

ACCOUNTING STANDARD

AASB 120

July 2004

Accounting for Government Grants and Disclosure of Government Assistance



Australian Government

**Australian Accounting
Standards Board**

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DIFFERENCES BETWEEN AASB 120 AND AASB 1004 *Page 17*

Australian Accounting Standard AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance* is set out in paragraphs Aus1.1 – 39. All the paragraphs have equal authority. Terms defined in this Standard are in *italics* the first time they appear in the Standard. AASB 120 is to be read in the context of other Australian Accounting Standards, including AASB 1048 *Interpretation and Application of Standards*, which identifies the UIG Interpretations. In the absence of explicit guidance, AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies.

PREFACE

Reasons for Issuing AASB 120

The Australian Accounting Standards Board (AASB) is implementing the Financial Reporting Council's policy of adopting the Standards of the International Accounting Standards Board (IASB) for application to reporting periods beginning on or after 1 January 2005. The AASB has decided it will continue to issue sector-neutral Standards, that is, Standards applicable to both for-profit and not-for-profit entities, including public sector entities. Except for Standards that are specific to the not-for-profit or public sectors or that are of a purely domestic nature, the AASB is using the IASB Standards as the "foundation" Standards to which it adds material detailing the scope and applicability of a Standard in the Australian environment. Additions are made, where necessary, to broaden the content to cover sectors not addressed by an IASB Standard and domestic, regulatory or other issues.

The IASB defines International Financial Reporting Standards (IFRSs) as comprising:

- (a) International Financial Reporting Standards;
- (b) International Accounting Standards; and
- (c) Interpretations originated by the International Financial Reporting Interpretations Committee (IFRIC) or the former Standing Interpretations Committee (SIC).

The Australian equivalents to IFRSs are:

- (a) Accounting Standards issued by the AASB that are equivalent to Standards issued by the IASB, being AASBs 1 – 99 corresponding to the IFRS series and AASBs 101 – 199 corresponding to the IAS series; and
- (b) UIG Interpretations issued by the AASB corresponding to the Interpretations adopted by the IASB, as listed in AASB 1048 *Interpretation and Application of Standards*.

Main Features of this Standard

Application Date

This Standard is applicable to annual reporting periods beginning on or after 1 January 2005. To promote comparability among the financial reports of Australian entities, early adoption of this Standard is not permitted.

First-time Application and Comparatives

Application of this Standard will begin in the first annual reporting period beginning on or after 1 January 2005 in the context of adopting all Australian equivalents to IFRSs. The requirements of AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards*, the Australian equivalent of IFRS 1 *First-time Adoption of International Financial Reporting Standards*, must be observed. AASB 1 requires prior period information, presented as comparative information, to be restated as if the requirements of this Standard had always applied. This differs from previous Australian requirements where changes in accounting policies did not require the restatement of the income statement and balance sheet of the preceding period.

Main requirements

The Standard:

- (a) applies to government grants and assistance received by for-profit entities;
- (b) requires that government grants be recognised as revenues only once there is reasonable assurance that the entity will comply with conditions attaching to the grants and they will be received;
- (c) requires government grants to be recognised as income over the periods necessary to match them with the related costs;
- (d) requires government grants receivable as compensation or for immediate support to be recognised as income when receivable;
- (e) requires government grants related to assets to be presented in the balance sheet as deferred income;
- (f) requires repayments of government grants to be treated as revisions to accounting estimates; and

- (g) requires disclosure of:
 - (i) the accounting policy adopted for government grants;
 - (ii) the nature and extent of government grants recognised and an indication of other forms of government assistance; and
 - (iii) unfulfilled conditions and other contingencies attaching to recognised government assistance.

Differences between this Standard and AASB 1004

The primary difference between this Standard and the AASB Standard that it supersedes, AASB 1004 *Revenue*, relates to the criteria for recognising government grants as revenue.

A more detailed description of the differences between this Standard and AASB 1004 accompanies this Standard under the heading “Differences between AASB 120 and AASB 1004”.

COMPARISON WITH INTERNATIONAL PRONOUNCEMENTS

AASB 120 and IAS 20

AASB 120 is equivalent to IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* issued by the IASB. Paragraphs that have been added to this Standard (and do not appear in the text of the equivalent IASB standard) are identified with the prefix “Aus”, followed by the number of the relevant IASB paragraph and decimal numbering.

Compliance with IAS 20

For-profit entities that comply with AASB 120 will simultaneously be in compliance with IAS 20.

AASB 120 and IPSAS

International Public Sector Accounting Standards (IPSASs) are issued by the Public Sector Committee of the International Federation of Accountants.

There is no specific IPSAS dealing with the receipt of government grants at present.

ACCOUNTING STANDARD AASB 120

The Australian Accounting Standards Board makes Accounting Standard AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance* under section 334 of the *Corporations Act 2001*.

Dated 15 July 2004

D.G. Boymal
Chair – AASB

ACCOUNTING STANDARD AASB 120

ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE

Application

- Aus1.1** This Standard applies to:
- (a)** each for-profit entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;
 - (b)** general purpose financial reports of each other for-profit reporting entity; and
 - (c)** financial reports of a for-profit entity that are, or are held out to be, general purpose financial reports.
- Aus1.2** This Standard applies to annual reporting periods beginning on or after 1 January 2005.
- Aus1.3** This Standard shall not be applied to annual reporting periods beginning before 1 January 2005.
- Aus1.4** The requirements specified in this Standard apply to the financial report where information resulting from their application is material in accordance with AASB 1031 *Materiality*.

- Aus1.5 **When applicable, this Standard supersedes AASB 1004 Revenue as notified in the Commonwealth of Australia Gazette No S 283, 17 June 1998.**
- Aus1.6 AASB 1004 issued in June 1998 remains applicable until superseded by this Standard.
- Aus1.7 Notice of this Standard was published in the *Commonwealth of Australia Gazette* No S 294, 22 July 2004.

Scope

1. **This Standard shall 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 entity 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 entity;
 - (d) government grants covered by AASB 141 *Agriculture*.

Definitions

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

***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.**

***Forgivable loans* are loans which the lender undertakes to waive repayment of under certain prescribed conditions.**

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

***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 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.**

***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.¹**

***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.**

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

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 entity 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 entity may be significant for the preparation of the financial report 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 report with those of prior periods and with those of other entities.

¹ See also UIG Interpretation 110 *Government Assistance – No Specific Relation to Operating Activities*, as identified in AASB 1048 *Interpretation and Application of Standards*.

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, 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.**
8. 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.
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 entity will meet the terms for forgiveness of the loan.
11. Once a government grant is recognised, any related contingent liability or contingent asset is treated in accordance with AASB 137 *Provisions, Contingent Liabilities and Contingent Assets*.
12. **Government grants shall 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 shall 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 entity 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 AASB 101 *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 entity 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 entity. In these circumstances the entity assesses the fair value of the non-monetary asset and accounts for both grant and asset at that fair value.

Presentation of Grants Related to Assets

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.**
25. [Deleted by the AASB]

- 26. The grant is treated as deferred income which is recognised as income on a systematic and rational basis over the useful life of the asset.
- 27. [Deleted by the AASB]
- 28. 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 often disclosed as separate items in the cash flow statement.

Presentation of Grants Related to Income

- 29. Grants related to income are presented as a credit in the income statement.
- 30. [Deleted by the AASB]
- 31. Disclosure of grants may be necessary for a proper understanding of the financial statements. Disclosure of the effect of grants on any item of income which is required to be separately disclosed is usually appropriate.

Repayment of Government Grants

- 32. **A government grant that becomes repayable shall be accounted for as a revision to an accounting estimate (see AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*). Repayment of a grant related to income shall 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 shall be recognised immediately as an expense. Repayment of a grant related to an asset shall be recorded by reducing the deferred income balance by the amount repayable.**
- 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 entity.

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 entity is a government procurement policy that is 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.
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 shall 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 entity has directly benefited; and**
 - (c) **unfulfilled conditions and other contingencies attaching to government assistance that has been recognised.**

Transitional Provisions

40. [Deleted by the AASB]

Effective Date of IAS 20

41. [Deleted by the AASB]

DIFFERENCES BETWEEN AASB 120 AND AASB 1004

This analysis of differences accompanies but is not part of, AASB 120.

This section identifies differences between AASB 1004 *Revenue*² and AASB 120 *Accounting for Government Grants and Disclosures of Government Assistance* under the following headings.

- A: Incompatibilities between AASB 1004 and AASB 120
- B: AASB 1004 is more detailed or restrictive
- C: AASB 120 is more detailed or restrictive
- D: AASB 1004 disclosures are more extensive
- E: AASB 120 disclosures are more extensive

The analysis of differences should not be taken as providing an exhaustive list of differences.

Introduction

AASB 1004 (issued in June 1998) applies to all types of entity, however, this analysis applies only in respect of for-profit entities, which is the scope of AASB 120.

AASB 120 applies to government grants related to biological assets measured at cost, where entities are unable to measure reliably the biological asset at fair value (AASB 141 *Agriculture*, paragraph 30). Government grants related to biological assets measured at fair value less estimated point-of-sale costs are dealt with in AASB 141.

Differences

A. Incompatibilities between AASB 1004 and AASB 120

A.1 Recognition of government grants

AASB 120.7 and 12 requires government grants (other than those related to biological assets measured at fair value less estimated point-of-sale costs under AASB 141) to be recognised as income on a systematic basis over the

² AASB 1004 *Contributions* issued in 2004 is not the subject of this analysis.

periods necessary to match them with the related costs which they are intended to compensate, but only when there is reasonable assurance that:

- (a) the entity will comply with the conditions attaching to them; and
- (b) the grants will be received.

In the case of a government grant for the acquisition or construction of an asset, AASB 120.24 requires the amount of the grant carried forward to be presented as deferred income.

Where a government grant relates to compensation for expenses or losses already incurred or for the purpose of giving immediate financial support with no future related costs the grant is recognised immediately as income in the period when it becomes receivable under AASB 120.20.

Under AASB 1004.5.1 and 9.1 and UIG Abstract 11 *Accounting for Contributions of, or Contributions for the Acquisition of, Non-Current Assets* (paragraphs 6–8), contributions of assets (including contributions that are government grants) are measured at the fair value of the contribution received or receivable and recognised immediately as revenue when:

- (a) the entity gains control of the contribution or the right to receive the contribution (which, in the case of developer or customer cash contributions in price-regulated industries, occurs when the service delivery network is extended or modified consistent with the terms of the contribution);
- (b) it is probable that the economic benefits comprising the contribution will flow to the entity; and
- (c) the amount of the contribution can be measured reliably.

A.2 Repayment of contributions

AASB 120.32 requires a government grant that becomes repayable to be treated as a revision of an accounting estimate in accordance with AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*. Where the grant was for the acquisition or construction of an asset, the repayment is recognised as a reduction in any deferred income balance. In all other cases, the repayment must be first applied against any deferred credit balance in respect of the grant and then, to the extent that the repayment exceeds the deferred credit balance, recognised immediately as an expense.

In contrast, UIG Abstract 11.9 requires a liability and an expense to be recognised in the reporting period in which a present obligation to repay a government grant arises.

B. AASB 1004 is more detailed or restrictive

None noted

C. AASB 120 is more detailed or restrictive

None noted

D. AASB 1004 disclosures are more extensive

None noted

E. AASB 120 disclosures are more extensive

E.1 Nature and extent of government grants

AASB 120.39 requires disclosure of:

- (a) the nature and extent of government grants recognised in the financial report and an indication of other forms of government assistance from which the entity has directly benefited; and
- (b) any unfulfilled conditions and other contingencies attaching to government assistance that has been recognised.

AASB 1004.12.1(a) and 12.1(b)(viii) only have general requirements to disclose the accounting policies adopted for the recognition of revenues and the amount of revenue recognised in relation to contributions of assets.