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ACCOUNTING SUMMARY 2017 - 05

IAS 20 Accounting for Government Grants and Disclosure of Government Assistance

Objective

The objective of this Standard is to specify the accounting treatment and disclosure for government grants and other forms of government assistance.

Government assistance takes many forms varying both in the nature of the assistance given and in the conditions which are usually attached to it. The purpose of the assistance may be to encourage an entity to embark on a course of action which it would not normally have taken if the assistance was not provided.

The receipt of government assistance by an entity may be significant for the preparation of the financial statements for two reasons namely:

- if resources have been transferred, an appropriate method of accounting for the transfer must be found; and
- it is desirable to give an indication of the extent to which the entity has benefited from such assistance during the reporting period.

This facilitates comparison of an entity's financial statements with those of prior periods and with those of other entities.

Scope

This Standard shall be applied in accounting for, and in the disclosure of, government grants and in the disclosure of other forms of government assistance.

This Standard does not deal with:

(a) the special problems arising in accounting for government grants in financial statements reflecting the effects of changing prices or in supplementary information of a similar nature.

(b) government assistance that is provided for an entity in the form of benefits that are available in determining taxable profit or tax loss, or are determined or limited on the basis of income tax liability. Examples of such benefits are income tax holidays, investment tax credits, accelerated depreciation allowances and reduced income tax rates.

(c) government participation in the ownership of the entity.

(d) government grants covered by IAS 41 *Agriculture*.

Effective date

This Standard becomes operative for financial statements covering periods beginning on or after 1 January 1984.

An entity adopting the Standard for the first time shall:

(a) comply with the disclosure requirements, where appropriate; and

(b) either:

(i) adjust its financial statements for the change in accounting policy in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; or
(ii) apply the accounting provisions of the Standard only to grants or portions of grants becoming receivable or repayable after the effective date of the Standard.

Defined terms

Government refers to government, government agencies and similar bodies whether local, national or international.

Government assistance is action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under certain criteria. Government assistance for the purpose of this Standard does not include benefits provided only indirectly through action affecting general trading conditions, such as the provision of infrastructure in development areas or the imposition of trading constraints on competitors.

Government grants are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

Grants related to assets are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may also be attached restricting the type or location of the assets or the periods during which they are to be acquired or held.

Grants related to income are government grants other than those related to assets.

Forgivable loans are loans which the lender undertakes to waive repayment of under certain prescribed conditions.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Recognition of government grants

Government grants, including non-monetary grants at fair value

Government grants, including non-monetary grants at fair value, shall be recognised when there is reasonable assurance that:

(a) the entity will comply with the conditions attaching to them; and
(b) the grants will be received.

Forgivable loan from government

A forgivable loan from government is treated as a government grant when there is reasonable assurance that the entity will meet the terms for forgiveness of the loan.

Government loan at a below-market rate of interest

The benefit of a government loan at a below-market rate of interest is treated as a government grant. The loan shall be recognised and measured in accordance with IFRS 9 *Financial Instruments*. The benefit of the below-market rate of interest shall be measured as the difference between the initial carrying value of the loan and the proceeds received.

The benefit is accounted for in accordance with this Standard. The entity shall consider the conditions and obligations that have been, or must be, met when identifying the costs for which the benefit of the loan is intended to compensate.

Capital and Income approach

Government grants shall be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate.

There are two broad approaches to the accounting for government grants: the capital approach, under which a grant is recognised outside profit or loss, and the income approach, under which a grant is recognised in profit or loss over one or more periods.

Those in support of the **capital approach** argue as follows:	Arguments in support of the **income approach** are as follows:
(a) government grants are a financing device and should be dealt with as such in the statement of financial position rather than be recognised in profit or loss to offset the items of expense that they finance. Because no repayment is expected, such grants should be recognised outside profit or loss. (b) it is inappropriate to recognise government grants in profit or loss, because they are not earned but represent an incentive provided by government without related costs.	(a) because government grants are receipts from a source other than shareholders, they should not be recognised directly in equity but should be recognised in profit or loss in appropriate periods. (b) government grants are rarely gratuitous. The entity earns them through compliance with their conditions and meeting the envisaged obligations. They should therefore be recognised in profit or loss over the periods in which the entity recognises as expenses the related costs for which the grant is intended to compensate. (c) because income and other taxes are expenses, it is logical to deal also with government grants, which are an extension of fiscal policies, in profit or loss.

It is fundamental to the income approach that government grants should be recognised in profit or loss on a systematic basis over the periods in which the entity recognises, as expenses, the related costs for which the grant is intended to compensate.

Therefore:

- grants in recognition of specific expenses are recognised in profit or loss in the same period as the relevant expenses.
- grants related to depreciable assets are usually recognised in profit or loss over the periods and in the proportions in which depreciation expense on those assets is recognised.
- grants related to non-depreciable assets may also require the fulfilment of certain obligations and would then be recognised in profit or loss over the periods that bear the cost of meeting the obligations.

A government grant that becomes receivable:

- as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs, shall be recognised in profit or loss of the period in which it becomes receivable.
- for the purpose of giving immediate financial support to an entity rather than as an incentive to undertake specific expenditures may warrant recognising a grant in profit or loss of the period in which the entity qualifies to receive it, with disclosure to ensure that its effect is clearly understood.
- as compensation for expenses or losses incurred in a previous period, is recognised in profit or loss of the period in which it becomes receivable, with disclosure to ensure that its effect is clearly understood.

Non-monetary government grants

A government grant may take the form of a transfer of a non-monetary asset, such as land or other resources, for the use of the entity. In these circumstances, it is usual to assess the fair value of the non-monetary asset and to account for both grant and asset at that fair value. An alternative course that is sometimes followed is to record both asset and grant at a nominal amount.

Measurement of government grants

Presentation of grants related to assets

Government grants related to assets, including non-monetary grants at fair value, shall be presented in the statement of financial position either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.

The options available within this Standard are:

Option 1: Deferred income One method recognises the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.	Option 2: Against the carrying amount of the asset The other method deducts the grant in calculating the carrying amount of the asset. The grant is recognised in profit or loss over the life of a depreciable asset as a reduced depreciation expense.

Presentation of grants related to income

Grants related to income are presented as part of profit or loss, either separately or under a general heading such as ‘Other income’; alternatively, they are deducted in reporting the related expense.

Repayment of government grants

A government grant that becomes repayable shall be accounted for as a change in accounting estimate (see IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*).

Repayment of a grant related:

(a) to income shall be applied first against any unamortised deferred credit recognised in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or when no deferred credit exists, the repayment shall be recognised immediately in profit or loss.

(b) to an asset shall be recognised by increasing the carrying amount of the asset or reducing the deferred income balance by the amount repayable. The cumulative additional depreciation that would have been recognised in profit or loss to date in the absence of the grant shall be recognised immediately in profit or loss.

Government assistance

Excluded from the definition of government grants are certain forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

Examples of assistance that cannot reasonably have a value placed upon them are free technical or marketing advice and the provision of guarantees. An example of assistance that cannot be distinguished from the normal trading transactions of the entity is a government procurement policy that is responsible for a portion of the entity's sales. The existence of the benefit might be unquestioned but any attempt to segregate the trading activities from government assistance could well be arbitrary.

The significance of the benefit in the above examples may be such that disclosure of the nature, extent and duration of the assistance is necessary in order that the financial statements may not be misleading.

In this Standard, government assistance does not include the provision of infrastructure by improvement to the general transport and communication network and the supply of improved facilities such as irrigation or water reticulation which is available on an ongoing indeterminate basis for the benefit of an entire local community.

Presentation and disclosure

An entity shall present and disclose information that enables users of the financial statements to evaluate the financial effects of government grants and other forms of government assistance:

In the Statement of Financial Position:

(a) Presentation of grants related to assets
- (i) government grants related to assets, including non-monetary grants at fair value, shall be presented in the statement of financial position either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.

In the Statement of Comprehensive Income

(a) Presentation of grants related to income
- (i) grants related to income are presented as part of profit or loss, either separately or under a general heading such as 'Other income'; alternatively, they are deducted in reporting the related expense.

In the Statement of Cash Flows:

(a) The purchase of assets and the receipt of related grants can cause major movements in the cash flow of an entity. For this reason and in order to show the gross investment in assets, such movements are often disclosed as separate items in the statement of cash flows regardless of whether or not the grant is deducted from the related asset for presentation purposes in the statement of financial position.

In the Notes to the financial statement:

(a) The following matters shall be disclosed:
- (i) the accounting policy adopted for government grants, including the methods of presentation adopted in the financial statements;
- (ii) the nature and extent of government grants recognised in the financial statements and an indication of other forms of government assistance from which the entity has directly benefited; and
- (iii) unfulfilled conditions and other contingencies attaching to government assistance that has been recognised.