HKAS 20
Revised ~~February 2014~~ September 2018

Hong Kong Accounting Standard 20

Accounting for Government Grants and Disclosure of Government Assistance

Hong Kong Institute of
Certified Public Accountants
香港會計師公會

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from paragraph

HONG KONG ACCOUNTING STANDARD 20
ACCOUNTING FOR GOVERNMENT GRANTS AND DISCLOSURE OF GOVERNMENT ASSISTANCE

Hong Kong Accounting Standard 20 *Accounting for Governments Grants and Disclosure of Government Assistance* (HKAS 20) is set out in paragraphs 1-48~~6~~. All the paragraphs have equal authority. HKAS 20 should be read in the context of the Basis for Conclusions, the *Preface to Hong Kong Financial Reporting Statements* and the *Conceptual Framework for Financial Reporting*. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Hong Kong Accounting Standard 20

Accounting for Government Grants and Disclosure of Government Assistance ✦

Scope

1 **This Standard shall be applied in accounting for, and in the disclosure of, government grants and in the disclosure of other forms of government assistance.**

2 This Standard does not deal with:

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

(b) government assistance that is provided for an entity in the form of benefits that are available in determining taxable profit or tax loss, or are determined or limited on the basis of income tax liability. Examples of such benefits are income tax holidays, investment tax credits, accelerated depreciation allowances and reduced income tax rates.

(c) government participation in the ownership of the entity.

(d) government grants covered by HKAS 41 *Agriculture.*

Definitions

3 **The following terms are used in this Standard with the meanings specified:**

Government **refers to government, government agencies and similar bodies whether local, national or international.**

Government assistance **is 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 purpose of this Standard 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 **are 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 with government which cannot be distinguished from the normal trading transactions of the entity.***

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

Grants related to income **are government grants other than those related to assets.**

✦ As part of *Improvements to HKFRSs* issued in October 2008 the HKICPA amended terminology used in this Standard to be consistent with other HKFRSs as follows: (a) ‘taxable income’ was amended to ‘taxable profit or tax loss’, (b) ‘recognised as income/expense’ was amended to ‘recognised in profit or loss’, (c) ‘credited directly to shareholders’ interests/equity’ was amended to ‘recognised outside profit or loss’, and (d)‘revision to an accounting estimate’ was amended to ‘change in accounting estimate’.

* See also HK(SIC)-Int 10 *Government Assistance – No Specific Relation to Operating Activities.*

Forgivable loans **are loans which the lender undertakes to waive repayment of under certain prescribed conditions.**

Fair value **is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. (See HKFRS 13 *Fair Value Measurement.*)**

4 Government assistance takes many forms varying both in the nature of the assistance given and in the conditions which are usually attached to it. The purpose of the assistance may be to encourage an entity to embark on a course of action which it would not normally have taken if the assistance was not provided.

5 The receipt of government assistance by an entity may be significant for the preparation of the financial statements for two reasons. Firstly, if resources have been transferred, an appropriate method of accounting for the transfer must be found. Secondly, it is desirable to give an indication of the extent to which the entity has benefited from such assistance during the reporting period. This facilitates comparison of an entity's financial statements with those of prior periods and with those of other entities.

6 Government grants are sometimes called by other names such as subsidies, subventions, or premiums.

Government grants

7 Government grants, including non-monetary grants at fair value, shall not be recognised until there is reasonable assurance that:

(a) the entity will comply with the conditions attaching to them; and

(b) the grants will be received.

8 A government grant is not recognised until there is reasonable assurance that the entity will comply with the conditions attaching to it, and that the grant will be received. Receipt of a grant does not of itself provide conclusive evidence that the conditions attaching to the grant have been or will be fulfilled.

9 The manner in which a grant is received does not affect the accounting method to be adopted in regard to the grant. Thus a grant is accounted for in the same manner whether it is received in cash or as a reduction of a liability to the government.

10 A forgivable loan from government is treated as a government grant when there is reasonable assurance that the entity will meet the terms for forgiveness of the loan.

10A The benefit of a government loan at a below-market rate of interest is treated as a government grant. The loan shall be recognised and measured in accordance with ~~HKAS 39~~ HKFRS 9 *Financial Instruments~~: Recognition and Measurement~~*. The benefit of the below-market rate of interest shall be measured as the difference between the initial carrying value of the loan determined in accordance with ~~HKAS 39~~ HKFRS 9 and the proceeds received. The benefit is accounted for in accordance with this Standard. The entity shall consider the conditions and obligations that have been, or must be, met when identifying the costs for which the benefit of the loan is intended to compensate.

11 Once a government grant is recognised, any related contingent liability or contingent asset is treated in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

12 Government grants shall be recognised in profit or loss 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.

13 There are two broad approaches to the accounting for government grants: the capital approach, under which a grant is recognised outside profit or loss, and the income approach, under which a grant is recognised in profit or loss over one or more periods.

14 Those in support of the capital approach argue as follows:

(a) government grants are a financing device and should be dealt with as such in the statement of financial position rather than be recognised in profit or loss to offset the items of expense that they finance. Because no repayment is expected, such grants should be recognised outside profit or loss.

(b) it is inappropriate to recognise government grants in profit or loss, because they are not earned but represent an incentive provided by government without related costs.

15 Arguments in support of the income approach are as follows:

(a) because government grants are receipts from a source other than shareholders, they should not be recognised directly in equity but should be recognised in profit or loss in appropriate periods.

(b) government grants are rarely gratuitous. The entity earns them through compliance with their conditions and meeting the envisaged obligations. They should therefore be recognised in profit or loss over the periods in which the entity recognises as expenses the related costs for which the grant is intended to compensate.

(c) because income and other taxes are expenses, it is logical to deal also with government grants, which are an extension of fiscal policies, in profit or loss.

16 It is fundamental to the income approach that government grants should be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grant is intended to compensate. Recognition of government grants in profit or loss on a receipts basis is not in accordance with the accrual accounting assumption (see HKAS 1 *Presentation of Financial Statements*) and would be acceptable only if no basis existed for allocating a grant to periods other than the one in which it was received.

17 In most cases the periods over which an entity recognises the costs or expenses related to a government grant are readily ascertainable. Thus grants in recognition of specific expenses are recognised in profit or loss in the same period as the relevant expenses. Similarly, grants related to depreciable assets are usually recognised in profit or loss over the periods and in the proportions in which depreciation expense on those assets is recognised.

18 Grants related to non-depreciable assets may also require the fulfilment of certain obligations and would then be recognised in profit or loss over the periods that bear the cost of meeting the obligations. As an example, a grant of land may be conditional upon the erection of a building on the site and it may be appropriate to recognise the grant in profit or loss over the life of the building.

19 Grants are sometimes received as part of a package of financial or fiscal aids to which a number of conditions are attached. In such cases, care is needed in identifying the conditions giving rise to costs and expenses which determine the periods over which the grant will be earned. It may be appropriate to allocate part of a grant on one basis and part on another.

20 A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs shall be recognised in profit or loss of the period in which it becomes receivable.

21 In some circumstances, a government grant may be awarded for the purpose of giving immediate financial support to an entity rather than as an incentive to undertake specific expenditures. Such grants may be confined to a particular entity and may not be available to a whole class of beneficiaries. These circumstances may warrant recognising a grant in profit or loss of the period in which the entity qualifies to receive it, with disclosure to ensure that its effect is clearly understood.

22 A government grant may become receivable by an entity as compensation for expenses or losses incurred in a previous period. Such a grant is recognised in profit or loss of the period in which it becomes receivable, with disclosure to ensure that its effect is clearly understood.

Non-monetary government grants

23 A government grant may take the form of a transfer of a non-monetary asset, such as land or other resources, for the use of the entity. In these circumstances it is usual to assess the fair value of the non-monetary asset and to account for both grant and asset at that fair value. An alternative course that is sometimes followed is to record both asset and grant at a nominal amount.

Presentation of grants related to assets

24 Government grants related to assets, including non-monetary grants at fair value, shall be presented in the statement of financial position either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.

25 Two methods of presentation in financial statements of grants (or the appropriate portions of grants) related to assets are regarded as acceptable alternatives.

26 One method recognises the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.

27 The other method deducts the grant in calculating the carrying amount of the asset. The grant is recognised in profit or loss over the life of a depreciable asset as a reduced depreciation expense.

28 The purchase of assets and the receipt of related grants can cause major movements in the cash flow of an entity. For this reason and in order to show the gross investment in assets, such movements are often disclosed as separate items in the statement of cash flows regardless of whether or not the grant is deducted from the related asset for presentation purposes in the statement of financial position.

Presentation of grants related to income

29 Grants related to income are ~~sometimes~~ presented as ~~a credit in the statement of comprehensive income~~part of profit or loss, either separately or under a general heading such as "Other income"; alternatively, they are deducted in reporting the related expense.

29A ~~If an entity presents the components of profit or loss in a separate income statement as described in paragraph 81 of HKAS 1 (as revised in 2007), it presents grants related to income as required in paragraph 29 in that separate statement.~~[Deleted]

30 Supporters of the first method claim that it is inappropriate to net income and expense items and that separation of the grant from the expense facilitates comparison with other expenses not affected by a grant. For the second method it is argued that the expenses might well not have been incurred by the entity if the grant had not been available and presentation of the expense without offsetting the grant may therefore be misleading.

31 Both methods are regarded as acceptable for the presentation of grants related to income. Disclosure of the grant may be necessary for a proper understanding of the financial statements. Disclosure of the effect of the grants on any item of income or expense which is required to be separately disclosed is usually appropriate.

Repayment of government grants

32 A government grant that becomes repayable shall be accounted for as a change in accounting estimate (see HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors***). Repayment of a grant related to income shall be applied first against any unamortised deferred credit recognised in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or when no deferred credit exists, the repayment shall be recognised immediately in profit or loss. Repayment of a grant related to an asset shall be recognised by increasing the carrying amount of the asset or reducing the deferred income balance by the amount repayable. The cumulative additional depreciation that would have been recognised in profit or loss to date in the absence of the grant shall be recognised immediately in profit or loss.**

33 Circumstances giving rise to repayment of a grant related to an asset may require consideration to be given to the possible impairment of the new carrying amount of the asset.

Government assistance

34 Excluded from the definition of government grants in paragraph 3 are certain forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

35 Examples of assistance that cannot reasonably have a value placed upon them are free technical or marketing advice and the provision of guarantees. An example of assistance that cannot be distinguished from the normal trading transactions of the entity is a government procurement policy that is responsible for a portion of the entity's sales. The existence of the benefit might be unquestioned but any attempt to segregate the trading activities from government assistance could well be arbitrary.

36 The significance of the benefit in the above examples may be such that disclosure of the nature, extent and duration of the assistance is necessary in order that the financial statements may not be misleading.

37 [Deleted]

38 In this Standard, government assistance does not include the provision of infrastructure by improvement to the general transport and communication network and the supply of improved facilities such as irrigation or water reticulation which is available on an ongoing indeterminate basis for the benefit of an entire local community.

Disclosure

39 The following matters shall be disclosed:

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

(b) the nature and extent of government grants recognised in the financial statements and an indication of other forms of government assistance from which the entity has directly benefited; and

(c) unfulfilled conditions and other contingencies attaching to government assistance that has been recognised.

Transitional provisions

40 [Not used]

Effective date

41 **This Standard becomes operative for financial statements covering periods beginning on or after 1 January 2005. Earlier application is encouraged. If an entity applies this Standard for a period beginning before 1 January 2005, it shall disclose that fact and apply Hong Kong (SIC) Interpretation (HK(SIC)-Int) 10** *Government Assistance – No Specific Relation to Operating Activities* **at the same time.**

41a This Standard supersedes SSAP 35 *Accounting for Government Grants and Disclosure of Government Assistance* (issued in March 2002).

42 HKAS 1 (as revised in 2007) amended the terminology used throughout HKFRSs. In addition it added paragraph 29A. An entity shall apply those amendments for annual periods beginning on or after 1 January 2009. If an entity applies HKAS 1 (revised 2007) for an earlier period, the amendments shall be applied for that earlier period.

43 Paragraph 37 was deleted and paragraph 10A added by *Improvements to HKFRSs* issued in October 2008. An entity shall apply those amendments prospectively to government loans received in periods beginning on or after 1 January 2009. Earlier application is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact.

44 ~~*[This paragraph refers to amendments with an effective date after 1 January 2013, and is therefore not included in this edition.]*~~[Deleted]

45 HKFRS 13, issued in June 2013, amended the definition of fair value in paragraph 3. An entity shall apply that amendment when it applies HKFRS 13.

46 *Presentation of Items of Other Comprehensive Income* (Amendment to HKAS 1), issued in July 2011, amended paragraph 29 and deleted paragraph 29A. An entity shall apply those amendments when it applies HKAS 1 as amended in July 2011.

47 [Deleted]

48 HKFRS 9, as issued in September 2014, amended paragraph 10A and deleted paragraphs 44 and 47. An entity shall apply those amendments when it applies HKFRS 9.

Appendix

Comparison with International Accounting Standards

This comparison appendix, which was prepared as at December 2004 and deals only with significant differences in the standards extant, is produced for information only and does not form part of the standards in HKAS 20.

The International Accounting Standard comparable with HKAS 20 is IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance.*

There are no major textual differences between HKAS 20 and IAS 20.

Basis for Conclusions on IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*

This Basis for Conclusions accompanies, but is not part of, IAS 20.

HKAS 20 is based on IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. In approving HKAS 20, the Council of the Hong Kong Institute of Certified Public Accountants considered and agreed with the IASB's Basis for Conclusions on IAS 20. Accordingly, there are no significant differences between HKAS 20 and IAS 20. The IASB's Basis for Conclusions is reproduced below. The paragraph numbers of IAS 20 referred to below generally correspond with those in HKAS 20.

BC1 This Basis for Conclusions summarises the International Accounting Standards Board's considerations in amending IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* as part of *Improvements to IFRSs* issued in May 2008.

BC2 IAS 20 was developed by the International Accounting Standards Committee in 1983 and did not include a Basis for Conclusions. This Basis refers to the insertion of paragraphs 10A and 43 and the deletion of paragraph 37. Those changes require government loans with below-market rates of interest to be recognised and measured in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*[*] and the benefit of the reduced interest to be accounted for using IAS 20.

Accounting for loans from government with a below-market rate of interest

BC3 The Board identified an apparent inconsistency between the guidance in IAS 20 and IAS 39.[*] It related to the accounting for loans with a below-market rate of interest received from a government. IAS 20 stated that no interest should be imputed for such a loan, whereas IAS 39 required all loans to be recognised at fair value, thus requiring interest to be imputed to loans with a below-market rate of interest.

BC4 The Board decided to remove this inconsistency. It believed that the imputation of interest provides more relevant information to a user of the financial statements. Accordingly the Board amended IAS 20 to require that loans received from a government that have a below-market rate of interest should be recognised and measured in accordance with IAS 39. The benefit of the government loan is measured at the inception of the loan as the difference between the cash received and the amount at which the loan is initially recognised in the statement of financial position. This benefit is accounted for in accordance with IAS 20.

BC5 Noting that applying IAS 39 to loans retrospectively may require entities to measure the fair value of loans at a past date, the Board decided that the amendment should be applied prospectively to new loans.

[*] IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39. This paragraph refers to matters relevant when IAS 20 was amended in 2008.