Exposure Draft

Accounting Standard (AS) 8
Accounting Policies, Changes in Accounting Estimates and Errors

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Accounting Standards Board
The Institute of Chartered Accountants of India

Exposure Draft

Accounting Standard (AS) 8, *Accounting Policies, Changes in Accounting Estimates and Errors*

(The Indian Accounting Standards (Ind AS), as notified by the Ministry of Corporate Affairs in February, 2015, have been applicable to the specified class of companies. For other class of companies, i.e., primarily the unlisted entities having net worth less than Rs. 250 crores, Accounting Standards, as notified under Companies (Accounting Standards) Rules, 2006, has been applicable. However, the Ministry of Corporate Affairs has requested the Accounting Standards Board of The Institute of Chartered Accountants of India (ICAI) to upgrade Accounting Standards, as notified under Companies (Accounting Standards) Rules, 2006, to bring them nearer to Indian Accounting Standards. Accordingly, the Accounting Standards Board, ICAI, initiated to upgrade these standards which will be applicable to all companies having net-worth less than Rs. 250 crores including non-corporate entities. While formulating these Accounting Standards, the Accounting Standards Board, ICAI, decided to maintain the consistency with the paragraph numbers and with the numbering of Standards of the Indian Accounting Standards).

In this direction, following is the Exposure Draft of the upgraded Accounting Standard (AS) 8, Accounting Policies, Changes in Accounting Estimates and Errors, issued by the Accounting Standards Board of the ICAI, for comments. The Board invites comments on any aspect of this Exposure Draft. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.

Comments can be submitted using one of the following methods so as to receive not later than December 07, 2015:

1. *Electronically: click on* ***http://www.icai.org/comments/asb/*** *to submit comments online*
2. *Email: Comments can be sent at commentsasb@icai.in*
3. *Postal: Deputy Director, Accounting Standards Board, The Institute of Chartered Accountants of India, ICAI Bhawan, Post Box No. 7100, Indraprastha Marg, New Delhi – 110 002*

Further clarifications on any aspect of this Exposure Draft may be sought by e-mail to geetanshu.bansal@icai.in.

(This Accounting Standard includes paragraphs set in ***bold*** *type and plain type, which have equal authority. Paragraphs in* ***bold*** *type indicate the main principles.)*

Accounting Standard (AS) 8

Accounting Policies, Changes in Accounting Estimates and Errors

*(This Accounting Standard includes paragraphs set in **bold** type and plain type, which have equal authority. Paragraphs in **bold** type indicate the main principles.)*

Objective

1 The objective of this Standard is to prescribe the criteria for selecting and changing accounting policies, together with the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates and corrections of errors. The Standard is intended to enhance the relevance and reliability of an entity's financial statements, and the comparability of those financial statements over time and with the financial statements of other entities.

2 Disclosure requirements for accounting policies, except those for changes in accounting policies, are set out in AS 1, *Presentation of Financial Statements*.

Scope

3 **This Standard shall be applied in selecting and applying accounting policies, and accounting for changes in accounting policies, changes in accounting estimates and corrections of prior period errors.**

4 [Refer Appendix 1].

Definitions

5 The following terms are used in this Standard with the meanings specified:

***Accounting policies* are the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements.**

A *change in accounting estimate* is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future

benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors.

(i) ***Accounting Standards (ASs):*** **for companies, the Accounting Standards other than Indian Accounting Standards prescribed under the Companies Act2013 ; and**

(ii) for entities other than companies, the accounting standards issued by the Institute of Chartered Accountants of India(ICAI).

Material **Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.**

Prior period errors **are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:**

(a) was available when financial statements for those periods were approved for issue; and

(b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

Retrospective computation **is calculating the impact of a new accounting policy to transactions, other events and conditions as if that policy had always been applied.**

Impracticable **Applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so. For a particular prior period, it is impracticable to calculate the impact of a change in an accounting policy retrospectively or to make a retrospective computation to correct an error if:**

(a) the effects of the retrospective computation are not determinable;

(b) the retrospective computation requires assumptions about what management's intent would have been in that period; or

(c) the retrospective computation requires significant estimates of amounts and it is impossible to distinguish objectively information about those estimates that:

(i) provides evidence of circumstances that existed on the date(s) as at which those amounts are to be recognised, measured or disclosed; and

(ii) would have been available when the financial statements for that prior period were approved for issue from other information.

***Prospective application* of a change in accounting policy and of recognising the effect of a change in an accounting estimate, respectively, are:**

(a) applying the new accounting policy to transactions, other events and conditions occurring after the date as at which the policy is changed; and

(b) recognising the effect of the change in the accounting estimate in the current and future periods affected by the change.

6 Assessing whether an omission or misstatement could influence economic decisions of users, and so be material, requires consideration of the characteristics of those users. The *Framework for the Preparation and Presentation of Financial Statements in accordance with Accounting Standards* issued by the Institute of Chartered Accountants of India states in paragraph 26 that 'users are assumed to have a reasonable knowledge of business and economic activities and accounting and study the information with reasonable diligence.' Therefore, the assessment needs to take into account how users with such attributes could reasonably be expected to be influenced in making economic decisions.

Accounting policies

Selection and application of accounting policies

7 **When an AS specifically applies to a transaction, other event or condition, the accounting policy or policies applied to that item shall be determined by applying the AS.**

8 ASs set out accounting policies that result in financial statements containing relevant and reliable information about the transactions, other events and conditions to which they apply. Those policies need not be applied when the effect of applying them is immaterial. However, it is inappropriate to make, or leave uncorrected, immaterial departures from ASs to achieve a particular presentation of an entity's financial position, financial performance or cash flows.

9 Some ASs are accompanied by application guidance that is integral part of AS to assist entities in applying their requirements. Such application guidance is mandatory.

10 In the absence of an AS that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in information that is:

(a) relevant to the economic decision-making needs of users; and

(b) reliable, in that the financial statements:

(i) represent faithfully the financial position, financial performance and cash flows of the entity;

(ii) reflect the economic substance of transactions, other events and conditions, and not merely the legal form;

(iii) are neutral, ie free from bias;

(iv) are prudent; and

(v) are complete in all material respects.

11 In making the judgement described in paragraph 10, management shall refer to, and consider the applicability of, the following sources in descending order:

(a) the requirements in ASs dealing with similar and related issues; and

(b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Framework*.

12 In making the judgement described in paragraph 10, management may also first consider the guidance given in Indian Accounting Standards (Ind AS). In absence thereof, the management consider the following in the following order:

(i) most recent pronouncements of the Institute of Chartered Accountants of India and

(ii) most recent pronouncement of the International Accounting Standards Board and

(iii) those of the other standard-setting bodies that use a similar conceptual framework to develop accounting standards,

(iv) other accounting literature and accepted industry practices, to the extent that these do not conflict with the sources in paragraph 11.

Consistency of accounting policies

13 **An entity shall select and apply its accounting policies consistently for similar transactions, other events and conditions, unless an AS specifically requires or permits categorisation of items for which different policies may be appropriate. If an AS requires or permits such categorisation, an appropriate accounting policy shall be selected and applied consistently to each category.**

Changes in accounting policies

14 **An entity shall change an accounting policy only if the change:**

(a) is required by an AS or by any statute or pronouncement specified in paragraph 12; or

(b) results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows.

15 Users of financial statements need to be able to compare the financial statements of an entity over time to identify trends in its financial position, financial performance and cash flows. Therefore, the same accounting policies are applied within each period and from one period to the next unless a change in accounting policy meets one of the criteria in paragraph 14.

16 **The following are not changes in accounting policies:**

(a) the application of an accounting policy for transactions, other events or conditions that differ in substance from those previously occurring; and

(b) the application of a new accounting policy for transactions, other events or conditions that did not occur previously or were immaterial.

17 **The initial application of a policy to revalue assets in accordance with other Accounting Standards, such as AS 16, *Property, Plant and Equipment,* or, is a change in an accounting policy to be dealt with as a revaluation in accordance with that AS, rather than in accordance with this Standard.**

18 Paragraphs 19–23 and 27- 28 do not apply to the change in accounting policy described in paragraph 17.

Accounting for changes in accounting policies

19 **Subject to paragraph 23:**

(a) an entity shall account for a change in accounting policy resulting from the initial application of an AS or a statute or a pronouncement specified in paragraph 12 in accordance with the specific transitional provisions, if any, in that AS or the statute or a pronouncement specified in paragraph 12, as the case may be; and

(b) when an entity changes an accounting policy upon initial application of an AS or a statute or a pronouncement specified in paragraph 12 that does not include specific transitional provisions applying to that change, or changes an accounting policy voluntarily, it shall compute the effect of the change retrospectively.

20 For the purpose of this Standard, early application of an AS is not a voluntary change in accounting policy.

21 [Refer Appendix 1].

Retrospective computation

22 Subject to paragraph 23, when the retrospective computation is made in accordance with any change in accounting policy , its impact on transactions, other events and conditions is computed in accordance with the new policy retrospectively as if the new accounting policy had always been applied. The deficit or surplus arising from the retrospective computation is recognised in the statement of profit and loss in the year in which the accounting policy is changed

Limitations on retrospective computation

23 When retrospective accounting is required by paragraph 19(a) or (b), effect of change in accounting policy shall be computed retrospectively except to the extent that it is impracticable to determine the the cumulative effect of the change.

24-26 [Refer Appendix 1]

27 When it is impracticable for an entity to compute the effect of a new accounting policy retrospectively, because it cannot determine the cumulative effect of applying the policy to all prior periods, the entity, , applies the new policy prospectively from the start of the earliest period practicable. It therefore disregards the portion of the cumulative adjustment to assets, liabilities and equity arising before that date. Changing an accounting policy is permitted even if it is impracticable to account for the policy prospectively for any prior period. Paragraphs 50–53 provide guidance on when it is impracticable to account for a new accounting policy to one or more prior periods.

Disclosure

28 **An entity shall disclose:**

(a) the nature of the change in accounting policy;

(b) the reasons why applying the new accounting policy provides reliable and more relevant information where change is made in accordance with paragraph 19(b);

(c) impact of, and the adjustments resulting from change in accounting policy which has material effect, in the financial statements of the period in which such change is made, to reflect the effect of such change. If a change is made in the accounting policies which has no material effect on the financial statements for the current period but which is reasonably expected to have a material effect in later periods, the fact of such change shall be appropriately disclosed in the period in which the change is adopted unless it is impracticable to estrimate the effect of the changes in accounting policy. In the latter case, the fact shall be disclosed.

(d) if retrospective computation is impracticable for a particular prior period, or for periods before those presented, the circumstances that led to the existence of that condition and a description of how and from when the change in accounting policy has been computed.

Financial statements of subsequent periods need not repeat these disclosures.

29-31 [Refer Appendix 1]

Changes in accounting estimates

32 As a result of the uncertainties inherent in business activities, many items in financial statements cannot be measured with precision but can only be estimated. Estimation involves judgements based on the latest available, reliable information. For example, estimates may be required of:

(a) bad debts;

(b) inventory obsolescence;

(c) [Refer Appendix 1];

(d) the useful lives of, or expected pattern of consumption of the future economic benefits embodied in, depreciable assets; and

(e) warranty obligations.

33 The use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability.

34 An estimate may need revision if changes occur in the circumstances on which the estimate was based or as a result of new information or more experience. By its nature, the revision of an estimate does not relate to prior periods and is not the correction of an error.

35 A change in the measurement basis applied is a change in an accounting policy, and is not a change in an accounting estimate. When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.

36 The effect of change in an accounting estimate, other than a change to which paragraph 37 applies, shall be recognised prospectively by including it in profit or loss in:

(a) the period of the change, if the change affects that period only; or

(b) the period of the change and future periods, if the change affects both.

37 To the extent that a change in an accounting estimate gives rise to changes in assets and liabilities, or relates to an item of equity, it shall be recognised by adjusting the carrying amount of the related asset, liability or equity item in the period of the change.

38 Prospective recognition of the effect of a change in an accounting estimate means that the change is applied to transactions, other events and conditions from the date of the change in estimate. A change in an accounting estimate may affect only the current period's profit or loss, or the profit or loss of both the current period and future periods. For example, a change in the estimate of the amount of bad debts affects only the current period's profit or loss and therefore is recognised in the current period. However, a change in the estimated useful life of, or the expected pattern of consumption of the future economic benefits embodied in, a depreciable asset affects depreciation expense for the current period and for each future period during the asset's remaining useful life. In both cases, the effect of the change relating to the current period is recognised as income or expense in the current period. The effect, if any, on future periods is recognised as income or expense in those future periods

Disclosure

39 An entity shall disclose the nature and amount of a change in an accounting estimate that has an effect in the current period or is expected to have an effect

in future periods, except for the disclosure of the effect on future periods when it is impracticable to estimate that effect.

40 If the amount of the effect in future periods is not disclosed because estimating it is impracticable, an entity shall disclose that fact.

Errors

41 Errors can arise in respect of the recognition, measurement, presentation or disclosure of elements of financial statements. Financial statements do not comply with ASs if they contain either material errors or immaterial errors made intentionally to achieve a particular presentation of an entity's financial position, financial performance or cash flows. Potential current period errors discovered in that period are corrected before the financial statements are approved for issue. However, material errors are sometimes not discovered until a subsequent period, and these prior period errors are corrected in the financial statements for that subsequent period (see paragraphs 42).

41A However, the errors which have effect on the presentation or disclosure are disclosed in the notes.

42 Subject to paragraph 43, an entity shall correct material prior period errors retrospectively by recognizing the same in the first set of financial statements approved for issue after their discovery by.

Limitations on retrospective computation

43 A prior period error shall be corrected by retrospective computation except to the extent that it is impracticable to determine the cumulative effect of the error.

[Refer Appendix 1]

45 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 compute the effect of the correction of the error prospectively from the earliest date practicable.

46 [Refer Appendix 1]

47 When it is impracticable to determine the amount of an error (eg a mistake in applying an accounting policy) for all prior periods, the entity, in accordance with paragraph 45, computes the amount prospectively from the earliest date practicable. It therefore disregards the portion of the cumulative effect arising before that date. Paragraphs 50–53 provide guidance on when it is impracticable to correct an error for one or more prior periods.

48 Corrections of errors are distinguished from changes in accounting estimates. Accounting estimates by their nature are approximations that may need revision as additional information becomes known. For example, the gain or loss recognised on the outcome of a contingency is not the correction of an error.

Disclosure of prior period errors

49 In applying paragraph 42, an entity shall disclose the following:

(a) the nature of the prior period error;
(b) the amount of the correction made to each financial statement line item:

(i) for each financial statement line item affected; and

(ii) if Ind AS 33 applies to the entity, for basic and diluted earnings per share;

(c) the amount of the correction at the beginning of the earliest prior period presented; and

(d) if retrospective computation 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.

Financial statements of subsequent periods need not repeat these disclosures.

Impracticability in respect of retrospective computation

50 In some circumstances, it is impracticable to compute retrospectively the effect of a change in accounting policy or a correction of an error. For example, data may not have been collected in the prior period(s) in a way that allows retrospective computation of a new accounting policy and it may be impracticable to recreate the information.

51 It is frequently necessary to make estimates in applying an accounting policy to elements of financial statements recognised or disclosed in respect of transactions, other events or conditions. Estimation is inherently subjective, and estimates may be developed after the reporting period. Developing estimates is potentially more difficult when retrospectively computing the effect of an accounting policy or to correct a prior period error, because of the longer period of time that might have passed since the affected transaction, other event or condition occurred. However, the objective of estimates related to prior periods remains the same as for estimates made in the current period, namely, for the estimate to reflect the circumstances that existed when the transaction, other event or condition occurred.

52 Therefore, retrospectively computing a new accounting policy or correcting a prior period error requires distinguishing information that

(a) provides evidence of circumstances that existed on the date(s) as at which the transaction, other event or condition occurred, and

(b) would have been available when the financial statements for that prior period were approved for issue

from other information. For some types of estimates, it is impracticable to distinguish these types of information. When retrospective computation would require making a significant estimate for which it is impossible to distinguish these two types of information, it is impracticable to compute the effect of a new accounting policy or correct the prior period error retrospectively.

53 Hindsight should not be used when computing the effect of a new accounting policy to, or correcting amounts for, a prior period, either in making assumptions about what management's intentions would have been in a prior period or estimating the amounts recognised, measured or disclosed in a prior period. For example, when an entity corrects a prior period error in calculating its liability for employees' accumulated sick leave in accordance with AS 19, *Employee Benefits*, it disregards information about an unusually severe influenza season during the next period that became available after the financial statements for the prior period were approved for issue. The fact that significant estimates are frequently required when amending comparative information presented for prior periods does not prevent reliable computation of the amounts retrospectively..

Appendix A

References to matters contained in other Accounting Standards

This Appendix is an integral part of the AS.

Appendix B, Liabilities arising from Participating in a Specific Market— Waste Electrical and Electronic Equipment, contained in AS 37, *Provisions, Contingent Liabilities and Contingent Assets,* makes reference to (AS) 8.

Appendix 1

Note: *This Appendix is not a part of the Accounting Standard. The purpose of this Appendix is only to bring out the major differences, if any, between Accounting Standard (AS) 8 and the corresponding Indian Accounting Standard (Ind AS) 8, Accounting Policies, Changes in Accounting Estimates and Errors.*

Comparison with Ind AS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*

1. Paragraph 4 of Ind AS 8 dealing with the tax effects of corrections of prior period errors and retrospective adjustments has been deleted in AS 8 since it has been decided to cover such provisions in AS 12, *Income Taxes*.

2. Ind AS 8 defines Indian Accounting Standards in paragraph 5, however in paragraph 5, the definition of AS is given.

3. Ind AS 8 deals with retrospective application, retrospective restatement of changes in accounting policy and estimate and errors. However, it is felt that for non Ind AS compliant entities, it is too onerous to apply retrospective application and retrospective restatement and, accordingly, the following paragraphs dealing with them have been deleted in AS 8. AS 8, requires the impact of changes in accounting policy to be retrospectively computed-

   (i) definition of retrospective computation is included in paragraph 5.

   (ii) in order to maintain consistency with paragraph numbers of Ind AS, following paragraph numbers have been retained in AS 8:
      (a) Paragraph 24
      (b) Paragraph 26
      (c) Paragraph 46

   (iii) Following paragraphs have been modified:
      (a) Definition of 'impracticable in paragraph 5
      (b) Heading above paragraph 19 is changed as Accounting for changes in accounting policies.
      (c) Paragraph 19(b)
      (d) Paragraphs 22-23
      (e) Paragraphs 25
      (f) Paragraphs 27
      (g) Paragraph 41- 42
      (h) Paragraph 49

(i) Paragraphs 50-53

5. Paragraph 6 is modified as per the *Framework for the Preparation and Presentation of Financial Statements of the existing Accounting Standards* applicable to non Ind AS compliant entities.

6. In paragraph 9, the guidance is referred to as 'application guidance as it appears to be more appropriate.

7. In paragraph 12 of Ind AS 8, it is mentioned that in absence of an Ind AS, management may first consider the most recent pronouncements of International Accounting Standards Board In AS 8, paragraph 12 is modified as management should first consider the guidance given in Ind AS and in absence thereof the most recent pronouncement of the Institute of Chartered Accountants of India and in absence thereof most recent pronouncement of the International Accounting Standards Board.

8. In paragraph 14 of AS 8, it is mentioned that an entity shall change an accounting policy if change is required by statute. Paragraph 19 (a) is also modified accordingly. Ind AS 8 does not mention so .

9. Paragraph 21 has been deleted as the requirements specified therein have been added in paragraph 19(a) and 19(b).

10 AS 8 requires less disclosures since it is considered to be too onerous for non Ind AS compliant entities to disclose the provisions contained in Ind AS 8.Accordingly, paragraphs 28 and 49 are modified and paragraph 29-31 are deleted. Howwever, in order to maintain consistency with Ind AS 8, paragraph numbers have been retained in AS 8

11. Paragraph 32(c) of Ind AS 8 gives the example of the fair value of financial assets or financial liabilities for the estimates required . AS 8 does not contains the same.