

IFRS in Focus

IASB proposes to amend the definitions of accounting policies and accounting estimates in IAS 8

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The International Accounting Standards Board (the IASB) is proposing to amend the definitions of *accounting policies* and *accounting estimates* in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. The proposal is set out in a recent Exposure Draft (ED).

- The IFRS Interpretations Committee has expressed concerns that there is diversity in how entities determine whether a change in how they apply a Standard is a change in an accounting policy or a change in an estimate.
- Changes in accounting policies must be applied retrospectively whereas changes in estimates are required to be accounted for prospectively.
- The proposed changes to IAS 8 involve modifying both the definition of an accounting policy and the definition of an accounting estimate.
- The proposal includes a specific interpretation in relation to inventories.
- An example illustrating prospective accounting when a retrospective change is not practicable will be deleted, because it is considered confusing.
- The comment period ends on 15 January 2018.

Why the amendments are being proposed

When an entity changes an accounting policy it is required to account for the particular matter in the current period as if it had always applied that policy, which means changing the comparative figures. This is retrospective accounting. When an entity changes an accounting estimate, it affects the period of change and, where relevant, future periods. Comparative information is not adjusted.

The IFRS Interpretations Committee was asked to examine whether different entities were distinguishing between policies and estimates in the same way. The Interpretations Committee concluded that there was inconsistency in practice. It was unable to solve the problem itself, so asked the IASB to amend IAS 8.

This is the IASB's response to that request.

For more information please see the following websites:

www.iasplus.com

www.deloitte.com

Observation

The IASB has not explained which of its Standards are creating the most problems, although the proposed inventory example suggests that changes in inventory cost formulas is a concern.

The definitions

The ED proposes changing the definition of *accounting policies* and replacing the definition of *a change in accounting estimate* with a new definition of *accounting estimates*.

Accounting policies

The IASB proposes amending the definition as indicated (the new word is underlined and the deleted words struck through):

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

The change is designed to make the definition clearer and more concise, and use words that are already in other Standards. The terms conventions and rules are not used in any other Standard.

Accounting estimates

IAS 8 currently defines a change in accounting estimate:

- *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.

The proposal is to change this to a definition of an accounting estimate, and to have the definition focus on estimation uncertainty. The proposed definition is:

- *Accounting estimates* are judgements or assumptions used in applying an accounting policy when, because of estimation uncertainty, an item in financial statements cannot be measured with precision.

Observation

Accounting policies and estimates both require judgement, and explaining the judgements that an entity has made that have a material effect on the financial statements is important.

The definitions of policies and estimates are important only because changes in policies require retrospective accounting whereas changes in estimates are required to be accounted for prospectively. The IASB is not planning to assess whether this accounting distinction, which was introduced in 2004, is helpful to the users of the financial statements.

Inventory

The proposal also includes a new paragraph in relation to inventory. IAS 2 *Inventories* states that when inventory is ordinarily interchangeable, entities are required to use either the first-in, first-out (FIFO) or weighted average cost formula. The proposed amendment to IAS 8 would state that selecting that cost formula constitutes selecting an accounting policy and not making an accounting estimate.

Observation

The inclusion of the inventory example in IAS 8 is unusual. IFRS 13 *Fair Value Measurement* and IAS 16 *Property, Plant and Equipment* both have paragraphs that explain whether a change is an estimate or policy. This will be the only change explained in IAS 8.

Timing of the proposals

The ED does not specify an effective date for the proposed amendments. The Board will determine the effective date after considering the comments they receive on the ED.

The Board is proposing that the amendments would apply to changes in accounting policies or estimates that occur after the application date.

The comment period ends on 15 January 2018.

Further information

The Exposure Draft is available free of charge from the IFRS Foundation website, along with information on how to submit your comments on the proposal: <http://www.ifrs.org/projects/open-for-comment/>

If you have any questions about the proposals, please speak to your usual Deloitte contact or get in touch with a member of the Global team.

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