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**MINUTES OF THE PROJECT GROUP MEETING OF THE ACCOUNTING STANDARDS BOARD ON THE PROPOSED RESPONSES TO ED 200 *POST-IMPLEMENTATION REVIEW OF GRAP 109 ACCOUNTING BY PRINCIPALS AND AGENTS* HELD ON 30 JANUARY 2024**

<b>Present:</b>	S Abraham	SARS
	R Alberts	Swartland Municipality
	R Bester	Wesgro
	M Dullabh	National Treasury
	P Lekay	City of Cape Town
	A Matebese	Road Traffic Infringement Agency
	L Maseko	eThekwini Municipality
	N Ngaka	Municipal Finance Improvement Programme
	K Nteleko	eThekwini Municipality
	S Nzimande	Eastern Cape Provincial Treasury
	S Qumba	National Treasury
	M Ranzwa	Council for the Built Environment
	F Salie	Western Cape Provincial Treasury
	L Selane	SARS
	J van Wyk	Municipal Finance Improvement Programme
<b>Secretariat:</b>		
	A Botha	Project Manager
	E van der Westhuizen	Head of Technical

Board Members: Ms P Moalusi (Chair), Mr A van der Burgh (Deputy Chair), Mr C Braxton, Ms W de Jager, Mr D Dlamini, Mr S Khan, Ms A Muller, Ms N Themba  
Chief Executive Officer: Ms J Poggiolini

## **1. WELCOME AND APOLOGIES**

Members were WELCOMED to the project group meeting. Apologies were NOTED from E Breedt, N Imam-Shah, S Nondlazi, J Poggiolini, O Stadler, M Tabane and S Treeby.

## **2. ED 200 POST-IMPLEMENTATION REVIEW OF GRAP 109 ACCOUNTING BY PRINCIPALS AND AGENTS**

2.1 The Secretariat TABLED the following documents at the meeting:

- Memorandum from the Secretariat.
- Summary of proposed responses to comments on ED 200.
- Summary of verbal comment on ED 200.
- Summary of written comment on ED 200.

### **Background to the project**

2.2 The Secretariat NOTED the background to the project and the purpose of the meeting.

### **Overview of the consultation process**

2.3 The Secretariat EXPLAINED how it raised awareness of ED 200, and ASSERTED that all the stakeholders identified in the project brief had sufficient opportunity to participate in the due process.

### **Development of proposals**

2.4 The Secretariat EXPLAINED the process followed to develop proposed responses to the comment received on ED 200. It was NOTED that the criteria applied to determine appropriate responses will be incorporated in the Due Process Handbook/Procedure Manual.

### **Application of materiality**

- 2.5 The Secretariat EXPLAINED the issues identified related to the application of materiality, and the proposed actions to address the issues.
- 2.6 A member NOTED that materiality is particularly relevant when identifying principal-agent arrangements. Some view the nature of the arrangement to be qualitatively material, similar to how related party arrangements are viewed.
- 2.7 The project group SUPPORTED the proposals to include a project on materiality in the next ASB work programme consultation, and to clarify existing principles in an FAQ.

**Secretariat**

### **Identifying principal-agent arrangements**

- 2.8 The Secretariat EXPLAINED the issues related to the identification of principal-agent arrangements, and the proposed actions to address the issues.
- 2.9 A member NOTED that one provincial treasury reached an agreement with the AGSA whereby the provincial treasury assesses arrangements within the province against the definition of a principal-agent arrangement before the AGSA. This avoids unnecessary disagreements between auditors and preparers. Another member RAISED a concern with the assessment being done by the provincial treasury, as they are not a party to the

arrangement and it exposes the provincial treasury to risks if they misclassify arrangements. A further concern was NOTED that this agreement for the provincial treasury to assess the nature of arrangements may lead to other tasks being given to provincial treasuries that are outside their role and scope of work.

#### *Subcontracting arrangements*

- 2.10 A member ASKED for clarity on the Secretariat's view that issues with housing arrangements, INEP and RBIG grant arrangements relate to subcontracting arrangements. The Secretariat NOTED there are often multiple parties involved in these arrangements, including a service provider that is used as a subcontractor for part of the arrangements. The review identified that the mere use of a subcontractor leads to the conclusion that an arrangement is a principal-agent arrangement, while it does not necessarily meet all the elements of the definition in GRAP 109.
- 2.11 A member ASKED that GRAP 109 should not be amended to explicitly exclude subcontracting arrangements from the Standard. The Secretariat NOTED there is no proposal to amend the scope of GRAP 109. Rather, the OAG will be asked to consider providing guidance on subcontracting arrangements and GRAP 109.
- 2.12 Members SUPPORTED that the Guideline on *Accounting for Arrangements Undertaken in terms of the National Housing Programme* be reviewed alongside the amendments to GRAP 109 to ensure consistent application of the principles. Members also SUPPORTED the review of examples on housing arrangements in GRAP 109.

**Secretariat**

#### *Level of assessment*

- 2.13 Members CONFIRMED there is confusion about the nature of arrangements where an entity has a certain designation/licence/accreditation etc. It is also difficult to assess an arrangement within a control relationship where a controlled entity performs a service on behalf of the controlling entity. This can be particularly difficult when the arrangement is not in writing. The Secretariat EXPLAINED the proposal to provide guidance on assessing the rights and obligations of each arrangement, irrespective of an entity's designation/licence/accreditation, etc or relationships such as a control relationship. Separate guidance will be provided on assessing whether an arrangement that is not in writing is a binding arrangement.

#### *Applying substance over form to the definition of a principal-agent arrangement*

- 2.14 A member NOTED that the assessment of substance over form often considers practice. The Secretariat EXPLAINED the proposed guidance on substance over form will clarify that the assessment considers the rights and obligations of the arrangement over the legal form of the arrangement. It does not mean considering practice over the terms and conditions of the arrangement.
- 2.15 Some members REQUESTED that the definition of a principal-agent arrangement be amended to require that the agent should be authorised to legally bind the principal in a transaction with third parties. Members NOTED the following in support of this proposal:
- A court ruling required representation by the agent of the principal for it to be a principal-agent arrangement. The ruling referred to the agent being able to "create,

alter or discharge” legal relationships between the principal and third parties. This is also aligned to the VAT Act.

- Amendments to GRAP 109 should assist in reducing the effort and time spent on assessing whether an entity is an agent or an independent contractor in an arrangement. Adding this requirement enhances GRAP 109 without requiring legal interpretations.
- It may be easier to understand GRAP 109 if the relationship between the principal and third parties is explained in relation to the arrangement with the agent.

2.16 Further in support of the inclusion of this requirement, a member NOTED that any pronouncement issued by the ASB has legal force, meaning that GRAP 109 is also a legal document. This may confuse the issue of substance over form as applying GRAP 109 could be seen to mean applying legal form. Another member NOTED that although substance over form should be applied, it is unclear how the principle could apply when a court ruling binds the parties to a specific outcome.

2.17 In support of a principles-based approach, another member NOTED the importance of each entity assessing each arrangement separately, even when transactions and arrangements are seemingly similar within an entity and among entities. There is no “one size fits all” conclusion and each assessment should be based on the specific circumstances, which may differ from the legal interpretation.

2.18 The Secretariat NOTED that although it may be inappropriate to change the definition to align to a specific court ruling, the review considered legal definitions of principal-agent arrangements, e.g. the VAT Act, and found the principles to be aligned. As noted in the proposals to issue 8 in attachment 2, GRAP 109 already explains that there must be enforceable rights and obligations for the parties to the arrangement for it to be binding. To meet the definition of a principal-agent arrangement, the nature of the rights and obligations should be such that the "principal" instructs the "agent" to undertake transactions with third parties on behalf of and for the benefit of the principal. An arrangement is not a principal-agent arrangement if there is no specific direction given by the "principal" in relation to transactions with third parties. The Secretariat further NOTED the proposal to issue 4, which is to add clarity in GRAP 109 on the nature of the rights and obligations of the principal versus those of the agent. The Secretariat also NOTED that changes to GRAP 109 will follow a due process.

2.19 On balance, the project group RECOMMENDED the proposed actions to the Technical Committee for consideration, with the following further proposed actions:

- A member SUPPORTED involving all role players to resolve the issues with identifying principal-agent arrangements, in particular the OAG. The member NOTED that the misclassification of arrangements often starts with the budget process and grant allocation letters sent to entities by the National Treasury. These letters often prescribe a particular accounting treatment, which may not align with the entity’s own assessment of the nature of the arrangement. It was SUGGESTED that this be raised with the OAG.
- Add examples on arrangements that are not principal-agent arrangements.
- Replace the statement that whether a “fee” is paid to an agent is irrelevant in the assessment, with whether “consideration or similar” is paid.

**Disclosure of principal-agent arrangements in financial statements**

2.20 The Secretariat EXPLAINED the issues related to the information on principal-agent arrangements provided in the financial statements, and the proposed actions to address the issues.

2.21 A member NOTED that the issue of incomplete disclosure of significant judgements (as required by GRAP 1 on *Presentation of Financial Statements*) is broader than the judgements applied in GRAP 109. The issue also applies to, for example, classifying assets between property, plant and equipment and investment property and the application of materiality. Although the project group SUPPORTED the proposal to develop an FAQ that links the GRAP 1 requirement to GRAP 109, they RECOMMENDED that awareness about the GRAP 1 requirement should be raised more broadly.

**Secretariat**

2.22 The project group SUPPORTED the proposals related to the disclosure issues, specifically noting the proposal for the OAG to include illustrative disclosures in a GRAP Accounting Guideline on GRAP 109.

**Secretariat**

**Other issues**

2.23 The Secretariat EXPLAINED the other issues identified from the review and the proposed actions to address the issues.

2.24 The project group RECOMMENDED the proposals related to other issues to the Technical Committee for consideration, with the below additional specific comments.

**Secretariat**

*Binding arrangements*

2.25 Members NOTED where an arrangement is not in writing, it is difficult to identify the rights and obligations of the parties to the arrangement, and whether those are enforceable. The project group SUPPORTED the proposed actions and RECOMMENDED that the following additional actions be considered:

- Emphasize that rights and obligations of the parties must be enforceable for an arrangement to be a binding arrangement. This will assist with understanding when past practice gives rise to a binding arrangement.
- Remind entities that arrangements that are not in writing should be considered for GRAP 109 and substance over form should still be applied.
- Consider adding an example of when a binding arrangement is not in writing.

**Secretariat**

*Criteria to assess which party is the agent*

2.26 The project group RECOMMENDED that guidance from the OAG's presentation should be considered for inclusion in an Accounting Guideline on GRAP 109.

**Secretariat**

*Applying GRAP 109 with other Standards of GRAP*

2.27 A member ASKED whether the issue with applying GRAP 109 and GRAP 32 on *Service Concession Arrangements* to the same arrangement is the order in which the Standards are applied. The Secretariat NOTED that the order of applying the Standards as well as providing the disclosures required by both Standards about the same arrangement have been raised as issues.

*Disclosing cash flow information*

2.28 Members SUPPORTED the proposed actions, including that an FAQ will explain the options to provide cash flow information on the net or the gross basis. It was NOTED that many entities are unaware of the options, and unsure how to classify cash flows in the cash flow statement.

2.29 A member RAISED an issue on the classification of consumer deposits as either financing or operating activities. The Secretariat's FAQ explains the circumstances when the cash flows could be operating or financing activities, however the National Treasury's specimen financial statements only provides for classifying the cash flows as financing activities. The issue should be raised with the OAG.

**Secretariat**

**Next steps**

2.30 The Secretariat NOTED the next steps are the Technical Committee and Board will consider the proposed responses in February and March 2024 respectively.

**3. CLOSING REMARKS**

Project Group members were THANKED for their time to prepare for the meeting, and their participation and input during the meeting.

**Prepared by: E van der Westhuizen 6 February 2024**