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ACCOUNTING STANDARD – 12

ACCOUNTING FOR GOVERNMENT GRANTS

1. DEFINITIONS

- **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.
- Government here means Central and State Government as well as Local Bodies.
- Government Grant **cannot be utilized to Pay Dividend** amount to the shareholders.
- Tax Exemptions, Deductions are not considered as Grant.

2. RECOGNITION OF GOVERNMENT GRANTS

Recognition of Govt. Grant means recording the Grant either in P&L as Income immediately or any other special treatment as per AS 12.

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

- The entity will **comply with the conditions** attaching to them; and
- The grants **will be received**.

If there is **doubt in complying with the conditions** and grant is already received, then treat it as **liability**:

Bank A/c	Dr.
	To Govt. Grant Liability A/c

Note: if the Grant is receivable in the current year for any previous year expenses already incurred. It should be recognised when it is receivable i.e. entry should be passed in current year only.

3. TYPES AND TREATMENT OF GOVERNMENT GRANTS

Sr. No.	Type of Grant	Treatment
1.	Grants related to Income (Revenue Nature) Examples: - Grant received to pay Salary - To Pay for medical facilities of Staff - To purchase vaccine for employees	(a) (first method) presented as an Income in the statement of profit and loss, either separately or under a general heading such as 'Other income'; 1) Bank a/c Dr To Govt. Grant Income A/c 2) Govt. Grant Income A/c Dr To P&L A/c (OR) (b) (Second method) deducted from Specific Expense A/c if grant received for incurring such Expense only: 1) Bank a/c Dr To Govt. Grant A/c (When grant is received) 2) Govt. Grant A/c Dr To Expense A/c (When Exp.is Incurred Grant is deducted from Expense)
2.	Grant for Expenses or Losses already incurred. or Grant for immediate financial Support (Bailout Package) Ex.: Grant received by Loss making companies	<u>If Un-conditional Grant:</u> Recognise directly to Profit and Loss a/c: 1) Bank A/c Dr. To Govt. Grant Income A/c 2) Govt. Grant Income A/c Dr. To Profit and Loss A/c <u>If Conditional Grant:</u> Deferred and Amortized over the period of fulfillment of conditions (Eg. Transfer to P&L Every year in parts and show un-amortised portion as Liability)
3.	Grant in the form of Promoters' Contribution (just like capital investment) Example: for working in Backward areas	Always transferred to <u>Capital Reserve</u> Bank A/c Dr. To Govt. Grant A/c Govt. Grant A/c Dr. To Capital Reserve A/c

4.	Non-Monetary Grant (In Kind) Example: Land received free of cost or at concessional price	(a) If acquired at Concessional Price, then Recognise the Grant at Actual Price Paid (acquired cost). Asset A/c Dr. To Bank A/c (b) If acquired at free of cost, then Recognise at Nominal Value. Nominal Value may be Rs. 1/- or 10/- Asset A/c Dr. To Capital Reserve A/c (Depreciation should not be charged here)
5.	Grants related to Non-depreciable Assets Example: Cash received for purchase of Land/stock	<u>Conditional Grant:</u> If it requires fulfillment of certain obligations then recognise in P&L a/c over the period of fulfilment of obligation. Dr 1) Bank A/c To Def. Govt. Grant A/c Dr. 2) Def. Govt. Grant A/c To P&L A/c (Amortised on systematic basis) <u>Unconditional Grant:</u> If it doesn't require any fulfillment of obligations in the future period then recognise the grant immediately in P&L a/c. Dr Govt. Grant A/c To P&L A/c
6.	Grants related to depreciable assets Example: Cash received to purchase machine/building/vehicle	<u>Option 1 - Deferred Income</u> Treat it as Deferred Income: Dr 1) Bank A/c To Def. Govt. Grant A/c DGG a/c shall be recognised in P&L a/c on a systematic basis over the useful life of the asset. Dr. 2) Def. Govt. Grant A/c To P&L A/c (Amortised on systematic basis) <u>Option 2 - Deduction from Cost</u> Should be presented by <u>deducting the grant amount</u> from Carrying Amount and depreciation

		shall be charged on net carrying amount after deduction.
	1) Bank A/c	Dr.
	To Govt. Grant A/c	
	2) Govt. Grant A/c	Dr.
	To PPE A/c	

Example: (Non-Monetary Grant)

X Convent wishes to open a school in locality A. It applies to the State authority for grant of land. The State authority grants the land for construction of the purposes of the school construction. The market value of the land is Rs. 20 crores however, the authority provides the land at a nominal cost of Rs. 50 lakhs including cost of registration.

The State authority requires that free education must be provided to the poor children by way of reserving 20% of the seats in the school for such children. There is a reasonable assurance that X Convent has reason to believe it will meet the above stated condition attached to the grant.

Thus, X Convent needs to recognise the cost of the land at its acquisition cost of Rs. 50 lakhs.

4. REPAYMENT (REFUND) OF GOVERNMENT GRANTS

Refund of Govt. Grant is treated as **Extra-ordinary** item as per AS 5.

Following is the treatment of Refund:

If Grant was recognised directly in P&L as income	If Grant was recognised as Deferred Income	If Grant was recognised as reduction from Cost of Asset
Refund of grant is debited to Profit and loss a/c	Refund of grant will be debited to Deferred Grant A/c to the extent of balance available. Any remaining amount of refund will be debited to Profit and loss a/c	Refund of grant will be debited to the same Asset A/c
G. Grant Refunded A/c Dr. To Bank A/c	Deferred Grant A/c Dr. Grant Refund Exp. A/c Dr. To Bank A/c	Asset A/c Dr. To Bank A/c
Profit and Loss A/c Dr. To G. Grant Refunded	Profit and Loss A/c Dr. To G. Grant Refund Exp.	Calculate Revised Depreciation on Asset for Further Years.

5. MCQ's from ICAI Study Material

1. To encourage industrial promotion, IDCI offers subsidy worth Rs. 50 lakhs to all new industries set up in the specified industrial areas. This grant is in the nature of **promoter's contribution**. How such subsidy should be accounted in the books?
 - (a) Credit it to capital reserve
 - (b) Credit it as 'other income' in the profit and loss account in the year of commencement of commercial operations
 - (c) Both (a) and (b) are permitted
 - (d) Credit it to general reserve

2. Government grants that are receivable as compensation for **expenses or losses incurred in a previous accounting period** or for the purpose of giving **immediate financial support** to the enterprise with no further related costs, should be
 - (a) recognised and disclosed in the Statement of Profit and Loss of the period in which they are receivable as an ordinary item.
 - (b) recognised and disclosed in the Statement of Profit and Loss of the period in which the losses or expenses were incurred.
 - (c) recognised and disclosed in the Statement of Profit and Loss of the period in which they are receivable, as an extraordinary item if appropriate as per AS 5.
 - (d) disclosed in the Statement of Profit and Loss of the period in which they are receivable, as an extraordinary item

3. Which of the following is an acceptable method of accounting presentation for a government grant relating to an asset?
 - (a) Credit the grant immediately to Income statement
 - (b) Show the grant as part of Capital Reserve
 - (c) Reduce the grant from the cost of the asset or show it separately as a deferred income on the Liability side of the Balance Sheet.
 - (d) Show the grant as part of general Reserve

4. X Ltd. has received a grant of Rs. 20 crores for the purchase of a qualified machine costing Rs. 80 crores. X Ltd has a policy to recognise the grant as a deduction from the cost of the assets. The expected remaining useful life of the machine is 10 years. Assume that there is no salvage value, and the depreciation method is straight-line. The amount of annual depreciation to be charged as an expense in Profit and Loss Statement will be:

- (a) Rs. 10 crores
- (b) Rs. 6 crores
- (c) Rs. 2 crores
- (d) Rs. 8 crores

5. X Ltd has received a grant of Rs. 20 crores for the purchase of a qualified machine costing Rs. 80 crores. X Ltd. has a policy to recognise the grant as deferred income. The expected remaining useful life of the machine is 10 years.

Assume that there is no salvage value, and the depreciation method is straight-line. The amount of other income to be to be recognised in Profit and Loss Statement will be:

- (a) Rs. 10 crores
- (b) Rs. 6 crores
- (c) Rs. 2 crores
- (d) Rs. 8 crores

ANSWERS	1	2	3	4	5
	a	a	c	b	c