

IAS 20- ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE- TWO ACCOUNTING ISSUES

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AGENDA



	Topic
1.	Background
2.	Issues and possible views
2.1	Whether Government grant receivable is a financial asset (under IFRS 9) or not?
2.2	Government grant income presentation: Revenue, Reduction of Related Expense or Other Income?
3.	Request for Feedback/Views

BACKGROUND



- In India, State and Central Government provides grants/ incentive schemes of various forms such as in form subsidy to promote or incentivise entities or for any other reason
- For example, **fertilizer subsidy scheme in India**
 - ✓ fertilizers are made available to farmers at affordable prices, i.e., at statutory notified uniform sale price.
 - ✓ statutorily notified sale price and indicative Maximum Retail Price (MRP) are generally less than the cost of production.
 - ✓ the difference between the cost of production and the selling price/MRP is paid as subsidy by the Government to the fertilizer manufacturers.
 - ✓ difference between cost of production and selling price is not expected to be included by the Government authority in establishing future selling price Hence, not covered by IFRS 14.



- Often, the entities also gives declaration that they will abide by all the terms and conditions of the grant/ incentive schemes.
- On complying with the stipulated conditions attached to the grant, the respective State/Central Government issues eligibility certificates or the entities are required to file subsidy claims, etc. to get the benefits attached to the grant.

Contd...

BACKGROUND

(Contd...)



- Under such grants, generally there is no one to one contract between Government and the entity.
- Applicant/potential entities have to meet the requirement of these grants in order to get benefit of the same.
- Often there are time lags between the grant becoming due and its actual receipt from the Government and these are treated as Government grants and are covered under IAS 20.
- IAS 20 prescribes initial measurement but does not deal with subsequent measurement of receivables arising from Government grants.
- IFRS 9 also does not have any provisions about subsequent measurement receivables arising from Government grants.

ISSUES



Issue I- Whether Government grant receivable is a financial asset (under IFRS 9) or not?

Issue II- How should the income arising from such grants be accounted for as-

- revenue;
- *reduction of related expense, viz., cost of production;* or
- other income

ISSUE-I WHETHER THE GOVERNMENT GRANT RECEIVABLE IS A FINANCIAL ASSET (UNDER IFRS 9) OR RECOGNISED AS OTHER ASSET (RECEIVABLE)



- Once the Government grant is accrued and recognised as an asset (receivable), does the receivable grant meet the definition of '*financial instruments*' or 'financial asset' under IAS 32 and its subsequent measurement under IFRS 9, considering there is no formal one to one contractual agreement between Government and the entity.
- Can the eligibility certificate given by Government / declarations submitted by the entity be construed as contracts since the eligibility certificate & the declarations clearly spell out the economic consequences of non compliances for the entity and the eligibility certificate binds the Government to honour the incentives if all the conditions are met.

Contd...

ISSUE-I WHETHER THE GOVERNMENT GRANT RECEIVABLE IS A FINANCIAL ASSET (UNDER IFRS 9) OR RECOGNISED AS OTHER ASSET (RECEIVABLE) (Contd...)



Definition as per IAS 32

- A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.
- A financial asset is any asset that is:
 - (a) cash;
 - (b) an equity instrument of another entity;
 - (c) a contractual right:
 - (i) to receive cash or another financial asset from another entity;
 - or
 - (ii) ...

Contd...

ISSUE-I WHETHER THE GOVERNMENT GRANT RECEIVABLE IS A FINANCIAL ASSET (UNDER IFRS 9) OR RECOGNISED AS OTHER ASSET (RECEIVABLE)) (Contd...)



IFRS 9 applies to all types of financial instruments other than a few exceptions as specified in the said Standard.

Contd...

ISSUE-I WHETHER THE GOVERNMENT GRANT RECEIVABLE IS A FINANCIAL ASSET (UNDER IFRS 9) OR RECOGNISED AS OTHER ASSET (RECEIVABLE) (Contd...)



View 1: Not a financial asset

- As there is no one to one contract between the entity and the Government as to the rights and obligations, the grant receivable is not a financial instrument.
- The rights under the grant in this situation are non- financial assets arising from the application of government grant accounting under IAS 20.
- Additionally, if there are substantive conditions attached to receiving the subsidy or if the amounts are variable then the economic substance of the arrangement may reflect that it is best accounted as a grant under IAS 20.

ISSUE-I WHETHER THE GOVERNMENT GRANT RECEIVABLE IS A FINANCIAL ASSET (UNDER IFRS 9) OR RECOGNISED AS OTHER ASSET (RECEIVABLE) (Contd...)



View 2: It is a financial asset

Paragraph 13 of IAS 32 states that, “In this Standard, ‘contract’ and ‘contractual’ refer to an agreement between two or more parties that has clear economic consequences that the parties have little, if any, discretion to avoid, usually because the agreement is enforceable by law. Contracts, and thus financial instruments, may take a variety of forms and need not be in writing.”

Paragraph 13 clarifies that contract need not be in writing only and may take various forms.

ISSUE-I WHETHER THE GOVERNMENT GRANT RECEIVABLE IS A FINANCIAL ASSET (UNDER IFRS 9) OR RECOGNISED AS OTHER ASSET (RECEIVABLE)



View 2 (contd...):

- In India, Government give incentives to promote entities or for some other reasons as the case may be. Although under such schemes, **there may not be a one to one contract** between the entity and the Government as to the rights and obligations **but there is an understanding between the Government and the potential applicant/entity** that on complying the stipulated conditions attached to the scheme, the entity will be granted benefits of the scheme.
- If the entity has complied with the conditions attached to the scheme then it rightfully becomes entitled to the grant attached to the scheme.

Such Government grant receivable will fall under the definition of financial instruments and its subsequent measurement will be accounted for as a financial asset as per IFRS 9.

ISSUE-I: RECOMMENDATION ON IAS 20, IAS 32 AND IFRS 9



- In absence of clarity and possible multiple views, there is need for amendment in IAS 20 that subsequent accounting of assets arising from Government grants should be accounted for under IFRS 9.
- It is also pertinent to note that accounting for initial measurement of Government grants is prescribed under IAS 20.
- This will be consistent with the accounting for contract assets as income arising from contract with a customer is governed by IFRS 15 while, accounting of assets/receivables arising from such contracts are governed by IFRS 9.

ISSUE-II GOVERNMENT GRANT: REVENUE, REDUCTION OF RELATED EXPENSE OR OTHER INCOME



- The Government grant objectives could be different .
- There are many Government grants given to compensate the entity for loss of revenue due to mandatory sale price of goods/services set at lower than cost of production.

Therefore, the question arises how to present such Government grant income.

ISSUE-II GOVERNMENT GRANT: REVENUE, REDUCTION OF RELATED EXPENSE OR OTHER INCOME



Paragraphs 29 -31 of IAS 20 state that-

- 29 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.
- 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 entity 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.

As can be seen from above provisions, there is lack of clarity as to how to present certain type of grants

ISSUE-II GOVERNMENT GRANT: REVENUE, REDUCTION OF RELATED EXPENSE OR OTHER INCOME



View I:

Presentation as part of revenue

It is appropriate to account for such grants as *revenue from operations*, considering that difference between the cost of production and the selling price/MRP is paid as grant to manufacturers as a part of total price of the product to the manufacturers.

ISSUE-II GOVERNMENT GRANT: REVENUE, REDUCTION OF RELATED EXPENSE OR OTHER INCOME



View II:

Presented as reduction of related expense, viz., cost of production

- Rationale for above view is that Government grant receivable is determined on difference between cost of production and selling price set by Government authority.

ISSUE-II GOVERNMENT GRANT: REVENUE, REDUCTION OF RELATED EXPENSE OR OTHER INCOME



View III:

Income arising from such grants be accounted for as other income

- As per paragraph 29 of Ind AS 20, 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.
- Since, the grant is not against a particular head of expense, so it is not appropriate to reduce it from the cost of production or present as revenue and hence be accounted for as '*other income*'.

FEEDBACK



Members may share the practice followed in their jurisdictions in this regard



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