Accounting Standards Board

Newsletter August 2021 Edition

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In this edition of the newsletter:

- Join our events
- New IPSAS 17? What may change?
- How can you improve your cash flow statement?
- What are financial instruments?
- Join the September IPSASB meeting

Join our events

We are hosting a series of events to discuss the recent Exposure Drafts issued by the IPSASB. We will host an education session and roundtable discussions for the Exposure Drafts. In the education session we will work through the proposals in the Exposure Draft and answer your questions. In the roundtable discussions you will be given an opportunity to share your comments, concerns and provide any other feedback on the IPSASB's proposals. The feedback received at the roundtable discussions will be used to formulate a comment letter which will be submitted to the IPSASB.

We look forward to your participation in our events.

Topic	Date	Time
Education session on IPSASB's Exposure Drafts on *Measurement* (ED 188 and ED 189) https://www.asb.co.za/comment-on-proposals/	6th of August 2021	09:00 to 11:30
E-mail tsholot@asb.co.za to join the discussion.		
Education session on IPSASB's Exposure Draft on revisions to IPSAS 17 on *Property, Plant and Equipment* (ED 190) https://www.asb.co.za/comment-on-proposals/	20th of August 2021	09:00 to 11:00
E-mail elizna@asb.co.za to join the discussion.		
Roundtable discussion on IPSASB's Exposure Drafts on *Measurement* (ED 188 and ED 189) https://www.asb.co.za/comment-on-proposals/	1 September 2021	09:00 to 12:00
E-mail tsholot@asb.co.za to join the discussion.		

Roundtable discussion on IPSASB's Exposure Draft on revisions to IPSAS 17 on *Property, Plant and Equipment* (ED 190) https://www.asb.co.za/comment-on-proposals/	15 September 2021	09:00 to 12:00
E-mail elizna@asb.co.za to join the discussion.		
Roundtable discussion on IPSASB's Exposure Draft on *Non-current Assets Held for Sale and Discontinued Operations* (ED 191) https://www.asb.co.za/comment-on-proposals/	22 September 2021	09:00 to 11:00
E-mail amandab@asb.co.za to join the discussion.		

New IPSAS 17? What may change?

The IPSASB published a revised IPSAS 17 on *Property, Plant and Equipment* for comment. The comment deadline is the 25th of October 2021. Given the proposed changes and the significance of property, plant and equipment in the public sector, it is critical that we provide our views to the IPSASB.

There are three key "themes" that resulted in changes being made to IPSAS 17:

- Changes in response to the proposed IPSAS on *Measurement.*
- The inclusion of heritage assets in the scope of IPSAS 17.
- Implementation guidance provided on infrastructure assets.

Changes in response to proposed IPSAS on *Measurement*

The most significant change is to the initial measurement of property, plant and equipment (PPE) acquired in a non-exchange transaction. Previously, non-exchange transactions were measured at fair value. The revisions to IPSAS 17 indicate that these transactions are measured at "deemed cost". Deemed cost is a current value measure and can be determined using three possible measurement techniques – market approach, income approach or cost approach. The ability to use three different techniques creates a greater range of potential valuation methods that could be used and would largely depend on the information available.

The options available for subsequent measurement are largely unchanged. Entities can still use cost or the revaluation model. The revaluation model allows the use of fair value and "current operational value". Additional disclosure is required when a current value measurement basis is used.

Inclusion of heritage assets in the scope of IPSAS 17

The IPSASB decided that there is no need for separate guidance on heritage assets. Heritage assets meet the definition of PPE and should be accounted for using IPSAS 17. As heritage assets are held indefinitely by entities for current and future generations, and are preserved to ensure their longevity, changes are proposed to accommodate their measurement.

A key change relates to depreciation. There is now a rebuttable presumption that items of PPE, other than land, can have finite useful lives. This means that entities could identify items of PPE (other than land) – for example, heritage assets – that have indefinite useful lives and need not be depreciated. However, because the rebuttable presumption is not limited to heritage assets, it could arguably apply to other assets. This could result in misuse/abuse of this principle.

The next change relates to the inclusion of disclosure requirements for heritage assets that is not recognised in the financial statements because a value could not be determined on initial measurement.

Entities should disclose:

(a) the difficulties in obtaining a reliable measurement; and

(b) the significance of the unrecognised asset(s) in relation to delivery of the entity's objectives.

Subsequent expenditure incurred on those unrecognised assets can be capitalised when the recognition criteria are met. Specific disclosure requirements apply in these instances.

Implementation guidance on infrastructure assets

Non-authoritative examples describing a range of issues relating to infrastructure assets are included in an appendix to IPSAS 17.

Read more

Access the full Exposure Draft and educational materials by following this link.

Have your say

We are hosting an education session on the 20th of August and a roundtable discussion on the 15th of September. To join these discussions, please contact Elizna van der Westhuizen at elizna@asb.co.za.

How can you improve your cash flow statement?

The cash flow statement is an integral part of an entity's annual financial statements. This statement enables users to understand how cash was raised to fund activities, on which items the cash was spent, and what cash and cash equivalents flowed to and from an entity during a particular reporting period.

The Accounting Standards Board (the ASB) recently undertook a review of cash flow statements presented in the financial statements. The objective of the review was to assess compliance with the requirements in the Standard of GRAP on *Cash Flow Statements* (GRAP 2), and to identify practices that entities apply when they prepare their cash flow statements. The results of this review are published in a Research Paper that is available on the ASB's website.

The cash flow statements need improvement

From the review, it was noted that the quality of the presentation and compilation of the cash flow statement needs improvement. Systemic issues have been identified that should be addressed to ensure that the quality of reporting is enhanced. These include:

- Insufficient time is allocated to prepare the cash flow statement – The cash flow statement is often the last component of the financial statements that is prepared before submission to the auditors for audit. It is challenging to complete the cash flow statement if insufficient resources are allocated to ensure the accurate and timely preparation of this statement.

- Lack of skill, capacity, and inadequate controls – A lack of skill and capacity within entities often leads to unnecessary mistakes in the preparation of the cash flow statement. The lack of adequate internal management processes and insufficient controls to ensure the accurate preparation may also contribute to unnecessary errors and/or mathematical mistakes.

- Not understanding the nature of an entity's activities – When preparers do not fully understand the nature of the entity's activities, often not all the items that need to be adjusted for in the cash flow statement, are adjusted. Adjustments could also be made incorrectly.

- Over reliance on software programs and templates – When preparers rely on software programs and templates, without adequately reviewing the outputs, not all the appropriate adjustments are made when the cash flow statement is prepared.

- Uncertainty about the role of materiality – Entities do not consider a different materiality when they prepare the components of the financial statements, and/or present specific line items in the financial statements.

  Preparers should familiarise themselves with the role that materiality plays when preparing the cash flow statement.

What can be improved?

The review of GRAP 2 identified common areas of non-compliance, such as:

- Not presenting certain items separately on the face of the cash flow statement – GRAP 2 requires certain items to be separately presented on the face of the cash flow statement. These include interest received, finance costs, taxation paid, and cash dividends received and paid. Entities often omit these items from the face of the cash flow statement.
- Separate presentation of non-cash adjustments and movements in working capital – In presenting the reconciliation of the surplus or deficit with the net cash flows from operating activities (the reconciliation), entities need to separate the adjustment for non-cash items from movements in working capital. If these components are not separated in the reconciliation, users will find it difficult to understand the nature of the adjustments presented in the reconciliation and may not be able to link the information back to the information presented elsewhere in the financial statements.
- Incorrect presentation of items in the cash flow statement – Entities incorrectly present movements in provisions, for example, leave pay, accrued leave, long-term service, performance bonuses, etc. as movements in working capital when in fact these movements consist of both cash and non-cash items.
- Incorrect classification of items in the cash flow statement – Some entities are uncertain about the treatment of some cash flow items, such as revenue received from insurance claims to cover losses and damages to assets. Revenue received from these claims should be reflected as investing activities as it represents a disposal of property, plant and equipment that was insured. Instead, some entities incorrectly reflect the revenue as a cash flow from an operating activity.

  Another incorrect classification is the presentation of increases and decreases in short term borrowings or loans. Some entities reflect these movements incorrectly as movements in working capital when it should be presented as movements in cash flows from financing activities. The movements in short term borrowings or loans should be treated similarly to increases or decreases in long term borrowings or loans.
- Adjusting for amounts in the reconciliation that are not presented in the financial statements, or that differ from amounts presented elsewhere in the financial statements – Amounts presented in the cash flow statement differ from amounts presented elsewhere in the financial statements. For example, adjustments for interest received and finance costs are included in the reconciliation as per the statement of financial performance, but with only some of the interest or finance costs presented as an operating, investing, or financing activity on the face of the cash flow statement. In other instances, the interest received, and finance costs are adjusted in the reconciliation, but the amounts adjusted differ from the amounts presented in the statement of financial performance or the notes to the financial statements.

  Reasons for these differences could be due to interest receivable or finance costs payable, differences between the effective and contractual interest rates applied or because interest could be capitalised to assets. However, without an explanation as to why these differences exist, users will not be able to understand the differences to make informed decisions.

Guidance to help entities prepare the cash flow statement

The National Treasury issued the Accounting Guideline on GRAP 2 on *Cash Flow Statements* that includes practical guidance and illustrative examples that entities can apply when preparing the cash flow statement.

Reference can also be made to the Frequently Asked Question 3.5 issued by the Secretariat of the ASB that explains what items should be included as 'cash and cash equivalents' (see FAQs on Standards of GRAP).

What are financial instruments?

Preparers often misclassify assets and liabilities as financial instruments. There are three basic points to consider in deciding whether you have a financial instrument or not…

- The arrangement is contractual rather than statutory.
- One party to the transaction has a financial asset, and the other party to the transaction has either a financial liability or a residual interest (‘equity’).
- The transaction is settled in cash or another financial instrument.

By applying these three basic points to arrangements, preparers will be able to analyse transactions and conclude whether they are contractual or statutory.

Contractual versus statutory arrangements

Assets and liabilities are accounted for differently depending on whether they are contractual or statutory. The table outlines the key differences:

Contractual arrangements	Statutory arrangements
Governed by law of contracts.	Governed by legislation, regulation, or similar means.
Willing parties to the transaction.	Compulsory transaction.
Rights and obligations for parties to the arrangement. The rights and obligations need not be equal.	Same as contractual arrangements.
Rights and obligations are enforceable.	Same as contractual arrangements.

Financial asset, financial liability, or residual interest

For a financial instrument to exist, one party to the arrangement has a financial asset, and the other party has a financial liability or a residual interest.

Typical examples include the following:

- An entity sells goods on credit. In this instance the entity selling the goods has a financial asset, while the party receiving the goods has a financial liability to pay for the goods received.
- An entity receives goods on credit. In this instance, the entity receiving the goods has a financial liability and the other party has a financial asset to receive payment.
- An entity (investor) invests in the ordinary shares of another entity. The shares are a residual interest as they entitle the investor to a portion of the investee’s net assets. The investor has a financial asset, and the investee has transferred a residual interest in the entity to the investor.

Settled in cash

Because of the requirement to have a financial asset in one entity and a financial liability or residual interest in another, financial instruments are settled in cash. Transactions or balances that are settled through the provision of goods or services are not financial liabilities. To illustrate: Prepaid insurance will be settled through the provision of insurance services rather than through the return of cash.

Find guidance on financial instruments

In response to the changes to GRAP 104, the Secretariat issued Fact Sheets to assist entities to apply the changes.

One of the Fact Sheets deals with applying the definition of financial instruments. As the definition between the old and the new versions of GRAP 104 is unchanged, the Fact Sheet can be applied regardless of the version of GRAP 104 being applied.

Access the Fact Sheet here.

Join the September IPSASB meeting

The IPSASB will be hosting its September meeting virtually. As the IPSASB meetings continue to be held virtually, it is a fantastic opportunity to hear the debates and deliberations firsthand.

The meeting will be held on multiple days in the 3rd and 4th weeks of September from 13:00 to 16:00 to accommodate the time differences in jurisdictions.

To get more information and register, follow this link.

Contact us
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