UNIT 2 : INDIAN ACCOUNTING STANDARD 20: ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE

LEARNING OUTCOMES

After studying this unit, you will be able to:

- ❑ Interpret the principles for recognition of government grant including non-monetary grants
- ❑ Recommend presentation requirements of grants related to assets and income
- ❑ Account for repayment of government grants

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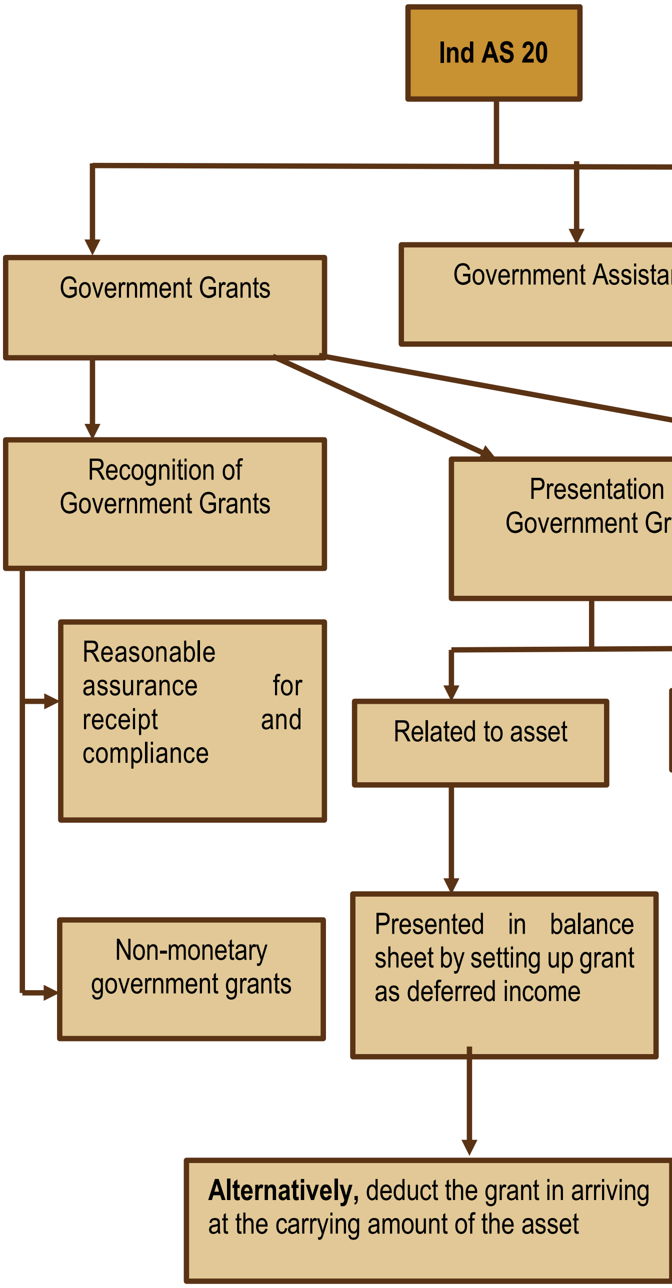
UNIT OVERVIEW



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2.1 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 require appropriate treatment in the books of accounts and disclosures in the 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.

2.2 SCOPE

2.2.1 Applicability

Ind AS 20 should be applied for:

(a) accounting and disclosure of government grants; and

(b) disclosure of other forms of government assistance.

2.2.2 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*.

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2.3 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.

Examples 1-4 : Government assistance

1. Free technical assistance or marketing advice and the provision of guarantees are forms of government assistance to which no value could reasonably be assigned.
2. 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

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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.

3. **Assistance in the form of priority bidding status:** The government specifies that entities below a certain size are to be given priority in bidding for a particular type of government contract by mandating a minimum number of such entities to obtain bidding status. Although the entities will benefit from the quota, the value cannot be identified, and the effects of the assistance cannot be segregated from the trading activities of the entities.

4. **Assistance in the form of credit facilities at market rates:** Three governments that amongst themselves own over 50% of the shares in an airline, participate in granting it a revolving credit facility at a market rate of interest. This is not a government grant as a loan is provided at market rate of interest which any private market participant might have accepted. However, it is government assistance as the benefit cannot be distinguished from normal trading activities of the airline.

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.

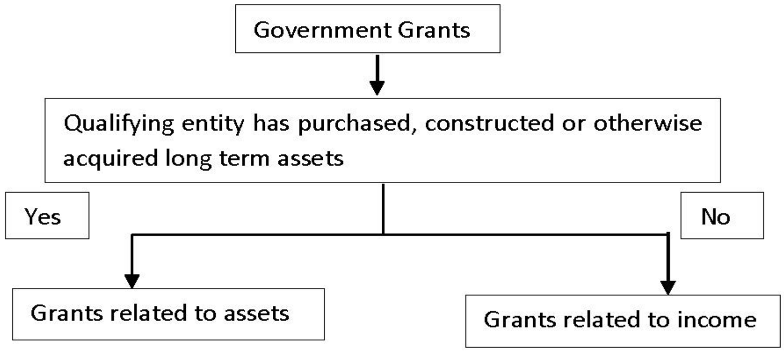
3. ***Government grants*** are assistance by the government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity.

   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.

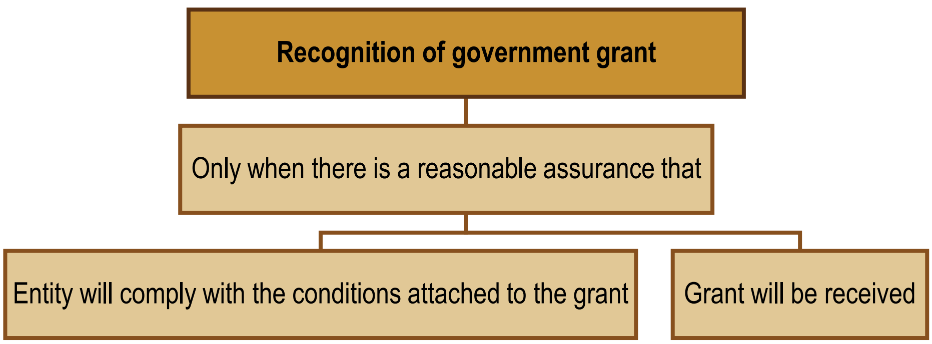
5. ***Grants related to income*** are government grants other than those related to assets.



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*).

2.4 RECOGNITION OF GOVERNMENT GRANTS



Government grants, including non-monetary grants at fair value, shall not be recognised until 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.

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Illustration 1

Government gives a grant of ₹ 10,00,000 for past research of H1N1 vaccine to A Pharmaceuticals Limited. There is no condition attached to the grant.

Examine how this government grant be recognised in the books of A Pharmaceuticals Limited.

Solution

The entire grant should be recognised immediately in the statement of profit and loss.

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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 this government grant be recognised assuming that A Pharmaceuticals Limited has reasonable assurance that the conditions attached to the grant will be complied with.

Solution

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

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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 this government grant be recognised.

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.*

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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.

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2.4.1 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.

2.4.2 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 recognised.

Solution

The fair value of the loan is calculated at ₹ 37,38,328 (refer Working Note).

Year	Opening Balance	Interest calculated @ 12%	Interest paid @ 5% on ₹ 50,00,000 + principal paid	Closing Balance
(a)	(b)	(c) = (b) x 12%	(d)	(e) =(b) + (c) – (d)
1	37,38,328	4,48,600	2,50,000	39,36,928
2	39,36,928	4,72,431	2,50,000	41,59,359
3	41,59,359	4,99,123	2,50,000	44,08,482
4	44,08,482	5,29,018	2,50,000	46,87,500
5	46,87,500	5,62,500	52,50,000	Nil

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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	Dr.	50,00,000	
To Deferred Income			12,61,672
To Loan Account			37,38,328

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

Working Note:

Particulars	Amount (₹)	Discounting factor	Present value taking 12% as the discount rate (₹)
Interest @ 5% for Year 1 on loan amount of ₹ 50 lakhs	2,50,000	0.893	2,23,214
Interest @ 5% for Year 2 on loan amount of ₹ 50 lakhs	2,50,000	0.797	1,99,298
Interest @ 5% for Year 3 on loan amount of ₹ 50 lakhs	2,50,000	0.712	1,77,945
Interest @ 5% for Year 4 on loan amount of ₹ 50 lakhs	2,50,000	0.636	1,58,880
Interest @ 5% for Year 5 on loan amount of ₹ 50 lakhs	2,50,000	0.567	1,41,857
Loan	50,00,000	0.567	28,37,134
Present value of loan at the beginning of Year 1			**37,38,328**

The above present value above has been computed on full scale basis.

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2.5 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.

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The Standard rejects the capital approach and 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

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(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.

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2.5.1 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.

2.5.2 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 5

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.

2.5.3 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.

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2.5.4 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.

2.5.5 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. Alternatively, an entity may measure both asset and grant at nominal value.

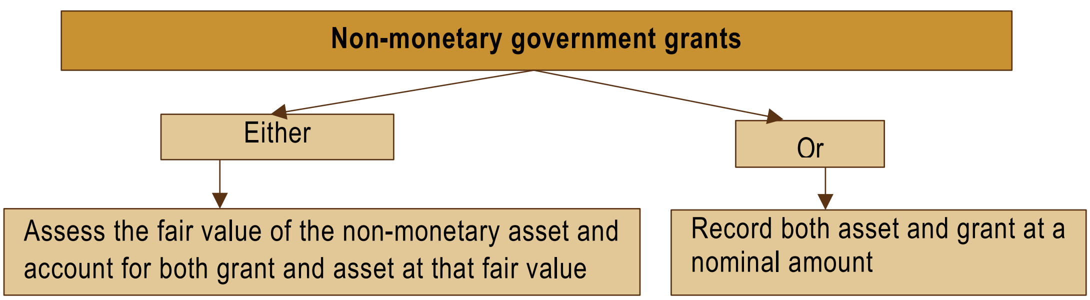

Illustration 6

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.

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Solution

A limited will recognise the land at fair value of ₹ 5,00,000 and ₹ 450,000 [(₹ 100,000 – ₹ 10,000) x 5)] as government grant. This government grant should be presented in the balance sheet by setting up the grant as deferred income.

Alternatively, the land may be recognised by A Ltd. at nominal value of ₹ 50,000 (₹ 10,000 x 5).

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2.5.6 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.

2.6 PRESENTATION OF GRANTS RELATED TO ASSETS

2.6.1 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.

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Alternatively, it can be presented in the balance sheet by deducting the grant in arriving at the carrying amount of the asset.

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 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.

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 depreciation is provided on straight line method basis. 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.

Alternatively, A Ltd. may deduct ₹ 50,00,000 from the cost of solar panel of ₹ 1,00,00,000.

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2.6.2 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. This presentation is done irrespective of the fact that the grant is deducted or not from the related asset, for the purpose of presentation in the balance sheet.

Illustration 8

Continuing with the facts given in 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 investing activities.

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2.7 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.

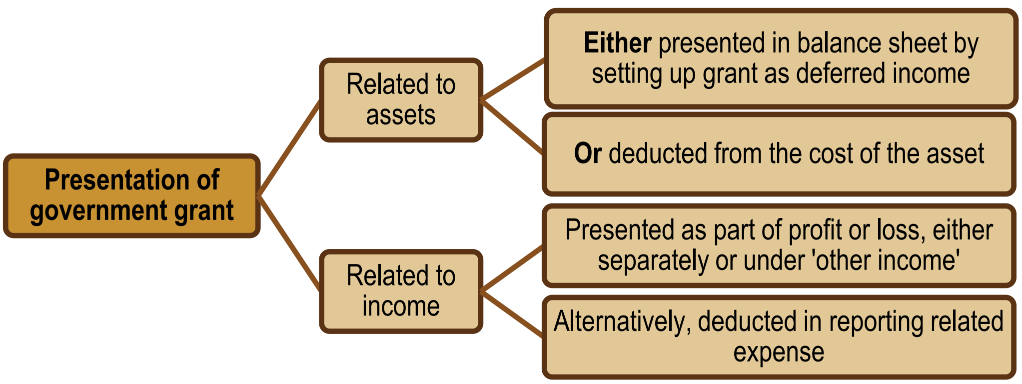

Illustration 9

A Ltd. received a government grant of ₹ 10,00,000 to defray expenses for environmental protection. Expected environmental costs to be incurred is ₹ 3,00,000 per annum for the next 5 years.

Determine the presentation of such grant related to income in the financial statements of A Ltd.?

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Solution

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.

In accordance with the above, presentation of grants related to income under both the methods are as follows:

Method 1: Credit in the statement of profit and loss

The entity can recognise the grant as income on a straight line basis i.e., ₹ 2,00,000 per year in the statement of profit and loss either separately or under the head "Other Income".

The supporters of this method consider it inappropriate to present income and expense items on a net basis and that 'separation of the grant from the expense facilitates comparison with other expenses not affected by a grant'.

Method 2: As a deduction in reporting the related expense

Since the grant relates to environmental expenses incurred/to be incurred by the entity, it can present the grant by reducing the grant amount every year from the related expense i.e., environmental expense of ₹ 1,00,000 (i.e., net expense ₹ 3,00,000 – ₹ 2,00,000).

The supporters of this method are of the view 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'.

The Standard regards both the methods as acceptable for the presentation of grants related to income. However, method 2 may be more appropriate when the company can relate the grant to a specific expenditure.

The Standard also provides that 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.

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2.8 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.*

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Repayment of a grant related to income

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 either by reducing the deferred income balance by the amount repayable or by increasing the carrying amount of the asset.

Repayment of government grant

Related to income	Related to asset	
First applied towards any unapplied deferred credit and then charged to profit and loss account immediately	***Either** recognised by increasing the carrying amount of the asset *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. * Check the possible impairment of the new carrying amount of the asset.	**Or** by reducing the deferred income balance by the amount payable

Illustration 10

A Ltd. has received a grant of ₹ 10,00,00,000 in the year 20X1-20X2 from local government in the form of subsidy for selling goods at lower price to lower income group population in a particular area for two years. A Ltd. had accounted for the grant as income in the year 20X1-20X2. While accounting for the grant in the year 20X1-20X2, A Ltd. was reasonably assured that all the conditions attached to the grant will be complied with. However, in the year 20X5-20X6, it was found that A Ltd. has not complied with the above condition and therefore notice of refund of grant has been served to it. A Ltd. has contested but lost in court in 20X5-20X6 and now grant is fully repayable. The accounting done in previous years was not incorrect and was not an error as per Ind AS 8.

Analyse how should A Ltd. reflect repayable grant in its financial statements ending 20X5-20X6?

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Solution

Paragraph 32 of Ind AS 20, states that a government grant that becomes repayable shall be accounted for as a change in accounting estimate (see Ind AS 8, Accounting Policies, Changes in Accounting Estimates and Errors).

Repayment of a grant related 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.

The following journal entries should be passed:

S. No.	Particulars		Nature of Account	Amount (₹ in crores)	
(i)	Repayment of Government Grant	Dr.	Expense (P/L)	10	
	To Grant repayable		Balance sheet (Liability)		10
	(Being recognition of repayment of grant in statement of profit or loss)				
(ii)	Grant repayable	Dr.	Balance sheet (Liability)	10	
	To Bank		Balance sheet (Asset)		10
	(Being grant refunded)				

Assuming that no deferred credit balance exists in the year 20X5-20X6, therefore repayment recognised in P&L.

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2.9 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

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

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2.10 EXTRACTS OF FINANCIAL STATEMENTS OF LISTED ENTITIES

Following is the extract from the financial statements of the listed entity 'Hindustan Unilever Limited' for the financial year 2021-2022 with respect to 'Government Grants'.

Government grants:

The Company has received approval under the Production Linked Incentive Scheme of the Government of India for specific product categories. Incentive under the scheme is subject to meeting certain committed investments and defined incremental sales threshold. Such grants are recognised as other operating revenue when there is a reasonable assurance that the Company will comply with all necessary conditions attached to that.

Income from such grants is recognised on a systematic basis over the periods to which they relate.

	Year ended 31st March, 2022	Year ended 31st March, 2021
Sale of products	50,336	45,311
Other operating revenue*		
Income from services rendered	281	225
Commission income on consignment sales	315	264
Government grants (GST budgetary support and Production linked incentives) #	140	108
Others (including scrap sales, rentals, etc)	121	88
Total	**51,193**	**45,996**

Previous period figures have been re-classified from Others for better presentation

(Source: Annual Report 2021-2022 – Hindustan Unilever Limited)

2.11 SIGNIFICANT DIFFERENCES BETWEEN IND AS 20 AND AS 12

S. No.	Particulars	Ind AS 20	AS 12
1.	Monetary grants related to non-depreciable assets	Taken to the statement of profit and loss assuming that all grants have conditions attached to it. Specifically prohibits recognition of grants directly in the shareholders' funds	Credited as capital reserve which is part of shareholder's funds. If such grant requires fulfilment of certain obligations, credit the grant amount to income over the same period over which the cost of meeting such obligations is charged to income.

2.	Non-monetary government grant given at a concessional rate	Accounted for at fair value or at nominal value	• Accounted for on the basis of their acquisition cost • Non-monetary assets given free of cost are recorded at a nominal value
3.	Grants in the nature of promoter's contribution	Ind AS 20 does not recognise government grants of the nature of promoters' contribution. As stated at (1) above, Ind AS 20 is based on the principle that all government grants would normally have certain obligations attached to them and it, accordingly, requires all grants to be recognised as income over the periods which bear the cost of meeting the obligation.	To be credited to capital reserve and to be treated as part of shareholders' funds
4.	Loan received from the government at below-market rate of interest	Measured in accordance with Ind AS 109 (which requires all loans to be recognised at fair value, thus requiring interest to be imputed to loans with a below-market rate of interest)	AS 12 does not deal with such cases
5.	Government assistance not falling within the definition of government grants	Requires an indication of other forms of government assistance from which the entity has directly benefited and should be disclosed in the financial statements	Does not deal with such government assistance

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FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

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 further 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 of 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.

   Recommend 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.

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Calculate the amount of government grant and pass necessary journal entry. Also examine how the government grant be recognised. 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.

3. MNC Ltd. has received grant in the nature of exemption of custom duty on capital goods with certain conditions related to export of goods under Export Promotion Capital Goods (EPCG) scheme of Government of India.

   State whether the same is a government grant under Ind AS 20, Government Grants and Disclosure of Government Assistance? If yes, then how the same is to be accounted for if it is

   (a) A grant related to asset; or

   (b) A grant related to income.

4. ABC Ltd is a government company and is a first-time adopter of Ind AS. As per the previous GAAP, the contributions received by ABC Ltd. from the government (which holds 100% shareholding in ABC Ltd.) which is in the nature of promoters' contribution have been recognised in capital reserve and treated as part of shareholders' funds in accordance with the provisions of AS 12, Accounting for Government Grants.

   State whether the accounting treatment of the grants in the nature of promoters' contribution as per AS 12 is also permitted under Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance.

5. Rainbow Limited carries out various projects for which it has either received government financial assistance or is in the process of receiving the same. The company has received two grants of ₹ 1,00,000 each, relating to the following ongoing research and development projects:

   (i) The first grant relates to the "Clean river project" which involves research into the effect of various chemicals waste from the industrial area in Madhya Pradesh. However, no major steps have been completed by Rainbow limited to commence this research as at 31st March, 20X2.

   (ii) The second grant relates to the commercial development of a new equipment that can be used to manufacture eco-friendly substitutes for existing plastic products. Rainbow Limited is confident about the technical feasibility and financial viability of this new technology which will be available for sale in the market by April 20X3.

   In September 20X1, due to the floods near one of its factories, the entire production was lost and Rainbow Limited had to shut down the factory for a period of 3 months. The State

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Government announced a compensation package for all the manufacturing entities affected due to the floods. As per the scheme, Rainbow Limited is entitled to a compensation based on the average of previous three months' sales figure prior to the floods, for which the company is required to submit an application form on or before 30th June, 20X2 with necessary figures. The financial statements of Rainbow Limited for the year ended 31st March 20X2 are to be adopted on 31st May, 20X2, by which date the claim form would not have been filed with the State Government.

Suggest the accounting treatment of, if any, for the two grants received and the flood-related compensation in the books of accounts of Rainbow Limited as at 31st March, 20X2.

6. An entity opens a new factory and receives a government grant of ₹ 15,000 in respect of capital equipment costing ₹ 1,00,000. It depreciates all plant and machinery at 20% per annum on straight-line basis.

Show the statement of profit and loss and balance sheet extracts in respect of the grant for first year under both the methods as per Ind AS 20.

Answers

1. ABC Ltd. should recognise the grants in the following manner:

- ₹ 20 lakhs have been received for immediate start-up of business. This should be recognised in Statement of Profit and Loss immediately as there are no further 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 grant should be presented in the balance sheet by setting up the grant as deferred income. Alternatively, deduct the amount of grant from the cost of the asset. In the given case, the land is granted at no cost. It will be presented in the books at nominal value.
- ₹ 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 case, ₹ 40,000 [₹ 2 lakhs/5] should be credited to profit and loss each year over a period of 5 years. Alternatively, ₹ 2,00,000 will be deducted from the cost of the asset and depreciation will be charged at reduced amount of ₹ 8,00,000 (₹ 10,00,000 – ₹ 2,00,000) every year.

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2. The fair value of the loan is calculated at ₹ 74,76,656 (refer Working Note).

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

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.

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.

Working Note:

Particulars	Rs.	Discounting factor@ 12%	Present value taking 12% as the discount rate (Rs.)
Interest @ 5% for Year 1 on loan amount of ₹ 1 crore	5,00,000	0.893	4,46,429
Interest @ 5% for Year 2 on loan amount of ₹ 1 crore	5,00,000	0.798	3,98,597
Interest @ 5% for Year 3 on loan amount of ₹ 1 crore	5,00,000	0.712	3,55,890
Interest @ 5% for Year 4 on loan amount of ₹ 1 crore	5,00,000	0.636	3,17,759
Interest @ 5% for Year 5 on loan amount of ₹ 1 crore	5,00,000	0.567	2,83,713
Loan	1,00,00,000	0.567	56,74,269
Present value of loan at the beginning of Year 1			**74,76,656**

The above present value above has been computed on full scale basis.

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3. Paragraph 3 of Ind AS 20 states that 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.

In accordance with the above, in the given case exemption of custom duty under EPCG scheme is a government grant and should be accounted for as per the provisions of Ind AS 20.

Ind AS 20 defines grant related to assets and grants related to income as follows:

"Grants related to asset 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."

Presentation

It is pertinent to note that the classification of the grant as related to asset or income will require exercise of judgement and careful examination of the facts, objective and conditions attached to the scheme of the government. Care is also required to ascertain the purpose of the grant and the costs for which the grant is intended to compensate. Based on the evaluation of facts, if it is ascertained that the grant is an asset related grant then the same shall be presented as per paragraphs 24 and 26 of Ind AS 20 which has been stated below:

Presentation of grants related to assets

As per para 24, government grants related to assets, including non-monetary grants at fair value, shall be presented in the balance sheet by setting up the grant as deferred income.

As per para 26, the grant set up as deferred income is recognised in profit or loss on a systematic basis over the useful life of the asset.

If it is determined that the grant is related to income then the same shall be presented as follows:

Presentation of grants related to income

As per para 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.

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It may be further noted that as per paragraph 12 of Ind AS 20, government grants shall be accounted as follows:

As per para 12, 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.

In the given case, if based on the terms and conditions of the scheme, the grant received is to compensate the import cost of assets subject to an export obligation as prescribed in the EPCG Scheme; recognition of grant in the statement of profit and loss should be linked to fulfilment of associated export obligations.

However, if the grant received is to compensate the import cost of the asset and based on the examination of the terms and conditions of the grant, if it can be reasonably concluded that conditions relating to export of goods are subsidiary conditions, then it is appropriate to recognise such grant in profit or loss over the life of the underlying asset.

4. Paragraph 2 of Ind AS 20, "Accounting for Government Grants and Disclosure of Government Assistance" inter alia states that the Standard does not deal with government participation in the ownership of the entity.

Since ABC Ltd. is a government company, it implies that government has 100% shareholding in the entity. Accordingly, as per Ind AS 20, the entity needs to determine whether the payment is provided as a shareholder contribution or as a government. Equity contributions will be recorded in equity while grants will be shown in the Statement of Profit and Loss.

Where it is concluded that the contributions are in the nature of government grant, the entity shall apply the principles of Ind AS 20 retrospectively as specified in Ind AS 101 'First Time Adoption of Ind AS'. Ind AS 20 requires all grants to be recognised as income 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. Unlike AS 12, Ind AS 20 requires the grant to be classified as either a capital or an income grant and does not permit recognition of government grants in the nature of promoter's contribution directly to shareholders' funds.

5. Accounting treatment for:

1. First Grant

The first grant for 'Clear River Project' involving research into effects of various chemicals waste from the industrial area in Madhya Pradesh, seems to be unconditional as no details regarding its refund has been mentioned. Even though the research has not been started nor any major steps have been completed by Rainbow Limited to commence the research, yet the grant will be recognised immediately in profit or loss for the year ended 31st March, 20X2.

Alternatively, in case, the grant is conditional as to expenditure on research, the grant will be recognised in the books of Rainbow Limited over the year the expenditure is being incurred.

2. Second Grant

The second grant related to commercial development of a new equipment is a grant related to depreciable asset. As per the information given in the question, the equipment will be available for sale in the market from April, 20X3. Hence, by that time, grant relates to the construction of an asset and should be initially recognised as deferred income.

The deferred income should be recognised as income on a systematic and rational basis over the asset's useful life.

The entity should recognise a liability in its balance sheets as at 31st March, 20X2 and 31st March, 20X3. Once the equipment starts getting used in the manufacturing process, the deferred grant income of ₹ 100,000 should be recognised over the asset's useful life to compensate for depreciation costs.

Alternatively, as per Ind AS 20, Rainbow Limited would also be permitted to offset the deferred income of ₹ 100,000 against the cost of the equipment as at 1st April, 20X3.

3. For flood related compensation

Rainbow Limited will be able to submit an application form only after 31st May, 20X2 ie in the year 20X2-20X3. Although flood happened in September, 20X1 and loss was incurred due to flood in the year 20X1-20X2, the entity should recognise the income from the government grant in the year when the application form related to it is submitted and approved by the government for compensation.

Since, in the year 20X1-20X2, the application form could not be submitted due to adoption of financials with respect to sales figure before flood occurred, Rainbow Limited should not recognise the grant income as it has not become receivable as at 31st March,20X2.

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6. (a) **When grant is treated as deferred income**

Statement of profit and loss – An extract

	₹
Depreciation (₹ 1,00,000 x 20%)	(20,000)
Government grant credit (W.N.1)	3,000

Balance Sheet - An extract

		₹
Non-current assets		
Property, plant and equipment	1,00,000	
Less: Accumulated depreciation	(1,00,000 x 20%) (20,000)	80,000
		XXXX
Non-current liabilities		
Government grant	[12,000 – 3,000 (current liability)]	9,000
Current liabilities		
Government grant	(15,000 x 20%)	3,000
		XXXX

Working Note:

1. Government grant deferred income account

	₹		₹
To Profit or loss (15,000 × 20%)	3,000	By Grant cash received	15,000
To Balance c/f	12,000		
	15,000		15,000

(b) **When grant is deducted from cost of the asset**

Statement of profit and loss – An extract

	₹
Depreciation [(₹ 1,00,000 – 15,000) x 20%]	(17,000)

Balance Sheet – An extract

		₹
Non-current assets		
Property, plant and equipment	(1,00,000-15,000) 85,000	
Less: Accumulated depreciation	(17,000)	68,000

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