

Reference: T7/2/1

TREASURY CIRCULAR NO 38/2014

THE PREMIER

THE MINISTER OF AGRICULTURE AND RURAL DEVELOPMENT
THE MINISTER OF COMMUNITY SAFETY
THE MINISTER OF CULTURAL AFFAIRS AND SPORT
THE MINISTER OF EDUCATION
THE MINISTER OF FINANCE, ECONOMIC DEVELOPMENT AND TOURISM
THE MINISTER OF HEALTH
THE MINISTER OF HUMAN SETTLEMENTS
THE MINISTER OF LOCAL GOVERNMENT, ENVIRONMENTAL AFFAIRS AND DEVELOPMENT PLANNING
THE MINISTER OF SOCIAL DEVELOPMENT
THE MINISTER OF TRANSPORT AND PUBLIC WORKS

} For information

THE SPEAKER: PROVINCIAL PARLIAMENT
THE DEPUTY SPEAKER: PROVINCIAL PARLIAMENT

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ACCOUNTING STANDARDS BOARD (ASB) – INVITATION TO COMMENT ON DISCUSSION PAPER 9 ON MATERIALITY – REDUCING COMPLEXITY AND IMPROVING REPORTING (DP9) AND DISCUSSION PAPER 10 – ACCOUNTING FOR LIVING AND NON-LIVING RESOURCES (DP10).

Purpose

1. The purpose of this circular is to seek comment on the Discussion Paper on Materiality – Reducing Complexity and Improving Reporting (DP9) and Discussion Paper 10 – Accounting for Living and Non-living Resources (DP10) issued by the Accounting Standards Board.

Background

1. The objective of these discussion papers is firstly, in DP9, to create awareness amongst accounting professionals on the role of materiality in reducing complexity of, and

improving reporting in, the financial statements and then in DP10 to outline the ASB's research, and proposals on living and non-living resources, as no comprehensive guidance exists on the accounting for living and non-living resources in the Standards of GRAP.

2. During the Board's consultation on its differential reporting project, a number of constituents highlighted that one of the most significant challenges they experience in preparing their financial statements, is how to apply materiality. As a result, entities often apply the individual requirements of the Standards of GRAP to immaterial transactions, rather than focusing on what is material. This has led to unnecessary complexity being created in the application of the Standards, as well as providing users with information that distracts their focus from key issues.
3. Entities hold a wide range of resources that include living resources such as animals and plants, and non-living resources, such as water, land and minerals, oil and gas, and other non-regenerative natural resources. Some entities hold these living and non-living resources to meet their mandate, while others act as a custodian for the benefit of present and future generations. As a result, accounting for living and non-living resources potentially has a far-reaching effect on financial reporting in the public sector. Comments received on the Discussion Paper, Accounting for Living and Non-living Resources will be used to develop accounting principles for living and non-living resources.

Action required

4. The Accounting Standards Board welcomes any comments from preparers, users, auditors, standard-setters and other parties with an interest in public sector financial reporting.
5. It is required of respondents to express an opinion on whether the DPs, in general, is supported and supplements this opinion with detailed comments, whether supportive or critical on the principles in the DP's.

6. **Invitation to comment on specific matters** as set out in this Discussion Paper on Materiality – Reducing Complexity and Improving Reporting: Practice Guideline on Reporting Service Performance Information

Question for respondents # 1:

Entities frequently use boilerplate templates (illustrative financial statements, accounting policies and note disclosures), checklists or similar tools to prepare their financial statements. While using these tools may assist entities' to assess compliance with the Standards of GRAP or to comply with specific requirements (e.g. consolidation templates), they often do not produce information that is relevant to an entity's users in assessing how items, transactions and events are accounted for, and describing any facts and circumstances that influenced the financial position, financial performance and cash flows. Where these templates and tools are used, the financial statements need to be refined by preparers to ensure that the financial statements provide relevant information to users.

As a preparer, would you be able to make appropriate adjustments and refinements to these templates using the concepts outlined in this Discussion Paper?

If not, please provide an indication of what is required to support this?

Question for respondents # 2:

It is often regulators and government agencies that require specific information to be reported by entities within a particular sector. Do they have a role to play in reducing the volume of disclosures in the financial statements? If yes, how can this be achieved?

Question for respondents #3:

The Board and the Office of the Accountant-General (OAG) have considered whether more explicit guidance should be developed on the application of materiality by preparers.

(a) Should more explicit guidance be developed?

(b) In the discussion outlined above, a broad process has been outlined.

The process is broadly as follows:

1. Identify the entity's users.
2. Determine the information needs of those users.
3. Assess when information is material, based on its nature and/or size.

4. Determine materiality thresholds.

5. Apply materiality thresholds when:

(i) Developing accounting policies (do the specific requirements of a Standard of GRAP apply to an item, transaction or event).

(ii) Assessing what information should be disclosed and how it should be presented.

(iii) Assessing omissions, misstatements and errors.

Would it be feasible to use this as a basis for any further guidance on the application of materiality?

Question for respondents # 4:

The Materiality and Significance Framework issued by the National Treasury addresses materiality more broadly in the context of an entity's operations and what items, transactions or events would result in reporting to the Executive Authority and others rather than focusing on materiality in the context of financial reporting to external users. One of the shortcomings highlighted during the Board's engagement with constituents, is the perceived lack of guidance on the development of quantitative thresholds.

(a) Should the Board or the OAG develop specific thresholds?

(b) If yes, provide suggested bases and margins that should be used in developing these thresholds based on the nature and operations of your specific entity?

7. **Invitation to comment on specific matters** as set out in this Discussion Paper 10 – Accounting for Living and Non-living Resources.

Defining living and non-living resources

The following definitions are proposed:

Living resources are resources that comprise elements that undergo biological transformation.

Non-living resources are resources, other than living resources that occur naturally, and are not created or modified by humankind.

Issue 1:

Do you agree that, in considering the types of natural resources in the public sector, these resources should be categorised as either living resources or non-living resources?

If not, please propose an alternative along with your reasons for this suggestion?

Issue 2:

Do you agree with the proposed definitions in paragraph 2.10 for:

(a) Living resources, and

(b) Non-living resources?

If not, how would you define these terms?

Issue 3:

Do you agree with the Board's view that extracted minerals, oil and gas, and other non-regenerative natural resources do not meet the definition of non-living resources and that guidance is already available to account for this resource?

If not, please explain your response.

Issue 4:

Do you agree with the Board's view that un-extracted minerals, oil and gas, and other non-regenerative natural resources meet the definition of non-living resources?

If not, please explain your response.

Issue 5:

In applying the definition of a non-living resource to land, it can be concluded that where land has not been modified or transformed by humankind and occurs in its original state, it meets the definition of a non-living resource.

Do you agree with this conclusion?

If not, please explain your response.

Issue 6:

Do you agree with the Board's view that water resources that are found in its natural state meet the definition of non-living resources, and that an entity needs to apply judgement to determine at what point the resource will be changed, modified or transformed its natural condition?

If not, please explain your response.

Issue 7:

Do you agree with the Board's view that water that has been changed, modified or transformed from its original natural state do not meet the definition of non-living resources and that guidance is already available to account for it?

If not, please explain your response.

Issue 8:

Do you agree that the principles in existing Standards of GRAP can be applied in accounting for the following living resources:

(a) GRAP 12, where living resources are held for sale or distribution in the ordinary course of operations; and

(b) GRAP 27, where living resources meets the definition of agricultural activity and an entity is actively involved in managing the biological transformation of the resource?

If not, please explain your response.

Issue 9:

Do you agree that, depending on the purpose for which land is held, the principles in existing Standards of GRAP, i.e. GRAP 12, GRAP 16, GRAP 17 or GRAP 103, can be applied in accounting for land?

If not, please explain your response.

Issue 10:

Paragraphs 4.19 to 4.35 list indicators that an entity should consider in determining whether the living and non-living resource is controlled.

Do you agree with these indicators of control? If not, please provide reasons for your view.

Are there any other indicators that should be considered in determining whether control exists? If yes, please provide details of these indicators and explain why they should also be considered.

Issue 11:

Paragraph 4.44 concluded that animals used in delivering goods and/or services and living resources held for rehabilitation, research and education or similar means are likely

to meet the definition of an asset and should therefore be recognised in the financial statements if the recognition criteria are met.

Do you agree with this conclusion?

If not, please explain why you disagree.

Issue 12:

Paragraph 4.45 concluded that living resources held in natural forests and conservation areas are likely not to meet the definition of an asset and should therefore not be recognised in the financial statements.

Do you agree with this conclusion?

If not, please explain why you disagree.

Issue 13:

Paragraph 4.50 concluded that un-extracted minerals, oil and gas, and other non-regenerative natural resources are unlikely to meet the definition of an asset and should therefore not be recognised in the financial statements.

Do you agree with this conclusion?

If not, please explain why you disagree.

Issue 14:

Paragraph 4.53 concluded that water held in its natural state and/or condition before it is changed, modified or transformed by humankind, are unlikely to meet the definition of an asset and should therefore not be recognised in the financial statements.

Do you agree with this conclusion?

If not, please explain why you disagree.

Issue 15:

Do you agree that, to the extent that certain living resources, such as plants, and non-living resources, such as un-extracted minerals, oil and gas, and other non-regenerative natural resources or certain natural water resources are part of the land and cannot be physically separated from the land, these factors should be taken into account when the value of the land is determined, and that specific disclosure requirements about that should be provided to the users of the financial statements?

If you do not agree, please explain your response.

Issue 16:

Paragraphs 5.46 and 5.47 propose that the existing requirements in the Standards of GRAP should be applied to initially measure living resources, i.e.:

- (a) living resources acquired in an exchange transaction should initially be measured at cost; and
- (b) living resources acquired at no or for a nominal consideration, including those that reproduce should initially be measured at fair value.

Do you agree this proposal?

If not, please explain why you disagree.

Issue 17:

The Board is of the view that, in some instances, replacement cost, realisable value, present value and market value may be appropriate in determining a value for some living resources as explained in paragraphs 5.28 to 5.48. However, in determining the most appropriate measurement bases, management needs to apply judgement based on its unique circumstances.

Do you agree that with this proposal?

If not, please explain why you disagree.

Issue 18:

Do you agree that, when reliable information is unavailable on initial recognition to reliably measure and determine a fair value for a living resource, the entity should only be required to disclosure relevant and useful information about the living resources in its financial statements?

If you do not agree with this view, please explain your response.

Issue 19:

Paragraph 5.50 concluded that fair value is the most appropriate measurement basis for the subsequent measurement of living resources.

Do you agree with this view?

If not, please explain your response.

Issue 20:

In applying fair value as a subsequent measurement basis for living resources, do you agree that:

- (a) Fair value should be determined by market based evidence, or by reference to quoted prices in an active and liquid market?
- (b) If no evidence is available to determine the market value in an active and liquid market, fair value may be established by reference to:
 - The most significant transaction price, provided that there has not been a significant change in economic circumstances between the date of that transaction and the reporting date; or
 - Market prices for similar resources, with similar characteristics, held or used in similar circumstances, with adjustments to reflect any differences; or
 - Sector benchmarks?

If you do not agree with the above view, how do you propose fair value should be determined to subsequently measure living resources?

Issue 21:

In the absence of any alternative in determining fair value, and in the absence of any other appropriate measurement bases, do you agree that the entity should be required to only disclose relevant and useful information about its living resources in its financial statements?

If you do not agree with this view, please explain your response.

Issue 22:

Do you agree with the conclusion in paragraph 5.53 that the frequency of valuations for living resources should be determined based on changes in the resource's lifecycle.

If you do not agree, please explain your response.

Issue 23:

Do you agree with the conclusion in paragraph 5.54 that depreciation should not be considered in measuring a living resource?

If you do not agree, please explain your response.

Issue 24:

(a) Do you agree with the disclosure objectives listed in paragraph 6.5? In your view, are there any other objectives which users of financial statements may find useful?

(b) Do you believe that the proposed disclosures relating to living and non-living resources as outlined in paragraph 6.6 meet these disclosure objectives? Please provide details of any other further information that, in your view, users may find useful.

(c) Do you believe that the proposed disclosure requirements as outline in paragraphs 6.8 and 6.9 can be provided where living and non-living resources were recognised and measured in an entity's financial statements? Please provide details of any other further information that, in your view, should be disclosed.

8. The Accounting Standard Board (ASB) would welcome comments on all matters discussed in these discussion papers. Comments are most helpful if they indicate the specific paragraph or groups of paragraphs to which they relate, contain a clear rationale and where applicable, provide a suggestion for alternative wording.

9. Entities and departments should please forward their comments in writing using the **Annexures A and B provided**, to Aslam.Abrahams@westerncape.gov.za **by no later than 14 November 2014** in order to enable **Provincial Accounting Service** to consolidate and provide inputs to the **Accounting Standards Board** by **16 January 2015**.

10. Thank you for your co-operation.


SENIOR MANAGER: PROVINCIAL ACCOUNTING SERVICES AND COMPLIANCE

DATE: 3/10/2014

Annexure A: Template to comment on this Discussion Paper

Discussion Paper 9 on Materiality – Reducing Complexity and Improving Reporting		
Name of department or Entity:		
Respondent's name and surname:		
Designation:		
Contact no# and email address:		
Specific matter for comment	Comments	Suggestion (where relevant)

General comments:

Signature of respondent:

Date:

Annexure B: Template to comment on this Discussion Paper

Discussion Paper 10 – Accounting for Living and Non-living Resources		
Name of department or Entity:		
Respondent's name and surname:		
Designation:		
Contact no# and email address:		
Specific matter for comment	Comments	Suggestion (where relevant)

General comments:

Signature of respondent:

Date: