UNIT 1:
INDIAN ACCOUNTING STANDARD 20: ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE

LEARNING OUTCOMES

After studying this unit, you will be able to:

- After studying this chapter, you will be able to understand:
- Principles for recognition of government grant including non-monetary grants
- Presentation requirements of grants related to assets and income
- Accounting for repayment of government grants
7.2 FINANCIAL REPORTING

UNIT OVERVIEW

Ind AS 20

Government Grants
- Recognition of Government Grants
  - Reasonable assurance for receipt and compliance
  - Non-monetary government grants

Government Assistance
- Presentation of Government Grants
  - Related to assets
    - Presented in balance sheet by setting up grant as deferred income
  - Related to income
    - Presented as part of profit or loss, either separately or under 'other income'
    - Alternatively, deducted in reporting related expense

Disclosure
1.1 INTRODUCTION

The government gives grants to entities for various purposes including for industrial, geographic and social development, to facilitate the flow of foreign investments, to promote entrepreneurship, as subsidies to reduce the prices of goods and services offered by these entities.

The grant could be in different forms, e.g., monetary or non-monetary government grants.

Government grants may be significant for an entity and requires appropriate treatment in the books of accounts and disclosures in financial statements to facilitate comparison with other entities and with prior periods. Ind AS 20, Accounting for Government Grants and Disclosure of Government Assistance, provides guidance on this.

1.2 SCOPE

1.2.1 Applicability

Ind AS 20 should be applied for:
(a) accounting and disclosure of government grants; and
(b) disclosure of other forms of government assistance.

1.2.2 Non-applicability

Ind AS 20 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.

(c) government participation in the ownership of the entity;
(d) government grants that will be covered by Ind AS 41, Agriculture.
1.3 DEFINITIONS

The following definitions are relevant for the purpose of understanding of Ind AS 20:

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

2. **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 Ind AS 20 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 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.

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:

- Firstly, if resources have been transferred, an appropriate method of accounting for the transfer must be found.
- Secondly, 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.

**Example**

Free technical assistance or marketing advice and the provision of guarantees are forms of government assistance to which no value could reasonably be assigned.

**Example**

An example of transactions with government which 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.

3. **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.

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

4. **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.

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

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

7. **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 (Ind AS 113, *Fair Value Measurement*).

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**1.4 RECOGNITION OF GOVERNMENT GRANTS**

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

(a) the entity will comply with the conditions attaching to them; and

(b) the grants will be received.

A government grant is not recognised until there is reasonable assurance that the entity will comply with the conditions attaching to it, and that the grant 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.
Illustration 1

Government gives a grant of ₹10,00,000 for research and development of H1N1 vaccine to A Pharmaceuticals Limited. There is no condition attached to the grant. Examine how the Government grant be realized.

Solution

The entire grant should be recognised immediately in profit or loss.

Illustration 2

Government gives a grant of ₹10,00,000 for research and development of H1N1 vaccine to A Pharmaceuticals Limited even though similar vaccines are available in the market but are expensive. The entity has to ensure by developing a manufacturing process over a period of 2 years that the costs come down by at least 40%. Examine how the Government grant be realized.

Solution

The entire grant should be recognised immediately as deferred income and charged to profit or loss over a period of two years.

Illustration 3

A village of artisans in a district got devastated because of an earthquake. A Limited was operating in that district and was providing employment to the artisans. The government gave a grant of ₹10,00,000 to A Limited so that 100 artisans are rehabilitated over a period of 3 years. Government releases ₹2,00,000. Examine how the Government grant be realized.

Solution

A Limited will recognise ₹10,00,000 as government grant and set it up as a deferred income and will recognise it in its profit or loss over the period of three years as per the principles enunciated in Ind AS 20.

Once a government grant is recognised, any related contingent liability or contingent asset is treated in accordance with Ind AS 37, Provisions, Contingent Liabilities and Contingent Assets.

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 or in the form of a non-monetary asset.
1.4.1 Forgivable loan

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.

1.4.2 Loans at less than 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 should be recognised and measured in accordance with Ind AS 109, Financial Instruments. The benefit of the below-market rate of interest should be measured as the difference between the initial carrying value of the loan determined in accordance with Ind AS 109 and the proceeds received. The benefit is accounted for in accordance with Ind AS 20. The entity should 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.

Illustration 4

A Limited received from the government a loan of ₹ 50,00,000 @ 5% payable after 5 years in a bullet payment. The prevailing market rate of interest is 12%. Interest is payable regularly at the end of each year. Calculate the amount of government grant and Pass necessary journal entry. Also examine how the Government grant be realized.

Solution

The fair value of the loan is calculated at ₹ 37,38,328.

<table>
<thead>
<tr>
<th>Year</th>
<th>Opening Balance</th>
<th>Interest calculated @ 12%</th>
<th>Interest paid @ 5% on ₹ 50,00,000 + principal paid</th>
<th>Closing Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a)</td>
<td>(b)</td>
<td>(c) = (b) x 12%</td>
<td>(d)</td>
<td>(e)</td>
</tr>
<tr>
<td>1</td>
<td>37,38,328</td>
<td>4,48,600</td>
<td>2,50,000</td>
<td>39,36,928</td>
</tr>
</tbody>
</table>
A Limited will recognise ₹ 12,61,672 (₹ 50,00,000 – ₹ 37,38,328) as the government grant and will make the following entry on receipt of loan:

Bank Account

<table>
<thead>
<tr>
<th></th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Deferred Income</td>
<td>50,00,000</td>
</tr>
<tr>
<td>To Loan Account</td>
<td>37,38,328</td>
</tr>
</tbody>
</table>

₹ 12,61,672 is to be recognised in profit or loss on a systematic basis over the periods in which A Limited recognised as expenses the related costs for which the grant is intended to compensate. (see Illustration 5 in this regard)

**1.5 ACCOUNTING OF GOVERNMENT GRANT**

There are two approaches to the accounting of government grant: ‘capital approach’ or ‘income approach’. Under capital approach, a grant is recognised outside profit or loss, i.e., grant is credited directly to equity whereas under the income approach grant is recognised in profit or loss over one or more periods.

The Standard prescribes only the income approach despite the following arguments in favour of capital approach:

(a) government grants are a financing device and should be dealt with as such in the balance sheet rather than be recognised in profit or loss to offset the items of expense that they finance. Since 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.

The income approach has been prescribed because of the following arguments in its favour:

(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) since 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.

Principle:

Thus, 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.

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 expenses. 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.

Illustration 5

Continuing with the facts given in the Illustration 4, state how the grant will be recognized in the
statement of profit or loss assuming:

(a) the loan is an immediate relief measure to rescue the enterprise
(b) the loan is a subsidy for staff training expenses, incurred equally, for a period of 4 years
(c) the loan is to finance a depreciable asset.

Solution

₹ 12,61,672 is to be recognised in profit or loss on a systematic basis over the periods in which A
Limited recognised as expenses the related costs for which the grant is intended to compensate.

Assuming (a), the loan is an immediate relief measure to rescue the enterprise. ₹ 12,61,672 will
be recognised in profit or loss immediately.

Assuming (b), the loan is a subsidy for staff training expenses, incurred equally, for a period of 4
years. ₹ 12,61,672 will be recognised in profit or loss over a period of 4 years.

Assuming (c), the loan is to finance a depreciable asset. ₹ 12,61,672 will be recognised in profit
or loss on the same basis as depreciation.

1.5.1 Whether receipts basis permissible

Recognition of government grants in profit or loss on a receipts basis is not in accordance with
the accrual accounting assumption (Ind AS 1, Presentation of Financial Statements) and would
be acceptable only if no basis existed for allocating a grant to periods other than the one in which
it was received.
1.5.2 Grants related to non-depreciable assets

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.

Example

A grant of land may be conditional upon the erection of a building on the site and it may be appropriate to recognise the grant in profit or loss over the life of the building once the building is constructed and put to use.

1.5.3 Conditional Grants received as part of a package of financial or fiscal aids

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.

1.5.4 Grant for expenses or losses already incurred and grant as an immediate financial support

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 should be recognised in profit or loss of the period in which it becomes receivable.

In some circumstances, a government grant may be awarded for the purpose of giving immediate financial support to an entity rather than as an incentive to undertake specific expenditures. Such grants may be confined to a particular entity and may not be available to a whole class of beneficiaries. These circumstances may warrant recognising a grant in profit or loss of the period in which the entity qualifies to receive it, with appropriate disclosures to ensure that its effect is clearly understood.

A government grant may become receivable by an entity as compensation for expenses or losses incurred in a previous period. Such a grant is recognised in profit or loss of the period in which it becomes receivable, with disclosure to ensure that its effect is clearly understood.

1.5.5 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 the fair value of the non-monetary asset is assessed and both grant and asset are accounted for at that fair value. An entity is not permitted to measure these grants at nominal value.

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Illustration 6

A Limited wants to establish a manufacturing unit in a backward area and requires 5 acres of land. The government provides the land on a leasehold basis at a nominal value of ₹10,000 per acre. The fair value of the land is ₹100,000 per acre. Calculate the amount of the Government grant to be recognized by an entity.

Solution

A limited will recognize ₹450,000 [((₹100,000 – ₹10,000) x 5)] as government grant.

1.5.6 Government Assistance – No Specific relation to Operating Activities

In some countries government assistance to entities may be aimed at encouragement or long-term support of business activities either in certain regions or industry sectors. Conditions to receive such assistance may not be specifically related to the operating activities of the entity.

Examples of such assistance are transfers of resources by governments to entities which:

(a) operate in a particular industry;
(b) continue operating in recently privatised industries; or
(c) start or continue to run their business in underdeveloped areas.

The issue is whether such government assistance is a ‘government grant’ within the scope of Ind AS 20 and, therefore, should be accounted for in accordance with Ind AS 20.

In this regard, Appendix A to Ind AS 20 provides that government assistance to entities meets the definition of government grants in Ind AS 20, even if there are no conditions specifically relating to the operating activities of the entity other than the requirement to operate in certain regions or industry sectors. Such grants should therefore not be credited directly to shareholders’ interests and should be recognised in profit or loss on a systematic basis.

1.6 PRESENTATION OF GRANTS RELATED TO ASSETS

1.6.1 Presentation in the Balance Sheet

Government grants related to assets should be presented in the balance sheet by setting up the grant as deferred income. The non-monetary grants at fair value should be presented in a similar manner.

The grant set up as deferred income is recognised in profit or loss on a systematic basis over the useful life of the asset.
The grant is not deducted in arriving at the carrying amount of the asset.

**Illustration 7**

A Limited establishes solar panels to supply solar electricity to its manufacturing plant. The cost of solar panels is ₹1,00,00,000 with a useful life of 10 years. The government gives ₹50,00,000 as a subsidy. Examine how the Government grant be realized.

**Solution**

A Limited will set up ₹50,00,000 as deferred income and will credit ₹5,00,000 equally to its statement of profit and loss over next 10 years.

### 1.6.2 Disclosure in the statement of cash flows

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 disclosed as separate items in the statement of cash flows.

**Illustration 8**

Continuing with the facts given in the Illustration 7 above, state how the same will be disclosed in the Statement of cash flows.

**Solution**

A Limited will show ₹1,00,00,000 being acquisition of solar panels as outflow in investing activities. The receipt of ₹50,00,000 from government will be shown as inflow under financing activities.

### 1.7 PRESENTATION OF GRANTS RELATED TO INCOME

Two methods are prescribed for presentation of grants related to income. The grant could be

(a) (first method) presented as a credit in the statement of profit and loss, either separately or under a general heading such as ‘Other income’; or

(b) (second method) deducted in reporting the related expense.

The first method lays it foundation on the base:

(a) that it is inappropriate to net income and expense items and

(b) that separation of the grant from the expense facilitates comparison with other expenses not affected by a grant.
It is argued for the second method:

(a) that the expenses might well not have been incurred by the entity if the grant had not been available; and

(b) thus, presentation of the expense without offsetting the grant may therefore be misleading.

Both methods are regarded as acceptable for the presentation of grants related to income. Disclosure of the grant may be necessary for a proper understanding of the financial statements. Disclosure of the effect of the grants on any item of income or expense which is required to be separately disclosed is usually appropriate.

1.8 REPAYMENT OF GOVERNMENT GRANTS

An entity may have to repay the government grant including in cases where conditions related to the grant are not fulfilled by it.

A government grant that becomes repayable should be accounted for as a change in accounting estimate and be treated in accordance with Ind AS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*.

The following steps should be followed in repayment of a grant related to income:

(a) The repayment should be applied first against any unamortised deferred credit recognised in respect of the grant.

(b) To the extent that the repayment exceeds any such deferred credit, or when no deferred credit exists, the repayment should be recognised immediately in profit or loss.

The repayment of a grant related to an asset should be recognised by reducing the deferred income balance by the amount repayable.
1.9 DISCLOSURE

The following should be disclosed:

(a) the accounting policy adopted for government grants;

(b) the methods of presentation adopted for government grants in the financial statements;

(c) the nature and extent of government grants recognised in the financial statements;

(d) an indication of other forms of government assistance from which the entity has directly benefited. At times, the significance of the benefit of government assistance 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; and

(e) unfulfilled conditions and other contingencies attaching to government assistance that has been recognised.

1.10 SIGNIFICANT DIFFERENCES BETWEEN IND AS 20 AND AS 12

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Particulars</th>
<th>Ind AS 20</th>
<th>AS 12</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Monetary grants related to non-depreciable assets (without conditions)</td>
<td>Taken to profit and loss account</td>
<td>Credited as capital reserve</td>
</tr>
<tr>
<td>2.</td>
<td>Non-monetary government grant</td>
<td>Accounted for at fair value</td>
<td>• Accounted for on the basis of their acquisition cost • Non-monetary assets given free of</td>
</tr>
<tr>
<td></td>
<td>Grants related to depreciable assets (fixed assets)</td>
<td>Present only by setting up the grant as deferred income</td>
<td>Presented by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset</td>
</tr>
<tr>
<td>---</td>
<td>--------------------------------------------------</td>
<td>------------------------------------------------------</td>
<td>-------------------------------------------------------------------</td>
</tr>
<tr>
<td>3</td>
<td>Grants in the nature of promoter’s contribution</td>
<td>Silent on this category (and, by implication, requiring recognition as income)</td>
<td>To be credited to capital reserve and to be treated as shareholders’ funds</td>
</tr>
<tr>
<td>4</td>
<td>Loan at concessional rates of interest</td>
<td>Loan to be measured at fair value and recognised as per Ind AS 109 - value of concession, i.e., difference between proceeds received and valuation done to be recognised as grant</td>
<td>Silent on this category</td>
</tr>
</tbody>
</table>

**QUICK RECAP**

**Basic principle for recognition of government grant** - 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 grants are intended to compensate.

**Grants related to assets**
- Recognised in profit or loss over the periods matching with depreciation expense on those assets
- Non monetary government grants recognised at fair value

**Grants related to income**
- Recognised in profit or loss in which the specific expenses are incurred
- Grants relating to past expenses or losses or for giving immediate financial support with no further cost should be recognised in profit and loss in the period in which it becomes receivable
Practical Questions

1. ABC Ltd. has received the following grants from the Government of Delhi for its newly started pharmaceutical business:
   - ₹ 20 lakhs received for immediate start-up of business without any condition.
   - ₹ 50 lakhs received for research and development of drugs required for the treatment of cardiovascular diseases with following conditions:
     - that drugs should be available to the public at 20% cheaper from current market price: and
     - the drugs should be in accordance with quality prescribed by the World Health Organisation [WHO].
   - Two acres of land (fair Value: ₹ 10 Lakhs) received for set up plant.
   - ₹ 2 lakhs received for purchase of machinery of ₹ 10 lakhs. Useful life of machinery is 5 years. Depreciation on this machinery is to be charged on straight-line basis.

   How should ABC Ltd. recognise the government grants in its books of accounts?

2. A Limited received from the government a loan of ₹1,00,00,000 @ 5% payable after 5 years in a bulleted payment. The prevailing market rate of interest is 12%. Interest is payable regularly at the end of each year. Calculate the amount of government grant and Pass necessary journal entry. Also examine how the Government grant be realized. Also state how the grant will be recognized in the statement of profit or loss assuming that the loan is to finance a depreciable asset.

Answers to Practical Questions

1. ABC Ltd. should recognise the grants in the following manner:
   - ₹ 20 lakhs has been received for immediate start-up of business. This should be recognised in Statement of Profit and Loss immediately as there are no conditions attached to the grant.
   - ₹ 50 lakhs should be recognised in profit or loss on a systematic basis over the periods which the entity recognises as expense the related costs for which the grants are intended to compensate provided that there is reasonable assurance that ABC Ltd. will comply with the conditions attached to the grant.
   - Land should be recognised at fair value of ₹ 10 lakhs and government grants should be presented in the balance sheet by setting up the grant as deferred income.
• ₹ 2 lakhs should be recognised as deferred income and will be transferred to profit and loss over the useful life of the asset. In this cases, ₹ 40,000 [₹ 2 lakhs/5] should be credited to profit and loss each year over period of 5 years.

2. The fair value of the loan is calculated at ₹ 74,76,656.

<table>
<thead>
<tr>
<th>Year</th>
<th>Opening Balance</th>
<th>Interest calculated @ 12%</th>
<th>Interest paid @ 5% on ₹ 1,00,00,000 + principal paid</th>
<th>Closing Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a)</td>
<td>(b)</td>
<td>(c) = (b) x 12%</td>
<td>(d)</td>
<td>(e) = (b) + (c) − (d)</td>
</tr>
<tr>
<td>1</td>
<td>74,76,656</td>
<td>8,97,200</td>
<td>5,00,000</td>
<td>78,73,856</td>
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<tr>
<td>2</td>
<td>78,73,856</td>
<td>9,44,862</td>
<td>5,00,000</td>
<td>83,18,718</td>
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<tr>
<td>3</td>
<td>83,18,718</td>
<td>9,98,246</td>
<td>5,00,000</td>
<td>88,16,964</td>
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<td>4</td>
<td>88,16,964</td>
<td>10,58,036</td>
<td>5,00,000</td>
<td>93,75,000</td>
</tr>
<tr>
<td>5</td>
<td>93,75,000</td>
<td>11,25,000</td>
<td>1,05,00,000</td>
<td>Nil</td>
</tr>
</tbody>
</table>

A Limited will recognise ₹ 25,23,344 (₹ 1,00,00,000 − ₹ 74,76,656) as the government grant and will make the following entry on receipt of loan:

Bank Account | Dr. | 1,00,00,000 |
-------------|-----|-------------|
To Deferred Income | 25,23,344 |
To Loan Account | 74,76,656 |

 ₹ 25,23,344 is to be recognised in profit or loss on a systematic basis over the periods in which A Limited recognised as expenses the related costs for which the grant is intended to compensate.

 ₹ 25,23,344 is to be recognised in profit or loss on a systematic basis over the periods in which A Limited recognised as expenses the related costs for which the grant is intended to compensate.

If the loan is to finance a depreciable asset, ₹ 25,23,344 will be recognised in profit or loss on the same basis as depreciation.