

International Accounting Standard (IAS-8)

*Accounting Policies, Changes in
Accounting Estimates and Errors*

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Objective Of IAS 8

- ➤ *it prescribes the criteria for:*
- ○ *selection of accounting policies;*
- ○ *changes in accounting policies;*
- ○ *accounting treatment;*
- ○ *disclosure of changes in accounting policies;*
- ○ *changes in accounting estimates; And*
- ○ *correction of errors;*

The achievement of the objective would result in:

- ➤ *enhancement of:*
- ○ *relevance and reliability of financial statements;*
- ○ *comparability of financial statements with the financial statements of other entities;*

WHAT ARE ACCOUNTING POLICIES?

- *These are:*
 - ➤ *Specific principles;*
 - ➤ *Bases;*
 - ➤ *Conventions;*
 - ➤ *Rules;*
 - ➤ *Practices;*
- *These are applied in preparing and presenting financial statements.*

RETROSPECTIVE APPLICATION

- *Retrospective application is applying a new accounting policy to transactions, other events and conditions as if that policy had always been applied.*

RETROSPECTIVE RESTATEMENT

- *Retrospective restatement is correcting the recognition, measurement and disclosure of amounts of elements of financial statements as if a prior period error had never occurred.*

IMPRACTICABLE

- *Applying a requirement is impracticable when the entity cannot apply it after making every possible effort.....*

PROSPECTIVE APPLICATION

- *Prospective application of a change in accounting policy and of recognizing the effect of a change in an accounting estimate, respectively, are:*
 - *Applying the new accounting policy to transactions, other events and conditions occurring after the date as at which the policy is changed; and.*
 - *Recognizing the effect of the change in the accounting estimate in the current and future periods affected by the change.*

Who will identify the change in financial statements is inevitable



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USERS OF FINANCIAL STATEMENTS

USERS OF FINANCIAL STATEMENTS ARE ASSUMED TO HAVE A REASONABLE KNOWLEDGE OF BUSINESS AND ECONOMIC ACTIVITY AND ACCOUNTING AND A WILLINGNESS TO STUDY THE INFORMATION WITH REASONABLE DILIGENCE.

- *[Para 25 of Framework for the preparation and presentation of financial statements.]*

CHARACTERISTICS OF AN ACCOUNTING POLICY

- *In devising an accounting policy, it should be:*
 - ➤ *relevant;*
 - ➤ *reliable;*
 - ➤ *faithful;*
 - ➤ *having economic substance;*
 - ➤ *neutral;*
 - ➤ *prudent;*
 - ➤ *complete;*

CHARACTERISTICS OF AN ACCOUNTING POLICY... continued

- *Relevant to the economic decision making needs of user; and*
- *Reliable in that the financial statements:*
 - *Represents faithfully the financial position, financial performance and cash flows of the entity;*
 - *Reflect the economic substance of transactions, other events and conditions, and not merely legal form;*
 - *Are prudent; and*
 - *Are complete in all material respects.*

CHARACTERISTICS OF AN ACCOUNTING
POLICY... continued

CONSISTENCY

What are not change in accounting policies?

- *The following are not change in accounting policies:*
- *The application of an accounting policy for transactions, other events or conditions that differ in substance from those previously occurring; and*
- *The application of a new accounting policy for transactions, other events or conditions that did not occur previously or were immaterial.*

Accounting treatment of change in accounting policy

- *When a change in accounting policy is applied retrospectively, the entity shall adjust the opening balances of each affected component of equity for the earliest prior period presented and the other comparative amounts disclosed for each prior period presented as if the new accounting policy had always been applied.*
- *When it is impracticable to determine the cumulative effect, at the beginning of the current period, of applying a new accounting policy to all prior periods, the entity shall adjust the comparative information to apply the new accounting policy prospectively from the earliest date practicable.*

DISCLOSURE REQUIREMENTS OF CHANGE IN ACCOUNTING POLICY

- ➤ *Title of the standard or interpretation*
- ➤ *Transitional provision if applicable*
- ➤ *Nature of change*
- ➤ *Description of transitional provision*
- ➤ *For the current period and each prior period presented, to the extent practicable, the amount of adjustment:*
 - ○ *For each financial statement line item affected;*
 - ○ *Earnings per share – revised*

WHAT IS A CHANGE IN ACCOUNTING ESTIMATE?

- ➤ *An adjustment of carrying amount of an asset or liability;*
- ➤ *An adjustment of the amount of periodic consumption of an asset; that results from:*
 - *The assessment of the present status of assets and liabilities*
 - *Expected future benefits of assets*
 - *Obligations associated with liabilities*
- ➤ *Change in accounting estimates result from:*
 - *New information; or*
 - *New developments*
- ➤ *Are NOT corrections of errors;*

REASON FOR ESTIMATION

- *When an item of financial statements cannot be measured precisely, it can only be estimated. This is because of:*
 - ➤ *Uncertainties inherent in the business;*
 - ➤ *Where judgments are involved;*

Where estimation is required?

- *Estimates may be required of:*
 - ➤ *Bad debts;*
 - ➤ *Inventory obsolescence;*
 - ➤ *Fair value of financial assets or financial liabilities;*
 - ➤ *The useful lives of, or expected pattern of consumption of the future economic benefits embodied in, depreciable assets; and*
 - ➤ *Warranty obligation etc*

When change in accounting estimate becomes necessary

- ➤ *If changes occur in the circumstances on which the estimate was based; or*
- ➤ *As a result of a new information; or*
- ➤ *More experience*

Recognition criteria of change in accounting estimate

- *Adjusting the carrying amount of the related asset, liability or equity item in the period of change recognizes a change in an accounting estimate.*
- *Example:*
- *Management estimates that provision for doubtful debts is estimated up to 5 percent of the total population of trade debts. However, upon identifying the age of the trade debts, it revealed that bad debts are about 6.5 percent of total population of trade debts. Management immediately recognizes the increase in bad debts expense in the books of accounts.*

DISCLOSURE REQUIREMENTS OF CHANGE IN ACCOUNTING ESTIMATE

- *Ø Nature and amount of a change in an accounting estimate for the current year and future period if practicable;*
- *Ø If estimation is impracticable, disclosure of this fact;*

ERRORS

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WHAT ARE PRIOR PERIOD ERRORS?

- ➤ *Omissions from; or*
- ➤ *Misstatements in*
- *The financial statements for one or more prior periods arising from:*
- *Continued.....*

WHAT ARE PRIOR PERIOD ERRORS? Continued.....

- ➤ *Failure to use or misuse of reliable information that was available when financial statements for those periods were authorized for issue;*
- ➤ *Failure to use or misuse of reliable information that could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.*

Examples of prior period errors are:

- ➤ *Effect of mathematical mistakes*
- ➤ *Mistakes in applying accounting policies*
- ➤ *Oversight and misinterpretation of facts and fraud.*

Rectification Criteria

- *An entity shall correct material prior period errors retrospectively in the first set of financial statements authorized for issue after their discovery by:*
 - ➤ *Restating the comparative amounts for the prior period(s) presented in which the error occurred; or*
 - ➤ *If the error occurred before the earliest prior period presented, restating the opening balances of assets, liabilities and equity for the earliest prior period presented.*

LIMITATION ON RETROSPECTIVE RESTATEMENT

- *Limitation on period specific effect*

- *When it is impracticable to determine the period specific effects of an error on comparative information for one or more prior periods presented, the entity shall restate the opening balances of assets, liabilities and equity for the earliest period for which retrospective restatement is practicable (which may be the current period).*

- *Limitation on cumulative effect*

- *When it is impracticable to determine the cumulative effect, at the beginning of the current period, of an error on all prior periods, the entity shall restate the comparative information to correct the error prospectively from the earliest date practicable.*

DISCLOSURE REQUIREMENTS

- ➤ *Nature of the prior period error*
- ➤ *To the extent practicable, the amount of the correction:*
 - ○ *For each financial statement line item affected; and*
 - ○ *Revision in earnings per share (EPS)*
- ➤ *The amount of the correction at the beginning of the earliest prior period presented; and*
- ➤ *If retrospective restatement is impracticable for a particular prior period, the circumstances that led to the existence of that condition and a description of how and from when the error has been corrected.*

Effective date of IAS-8

- *This standard is applicable from annual periods beginning on or after 1 January 2005.*

End of slides

Thank you

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