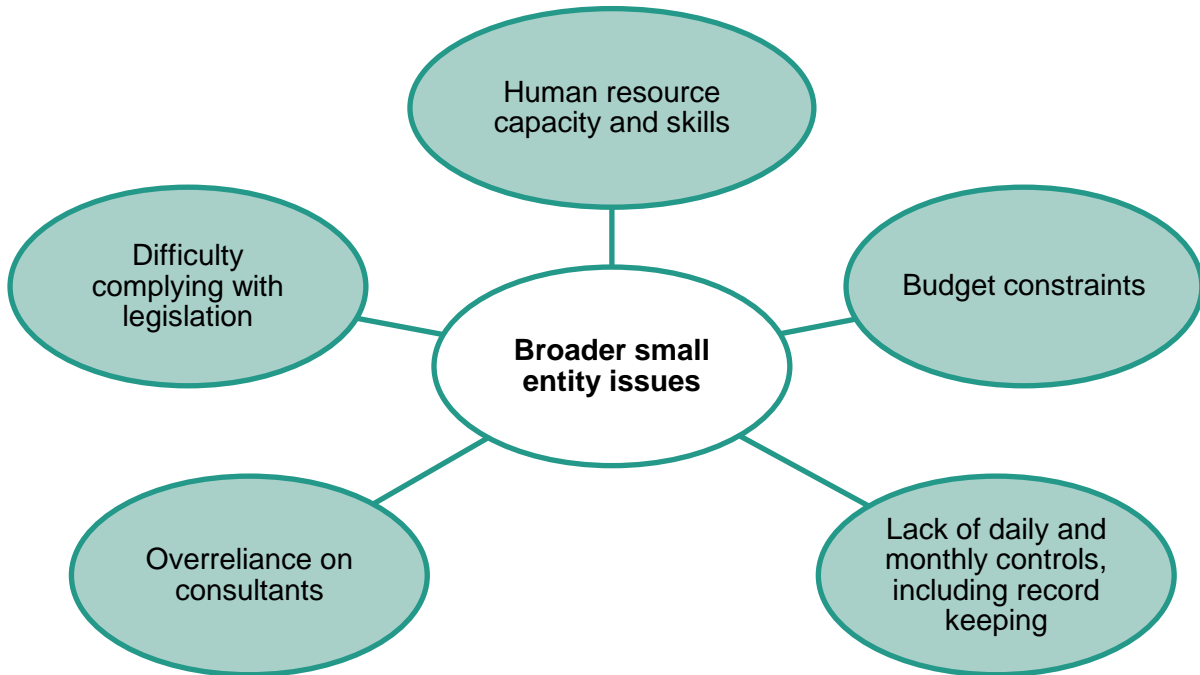
These challenges most often relate to areas where judgement is required. Small entities do not have the necessary skills to apply judgement, nor do they have the resources to acquire those skills. Areas were also identified where the requirements of the Standards of GRAP may be misunderstood and misapplied. The most prevalent of these challenges were as follows:



Refer to Appendix C Table 1 for the detailed information.

Broader small entity environment

A number of issues impact on entities’ ability to prepare GRAP financial statements when they are small, although not directly related to accounting. Addressing these issues is outside the Board’s mandate. The key issues are set out below:



Refer to Appendix C Table 2 for the detailed information.



Section 3 – Board’s considerations and conclusions on the project

What did the Board consider?

The Board considered the factors below in concluding on the project:

- (a) Legislative environment.
- (b) Impact on consolidations and other reporting requirements.
- (c) Effectiveness to address challenges.
- (d) Stakeholder views.

Legislative environment

The Board noted the importance of considering current legislation that affects the financial reporting environment of small entities in the public sector. The legislation identified by the research as relevant and important is included in Appendix D.

To support current legislative requirements, a consistent reporting framework is needed to measure all entities.

Impact on consolidations and other reporting requirements

Whole-of-government consolidation

The Board’s Position Paper in 2011 noted government’s intention to prepare whole-of-government consolidated financial statements as a reason why differential reporting was considered inappropriate. At the time of this research, government was still unable to prepare such a consolidation because departments apply the MCS. Government still intends to prepare whole-of-government consolidated financial statements.

Other consolidations and reporting requirements

The Board identified areas where information needs to be provided by small entities to meet other reporting requirements:

- PFMA legislated consolidations prepared by National and provincial treasuries.
- Consolidations of an economic entity as required by Standards of GRAP.
- Consolidations performed by oversight bodies, such as the SARB and National Treasury for statistical purposes, and DHET for oversight over colleges.
- The SARB and National Treasury require certain information from the financial statements to meet other reporting requirements, for example reporting commitments with the G20 and International Monetary Fund.

The above information needs demonstrate that consistent information should be available for all entities.



Effectiveness to address challenges

The Board considered the challenges in the environment and the actions that could best address those challenges (see Appendix C).

They are mostly related to constrained human and financial resources. These challenges would not be solved by introducing a different reporting framework or guidance for small entities and may exacerbate the challenges. It was further noted that the challenges are not unique to small entities as many entities in the public sector struggle with the same issues.

Stakeholder views

Most stakeholders did not support a different reporting framework for small entities. They noted that users of financial statements generally expressed concern about the information they need no longer being available in financial statements if different or less information is available for small entities.

They considered that, since entities struggle with the basics, adding another framework to the environment, which already includes IFRS, Standards of GRAP and MCS, would not resolve the challenges that exist.

What did the Board decide?

The Board decided not to introduce reporting requirements or guidance for small entities. This decision was based on the research indicating that small entities' challenges could not be resolved by such an action. The Board concluded that other actions that would be more appropriate for the environment should be taken, including:

- A number of the Board's projects and related guidance would assist entities with the accounting challenges identified, as indicated in Appendix C Table 1. Most notably, the materiality guideline contains guidance that would be useful to address some of these challenges.
- Publishing the results of the research and the resources available may assist entities.
- Issues that are outside the Board's mandate to address (inherent to small entities and their environment) have been communicated to stakeholders that may be able to assist small entities.



Appendix A

STAKEHOLDER ENGAGEMENTS

The following stakeholders were involved in the research:

Stakeholder group	Who was involved
Preparers	Public entities, municipalities and municipal entities Consultants involved in preparing financial statements
Users ¹	<ul style="list-style-type: none"> • COGTA • The National Treasury (OAG, Local Government Budget Analysis unit, Public Finance unit, and Public Entity Governance unit) • DHET and SAICA representatives at TVET and CET colleges • Provincial treasuries • Provincial legislatures • SARB
Membership bodies	SAICA, SALGA and IRBA
Auditors	Audit firms, ARD of the AGSA and AGSA auditors of “small auditees”
Technical specialists	Technical specialists from audit and consultancy firms

¹ Initial engagements were held with ASISA and BASA to involve financial institutions and banks in the project. They would have been further involved had the Board decided to progress the project to a next phase. Municipal councils were not directly involved; however, SALGA was extensively involved in the project.

SMALL ENTITY CHARACTERISTICS

Table 1: Existing characteristics of small entities

The research considered the international and national environment to classify entities as small. The table below includes the characteristics used and the purpose.

Body / jurisdiction	Framework and purpose	Characteristics
International		
IASB	IFRS for SMEs which simplifies IFRS requirements	Public accountability, which an entity is deemed to have if e.g. its debt or equity instruments are traded in a public market or it holds assets in a fiduciary capacity for a broad group of external parties.
IAASB ²	Guidance in ISAs to small entities	<ul style="list-style-type: none"> • Concentration of ownership / management and levels of management • Complexity of transactions • Lines of business • Number of employees • Simple internal controls
United Kingdom	Less complex frameworks: <ul style="list-style-type: none"> • FRS for Small Entities • FRS applicable to Micro-entities Regime 	<ul style="list-style-type: none"> • Number of employees • Value of turnover • Book value of total assets

² The IAASB is exploring the topic of the audit of less complex entities, to understand the needs of Small and Medium Practices when applying audit and non-audit IAASB standards. As the project was in early stages at the time of the research, no specific considerations for the project were identified.

Body / jurisdiction	Framework and purpose	Characteristics
	Reduced Disclosure Framework	Controlled entities included in publicly available consolidated financial statements
New Zealand	<ul style="list-style-type: none"> Less complex framework Reduced Disclosure Framework 	<ul style="list-style-type: none"> Public accountability (linked to the IASB definition) Value of expenses
Australia	Reduced Disclosure Framework	Public accountability (linked to the IASB definition)
National		
Companies Act and Regulations	Public Interest score to determine reporting frameworks and audit requirements	<ul style="list-style-type: none"> Number of employees Value of turnover Value of 3rd party liabilities
FRSC	Proposed Reduced Disclosure Framework	Wholly-owned subsidiaries consolidated in IFRS parent AFS
Government Gazette on Municipal upper limits of remuneration	Sets remuneration limits	<ul style="list-style-type: none"> Total municipal income Total population Total municipal equitable share
National Small Enterprise Act	Guidelines to promote small business	<ul style="list-style-type: none"> Number of employees Value of turnover Gross asset value



Body / jurisdiction	Framework and purpose	Characteristics
SARS	Small business classification for tax purposes	<ul style="list-style-type: none"> • Value of turnover • Different requirements for “small business corporation”
SARB	Classification of Public Corporations, Public Enterprises, Extra-Budgetary Institutions and Funds into categories for statistical analysis purposes	List of 10 characteristics, including: <ul style="list-style-type: none"> • Controlling shareholding • Producing goods and services for the open market; Unique goods or services • Financial independence; Profit motive • Right to issue bonds • Dividend and authorised share capital • Legislative requirement
	Requesting surveys for SARB’s economic statistical purposes	<ul style="list-style-type: none"> • Value total assets (when looking at balance sheet) • Value of revenue (when looking at income statement) • Number of employees (when considering social aspects) • Economic subclassification of entities
AGSA	Small auditee methodology prescribing more effective audit approach for these entities	Characteristics included in the AGSA audit methodology
National Treasury Budget unit	Determining which entities’ financial information to review for oversight purposes	Value of budget



Body / jurisdiction	Framework and purpose	Characteristics
National Treasury Public Entity Governance unit	To establish board remuneration categories	Classification framework based on functions. Weighting of below depends on classification: <ul style="list-style-type: none"> • Span of control and mandate • Impact of decisions (local, provincial, national, international) • Size and structure • Skills required
DHET	Classify TVET colleges for funding purposes	Geographical location of college (rural, semi-rural, urban)

Deloitte maintains information about how the IASB and various jurisdictions deal with the financial reporting needs and requirements of different categories of entities, including listed entities, private entities, not-for-profit entities and public sector entities, which can be accessed here: <https://www.iasplus.com/en/resources/topics/differential-reporting>.



Table 2: Stakeholder views on appropriate characteristics

Stakeholders supported the use of the following characteristics to classify entities, in order of support.

Characteristic	Description
Value of revenue	Stakeholders largely supported using the value of total revenue as a criterion. Some stakeholders supported using only government funding, as it represents the funds for which entities are publicly accountable, while others supported using only an entity's own revenue as an indication of the complexity of the entity's transactions.
Number of employees	Although widely supported, some stakeholders considered it arbitrary and inward-looking.
Functions performed by entity	This criterion would assess the nature and extent of the functions an entity is responsible for in accordance with its mandate. Many considered this as telling of how complex an entity is and should weigh more than quantitative measures. This can be assessed with reference to legislation such as the Constitution and Municipal Systems Act for municipalities. For public entities, the classification framework used by the National Treasury's Public Entity Governance unit can be used (see table 1 above). Stakeholders proposed that the criterion should also consider subsidiaries, as functions may have been transferred to them.
Value of expenses	Stakeholders viewed this as telling of the scale of an entity's responsibilities.
Value of budget	
Value of total assets	Support was expressed for looking at the value of total assets, as well as the value of assets that are used to deliver services or to deliver on an entity's mandate.
Wholly owned / controlled entities	Stakeholders supported this criterion because the users of wholly owned and controlled entities are likely limited to the controlling entity and oversight structures. Consolidated information is available from the controlling entity.



Characteristic	Description
Complexity of transactions	Stakeholders agreed that assessing how complex an entity's transactions are would be more meaningful than quantitative measures. The complexity could be assessed at an entity level, based on an entity's activities and the skills required to account for the entity's transactions.
Who are the users	Stakeholders noted that entities with few users may not need to prepare general purpose financial statements.
Immaterial for consolidations	<p>Entities that are immaterial for consolidation purposes also likely have only a few users and may not need to prepare general purpose financial statements.</p> <p>This was noted for various levels of consolidations, including economic entity consolidations and legislated PFMA consolidations by national and provincial governments.</p>
Public accountability	<p>As used in IFRS for SMEs, this refers to the level of an entity's accountability to a wide group of users. The level would be high when an entity has e.g. listed instruments or holds assets in a fiduciary capacity.</p> <p>It was not widely supported as the general view is that all public sector entities receive public funds and manage public assets and are publicly accountable for their use. It was therefore not seen as a distinguishing factor.</p> <p>However, public accountability could be used as an umbrella term and can include assessing the mandate, function, influence, service recipient base, impact on citizens, etc. of an entity.</p>
Number of service recipients	Stakeholders noted that this could also include a geographical assessment of how widely services are delivered.

CHALLENGES IDENTIFIED BY THE RESEARCH

Table 1: Accounting challenges and existing guidance that may assist entities with the challenges

Challenge	Description	Projects and guidance of the Board and Secretariat
Non-current assets: Measurement, applying judgement and accounting for fully depreciated assets	Determining fair value, which was raised as an on-going challenge and not only once-off.	The challenge was mostly raised in the context of the Standard of GRAP on <i>Heritage Assets</i> (GRAP 103). The Board is undertaking a post-implementation review of GRAP 103 and the challenges identified from the research related to GRAP 103 are being considered as part of the post-implementation review.
	Applying judgement to separate assets into components.	The Board has published the materiality guideline, which will assist small entities in deciding when it is necessary to apply the requirements to separate assets into components.
	Applying judgement to determine e.g. useful lives and residual values of assets, and adjusting for fully depreciated assets still in use.	<ul style="list-style-type: none"> The materiality guideline will assist entities to determine when it is necessary to adjust the financial statements for changes to useful lives and residual values, and for fully depreciated assets, based on materiality. As an outcome of developing the materiality guideline, the Secretariat updated an FAQ on <i>What is the treatment of fully depreciated assets still in use (other than on the initial adoption of the Standards of GRAP)?</i>. Awareness is being raised on the FAQ through a webcast and social media. The Secretariat has an FAQ on <i>Must an asset always have a residual value?</i>.
GRAP is complex	The Standards of GRAP are complex and difficult to understand and apply, especially when a reader is not financially literate.	<p>The materiality guideline assists preparers in applying materiality when preparing financial statements:</p> <ul style="list-style-type: none"> Entities should develop accounting policies that are appropriate for their nature, size and complexity of their transactions. The Secretariat has developed material to assist entities with developing appropriate accounting policies, e.g. articles

Challenge	Description	Projects and guidance of the Board and Secretariat
		<p>published in the ASB newsletter and presentations available on the ASB's website.</p> <ul style="list-style-type: none"> • Entities need not apply requirements of the Standards of GRAP when the effect of applying them is immaterial.
Accounting for, and disclosure of, financial instruments	A general inability to account for and disclose financial instruments was raised as the Standard is complex.	<ul style="list-style-type: none"> • As an outcome of the review of GRAP 104, fact sheets have been developed to explain the basic principles of the Standard for specific types of instruments. Although the fact sheets are based on the revised GRAP 104 (2019), the guidance on the basic principles are relevant for the current GRAP 104 (2009), e.g. which instruments are financial instruments. • The materiality guideline will assist entities to develop GRAP accounting policies for material items, and to only disclose information that is material. • The Secretariat has issued the following FAQs on GRAP 104 (2009): <ul style="list-style-type: none"> ○ <i>When (and/or how) should receivables and payables be discounted in accordance with GRAP 104?</i> ○ <i>What is the effective interest rate and how do you calculate it?</i> ○ <i>How do statutory receivables arise?</i> which provides guidance on distinguishing statutory and contractual receivables.
Keeping up-to-date with changes in the reporting framework	The requirements of the Standards change on an annual basis as new Standards become effective and amendments are made to existing Standards. Respondents indicated an inability to keep up-to-date with changes.	<ul style="list-style-type: none"> • The Board publishes an updated annexure to Directive 5 on <i>Determining the GRAP Reporting Framework</i> annually, which outlines changes in the reporting framework from one year to the next. • The Secretariat annually updates FAQs on the GRAP reporting framework applicable for a reporting period. • The Secretariat (with SAICA) creates awareness of newly effective pronouncements through bi-annual GRAP updates in the form of webcasts. Recordings of past webcasts are available on the ASB's website.

Challenge	Description	Projects and guidance of the Board and Secretariat
		<ul style="list-style-type: none"> • CIGFARO and provincial treasuries assist the Secretariat by hosting sessions to raise awareness of newly effective Standards. • Recordings are done (with SAICA) on newly effective Standards of GRAP and other topical matters. These are available on the ASB’s website. • The Secretariat uses social media and the ASB newsletter to reach stakeholders and create awareness with stakeholders of changes, proposed changes and other topical matters.
Applying materiality, including determining appropriate accounting policies	Preparers are unable to apply materiality, including determining appropriate accounting policies. This results in resources being spent to account for and disclose immaterial transactions and information.	<ul style="list-style-type: none"> • The Board published the materiality guideline. • The Secretariat issued a FAQ on <i>What is the role of materiality in the reporting of information in the financial statements?</i> • See challenge on GRAP is complex above for determining appropriate accounting policies.
Disclosures are onerous	Disclosures are onerous for a small entity, specifically applying judgement to decide which disclosures to provide.	The materiality guideline will assist small entities to only disclose information that is material.
Year-end adjustments	These adjustments usually require technical skills and knowledge as well as capacity, which small entities do not have.	<p>See the challenge on “non-current assets” above, which is an area where year-end adjustments arise, for example impairment adjustments.</p> <p>This challenge was further found to stem from other challenges related to the environment of small entities, such as human resource and budget constraints.</p>

The research identified other sources of guidance that may further assist entities. These resources are available on the particular stakeholders’ websites and include the following:

- The OAG’s GRAP Accounting Guidelines, providing practical implementation and application guidance.
- The OAG’s tool on financial instrument disclosure.



- The OAG's GRAP disclosure checklist.
- SAICA recordings and webcasts on GRAP updates and newly effective Standards of GRAP.
- SAICA's monthly TechTalk on public sector matters.



Table 2: Issues related to the broader small entity environment

Challenge	Description
Human resources	<ul style="list-style-type: none"> • Small entities do not have human resource capacity and lack skills to prepare financial statements. • One person is often responsible for a wide range of tasks with limited time and support. • Preparers are not educated on the requirements of Standards of GRAP. • Small entities are unable to train staff due to budget and time constraints. • Due to the geographical location of some entities, they are unable to attract skills. • There is high staff turnover as small entities are often used as “steppingstones”.
Constrained budget	<ul style="list-style-type: none"> • Small entities have limited budgets and noted high costs to comply with the requirements of the Standards, e.g. appointing experts and consultants. • Entities do not have funds to train or upskill staff.
Daily and monthly controls	<ul style="list-style-type: none"> • Regular controls are not in place, leading to unreliable financial information. • Record keeping is lacking, and asset management is a challenge. • Accounting software is a challenge as limited GRAP compliant software is available. The software available is costly and does not support small entities to streamline the software for their limited needs.
Use of consultants	<ul style="list-style-type: none"> • There is overreliance on consultants. • Skills are not transferred as small entities have capacity constraints.
Broader compliance	<p>The issues go beyond preparing financial statements and include an inability to comply with broader legislative requirements.</p>
Existence of entities	<p>The establishment of seemingly unnecessary entities is a challenge. Some small entities should not exist as separate legal entities.</p>



Appendix D

LEGISLATION AFFECTING THE FINANCIAL REPORTING ENVIRONMENT

The following legislation was identified that impact on the financial reporting environment of small entities.

Legislation	Requirement
PFMA, MFMA and similar legislation	<p>All entities subject to the acts are required to prepare financial statements in accordance with generally recognised accounting practice, where the Board has so determined.</p> <p>The acts define “generally recognised accounting practice” as an accounting practice complying in material respects with standards issued by the Board. Both acts also require all entities subject to the acts to prepare financial statements in accordance with a “fair presentation” framework³.</p> <p>Similar legislation applicable to entities not subject to the PFMA or MFMA require preparation of financial statements in accordance with a “fair presentation” framework, “standards of generally recognised accounting practice”, or “Standards of GRAP”. For example, legislation applicable to traditional authorities and the Government Gazette issued by the Minister of Higher Education and Training for TVET and CET colleges.</p>
Section 216(1) of the Constitution	The section requires uniform expenditure classifications and uniform treasury norms and standards.
PAA	The PAA was recently amended to remove the requirement for the auditor to express a “fairly present” audit opinion on the financial statements of all entities. For those entities where the AGSA decides in future to not express a “fairly present” audit opinion, financial statements could be prepared on a fair presentation or compliance framework.
AGSA Directive	The AGSA Directive, issued in terms of the PAA, requires that the financial statements of an “auditee” (as defined in the PAA), that is not subject to the PFMA, the MFMA or any other legislation that is prescriptive in respect of the financial statements, must be prepared in accordance with Standards of GRAP.

³ The ISA glossary defines a general purpose framework, which could be a fair presentation or compliance framework. The terms *fair presentation framework* and *compliance framework* are also defined in the ISA glossary.

LIST OF ABBREVIATIONS

Abbreviation	Meaning
AGSA	Auditor-General South Africa
ARD	Audit Research and Development unit
ASISA	Association for Savings and Investments
BASA	Banking Association South Africa
Board	Accounting Standards Board
CET college	Community Education and Training college
COGTA	Department of Cooperative Governance and Traditional Affairs
Companies Act	Companies Act, Act No. 71 of 2008
Constitution	Constitution of the Republic of South Africa, 1996
DHET	Department of Higher Education and Training
FRS	Financial Reporting Standard
FRSC	Financial Reporting Standards Council
IAASB	International Auditing and Assurance Standards Board
IASB®	International Accounting Standards Board
IFRS®	International Financial Reporting Standards
IFRS for SMEs®	IFRS for Small and Medium-sized Entities
IRBA	Independent Regulatory Board for Auditors
ISAs	International Standards on Auditing
MCS	Modified Cash Standard
MFMA	Municipal Financial Management Act, Act No. 56 of 2003
Municipal Systems Act	Municipal Systems Act, Act No. 32 of 2000
National Small Enterprise Act	National Small Enterprise Act, Act No. 102 of 1996
OAG	Office of the Accountant-General
PAA	Public Audit Act, Act No. 25 of 2004
PFMA	Public Finance Management Act, Act No. 1 of 1999
PSAF	Public Sector Accounting Forum
SAICA	South African Institute of Chartered Accountants
SALGA	South African Local Government Association
SARB	South African Reserve Bank



SARS	South African Revenue Service
TVET college	Technical and Vocational Education and Training college