

Accounting for Government Grant

AS 12

Practice Questions [PQ]

PQ 1: ₹ 100 lakhs received from the Central Govt. as subsidy for setting up a Plant in backward area. Cost of Plant ₹ 500 Lakh.

Answer: As per AS 12, government grant of the nature of promoter's contribution should be credited to capital reserve and treated as a part of shareholders' fund.

In this case grant of ₹ 100 lakh is in nature of promoters' contribution hence it should be credited to Capital Reserve which can neither be distributed as dividend nor considered as deferred income.

PQ 2: (2 marks Nov 08) How would you record a non-monetary grant received from the government as per AS 12?

Answer: According to Para 7.1 of AS 12 "Accounting for Government Grants", government grants may take the form of non-monetary assets such as land or other resources, given at concessional rates. In these circumstances, it is usual to account for such assets at their acquisition cost. Non-monetary grants given free of cost are recorded at a nominal value.

PQ 3: A fixed asset is purchased for ₹ 30 lakhs. Government grant received towards it is ₹ 12 lakhs. Residual Value is ₹ 6 lakhs and useful life is 4 years. The company charges depreciation based on Straight-Line method. Asset is shown in the balance sheet net of grant. After 1 year, grant becomes refundable to the extent of ₹ 7.5 lakhs due to non-compliance with certain conditions. You are required to give necessary journal entries for second year.

Answer:

Journal Entries

(₹ in lakhs)

| Year | Particulars | (Dr.) | (Cr.) |
|------|---|-------|-------|
| 2nd | Fixed Asset Account | 7.5 | |
| | To Bank Account | | 7.5 |
| | (Being government grant on asset partly refunded which increased the cost of fixed asset) | | |

| | | |
|--|-----|-----|
| Depreciation Account (W.N.) To Fixed Asset Account (Being depreciation charged on SLM on revised value of fixed asset prospectively) | 5.5 | 5.5 |
| Profit & Loss Account To Depreciation Account (Being depreciation transferred to Profit and Loss Account at the end of year 2) | 5.5 | 5.5 |

Working Note: Depreciation for Year 2

| | ₹ in lakhs |
|---|------------|
| Cost of the Asset | 30 |
| Less: Government grant received | (12) |
| | 18 |
| Less: Depreciation for the first year [18-6/ 4] | 3 |
| | 15 |
| Add: Government grant refundable | 7.5 |
| | 22.5 |
| Depreciation for the second year [(22.5-6) /3] | 5.5 |

PQ 4: How the refund of government grant related to revenue should be treated in the books?

Answer:

Para 11 of AS 12, "Accounting for Government Grants", explains treatment of government grants in following situations:

(a) When deferred credit account has a balance: the amount of government grant refundable will be adjusted against unamortized deferred credit balance remaining in respect of the grant. To the extent that the amount refundable exceeds any such deferred credit the amount is immediately charged to profit and loss account.

(b) where no deferred credit account balance exists: the amount of government grant refundable will be charged to profit and loss account.

PQ 5: How government grant related to specific fixed asset should be treated in the books?

Answer: In accordance with AS 12, Government grants related to specific fixed assets should be presented in the balance sheet by showing the grant as a deduction from the gross value of the assets concerned in arriving at their book value.

- ⇒ Where the grant related to a specific fixed asset equals the whole, or virtually the whole of the cost of the asset the asset should be shown in the balance sheet at a nominal value.
- ⇒ Alternatively, government grants related to depreciable fixed assets may be treated as deferred income which should be recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset, i.e. such grants should be allocated to income over the periods and in the proportions in which depreciation on those assets is charged.
- ⇒ Grants related to non-depreciable assets are credited to capital reserve under this method as there is usually no charge to income in respect of such assets.
- However, if a grant related to a non-depreciable asset requires the fulfillment of certain obligations, the grant is credited to income over the same period over which the cost of meeting such obligation is charged to income. The deferred income is suitably disclosed in the balance sheet pending its apportionment to profit and loss account.

PQ 6: How the refund of government grant related to specific fixed asset should be treated in the books?

Answer:

- (a) Where at the time of receipt the amount of government grant reduced the cost of asset: the amount of government grant refundable will increase the book value of the asset.
- (b) where at the time of receipt, the amount of government grant was credited to "deferred grant account" the amount of government grant refundable will reduce the capital reserve or unamortized balance of deferred grant account as appropriate.

PQ 7: How the refund of government grant related to promotor's contribution should be treated in the books?

Answer:

The amount of government grant refundable in part or in full on non-fulfillment of specific conditions, the relevant amount recoverable by the government will be reduced from capital reserve.

A government grant that becomes refundable is treated as an extra-ordinary item.