Solution 1.10.

Component: Assets / Property plant and equipment (IAS 20) and Liabilities (IAS 20)

Short title: Accounting for government grants and disclosure of government assistance

Issue

Metals companies often receive investment grants from governments as a contribution towards capital expenditures. The government grant may take the form of a transfer of a non-monetary asset, such as land, for use by the company or cash.

When and how should the company recognise such government grants and how should these grants be measured?

Solution

IAS 20 "Accounting for Government Grants and Disclosure of Government Assistance" provides accounting and disclosure standards for government grants and other forms of government assistance to business enterprises.

The grant should be recognised when there is reasonable assurance that the enterprise will comply with the conditions attached and that the grants will be received [IAS 20.7]. The reporting entity should have fulfilled all conditions attached to the grant.

Grants that require the recipient to purchase, construct, or otherwise acquire long-lived assets, including intangible assets, should be recognised either by setting up the grant as deferred income (a liability) or by deducting the grant from the carrying amount of the asset [IAS 20.24]. Deferred income must be recognised in the income statement on a systematic and rational basis over the useful life of the asset.

Non-monetary grants that are intended to compensate an enterprise for specific costs should be recognised systematically as income over the periods necessary to match those grants with the costs they are intended to compensate [IAS 20.12].

Non-monetary grants (such as transfer of land) may be reported at the nominal amount or at fair value [IAS 20.23]. Grants related to assets may be reported as a reduction in the cost of the asset.

However, valuing non-monetary assets at fair value and recognising an asset with a corresponding deferred income is preferable, as it more fully reflects the substance of the underlying arrangement.

For an illustrative example please refer to the Appendix 3 "Accounting for government grants and disclosure of government assistance".

Appendix 3 "Accounting for government grants and disclosure of government assistance"

The following example serves to illustrate the appropriate accounting.

Assume that at 31 December of 2004 an enterprise received from government a grant in the form of the transfer of a pipeline infrastructure (to be used for hazardous emission) with a fair value of US$ 1,000,000 and estimated useful life of 10 years. The enterprise's accounting policy for grants related to non-monetary assets is to recognise such grants at fair value. The recording entries are the follows:

Year/Accounting	DR, US$	CR, US$
31 December 2004		
Property, plant and equipment	1,000,000	
Deferred income – government grant		1,000,000
31 December 2005		
Depreciation expense	100,000	
Property, plant and equipment – accumulated depreciation		100,000
Deferred income – government grant	100,000	
Amortisation of government grant (income)		100,000