GRAP 104 on *Financial Instruments* (Revised)

Your guide to understanding and applying the revised Standard

This article is part of a series of articles that discuss the key amendments to GRAP 104 (revised). GRAP 104 is the authoritative source. Other supplementary resources are intended to be read alongside GRAP 104 and do not replace or override its guidance. The article has been prepared by the Secretariat of the ASB for information purposes only. It has not been reviewed, approved, or otherwise acted on by the Board.

Accounting for payables under GRAP 104 (2019)

When an entity receives goods or service on credit, a payable arises. A payable meets the definition of a financial instrument in GRAP 104 on *Financial Instruments* when an entity becomes a party to a contractual obligation of the instrument. This will be, for example, when an entity has a contractual obligation to pay cash for materials or consumables already received that are unpaid at year-end. A payable can arise from an exchange or non-exchange transaction.

A contractual obligation that requires the outflow of economic benefits associated with the delivery of goods or services rather than a contractual obligation to pay cash, or a payable that arises from legislation or similar means are not financial liabilities. These liabilities are accounted for using GRAP 19 on *Provisions, Contingent Liabilities and Contingent Assets*, another Standard of GRAP or the *Conceptual Framework for General Purpose Financial Reporting*.

Classification of payables

The classification of a payable determines how the payable will subsequently be measured. A payable is classified at amortised cost unless:

(a) the payable qualifies to be measured at fair value through surplus or deficit, for example a derivative; or

(b) the payable relates to a financial liability that arises because the entity has retained substantially all the risks and rewards of ownership of a transferred asset for which consideration was received. In subsequent periods, the revenue on the transferred asset, and any expenses incurred on the financial liability are separately recognised.

Measurement of payables

A payable that is subsequently measured at amortised cost is initially measured at the fair value of the consideration received minus any transaction costs that are directly attributable to the financial liability.

The fair value on initial recognition is the transaction price, unless the terms of the arrangement are not market related. This will be, for example, where goods and services are received interest-free, or a below-market rate of interest is charged for the initial credit period granted (i.e. the period between the transaction date and the due date for payment). If the fair value of a payable is affected by off-market elements, the contractual interest rate is compared to an interest rate for a similar instrument with similar risk characteristics and the same maturity. The government bond rate of an instrument with the same maturity and risk profile can be used to determine a market-related rate of interest for debts owed to government entities.

If the initial credit period is not in line with a period granted consistent with terms used in the public sector, either through established practice or specific legislation, the effect of discounting is considered, if material. This means that the initial transaction should be separated between expenses and interest.

For subsequent measurement, amortised cost is the amount at which the payable is initially recognised adjusted for principal repayments and cumulative amortisation. Cumulative amortisation is calculated as the difference between the initial amount and the maturity amount, using the effective interest rate.

When will a payable be derecognised?

A payable will be removed from an entity's statement of financial position when the financial liability is extinguished. This will be when the liability is:

(a) settled, i.e. the creditor or supplier is paid (in full or in part);

(b) expires through law, or because it is cancelled; or

(c) waived, as the debt is assumed by another entity through a non-exchange transaction. These transactions are accounted for using GRAP 23 on *Revenue from Non-exchange Transactions (Taxes and Transfers).*

When the terms of an existing payable, or part thereof, are substantially modified or re-negotiated, the original liability is derecognised and a new payable is recognised. This will be when the revised terms are such that the discounted present value of the cash flows under the new terms, discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original payable. An example will be where short-term debt is converted into long-term debt. Any gain or loss that arises from the derecognition of a financial liability is recognised in surplus or deficit.

The GRAP 104 Fact-sheet on Payables is available to further explain the GRAP 104 requirements to payables.