



HM TREASURY

Financial Reporting Advisory Board Paper

INTERNATIONAL ACCOUNTING STANDARD (IAS) 20: ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE and SIC 10: GOVERNMENT ASSISTANCE – NO SPECIFIC RELATION TO OPERATING ACTIVITIES

Issue:	Implementing IAS 20 and SIC 10.
Impact on guidance:	The proposed text in Annex B relates to the IFRS-based FReM.
IAS/IFRS adaptation?	No – although grants-in-aid are to be accounted for on a cash basis (contrary to the spirit of IAS 20), the paper argues that grants-in-aid do not fall within the scope of IAS 20.
IPSAS compliant?	There is no IPSAS on this topic.
Interpretation for the public sector context?	Minor interpretations – see proposed text for the IFRS-based FReM.
Impact on budgetary regime?	The adoption of IAS 20 will not impact on the budgetary regime.
Alignment with National Accounts	No obvious implications for National Accounts.
Impact on Estimates?	The adoption of IAS 20 will not impact on Estimates.
Recommendation:	The FRAB is invited to consider the points made in the following paragraphs and, subject to their comments, to approve the wording of the proposed text for the IFRS-based FReM.
Timing:	Not yet known: depends on future decision on date for moving to EU-adopted IFRS.

DETAIL

Background

1. IAS 20 is long established and became operative for financial statements covering periods beginning on or after 1 January 1984. It provides guidance on the accounting treatment of government grants (which is very similar to that in the equivalent standard in the United Kingdom - SSAP 4) and on the disclosure requirements for government grants and other forms of government assistance. A programme to amend IAS 20 was considered but has been deferred pending completion of other related projects, although an exposure draft is expected in the second half of 2007.

2. IAS 20 (paragraph 2(c)) does not apply to "government participation in the ownership of the entity" and hence will apply only to those grants and (less likely) grants-in-aid that are given in exchange for goods or services. As previously agreed, grants-in-aid (whether for capital or revenue purposes) should be treated as contributions from controlling parties and credited to reserves as they are given to support the general revenue or capital expenditure of the entity.

3. IAS 20's definitions of "government assistance", "government grants", and "grants related to assets" are given in Annex A attached. IAS 20 does not distinguish between "grant" and "grant-in-aid" and, as the treatment of each type of assistance may be different, the proposed wording for the IFRS-based FReM draws the necessary distinctions.

Impact on disclosures in resource and other accounts

4. IAS 20 requires the disclosure of information about the accounting policies adopted and methods of presentation in respect of government grants; the nature and extent of government grants recognised; and details of any unfulfilled conditions and other contingencies attaching to government assistance. It is not expected that these requirements will result in any disclosures additional to those provided at present.

IAS/IFRS compliance

5. IAS 20 requires government grants in respect of revenue expenditure to be credited to income, and those in respect of capital expenditure either to be credited to deferred income or deducted from the cost of the asset. As previously agreed in connection with the application of SSAP 4, the option of deducting grants or grants-in-aid from the cost of the asset is not permitted.

6. In order to conform to the treatment in Estimates, grants-in-aid should be recognised on a cash basis, notwithstanding the requirements in IAS 20 (and IAS 1) that the accruals basis should be adopted. Grants may be accounted for on an accruals basis so long as the conditions in *Government Accounting* are satisfied.

IPSAS compliance

7. There is no IPSAS on this topic.

Proposed text for the IFRS-based Government Financial Reporting Manual

8. See Annex B for the proposed text for the IFRS-based FReM.

Impact on the budgetary regime

9. Applying IAS 20 will have no impact on the budgetary regime which recognises the expenditure of an NDPB rather than the grants-in-aid given to the NDPB.

Other points

10. IAS 20 has been the subject of an interpretation by the Standards Interpretation Committee (SIC-10 *Government Assistance – No Specific Relation to Operating Activities*). The interpretation concerns the treatment of government assistance which is given to encourage or provide long-term support to business activities either in certain regions or industry sectors. Although such assistance may not be specifically related to the operating activities of the entity, the consensus was that it meets the definition of government grants even though there may be no conditions other than a requirement to operate in certain regions or industry sectors. SIC 10 notes that such grants should not be credited to equity.

11. It is considered unlikely that entities falling within the scope of the FReM will be eligible to receive such government assistance.

Summary and recommendation

12. This paper considers the implications of IAS 20 and SIC 10 and recommends that it be adopted, subject to a minor interpretation to allow grants to be credited to a government grant reserve rather than to deferred income. Grants-in-aid are to be accounted for on a cash basis for consistency with the current Estimates arrangements

13. The FRAB is invited to consider the points made in the paper and, subject to its comments, approve the suggested wording for the IFRS-based FReM

HM Treasury
31 October 2006

DEFINITIONS

Government Assistance

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 purposes of this Standard [IAS 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 grants

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 which cannot be distinguished from the normal trading transactions of the entity.

Grants related to assets

Government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may be attached restricting the type or location of the assets or the periods during which they are to be acquired or held.

ANNEX B

PROPOSED TEXT FOR THE IFRS-BASED GOVERNMENT FINANCIAL REPORTING MANUAL

IAS 20: ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE and SIC 10 GOVERNMENT ASSISTANCE – NO SPECIFIC RELATION TO OPERATING ACTIVITIES

Applicability

IAS 20 and SIC 10 apply, as interpreted.

Objectives of IAS 20

The Standard and the Interpretation apply when accounting for, and disclosing, government grants and in the disclosure of other forms of government assistance, including assistance provided which has no specific relation to the operating activities of the entity. IAS 20 does not apply to "government participation in the ownership of the entity", ie grants-in-aid or (less likely) grants given to support the general revenue and capital expenditure of an entity.

Interpretation of IAS 20 for the public sector context

The following interpretation of IAS 20 applies to entities required to prepare their financial statements in accordance with the guidance in this Manual:

- Entities receiving a grant (not grant-in-aid) to fund the purchase of a specific asset should credit that grant to a government grant account which should be released to income over the useful life of the asset. The option provided in IAS 20 to offset the grant against the cost of the asset is not available.

Other requirements

The following requirements should be observed by entities required to prepare their financial statements in accordance with the guidance in this Manual:

- The notes to the financial statements should distinguish between grants from UK Government entities and those from the European Union;
- As it is important for monitoring and control purposes, entities in receipt of a grant or a grant-in-aid that is intended to finance both revenue and capital expenditure should analyse the grant or grant-in-aid between its constituent parts (notwithstanding that the grant or grant-in-aid will be credited to reserves);

Summary of accounting treatment

Grants-in-aid and grants should be accounted for as follows:

- **Grants-in-aid**, whether for revenue or capital purposes, are to be treated as contributions from controlling parties giving rise to a financial interest in the residual interest of the body, and are to be credited to general reserves and not to, respectively, income or deferred income. In the case of grants-in-aid for capital purposes, it will not be necessary to release amounts to the income and expenditure account to offset the depreciation charge.
- **Grants for revenue purposes** will normally be accounted for in the same way as grants-in-aid, unless it can be demonstrated that they are provided in return for specific goods or services, in which case they are to be credited to income. Any proposal to account for grants as income should be approved by the department responsible for the NDPB and the relevant authority.
- **Grants provided to finance the purchase of a specific fixed asset** are to be credited to a government grant reserve which is released to income over the useful economic life of the asset.
- On disposal of an asset financed by a **grant**, the profit or loss is taken to the income and expenditure account/operating cost statement and is offset by a transfer from the government grant reserve of the same proportion of the profit or loss that the amount of the grant bears to the original acquisition cost of the asset. The balance on the government grant reserve in respect of that asset should be transferred to the income and expenditure reserve/general fund representing that same proportion of the proceeds. The profit or loss on disposal of an asset financed by a **grant-in-aid** is simply taken to the income and expenditure account/operating cost statement.
- **Grant-in-aid** is provided to match the recipient's cash needs and is to be accounted for on a cash basis, except in somewhat exceptional circumstances where a recipient has spent the money by the end of the year, and the amount of the accrual is within the department's resource allocation for grant-in-aid. In line with the provisions of *Government Accounting* (9.4.2) any voted provision for grant-in-aid that has not been paid by the sponsoring department by the end of the financial year must be surrendered to the Consolidated Fund. Once the grant-in-aid has been paid over to the recipient, any unspent balances held by the recipient are not liable for surrender to the Consolidated Fund at the year-end. The accounting treatment of **grants** is given in section 9.3.1 of *Government Accounting*.