**STATUTORY BOARD FINANCIAL REPORTING STANDARD**

**SB-FRS 20**

# Accounting for Government Grants and Disclosure of Government Assistance

SB-FRS 20 *Accounting for Government Grants and Disclosure of Government Assistance* was operative for Statutory Boards' financial statements for annual periods beginning on or after 1 January 2005.

This Standard is equivalent to FRS 20 *Accounting for Government Grants and Disclosure of Government Assistance* issued by the Council on Corporate Disclosure and Governance on 7 July 2004.

# Contents

Statutory Board Financial Reporting Standard 20 *Accounting for Government Grants and Disclosure of Government Assistance* (SB-FRS 20) is set out in paragraphs 1-41. All the paragraphs have equal authority. SB-FRS 20 should be read in the context of the *Preface to the Statutory Board Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. SB-FRS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

# STATUTORY BOARD FINANCIAL REPORTING STANDARD SB-FRS 20

## Accounting for Government Grants and Disclosure of Government Assistance

## Scope

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

2. 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 enterprise in the form of benefits that are available in determining taxable income or are determined or limited on the basis of income tax liability (such as income tax holidays, investment tax credits, accelerated depreciation allowances and reduced income tax rates);

   (c) government participation in the ownership of the enterprise;

   (d) government grants covered by SB-FRS 41 *Agriculture*.

## Definitions

***3. The following terms are used in this Standard with the meanings specified:***

***<u>Government</u> refers to government, government agencies and similar bodies whether local, national or international.***

***<u>Government assistance</u> is action by government designed to provide an economic benefit specific to an enterprise or range of enterprises 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.***

***<u>Government grants</u> are assistance by government in the form of transfers of resources to an enterprise in return for past or future compliance with certain conditions relating to the operating activities of the enterprise. 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 enterprise.*** [1]

***<u>Grants related to assets</u> are government grants whose primary condition is that an enterprise qualifying for them should purchase, construct or otherwise acquire long-term***

[1] See also INT - 10, Government Assistance - No Specific Relation to Operating Activities

***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 amount for which an asset could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction.*

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 enterprise to embark on a course of action which it would not normally have taken if the assistance was not provided.

5. The receipt of government assistance by an enterprise 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 enterprise has benefited from such assistance during the reporting period. This facilitates comparison of an enterprise's financial statements with those of prior periods and with those of other enterprises.

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

## Government Grants

***7. Government grants, including non-monetary grants at fair value, should not be recognised until there is reasonable assurance that:***

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

***(b) the grants will be received.***

8. A government grant is not recognised until there is reasonable assurance that the enterprise 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.

9. 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.

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

11. Once a government grant is recognised, any related contingency would be treated in accordance with SB-FRS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

***12. Government grants should be recognised as income over the periods necessary to match them with the related costs which they are intended to compensate, on a systematic basis. They should not be credited directly to shareholders' interests.***

13. Two broad approaches may be found to the accounting treatment of government grants: the capital approach, under which a grant is credited directly to shareholders' interests, and the income approach, under which a grant is taken to income over one or more periods.

14. Those in support of the capital approach argue as follows:

    (a) government grants are a financing device and should be dealt with as such in the balance sheet rather than be passed through the income statement to offset the items of expense which they finance. Since no repayment is expected, they should be credited directly to shareholders' interests; and

    (b) it is inappropriate to recognise government grants in the income statement, since they are not earned but represent an incentive provided by government without related costs.

15. Arguments in support of the income approach are as follows:

    (a) since government grants are receipts from a source other than shareholders, they should not be credited directly to shareholders' interests but should be recognised as income in appropriate periods;

    (b) government grants are rarely gratuitous. The enterprise earns them through compliance with their conditions and meeting the envisaged obligations. They should therefore be recognised as income and matched with the associated costs which the grant is intended to compensate; and

    (c) as income and other taxes are charges against income, it is logical to deal also with government grants, which are an extension of fiscal policies, in the income statement.

16. It is fundamental to the income approach that government grants be recognised as income on a systematic and rational basis over the periods necessary to match them with the related costs. Income recognition of government grants on a receipts basis is not in accordance with the accrual accounting assumption (see SB-FRS 1 *Presentation of Financial Statements*) and would only be acceptable if no basis existed for allocating a grant to periods other than the one in which it was received.

17. In most cases the periods over which an enterprise recognises the costs or expenses related to a government grant are readily ascertainable and thus grants in recognition of specific expenses are recognised as income in the same period as the relevant expense. Similarly, grants related to depreciable assets are usually recognised as income over the periods and in the proportions in which depreciation on those assets is charged.

18. Grants related to non-depreciable assets may also require the fulfilment of certain obligations and would then be recognised as income over the periods which bear the cost of meeting the obligations. As an example, a grant of land may be conditional upon the erection of a building on the site and it may be appropriate to recognise it as income over the life of the building.

19. 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.

***20. 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 as income of the period in which it becomes receivable.***

21. 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 an individual entity and may not be available to a whole class of beneficiaries. These circumstances may warrant recognising a grant as income in the period in

which the entity qualifies to receive it, with disclosure to ensure that its effect is clearly understood.

22. 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 as income of the period in which it becomes receivable, with disclosure to ensure that its effect is clearly understood.

## Non-Monetary Government Grants

23. 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 enterprise. 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 Related to Assets

***24. Government grants related to assets, including non-monetary grants at fair value, should be presented in the balance sheet either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.***

25. Two methods of presentation in financial statements of grants (or the appropriate portions of grants) related to assets are regarded as acceptable alternatives.

26. One method sets up the grant as deferred income which is recognised as income on a systematic and rational basis over the useful life of the asset.

27. The other method deducts the grant in arriving at the carrying amount of the asset. The grant is recognised as income over the life of a depreciable asset by way of a reduced depreciation charge.

28. The purchase of assets and the receipt of related grants can cause major movements in the cash flow of an enterprise. For this reason and in order to show the gross investment in assets, such movements are often disclosed as separate items in the cash flow statement regardless of whether or not the grant is deducted from the related asset for the purpose of balance sheet presentation.

## Presentation of Grants Related to Income

29. Grants related to income are sometimes presented as a credit in the income statement, either separately or under a general heading such as "Other income"; alternatively, they are deducted in reporting the related expense.

30. Supporters of the first method claim that it is inappropriate to net income and expense items and that separation of the grant from the expense facilitates comparison with other expenses not affected by a grant. For the second method it is argued that the expenses might well not have been incurred by the enterprise if the grant had not been available and presentation of the expense without offsetting the grant may therefore be misleading.

31. 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.

### Repayment of Government Grants

***32. A government grant that becomes repayable should be accounted for as a revision to an accounting estimate (see SB-FRS 8*** **Accounting Policies, Changes in Accounting Estimates and Errors*****). Repayment of a grant related to income should be applied first against any unamortised deferred credit set up in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or where no deferred credit exists, the repayment should be recognised immediately as an expense. Repayment of a grant related to an asset should be recorded 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 to date as an expense in the absence of the grant should be recognised immediately as an expense.***

33. Circumstances giving rise to repayment of a grant related to an asset may require consideration to be given to the possible impairment of the new carrying amount of the asset.

## Government Assistance

34. Excluded from the definition of government grants in paragraph 3 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 enterprise.

35. 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 enterprise is a government procurement policy that is responsible for a portion of the enterprise'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.

36. 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.

37. Loans at nil or low interest rates are a form of government assistance, but the benefit is not quantified by the imputation of interest.

38. 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.

## Disclosure

***39. The following matters should be disclosed:***

- ***(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 enterprise has directly benefited; and***
- ***(c) unfulfilled conditions and other contingencies attaching to government assistance that has been recognised.***

## Transitional Provisions

***40. An enterprise adopting the Standard for the first time should:***

- ***(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 SB-FRS 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.***

## Effective Date

***41. Statutory Boards' shall apply this Standard for annual periods beginning on or after 1 January 2005.***