AcSB
Accounting Standards Board

COVID-19 Resource

Accounting for Government Loan Programs by Borrowers and Lenders

What you need to know (June 2020)

What's the issue?

1. Governments[1] have established various borrowing programs consisting of interest-free or forgivable loans to individuals and businesses to help them overcome economic challenges arising from the COVID-19 pandemic. As many of these programs require borrowers to apply for these loans through their financial institutions, both borrowers and their financial institutions should carefully review the programs details to determine the appropriate accounting.

2. Borrowers should consider the program eligibility requirements to assess whether these loans should be accounted for in accordance with IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* or in accordance with IFRS 9 *Financial Instruments*. Since many of these government programs were only recently announced, borrowers should consider the status of these programs at the financial reporting date to ensure that recognition of the government grant is appropriate.

3. As the lender, financial institutions should also review the arrangements made with the government to assess whether the loans qualify for asset derecognition under IFRS 9.

---

[1] For the purposes of this publication, governments refer to federal and provincial governments or government-owned agencies.

How should borrowers account for government loans?

4. Government loan programs often include conditions that borrowers must meet throughout the term of the loan. Borrowers should recognize a government grant when there is reasonable assurance that they will meet the conditions attached to it and will receive the funds. [IAS 20.7 and IAS 20.8]

5. A borrower may receive a loan from the government that, if certain conditions are met, all or a portion of the loan will be forgiven. If there is reasonable assurance that the borrower will meet the terms for the forgiveness of the loan, the loan is treated as a government grant in accordance with IAS 20. Otherwise, the loan should be accounted for in accordance with IFRS 9. [IAS 20.10]

6. In other programs, a borrower may receive a below-market interest rate loan from the government. A below-market interest loan is initially recognized at its fair value plus or minus any transaction costs in accordance with IFRS 9. The interest rate differential, measured as the difference between the initial carrying value of the loan and the proceeds received, is treated as a government grant and accounted for in accordance with IAS 20. [IAS 20.10A and IFRS 9.5.1.1]

7. Subsequently, the borrower should recognize the government grant, that may include the forgivable loan or the interest rate differential in the below-market interest rate loan, in profit or loss on a systematic basis over the same periods as the expenses the grant is intended to compensate are recognized. To determine the appropriate periods to recognize the government grant, the borrower should consider whether the grant compensates for expenses already incurred, or for current or future costs. If the government grant is a compensation for expense or losses already incurred or as an immediate financial support with no future related costs, the borrower should recognize the grant in profit or loss of the period in which it becomes receivable. [IAS 20.12, IAS 20.17, IAS 20.20 and IAS 20.21]

How should a financial institution account for certain government loan programs?

8. When eligible borrowers apply for the loan through their financial institution, the financial institution becomes a party to the loan contract and has a legal right to receive cash payments from the borrowers. Therefore, the financial institution recognizes the loan receivable on its balance sheet. [IFRS 9.3.1.1 and IFRS 9.B3.1.2(a)]

9. However, the financial institution may derecognize the loan from its balance sheet if the arrangement with the government can be treated as a transfer and when the transfer qualifies for derecognition in accordance with IFRS 9. [IFRS 9.3.2.3]

10. Under IFRS 9, the loan is transferred to the government when the financial institution either:
    (a) transfers its contractual rights to receive loan payments [IFRS 9.3.2.4 (a)]; or
    (b) retains those contractual rights but also assumes a contractual obligation to pass on those cash flows to the government (often referred to as a “pass-through” arrangement). [IFRS 9.3.2.4 (b)]

11. Some government loans are structured as co-lending programs, where the financial institution sells a percentage of its interests in the loan to the government. In these scenarios, the financial institution

should review the agreement to assess whether, by selling an interest in the loan, it has transferred a portion of the contractual rights to the government. When making this assessment, a financial institution may consider if:

(a) the financial institution's rights, title, and interest in the loan are sold, assigned or transferred to the government;

(b) the financial institution's creditors, such as its bond holders, have access to the loan for any proceedings against the financial institution;

(c) the financial institution and the government have rights to each other's interest in the loan; and

(d) the government has recourse to the financial institution if the borrower defaults on the loan.

12. In other government loan programs, the financial institution uses funding it received from the government to originate a loan and retains the contractual right to receive loan payments under the arrangement. At the same time, the financial institution may also be contractually required to remit any loan payments received to the government. In this scenario, since the financial institution has the contractual right to receive loan payments, it should assess whether this arrangement meets all three pass-through criteria in paragraph IFRS 9.3.2.5 to be considered as a transfer of the loan. When evaluating these criteria, the financial institution should consider factors such as:

    (a) whether the financial institution is liable to pay the government any amount uncollectible on the loan;

    (b) whether the government has recourse to the financial institution if the borrower defaults on the loan;

    (c) whether the financial institution can sell, assign, pledge or grant a security interest in the loans to anyone but the government;

    (d) the time required for the financial institution to remit the loan payments received to the government; and

    (e) whether the financial institutions can reinvest the loan payments received and if so, the type of investments and whether the return is remitted to the government.

13. Once the financial institution has established that the loan is transferred to the government, it should then evaluate whether it has transferred substantially all of the risks and rewards of ownership. Some examples of the risks and rewards related to the loan include credit risk, prepayment risk, interest rate risk, and whether the creditors of the financial institution have recourse to the loan. [IFRS 9.3.2.6]

14. Finally, if the financial institution determines that it has transferred substantially all of the risk and rewards of ownership, it should derecognize the loan from its balance sheet. Furthermore, the financial institution will not re-recognize the transferred loan in a future period unless it reacquires the transferred loan in a new transaction. [IFRS 9.B3.2.6]

Has the IFRS® Discussion Group talked about this topic?

15. The Group has had several conversations on the accounting for government assistance. The discussions listed below may be helpful as you think how COVID-19 could affect the accounting for government loans and other considerations related to accounting for financial assets under IFRS 9:

Meeting Date	Topic	Meeting Report
May 27, 2020	Financial Reporting Considerations of COVID-19	View Document
October 5, 2017	Classification of Financial Assets	View Document
May 30, 2017	IFRS 9 Matters for Non-Financial Entities	View Document
December 9, 2014	Fair Value Measurement of Government Loans	View Document

16. Learn how to submit an issue to the IFRS® Discussion Group for their consideration at a future meeting.

What other resources are available?

17. Do you need more information? The following publication may provide more insight:

PwC podcast, "Government Grants and Coronavirus (COVID-19)" April 2020.

Extracts from relevant IFRS® Standards

Standard	Guidance
IFRS 9	3.1.1 An entity shall recognise a financial asset or a financial liability in its statement of financial position when, and only when, the entity becomes party to the contractual provisions of the instrument (see paragraphs B3.1.1 and B3.1.2). When an entity first recognises a financial asset, it shall classify it in accordance with paragraphs 4.1.1–4.1.5 and measure it in accordance with paragraphs 5.1.1–5.1.3. When an entity first recognises a financial liability, it shall classify it in accordance with paragraphs 4.2.1 and 4.2.2 and measure it in accordance with paragraph 5.1.1 3.2.3 An entity shall derecognise a financial asset when, and only when: (a) the contractual rights to the cash flows from the financial asset expire, or (b) it transfers the financial asset as set out in paragraphs 3.2.4 and 3.2.5 and the transfer qualifies for derecognition in accordance with paragraph 3.2.6. 3.2.4 An entity transfers a financial asset if, and only if, it either: (a) transfers the contractual rights to receive the cash flows of the financial asset, or (b) retains the contractual rights to receive the cash flows of the financial asset, but assumes a contractual obligation to pay the cash flows to one or more recipients in an arrangement that meets the conditions in paragraph 3.2.5. 3.2.5 When an entity retains the contractual rights to receive the cash flows of a financial asset (the 'original asset'), but assumes a contractual obligation to pay those cash flows to one or more entities (the ‘eventual recipients’), the entity treats the transaction as a transfer of a financial asset if, and only if, all of the following three conditions are met. (a) The entity has no obligation to pay amounts to the eventual recipients unless it collects equivalent amounts from the original asset. Short-term advances by the entity with the right of full recovery of the amount lent plus accrued interest at market rates do not violate this condition. (b) The entity is prohibited by the terms of the transfer contract from selling or pledging the original asset other than as security to the eventual recipients for the obligation to pay them cash flows. (c) The entity has an obligation to remit any cash flows it collects on behalf of the eventual recipients without material delay. In addition, the entity is not entitled to reinvest such cash flows, except for investments in cash or cash equivalents (as defined in IAS 7 *Statement of Cash Flows*) during the short settlement period from

Standard	Guidance
	the collection date to the date of required remittance to the eventual recipients, and interest earned on such investments is passed to the eventual recipients. 3.2.6 When an entity transfers a financial asset (see paragraph 3.2.4), it shall evaluate the extent to which it retains the risks and rewards of ownership of the financial asset. In this case: (a) if the entity transfers substantially all the risks and rewards of ownership of the financial asset, the entity shall derecognise the financial asset and recognise separately as assets or liabilities any rights and obligations created or retained in the transfer. (b) if the entity retains substantially all the risks and rewards of ownership of the financial asset, the entity shall continue to recognise the financial asset. (c) if the entity neither transfers nor retains substantially all the risks and rewards of ownership of the financial asset, the entity shall determine whether it has retained control of the financial asset. In this case: (i) if the entity has not retained control, it shall derecognise the financial asset and recognise separately as assets or liabilities any rights and obligations created or retained in the transfer. (ii) if the entity has retained control, it shall continue to recognise the financial asset to the extent of its continuing involvement in the financial asset (see paragraph 3.2.16). 5.1.1 Except for trade receivables within the scope of paragraph 5.1.3, at initial recognition, an entity shall measure a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. B3.1.2 The following are examples of applying the principle in paragraph 3.1.1: (a) Unconditional receivables and payables are recognised as assets or liabilities when the entity becomes a party to the contract and, as a consequence, has a legal right to receive or a legal obligation to pay cash. (b) Assets to be acquired and liabilities to be incurred as a result of a firm commitment to purchase or sell goods or services are generally not recognised until at least one of the parties has performed under the agreement. For example, an entity that receives a firm order does not generally recognise an asset (and the entity that places the order does not recognise a liability) at the time of the commitment but, instead, delays recognition until the ordered goods or services have

Standard	Guidance
	been shipped, delivered or rendered. If a firm commitment to buy or sell non-financial items is within the scope of this Standard in accordance with paragraphs 2.4–2.7, its net fair value is recognised as an asset or a liability on the commitment date (see paragraph B4.1.30(c)). In addition, if a previously unrecognised firm commitment is designated as a hedged item in a fair value hedge, any change in the net fair value attributable to the hedged risk is recognised as an asset or a liability after the inception of the hedge (see paragraphs 6.5.8(b) and 6.5.9). (c) A forward contract that is within the scope of this Standard (see paragraph 2.1) is recognised as an asset or a liability on the commitment date, instead of on the date on which settlement takes place. When an entity becomes a party to a forward contract, the fair values of the right and obligation are often equal, so that the net fair value of the forward is zero. If the net fair value of the right and obligation is not zero, the contract is recognised as an asset or liability. (d) Option contracts that are within the scope of this Standard (see paragraph 2.1) are recognised as assets or liabilities when the holder or writer becomes a party to the contract. (e) Planned future transactions, no matter how likely, are not assets and liabilities because the entity has not become a party to a contract. B3.2.6 If an entity determines that as a result of the transfer, it has transferred substantially all the risks and rewards of ownership of the transferred asset, it does not recognise the transferred asset again in a future period, unless it reacquires the transferred asset in a new transaction.
IAS 20	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. 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 IFRS 9 *Financial Instruments*. The benefit of the below-market rate of interest shall be measured as the difference between the initial

Standard	Guidance
	carrying value of the loan determined in accordance with IFRS 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. 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. 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. 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.