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ACCOUNTING AND TAX CONSEQUENCES OF COVID-19 RELATED SUPPORT

GUIDE

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In this guide we outline the accounting and tax implications of the main types of support packages offered by government to companies during the pandemic.

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Introduction

Since the beginning of the pandemic the UK government has provided support for business through a variety of packages, some depending on the size of the business, others depending on the sector in which the business operates. For companies applying FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*, the accounting treatment is generally covered by the requirements of Section 24 *Government Grants* and in most cases the tax treatment follows the accounting treatment.

This guide is designed to provide an overview of the accounting and tax consequences of receiving government assistance and also the consequences if the company chooses to repay any assistance received. It also signposts where further guidance can be found. It is not intended to cover all eventualities and only sets out the tax consequences for companies, rather than unincorporated entities.

Below is a summary of the more detailed accounting guidance which is available in the Technical Advisory helpsheet Accounting for coronavirus government support schemes under FRS 102.

General principles underlying accounting treatment

Section 24 *Government Grants* of FRS 102 permits an entity to recognise grants based on either the performance model or the accrual model; practically, this choice does not make a difference to the accounting treatments discussed below.

A grant should not be recognized until there is reasonable assurance that:

- the entity will comply with the conditions attaching to them; and
- the grant will be received.

There may be an element of judgement involved as the term ‘reasonable assurance’ is not defined.

Coronavirus Job Retention Scheme (CJRS)

CJRS results in cash payments from government to compensate employers for part of the payroll costs of employees who have been placed on furlough.

Accounting implications

The income from the grant will normally be recognised on a straight-line basis over the furlough period for each relevant employee and shown within other income. There would be either a debtor or a deferred income balance recognised depending upon when the cash was received from HMRC.

It is not appropriate to net the grant income off against wages and salaries costs (FRS 102 paragraph 2.52).

Tax implications

There are no specific rules which would cause the timing of the recognition of the payments to differ from the accounting treatment. Hence, the payments would fall taxable at the time they are recognised under GAAP.

So, for example, if the company is carrying on a trading business, the payment will form part of its trading profits.

A Coronavirus Support Payment under an employment-related scheme like CJRS is referable to the business of the company entitled to the payment. There are two implications of this.

Firstly, if a company has more than one business, it is necessary to consider which business the payment relates to. For example, a payment relating to a trading business of a company which also has a property business will form part of the trading profits of the trade.

Secondly, for CJRS, the company entitled to the payment is the PAYE employer (which may be different to the actual employer where, for example, a single company performs the payroll activity for a group of companies). It is therefore possible that the company that obtains a deduction for salaries and other employment costs is different to the one that is taxed on the CJRS payments.

Where the payments would not otherwise be treated as taxable income (perhaps because the PAYE employer is based overseas and has no UK taxable presence) and another company receives a tax deduction for the salary and other employment costs to which the payments relate, there are anti-avoidance rules at para 5 Sch 15 FA 2020 that ensure that the payments are taxable on the company receiving the payment.

If a CJRS payment is received in advance of a company commencing to trade, the payment will be deducted from the pre-trading expenditure that it can then deduct from taxable profits arising in its first period of trade.

Example

“In February 2020, a new company is formed and employs a manager to help set up and run a restaurant. As a result of the coronavirus pandemic, the restaurant is delayed in opening its doors and no trade has commenced. The company furloughs its manager and receives CJRS income which it uses to pay the salary of its furloughed manager.

If the trade eventually commences without the income being brought into account in calculating the profits of that newly commenced trade, any pre-trading expenditure (under section 61 CTA 2009) of the company which relates to the employment costs covered by the CJRS is reduced by the CJRS income received.”

Small Business Grant Fund (SBGF), Retail, Hospitality and Leisure Grant Fund (RHLGF) and Discretionary Fund

These funds represent cash payments from local authorities to eligible businesses. These are government grants for which there are no future performance-related conditions.

Accounting implications

A grant that does not impose specified future performance-related conditions on the recipient is recognised in income when there is reasonable assurance that the grant proceeds are received or receivable. Reasonable assurance is not a defined term and it may be a matter of judgement whether this threshold has been met. For some grants eg, the RHLGF, this will be when the eligibility criteria are published; for others eg, the Discretionary Fund, this will be when confirmation of eligibility has been received.

The grant will be shown within other income, with a corresponding debtor until the cash has been received from the local authority.

Tax implications

As with CJRS, the general rule is that the tax treatment of such grants follows GAAP. The payment will be referable to the business of the company entitled to the payment. So, for example, if the recipient is carrying on a trading business, the payment will form part of its trading profits. Specific apportionment rules apply where, for example, a single grant is paid in respect of multiple businesses.

Business rates holiday

Eligible nurseries and businesses in the retail, hospitality and leisure sectors will not have to pay business rates for the 2020-21 tax year.

Accounting implications

Under FRS 102, this simply represents a reduction in the rates expense.

If the financial year of the business is aligned to the tax year, the business would simply have a zero rates expense for the year. In most cases, the financial year will not be aligned to the tax year, so time apportionment will be necessary.

Tax implications

The reduction in business rates will result in a decrease in the amount of expenditure eligible to be deducted from taxable profits in accordance with GAAP. If part of the premises concerned is used for non-business purposes (eg, living accommodation) then a proportion of the rates payable would have been disallowed for tax purposes.

Statutory Sick Pay (SSP) Rebate Scheme

The SSP rebate results in cash payments from government to compensate employers for the SSP they pay to employees because they either a) have coronavirus, b) cannot work because they are self-isolating at home, or c) are shielding in line with public health guidance.

Accounting implications

The grant income will be recognised within other income on a straight-line basis over the period a relevant employee is off sick. There may be a debtor balance recognised depending upon when the cash was received from HMRC.

It is not appropriate to net the grant income off against wages and salaries costs (FRS 102 paragraph 2.52).

Tax implications

The tax treatment of the SSP rebate follows the same rules as for other employment-related Coronavirus support payments (see CJRS above).

Coronavirus Business Interruption Loan Scheme (CBILS) and Bounce Back Loans (BBLs)

CBILS and BBLs are essentially arrangements whereby a bank loan is supported by a government guarantee and the government pays any fees and interest for the first twelve months.

Accounting implications

Although the interest and fees under these schemes are paid by government directly to the lender for the first year (and not to the entity), the transfer of resources is generally considered to be a government grant from the perspective of the entity. The interest expense recognised in profit and loss will include the element paid by government directly to the lender. Views differ as to whether to present the assistance received from government towards the interest expense as other income or finance income.

Illustrative examples are available in the TAS helpsheet Accounting for coronavirus government support schemes under FRS 102.

Tax implications

Bank loans are treated for tax purposes by companies as loan relationships. The loan relationship rules require companies to bring amounts into account for tax purposes in accordance with GAAP. This means all the debits and credits arising from the loan relationship which when taken together, fairly represent the profits and losses on the loan for the accounting period in question. This includes bringing in amounts not just in the company's income statement but also, for example, the statement of changes in equity.

Hence, the amounts taken into account in this case are the credits for the grant income and debits for the deemed interest.

If the debits and credits are perfectly matched in each accounting period, then the overall tax effect should be nil. If there is a mismatch in timing or amount of grant and deemed interest for accounts purposes then there will also be a mismatch for tax purposes. For example, if the grant income is recognised in an earlier period than the deemed interest then the income may be taxed without a corresponding allowable expense. Although the expense will be recognised in the subsequent period, if there is not sufficient profit in that year to utilise the expense, it may need to be carried forward to off-set in future periods.

Repayments

Some entities have chosen to repay some of the support they have received from government.

Accounting implications

When an entity chooses to repay a grant for which it was eligible, it will be recognised when the repayment is made, or when there is a constructive obligation to make the repayment. A constructive obligation, in this context, might be when the company has made public its intention to make the repayment (FRS 102 paragraph 21.6).

The income and the repayment would be shown separately in profit or loss (FRS 102 paragraph 2.52).

Tax implications

Where a company makes a payment to a public authority to repay a relief from an expense which had the purpose of supporting the company in connection with coronavirus (eg, business rates relief), it may claim a corporation tax deduction equal to the lower of the repayment and the original liability being relieved, provided the liability would itself have been deductible. The deduction will arise in the same accounting period as the original liability would have been due and paid.

Further resources

More detailed guidance on the accounting implications, together with illustrative examples, is available in the helpsheets:

- Accounting for coronavirus government support schemes under FRS 102
- Accounting for coronavirus government support schemes under FRS 105

Further guidance on COVID-19-related issues includes:

- Fraud and government support – a guide for auditors
- Coronavirus and tax

ICAEW insights and guidance on tax, audit, financial reporting and other technical issues emerging from the coronavirus COVID-19 pandemic can be found at icaew.com/coronavirus/technical-updates-and-guidance.

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