AS 12 - ACCOUNTING FOR GOVERNMENT GRANTS

10

CHAPTER

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1. Objective

Accounting treatment of government grant is generally significant to the entity in preparation of financial statements. This Standard discusses about the appropriate method of accounting for grants and disclosure of information so as to make the financial statements comparable.

Government grants are also called subsidies, cash incentives, duty drawbacks, etc.

2. Scope

This standard is NOT applicable for the following:

(a) The special problems arising in accounting for government grants in financial statements reflecting the effects of changing prices or in the supplementary information of a similar nature;

(b) Government assistance *other than* in the form of government grants; (Refer concept capsule **1**)

(c) Government *participation in the ownership* of the entity; (Government is also the owner)

3. Definitions

Government means local, national or international government, government agencies and similar bodies.

Government grant → is assistance IN CASH or KIND

Why? For past ***or*** future compliance of conditions

Any government assistance, which CANNOT be reasonably valued, is EXCLUDED from the Standard.

> ***Concept capsule 1***
>
> X Ltd. has established a factory in a backward area in Bihar. Generally electricity charges are ₹10 per unit. As per the government policies, the company gets a subsidy of ₹6 in its electricity charges. So the net charges for the company are ₹4 per unit (₹10 – ₹6). Can this be treated as government grant as per AS 12?
>
> ***Suggested Answer***
>
> As per AS 12, Government grant is assistance in cash or kind for past or future compliances of conditions. In the given case, the subsidy is assistance but it is not received in cash or kind. Hence it is not treated as a government grant as per AS 12.

4. Accounting Treatment

The accounting treatment should be based on the nature of the government grant. If the grant is in the nature of the promoter's contribution, it should be transferred to capital reserve and otherwise it is appropriate to recognise in P&L statement.

There are broadly **two approaches** for accounting government grants. These are

1. Capital approach;
2. Income approach.

The following table helps you to identify & understand the nature of grant and accounting treatment for the same.

Capital approach	Income approach
❖ The grant is in the nature of the promoter's contribution towards the capital requirements of the entity at the initial stages.	❖ These are received during the running stage and these grants are received only after compliance of conditions.
❖ Generally received at the initial stage of the entity.	
❖ Repayment is NOT expected in general and NO related costs to get these grants.	❖ These are rarely gratuitous (free of cost). Entity generally incurs expenditure to get these grants.

Capital approach	Income approach
❖ These are NOT earned by the entity and received without relating costs, hence transferred to "***capital reserve***".	❖ The Income-tax Act or other Acts treat these grants as '*income*' in general. ❖ It is logical to recognise as income in P&L statement so as to match the expenditure.

Under the income approach, government grants are recognised in the P&L statement on a ***systematic and rational basis*** over the periods necessary ***to match them with the related costs*** (Matching concept).

5. Recognition of Government Grant

Government Grant is recognised in the books only when **both** of the following conditions are satisfied:

1. When there is ***reasonable assurance*** that the entity will ***comply*** with the conditions; **and**
2. When ***ultimate collection is reasonably certain***.

Mere receipt of grant money is NOT the conclusive evidence. If money is received and entity doesn't have reasonable assurance on compliance of conditions, the entity should NOT recognise grant; it should record the receipt as payable to government.

Concept capsule 2

X Ltd. started its operations in a backward area in Andhra Pradesh with 5 crore. As per the public scheme announced by the State Government, the entity is entitled to receive 20% of its investment as a government grant. The grant money is received during the current year. What is the accounting treatment in the books of X Ltd? (***IPCC- May 2015***)

Suggested Answer

As per AS 12, if the grant is in the nature of the promoter's contribution, it should be transferred to capital reserve.

In the given case, it is in the nature of the promoter's contribution as the grant is received initially for establishing the company; hence it should be transferred to capital reserve by recording the following JE:

Cash/ Bank a/c................ Dr 1 crore
To Capital reserve a/c 1 crore

Concept capsule 3

X Ltd. has received the grant money of ₹5,00,000 on 15-01-2017. The entity has to satisfy some conditions attached to the grant by 31-03-2018. The entity needs to incur the expenditure of ₹3,00,000. (₹50,000 till 31-03-2017 and ₹2,50,000 during 2017-18). If the entity is not able to satisfy the conditions, it has to refund the grant. On 15-01-2017, the entity doesn't have reasonable assurance on satisfying the conditions and the same position continued till 31-03-2017. However, it could satisfy the conditions as on 31-03-2018. Discuss the accounting treatment as on 31-03-2017 & 31-03-2018.

Suggested Answer

As the relevant costs (₹3,00,000) are being incurred, it is logical to recognise the grant as income in P&L statement. As per AS 12, the government grant can be recognised only when there is reasonable assurance on compliance of conditions.

Based on the given information, there is no reasonable assurance, hence the entity should record the money received as payable to the government.

15-01-2017	Cash/Bank a/c …………Dr	5,00,000	
	To Payable to government		5,00,000

The expenditure incurred ₹50,000 as of YE should be charged to P&L statement asset cannot be recognised as it doesn't satisfy the conditions of an asset, i.e., probable future economic benefits inflow does not exist.

As on 31-03-2018

As the entity satisfied the conditions as on balance sheet date, it should recognise the grant as income by recording the following journal entry:

31-03-2018	Payable to government a/c …………Dr	5,00,000	
	To Grant Income (P&L)		5,00,000

The expenditure incurred (₹2,50,000) during 2017-18 should be charged to P&L statement.

Concept capsule 4

X Ltd. is awarded a government grant of ₹6,00,000 receivable over three years (₹4,00,000 in year 1 and ₹1,00,000 in each of years 2 and 3). As part of the conditions, it should create 10 new jobs and maintain them for three years. The cost of recruiting the employees is ₹50,000 and the wage payable to them in year 1 - ₹80,000, Year 2 – 1,10,000 and Year 3 – 1,20,000. The entity has reasonable assurance on satisfying the conditions. What is the accounting treatment for this in the books of the entity?

Suggested Answer

It is logical to account for the grant <u>under the income approach</u> as the related cost is incurred to receive the grant. Under this approach, grant should be recognised in the P&L a/c on a ***systematic and rational basis*** over the periods necessary ***to match them with the related costs*** (matching concept). It should recognise income over three years in proportion to expenses and the balance income as on balance sheet date should be presented as *deferred income* in reserves and surplus.

Total government grant receivable = ₹6,00,000

Year	Estimated Labour cost	Grant to be recognised	Calculations	Deferred Income	Calculation
1	1,30,000	2,16,667	6,00,000 × (130/360)	3,83,333	(6,00,000 - 2,16,667)
2	1,10,000	1,83,333	6,00,000 × (110/360)	2,00,000	(3,83,333 - 1,83,333)
3	1,20,000	2,00,000	6,00,000 × (120/360)	-	(2,00,000 - 2,00,000)
	3,60,000	**6,00,000**			

Journal entries

At the time of receipt of grant

Cash/ Bank a/c …………Dr	4,00,000	
Grant receivable a/c …….Dr	2,00,000	
To Deferred income a/c		6,00,000

At the end of Year 1

Deferred Income a/c ….. Dr	2,16,667	
To Govt. grant income (P&L a/c)		2,16,667

The remaining Deferred income (i.e. 3,83,333) at the end of the first year will be transferred to P&L as described in the above table i.e. year 2 - ₹ 1,83,333 and in year 3 - ₹ 2,00,000.

The expense incurred should be transferred to P&L statement as and when incurred by the entity.

6. Special circumstances

When any entity receives any government grant under the following two situations, such receipt should be ***presented as*** **EXTRAORDINARY ITEM** in the P&L statement. (as per AS 5)

Situation 1: Immediate financial support to only one entity in the industry

- Government grant is received for immediate financial support and NOT for any specific expenditure;
- It is received only by one entity but NOT by the whole class of such entities (Industry); and
- The entity recorded such grant as income in P&L based on the circumstances existing at that time.

Reason: As the grant is received by only one entity in the industry, the performance of the entity may not be comparable with that of others; hence it is presented separately as an extraordinary item.

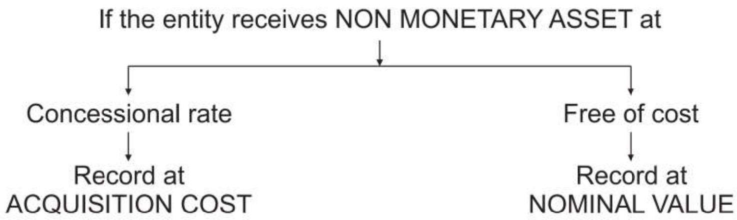
Situation 2: Received for previous year expense or losses:

- Grant is received <u>in the current year</u> as compensation ***for the previous year expenses or losses***; **and**
- It is recognised as income in CY P&L statement.

Reason: Expenses or losses are recognised in PY and income is recognised in CY; to make the financials comparable it is presented separately as an extraordinary item.

7. Non-monetary Government Grants

Government may give grants in the form of non-monetary assets, such as land, buildings or other resources.



Nominal value = small/immaterial amount;

Concept capsule 5

Govinda Ltd. received 20 acres of land from AP Government for ₹5,00,000 per acre. The fair value of the land is ₹12,00,000 per acre. How do you account for the land acquired by the entity? If the same is received by the entity at free of cost what would be the accounting treatment?

Suggested Answer

As per AS 12, Non-monetary government grants should be recorded at acquisition cost if received at concessional rate and at nominal value if received at free of cost.

Land is a non-monetary asset and the entity received at a concessional rate of ₹5,00,000 per acre. The land should be recognised at acquisition cost of ₹1 crore (₹5 lakh × 20 acres) by recording the following journal entry:

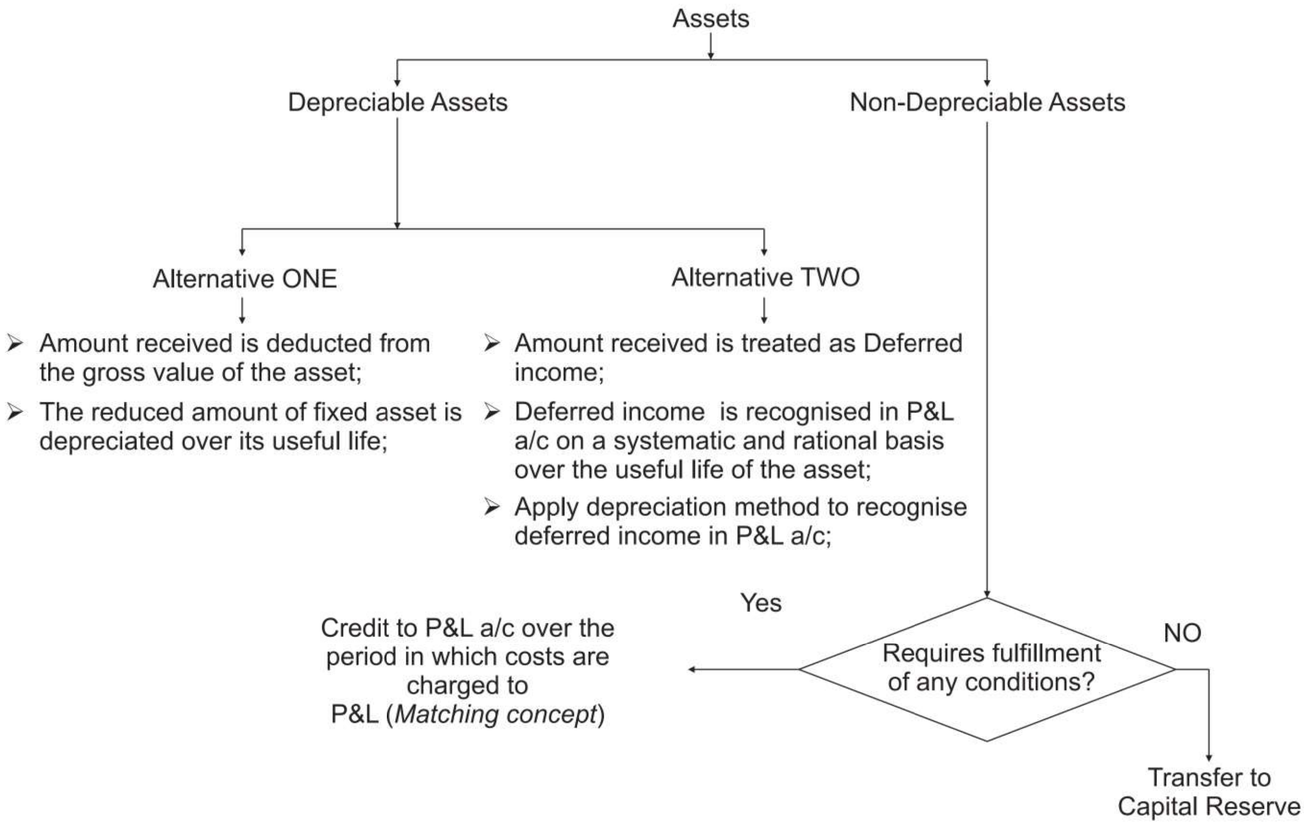
Land a/c …………Dr	1 Crore	
To Cash/Bank a/c		1 Crore

If the same is received at free of cost, it should be accounted at nominal value. i.e. 100 or any immaterial value.

8. Grants Related to Specific Fixed Assets

These grants are related to *specific fixed assets* and these are received when the entity purchases or constructs the asset as per the specifications made by the government.

Accounting treatment is based on the nature of asset i.e. Depreciable **or** Non-depreciable assets. The following diagram helps you to understand the accounting treatment:



If the asset is depreciable, two options are available. The entity can select any one method and can apply the same consistently.

Disclosure of these grants in Balance sheet and Cash flow statement:

Balance sheet disclosure: As per the guidance of the Standard, deferred government grant (Deferred income) should be presented ***after/in*** 'Reserves and surplus' ***before*** 'long-term liabilities'. (Revised Schedule VI)

Cash flow statement (CFS): In cash flow statement, purchase of assets and receipt of grants should be disclosed separately i.e. should NOT disclose net cash flows. E.g. an entity purchased a machine for ₹25 lakh and it received a grant of ₹10 lakh. In CFS it should disclose ₹25 lakh as outflow of cash and ₹10 lakh as inflow of cash separately and it should NOT disclose the net outflow i.e. ₹15 lakh.

Concept capsule 6

Madhava Ltd. purchased a machinery for ₹5,00,000 as on 01-04-2018. It received ₹2,00,000 from the government for acquisition of the asset. As per the accounting policy, the company follows the SLM method of depreciation – 10 years life –Residual value is Nil. Discuss the options of accounting for the government grant as per AS 12 with the help of journal entries. (***PCC May 2012***)

Suggested Answer

As per AS 12, when a grant received relates to a depreciable fixed asset – the entity has two options in accounting for the same. The options are discussed as follows:

Alternative ONE

As per the first method, amount received should be deducted from the gross value of the asset. The reduced balance of asset should be depreciated over the useful life of the asset. The following JE can be recorded:

At the time of acquisition of asset

Machinery a/c ....Dr	5,00,000	
To Cash/Bank a/c		5,00,000

When grant is received

Cash/ Bank a/c ....Dr	2,00,000	
To Machinery		2,00,000

Depreciation JE at the end of Year 1

Depreciation a/c ....Dr	30,000	
To Machinery a/c		30,000
[(5,00,000 – 2,00,000) /10 Years)		

Alternative TWO

As per Second method, the received grant should be treated as a deferred government grant (deferred income) and it should be amortised in a systematic and rational basis over the useful life of the asset.

When grant received

Cash/ Bank a/c ....Dr	2,00,000	
To Deferred government grant a/c		2,00,000

The above JE does not affect the machinery account and its value continues at ₹5,00,000.

At the end of Year 1

Depreciation a/c …………Dr	50,000	
To Machinery a/c		50,000
(5,00,000 / 10 years)		
P&L a/c …………………..Dr	50,000	
To Depreciation a/c		50,000
Deferred government grant a/c... Dr	20,000	
To P & L a/c		20,000
(2,00,000 /10 years)		

Amortisation of deferred government grant should be done in a systematic and rational basis. In the given situation it is rational to amortise in the same way how the asset is depreciated.

Concept capsule 7

How would you treat the Government Grant received relating to a depreciable asset under the following cases as per AS 12?

Case 1: Gross value of asset is ₹2 crore and Grant received is ₹20 lakh only.

Case 2: Gross value of asset is ₹2 crore and Grant received is ₹2 crore.

Suggested answer

Case 1: As per AS 12, Govt. Grant related to a specific asset can either be deducted from the gross value of fixed assets or credited to Deferred Grant A/c.

Therefore, the grant of ₹20 lakh can be credited to fixed assets a/c or to Deferred Grant a/c. The balance of ₹1.8 crore should be shown as an asset in the Balance Sheet and Depreciation should be charged on ₹1.8 crore.

Case 2: If the grant received is equal to the cost of the asset, then

(i) If it is deducted from cost of the asset, then the Asset should be recorded at a Nominal Value. NO Depreciation is to be charged in this case.

(ii) If it is credited to Deferred Grant a/c, then it must be recognized in the Profit & loss A/c on a systematic basis over the useful life.

9. Revenue grants presentation in P&L

Revenue grants can be presented in two ways as discussed below:

1st Method

Present as income in the profit and loss statement as "**other income**" and NOT as part of REVENUE.

2nd Method

Grant received can be deducted from the related expense in P&L.

Adding to Sales revenue is NOT a fair presentation. Always present the grant income separately.

Concept capsule 8

Fertilizers Ltd receives subsidy from the government on sale of certain fertilizers at a discounted price. The subsidy is a compensation for loss of revenue, and consequently, Fertilizers Ltd. wants to disclose it as revenue. Is that an appropriate accounting treatment?

Suggested Answer

As per AS 12, government grants related to revenue should be recognised on a systematic basis in P&L statement, over the periods necessary to match them with the related costs. Such grants should either be shown separately under 'other income' or alternatively it should be deducted from the related expense.

In the given case, the entity wants to disclose it as sales revenue which is NOT in compliance of AS 12. Presenting it as "other income" is appropriate.

10. Refund of Government grant

Government grants are generally refundable when the entity does not fulfill certain conditions. Refund of grant is treated as an extraordinary item as per AS 5.

Accounting for refund of grant is based on the **initial** recognition of government grant. At the time of refund the entries so far recorded will be reversed. The following table helps you to understand the accounting on refund of grant:

Initial accounting	Refund accounting treatment
I. *Revenue Grant* **II.** On receipt of grant, if it is initially transferred to Deferred government grant account and subsequently transferred to P&L in a systematic and rational basis over a period of time. (Matching concept)	*If balance exists in deferred government grant (BS)*: ❖ First reverse the existing balance in deferred government grant a/c; ❖ Remaining amount should be charged to P&L. **JE** Deferred Govt. Grant a/c ....Dr (balance in BS) P&L a/c ....Dr (balancing fig.) To Cash/ Bank (Refunded amount) *If NO balance exists in deferred government grant (i.e. it is fully transferred to P&L)*: ❖ Charge total refunded amount to P&L a/c. **JE** P&L a/c ....Dr (Refunded amount) To Cash/ Bank (Refunded amount)
III. ***Capital grant (Capital approach)***: Initially it is transferred to capital reserve a/c	❖ Capital reserve balance should be reversed. **JE** Capital reserve a/c ..... Dr To Cash/ Bank a/c (Refunded amount)
IV. ***Grant related to specific fixed asset***: **A.** ***Depreciable Asset*** **Method 1** ➢ Deducted from the gross value	❖ Add the refunded amount to fixed asset carrying amount; and ❖ Depreciate the increased carrying amount over the remaining useful life of the asset ***prospectively***. **JE** Machinery a/c ..... Dr To Cash/ Bank a/c (Refunded amount)

Initial accounting	Refund accounting treatment
Method 2 ➢ Grant received is credited to deferred government grant a/c and transferred to P&L in a systematic and rational basis over the useful life of the asset.	First utilise the balance existing in deferred government grant a/c and if any balance charge to P&L a/c. **JE** Deferred Govt. Grant a/c … Dr (Balance in BS) P&L a/c …………………Dr (Balancing fig.) To Cash/ Bank (Refunded amount)
B. ***Non-depreciable asset*** ➢ Credited to capital reserve if no conditions need to be satisfied. ➢ If conditions need to be satisfied, initially recognised as deferred govt grant and transferred to P&L in systematic and rational basis so as to match the revenue with expenditure.	Reverse the capital reserve with refunded amount. **JE** Capital reserve a/c ….. Dr To Cash/ Bank a/c (Refunded amount) Refer ***I. Revenue grant refund*** (as discussed above)

Concept capsule 9

X Ltd. received a grant of ₹2 crore from the Central Government for the purpose of special machinery during 2013-14. The cost of Machinery was ₹20 crore and had a useful life of 9 years. During 2017-18 (after 4 years), the grant has become refundable due to non-fulfillment of certain conditions attached to it. Assuming the entire grant was deducted from the cost of machinery in the year of acquisition, state with reasons the accounting treatment to be followed in the year 2017-18.

(PCC Nov. 2007 – modified)

Suggested Answer

As per AS 12, in case of refund of government grant, which was already deducted from the carrying amount, refunded amount should be added to the carrying amount of the asset on the date of refund. The revised book value is depreciated over the remaining useful life of the asset *prospectively*.

In the given case, book value of machinery will be increased by ₹2 crore in 2017-2018. Depreciation for FY 2017-18 onwards continues as follows:

	₹ in crores
Cost of machinery (Initial cost)	20
Less: Grant received (at the time of receipt)	2
Cost of machinery	**18**
Useful life of machinery	9 years
Annual Depreciation as per SLM (₹18/9 years)	2
(Residual value is assumed as zero)	
Total depreciation for 4 years (2013-14 to 2016-2017) (4 × 2)	8
Carrying amount on the date of refund (in FY 2017-2018) (₹18 – 8)	**10**
Add: Grant refunded	2
Revised book value	12
Remaining useful life (9 – 4 years)	5 years
Revised annual depreciation (₹12/5 years)	**2.40**

Thus, book value of machinery will be ₹12 crore in the year 2017-18 and the annual depreciation of ₹2.4 crore will be charged on machinery over remaining five years of life (including 2017-18).

Concept capsule 10

Continuation to the above example, if the company had credited the grant received to deferred government grant (deferred income a/c), discuss the accounting treatment.

Suggested Answer

As per AS 12, if the entity receives a grant specific to a fixed asset, it can credit the amount received to deferred government grant a/c and it can transfer to P&L in a systematic and rational basis over the useful life of the asset. In this case if government grant is refunded, the existing balance in deferred govt. grant should be debited and the balance should be charged to P&L statement.

	₹ in crores
Amount credited to deferred govt. grant a/c when grant received	2
Less: Amount transferred to P&L over 4 years (2013-14 to 2016-2017)	0.89
(2 crores/9 years × 4 years)	
Balance remaining in deferred govt. grant a/c	**1.11**

The JE to be recorded at the time of refund

Deferred govt. grant a/c …………Dr	1.11 crore	
P&L a/c ………………………….Dr	0.89 crore	
To Cash/ Bank a/c		2 crore

As the received grant is credited to deferred govt. grant a/c, it doesn't affect the depreciation computation.

Concept capsule 11

X Ltd. received a revenue grant of ₹10 crore during 2016-17 from Government for welfare activities to be carried on by the company for its employees. The grant prescribed the conditions for utilization. However, during the year 2018-19, it was found that the prescribed conditions were not fulfilled and the grant should be refunded to the Government. State how this matter will have to be dealt with in the financial statements of X Ltd. for the year ended 2018-19.

Suggested answer

As per AS 12, the amount refundable in respect of a government grant related to revenue, is applied first against any unamortised deferred credit remaining in respect of the grant. To the extent that the amount refundable exceeds any such deferred credit, or where no deferred credit exists, the amount is charged immediately to profit and loss statement. Therefore, refund of grant of ₹10 crores should be shown in the profit and loss account of the company as an extra-ordinary item during the financial year 2018-19.

11. Disclosures

The following disclosures are appropriate:

(i) The accounting policy adopted for government grants, including the methods of presentation in the financial statements;

(ii) The nature and extent of government grants recognised in the financial statements, including grants of non-monetary assets given at a concessional rate or free of cost.

Questions & Answers

Question No. 1

S Ltd has received a grant of ₹8 crore from Government for setting up a factory in a backward area. Out of this grant, the company distributed ₹2 crore as dividend. Also, S Ltd received land for free of cost from the State Government but it has NOT recorded it in the books as no money has been spent. Examine whether the treatment is correct. **(*IPCC- May 2010*)**

Answer

As per AS 12, when government grant is received for a specific purpose, it should be utilised for the same. So the grant received for setting up a factory is not available for distribution of dividend. As the company did not satisfy the conditions given, it is liable to repay the same, hence it should recognise the liability for the same amount;

In the second case, even if the company has not spent money for the acquisition of land, land should be recorded in the books of accounts at a nominal value. The treatment of both the grants is incorrect as per AS 12.

Question No. 2

A Ltd company purchased a machinery for ₹40 lakh whose useful life is 4 years and residual value is ₹8 lakhs. It has received a Government Grant of ₹16 lakh. Due to non-compliance of certain conditions, the grant becomes refundable in 3rd year to the extent of ₹12 lakh.

Show the journal entry to be passed at the time of refund and the value of fixed assets, if

(i) The grant is credited to fixed assets

(ii) The grant is credited to deferred grant a/c. ***(CA IPCC – May 2017)***

Answer

As per AS-12, the entries to be passed at *the time of refund* are

Case 1:	Fixed Assets A/c Dr	12,00,000
	To Bank	12,00,000
Case 2:	Profit & Loss A/c Dr	4,00,000
	Deferred Govt. Grant A/c	8,00,000
	To Bank A/c	12,00,000

Question No. 3

On 01.04.2013, ABC Ltd. received Government grant of ₹300 lakh for acquisition of a machinery costing ₹1,500 lakh. The grant was credited to the cost of the asset. The life of the machinery is 5 years. The machinery is depreciated at 20% on WDV basis. The Company had to refund the grant in May 2016 due to non-fulfillment of certain conditions. Assuming the company deducted the grant received from the cost of asset, how would you deal with the refund of grant in the books of ABC Ltd.? **(*CA Inter May 2018*)**

Answer

According to AS 12, the amount refundable in respect of a grant related to a specific fixed asset should be recorded by increasing the book value of the asset or by reducing the capital reserve or deferred income balance, as appropriate, by the amount refundable. As the entity reduced the book value of the asset initially, the book value is increased and depreciation on the revised book value should be provided prospectively over the remaining useful life of the asset.

		₹ *(in lakhs)*
1st April, 2013	Acquisition cost of machinery (₹1,500 – 300)	1,200.00
31st March, 2014	*Less*: Depreciation @ 20%	240.00
	Book value	960.00
31st March, 2015	*Less*: Depreciation @ 20%	192.00
	Book value	768.00
31st March, 2016	*Less*: Depreciation @ 20%	153.60
1st April, 2016	Book value	614.40
May, 2016	*Add*: Refund of grant	300.00
	Revised book value	914.40

Depreciation @ 20% on the revised book value amounting to ₹914.40 lakh is to be provided prospectively over the residual useful life of 2 years ended 31st March, 2017 and 31st March, 2018.

Question No. 4

A Government grant of ₹25 lakh received 3 years ago in respect of a machinery which costs ₹200 lakh, became refundable in March, 2018.

(i) How the **receipt** of grant would have been recorded in the books of the recipient?

(ii) How the **refund** of grant would be reflected in the books, at the time of its refund?

Answer

As per AS 12, government grant related to specific asset can be accounted in two ways. As per the first method, the grant can be deducted from the gross value of the asset. Depreciation on machinery would be charged on the reduced value of ₹175 lakhs. Second method, the grant may be treated as deferred income which should be credited to profit and loss statement on a systematic and rational basis over the useful life of the asset.

As per the standard, the amount refundable in respect of a grant related to a specific fixed asset should be recorded by increasing the book value of the asset **or** by reducing the capital reserve **or** the deferred income balance, as appropriate, by the amount refundable. In the first alternative, i.e., where the book value of the asset is increased, depreciation on the revised book value should be provided prospectively over the residual useful life of the asset.

Question No. 5

Top & Top Limited has set up its business in a designated backward area which entitles the company to receive from the Government of India a subsidy of 20% of the cost of investment. Having fulfilled all the conditions under the scheme, the company on its investment of ₹ 50 crore in capital assets received ₹ 10 crore from the Government in January, 2017 (accounting period being 2016-2017). The company wants to treat this receipt as an item of revenue and thereby reduce the losses on profit and loss account for the year ended on 31st March, 2017.

Keeping in view the relevant Accounting Standard, discuss whether this action is justified or not.

Answer

As per AS-12, where the government grants are of the nature of promoters' contribution, i.e. they are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay (for example, central investment subsidy scheme) and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.

In the given case, the subsidy received is neither in relation to specific fixed asset nor in relation to revenue. Thus it is inappropriate to recognise government grants in the profit and loss statement, since they are not earned but represent an incentive provided by government without related costs. The correct treatment is to credit the subsidy to capital reserve. Therefore, the accounting treatment desired by the company is not proper.

"We could never learn to be brave and patient, if there were only joy in the world"

– Helen Keller

AS 12 : Govt. grants

Govt. assistance in cash/kind for compliance of future/past conditions

To Recognise – 2 conditions to be satisfied

1.Reasonable assurance exists that conditions will be complied; and

2.No uncertainty in ultimate receipt

A/c Treatment

Grant Received

- Cash
- Non-Monetary asset like Land & Building
  - Received at
    - Free of cost
      - Record at nominal value
    - Concessional price
      - At Acquisition rate

Related to

- Specific asset
  - Depreciable asset
    - • Deduct from Gross value
      • Depreciate the balance after deduction
    - • Treat as Deferred grant & Recognise as income in proportion to depreciation
      • Depreciate the asset as usual
  - Non-Depreciable asset
    - No conditions to be fulfilled
      - Credit to Capital Reserve
    - Conditions to be fulfilled
      - Credit to P & L in a systematic manner (Matching concept)
- Revenue expenses
  - *2 Options*
    - Deduct from related expense
    - Credit to P & L as 'Other Income' in a systematic basis (Matching concept)

Refund of Government Grant

- Related to Revenue
  - • Apply first against unamortized deferred GG.
    • Balance (if any) – Debit P & L.
- Relating to promoter's contribution
  - Debit Capital Reserve
- Related to Fixed Asset
  - • Debit to FA &
    • Depreciate the Revised Book Value prospectively over the remaining useful life.
    • Debit from Capital Reserve/ Deferred GG. (if any)

Disclosure

- Accounting Policy followed
- Nature & Extent of GG recognized in FS.