

ACCOUNTING GUIDELINE

GRAP 20

Related Party Disclosures



national treasury

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REPUBLIC OF SOUTH AFRICA



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Note that this document is not part of the GRAP standard. The GRAP takes precedence while this guideline is used mainly to provide further explanations on the concepts already in the GRAP.

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***Included an additional discussion on Constitutional Institutions (page 8), new guidance on interventions undertaken in terms of the Constitution (page 10) and further discussion on the disclosure requirements (page 15) – March 2021**

1. Introduction

This document provides guidance on the identification and disclosure of related party relationships and certain transactions with related parties.

The contents should be read in conjunction with GRAP 20.

For purposes of this guide, “entities” refer to the following bodies to which the standard of GRAP relate to, unless specifically stated otherwise:

- Public entities
- Constitutional institutions
- Municipalities and all other entities under their control
- Trading entities and government components applying the standards of GRAP
- Parliament and the provincial legislatures
- TVET and CET colleges

Explanation of images used in manual:

	Definition
	Take note
	Management process and decision making
	Example

2. Scope

GRAP 20 is applicable to all entities on the accrual basis of accounting in identifying and disclosing related party relationships, transactions and balances at year-end, including commitments.



Disclosure of certain related party relationships and related party transactions and the relationships underlying those transactions is necessary for accountability purposes and enables users to better understand the financial statements of the reporting entity because:

- Related party relationships can influence the way in which an entity operates with other entities in achieving its individual objectives, and the way in which it co-operates with other entities in achieving common or collective objectives;
- Related party relationships might expose an entity to risks or provide opportunities that would not have existed in the absence of the relationship;
- Related parties may enter into transactions that unrelated parties would not enter into, or may agree to transactions on different terms and conditions than those that would normally be available to unrelated parties. This occurs frequently in government departments and agencies where goods and services are transferred between departments at less than full cost recovery as a part of normal operating procedures consistent with the achievement of the objectives of the reporting entity and the government. Governments and individual public sector entities are expected to use resources efficiently, effectively and in the manner intended, and to deal with public monies with the highest levels of integrity. The existence of related party relationships means that one party can control or significantly influence the activities of another party. This provides the opportunity for transactions to occur on a basis that may advantage one party inappropriately at the expense of another.

3. Definition and Identification



Parties are considered to be related if one party has the ability to control (or jointly control) the other party or exercise significant influence over the other party, or vice versa, or an entity that is subject to common control, or joint control.

3.1 Identifying related party relationships

The definition of related parties includes entities owned by management personnel, close family members of such individuals or major shareholders (or equivalent) of the reporting entity. The definition of a related party also includes circumstances in which one party has the ability to exercise significant influence over the other party. In the public sector, an individual or entity may be given oversight responsibility for a reporting entity, which gives them significant influence, but not control, over the financial and operating decisions of the reporting entity. Entities under joint control are also considered to have significant influence.



As a minimum, the following are regarded as related parties of the reporting entity:

- A person or a close member of that person's family is related to the reporting entity if that person:
 - has control or joint control over the reporting entity;
 - has significant influence over the reporting entity; or
 - is a member of the management of the entity or its controlling entity.
- An entity is related to the reporting entity if any of the following conditions apply:
 - The entity is a member of the same economic entity;
 - One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of an economic entity of which the other entity is a member);
 - Both entities are joint ventures of the same third party;
 - One entity is a joint venture of a third entity and the other entity is an associate of the third entity;
 - The entity is a post-employment benefit plan for the benefit of employees of either the entity or an entity related to the entity. If the reporting entity is itself such a plan, the sponsoring employers are related to the entity;
 - The entity is controlled or jointly controlled by a related person; and
 - A person who has control or joint control over the reporting entity has significant influence over that entity or is a member of the management of that entity (or its controlling entity).

In identifying related party relationships, attention should be given to the substance of a relationship and not merely its legal form.



Where two entities have a member of management in common, it is necessary to consider the possibility, and to assess the likelihood, that this person would be able to affect the policies of both entities in their mutual dealings. However, the mere fact that two entities have a member of management in common does not necessarily create a related party relationship.

The following other instances also do not necessarily create related party relationships:

- Two venturers merely because they share joint control over a joint venture;
- Providers of finance and trade unions;
- A customer, supplier, distributor or general agent with whom an entity transacts a significant volume of business, merely by virtue of the resulting economic dependence.

Other factors could, however, result in the parties being related.

3.2 Control



Control is the power to govern the financial and operating policies of another entity so as to benefit from its activities.

An entity (or a person or body of persons) has control over another entity when it has certain decision-making capabilities over another and that it benefits from the activities of that entity.

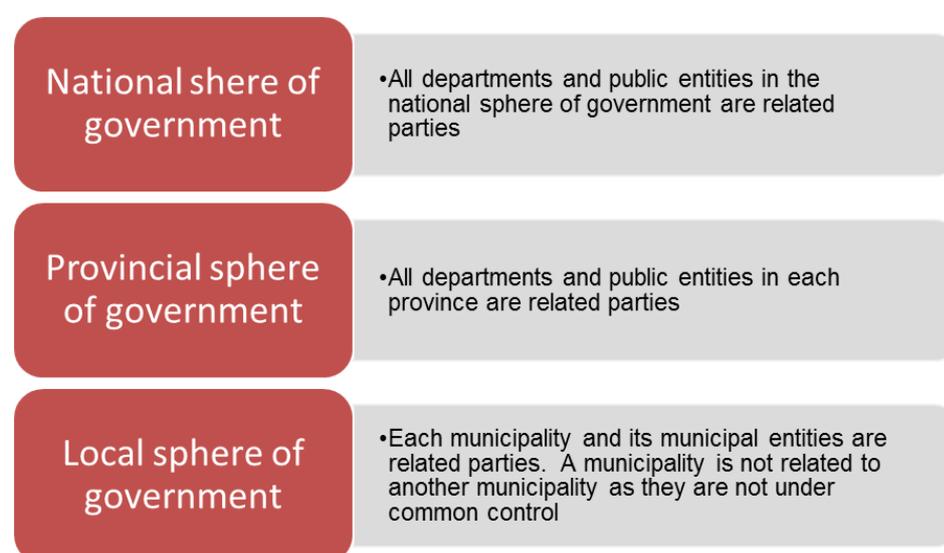


Further indicators that can also individually or collectively be indicative of control:

- The entity has the ability to veto operating and capital budgets of the other entity;
- The entity has the ability to veto, overrule, or modify the board of directors or equivalent governing body decisions of the other entity;
- The entity has the ability to approve the hiring, reassignment and removal of key personnel of the other entity;
- The mandate of the other entity is established and limited by legislation;
- The entity holds a “golden share” (or equivalent) in the other entity that confers rights to govern the financial and operating policies of that entity;
- The entity holds direct or indirect title to the net assets of the other entity;
- The entity has a right to a significant level of the net assets of the other entity in the event of a liquidation or in a distribution other than a liquidation;
- The entity is able to direct the other entity to co-operate with it in achieving its objectives;

In the South African context, the government is divided into three spheres, namely the national, provincial and local spheres of government. Although provinces and municipalities are responsible for executing its assigned functions in line with the overall policies and objectives set by the relevant national department, the autonomy of the different spheres is guaranteed in terms of the Constitution of South Africa and provinces and municipalities can therefore decide how it will achieve those objectives. The national government does not control provinces or municipalities for accounting purposes, although funding may be received from the national government.

The following figure illustrates the related parties in the South African government context (note that the different spheres of government are not related to each other):



**for the purpose of the above, public entities include Constitutional Institutions and trading entities. Departments include government components.*



Why are Constitutional Institutions related parties within the national sphere of government?

Even though section 181(2) of the Constitution provides that constitutional institutions are independent and subject only to the Constitution and the law, these institutions are accountable to the National Assembly (which forms part of Parliament). Similarly, national departments, national trading entities and national public entities are accountable to Parliament.

In addition, the National Assembly has the responsibility to:

- to ensure that all executive organs of state in the national sphere of government are accountable to it; and
- to maintain oversight of:
 - o the exercise of national executive authority, including the implementation of legislation; and
 - o any organ of state.

Section 239 of the Constitution defines an “organ of state” as:

- (a) any department of state or administration in the national, provincial or local sphere of government; or
- (b) any other functionary or institution:
 - (i) exercising a power or performing a function in terms of the Constitution or a provincial constitution; or
 - (ii) exercising a public power or performing a public function in terms of any legislation, but does not include a court or a judicial officer;

Therefore, the National Assembly has a Constitutional responsibility to:

- maintain oversight over both constitutional institutions and other national public sector entities (national departments, national trading entities and national public entities, etc.)
- hold both constitutional institutions and other national public sector entities to account

The National Assembly’s ability to govern over these organs of state results in them being regarded as related parties (i.e. seen as being under common control).



Example: Related parties within the relevant spheres of government

National sphere:

For example: Telkom, the Post Office, Transnet, the National Departments of Public Works and Trade and Industry, the Competition Commission and the Market Theatre will all be related parties, as they fall within the national sphere of government.

Provincial sphere:

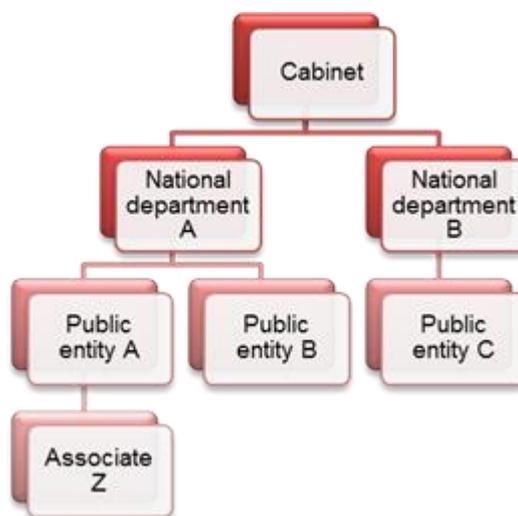
For example: The Gauteng Department of Health, Gauteng Economic Development Agency, Gauteng Gambling Board and the Gauteng Tourism Authority will all be related parties, as they fall within the same province. Note that these entities will be unrelated to any departments or public entities from another province.

Local sphere:

For example: The City of Johannesburg and its municipal entities are related parties. The City of Tshwane and the City of Johannesburg are not related parties as they are not under common control.



Example: Related parties in the national sphere of government



In this example:

- Public entity A, B, C, Associate Z and National departments A and B are related parties, as they are ultimately under common control.
- Department A has significant influence over Associate Z through its control over Public entity A.
- Public entity A controls Associate Z.

3.3 Interventions in terms of sections 100 or 139 of the Constitution

From time to time, an entity in one sphere of government may take temporary control of an entity in another sphere through legislation. During this period of temporary control, the entity under temporary control and the entity taking temporary control are related parties, provided the nature and extent of the intervention results in control; i.e. the entity taking temporary control governs or participates in the financing and operating policies of the entity under temporary control.

Where the legality of a section 100(1) or section 139(1) intervention is subject to legal proceedings or disputes, it will be necessary to obtain a legal view in order to determine:

- whether the intervention to place an entity under administration has been legally established; and
- the intervention period start- and end-dates.



Example: Temporary control

The NW provincial department of local government (an entity in the provincial sphere of government) has intervened in the administration of a municipality in the NW province (an entity in the municipal sphere of government) by invoking section 139(1) of the Constitution and taking control of the municipality's financing and operating policy decisions.

During this period of temporary control, the municipality (and any entities it controls) is a related party of all the organs of state within the NW provincial sphere of government, and the municipality is required to include the GRAP 20 related party disclosures in its financial statements from the date that it was placed under administration and until the end thereof. An example of the disclosure note is included below:

When organs of state are related parties for only part of a financial year, the GRAP 20 disclosures are only required for the period during which the organs of state are related. Where organs of state are related for part of a financial year, but are no longer related at the reporting date, the relevant GRAP 20 disclosures are still required for the period during which the organs of state were related.

This applies equally for organs of state that are related parties as a result of a section 110(1) or section 139(1) intervention.

3.4 Significant influence



Significant influence is the power to participate in the financial and operating policy decisions of an entity, but is not control over those policies.

Significant influence may be exercised in several ways, usually by representation on the board of directors or equivalent governing body but also by, for example, participation in the policy making process. Significant influence may be gained by an ownership interest, statute, or agreement.



Example: Significant influence

The national government owns 40% of the shareholding of a public company. The national government can therefore exert significant influence over the operations of the company, although it does not ultimately control the financial and operating decisions of the company.

The government and the public company are therefore related parties.

3.5 Management



Management are those persons responsible for planning, directing and controlling the activities of the entity, including those charged with the governance of the entity in accordance with legislation, in instances where they are required to perform such functions.

Management may include any sub-committees of the governing body or key advisors of a member of management as well as the senior management group of the entity (if not part of the governing body of the entity).

Management hold positions of responsibility within an entity. They are responsible for the strategic direction and operational management of an entity and are entrusted with significant authority. This responsibility may enable them to influence the decisions of the entity and therefore the benefits of office that may flow to them or their related parties.



Example: Management within the different spheres of government

In respect of an entity within the national or provincial spheres of government, the accounting officer or all the members (e.g. board members), and their close family relatives, are related parties of the entity.

In respect of a municipality, the accounting authority or all the members (e.g. major, speaker, council members), and their close family relatives, are related parties of the municipality.

The senior management team of entities across all spheres of government (including the chief executive or permanent head of the entity) also form part of management.

3.6 Close family members



Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity. A person is considered to be a close member of the family of another person if they:

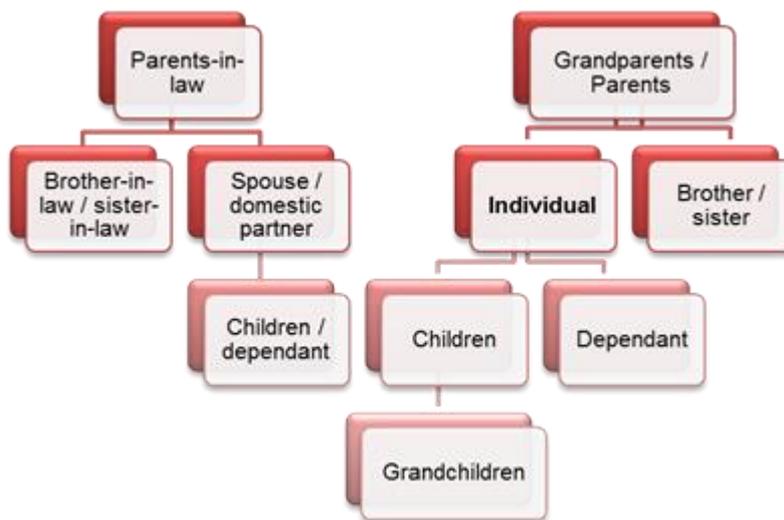
- are married or live together in a relationship similar to a marriage; or
- are separated by no more than two degrees of natural or legal consanguinity or affinity.

Close family members of management (and entities under significant influence of such individuals) are related parties of an entity.



The reason for the inclusion of close family members in the definition of a related party is to prevent entities from transacting with these individuals rather than with management in order to circumvent the disclosure requirements of the standard.

Judgement will be necessary in determining whether an individual should be identified as a close member of the family of an individual for purposes of related party disclosures. However, in the absence of information to the contrary, the following immediate family members and close relatives are presumed to have, or be subject to, such influence as to satisfy the definition of close members of the family of an individual:



4. Related Party Transactions



A related party transaction is a transfer of resources or obligations between related parties, regardless of whether a price is charged.

According to GRAP 20, an entity should disclose all transactions with its related parties other than transactions that would occur within [the disclosure exemption]:

- Normal supplier or client/recipient relationship on terms and conditions no more or less favourable than those which it is reasonable to expect the entity would have adopted if dealing with that individual entity or person in the same circumstances; and

- Terms and conditions within the normal operating parameters established by that reporting entity's legal mandate.



Example: Transaction with an entity under the control of a close family member of a member of management

The wife of the Chief Executive Officer of Public Entity A is the sole shareholder of Easyclean CC, which has been awarded a contract for the provision of cleaning services to Public Entity A. (Assume that the proper Supply Chain Management procedures were followed).

As Easyclean CC is under the control of a close family member of a key member of management, Easyclean CC and Public Entity A will be related parties. The nature of the relationship, all transactions with Easyclean CC and any other relevant information should be disclosed in the financial statements of Public Entity A.



Entities do not need to disclose the value of transactions where the transactions are concluded within normal operating procedures and on terms that are no more or no less favourable than the terms it would use to conclude transactions with another entity or person.

Therefore, public entities in the national sphere of government do not need to disclose the value of transactions with normal government service providers such as Telkom, the Post Office, the Unemployment Insurance Fund, etc., unless the transactions were on terms that are not ordinarily available to other entities or individuals, in which case the full disclosure required by GRAP 20 should be made.

However, where entities are exempt from the disclosure requirements, narrative information about the nature of the transactions and the related outstanding balances should be disclosed to enable the users of the financial statements to understand the effect of related party transactions on the entity's financial statements.



Example: Narrative disclosures where disclosure exemption applies

In the year ended 30 June 20X1 Municipality C provided Entity D, a municipal entity in which it has a 100% shareholding, with a loan equivalent to 50% of its funding requirements, repayable in quarterly instalments over the next five years. Interest is charged on the loan at a rate of 3%, which is comparable to that charged on Entity D's bank loans. At year-end, the outstanding loan balance was Rxxx.

Government owns 100% of Entity E's shares. Entity E's significant transactions with Government and other entities controlled, jointly controlled or significantly influenced by Government are [a large portion of its sales of goods and purchases of raw materials] or [about 50% of its sales of goods and about 35 % of its purchases of raw materials]. At 31 March 2010, the following amounts were owing to Entity E by other national public sector entities, which amounts are included in short-term receivables):

...

Entity B, a provincial public entity under the control of the WC provincial government, receives [substantially all] or [97%] of its funding via the WC Department of Environmental Affairs and Development Planning, from monies appropriated by the WC provincial government, as more fully set out in the WC Appropriation Act xx of 20X1. There were no amounts owing to or by entity B to the Department at year-end.

Related party transfers/ payments of appropriated funds, specific-purpose allocations, etc. would generally fall under the disclosure exemption in GRAP 20, as this is the manner in which government funds organs of state, and such transfers and allocations are therefore part of the normal supplier and/or client/ recipient relationships.



Example: Examples of transactions that may indicate a related party relationship

- Arrangements where one party incurs expenses on behalf of another party (these costs may or may not be recovered);
- Lease arrangements at more or less than market value or for no consideration;
- Sales without substance (funds are transferred to an entity for goods or services that were never rendered/delivered);
- Services or goods are purchased at nominal or no cost;
- Guarantees; and
- Finance arrangements (including loans, capital contributions, transfer payments in cash and in-kind).

5. Disclosure

It is important to understand and keep GRAP 20's objective in respect of related party disclosures in mind. The overall objective of GRAP 20 is to ensure that the entity's financial statements provide the disclosures necessary to draw users' attention to the possibility that the entity's financial position and financial performance may have been affected by the existence of related parties and by transactions and outstanding balances with such parties.

The aim of the disclosure exemption in GRAP 20 is to release an entity from the extensive related party disclosures for transactions that are unaffected by the related party relationship, and to ensure that transactions that are affected by the related party relationship are not obscured by excessive disclosures about unaffected transactions.

However, in order to meet the overall objective of GRAP 20, GRAP 20 still requires some disclosures even when the exemption applies. Those disclosures are intended to inform users that related party transactions have occurred and to provide an understanding of their nature and extent, as well as to give an indication of the related outstanding balances. The disclosures should focus on transactions that, in the context of the entity's specific facts and circumstances, are of more interest to users and are more likely to be affected by the related party relationship.

It will be necessary for the entity to use judgement to determine the nature and level of detail that it should disclose in its financial statements, also taking into consideration the principles

of materiality and aggregation in the GRAP Conceptual Framework, GRAP 1 on *Presentation of Financial Statements* and the GRAP Guideline on *The Application of Materiality to Financial Statements*.

The related party disclosures should speak to the specific entity's facts and circumstances; i.e. it should tell the entity's own story, and it may be relevant to consider factors in respect of both the related party relationship, as well as the underlying transactions and balances, to determine the related party disclosures. Such factors may for example include the following:

- the closeness of the related party relationship
- the materiality in terms of size and nature
- carried out on non market terms
- outside normal day to day operations
- disclosed to regulatory or supervisory authorities
- reported to senior management
- subject to external approval
- etc.

Generally, the more clearly significant the relationships, transactions and balances are to the entity, and/or the greater the likelihood that the transactions and balances were affected by the existence of the related party relationship, the greater the need for more detailed information.

In summary, an entity discloses the following in the notes to the financial statements:

- related party relationships where control exists, irrespective of whether there have been transactions between the related parties. This disclosure includes the name of its controlling party and if different, the ultimate controlling party.
- the nature of any related party relationships as well as required information about transactions and outstanding balances, including commitments, necessary for users to understand the potential effect of the relationship on the financial statements.
- the remuneration of management per person and in aggregate, for each class of management.



Disclosure of management remuneration

- An entity should disclose the remuneration of management per person and in aggregate, for each class of management, in the following categories:
- Fees for services as a member of management;
- Basic salary;
- Bonuses and performance related payments;
- Other short-term employee benefits;
- Post-employment benefits such as pensions, other retirement benefits, post-employment life insurance and post-employment medical care;
- Termination benefits;
- Other long-term benefits;
- Any commission, gain or surplus sharing arrangements; and
- Any other benefits received.

Entities shall make separate disclosures about the major classes of management that they have. For example, where an entity has a governing body, such as a board or a council, which is separate from its senior management group, disclosures about remuneration of the two groups must be made separately.

Where a person is a member of both the governing body and the senior management group, that person will be included in only one of those groups.

Remuneration of management excludes any consideration provided solely as a reimbursement for expenditure incurred by those persons for the benefit of the entity, such as subsistence or the reimbursement of accommodation costs associated with work-related travel.

Employees who meet the definition of key management personnel include those in an acting position, seconded and promoted, during the financial.

6. Useful links and references

Reference	Location of reference
Frequently Asked Questions (FAQs) on the Standards of GRAP	ASB website: http://www.asb.co.za/frequently-asked-questions/
Guideline on The Application of Materiality to Financial Statements	ASB website: http://www.asb.co.za/guidelines/
Standard Chart of Accounts for Local Government (mSCOA)	National Treasury website: http://mfma.treasury.gov.za (mSCOA – Municipal Standard Chart of Accounts)
Illustrative Financial Statements for local government	National Treasury website: http://mfma.treasury.gov.za (mSCOA – Municipal Standard Chart of Accounts)