IAS 20 – Accounting for Government Grants and Disclosure of Government Assistance

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Examiner: Formation 2 Financial Accounting

This article provides information and application in relation to *IAS 20 – Accounting for Government Grants and Disclosure of Government Assistance*.

Government Grants – What are they?

Government grants per paragraph 3 of IAS 20 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.

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

Per paragraph 4, 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.

Government grants are sometimes called by other names such as subsidies, subventions, or premiums.

Government grants, including non-monetary grants at fair value shall not be recognised until there is a reasonable assurance that

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

Receipt of a grant does not of itself provide conclusive evidence that the conditions attaching to the grant have been or will be fulfilled. The manner in which a grant is received does not affect the accounting method to be adopted in regard to the grant. Thus a grant is accounted for in the same manner whether it is received in cash or as a reduction of a liability to the government.

Paragraph 12 of IAS 20 states that 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 i.e. if an asset is to be depreciated over ten years, then the government grant will be amortised to profit or loss over ten years as well.

Two approaches to accounting for Government Grants

1. Capital Approach
   This is where a grant is recognised outside profit or loss usually by crediting deferred income in liabilities; and

2. Income Approach
   This is where a grant is recognised in profit or loss over one or more periods usually as a credit to other income.

In most cases the periods over which an entity recognises the costs or expenses related to a government grant are readily ascertainable. Thus grants in recognition of specific expenses are recognised in profit or loss in the same period as the relevant expense. Similarly, 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 are sometimes received as part of a package of financial or fiscal aids to which a number of conditions are attached. In such cases, care is needed in identifying the conditions giving rise to costs and expenses which determine the periods over which the grant will be earned. It may be appropriate to allocate part of a grant on one basis and part on another.

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.

Presentation of Grants

Per paragraph 24, government grants related to grants, 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.

Two methods of presentation of government assets related to assets are permitted

a) Recognise the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.

b) 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.

Example of presentation of grants using both methods;

A grant of €100,000 was received. This grant related to the purchase of equipment costing €200,000 and which would be depreciated over ten years.

Method (a)

The asset would be capitalised as follows:

Dr.	Property, Plant & Equipment (PPE)	€200,000	
Cr.	Bank/Trade Payables		€200,000

Receipt of Grant

Dr.	Bank	€100,000	
Cr.	Deferred Income – Liabilities		€100,000

Depreciation of the asset

Dr.	Depreciation Expense	€20,000	
Cr.	Accumulated Depreciation (PPE)		€20,000

Amortisation of Grant

Dr.	Deferred Income	€10,000	
Cr.	Other Income		€10,000

Method (b)

The asset would be capitalised as follows:

Dr.	Property, Plant & Equipment (PPE)	€200,000	
Cr.	Bank/Trade Payables		€200,000

Receipt of Grant

Dr.	Bank	€100,000	
Cr.	Property, Plant & Equipment (PPE)		€100,000

Depreciation of the asset – (Cost €200,000 – Grant €100,000) / 10 years

Dr.	Depreciation Expense	€10,000	
Cr.	Accumulated Depreciation (PPE)		€10,000

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

A government grant per paragraph 32 that becomes repayable shall be accounted for as a change in accounting estimate. Repayment of a grant related to income shall be applied first against any unamortised deferred credit recognised in respect of the grant and then in profit or loss. Repayment of a grant related 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.

Disclosure

a) The accounting policy adopted for government grants, including the methods of presentation adopted in the financial statements;
b) 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
c) Unfulfilled conditions and other contingencies attaching to government assistance that has been recognised.

Example 1

Ramona Limited received a government grant of €60,000 in relation to the building of an extension to its buildings which cost €200,000 in total. Ramona Limited paid the net amount out of its bank account. Ramona Limited believe that the grant should be amortised over twenty years.

Required: Outline the journal entries in relation to the government grant.

Solution Example 1

			€	€
Dr. Bank	Current Assets	SOFP	60,000	
Cr. Government Grants	Non-Current Liabilities	SOFP		60,000

Amortisation of the Government Grants

Dr. Government Grants	Non-Current Liabilities	SOFP	3,000	
Cr. Amortisation – Government Grants	Other Income	SOFP & OCI		3,000

Example 2

The following issued affect Konas Limited in relation to government grants for the year-ended 31 December 2016.

1. The Irish government decided to set up a development zone in Leitrim and it offered to compensate businesses for their relocation costs. €30,000 was received by Konas Limited for relocating.
2. Due to Konas Limited not meeting in full grant conditions, €15,000 of a grant previously received and credited in full to profit or loss had to be repaid in 2016.
3. €80,000 was received by Konas Limited from the government in relation to the purchase of equipment. The equipment cost €160,000 and it is expected to be depreciated over its useful life of eight years with no residual value at the end of the eight years.

Required: **Calculate how much of the government grants should be included in the Statement of Profit or Loss and Other Comprehensive Income and in the Statement of Financial Position for the year ended 31 December 2016.**

Solution Example 2

	Statement of Profit or Loss & Other Comprehensive Income	**Statement of Financial Position (Deferred Income)**
	€	**€**
Relocation Costs	Cr. 30,000	
Repayment of Grant	Dr. 15,000	
Equipment Grant		Cr. 80,000
Amortisation of Equipment Grant	Cr. 10,000	Dr. 70,000
	Cr. 25,000	**Cr. 70,000**

Example 3

Mreeu Limited purchased some plant in June 2016 costing €1,600,000. Its useful life is expected to be ten years and the residual value at the end of its useful will be €100,000. It received a grant of 30% of the cost of the asset in August 2016 having received government approval before it purchased the plant. Any grant received becomes repayable if the asset is sold within five years. Its company policies are to depreciate in full in the year of purchase and none in the year of sale and to maximise asset values.

Required: **Prepare the relevant extracts for the financial statements for the year ended 31 December 2016.**

Solution Example 3

Statement of Profit or Loss & Other Comprehensive Income (Extracts)

Other Income	**€**
Amortisation of Grant (W1)	48,000
Expenses	
Depreciation Expense (W2)	- 150,000

Statement of Financial Position (Extracts) **€**

Non-Current Assets		
Property, Plant & Equipment		1,450,000
Non-Current Liabilities		
Deferred Income (W1)		- 384,000
Current Liabilities		
Deferred Income (W1)		- 48.000

Working 1

Deferred Income

Grant Received	€1,600,000 x 30%	480,000
Amortisation for 2016	(€480,000 / 10 years)	- 48,000
		432,000
Current Liability		48,000
Non-Current Liability		384,000
Total		432,000

Working 2

Property, Plant & Equipment

Cost	1,600,000
Accumulated Depreciation	
(€1,600,000 – €100,000) / 10	- 150,000
Total	**1,450,000**