



ACCOUNTING STANDARDS BOARD

INTERPRETATION OF THE STANDARDS OF GENERALLY RECOGNISED ACCOUNTING PRACTICE

ACCOUNTING FOR ADJUSTMENTS TO REVENUE (IGRAP 20)



IGRAP 20

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Introduction

This pronouncement is set out in paragraphs .01 to .20. All paragraphs in this pronouncement have equal authority. The status and authority of appendices are dealt with in the preamble to each appendix. This pronouncement should be read in the context of its objective, its basis for conclusions and/or the basis for conclusions of its international equivalent, if applicable, the *Preface to the Standards of GRAP* and the *Framework for the Preparation and Presentation of Financial Statements*¹.

Standards of GRAP and Interpretations of the Standards of GRAP should also be read in conjunction with any directives issued by the Board prescribing transitional provisions, as well as any regulations issued by the Minister of Finance regarding the effective dates of the Standards, published in the Government Gazette.

Directives should be read in conjunction with the applicable Standards of GRAP and Interpretations of the Standards of GRAP.

¹ In June 2017, the Board replaced the *Framework for the Preparation and Presentation of Financial Statements* with the *Conceptual Framework for General Purpose Financial Reporting*.

Interpretation of the Standards of GRAP on *Accounting for Adjustments to Revenue*

References

- GRAP 3 *Accounting Policies, Changes in Accounting Estimates and Errors*
- GRAP 9 *Revenue from Exchange Transactions*
- GRAP 19 *Provisions, Contingent Liabilities and Contingent Assets*
- GRAP 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)*
- GRAP 108 *Statutory Receivables*
- GRAP 109 *Accounting by Principals and Agents*
- IGRAP 1 *Applying the Probability Test on Initial Recognition of Revenue*

Background

- .01 In the public sector, there are a number of legislative and regulatory processes (hereafter referred to as “legislation or similar means”) that govern how entities levy, charge or calculate (hereafter referred to as “charge”) revenue.
- .02 Adjustments to revenue already recognised in terms of legislation or similar means arise from the completion of an internal review process within the entity, and/or the outcome of an external appeal or objection process undertaken in terms of legislation or similar means. Adjustments to revenue include any refunds that become payable as a result of the completion of a review, appeal or objection process.
- .03 The adjustments to revenue already recognised following the outcome of a review, appeal or objection process can either result in a change in an accounting estimate, or a correction of an error.

Scope

- .04 This Interpretation clarifies the accounting for adjustments to:
- (a) exchange and non-exchange revenue charged in terms of legislation or similar means; and
 - (b) interest and penalties that arise from revenue already recognised as a result of the completion of a review, appeal or objection process.
- Changes to the measurement of receivables and payables, other than those changes arising from applying this Interpretation, are dealt with in accordance with the applicable Standards of GRAP (also see paragraph .06(d)).

- .05 The principles in this Interpretation may be applied, by analogy, to the accounting for adjustments to exchange or non-exchange revenue that arises from contractual arrangements where the fact patterns are similar to those in paragraphs .07 and .08.
- .06 This Interpretation does not deal with the:
- (a) classification of the revenue as either exchange or non-exchange revenue (see the Standards of GRAP on *Revenue from Exchange Transactions* and *Revenue from Non-Exchange Transactions (Taxes and Transfers)*);
 - (b) application of the probability test on initial recognition and measurement of revenue (see the Interpretation of the Standards of GRAP on *Applying the Probability Test on Initial Recognition of Revenue*);
 - (c) assessment of whether the entity undertakes transactions as the principal or agent in a principal-agent arrangement (see the Standard of GRAP on *Accounting by Principals and Agents*); and
 - (d) changes to the measurement of receivables or payables, other than those changes arising from applying this Interpretation, following any adjustments to revenue already recognised (see the Standards of GRAP on *Statutory Receivables or Provisions, Contingent Liabilities and Contingent Assets*).

Issues

- .07 Some revenue is based on prescribed tariffs, bases, percentages or formulas that are promulgated in legislation or similar means after the completion of a due process.
- .08 Revenue charged can be appealed by the person or entity responsible for the payment of the revenue charged through the following processes:
- (a) an appeal or objection process established by the entity that charged the revenue;
 - (b) specific legislation or similar means that establishes an appeal and/or an objection process; and/or
 - (c) another legal process.
- .09 The entity that charges revenue can also apply its own internal review process to assess if the revenue was charged correctly in terms of the prescribed tariff, basis, percentage or formula as promulgated in legislation or similar means. This may result in the entity itself identifying that the revenue already recognised needs to be adjusted.
- .10 Following the outcome of the processes in paragraphs .07 to .09, this Interpretation addresses how revenue already recognised, including interest and penalties, is adjusted when:

- (a) a due process was not followed in promulgating the tariff, basis, percentage or formula that led to the charging of the revenue;
- (b) the tariff, basis, percentage or formula was incorrectly applied in charging revenue; and/or
- (c) an estimate may need revision as a result of changes in the circumstances on which the estimate was based, or as a result of new information that becomes known to the entity.

Consensus

General

- .11 In accordance with the Standard of GRAP on *Accounting Policies, Changes in Accounting Estimates and Errors* (GRAP 3), adjustments to revenue are either accounted for as a change in an accounting estimate, or a correction of an error.
- .12 GRAP 3 defines a change in an accounting estimate as “an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities”.
- .13 GRAP 3 defines a prior period error as “omissions from, and misstatements in, the entity’s financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:
 - (a) was available when financial statements for those periods were authorised for issue; and
 - (b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.
 Errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud”.
- .14 Determining whether an adjustment to revenue charged in terms of legislation or similar means is a correction of an error or a change in an accounting estimate requires the application of judgement by management. When adjustments to revenue already recognised arise from new information that becomes known to the entity, the following considerations may be applied to determine whether the adjustment to revenue already recognised is a correction of an error or a change in an accounting estimate:
 - (a) If information becomes known to the entity, and the entity could reasonably have been expected to know of the information and/or the information used was incorrect, the adjustment to revenue is likely to be a correction of an error.
 - (b) If information becomes known to the entity, but the entity could not reasonably have been expected to know of this information when the revenue was

charged, the adjustment to revenue is likely to be a change in an accounting estimate.

- .15 GRAP 3 clarifies that, as a result of uncertainties inherent in delivering services, conducting trading or other activities, many items in the financial statements cannot be measured with precision, but can only be estimated. The use of estimates is an essential part of the accrual basis of accounting, and estimation involves judgements based on the latest available information. The entity also needs to consider any additional facts and circumstances that may exist at the reporting date.

Accounting for adjustments to revenue that correct an error or prior period error

- .16 Following the outcome of the processes in paragraphs .07 to .09 and assessing whether this is new information that becomes known to the entity as noted in paragraph .14(a), an entity accounts for an adjustment to revenue already recognised, including interest and penalties, as the correction of an error or prior period error where the entity:
- (a) has not followed a proper due process to promulgate the tariff, basis, percentage or formula to charge the revenue; and/or
 - (b) incorrectly applied the tariff, basis, percentage or formula in charging revenue.
- .17 Errors discovered within the reporting period which relates to that period should be corrected before the financial statements are authorised for issue. The principles in GRAP 3 are applied to account for the adjustment to revenue already recognised as a result of the correction of a prior period error.

Accounting for adjustments to revenue as a change in an accounting estimate

- .18 Following the outcome of the processes in paragraphs .07 to .09 and assessing whether this is new information that becomes known to the entity as noted in paragraph .14(b), an entity accounts for any adjustment to revenue already recognised, including interest and penalties, as a change in an accounting estimate if changes occur in the circumstances that led to the recognition of the revenue.
- .19 The principles in GRAP 3 are applied to account for a change in an accounting estimate.

Effective date

- .20 ***An entity shall apply this Interpretation prospectively for annual financial statements covering periods beginning on or after 1 April 2020. Earlier application is permitted.***

Appendix – Illustrative examples

This appendix is illustrative only and does not form part of this Interpretation. The purpose of this appendix is to illustrate the application of this Interpretation and to assist in clarifying its meaning.

Example 1 - Change in an accounting estimate following an adjustment to a property value as reflected in the valuation roll

Municipality A levies property taxes on property owner X based on the value reflected in its updated valuation roll.

The valuation roll was updated in the previous financial period after Municipality A compiled an analysis of property values in its area. The analysis was based on the physical inspection and valuation of each property. Municipality A's accounting policy indicates that it can use estimates to compile and update its valuation roll where it is unable to inspect and value a particular property.

In updating the valuation roll, Municipality A issued the roll as part of its public consultation process as required in legislation, allowing property owners the opportunity to object to the value of their property. During this consultation process, no objections were received from any resident. The updated valuation roll became effective on 1 July 20X0.

As part of its internal review process, Municipality A undertakes a physical inspection of properties that could not be accessed during the initial inspection process to ensure the accuracy of the property values. During this assessment, Municipality A concluded that the value of the property of owner X is understated as a result of additional developments on the property.

Following the outcome of the physical inspection, Municipality A needs to adjust the value of the property for owner X as the municipality concluded that the value of the property, as currently reflected in the valuation roll, is understated. The property tax that was charged to property owner X in the previous reporting period needs to be adjusted following the change in property value.

Municipality A appropriately applied its policy in updating its valuation roll, and followed the required due process prior to updating the valuation roll. The adjustment to revenue already recognised should therefore be accounted for as a change in an accounting estimate.

Example 2 - Accounting for an adjustment to revenue as a correction of an error or prior period error

Municipality A levies property rates on a municipal valuation roll that is effective for a period of four years. At the commencement of the current reporting period, Municipality A updated its municipal valuation roll. However, Municipality A neglected to publish the valuation roll in the Government Gazette for public inspection and comment.

After Municipality A followed its own internal review process, it concluded that the new values in the valuation roll cannot be used to levy property taxes as it did not follow the legislative due process. As a result, the difference between the property tax levied using the valuation roll that was not promulgated, and the property tax that should have been levied using Municipality A's existing valuation roll, is accounted for as a correction of an error, or a prior period error.

Example 3 - Accounting for an adjustment to revenue as a change in an accounting estimate

Municipality A issues Mr X with an infringement notice following a traffic violation. Mr X makes a representation to the Road Traffic Infringement Agency that appoints a representation officer to consider the representation made by Mr X.

The representation officer concludes that the infringement of Mr X should be reduced due to Mr X's personal circumstances, and that Mr X should not be held liable to pay the full fine.

Based on the outcome of the appeal by Mr X, Municipality A needs to account for the adjustment to revenue as a change in an accounting estimate as a result of the new information that became known.

The effect of the change in the accounting estimate is accounted for in the current period's surplus or deficit, even if Municipality A accounted for the traffic fine in a previous reporting period.

Example 4 - Accounting for an adjustment to revenue as a correction of an error

Assume the same fact pattern as in example 3, except that the representation officer concludes that Municipality A did not recalibrate the traffic camera that led to Mr X's traffic fine.

The representation officer concluded that Mr X's traffic fine should be voided as Municipality A did not comply with the legislative requirements in relation to the recalibration of traffic cameras.

As a result of the non-compliance with legislation, the adjustment to revenue already recognised, is accounted for as a correction of an error or prior period error by Municipality A.



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Example 5 - Consider whether an adjustment to revenue is a correction of an error or a change in an accounting estimate

A new taxpayer omits to include information on royalties in his/her tax return. As it is a new taxpayer with no historical information known to the South African Revenue Service (SARS), SARS could not have been reasonably expected to know that the taxpayer received income from royalties when revenue was initially charged.

When SARS adjusts the revenue already recognised to its administrative accounts following the subsequent submission of information by the taxpayer, the adjustment to revenue is accounted for as a change in an accounting estimate.

Basis for conclusions

The basis for conclusions gives the Accounting Standard Board's (the Board's) reasons for accepting or rejecting certain proposals to the accounting for adjustments to revenue. This basis for conclusions accompanies, but is not part of, this Interpretation.

Background

- BC1. A number of issues have been raised about whether adjustments to revenue should be treated as a change in an accounting estimate or as a correction of an error. Most of the issues were raised in the context of non-exchange revenue transactions such as property taxes, fines or levies charged in terms of legislation or similar means. As a result of legislation or similar means that governs the charging of these types of revenues, it is often unclear when circumstances give rise to a change in an accounting estimate or a correction of an error.
- BC2. Following the consultation on its 2017 to 2020 work programme, the Board agreed to develop a pronouncement to provide guidance on accounting for adjustments to exchange and non-exchange revenue already recognised.

Analysis of legislation or similar means

- BC3. An analysis of the applicable legislation that govern entities' ability to levy revenue were undertaken to consider:
- (a) how revenue is levied in terms of legislation or similar means. This includes revenue levied through by-laws or similar pronouncements, for example water and electricity tariffs;
 - (b) the appeal and objection processes, if any, that can be followed by a person or entity that is required to pay the revenue charged; and
 - (c) how, and under what circumstances, refunds are granted by the entity.
- BC4. The analysis highlighted that revenue is often levied on prescribed tariffs, bases, percentages or formulas that are promulgated in legislation or similar means after the completion of a due process, where after the tariff, basis, percentage or formula becomes effective.

Appeal and objection processes that can be followed

- BC5. The entity that charged the revenue will, in some instances, establish its own appeal or objection process that can be followed by the person or entity responsible for the payment of the revenue charged. Alternatively, the legislation or similar means that promulgated the revenue, can establish an appeal or objection process that can be followed to object to the revenue charged. Other legal processes also establish a general appeal process that can be followed in a court of law to appeal or object against the revenue charged.
- BC6. Some entities also establish their own internal review processes to assess if the

revenue was charged correctly in terms of the prescribed tariff, basis, percentage or formula.

- BC7. Following the outcome of these internal and/or external review processes, the revenue already recognised may need to be adjusted.

Basis for consensus

Changes in accounting estimates

- BC8. GRAP 3 defines changes in accounting estimates in relation to an adjustment to the carrying amount of an asset or liability, or the periodic consumption of the asset. Even though the definition focuses on assets and liabilities, the guidance on how to account for changes in accounting estimates, applies equally to changes in the revenue and expenses arising from the change in the measurement of the related asset or liability. The principles in GRAP 3 on accounting for changes in accounting estimates have therefore been applied in providing guidance on adjustments to revenue already recognised.

Adjustments to revenue

- BC9. From the analysis of the legislative requirements, the Board noted that the tariff, basis, percentage or formula that is used to charge revenue, only becomes effective after completion of the required legislative due process. The Board therefore concluded that, where the entity that charges revenue did not follow the required legislative due processes prior to charging the revenue, this results in non-compliance with the applicable legislation or similar means. As a result of the non-compliance, the revenue levied could be misstated in the financial statements. Similarly, where the entity charged revenue on an incorrect tariff, basis, percentage or formula, the Board concluded that this constitutes a correction of an error.
- BC10. The Board further concluded that where adjustments to revenue already recognised result from changes in the circumstances that led to the recognition of the revenue, or from new information that becomes available following the outcome of an internal review, and/or external appeal or objection process, the adjustment constitutes a change in an accounting estimate.
- BC11. Some stakeholders indicated that in practice, it may be difficult to distinguish between an error and a change in an accounting estimate. The Board agreed to make this distinction by explaining that:
- (a) an adjustment to revenue that results from new facts that become known to the entity, is likely to be accounted for as a change in an accounting estimate; and
 - (b) an adjustment to revenue is likely to be accounted for as a correction of an error when new facts become known to the entity that it could reasonably have been expected to know.

Respondents to the Exposure Draft supported the clarification included in the Interpretation.

- BC12. The Board noted that new information that becomes known to the entity and that could impact the revenue initially recognised includes, for example (a) information arising from assessing non-compliance with internal policies, that is likely to result in the correction of an error; and (b) new interpretations of legislation, that are likely to result in a change in an accounting estimate.

Application of the principles to revenue that arises from contractual arrangements

- BC13. During the consultation process, respondents questioned whether the guidance could also be applied to adjustments to revenue that arises from contractual arrangements. In debating this recommendation, the Board noted that, irrespective of how revenue is charged, i.e. through legislation or similar means or contractual arrangements, assessing whether an adjustment to the revenue already recognised is a correction of an error or a change in an accounting estimate in terms of GRAP 3, will remain the same.
- BC14. The Board concluded that, as the principles in this Interpretation explain the appropriate treatment of adjustments to revenue already recognised based on the principles in the GRAP 3, the guidance in the Interpretation can be applied to the adjustments to revenue that arise from contractual arrangements. An amendment has been made to indicate that the principles in the Interpretation may be applied, by analogy, in accounting for adjustments to revenue that arises from contractual arrangements where the fact patterns are similar to that in paragraphs .07 to .09. For revenue that arises from contractual arrangements, the Standard of GRAP on *Financial Instruments* is considered to account for changes to the measurement of receivables or payables following an adjustment to revenue already recognised.

Refunds

- BC15. The Board noted the uncertainties expressed by preparers on the appropriate treatment of refunds that become payable following the outcome of an internal review, and/or external appeal or objection process. The Board concluded that refunds are part of adjustments to revenue as a refund represents an overstatement of revenue already recognised. As information presented in the financial statements should faithfully represent the transactions or other events it purports, the Board concluded that a refund should not be accounted for as an expense.
- BC16. Adjustments to revenue already recognised results in changes in the measurement of the related receivables and payables. The Board agreed that this Interpretation will not provide guidance on the measurement of receivables or payables, other than those changes in measurement that arise as a result of adjustments to revenue already recognised.



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- BC17. The Board also agreed that the recognition of any new interest and penalties following the completion of a review, appeal or objection process, is not within the scope of this Interpretation.

Other considerations

- BC18. The Board noted that, in limited circumstances, accounting for adjustments to revenue can result in revenue reflected at a negative amount in the financial statements. The possible recognition of negative revenue is a consequence of applying the principles in GRAP 3. As a result, an entity can provide additional information to the users of the financial statements in terms of the Standard of GRAP on *Presentation of Financial Statements* to inform users of the effect of the adjustment to revenue already recognised.
- BC19. The Board considered the extent to which the principles on adjustments to revenue can be applied to the return of surpluses by public sector entities as currently required in legislation or similar means. The Board concluded that guidance on the return of surpluses is outside the scope of this Interpretation as the relevant guidance is provided by the National Treasury.