

Hong Kong Accounting Standard 8

Accounting Policies, Changes in Accounting Estimates and Errors

An entity shall apply amendments resulting from *Improvements to HKFRSs* issued in October 2008 for annual periods beginning on or after 1 January 2009.

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TABLE OF CONCORDANCE

Hong Kong Accounting Standard 8 *Accounting Policies, Changes in Accounting Estimates and Errors* (HKAS 8) is set out in paragraphs 1-56 and the Appendix. All the paragraphs have equal authority. HKAS 8 should be read in the context of its objective and the Basis for Conclusions, the *Preface to Hong Kong Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*.

Hong Kong Accounting Standard 8

Accounting Policies, Changes in Accounting Estimates and Errors

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 HKAS 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. The tax effects of corrections of prior period errors and of retrospective adjustments made to apply changes in accounting policies are accounted for and disclosed in accordance with HKAS 12 *Income Taxes*.

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.

Hong Kong Financial Reporting Standards (HKFRSs) are Standards and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (HKICPA). They comprise:

- (a) *Hong Kong Financial Reporting Standards;*
- (b) *Hong Kong Accounting Standards; and*
- (c) *Interpretations.*

Material Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions of users taken 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 authorised 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 application is applying a new accounting policy to transactions, other events and conditions as if that policy had always been applied.

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 reasonable effort to do so. For a particular prior period, it is impracticable to apply a change in an accounting policy retrospectively or to make a retrospective restatement to correct an error if:

- (a) the effects of the retrospective application or retrospective restatement are not determinable;
- (b) the retrospective application or retrospective restatement requires assumptions about what management's intent would have been in that period; or
- (c) the retrospective application or retrospective restatement 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 authorised 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* states in paragraph 25 that “users are assumed to have a reasonable knowledge of business and economic activities and accounting and a willingness to 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 a Standard or an Interpretation specifically applies to a transaction, other event or condition, the accounting policy or policies applied to that item shall be determined by applying the Standard or Interpretation and considering any relevant Implementation Guidance issued by the HKICPA for the Standard or Interpretation.***
8. HKFRSs set out accounting policies that the HKICPA has concluded 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 HKFRSs to achieve a particular presentation of an entity’s financial position, financial performance or cash flows.
9. Implementation Guidance for Standards issued by the HKICPA does not form part of those Standards, and therefore does not contain requirements for financial statements.
10. ***In the absence of a Standard or an Interpretation 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 and guidance in Standards and Interpretations 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 consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards, 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 a Standard or an Interpretation specifically requires or permits categorisation of items for which different policies may be appropriate. If a Standard or an Interpretation 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 a Standard or an Interpretation; 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.*

* In the context of Hong Kong, other accounting literature includes Accounting Guidelines and Accounting Bulletins.

17. ***The initial application of a policy to revalue assets in accordance with HKAS 16 Property, Plant and Equipment or HKAS 38 Intangible Assets is a change in an accounting policy to be dealt with as a revaluation in accordance with HKAS 16 or HKAS 38, rather than in accordance with this Standard.***
18. Paragraphs 19-31 do not apply to the change in accounting policy described in paragraph 17.

Applying 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 a Standard or an Interpretation in accordance with the specific transitional provisions, if any, in that Standard or Interpretation; and***
- (b) ***when an entity changes an accounting policy upon initial application of a Standard or an Interpretation that does not include specific transitional provisions applying to that change, or changes an accounting policy voluntarily, it shall apply the change retrospectively.***
20. For the purpose of this Standard, early application of a Standard or an Interpretation is not a voluntary change in accounting policy.
21. In the absence of a Standard or an Interpretation that specifically applies to a transaction, other event or condition, management may, in accordance with paragraph 12, apply an accounting policy from the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards. If, following an amendment of such a pronouncement, the entity chooses to change an accounting policy, that change is accounted for and disclosed as a voluntary change in accounting policy.

Retrospective application

22. ***Subject to paragraph 23, when a change in accounting policy is applied retrospectively in accordance with paragraph 19(a) or (b), the entity shall adjust the opening balance 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.***

Limitations on retrospective application

23. ***When retrospective application is required by paragraph 19(a) or (b), a change in accounting policy shall be applied retrospectively except to the extent that it is impracticable to determine either the period-specific effects or the cumulative effect of the change.***
24. ***When it is impracticable to determine the period-specific effects of changing an accounting policy on comparative information for one or more prior periods presented, the entity shall apply the new accounting policy to the carrying amounts of assets and liabilities as at the beginning of the earliest period for which retrospective application is practicable, which may be the current period, and shall make a corresponding adjustment to the opening balance of each affected component of equity for that period.***

25. ***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.***
26. When an entity applies a new accounting policy retrospectively, it applies the new accounting policy to comparative information for prior periods as far back as is practicable. Retrospective application to a prior period is not practicable unless it is practicable to determine the cumulative effect on the amounts in both the opening and closing balance sheets for that period. The amount of the resulting adjustment relating to periods before those presented in the financial statements is made to the opening balance of each affected component of equity of the earliest prior period presented. Usually the adjustment is made to retained earnings. However, the adjustment may be made to another component of equity (for example, to comply with a Standard or an Interpretation). Any other information about prior periods, such as historical summaries of financial data, is also adjusted as far back as is practicable.
27. When it is impracticable for an entity to apply a new accounting policy retrospectively, because it cannot determine the cumulative effect of applying the policy to all prior periods, the entity, in accordance with paragraph 25, 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 apply the policy prospectively for any prior period. Paragraphs 50-53 provide guidance on when it is impracticable to apply a new accounting policy to one or more prior periods.

Disclosure

28. ***When initial application of a Standard or an Interpretation has an effect on the current period or any prior period, would have such an effect except that it is impracticable to determine the amount of the adjustment, or might have an effect on future periods, an entity shall disclose:***
- (a) ***the title of the Standard or Interpretation;***
 - (b) ***when applicable, that the change in accounting policy is made in accordance with its transitional provisions;***
 - (c) ***the nature of the change in accounting policy;***
 - (d) ***when applicable, a description of the transitional provisions;***
 - (e) ***when applicable, the transitional provisions that might have an effect on future periods;***
 - (f) ***for the current period and each prior period presented, to the extent practicable, the amount of the adjustment:***
 - (i) ***for each financial statement line item affected; and***
 - (ii) ***if HKAS 33 Earnings per Share applies to the entity, for basic and diluted earnings per share;***

- (g) *the amount of the adjustment relating to periods before those presented, to the extent practicable; and*
- (h) *if retrospective application required by paragraph 19(a) or (b) 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 applied.*

Financial statements of subsequent periods need not repeat these disclosures.

29. *When a voluntary change in accounting policy has an effect on the current period or any prior period, would have an effect on that period except that it is impracticable to determine the amount of the adjustment, or might have an effect on future periods, 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;*
- (c) *for the current period and each prior period presented, to the extent practicable, the amount of the adjustment:*
 - (i) *for each financial statement line item affected; and*
 - (ii) *if HKAS 33 applies to the entity, for basic and diluted earnings per share;*
- (d) *the amount of the adjustment relating to periods before those presented, to the extent practicable; and*
- (e) *if retrospective application 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 applied.*

Financial statements of subsequent periods need not repeat these disclosures.

30. *When an entity has not applied a new Standard or Interpretation that has been issued but is not yet effective, the entity shall disclose:*

- (a) *this fact; and*
- (b) *known or reasonably estimable information relevant to assessing the possible impact that application of the new Standard or Interpretation will have on the entity's financial statements in the period of initial application.*

31. In complying with paragraph 30, an entity considers disclosing:

- (a) the title of the new Standard or Interpretation;
- (b) the nature of the impending change or changes in accounting policy;
- (c) the date by which application of the Standard or Interpretation is required;

- (d) the date as at which it plans to apply the Standard or Interpretation initially; and
- (e) either:
 - (i) a discussion of the impact that initial application of the Standard or Interpretation is expected to have on the entity's financial statements; or
 - (ii) if that impact is not known or reasonably estimable, a statement to that effect.

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) the fair value of financial assets or financial liabilities;
 - (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 a 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 HKFRSs 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 authorised for issue. However, material errors are sometimes not discovered until a subsequent period, and these prior period errors are corrected in the comparative information presented in the financial statements for that subsequent period (see paragraphs 42-47).
42. *Subject to paragraph 43, an entity shall correct material prior period errors retrospectively in the first set of financial statements authorised for issue after their discovery by:*
- (a) *restating the comparative amounts for the prior period(s) presented in which the error occurred; or*
 - (b) *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.*

Limitations on Retrospective Restatement

43. *A prior period error shall be corrected by retrospective restatement except to the extent that it is impracticable to determine either the period-specific effects or the cumulative effect of the error.*
44. *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).*
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 restate the comparative information to correct the error prospectively from the earliest date practicable.*
46. The correction of a prior period error is excluded from profit or loss for the period in which the error is discovered. Any information presented about prior periods, including any historical summaries of financial data, is restated as far back as is practicable.
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, restates the comparative information prospectively from the earliest date practicable. It therefore disregards the portion of the cumulative restatement of assets, liabilities and equity 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) *for each prior period presented, to the extent practicable, the amount of the correction:*
 - (i) *for each financial statement line item affected; and*
 - (ii) *if HKAS 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 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.*

Financial statements of subsequent periods need not repeat these disclosures.

Impracticability in Respect of Retrospective Application and Retrospective Restatement

50. In some circumstances, it is impracticable to adjust comparative information for one or more prior periods to achieve comparability with the current period. For example, data may not have been collected in the prior period(s) in a way that allows either retrospective application of a new accounting policy (including, for the purpose of paragraphs 51-53, its prospective application to prior periods) or retrospective restatement to correct a prior period error, 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 balance sheet date. Developing estimates is potentially more difficult when retrospectively applying an accounting policy or making a retrospective restatement 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 applying 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 authorised for issue

from other information. For some types of estimates (eg an estimate of fair value not based on an observable price or observable inputs), it is impracticable to distinguish these types of information. When retrospective application or retrospective restatement would require making a significant estimate for which it is impossible to distinguish these two types of information, it is impracticable to apply the new accounting policy or correct the prior period error retrospectively.

53. Hindsight should not be used when applying 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 measuring financial assets previously classified as held-to-maturity investments in accordance with HKAS 39 *Financial Instruments: Recognition and Measurement*, it does not change their basis of measurement for that period if management decided later not to hold them to maturity. In addition, when an entity corrects a prior period error in calculating its liability for employees' accumulated

sick leave in accordance with HKAS 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 authorised for issue. The fact that significant estimates are frequently required when amending comparative information presented for prior periods does not prevent reliable adjustment or correction of the comparative information.

Effective Date

54. *An entity shall apply this Standard for annual periods beginning on or after 1 January 2005. Earlier application is encouraged. If an entity applies this Standard for a period beginning before 1 January 2005, it shall disclose that fact.*

54A. If an entity decides to apply this Standard for an earlier period, it is not required to apply all the HKASs with the same effective date for that same period. However, it is required to apply the amendments set out in the appendix on amendments to other pronouncements for that earlier period.

Withdrawal of Other Pronouncements

55. This Standard supersedes SSAP 2 *Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies*, revised in 2001.

56. [Not used]

Appendix

Comparison with International Accounting Standards

This comparison appendix, which was prepared as at 9 March 2004 and deals only with significant differences in the standards extant, is produced for information only and does not form part of the standards in HKAS 8.

The International Accounting Standard comparable with HKAS 8 is IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

There are no major textual differences between HKAS 8 and IAS 8.

Appendix

Amendments to Other Pronouncements

The amendments in this appendix shall be applied for annual periods beginning on or after 1 January 2005. If an entity applies this Standard for an earlier period, these amendments shall be applied for that earlier period.

* * *

The amendments contained in this appendix when this Standard was issued have been incorporated into the relevant Standards.

As explained in the introduction to this Standard, the accounting standard and paragraph references that appear below may differ from those found in the existing SSAPs as they have taken into account the changes to be made to the name, number, paragraph numbering as well as appendix referencing of the existing SSAPs in order to conform to those of the equivalent IASs.

A1. HKAS 7 Cash Flow Statements is amended as follows:

Paragraphs 29 and 30 on extraordinary items are deleted.

Appendix A, which illustrates a cash flow statement for an entity other than a financial institution, is amended to remove an extraordinary item. The revised Appendix is set out below:

Appendix A

Cash Flow Statement for an Entity other than a Financial Institution

This appendix accompanies, but is not part of, the Standard.

1. The examples show only current period amounts. Corresponding amounts for the preceding period are required to be presented in accordance with HKAS 1 Presentation of Financial Statements.

2. Information from the income statement and balance sheet is provided to show how the statements of cash flows under the direct method and indirect method have been derived. Neither the income statement nor the balance sheet is presented in conformity with the disclosure and presentation requirements of other Standards.

3. The following additional information is also relevant for the preparation of the statements of cash flows:

- all of the shares of a subsidiary were acquired for 590. The fair values of assets acquired and liabilities assumed were as follows:

<u>Inventories</u>	<u>100</u>
<u>Accounts receivable</u>	<u>100</u>
<u>Cash</u>	<u>40</u>
<u>Property, plant and equipment</u>	<u>650</u>
<u>Trade payables</u>	<u>100</u>

~~Long-term debt~~

~~200~~

- ~~250 was raised from the issue of share capital and a further 250 was raised from long-term borrowings.~~
- ~~interest expense was 400, of which 170 was paid during the period. Also, 100 relating to interest expense of the prior period was paid during the period.~~
- ~~dividends paid were 1,200.~~
- ~~the liability for tax at the beginning and end of the period was 1,000 and 400 respectively. During the period, a further 200 tax was provided for. Withholding tax on dividends received amounted to 100.~~
- ~~during the period, the group acquired property, plant and equipment with an aggregate cost of 1,250 of which 900 was acquired by means of finance leases. Cash payments of 350 were made to purchase property, plant and equipment.~~
- ~~plant with original cost of 80 and accumulated depreciation of 60 was sold for 20.~~
- ~~accounts receivable as at the end of 20-2 include 100 of interest receivable.~~

~~Consolidated Income Statement for the period ended 20-2~~

Sales	30,650
Cost of sales	(26,000)
	<hr/>
Gross profit	4,650
Depreciation	(450)
Administrative and selling expenses	(910)
Interest expense	(400)
Investment income	500
Foreign exchange loss	(40)
	<hr/>
Profit before taxation	3,350
Taxes on income	(300)
	<hr/>
Profit	3,050
	<hr/>

Consolidated Balance Sheet as at the end of 20-2-

	20-2	20-1
Assets		
Cash and cash equivalents	230	160
Accounts receivable	1,900	1,200
Inventory	1,000	1,950
Portfolio investments	2,500	2,500
Property, plant and equipment at cost	3,730	1,910
Accumulated depreciation	(1,450)	(1,060)
Property, plant and equipment net	<u>2,280</u>	<u>850</u>
Total assets	<u>7,910</u>	<u>6,660</u>
Liabilities		
Trade payables	250	1,890
Interest payable	230	100
Income taxes payable	400	1,000
Long-term debt	2,300	1,040
Total liabilities	<u>3,180</u>	<u>4,030</u>
Shareholders' Equity		
Share capital	1,500	1,250
Retained earnings	3,230	1,380
Total shareholders' equity	<u>4,730</u>	<u>2,630</u>
Total liabilities and shareholders' equity	<u>7,910</u>	<u>6,660</u>

Direct Method Cash Flow Statement (paragraph 18a)

		20-2
Cash flows from operating activities		
Cash receipts from customers	30,150	
Cash paid to suppliers and employees	(27,600)	
	<hr/>	
Cash generated from operations	2,550	
Interest paid	(270)	
Income taxes paid	(900)	
	<hr/>	
<i>Net cash from operating activities</i>		1,380
Cash flows from investing activities		
Acquisition of subsidiary X, net of cash acquired (Note A)	(550)	
Purchase of property, plant and equipment (Note B)	(350)	
Proceeds from sale of equipment	20	
Interest received	200	
Dividends received	200	
	<hr/>	
<i>Net cash used in investing activities</i>		(480)
Cash flows from financing activities		
Proceeds from issue of share capital	250	
Proceeds from long-term borrowings	250	
Payment of finance lease liabilities	(90)	
Dividends paid*	(1,200)	
	<hr/>	
<i>Net cash used in financing activities</i>		(790)
Net increase in cash and cash equivalents		110
Cash and cash equivalents at beginning of period (Note C)		120
		<hr/>
Cash and cash equivalents at end of period (Note C)		230
		<hr/>

*This could also be shown as an operating cash flow.

Indirect Method Cash Flow Statement (paragraph 18b)

		20-2
Cash flows from operating activities		
Profit before taxation	3,350	
Adjustments for:		
Depreciation	450	
Foreign exchange loss	40	
Investment income	(500)	
Interest expense	400	
	3,740	
Increase in trade and other receivables	(500)	
Decrease in inventories	1,050	
Decrease in trade payables	(1,740)	
Cash generated from operations	2,550	
Interest paid	(270)	
Income taxes paid	(900)	
	1,380	1,380
Cash flows from investing activities		
Acquisition of subsidiary X net of cash acquired (Note A)	(550)	
Purchase of property, plant and equipment (Note B)	(350)	
Proceeds from sale of equipment	20	
Interest received	200	
Dividends received	200	
	(480)	(480)
Cash flows from financing activities		
Proceeds from issue of share capital	250	
Proceeds from long-term borrowings	250	
Payment of finance lease liabilities	(90)	
Dividends paid*	(1,200)	
	(790)	(790)
Net increase in cash and cash equivalents		110
Cash and cash equivalents at beginning of period (Note C)		120
Cash and cash equivalents at end of period (Note C)		230

*This could also be shown as an operating cash flow.

**Notes to the Cash Flow Statement
(direct method and indirect method)****A. Acquisition of Subsidiary**

During the period the group acquired subsidiary X. The fair value of assets acquired and liabilities assumed were as follows:

Cash	40
Inventories	100
Accounts receivable	100
Property, plant and equipment	650
Trade payables	(100)
Long-term debt	(200)
Total purchase price	590
Less: Cash of X	(40)
Cash flow on acquisition net of cash acquired	(550)

B. Property, Plant and Equipment

During the period, the Group acquired property, plant and equipment with an aggregate cost of 1,250 of which 900 was acquired by means of finance leases. Cash payments of 350 were made to purchase property, plant and equipment.

C. Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand and balances with banks, and investments in money market instruments. Cash and cash equivalents included in the cash flow statement comprise the following balance sheet amounts:

	20-2	20-1
Cash on hand and balances with banks	40	25
Short-term investments	190	135
Cash and cash equivalents as previously reported	230	160
Effect of exchange rate changes	-	(40)
Cash and cash equivalents as restated	230	120

Cash and cash equivalents at the end of the period include deposits with banks of 100 held by a subsidiary that are not freely remissible to the holding company because of currency exchange restrictions.

The Group has undrawn borrowing facilities of 2,000, of which 700 may be used only for future expansion.

D. Segment Information

	Segment A	Segment B	Total
Cash flows from:			
Operating activities	1,520	(140)	1,380
Investing activities	(640)	160	(480)
Financing activities	(570)	(220)	(790)
	310	(200)	110

Alternative Presentation (indirect method)

As an alternative, in an indirect method cash flow statement, operating profit before working capital changes is sometimes presented as follows:

Revenues excluding investment income	30,650	
Operating expense excluding depreciation	(26,910)	
Operating profit before working capital changes		3,740

A2. HKAS 12 *Income Taxes* is amended as described below.

Paragraph 62(b) is amended to read as follows:

- (b) an adjustment to the opening balance of retained earnings resulting from either a change in accounting policy that is applied retrospectively or the correction of an error (see HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*).

~~Paragraph 80(h) is amended to read as follows:—~~

- ~~(h) — the amount of tax expense (income) relating to those changes in accounting policies and errors that are included in profit or loss in accordance with HKAS 8, because they cannot be accounted for retrospectively.—~~

~~Paragraphs 81(b) and 83 are deleted.—~~

~~A3.— HKAS 14 *Segment Reporting* is amended as described below.—~~

~~The definition of accounting policies in paragraph 8 is amended to read as follows:~~

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

~~Paragraph 60 is amended to read as follows:—~~

- ~~60.— HKAS 1 requires that when items of income and expense are material, their nature and amount shall be disclosed separately. HKAS 1 offers a number of examples, including write-downs of inventories and property, plant, and equipment, provisions for restructurings, disposals of property, plant, and equipment and long-term investments, discontinuing operations, litigation settlements, and reversals of provisions. Paragraph 59 is not intended to change the classification of any such items or to change the measurement of such items. The disclosure encouraged by that paragraph, however, does change the level at which the significance of such items is evaluated for disclosure purposes from the entity level to the segment level.—~~

~~Paragraphs 77 and 78 are amended to read as follows:—~~

- ~~77.— Changes in accounting policies applied by the entity are dealt with in HKAS 8. HKAS 8 requires that changes in accounting policy shall be made only if required by a Standard or Interpretation, or if the change will result in reliable and more relevant information about transactions, other events or conditions in the financial statements of the entity.—~~

- ~~78.— Changes in accounting policies applied at the entity level that affect segment information are dealt with in accordance with HKAS 8. Unless a new Standard or Interpretation specifies otherwise, HKAS 8 requires that:—~~

- ~~(a) — a change in accounting policy shall be applied retrospectively and prior period information restated unless it is impracticable to determine either the cumulative effect or the period-specific effects of the change;—~~
- ~~(b) — if retrospective application is not practicable for all periods presented, the new accounting policy shall be applied retrospectively from the earliest practicable date; and—~~
- ~~(c) — if it is impracticable to determine the cumulative effect of applying the new accounting policy at the start of the current period, the policy shall be applied prospectively from the earliest date practicable.—~~

~~The following changes are made to remove references to extraordinary items:~~

- ~~(a) in paragraph 16, in the definition of segment revenue, subparagraph (a) is deleted.~~
- ~~(b) in paragraph 16, in the definition of segment expense, subparagraph (a) is deleted.~~
- ~~(c) in Appendix B, Schedule A, the line items 'Profit from ordinary activities' and 'Extraordinary loss: uninsured earthquake damage to factory' are deleted, and 'Net profit' is amended to 'Profit'. The profit for 20x1 is amended from 14 to 17.~~
- ~~(d) in Appendix B, the final paragraph is deleted.~~

~~A4. HKAS 19 *Employee Benefits* is amended as described below.~~

~~Paragraph 131 is amended to read as follows:~~

~~131. Although this Standard does not require specific disclosures about other long-term employee benefits, other Standards may require disclosures, for example, when the expense resulting from such benefits is material and so would require disclosure in accordance with HKAS 1 *Presentation of Financial Statements*. When required by HKAS 24 *Related Party Disclosures*, an entity discloses information about other long-term employee benefits for key management personnel.~~

~~Paragraph 142 is amended to read as follows:~~

~~142. As required by HKAS 1, an entity discloses the nature and amount of an expense if it is material. Termination benefits may result in an expense needing disclosure in order to comply with this requirement.~~

~~Paragraph 160 is amended to read as follows:~~

~~160. HKAS 8 applies when an entity changes its accounting policies to reflect the changes specified in paragraphs 159 and 159A. In applying those changes retrospectively, as required by HKAS 8, the entity treats those changes as if they had been applied at the same time as the rest of this Standard.~~

~~A5. In HKAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*, paragraphs 20-22 are amended to read as follows:~~

~~**20. A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs shall be recognised as income of the period in which it becomes receivable.**~~

~~21. In some circumstances, a government grant may be awarded for the purpose of giving immediate financial support to an entity rather than as an incentive to undertake specific expenditures. Such grants may be confined to an individual entity and may not be available to a whole class of beneficiaries. These circumstances may warrant recognising a grant as income in the period in which the entity qualifies to receive it, with disclosure to ensure that its~~

~~effect is clearly understood.~~

~~22. A government grant may become receivable by an entity as compensation for expenses or losses incurred in a previous period. Such a grant is recognised as income of the period in which it becomes receivable, with disclosure to ensure that its effect is clearly understood.~~

~~A6. In HKAS 22 *Business Combinations*, paragraph 100 is deleted.~~

~~A7. In HKAS 23 *Borrowing Costs*, paragraph 30 is amended to read as follows:~~

~~30. When the adoption of this Standard constitutes a change in accounting policy, an entity is encouraged to adjust its financial statements in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Alternatively, entities shall capitalise only those borrowing costs incurred after the effective date of the Standard that meet the criteria for capitalisation.~~

~~A8. HKAS 34 *Interim Financial Reporting* is amended as described below.~~

~~Paragraph 17 is amended to read as follows:~~

~~17. Examples of the kinds of disclosures that are required by paragraph 16 are set out below. Individual Standards and Interpretations provide guidance regarding disclosures for many of these items:~~

~~(a) the write-down of inventories to net realisable value and the reversal of such a write-down;~~

~~(b) recognition of a loss from the impairment of property, plant and equipment, intangible assets, or other assets, and the reversal of such an impairment loss;~~

~~(c) the reversal of any provisions for the costs of restructuring;~~

~~(d) acquisitions and disposals of items of property, plant and equipment;~~

~~(e) commitments for the purchase of property, plant and equipment;~~

~~(f) litigation settlements;~~

~~(g) corrections of prior period errors;~~

~~(h) [deleted];~~

~~(i) any loan default or breach of a loan agreement that has not been remedied on or before the balance sheet date; and~~

~~(j) related party transactions.~~

~~Paragraphs 24, 25 and 27 are amended to read as follows:~~

~~24. HKAS 1 *Presentation of Financial Statements* and HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* define an item as material if its omission or misstatement could~~

~~influence the economic decisions of users of the financial statements. HKAS 1 requires separate disclosure of material items, including (for example) discontinuing operations, and HKAS 8 requires disclosure of changes in accounting estimates, errors and changes in accounting policies. The two Standards do not contain quantified guidance as to materiality.~~

~~25. While judgement is always required in assessing materiality, this Standard bases the recognition and disclosure decision on data for the interim period by itself for reasons of understandability of the interim figures. Thus, for example, unusual items, changes in accounting policies or estimates, and errors are recognised and disclosed on the basis of materiality in relation to interim period data to avoid misleading inferences that might result from non-disclosure. The overriding goal is to ensure that an interim financial report includes all information that is relevant to understanding an entity's financial position and performance during the interim period.~~

~~27. HKAS 8 requires disclosure of the nature and (if practicable) the amount of a change in estimate that either has a material effect in the current period or is expected to have a material effect in subsequent periods. Paragraph 16(d) of this Standard requires similar disclosure in an interim financial report. Examples include changes in estimate in the final interim period relating to inventory write-downs, restructurings, or impairment losses that were reported in an earlier interim period of the financial year. The disclosure required by the preceding paragraph is consistent with the HKAS 8 requirement and is intended to be narrow in scope—relating only to the change in estimate. An entity is not required to include additional interim period financial information in its annual financial statements.~~

~~Paragraphs 43 and 44 are amended to read as follows:~~

~~43. *A change in accounting policy, other than one for which the transition is specified by a new Standard or Interpretation, shall be reflected by:*~~

~~(a) *restating the financial statements of prior interim periods of the current financial year and the comparable interim periods of any prior financial years that will be restated in the annual financial statements in accordance with HKAS 8; or*~~

~~(b) *when it is impracticable to determine the cumulative effect at the beginning of the financial year of applying a new accounting policy to all prior periods, adjusting the financial statements of prior interim periods of the current financial year, and comparable interim periods of prior financial years to apply the new accounting policy prospectively from the earliest date practicable.*~~

~~44. One objective of the preceding principle is to ensure that a single accounting policy is applied to a particular class of transactions throughout an entire financial year. Under HKAS 8, a change in accounting policy is reflected by retrospective application, with~~

~~restatement of prior period financial data as far back as is practicable. However, if the cumulative amount of the adjustment relating to prior financial years is impracticable to determine, then under HKAS 8 the new policy is applied prospectively from the earliest date practicable. The effect of the principle in paragraph 43 is to require that within the current financial year any change in accounting policy is applied either retrospectively or, if that is not practicable, prospectively, from no later than the beginning of the financial year.~~

~~A9. In HKAS 35 *Discontinuing Operations*, paragraphs 41, 42 and 50 are deleted.~~

~~A10. In HKAS 36 *Impairment of Assets*, paragraphs 120 and 121 are deleted.~~

~~A11. In HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, paragraph 94 is deleted.~~

~~A12. In HKAS 38 *Intangible Assets*, paragraph 120 is deleted.~~

~~A13. [Not used]~~

~~A14. [Not used]~~

~~A15. In HKAS Int 21 *Income Taxes – Recovery of Revalued Non-Depreciable Assets*, the effective date paragraph is amended to read as follows:~~

~~**Effective Date:** This consensus becomes effective on 1 January 2003. Changes in accounting policies shall be accounted for in accordance with HKAS 8.~~

~~A16. In HKAS Int 22 *Business Combinations – Subsequent Adjustment of Fair Values and Goodwill Initially Reported*, paragraph 11 of the Basis for Conclusions should be read as follows:~~

~~[The original text has been marked up to reflect the revision of HKAS 8 in 2003: new text is underlined and deleted text is struck through.]~~

~~11. HKAS 22.93 requires disclosure if the fair values of identifiable assets and liabilities can only be determined on a provisional basis. This implies that in such circumstances, the entity enterprise is aware that reliable estimates cannot yet be made and therefore the adjustment is not accounted for as a change in estimate in accordance with addressed in paragraphs .23 through .30 of HKAS 8.~~

~~A17. In HKAS Int 25 *Income Taxes – Changes in the Tax Status of an Entity or its Shareholders*, the effective date paragraph is amended to read as follows:~~

~~**Effective Date:** This consensus becomes effective on 15 July 2000. Changes in accounting policies shall be accounted for in accordance with HKAS 8.~~

~~A18. In HKAS Int 27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*, the effective date paragraph is amended to read as follows:~~

~~**Effective Date:** This Interpretation becomes effective on 29 June 2001. Changes in accounting policies shall be accounted for in accordance with HKAS 8.~~

~~A19. In HKAS Int 31 Revenue – Barter Transactions Involving Advertising Services, the effective date paragraph is amended to read as follows:–~~

~~**Effective Date:** This Interpretation becomes effective on 25 June 2002. Changes in accounting policies shall be accounted for in accordance with HKAS 8.–~~

~~A20. In HKFRS 1 First time Adoption of International Financial Reporting Standards, the definition of Hong Kong Financial Reporting Standards in Appendix A is amended to read as follows:–~~

~~**Hong Kong Financial Reporting Standards (HKFRSs)**~~

~~Standards and Interpretations issued by the Hong Kong Society of Accountants (HKSA). They comprise:–~~

~~(a) Hong Kong Financial Reporting Standards;–~~

~~(b) Hong Kong Accounting Standards (HKASs); and–~~

~~(c) Interpretations–~~

~~A21. The rubric of HKFRS 1 First time Adoption of Hong Kong Financial Reporting Standards is amended to read as follows:–~~

~~Hong Kong Financial Reporting Standard 1 First time Adoption of Hong Kong Financial Reporting Standards (HKFRS 1) is set out in paragraphs 1–47 and Appendices A–C. All the paragraphs have equal authority. Paragraphs in **bold type** state the main principles. Terms defined in Appendix A are in *italics* the first time they appear in the Standard. Definitions of other terms are given in the Glossary for Hong Kong Financial Reporting Standards. HKFRS 1 should be read in the context of its objective and the Basis for Conclusions, the *Preface to Hong Kong Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.–~~

~~A22. The rubrics of all other Hong Kong Accounting Standards are replaced by a new rubric in the following form:–~~

~~Hong Kong Accounting Standard X *Title in Words* (HKAS X) is set out in paragraphs 1–000 [and Appendices A–C]*. All the paragraphs have equal authority. HKAS X should be read in the context of [its objective and the Basis for Conclusions,]† the *Preface to Hong Kong Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.–~~

~~* used only for those appendices that are part of the Standard.–~~

~~† used only where the Standard contains an objective or is accompanied by a Basis for Conclusions.–~~

~~A23.— In Hong Kong Financial Reporting Standards, including Hong Kong Accounting Standards and Interpretations, applicable at December 2003, references to the current version of SSAP 2 *Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies* are amended to HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.~~

Appendix

Amendments resulting from other HKFRSs

The following sets out amendments required for this Standard resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Standard and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

HKAS 1 *Presentation of Financial Statements* (issued in December 2007) - effective for annual periods beginning on or after 1 January 2009

Paragraph 5 is amended as follows:

- in the definition of *Material*, ‘~~of users taken~~’ is amended to ‘that users make’.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, HKAS 8.

HKAS 8 is based on IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*. In approving HKAS 8, the Council of the Hong Kong Institute of Certified Public Accountants considered and agreed with the IASB's basis for conclusions on IAS 8 (as revised 2003). Accordingly, there are no significant differences between HKAS 8 and IAS 8. The IASB's basis for conclusions is reproduced below for reference. The paragraph numbers of IAS 8 referred to below generally correspond with those in HKAS 8.

Introduction

- BC1. This Basis for Conclusions summarises the International Accounting Standards Board's considerations in reaching its conclusions on revising IAS 8 *Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies* in 2003. Individual Board members gave greater weight to some factors than to others.
- BC2. In July 2001 the Board announced that, as part of its initial agenda of technical projects, it would undertake a project to improve a number of Standards, including IAS 8. The project was undertaken in the light of queries and criticisms raised in relation to the Standards by securities regulators, professional accountants and other interested parties. The objectives of the Improvements project were to reduce or eliminate alternatives, redundancies and conflicts within Standards, to deal with some convergence issues and to make other improvements. In May 2002 the Board published its proposals in an Exposure Draft of *Improvements to International Accounting Standards*, with a comment deadline of 16 September 2002. The Board received over 160 comment letters on the Exposure Draft.
- BC3. The Standard includes extensive changes to the previous version of IAS 8. The Board's intention was not to reconsider all of the previous Standard's requirements for selecting and applying accounting policies, and accounting for changes in accounting policies, changes in accounting estimates and corrections of errors. Accordingly, this Basis for Conclusions does not discuss requirements in IAS 8 that the Board did not reconsider.

Removing Allowed Alternative Treatments

- BC4. The previous version of IAS 8 included allowed alternative treatments of voluntary changes in accounting policies (paragraphs 54-57) and corrections of fundamental errors (paragraphs 38-40). Under those allowed alternatives:
- (a) the adjustment resulting from retrospective application of a change in an accounting policy was included in profit or loss for the current period; and
 - (b) the amount of the correction of a fundamental error was included in profit or loss for the current period.
- BC5. In both circumstances, comparative information was presented as it was presented in the financial statements of prior periods.

- BC6. The Board identified the removal of optional treatments for changes in accounting policies and corrections of errors as an important improvement to the previous version of IAS 8. The Standard removes the allowed alternative treatments and requires changes in accounting policies and corrections of prior period errors to be accounted for retrospectively.
- BC7. The Board concluded that retrospective application made by amending the comparative information presented for prior periods is preferable to the previously allowed alternative treatments because, under the now required method of retrospective application:
- (a) profit or loss for the period of the change does not include the effects of changes in accounting policies or errors relating to prior periods.
 - (b) information presented about prior periods is prepared on the same basis as information about the current period, and is therefore comparable. This information possesses a qualitative characteristic identified in the *Framework for the Preparation and Presentation of Financial Statements*, and provides the most useful information for trend analysis of income and expenses.
 - (c) prior period errors are not repeated in comparative information presented for prior periods.
- BC8. Some respondents to the Exposure Draft argued that the previously allowed alternative treatments are preferable because:
- (a) correcting prior period errors by restating prior period information involves an unjustifiable use of hindsight;
 - (b) recognising the effects of changes in accounting policies and corrections of errors in current period profit or loss makes them more prominent to users of financial statements; and
 - (c) each amount credited or debited to retained earnings as a result of an entity's activities has been recognised in profit or loss in some period.
- BC9. The Board concluded that restating prior period information to correct a prior period error does not involve an unjustifiable use of hindsight because prior period errors are defined in terms of a failure to use, or misuse of, reliable information that was available when the prior period financial statements were authorised for issue and could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.
- BC10. The Board also concluded that the disclosures about changes in accounting policies and corrections of prior period errors in paragraphs 28, 29 and 49 of the Standard should ensure that their effects are sufficiently prominent to users of financial statements.
- BC11. The Board further concluded that it is less important for each amount credited or debited to retained earnings as a result of an entity's activities to be recognised in profit or loss in some period than for the profit or loss for each period presented to represent faithfully the effects of transactions and other events occurring in that period.

Eliminating the Distinction Between Fundamental Errors and Other Material Prior Period Errors

BC12. The Standard eliminates the distinction between fundamental errors and other material prior period errors. As a result, all material prior period errors are accounted for in the same way as a fundamental error was accounted for under the retrospective treatment in the previous version of IAS 8. The Board concluded that the definition of ‘fundamental errors’ in the previous version was difficult to interpret consistently because the main feature of the definition—that the error causes the financial statements of one or more prior periods no longer to be considered to have been reliable—was also a feature of all material prior period errors.

Applying a Standard or an Interpretation that Specifically Applies to an Item

BC13. The Exposure Draft proposed that when a Standard or an Interpretation applies to an item in the financial statements, the accounting policy (or policies) applied to that item is (are) determined by considering the following in descending order:

- (a) the Standard (including any Appendices that form part of the Standard);
- (b) the Interpretation;
- (c) Appendices to the Standard that do not form a part of the Standard; and
- (d) Implementation Guidance issued in respect of the Standard.

BC14. The Board decided not to set out a hierarchy of requirements for these circumstances. The Standard requires only applicable Standards and Interpretations to be applied. In addition, it does not mention Appendices.

BC15. The Board decided not to rank Standards above Interpretations because the definition of International Financial Reporting Standards (IFRSs) includes Interpretations, which are equal in status to Standards. The rubric to each Standard clarifies what material constitutes the requirements of an IFRS and what is Implementation Guidance. The term ‘Appendix’ is retained only for material that is part of an IFRS.

Pronouncements of Other Standard-setting Bodies

BC16. The Exposure Draft proposed that in the absence of a Standard or an Interpretation specifically applying to an item, management should develop and apply an accounting policy by considering, among other guidance, pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards. Respondents to the Exposure Draft commented that this could *require* entities to consider the pronouncements of various other standard-setting bodies when IASB guidance does not exist. Some commentators argued that, for example, it could require consideration of all components of US GAAP on some topics. After considering these comments, the Board decided that the Standard should indicate that considering such pronouncements is voluntary (see paragraph 12 of the Standard).

BC17. As proposed in the Exposure Draft, the Standard states that pronouncements of other standard-setting bodies are used only if they do not conflict with:

- (a) the requirements and guidance in Standards and Interpretations dealing with similar and related issues; and

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

- BC18. The Standard refers to the most recent pronouncements of other standard-setting bodies because if pronouncements are withdrawn or superseded, the relevant standard-setting body no longer thinks they include the best accounting policies to apply.
- BC19. Comments received indicated that it was unclear from the Exposure Draft whether a change in accounting policy following a change in a pronouncement of another standard-setting body should be accounted for under the transitional provisions in that pronouncement. As noted above, the Standard does not mandate using pronouncements of other standard-setting bodies in any circumstances. Accordingly, the Board decided to clarify that such a change in accounting policy is accounted for and disclosed as a voluntary change in accounting policy (see paragraph 21 of the Standard). Thus, an entity is precluded from applying transitional provisions specified by the other standard-setting body if they are inconsistent with the treatment of voluntary changes in accounting policies specified by the Standard.

Materiality

- BC20. The Standard states that accounting policies specified by IFRSs need not be applied when the effect of applying them is immaterial. It also states that financial statements do not comply with IFRSs if they contain material errors, and that material prior period errors are to be corrected in the first set of financial statements authorised for issue after their discovery. The Standard includes a definition of material omissions or misstatements, which is based on the description of materiality in the previous version of IAS 1 *Presentation of Financial Statements* and in the *Framework*.
- BC21. The former *Preface to Statements of International Accounting Standards* stated that International Accounting Standards were not intended to apply to immaterial items. There is no equivalent statement in the *Preface to International Financial Reporting Standards*. The Board received comments that the absence of such a statement from the *Preface* could be interpreted as requiring an entity to apply accounting policies (including measurement requirements) specified by IFRSs to immaterial items. However, the Board decided that the application of the concept of materiality should be in Standards rather than in the *Preface*.
- BC22. The application of the concept of materiality is set out in two Standards. The revised IAS 1 *Presentation of Financial Statements* continues to specify its application to disclosures. IAS 8 specifies the application of materiality in applying accounting policies and correcting errors (including errors in measuring items).

Criterion for Exemption from Requirements

- BC23. The previous version of IAS 8 included an impracticability criterion for exemption from retrospective application of voluntary changes in accounting policies and retrospective restatement for fundamental errors, and from making related disclosures, when the allowed alternative treatment of those items was not applied. The Exposure Draft proposed instead an exemption from retrospective application and retrospective restatement when it gives rise to undue cost or effort.

BC24. In the light of comments received on the Exposure Draft, the Board decided that an exemption based on management's assessment of undue cost or effort is too subjective to be applied consistently by different entities. Moreover, the Board decided that balancing costs and benefits is a task for the Board when it sets accounting requirements rather than for entities when they apply those requirements. Therefore, the Board decided to retain the impracticability criterion for exemption in the previous version of IAS 8. This affects the exemptions in paragraphs 23-25, 39 and 43-45 of the Standard. Impracticability is the only basis on which specific exemptions are provided in Standards and Interpretations from applying particular requirements when the effect of applying them is material.

Definition of 'impracticable'

BC25. The Board decided to clarify the meaning of 'impracticable' in relation to retrospective application of a change in accounting policy and retrospective restatement to correct a prior period error.

BC26. Some commentators suggested that retrospective application of a change in accounting policy and retrospective restatement to correct a prior period error are impracticable for a particular prior period whenever significant estimates are required as of a date in that period. However, the Board decided to specify a narrower definition of impracticable because the fact that significant estimates are frequently required when amending comparative information presented for prior periods does not prevent reliable adjustment or correction of the comparative information. Thus, the Board decided that an inability to distinguish objectively information that both provides evidence of circumstances that existed on the date(s) as at which those amounts are to be recognised, measured or disclosed and would have been available when the financial statements for that prior period were authorised for issue from other information is the factor that prevents reliable adjustment or correction of comparative information for prior periods (see part (c) of the definition of 'impracticable' and paragraphs 51 and 52 of the Standard).

BC27. The Standard specifies that hindsight should not be used when applying 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 in a prior period. This is because management's intentions in a prior period cannot be objectively established in a later period, and using information that would have been unavailable when the financial statements for the prior period(s) affected were authorised for issue is inconsistent with the definitions of retrospective application and retrospective restatement.

Applying the Impracticability Exemption

BC28. The Standard specifies that when it is impracticable to determine the cumulative effect of applying a new accounting policy to all prior periods, or the cumulative effect of an error on all prior periods, the entity changes the comparative information as if the new accounting policy had been applied, or the error had been corrected, prospectively from the earliest date practicable (see paragraphs 25 and 45 of the Standard). This is similar to paragraph 52 of the previous version of IAS 8, but it is no longer restricted to changes in accounting policies. The Board decided to include such provisions in the Standard because it agrees with comments received that it is preferable to require prospective application from the start of the earliest period practicable than to permit a change in accounting policy only when the entity can determine the cumulative effect of the change for all prior periods at the beginning of the current period.

BC29. Consistently with the Exposure Draft's proposals, the Standard provides an impracticability exemption from retrospective application of changes in accounting policies, including retrospective application of changes made in accordance with the transitional provisions in a Standard or an Interpretation. The previous version of IAS 8 specified the impracticability exemption for retrospective application of only *voluntary* changes in accounting policies. Thus, the applicability of the exemption to changes made in accordance with the transitional provisions in a Standard or an Interpretation depended on the text of that Standard or Interpretation. The Board extended the applicability of the exemption because it decided that the need for the exemption applies equally to all changes in accounting policies applied retrospectively.

Disclosures about Impending Application of Newly Issued Standards and Interpretations

BC30. The Standard requires an entity to provide disclosures when it has not yet applied a new Standard or Interpretation that has been issued but is not yet effective. The entity is required to disclose that it has not yet applied the Standard or Interpretation, and known or reasonably estimable information relevant to assessing the possible impact that initial application of the new Standard or Interpretation will have on the entity's financial statements in the period of initial application (paragraph 30). The Standard also includes guidance on specific disclosures the entity should consider when applying this requirement (paragraph 31).

BC31. Paragraphs 30 and 31 of the Standard differ from the proposals in the Exposure Draft in the following respects:

- (a) they specify that an entity needs to disclose information only if it is known or reasonably estimable. This clarification responds to comments on the Exposure Draft that the proposed disclosures would sometimes be impracticable.
- (b) whereas the Exposure Draft proposed to mandate the disclosures now in paragraph 31, the Standard sets out these disclosures as items an entity should consider disclosing to meet the general requirement in paragraph 30. This amendment focuses the requirement on the objective of the disclosure, and, in response to comments on the Exposure Draft that the proposed disclosures were more onerous than the disclosures in US GAAP, clarifies that the Board's intention was to converge with US requirements, rather than to be more onerous.

Recognising the Effects of Changes in Accounting Estimates

BC32. The Exposure Draft proposed to retain without exception the requirement in the previous version of IAS 8 that the effect of a change in accounting estimate is *recognised 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.

BC33. Some respondents to the Exposure Draft disagreed with requiring the effects of all changes in accounting estimates to be recognised in profit or loss. They argued that this is inappropriate to the extent that a change in an accounting estimate gives rise to changes in assets and liabilities, because the entity's equity does not change as a result. These commentators also argued that it is inappropriate to preclude recognising the effects of changes in accounting estimates directly in equity when that is required or permitted by a Standard or an Interpretation. The Board concurs, and decided to provide an exception to the requirement described in paragraph BC32 for these circumstances.

Appendix

Amendments resulting from other Basis for Conclusions

The following sets out amendments required for this Basis for Conclusions resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Basis for Conclusions and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

HKAS 1 *Presentation of Financial Statements* (issued in December 2007) – effective for annual periods beginning on or after 1 January 2009

In paragraph BC29, ‘a Standard or an Interpretation’ is amended to ‘an IFRS’.

In paragraphs BC29 and BC30, ‘Standard or Interpretation’ is amended to ‘IFRS’.

In paragraphs BC14, BC17, BC24 and the heading above paragraph BC30, ‘Standards and Interpretations’ is amended to ‘IFRSs’.

Paragraphs BC20 and BC22 are amended as follows:

BC20 The Standard ... includes a definition of material omissions or misstatements, which is based on the description of materiality in ~~the previous version of~~ IAS 1 *Presentation of Financial Statements* (as issued in 1997) and in the *Framework*.

BC22 The application of the concept of materiality is set out in two Standards. ~~The revised~~ IAS 1 *Presentation of Financial Statements* (as revised in 2007) continues to specify its application to disclosures. IAS 8 ...

In paragraph BC24, the last sentence is footnoted as follows:

In 2006 the IASB issued IFRS 8 *Operating Segments*. As explained in paragraphs BC46 and BC47 of the Basis for Conclusions on IFRS 8, that IFRS includes an exemption from some requirements if the necessary information is not available and the cost to develop it would be excessive.

Guidance on Implementing HKAS 8

This guidance accompanies, but is not part of, HKAS 8.

Example 1 – Retrospective Restatement of Errors

- 1.1 During 20-2, Beta Co discovered that some products that had been sold during 20-1 were incorrectly included in inventory at 31 December 20-1 at CU6,500.*
- 1.2 Beta's accounting records for 20-2 show sales of CU104,000, cost of goods sold of CU86,500 (including CU6,500 for the error in opening inventory), and income taxes of CU5,250.
- 1.3 In 20-1, Beta reported:

	CU
Sales	73,500
Cost of goods sold	(53,500)
Profit before income taxes	<u>20,000</u>
Income taxes	<u>(6,000)</u>
Profit	<u><u>14,000</u></u>

- 1.4 20-1 opening retained earnings was CU20,000 and closing retained earnings was CU34,000.
- 1.5 Beta's income tax rate was 30 per cent for 20-2 and 20-1. It had no other income or expenses.
- 1.6 Beta had CU5,000 of share capital throughout, and no other components of equity except for retained earnings. Its shares are not publicly traded and it does not disclose earnings per share.

* In these examples, monetary amounts are denominated in 'currency units' (CU).

Beta Co
Extract from the Income Statement

	20-2	(restated) 20-1
	CU	CU
Sales	104,000	73,500
Cost of goods sold	(80,000)	(60,000)
Profit before income taxes	24,000	13,500
Income taxes	(7,200)	(4,050)
Profit	16,800	9,450

Beta Co
Statement of Changes in Equity

	Share capital	Retained earnings	Total
	CU	CU	CU
Balance at 31 December 20-0	5,000	20,000	25,000
Profit for the year ended 31 December 20-1 as restated		9,450	9,450
Balance at 31 December 20-1	5,000	29,450	34,450
Profit for the year ended 31 December 20-2		16,800	16,800
Balance at 31 December 20-2	5,000	46,250	51,250

Extracts from the Notes

1. Some products that had been sold in 20-1 were incorrectly included in inventory at 31 December 20-1 at CU6,500. The financial statements of 20-1 have been restated to correct this error. The effect of the restatement on those financial statements is summarised below. There is no effect in 20-2.

	Effect on 20-1
	CU
(Increase) in cost of goods sold	(6,500)
Decrease in income tax expense	1,950
(Decrease) in profit	(4,550)
(Decrease) in inventory	(6,500)
Decrease in income tax payable	1,950
(Decrease) in equity	(4,550)

Example 2 – Change in Accounting Policy with Retrospective Application

- 2.1 During 20-2, Gamma Co changed its accounting policy for the treatment of borrowing costs that are directly attributable to the acquisition of a hydro-electric power station under construction for use by Gamma. In previous periods, Gamma had capitalised such costs. Gamma has now decided to treat these costs as an expense,

rather than capitalise them. Management judges that the new policy is preferable because it results in a more transparent treatment of finance costs and is consistent with local industry practice, making Gamma's financial statements more comparable.

- 2.2 Gamma capitalised borrowing costs incurred of CU2,600 during 20-1 and CU5,200 in periods before 20-1. All borrowing costs incurred in previous years in respect of the acquisition of the power station were capitalised.
- 2.3 Gamma's accounting records for 20-2 show profit before interest and income taxes of CU30,000; interest expense of CU3,000 (which relates only to 20-2); and income taxes of CU8,100.
- 2.4 Gamma has not yet recognised any depreciation on the power station because it is not yet in use.
- 2.5 In 20-1, Gamma reported:

	CU
Profit before interest and income taxes	18,000
Interest expense	-
Profit before income taxes	<u>18,000</u>
Income taxes	<u>(5,400)</u>
Profit	<u><u>12,600</u></u>

- 2.6 20-1 opening retained earnings was CU20,000 and closing retained earnings was CU32,600.
- 2.7 Gamma's tax rate was 30 per cent for 20-2, 20-1 and prior periods.
- 2.8 Gamma had CU10,000 of share capital throughout, and no other components of equity except for retained earnings. Its shares are not publicly traded and it does not disclose earnings per share.

Gamma Co
Extract from the Income Statement

	20-2	(restated) 20-1
	<u>CU</u>	<u>CU</u>
Profit before interest and income taxes	30,000	18,000
Interest expense	<u>(3,000)</u>	<u>(2,600)</u>
Profit before income taxes	27,000	15,400
Income taxes	<u>(8,100)</u>	<u>(4,620)</u>
Profit	<u><u>18,900</u></u>	<u><u>10,780</u></u>

Gamma Co
Statement of Changes in Equity

	Share capital	(restated) Retained earnings	Total
	CU	CU	CU
Balance at 31 December 20-0 as previously reported	10,000	20,000	30,000
Change in accounting policy for the capitalisation of interest (net of income taxes of CU1,560) (Note 1)		(3,640)	(3,640)
Balance at 31 December 20-0 as restated	10,000	16,360	26,360
Profit for the year ended 31 December 20-1 (restated)		10,780	10,780
Balance at 31 December 20-1	10,000	27,140	37,140
Profit for the year ended 31 December 20-2		18,900	18,900
Balance at 31 December 20-2	10,000	46,040	56,040

Extracts from the Notes

- 1 During 20-2, Gamma changed its accounting policy for the treatment of borrowing costs related to a hydro-electric power station under construction for use by Gamma. Previously, Gamma capitalised such costs. They are now written off as expenses as incurred. Management judges that this policy provides reliable and more relevant information because it results in a more transparent treatment of finance costs and is consistent with local industry practice, making Gamma's financial statements more comparable. This change in accounting policy has been accounted for retrospectively, and the comparative statements for 20-1 have been restated. The effect of the change on 20-1 is tabulated below. Opening retained earnings for 20-1 have been reduced by CU3,640, which is the amount of the adjustment relating to periods prior to 20-1.

<i>Effect on 20-1</i>	CU
(Increase) in interest expense	(2,600)
Decrease in income tax expense	<u>780</u>
(Decrease) in profit	(1,820)
 <i>Effect on periods prior to 20-1</i>	
(Decrease) in profit (CU5,200 interest expense less tax of CU1,560)	(3,640)
(Decrease) in assets in the course of construction and in retained earnings at 31 December 20-1	<u>(5,460)</u>

Example 3 - Prospective Application of a Change in Accounting Policy When Retrospective Application is not Practicable

- 3.1 During 20-2, Delta Co changed its accounting policy for depreciating property, plant and equipment, so as to apply much more fully a components approach, whilst at the same time adopting the revaluation model.
- 3.2 In years before 20-2, Delta's asset records were not sufficiently detailed to apply a components approach fully. At the end of 20-1, management commissioned an engineering survey, which provided information on the components held and their fair values, useful lives, estimated residual values and depreciable amounts at the beginning of 20-2. However, the survey did not provide a sufficient basis for reliably estimating the cost of those components that had not previously been accounted for separately, and the existing records before the survey did not permit this information to be reconstructed.
- 3.3 Delta's management considered how to account for each of the two aspects of the accounting change. They determined that it was not practicable to account for the change to a fuller components approach retrospectively, or to account for that change prospectively from any earlier date than the start of 20-2. Also, the change from a cost model to a revaluation model is required to be accounted for prospectively. Therefore, management concluded that it should apply Delta's new policy prospectively from the start of 20-2.

3.4 Additional information:

Delta's tax rate is 30 per cent.

	CU
Property, plant and equipment at the end of 20-1:	
Cost	25,000
Depreciation	<u>(14,000)</u>
Net book value	<u>11,000</u>
Prospective depreciation expense for 20-2 (old basis)	1,500
Some results of the engineering survey:	
Valuation	17,000
Estimated residual value	3,000
Average remaining asset life (years)	7
Depreciation expense on existing property, plant and equipment for 20-2 (new basis)	2,000

Extract from the Notes

- 1 From the start of 20-2, Delta changed its accounting policy for depreciating property, plant and equipment, so as to apply much more fully a components approach, whilst at the same time adopting the revaluation model. Management takes the view that this policy provides reliable and more relevant information because it deals more accurately with the components of property, plant and equipment and is based on up-to-date values. The policy has been applied prospectively from the start of 20-2 because it was not practicable to estimate the effects of applying the policy either retrospectively, or prospectively from any earlier date. Accordingly, the adoption of the new policy has no effect on prior years. The effect on the current year is to increase the carrying amount of property, plant and equipment at the start of the year by CU6,000; increase the opening deferred tax provision by CU1,800; create a revaluation reserve at the start of the year of CU4,200; increase depreciation expense by CU500; and reduce tax expense by CU150.

Appendix

Amendments resulting from other Implementation Guidance

The following sets out amendments required for this Guidance resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Guidance and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

HKAS 23 Revised *Borrowing Costs* (issued in June 2007) – effective for annual periods beginning on or after 1 January 2009

In the Guidance on Implementing HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, Example 2 is deleted.

Table of Concordance

This table shows how the contents of the superseded SSAP 2 and the current HKAS 8 correspond. Paragraphs are treated as corresponding if they broadly address the same matter even though the guidance may differ.

Superseded SSAP 2 paragraph	Current HKAS 8 paragraph
Objective	1
1	3
2	55
3	2
4	None
5	5
6	(HKAS 1.78)
7	(HKAS 1.79)
8	(HKAS 1.80)
9	(HKAS 1.85)
10	None
11	None
12	None
13	None
14	None
15	(HKAS 1.86)
16	None
17	(HKAS 1.87)
18	None
19	None
20	None
21	None
22	32, 33
23	34

Superseded SSAP 2 paragraph	Current HKAS 8 paragraph
24	35
25	36
26	38
27	None
28	None
29	39, 40
30	41
31	41
32	48
33	42
34	46
35	None
36	49
37	15
38	14
39	14
40	16-18
41	None
42	19
43	None
44	30, 31
45	22, 23

Superseded SSAP 2 paragraph	Current HKAS 8 paragraph
46	26
47	None
48	24, 25
49	28, 29
50	54
Appendix	Guidance on Implementing HKAS 8

Superseded SSAP 2 paragraph	Current HKAS 8 paragraph
None	4
None	6
None	13
None	20, 21
None	27
None	37
None	43-45
None	47
None	50-53
None	56