INSTITUTE OF CHARTERED ACCOUNTANTS OF BARBADOS

Guidance Note: Government Grants – Section 24 of the IFRS for SMEs

Governments across the globe have introduced measures to assist businesses impacted by COVID-19. For example, the Government of Barbados introduced the BEST Program in response to COVID-19's social and economic impact on the Barbados tourism sector.

Government assistance can take many forms, for example, subsidized payroll costs, direct cash injections, forgiveness of debt or financing at below market rates. Entities will need to assess the economic substance of any government assistance received to determine the appropriate accounting treatment. Given the unprecedented nature of the pandemic, many entities will not have previously received government assistance and will therefore need to develop an appropriate accounting policy.

Section 24 of the IFRS for SMEs *Government Grants* (herein "Section 24") provides authoritative guidance. However, care should be taken in determining whether the nature of assistance received is covered within the scope of Section 24.

Section 24 is drafted in simple language with less application guidance than is provided in the IFRS equivalent - IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* (herein "IAS 20"). Preparers of financial statements in accordance with the IFRS for SMEs may also wish to review the equivalent guidance note on IAS 20. While there are distinct differences, as highlighted below, it does provide additional context.

(i) Is the government assistance received within the scope of Section 24?

In determining the applicability of Section 24, it is important to consider the definitions of both government assistance and government grants; the latter being a subset of the former. Section 24 defines government assistance as *an action by government designed to provide an economic benefit specific to an entity or range of entities under specified criteria*. A government grant is defined *as assistance by government in the form of a transfer of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity*. These definitions are consistent with IAS 20.

Government grants exclude forms of government assistance which cannot reasonably have a value placed on them and transactions which cannot be distinguished from the normal trading transactions of the entity.

Naturally, it is a prerequisite that the grant should be provided by a government entity. Government is not defined in Section 24. Reference may be made to IAS 20 which defines government broadly to include not only central government, but also government agencies and similar bodies whether local, national, or international.

Finally, there is a specific carve-out from the scope of Section 24 for assistance provided in the form of benefits that are available in determining taxable income/losses or determined or limited on the basis of income tax liability (e.g., tax holidays, reduced tax rates etc.). These measures are covered by Section 29 *Income Taxes*. Whereas IAS 20 does not apply to government participation in the ownership of an entity, Section 24 does not include the equivalent carve out.

(ii) What is the appropriate recognition and measurement?

Section 24 is drafted in simple language with less application guidance than is provided in IAS 20. Whereas IAS 20 provides several options, Section 24 contains only one option as follows:

An entity should recognize government grants as follows:

- a grant that does not impose specified future performance conditions on the recipient is recognized in income when the grant proceeds are receivable;
- a grant that imposes specified future performance conditions on the recipient is recognized in income only when the performance conditions are met; and
- grants received before revenue recognition criteria are satisfied are recognized as a liability.

An entity shall measure grants at the fair value of the asset received or receivable.

There are two important distinctions between Section 24 and IAS 20 as it relates to recognition and measurement. This can result in significantly different outcomes as described below.

Firstly, a government grant is not recognized under Section 24 until the conditions are actually satisfied. This differs from the reasonable assurance approach taken by IAS 20 where the recognition criteria may be satisfied at an earlier stage providing there is reasonable assurance that the entity will comply with the conditions attaching to the grants and the grants will be received.

Secondly, IAS 20 requires recognition of government grants in profit or loss on a systematic basis over the periods in which the entity recognizes as expenses the related costs for which the grants are intended to compensate (the matching concept). Section 24 however requires government grants to be recognized as income when specified future performance conditions are met independent of the entity's recognition of the related costs for which the grants are intended to compensate. Deferring recognition until performance conditions are actually met could result in a mismatch between the recognition of grant income and the relevant costs that the grants is intended to compensate. For example, a grant intended to subsidize payroll costs may not satisfy the performance conditions until a future date after the associated payroll costs have already been incurred.

(iii) What if the grant later becomes repayable?

Section 24 does not address circumstances where a grant becomes later repayable. Presumably, there is no need for this as the recognition criteria under Section 24 preclude a government grant from being recognized until the conditions are actually satisfied.

(iv) How should grants be presented in the financial statements?

Section 24 does not prescribe presentation requirements as does IAS 20. Management will need to determine the appropriate presentation based on the nature and circumstances surrounding the grant.

(v) What should be disclosed in the financial statements?

Section 24 requires the following disclosures:

- nature and amounts of government grants that have not been recognized in income;
- unfulfilled conditions and other contingencies attaching to recognized grants; and
- indication of other forms of government assistance from which the entity has directly benefited.

The IFRS for SMEs also requires the disclosure of the judgments and estimates employed by management that have the most significant effect on the amounts recognized in the financial statements. Given that Section 24 does not provide options for recognition and measurement and does not employ the same concept of reasonable assurance, it is anticipated that less judgment will be required than is the case with IAS 20. To the extent that significant estimates are involved, these should be disclosed appropriately.

(vi) Conclusion

Government assistance may take many forms and the circumstances of each recipient will likely vary. As a result, it is important that each entity consider the economic substance of the arrangement and their ability to satisfy any conditions attaching to the grant before determining the appropriate accounting treatment (substance over form). This guidance note provides an overview of Section 24 to assist entities in this regard. It is not intended to be prescriptive as there is no substitute for judgment.