

MODULE INSTRUCTOR

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Block D-Admission Office

Topics to be covered

- 1.1 Apply IAS 10 to report events after reporting period.
- 1.2 Apply IFRS 10 and IFRS 3 in preparation of financial reports of a group
- 1.3 Apply IFRS 11 to Account for Joint Arrangements
- 1.4 Apply IAS 28 to Account for Investment in Associate and Joint ventures
- 1.5 Apply IFRS 12 to Account for disclosure of interests in Other Entities
- 1.6 Apply IAS 20 to record, analyze and report transactions relating to Government Grant and Government Assistance
- 1.7 Apply IAS 23 in recognizing borrowing costs

Mode of delivery and advise

- Lectures
- Tutorials
- Access of materials on eLearning (everyone must register in a class)
- Class attendance should be at least 75% to succeed in this module
- Taking notes from what is demonstrated in a lecture is crucial for this module (Slides are only a summary)

ASSESSMENT

- ASSIGNMENT(S) – 10%
- TUTORIALS 3%
- QUIZZES-WEB BASED – 7%
- TEST – 20%
- END OF SEMESTER EXAM – 60%
- No Marks will be rewarded for non participants (Zero is also a Mark)

TOPIC 1: IAS 20: ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE

INTRODUCTION

Traditionally there has been a significant amount of 'government money' available for businesses to:

- help with capital expenditure
- stimulate business growth through technological innovation
- support the export of goods and services
- recruit and train new and current employees

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- **Effective date:** 1 January 1984
 - **What it does:**
 - It ***defines government grants, government assistance,*** government, grant related to assets, grants related to income and forgivable loans.
 - It states ***conditions for recognition of grants and measurement*** of non-monetary government grants.
 - It outlines ***presentation rules*** for:
 - Grants related to assets;
 - Grants related to income.
 - It describes how to deal with ***repayments*** of government grants.
 - It sets the ***disclosures*** in respect of government grants and assistance.

IAS 20 Accounting for Government Grants and Disclosure of Government Assistance

International Accounting Standard 20



*IAS 20 Accounting for
Government Grants and Disclosure
of Government Assistance*

=> 1 January 1984



Objective

=> To prescribe the accounting for and disclosure of



Government grants



Government assistance

EXCLUSIONS:

Tax reliefs

Agricultural grants

Government as part-owner

Changing prices

IAS 20 ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE

Key definitions:

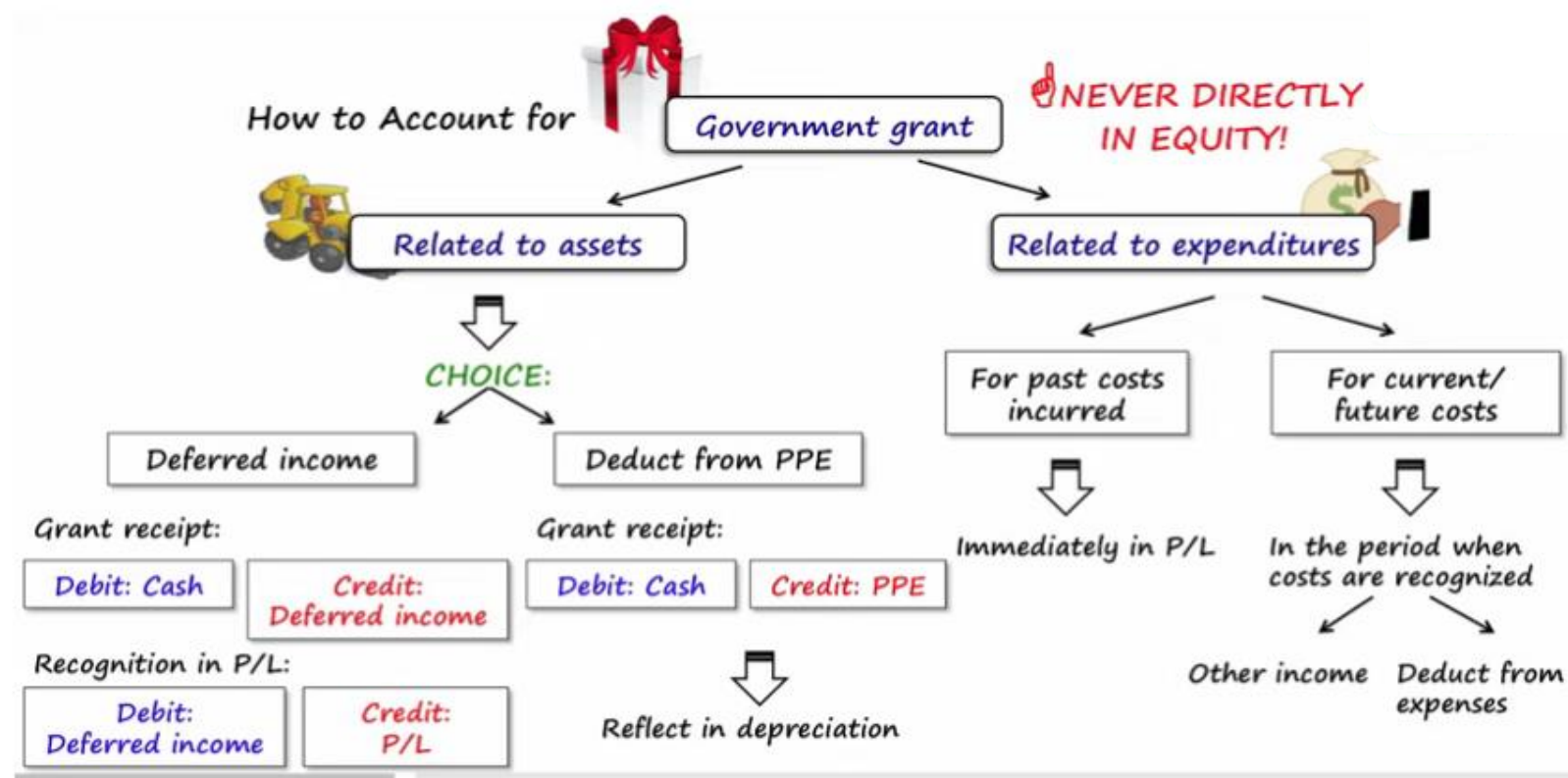
- ***Government*** – includes local and national agencies
- ***Government grants*** – assistance in the form of transfers of resources in return for past or future compliance with conditions relating to operating activities
- ***Government assistance*** – action designed to provide economic benefits when qualifying criteria are met

General principles

- Government grants should **not** be recognised in SPLOCI until there is reasonable assurance that:
 - Entity will comply with conditions
 - Grants will be received
- Grants should be recognised in SPLOCI 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
- Government grants should **not** to be credited to equity
- Government grants relating to past expenses or losses, or for immediate financial support, should be taken to SPLOCI

IAS 20 Accounting for Government Grants and Disclosure of Government Assistance

International Accounting Standard 20



Government grants – question:

ABC receives the following government grants in 2022:

1. Grant of TZS 40,000,000 to acquire a water cleaning station. The cost of the station was TZS 100,000,000 and its useful life is 8 years. ABC acquired the station on 1 July 20X2 and recognized depreciation on a straight-line monthly basis.
2. Grant of TZS 10,000,000 to cover the expenses for ecological measures during 2022 – 2025. ABC assumes to spend TZS 3,000,000 in 2022-2025 and TZS 2,000,000 in 2026 (TZS 14,000,000 in total).
3. Grant of TZS 3,000,000 to cover the expenses for ecological measures made by ABC in 2020-2021.

Required: Prepare the journal entries in the year ended 31 December 2022.

Suggested Solution

As there are 3 different grants, let's solve them one by one.

1. Grant for a water cleaning station

This grant is a typical grant to acquire property, plant and equipment. As written above, we have 2 choices to present it:

Option #1: Deferred income

ABC can credit the grant to deferred income and amortize it over the useful life of a water cleaning station in order to match the grant income with the relevant costs (in this case depreciation charges).

In 2022, ABC recognizes ***TZS 2,500,000 in profit or loss*** (calculated as the grant of TZS 40,000,000 divided by 8 years times 6 months in 2022 divided by 12 months in a year: $(40,000,000/8 \times 6/12)$).

Journal entries are

Description	Amount TZS	Debit (Dr)	Credit (Cr)
Receipt of the grant	40,000,000	SFP – Cash/Bank account	SFP – Deferred income
Recognition in P/L in 2022	2,500,000	SFP – Deferred income	P/L – Income from government grant

Option #2: Deduction from an asset

BC can deduct the grant amount to arrive at carrying amount of a water cleaning station. Then its recognition in profit or loss is automatically reflected in depreciation charges.

As a result, the new carrying amount of a water cleaning station upon initial recognition is TZS 60,000,000 (cost of TZS 100,000,000 less grant of TZS 40,000,000) and the annual depreciation charge is TZS 7,500,000 (TZS 60,000,000 divided by 8) instead of TZS 12,500,000 (TZS 100,000,000 divided by 8). In the first year, it's TZS 3,750,000 (6 months only).

Our journal entries are:

Description	Amount	Debit	Credit
Receipt of the grant	40,000,000	SFP - Cash/Bank account	SFP - PPE (Water cleaning station)
Recognition in P/L in 2022 (within depreciation charge)	3,750,000	P/L - Depreciation of water cleaning station	SFP - PPE (water cleaning station)

2. Grant for ecological measures in 2022-2025

Apparently, the second grant is provided to reimburse the expenses for ecological measures in 2022 to 2025. In other words, it is a ***grant for current and future expenses***.

ABC needs to recognize the income from grant in the periods when relevant expenses are incurred.

In this example, we can calculate the portion recognized in P/L in 2022 on a proportionate basis, i.e. assumed TZS 3,000,000 in 2022 divided by total assumed expenses of TZS14,000,000 times the grant of TZS10,000,000.

The credit entry goes in profit or loss, but here, ABC has a choice to present the grant income as a separate line item (that's easier) or to deduct it from the expenses.

The journal entries are:

Description	Amount	Debit	Credit
Receipt of the grant	10,000,000	SFP - Cash/Bank account	SFP - Deferred income
Recognition in P/L in 2022	2,142,857 (3,000,000/14,000,000*10,000,000)	SFP - Deferred income	P/L - Income from grants (or relevant expense)

Grant for ecological measures in 2020-2021

The third grant relates to the expenses that had already been incurred in the previous years 2020 and 2021.

As a result, the grant is recognized immediately in profit or loss

The journal entry is:

Description	Amount	Debit	Credit
Receipt of the grant	3,000,000	SFP - Cash/Bank account	P/L - Income from government grant

Grants related to income

IAS 20 allows two possible treatments:

1. Present as a credit in SPLOCI, either separately or under a general heading, such as 'other income', by debiting bank and crediting income; **or**
2. Deduct from the related expense, by debiting bank and crediting expense.

e.g. training costs

Disclosure may be necessary for proper understanding of the financial statements

Grants related to income

In 2022 a company incurred training expenses of TZS500,000 and received a grant towards 10% of this cost.

Requirement

How should the grant be accounted for under the two methods allowed in IAS 20?

Grants related to income

<i>Method (i):</i>	TZS
Gross Profit	X
plus: Other Income	<u>50,000</u>
	X
Less: Expenses	
Training Expenses	<u>(500,000)</u>
Net Profit	<u>X</u>
 <i>Method (ii):</i>	 TZS
Gross Profit	X
Less: Expenses	
Training Expenses	
(500,000-50,000)	<u>(450,000)</u>
Net Profit	<u>X</u>

Grants related to assets

For example, certain categories of capital expenditure on PPE

Credit grant to revenue in SPLOCI – P/L over the useful life of the asset to which it relates by:

1. Reducing the cost of the PPE by the amount of the grant and depreciating the 'net' cost; (ie Deducting the grant in arriving at the carrying value of the asset, in which case the grant is recognised in income over the life of the asset by way of a reduced depreciation charge.) **or**
2. Treating the amount of the grant as a deferred credit in SFP, a portion of which is transferred to SPLOCI – P/L annually over the life of the **asset**(ie Present the grant as deferred income which is recognised as income on a systematic and rational basis over the useful life of the asset) .

Government grants – question:

ABC receives the following government grants in 2022:

1. Grant of TZS 40,000,000 to acquire a water cleaning station. The cost of the station was TZS100,000,000 and its useful life is 8 years. ABC acquired the station on 1 July 2022 and recognized depreciation on a straight-line monthly basis.
2. Grant of TZS10,000,000 to cover the expenses for ecological measures during 2022 – 2025. ABC assumes to spend TZS 3,000,000 in 2022-2025 and TZS2,000,000 in 2026 (TZS 14,000,000 in total).
3. Grant of TZS, 3,000,000 to cover the expenses for ecological measures made by ABC in 2020-20X2.

Required: Prepare the journal entries in the year ended 31 December 2022.

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- The profits recorded under both approaches will be exactly the same in each financial period.

EXAMPLE

- Rahara Ltd purchased a piece of equipment for TZS600,000 on the 1st January 2021. The equipment is expected to have an economic life of 5 years and will have no residual value. Depreciation is calculated on a straight-line basis over the life of the asset. The company received a government grant of TZS 200,000 towards the purchase of the equipment. The financial year end of the company is December 31st each year

Required:

Show the relevant extracts from the financial statements for the years ended 31/12/21 & 31/12/22 under each of the two allowable methods of presentation.

Method 1: Set up a deferred grant income account.

This involves opening a deferred grant income account when the grant is received:

Dr Bank TZS 200,000

Cr Deferred grant income account TZS
200,000

A portion of the deferred grant income is transferred to the Income Statement as income, each year over the useful life of the asset. In this example (TZS 200,000/5years) TZS 40,000 will be transferred to the Income Statement each year. At the end of December 2021 the remaining balance in the deferred grant income account is (TZS 200,000 – TZS 40,000) TZS160,000 and this must be recorded as a liability in the balance sheet. This liability must be split between non-current liabilities (TZS120,000) and current liabilities (TZS40,000). At the end of December 2022 two years deferred income will have been transferred to the Income Statement and the remaining balance in the deferred grant income account is

(TZS200,000 - TZS40,000 - TZS40,000) TZS120,000. This balance must then be split between noncurrent liabilities (TZS80,000) and current liabilities (TZS40,000).

Income Statement Extract of Rahara Ltd for the year ended:

31/12/21 31/12/22

Depreciation (TZS600,000/5 years)	(120,000)	(120,000)
Deferred grant income	40,000	40,000

Balance Sheet extract of Rahara Ltd as at:

	31/12/21	31/12/22
	TZS	TZS
Non-current Asset		
Equipment	480,000	360,000
Non-Current Liabilities		
Deferred grant income	120,000	80,000
Current Liabilities		
Deferred grant income	40,000	40,000

Deducting the grant in arriving at the carrying value of the asset

Under this method the cost of the asset of TZS600,000 is reduced by the value of the grant of TZS200,000 to give an initial carrying value of the asset of TZS400,000. This will result in a reduced annual depreciation charge of $(TZS400,000/5 \text{ years})$ TZS80,000.

Income Statement Extract of Rahara Ltd for the year ended:

	31/12/21	31/12/22
	TZS	TZS
Depreciation $(TZS400,000/5 \text{ years})$	(80,000)	(80,000)

Balance Sheet extract of Rahara Ltd as at:

	31/12/21	31/12/22
	TZS	TZS
Non-current Asset		
Equipment	*320,000	**240,000

* NBV of equipment at 31/12/21 is $[400,000 - 80,000]$ 320,000.

** NBV of equipment at 31/12/22 is $[400,000 - 80,000 - 80,000]$ 240,000.

2: Grants related to assets

Company A purchases a machine for TZS120,000. It received a grant towards 20% of the cost of the machine. The machine has an expected life of 3 years with an expected nil residual value. Profit for each year is TZS100,000 (before depreciation).

Requirement

How should the grant be accounted for under the two methods allowed in IAS 20?

Grants related to assets

Method (i) - Reducing the cost of the asset:

SPLOCI – P/L	Year 1	Year 2	Year 3
	TZS	TZS	TZS
Profit before depn	100,000	100,000	100,000
Depreciation	<u>(32,000)*</u>	<u>(32,000)</u>	<u>(32,000)</u>
Profit	<u>68,000</u>	<u>68,000</u>	<u>68,000</u>

*(120,000 - 24,000) ÷ 3

SFP	Year 1	Year 2	Year 3
	TZS	TZS	TZS
NCA at Cost	96,000	96,000	96,000
Accumulated Depn	<u>32,000</u>	<u>64,000</u>	<u>96,000</u>
Net Book Value	<u>64,000</u>	<u>32,000</u>	<u>-</u>

Method (ii) - Treating the grant as a deferred credit:

SPLOCI – P/L	Year 1	Year 2	Year 3
	TZS	TZS	TZS
Profit before grant & depn	100,000	100,000	100,000
Depreciation	(40,000)	(40,000)	(40,000)
Grant	<u>8,000</u>	<u>8,000</u>	<u>8,000</u>
Profit	<u>68,000</u>	<u>68,000</u>	<u>68,000</u>
SFP	Year 1	Year 2	Year 3
	TZS	TZS	TZS
Non-current asset (cost)	120,000	120,000	120,000
Accumulated depreciation	<u>40,000</u>	<u>80,000</u>	<u>120,000</u>
Net book value	<u>80,000</u>	<u>40,000</u>	<u>-</u>
Non-current liabilities			
Deferred Y - govt grants	8,000	0	0
Current liabilities			
Deferred Y - govt grants	<u>8,000</u>	<u>8,000</u>	<u>Nil</u>
Closing balance	<u>16,000</u>	<u>8,000</u>	<u>-</u>

3 Changing method

CUISINE Limited acquired certain items of equipment at a cost of TZS100,000 during the year ended 31 December 2020 for which the company received a government grant of 20%. The new accountant has recorded these items in PPE at the net cost to CUISINE. The equipment has a useful life of four years.

Requirement

Illustrate the alternative method for recording the equipment in accordance with IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*.

Current Treatment		Alternative Treatment	Adjustment
TZS		TZS	TZS
Equipment	80,000	100,000	20,000
Depreciation (1/4)	<u>(20,000)</u>	<u>(25,000)</u>	5,000
	<u>60,000</u>	<u>75,000</u>	
Grant received: 20% x TZS100,000 = TZS 20,000			
		DR TZS	CR TZS
DR	Equipment	20,000	
DR	Depreciation (SPLOCI – P/L)	5,000	
CR	Capital grant reserve		20,000
CR	Equipment acc. Depreciation		5,000
DR	Capital grant reserve	5,000	
CR	SPLOCI – P/L		5,000

Recording PPE at 'net' cost is acceptable under IAS 20. The grant is deducted from the asset, and recognised as income each year through the reduced depreciation charge. This creates the same impact as the deferred income approach. The approach adopted should be applied consistently and disclosed in the accounting policies.

Repayment of grants

- A grant becomes repayable should be treated as a revision of an accounting estimate
- If **income-related grant**:
 - Apply against deferred income, with any excess being expensed

Dr	Unamortised deferred credit
Dr	SPLOCI – P/L
Cr	Bank

- If **asset-related grant**:
 - Increase carrying value of the asset (and expense depreciation that would have been incurred or decrease deferred income

Dr	Asset or Unamortised deferred income
Cr	Bank

DISCLOSURES

1. Accounting policy including methods of presentation
2. Nature and extent of recognised grants
3. Indication of other forms of assistance from which the entity has directly benefited
4. Unfulfilled conditions and other contingencies for recognised government assistance