

Technical Line

A closer look at how to account for government assistance received under the CHIPS Act

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What you need to know

- ▶ The semiconductor provisions of the CHIPS Act provide funding and loans to semiconductor manufacturers and certain participants in the supply chain. The provisions also include a 25% advanced manufacturing investment tax credit for investments in the manufacture of semiconductors and semiconductor manufacturing equipment in the US.
- ▶ Entities eligible to receive assistance under the CHIPS Act should determine the appropriate accounting guidance based on the terms and conditions of the assistance received.
- ▶ For-profit business entities that analogize to a grant or contribution accounting model must consider the disclosure requirements for government assistance under ASC 832.
- ▶ Various departments of the US government will issue additional resources to help entities understand the different programs and eligibility under the CHIPS Act. Entities should monitor developments related to CHIPS Act programs and continuously assess the accounting and reporting impacts of the CHIPS Act based on their own facts and circumstances.

Overview

The Creating Helpful Incentives to Produce Semiconductors and Science Act of 2022 (CHIPS Act) directs \$280 billion in federal funds to build a domestic supply chain for semiconductor chips and to fund scientific and technological research, in order to advance US economic and national security. This publication focuses on the semiconductor provisions of the CHIPS Act,

which includes \$52.7 billion allocated to the provisions supporting domestic manufacturing of semiconductors and \$24 billion estimated for an advanced manufacturing investment credit (AMIC). It does not focus on the remaining non-semiconductor provisions related to scientific and technological research and other activities.

The semiconductor provisions of the CHIPS Act contain funding to assist entities in supporting the law's objectives. Generally, assistance received under this law is implemented through a grant funding and a tax incentive mechanism. To receive the assistance, entities may be required to agree to certain conditions or restrictions commonly referred to as guardrails. For example, recipients are not permitted to build or expand chip fabrication plants in countries of concern and cannot use the money to repurchase stock, pay dividends or make other capital distributions.

Entities that receive assistance provided through programs established by the CHIPS Act need to carefully consider the terms of the programs to make sure they are eligible and to apply the appropriate accounting treatment. This includes monitoring ongoing developments related to the CHIPS Act programs and proposed regulations.

Manufacturing semiconductor provisions

Semiconductor manufacturers and semiconductor materials and equipment manufacturers looking to construct, expand or modernize US semiconductor facilities are eligible to apply for the domestic manufacturing incentives funding, which will be in the form of grants, loans and loan guarantees (i.e., not income tax credits).

The \$52.7 billion in funding under the manufacturing semiconductor provisions is allocated to four funds (CHIPS for America Fund, CHIPS for America Defense Fund, CHIPS for America International Technology Security and Innovation Fund and CHIPS for America Workforce and Education Fund). These funds provide incentives to develop domestic semiconductor manufacturing, conduct research and development, and create workforce development programs.

The CHIPS Act requires recipients to demonstrate significant labor and community investments, provide opportunities to small businesses and disadvantaged communities and make sure semiconductor incentives support equitable economic growth and development. The allocation of funds under these provisions will be administered by the Department of Commerce through various application processes.

Advanced manufacturing investment tax credit

The AMIC (Section 48D tax credit) is a 25% investment tax credit for investments in the manufacture of semiconductors and semiconductor manufacturing equipment. Entities are allowed to treat the credit as a payment against tax (direct pay) and receive a refund of such payment in the absence of any taxable income. The credit is provided for property that is placed in service after 31 December 2022. However, it does not apply to property for which the construction begins after 31 December 2026. In addition, in the case of any qualified property placed in service after 31 December 2022, but the construction of which began prior to 1 January 2023, the Section 48D tax credit is available only to the extent of the basis of qualified property attributable to the construction, reconstruction or erection after 9 August 2022 (the date of enactment of the CHIPS Act).

This aspect of the CHIPS Act is administered by the Internal Revenue Service (IRS) and is estimated to cost \$24 billion. This Section 48D tax credit can be retroactively "recaptured" by the IRS if a taxpayer undertakes certain activities associated with foreign countries of concern.

Government assistance accounting

Each government program established under the CHIPS Act has its own requirements that an entity must carefully assess to determine both its eligibility and the proper accounting treatment of any government assistance it receives. A for-profit business entity should evaluate whether the assistance is in the scope of existing US GAAP guidance, such as an income tax credit in the scope of Accounting Standards Codification (ASC) 740,¹ a payment for goods or services in the scope of ASC 606,² or a loan in the scope of ASC 470³ based on facts and circumstances (including the program's terms and conditions) before concluding that the appropriate accounting for the assistance is an analogy to a grant or a contribution model. The accounting and disclosure implications (e.g., timing of recognition, financial statement presentation) may vary significantly, depending on the outcome of this evaluation.

A not-for-profit entity that receives a government grant should apply ASC 958-605.⁴

How we see it

An entity's accounting for and disclosures about government assistance depend on the type of government assistance it receives. Legislation providing assistance may use terms such as "grant" or "credit" to describe the form of the assistance, but companies will need to carefully evaluate the substance of the legislation to determine the appropriate accounting.

Refundable tax credits may not be subject to the provisions of ASC 740, since receipt of such credits is not dependent on having taxable income.

Determining whether government assistance is in the scope of ASC 740

For-profit business entities need to evaluate the provisions of assistance provided under the CHIPS Act to determine whether the assistance is in the scope of ASC 740 or other accounting guidance. Assistance from a government entity that is not dependent on taxable income to be realized (e.g., a refundable credit) would generally be outside the scope of ASC 740. We observe that the CHIPS Act generally has the following provisions:

- ▶ Manufacturing semiconductor provisions: The incentives provided under these provisions are generally application-based in which the funding will be in the form of grants, loans and loan guarantees. The funding does not involve any taxing authorities and is not issued in the form of income tax credits.
- ▶ AMIC (Section 48D tax credit): These provisions generally allow for an entity to make a direct pay election and receive a payment of the tax credit in the absence of any taxable income (refundable tax credit).

Refer to section 2.5.1, *Determining whether government assistance is in the scope of ASC 740*, of our Financial reporting developments publication, **Income taxes**, for a discussion on whether the guidance in ASC 740 applies to the receipt of government assistance.

If entities determine that ASC 740 does not apply to the government assistance provided under the provisions of the CHIPS Act, for-profit business entities need to carefully evaluate the nature and characteristics of the assistance received to determine the appropriate accounting guidance to be applied. The section below highlights some considerations.

Accounting for government assistance outside of the scope of ASC 740

As discussed above, assistance from a government entity that is not dependent on taxable income to be realized (e.g., a refundable credit) would generally be outside of the scope of ASC 740. A for-profit business entity receiving such assistance considers whether the payment represents revenue in accordance with ASC 606 or a loan in accordance with ASC 470. If not, the entity accounts for the assistance in accordance with other GAAP by analogy (e.g., International Accounting Standard (IAS) 20,⁵ ASC 450-30⁶ or ASC 958-605). The evaluation should be performed based on facts and circumstances, including the terms and conditions of the various programs funded by the CHIPS Act.

If an entity determines that the assistance represents revenue from a contract with a customer, the transaction is subject to ASC 606. We believe ASC 606 would not apply to government assistance received through the provisions in the CHIPS Act unless the assistance is payment for goods or services transferred to the government by the recipients.

If an entity determines that it receives government assistance in the form of a loan, we generally believe that it should account for the assistance as debt under ASC 470, unless the loan is forgivable and the entity expects to meet the loan forgiveness criteria, in which case, it may be acceptable to account for it by analogy to a grant or contribution model rather than a loan.

When the government assistance received is in the form of a government grant and is not an income tax credit in the scope of ASC 740 or a loan and does not represent revenue, we generally believe that for-profit business entities should account for it by analogy to IAS 20. However, analogies to other guidance, such as ASC 958-605 for contributions received by not-for-profit entities or ASC 450-30 for gain contingencies, also may be appropriate. A not-for-profit entity that receives a government grant should apply ASC 958-605.

Before selecting an accounting policy for any government grant received, an entity should consider whether it has received a similar government grant in the past and has an accounting policy for such grant. If not, it should consider the facts and circumstances associated with the grant and which accounting model would best reflect the nature and substance of the grant. Regardless of the accounting model it applies, the entity should adequately disclose its accounting policy and the impact on the financial statements. A change to an existing policy is a voluntary change in accounting policy that requires a preferability analysis.

For-profit business entities that analogize to IAS 20

Under IAS 20, government grants fall into two categories: grants related to assets and grants related to income. The type of grant an entity receives will determine how it presents the grant on the financial statements. 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. IAS 20 defines grants related to income as all government grants other than those related to assets. The manner in which the grant is received does not affect the accounting method to be adopted. That is, a grant would be accounted for in the same manner regardless of whether it is received in cash or as a reduction of a liability to the government.

Government grants under IAS 20 are recognized when there is “reasonable assurance” that the entity will comply with the conditions attached to the grant and it will receive the grant.⁷ The term “reasonable assurance” is generally considered analogous to “probable” in US GAAP. However, once this threshold is met, an entity does not necessarily recognize the entire grant as income at that time.

An entity may receive several forms of the government assistance under the CHIPS Act to which a number of conditions are attached. In such cases, it may need to exercise judgment to determine whether the criteria for recognizing each of the grants have been met. Further, grants could have “recapture” provisions that require the entity to repay the grant if certain conditions are not satisfied. The entity needs to carefully consider these provisions to determine how they affect the entity’s accounting for the government assistance.

IAS 20 notes that receiving the grant does not provide conclusive evidence that the conditions attached to the grant have been or will be fulfilled.⁸ That is, entities are required to evaluate whether they have met the threshold for “reasonable assurance” before the grant can be recognized even if payment has been received for the grant. Further, we do not believe that simply having approval of an application to participate in a federal assistance program provides such evidence either.

How we see it

Determining whether the “reasonable assurance” threshold is met requires careful analysis of the conditions attached to each of the programs under the CHIPS Act. The evaluation is driven by facts and circumstances of an entity. The “reasonable assurance” threshold may be met before, upon or after receipt of payment. This determination must be thoughtfully assessed even if an entity has an approved application or has received payment. An entity may need to apply significant judgment in assessing whether there is “reasonable assurance.”

Grants should be recognized as income “on a systematic and rational basis over the periods in which the entity recognizes as expenses the related costs for which the grants are intended to compensate.”⁹ The method of income recognition should also consider any conditions or “recapture” provisions. Recognition of grants solely based on cash receipts would only be appropriate if no basis exists for allocating the grant to periods other than the one in which it was received.¹⁰

In many cases, the appropriate method to recognize the grant as income will be apparent. For example, grants related to specific expenses would be recognized in the same period that those expenses are recognized. Similarly, grants related to depreciable assets are usually recognized over the same periods in which depreciation expense on those assets is recognized.¹¹ Further, it may be appropriate to recognize part of a grant on one basis and the other part on another basis.¹² However, significant judgment will be required to determine whether it is appropriate to separate a grant into different elements and/or whether an entity may have received multiple grants that should be accounted for separately.

To the extent a grant becomes receivable to compensate an entity for expenses or losses already incurred, or for the purpose of giving immediate financial support to the entity with no future related costs (and for which there are no repayment or “recapture” features), the grant should be recognized as income in the period in which it becomes receivable.¹³

Presentation of grants related to assets

Under the CHIPS Act, we generally believe that certain manufacturing semiconductor provisions within the CHIPS for America Fund, and the AMIC (Section 48D tax credit) contain grants related to assets, given that the primary condition of the grants is that a qualifying entity purchase, construct or acquire long-term assets, such as property, plant and equipment. IAS 20 indicates that grants related to assets should be presented on the balance sheet using one of the following two methods, which should be applied consistently to all similar grants:

- ▶ The grants are presented as deferred income. The deferred income is then recognized as grant income over the useful life of the related asset(s), which is frequently the same period of depreciation for the related asset, although other periods may also be appropriate.¹⁴
- ▶ The grants are deducted from the carrying amount of the related asset. This results in the qualifying asset being recorded at a lower amount and, therefore, a reduction of depreciation expense over the life of the asset.¹⁵

The method selected is not expected to have an effect on net income.

Illustration 1 – Grants related to assets – Deferred income

When there is “reasonable assurance” that an entity will comply with the conditions attached to the grant provided under the CHIPS Act and the grant is presented as deferred income, the following journal entry is recorded (for more information, refer to the “Receivable or payable, or cash” section):

Dr. Receivable or payable, or cash
 Cr. Deferred income (liability)

In each of the subsequent reporting periods over the useful life of the asset, the following journal entry is recorded:

Dr. Deferred income (liability)
 Cr. Grant income

Illustration 2 – Grants related to assets – Deduct from the carrying amount of the related asset

When there is “reasonable assurance” that an entity will comply with the conditions attached to the grant provided under the CHIPS Act and the grant is deducted from the carrying amount of the related asset, the following journal entry is recorded (for more information, refer to the “Receivable or payable, or cash” section):

Dr. Receivable or payable, or cash
 Cr. Property, plant and equipment

Note: Reducing the carrying amount of the related asset will also result in a reduction to the depreciation expense recognized over the useful life of the asset (i.e., depreciation expense will be calculated based on the reduced carrying amount of the related asset).

Presentation of grants related to income

Certain application-based grants under the CHIPS Act may be dependent on expanding workforce size, training or development opportunities, or maintaining prevailing wages. Although these requirements may indicate that these provisions represent grants related to income (i.e., they are not grants related to assets), the determination will be based on facts and circumstances, which may require judgment. Grants related to income can be presented under IAS 20 in one of the following two ways:

- A credit in the income statement, either separately or under a general heading such as “other income”¹⁶
- A reduction to the related expense

These types of grants are recognized in the income statement beginning in the period that the “reasonable assurance” threshold has been met, which will likely depend on the conditions of the grant, and as the related costs for which the grants are intended to compensate are recognized as expenses. As discussed above, the appropriate method to recognize the grant as income will be apparent in many cases. For example, grants and subsidies to reimburse expenses incurred or to supplement sales proceeds are recorded in the period in which the related expenses or sales are recorded. Grants and subsidies received to defray future expenses (e.g., salaries of a new labor force) or to supplement future sales revenues are deferred and recognized in proportion to the expenses or sales to which they relate.

Entities should carefully evaluate the substance of the government assistance arrangement and the conditions attached to the grant.

Illustration 3 – Grants related to income – Recognize other income in the current period

When there is “reasonable assurance” that an entity will comply with the conditions attached to the grant provided under the CHIPS Act and the grant is presented as other income in the current period, the following journal entry is recorded (for more information, refer to the “Receivable or payable, or cash” section):

Dr. Receivable or payable, or cash
Cr. Other income

Illustration 4 – Grants related to income – Recognize other income in future periods

When there is “reasonable assurance” that an entity will comply with the conditions attached to the grant provided under the CHIPS Act and the grant is presented as other income in future periods, the following journal entry is recorded (for more information, refer to the “Receivable or payable, or cash” section):

Dr. Receivable or payable, or cash
Cr. Deferred income (liability)

In each of the subsequent reporting periods, other income is recognized in proportion to the expenses or sales to which the grant relates, through the following journal entry:

Dr. Deferred income (liability)
Cr. Other income

Illustration 5 – Grants related to income – Reduce current period expenses

When there is “reasonable assurance” that an entity will comply with the conditions attached to the grant provided for under the CHIPS Act and the grant is presented as a reduction to the related expense, the following journal entry is recorded (for more information, refer to the “Receivable or payable, or cash” section):

Dr. Receivable or payable, or cash
Cr. Expense

Illustration 6 – Grants related to income – Reduce future period expenses

When there is “reasonable assurance” that an entity will comply with the conditions attached to the grant provided for under the CHIPS Act and the grant is presented as a reduction to the related expense, the following journal entry is recorded (for more information, refer to the “Receivable or payable, or cash” section):

Dr. Receivable or payable, or cash
Cr. Deferred income (liability)

In each of the subsequent reporting periods, a reduction to the related expense is recognized in proportion to the expenses incurred to which the grant relates, through the following journal entry:

Dr. Deferred income (liability)
Cr. Expense

Entities should carefully evaluate the substance of the grant and the conditions attached to the grant and should adopt a presentation method that is consistently applied to similar fact patterns.

Receivable or payable, or cash

The above examples illustrate the accounting and presentation when there is “reasonable assurance” that an entity will comply with the conditions attached to the grant and it will receive the grant. The “reasonable assurance” threshold may be met before, upon or after receipt of cash, and an entity will need to evaluate the facts and circumstances for the grant when recognizing it in its financial statements. In certain situations, when the “reasonable assurance” threshold is met before cash is received, it may be appropriate to record an asset (e.g., income tax receivable, other receivable). For refundable tax credits, it may also be acceptable to reduce income tax payable when the entity expects to use the refundable tax credits earned to reduce the amount of tax owed to the US government on the current year’s tax return.

Not-for-profit entities and for-profit business entities that analogize to ASC 958-605

Generally, under ASC 958-605, government assistance is treated as contributions received and should be recognized as revenue or gains in the period received, unless donor-imposed conditions exist. If a recipient entity determines that it must meet certain conditions imposed by the government entity to be entitled to receive or keep the grant, recognition of contributions in the income statement is deferred until the condition, or conditions, are “substantially met.”¹⁷ In certain situations, the condition or conditions imposed by the government entity may be “substantially met” prior to the receipt of cash and it may be appropriate to record an asset, such as a receivable when the condition, or conditions, are “substantially met.”

While the term “substantially met” is not defined in the standard, it is generally considered to be a higher threshold than “probable.” The likelihood that conditions will be met is not considered by a not-for-profit entity in determining whether grants are conditional or unconditional. Until conditions have been “substantially met,” or explicitly waived, the conditional contribution received should be accounted for as a refundable advance.

The classification of contributions received as revenue or gains depends on whether they are transactions that are part of the entity’s ongoing major or central activities or are peripheral or incidental to the entity.¹⁸ If they are part of the entity’s ongoing major or central activities, they should be presented as revenue (separate from revenue from contracts with customers). Otherwise, they should be presented as gains.

If the government assistance received under the CHIPS Act is part of the entity’s ongoing major or central activities, the government assistance should be presented as revenue (separate from revenue from contracts with customers). If the government assistance received under the CHIPS Act is peripheral or incidental to the entity, the government assistance should be presented as a gain.

For-profit business entities that analogize to ASC 450-30

Gain contingencies usually are not recognized in the financial statements until the period in which all contingencies are resolved and the gain is realized or realizable. Determining whether a gain can be recognized may require judgment, and the entity should consider all facts and circumstances, including:

- Whether a legally enforceable contract specifies the terms of the settlement
- Whether the counterparty has the ability to pay the settlement

Prior to realization, the existence of gain contingencies may require disclosure, but entities should be careful to avoid misleading users of the financial statements about the likelihood of the realization of the gain contingency.

Gain contingencies are considered nonrecognized subsequent events (i.e., gain contingencies are not recognized until the period in which all contingencies are resolved, even if resolution occurs after the balance sheet date but before the financial statements are issued or are available to be issued).

Statement of cash flows considerations

The presentation of government assistance under the CHIPS Act on the statement of cash flows depends on whether the assistance is received in cash and the framework that an entity applies to account for the transaction.

If the government assistance is not refunded in cash (i.e., the assistance would offset any income tax liability due), there are no cash flow effects on the statement of cash flows.

If the government assistance is refunded to the entity in cash, we believe classification on the statement of cash flows generally aligns with the entity's chosen balance sheet presentation. For example, when an entity applies IAS 20 by analogy and the government assistance is related to assets, an entity can choose to present the amount of the assistance separately as deferred income or deduct it from the carrying amount of the related asset on the balance sheet. On the statement of cash flows, cash received by an entity that is presented as deferred income is presented as an operating cash inflow. Cash received by an entity that is deducted from the carrying amount of the related asset is presented as an investing cash inflow. When an entity applies IAS 20 by analogy and the government assistance relates to income, we believe the cash received is generally an operating cash inflow. For not-for-profit entities and for-profit business entities that analogize to ASC 958-605 and for-profit business entities that analogize to ASC 450-30, the cash received is generally an operating cash inflow.

In addition, the cash received for government assistance should be presented gross of any related cash outflows. For example, if an entity receives the cash from government assistance in the same period it pays for a related asset, the cash inflow and cash outflow are required to be presented separately (i.e., gross presentation) on the statement of cash flows and not combined (i.e., net presentation), even if the purchase of the asset and the government assistance are presented net on the balance sheet.

Prior to receiving the government assistance in cash, there are no cash flow effects on the statement of cash flows.

An entity that prepares its statement of cash flows using the indirect method is required to disclose the amount of income taxes paid (ASC 230-10-50-2). When refundable credits (i.e., AMIC) are used to reduce income taxes due on the tax return (i.e., credits are not refunded), the income taxes paid disclosure would reflect the actual amount of cash paid for income taxes.

Financial statement disclosures

The financial statement disclosures of government assistance depend on which accounting standards an entity applies or analogizes to (e.g., IAS 20, ASC 958-605). ASC 832¹⁹ requires for-profit business entities that account for transactions with a government by analogizing to a grant or contribution accounting model (e.g., IAS 20, ASC 958-605) to make certain annual disclosures. That is, the disclosure requirements in ASC 832 don't apply to transactions with a government that are accounted for in accordance with existing US GAAP (e.g., ASC 450 on contingencies, ASC 740 on income taxes, ASC 606 on revenue from contracts with customers, ASC 470 on debt). For-profit business entities would look to the disclosure requirements of those US GAAP standards for required disclosures. Not-for-profit entities within the scope of ASC 958-605 are excluded from ASC 832's disclosure requirements.

Entities need to consider whether the government assistance presents any new or heightened financial reporting risks and whether internal controls are still sufficiently precise to mitigate the risks.

ASC 832 requires for-profit business entities to disclose in their annual financial statements the following information about transactions with a government in its scope:

- ▶ The nature of the transactions, including a general description of the transactions and the form in which the assistance has been received (e.g., cash, other assets)
- ▶ The accounting policies used for the transactions as required by ASC 235-10-50-1
- ▶ The balance sheet and income statement line items in which the transactions are recorded and the amounts reflected in each line item in the current reporting period
- ▶ The significant terms and conditions of the transactions (e.g., the duration or period of the agreement, commitments made by the reporting entity and the government, any provisions under which the government is permitted to “recapture” amounts it provided)

Internal control over financial reporting

Entities that report on internal control over financial reporting must also consider whether the assistance received under the CHIPS Act presents any new or heightened financial reporting risks and whether internal controls continue to be sufficiently precise to mitigate those risks.

Entities should have controls in place to make sure they select and consistently apply an appropriate accounting framework and accounting policies. These controls should address an entity’s policies for determining the appropriate guidance for the recognition, measurement, presentation and disclosure of government assistance. These controls should also address the accounting effects of the ongoing developments in both the entity’s business and the CHIPS Act programs. Entities should maintain appropriate books and records, regardless of the underlying accounting methodology applied.

Endnotes:

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- ¹ ASC 740, *Income Taxes*.
 - ² ASC 606, *Revenue from Contracts with Customers*.
 - ³ ASC 470, *Debt*.
 - ⁴ ASC 958-605, *Not-for-Profit Entities – Revenue Recognition – Contributions*.
 - ⁵ IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*.
 - ⁶ ASC 450-30, *Gain Contingencies*.
 - ⁷ IAS 20.7.
 - ⁸ IAS 20.8.
 - ⁹ IAS 20.12.
 - ¹⁰ IAS 20.16.
 - ¹¹ IAS 20.17.
 - ¹² IAS 20.19.
 - ¹³ IAS 20.20.
 - ¹⁴ IAS 20.26.
 - ¹⁵ IAS 20.27.
 - ¹⁶ IAS 20.29.
 - ¹⁷ ASC 958-605-25-5F.
 - ¹⁸ ASC 958-605-25-2.
 - ¹⁹ ASC 832, *Government Assistance*.

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