# Government guarantees for SMEs and the arts

## Reporting Update

7 May 2021, 21RU-011

## Highlights

- New schemes launched by the Australian Government to aid economic recovery
- SME Recovery Loan Scheme expands on a previous government assistance package
- Show Starter Loan Scheme provides additional support to the arts and entertainment sector

**New schemes have been launched to complement the existing suite of programs**

## New schemes launched by the Australian Government to aid economic recovery

In our Reporting Update issued on 6 May 2020 we provided an overview of several Australian Government initiatives aimed at supporting the flow of credit during the coronavirus pandemic and discussed the associated financial reporting implications for both the lender and the borrower.

Since then, the Australian Government has launched new schemes which add to the existing suite of initiatives.

Similar to the original suite of initiatives, these new programs are specifically targeted at small and medium enterprises (SMEs) and are intended to help ensure that these entities continue to have access to credit while the economy recovers from the effects of the pandemic.

The new schemes include the:

- SME Recovery Loan Scheme, and
- Show Starter Loan Scheme.

The SME Recovery Loan Scheme also applies to eligible businesses that are impacted by the March 2021 floods.

This publication provides information about the new schemes and the related financial reporting implications for both the lender and the borrower.

**SMEs continue to be a major focus given their importance to the Australian economy**

# SME Recovery Loan Scheme expands on a previous government assistance package

## What is it?

Under the scheme, the Government provides a guarantee for eligible loans granted by participating lenders equal to 80% of the loan amount. The loans can be for terms up to 10 years, with an optional repayment holiday period (during which no repayments of principal or interest are required however interest continues to accrue on the loan balance). Loans can be either unsecured or secured (excluding residential property) with interest rates set by the lenders, subject to a cap of 7.5 per cent for fixed rate loans and BBSY + 7.5% for variable rate loans.

Similar to the 'Coronavirus SME Guarantee Scheme', the Government compensates the lender for any losses incurred up to the guaranteed amount of the loan and this amount can be claimed at the earlier of write- off or impairment, in line with the lender's standard process.

The key difference between the new scheme and the existing Coronavirus SME Guarantee Scheme is that the Government guarantees 80% of the amount borrowed under the SME Recovery Loan Scheme whereas it only guarantees 50% under the existing scheme. In addition, loans granted under the new scheme can be for up to 10 years whereas the maximum term under the existing scheme is 3 years.

## Accounting implications for lenders

Whilst some of the terms of the program may differ (as noted above), the accounting for loans granted under the SME Recovery Loan Scheme is the same as for those granted under the Coronavirus SME Guarantee Scheme. That is, because loans are granted at market rates of interest that consider the benefit derived from the guarantee, the lender will only recognise a loan asset (generally a receivable from the customer) and does not separately recognise a government grant under AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance*.

The guarantee is considered to be an integral part of the loan and therefore impacts the **measurement** of expected credit losses (ECLs) associated with the loan by reducing the amount that the lender may expect to lose in the event a default occurs, that is, it affects the "loss given default" estimate, reflecting that the government guarantees 80% of the loan balance.

### Disclosure

The disclosure of information about the credit enhancement held on such loans will enable users of financial statements to understand how the credit risks are being managed. This may be achieved by providing a narrative description of the nature, extent and duration of the guarantee, the volume of loans covered by the guarantee and how the guarantee impacts the estimation of ECLs. This includes the quantification of the extent to which the guarantee mitigates the credit risk for such loans that are credit impaired at the reporting date.

**Example disclosure**

Below is an illustrative disclosure that a lender participating in one of these schemes may consider providing in its annual financial statements.

***Collateral held and other credit enhancements***

*In respect of loans and advances to corporate customers the Group may take collateral in the form of a first charge over real estate, floating charges over all corporate assets and other liens and guarantees. In response to the COVID-19 coronavirus pandemic the Australian Commonwealth Government has offered guarantees over new loans granted during the period to small and medium sized enterprises. Depending on the nature of the borrower and their individual eligibility the extent of the guarantee provided by the Government is either 50% or 80% of the loan amount. Loans subject to the 50% guarantee can be for a maximum term of 3 years whereas loans subject to the 80% guarantee can be for a maximum term of 10 years. All loans are granted in accordance with the Group's standard lending credit criteria and are priced at commercial rates of interest*[1].

*The Group can claim losses incurred on the guaranteed loans at the earlier of when the loan becomes impaired (i.e. moves to Stage 3) or is written off in accordance with the Group's credit risk management policies.*

*The Group factors in the impact of the guarantees when estimating expected credit losses (ECLs) by reducing the amount expected to be lost in the event of a default by the borrower (the "loss given default" estimate). The guarantee does not impact the Group's staging assessment of these loans.*

*As at the reporting date, the Group has granted $7m of loans subject to the 50% guarantee (2020: $3m) and $4m of loans subject to the 80% guarantee (2020: nil). None of the loans granted under the schemes were impaired or written off as at the reporting date (2020: nil).*

## Accounting implications for SME borrowers

### Measurement of loan payable and accounting for Government assistance

There is discussion on whether borrowers should recognise a government grant for the government guarantee. In our view entities have an accounting policy choice to account for this on a "gross" or "net" basis and this accounting policy must be applied consistently.

If an entity applies the gross approach to government assistance, then the guarantee is accounted for as a separate government grant under AASB 120. That is, it recognises the loan payable to the lender by discounting the contractual cash flows at the market rate of interest as if there had been no government guarantee, which would be higher than the contracted rate. It then separately recognises a liability which represents the benefit of the government guarantee, measured as the difference between the value of the loan recognised and the amount received. This liability is amortised over time to the income statement on a systematic basis over the term of the loan.

If an entity applies the net approach to government assistance, the government benefit is considered part of the unit of account in determining the fair value of the loan, that is, the entity recognises a loan payable to the lender by discounting the contractual cash flows at the rate of interest charged by the lender.

### Disclosure

Borrowers should consider including information about the nature and extent of government assistance received and how it has been accounted for in the

[1] Given the loans are granted on an arm's length basis in accordance with the participating lenders standard credit criteria (subject to borrowers meeting the government's eligibility criteria) we have assumed the rate will reflect a market rate of interest.

financial statements. As part of the liquidity risk disclosures, the payment profile of the funding arrangement is included in the maturity analysis of liabilities.

Our *Guides to financial statements* are designed to help you to prepare financial statements in accordance with IFRS® Standards. We have published a *COVID-19 supplement* which illustrates additional disclosures on accounting issues arising from the COVID-19 coronavirus pandemic.

**Entities in the arts and entertainment industry are also able to obtain government assistance to aid in their recovery**

## Show Starter Loan Scheme provides additional support to the arts and entertainment sector

### What is it?

This scheme is similar to the SME Recovery Loan Scheme except that it is targeted at eligible arts and entertainment entities that have been adversely affected by COVID-19. The other key difference between the Show Starter Loan Scheme and the SME Recovery Loan Scheme is that under this scheme the government will guarantee 100% of the amount borrowed (rather than 80% as is the case for SMEs).

Loans will continue to be provided by participating lenders at market rates taking into consideration the impact of the guarantee. Unlike the SME loans, there is no cap on the interest rate that may be charged under this scheme.

### Accounting and disclosure implications

The financial reporting considerations for the Show Starter Loan Scheme are the same as those noted above in relation to the SME Recovery Loan Scheme for bother lenders and borrowers.

***"The Commonwealth Government remains focussed on ensuring that SMEs, which are vital to the Australian economy's revival, continue to have access to credit as they navigate through to the other side of the COVID-19 coronavirus pandemic. In addition, new support measures have been launched which focus on the arts and entertainment sector, being one of the worst affected by the pandemic. The new and updated schemes involve the provision of guarantees by the Commonwealth. Entities participating in these programmes need to consider the financial reporting impacts in their upcoming financial statements".***

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