

***Query No. 16***

***Subject: Accounting Treatment of Status Holder Incentive Scheme (SHIS) Scrips.<sup>1</sup>***

**A. Facts of the Case**

1. A company (hereinafter referred to as ‘the company’) is a private limited non-listed company established in the year 2006. The company is engaged in the business of manufacturing yarn.

2. The querist has stated that the Central Government has announced its Foreign Trade Policy (FTP) for 27.08.2009 to 31.03.2014 on 27.08.2009. Latest amendment to the policy was made on 05.06.2012. The Policy describes ‘Promotion measures’ in Chapter 3. Status Holders Incentive Scheme (hereinafter referred as the ‘Scheme’) is one of the promotional measures given in the Chapter 3 of the Policy. Paragraph 3.16 of the FTP deals with the provisions of the Scheme. Provisions of the Scheme have been reproduced by the querist as follows:

“3.16 Status Holders Incentive Scrip (SHIS)

3.16.1 (a) Objective of SHIS is to promote investment in upgradation of technology.

(b) Status Holders of sectors specified in Para 3.16.4 below, shall be entitled to a Duty Credit Scrip @1% of FOB value of exports made during 2009-10, 2010-11, 2011-12 and 2012-13.

(c) Status Holders of additional sectors listed in Para 3.10.8 of HBPv1<sup>2</sup> 2009- 14 (RE-2010) shall also be eligible for this Status

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<sup>1</sup> Opinion finalised by the Committee on 16.7.2013.

<sup>2</sup> HBPv1 stands for Handbook of Procedures Volume 1

Holders Incentive Scrip on exports made during 2010-11, 2011-12 and 2012-13.

(d) This shall be over and above any Duty Credit Scrip claimed/availed under this chapter.

3.16.2 Status Holders availing Technology Upgradation Fund Scheme (TUFS) benefits (administered by Ministry of Textiles) during a particular year shall not be eligible for Status Holders Incentive Scrip for exports of that year.

3.16.3 The Status Holders Incentive Scrip will be subject to actual user condition. However transferability will be permitted amongst status holders subject to the condition that the transferee status holder is a manufacturer. Status Holder Incentive Scrip shall be used for import of capital goods (as defined in FTP) relating to sectors specified in Para 3.16.4 below and para 3.10.8 of HBP. Only in respect of CG<sup>3</sup> imported earlier, upto 10% value of the Duty Credit Scrip can be used for import of components, spares/parts of such CG.

3.16.4 Status Holders of the following Sectors shall be eligible for the Status Holders Incentive Scrip:

(i) Leather Sector (excluding finished leather);

(ii) Textiles and Jute Sector;

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<sup>3</sup> CG stands for Capital Goods

(iii) Handicrafts;

(iv) Engineering Sector (excluding Iron & Steel,..)

...”

3. The querist has further stated that as the company deals in textile sector, it is eligible for SHIS scrip as per paragraph 3.16.4 (ii). However, due to lack of clarity in respect of the company’s eligibility under this scheme, the company could not apply for SHIS scrips during 2009-10 to 2011-12 and pursuant to a recent clarification, the company has applied for SHIS scrips for financial years 2009-10 and 2010-11 during the current financial year 2012-13. The company did not apply for SHIS scrips for the financial year 2011-12 as the company had availed TUF benefit during this year. The company has also received SHIS scrip from the Director General of Foreign Trade (DGFT) during the current financial year 2012-13.

4. The querist has reproduced the following paragraphs of Accounting Standard (AS) 12, ‘Accounting for Government Grants’, notified under the Companies (Accounting Standards) Rules, 2006 (hereinafter referred to as the ‘Rules’):

“1. This Standard deals with accounting for government grants. Government grants are sometimes called by other names such as subsidies, cash incentives, duty drawbacks, etc.”

“3.2 Government grants are assistance by government in cash or kind to an enterprise for past or future compliance with certain conditions. ...”

“5.2 ...

- (ii) 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.”

“5.4 It is generally considered appropriate that accounting for government grant should be based on the nature of the relevant grant. Grants which have the characteristics similar to those of promoters’ contribution should be treated as part of shareholders’ funds. Income approach may be more appropriate in the case of other grants.”

“10.1 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.”

*Company’s view*

5. Looking to the above objective and provisions, the querist is of the view that SHIS scrips are capital incentive from the Government, hence the same should be credited to capital reserve at the time of its utilisation.

6. The querist has also provided the following accounting entries:

a. On accrual:

SHIS receivable A/c	Dr.	With face value
To SHIS capital reserve A/c		With face value

b. On utilisation in import of capital items / spare parts:

Asset / Mill Store A/c	Dr.	With invoice value
Cenvat receivable A/c	Dr.	With duty amount
To sundry creditors A/c		With Invoice value
To SHIS receivable A/c		With duty amount

c. On sale of scrips:

Sundry debtors A/c	Dr.	With Invoice value
To SHIS Receivable A/c		With sale value
To Vat payable A/c		With VAT amount

SHIS capital reserve A/c	Dr.	With discount value
To SHIS receivable		With discount value

**B. Query**

7. On the basis of the above, the querist has sought the opinion of the Expert Advisory Committee on the following issues:

- (i) Whether SHIS scrip falls under the definition of ‘government grant’ or these should be considered as ‘incentive income’.
- (ii) Considering the objective and conditional use for capital goods only, whether it would be correct to treat the SHIS scrip as a capital grant in the nature of ‘promoters contribution’.

- (iii) Whether this scrip should be credited directly in capital reserve or as deferred income or current income.
- (iv) Whether it will affect accounting treatment if scrip is sold in the market instead of self-use.
- (v) What would be accounting treatment if market value of the scrip is 30% at the time of receipt and will be 25% at the balance sheet date?
- (vi) Whether receipt of earlier year's SHIS scrip will be treated as 'prior period income' during current financial year 2012-2013.

### C. Points considered by Committee

8. The Committee notes that the basic issue raised in the query relates to accounting for SHIS scrips received under the Scheme of the Foreign Trade Policy. Therefore, the Committee has considered only this issue and has not examined any other issue that may arise from the Facts of the Case, such as, presentation and disclosure of SHIS scrips in the financial statements, treatment of amount received by the company on utilisation/sale of SHIS scrips, accounting for imported capital goods or spares/components against which scrips would be utilised, timing of recognition of the scrips entitlement, etc.

9. With regard to the issue raised by the querist as to whether SHIS scrips fall under the definition of the term, 'government grant', the Committee notes paragraph 3.2 of Accounting Standard (AS) 12, 'Accounting for Government Grants', notified under the 'Rules' as follows:

***“3.2 Government grants are assistance by government in cash or kind to an enterprise for past or future compliance with certain conditions. 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 enterprise.”***

From the Facts of the Case, the Committee notes that SHIS scrips are assistance in kind by the Government as the company receives scrips that may be either adjusted against import of capital goods or their spare parts/ components or can be sold to another status holder subject to certain conditions. Further, these are awarded on the basis of pre-specified percentage of exports made by the company and accordingly, the value placed upon them is reasonably determinable. Therefore, these are of the nature of government grant.

10. With regard to nature of grant obtained, the Committee notes paragraphs 8.1 and 10.1 of AS 12 which provide as below:

“8.1 Grants related to specific fixed assets are government grants whose primary condition is that an enterprise qualifying for them should purchase, construct or otherwise acquire such assets. Other 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.”

“10.1 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.”

The Committee notes that as per the Foreign Trade Policy, the SHIS scrips are granted to the exporters with the objective to promote investment in upgradation of technology. However, the grant is awarded with reference to exports made by the company and not with reference to total investment in an undertaking or by way of contribution towards its capital outlay. Accordingly, the Committee is of the view that it would not be appropriate to treat the SHIS scrips as 'promoters' contribution'. Further, the Committee is of the view that the scrips granted cannot be considered as a grant related to specific fixed assets as at the time of awarding such scrips, no specific asset has been identified for its utilisation. The Committee notes that such scrips can be utilised not only for payment of duty on import of capital goods but also for their spare parts or components which can be revenue in nature. Moreover, it is not necessary under the policy that its recipient should utilise the scrips for technology upgradation only. The recipient may transfer it to another status holder subject to certain conditions resulting into an income for him. Thus, the award of SHIS scrips should be considered to be generating income to the company. Accordingly, the Committee is of the view that as per the principles of AS 12, the scrips granted should be treated as a grant related to revenue.

11. With regard to measurement of government grant, the Committee is of the view that basis of measurement depends on its intended use. The Committee notes that there could be two intended uses of these scrips, i.e., these can either be utilised against the purchase of capital goods and spares in accordance with the Policy or can be held for sale. In case the company intends to utilise these scrips against the import of capital goods and spares, these should be recognised at the value of the scrips granted as these would be utilised at the same value against the settlement of import duty. However, in case the company intends to sell these scrips, these should be valued at the lower of the original value of the scrip or its estimated net realisable value.

12. As regards the situation where the company was entitled to SHIS scrips in earlier years but same was not claimed by the company, the Committee is of the view that it is not an error or omission in the preparation of the financial statements. The company has not claimed the SHIS scrips due to lack of clarity on its eligibility and has applied for it pursuant to 'recent clarifications'. Accordingly, the Committee is of the view that it would not be appropriate to recognise receipt of the SHIS scrips for earlier years as prior period income. In this regard, the Committee notes the definition of the term 'prior period items' as defined in Accounting Standard (AS) 5, 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', notified under the 'Rules' as follows:

***“4.3 Prior period items are income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more prior periods.”***

#### **D. Opinion**

13. On the basis of above, the Committee is of the following opinion on the issues raised in paragraph 7 above:

- (i) SHIS scrips fall under the definition of 'government grant', as discussed in paragraph 9 above.
- (ii) No, it would not be correct to treat the SHIS scrip as a capital grant in the nature of 'promoters' contribution', as discussed in paragraph 10 above.
- (iii) The scrips should not be credited directly in capital reserve or treated as deferred income, rather these should be recognised as grants related to revenue as per the principles of AS 12, as discussed in paragraph 10 above.
- (iv) It is the valuation and not recognition of scrip which may be affected by the fact that the scrip is intended to be sold in the market or is intended to be used internally

against import of capital goods and spares/components, as discussed in paragraph 11 above.

- (v) If the scrips are intended to be sold in the market, then these should be valued at lower of original scrip value or estimated net realisable value. In other cases, it will not affect the valuation of scrips.
- (vi) In a situation when the company was entitled to SHIS scrips in earlier years but same was not claimed by the company, it would not be appropriate to treat the receipt of SHIS scrips as prior period income, as discussed in paragraph 12 above.