LKAS 8
Accounting Policies, Changes in Accounting Estimates and Errors

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Overview

- Objective and scope
- Accounting policies
- Changes in accounting estimates
- Errors
- Disclosures

Objective and scope

- Selecting and applying accounting **policies**

- Accounting for changes in:
  - Accounting **policies**
  - Accounting **estimates**

- Corrections of **prior period errors**

Accounting policies

Specific **principles**, **bases**, **conventions**, **rules** and **practices** applied by an entity in **preparing and presenting** financial statements.

Selection and application of accounting policies

- Accounting policy determined by
  - **Applying a specific SLFRS**

- In absence of a specific SLFRS
  - **Use judgement** to develop an accounting policy that results in relevant and reliable information
    - First, refer to **SLFRSs dealing with similar and related issues** and second, to **framework**
    - Consider **pronouncement of other setters or industry practices** if consistent with above

Consistency of accounting policies

- Select and apply accounting policy **consistently** for similar transactions, other events and conditions

- May adopt **different policies**
  - When an **SLFRS requires or permits categorisation** of items for which different policies may be appropriate
  - But accounting policy selected and applied should be **consistent to each category**

Eg: Changes in Accounting Policy

An entity changes from presenting a **classified statement of financial position** (current and non-current assets and current and non-current liabilities shown as separate classifications) **to** a **liquidity presentation** (items presented in order of liquidity without current/non-current classification) because, in the entity's particular circumstances, a liquidity presentation provides information that is reliable and more relevant.

The entity **restated its statement of financial position for the comparable prior period** because it regarded the change to a liquidity presentation as a change in accounting policy.

Is the entity's treatment correct?

Yes, Accounting policies include **not only the principles for recognising and measuring** assets, liabilities, income and expenses but also the **principles and practices for presenting** them in financial statements. Current/noncurrent versus liquidity presentation is an example. Retrospective restatement is required.

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Changes in accounting policies

- **Consistency** is important

- Change an accounting policy only if the change:
  - is **required by an SLFRS**; or
  - results in the financial statements providing **reliable** and **more relevant** information

Changes in accounting policies cont…

- A change an accounting policy occurs, if there has been a change in:
  - **Recognition**

    e.g. an expense is now recognized rather than an asset
  - **Presentation**

    e.g. depreciation is now included in cost of sales rather than administrative expenses or
  - **Measurement basis**

    e.g. stating assets at fair value rather than historical cost

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Applying changes in accounting policies

Changes in accounting policies

Application of a standard or interpretation

Voluntary change in accounting policy

Specific transitional provisions

No

Apply change retrospectively

Yes

Apply specific transitional provisions

Application of a standard or interpretation Eg:

There were no transactions with the key management personnel of the Company and its parent for the year ended 31 March 2017. Further there were no key management compensation paid during the year other than those disclosed in Note 8.

36.3. **Other related party disclosures**

Legal fees amounting to Rs. 1,083,257/- was paid by the Company last year 2015/16, to an entity in which a key management personnel was a partner.

37. **IMPACT OF AMENDMENTS TO LKAS 16 AND LKAS 41**

The prior year figures have been restated due to the following adjustment and the total effect to the Financial Statements is summarized below.

Amendment to LKAS 16 and LKAS 41, on bearer plants are effective for annual reporting periods beginning on or after 1 January 2016. Accordingly harvestable biological assets growing on the bearer plants are measured at their fair value less cost to harvest and accounted retrospectively.

STATEMENT OF PROFIT OR LOSS	2016 Previously Reported Amount Rs.'000	2016 Adjusted Amount Rs.'000.	2016 Restated Amount Rs.'000.
Change in Fair Value of Biological Assets	5,728	(111)	5,617
STATEMENT OF FINANCIAL POSITION			
Produce on Bearer Biological Assets			
As at the beginning of the year	-	3,423	3,423
As at the end of the year	-	3,312	3,312
Accumulated Profit / (Loss)			
As at the beginning of the year	2,934,636	3,423	2,938,059
As at the end of the year	1,957,492	3,312	1,960,803

3.24 Change in Accounting Policies and Disclosures

Amendment to LKAS 41 & 16 - Harvestable Produce Growing on Bearer Biological Assets

Amendments to LKAS 16 - Property, Plant & Equipment and LKAS 41 - Agriculture, require entity to recognize agricultural produce growing on Bearer Plants at fair value less cost to sell separately from its bearer plants prior to harvest. After initial recognition, changes in the fair value of such agricultural produce growing on Bearer Plants, recognised in profit or loss at the end of each reporting period.

Accordingly, the Company has applied these amendments retrospectively in the Financial Statements. For the details refer Note 37.

(a) **Bearer Biological Assets**

The bearer biological assets are measured at cost less accumulated depreciation and accumulated impairment losses, if any, in terms of LKAS 16 – Property Plant & Equipment.

The cost of land preparation, rehabilitation, new planting, replanting, crop diversification, inter planting and fertilizing etc., incurred between the time of planting and harvesting (when the planted area attains maturity), are classified as immature plantations. These immature plantations are shown at direct costs plus attributable overheads, including interest attributable to long-term loans used for financing immature plantations. The expenditure incurred on bearer biological assets (Tea, Rubber and Timber fields) which comes into bearing during the year, is transferred to mature plantations.

(b) **Consumable Biological Assets**

Consumable biological assets include managed timber that are to be harvested as agricultural produce or sold as biological assets.

The managed timber trees are measured on initial

Selling price	Estimated based on prevailing Sri Lankan market prices. Factor all the conditions to be fulfilled in bringing the trees into saleable condition.
Planting cost	Estimated costs for the further development of immature areas are deducted.
Discount rate	Future cash flows are discounted at 14%

Nursery cost includes the cost of direct materials, directly attributable overheads, less provision for overgrown plants.

The gain or loss arising on initial recognition of consumable biological assets at fair value less cost to sell and from a change in fair value less cost to sell of consumable biological assets are included in profit or loss for the period in which it arises.

(c) **Produce Growing on Bearer Biological Assets**

In accordance with LKAS 41, Company recognise agricultural produce growing on bearer plants at fair value less cost to sell. Change in the fair value of such agricultural produce recognized in profit or loss at the end of each reporting period.

Application of a standard or interpretation Eg:

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STATEMENT OF CHANGES IN EQUITY

Year Ended 31 March

Company	Stated Capital Rs.'000	General Reserve Rs.'000	Retained Earnings Rs.'000	Available-for-Sale Reserve Rs.'000	Timber Reserve Rs.'000	Total Rs.'000
As at 31 March 2015	250,000	225,000	2,934,636	-	2,758	3,412,393
Impact of the Amendment of LKAS 41 (Note LKAS 16.3)	-	-	3,423	-	-	3,423
As at 01 April 2015- As Previously Reported	250,000	225,000	2,938,059	-	2,758	3,415,817
Super Gain Tax Paid	-	-	(20,684)	-	-	(20,684)
As at 01 April 2015 - Restated	250,000	225,000	2,917,375	-	2,758	3,395,133
Profit for the year - Restated	-	-	101,330	-	-	101,331
Other Comprehensive Income - Restated	-	-	72,826	(7,980)	-	64,846
Timber Reserve	-	-	(5,728)	-	5,728	-
Dividends paid	-	-	(1,125,000)	-	-	(1,125,000)
Balance as at 31 March 2016 - Restated	250,000	225,000	1,960,803	(7,980)	8,485	2,436,309
Profit for the year	-	-	217,263	-	-	217,263
Other Comprehensive Income	-	-	36,544	56,580	-	93,124
Timber Reserve	-	-	(5,035)	-	5,035	-
Dividends paid	-	-	(125,000)	-	-	(125,000)
Balance as at 31 March 2017	250,000	225,000	2,084,575	48,600	13,521	2,621,694

STATEMENT OF FINANCIAL POSITION

As at 31 March — Company

ASSETS	Notes	2017 Rs.'000	2016 Restated Rs.'000	2015 Restated Rs.'000
Non Current Assets				
Lease hold Property, Plant and Equipment	14	208,326	224,154	239,983
Free hold Property, Plant and Equipment	15	284,038	323,978	365,251
Bearer Biological Assets	16.1	2,022,742	1,910,589	1,753,216
Consumable Biological Assets	16.2	107,220	94,919	78,746
Financial Assets	17	1,200,880	1,144,300	1,000,000
Long Term Investments	18.3	491,850	491,850	611,850
Total Non Current Assets		4,315,057	4,189,791	4,049,045

Applying changes in accounting policies cont…

Prop-Rent Plc is an entity that buys apartments in Colombo and then leases them out to individuals. The entity's Finance Manager read that, according to LKAS 40, the entity has the option to value its investment property at either **fair value**, or by using the **cost model**.

In the past the entity has valued its investment property by using the cost model.

The Finance Manager considered changing the measurement model to the fair value model.

- LKAS 40 gives the entity the option to select the fair value model of measurement
- Therefore the entity may value its investment property in terms of the fair value model
- If change results in more relevant or reliable presentation of financial statements, it is a voluntary change in accounting policy
- The change is permitted by LKAS 40, and as a result should be accounted for and disclosed as specified in LKAS 8 as a voluntary change

Voluntary change in accounting policy Eg:

Extract of Abans PLC Annual Report 2017/18 (Please refer the annexure)

Accounting for a change in accounting policy

- The change should be applied **retrospectively**, with an **adjustment to the opening balance of each affected component in equity** for the earliest prior period presented

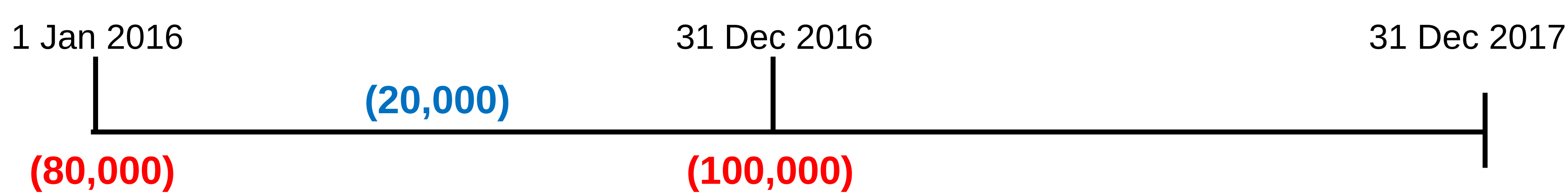
- **Comparative amounts** disclosed for each prior period should be **restated**

- **If it is impracticable to quantify** the change, the entity **applies the new policy from the beginning of the earliest period** for which retrospective application is practicable

Changes in accounting policies – disclosure

In 2017, the entity was required to comply with an amendment to the SLFRSs. The cumulative effect of the change in accounting policy on the retained earnings of the entity at the beginning of 2015 is a Rs.80,000 decrease. The effect on profit before tax for 2016 is a Rs.25,000 decrease, with a resultant decrease in income tax expense of Rs.5,000.

	2017	*2016*
		Restated
	Rs.	*Rs.*
Profit before tax (2016: previously stated Rs. 185,000)	200,000	160,000
Income tax expense (2016: previously stated Rs. 45,000)	(50,000)	(40,000)
Profit for the year (2016: previously stated Rs. 140,000)	150,000	120,000
Retained earning at the beginning of the year	320,000	200,000
- as previously stated	420,000	280,000
- effect of the change in accounting policy	**(100,000)**	**(80,000)**
Retained earning at the end of the year	470,000	320,000



Changes in accounting policies – disclosure cont…

- When **not applying a new SLFRS** that has been **issued but is not yet effective**, <u>disclose</u>
  - This **fact**
  - Known or reasonably estimable information relevant to assessing the **possible impact** that application of the new SLFRS will have on the financial statements in the period of initial application

Changes in accounting estimates

- Include the effect of a change in an accounting estimate **in profit or loss** in:
  - The **period of the change**, if the change affects the period only, or
  - The period of the change and future periods, if the change affects both

- **Adjust the carrying amount of an asset, liability or equity** item in the period of change

Changes in accounting estimates cont…

- If **difficult to distinguish** between change in accounting estimate and in accounting policy
  - Treat the change as **a change in accounting estimate**

- Disclose the **nature and amount of a change** in an estimate:
  - That has an effect in the **current period**, or
  - Is expected to have an **effect in the future periods**

- If impracticable to quantify the amount of the effect in future periods, disclose that fact

Change in Accounting Estimates Eg:

- Change the useful life of a building and the resulting impact on depreciation
- Receipt of the overdue amount of a debtor, on which a provision for bad and doubtful debt has been made.

Changes in accounting estimates cont…

Power Ltd is a household electronics manufacturer and retailer. In the past the entity had created a provision of 5% on total sales for the year. Due to the increase in sales returns over the past 3 years, the entity changed the percentage applied to sales warranties to 8.5%.

The Finance Manger of the company was keen to determine whether the change in the warranty percentage will be a change in accounting estimate or change in accounting policy

- Certain financial statement items cannot be measured with certainty - but are estimates.
- The change in the percentage of sales warranty provision is a change in accounting estimates, and as a result should be accounted for and disclosed in terms of the rules in LKAS 8 that governs a change in accounting estimates

Prior period errors

- Errors in respect of **recognition, measurement, presentation or disclosure**

- Prior period errors
  - **Omission and misstatements** for one or more prior periods arising from a failure to use, or misuse of, reliable information

- Such errors include
  - The effects of **mathematical mistakes** in applying accounting policies
  - **Oversights** or **misinterpretations** of facts
  - **Fraud**

Correction of material prior period errors

- Correct material prior period errors **retrospectively** in the first set of financial statements authorised for issue after their discovery

- **Restate comparative amounts** for prior periods presented

- If the error occurred before the earliest prior period presented, **restate opening balances of assets, liabilities and equity for the earliest prior period presented**

Correction of material prior period errors cont…

Upon investigation, Star Ltd discovered that the entity had not depreciated its lab equipment since the purchase of the equipment 4 years ago in 2014

How should this be accounted in terms of LKAS 8?

Note: *The entity presents current year (2018) and the prior year (2017) on the financial statements.*

- This is an error
- The error should be accounted for retrospectively
- Due to the fact that the error occurred before the earliest period presented, the opening balance of retained earnings for the earliest period presented should be restated
- Comparative figures for the prior period should also be adjusted to correct the error

Correction of prior period errors Eg:

In 2018, after the entity's 2017 financial statements were approved for issue, the entity discovered that, as a result of a computational error, depreciation expense for 2017:

Scenario 1 - was understated by Rs. 10

Underestimate of depreciation is a prior period error—the misstatement in the entity's 2017 financial statements arose from the misuse (mathematical error) of reliable information that was available when financial statements for those periods were authorised for issue. However, it is probably not material. If so, it can be ignored.

Correction of prior period errors Eg:

In 2018, after the entity's 2017 financial statements were approved for issue, the entity discovered that, as a result of a computational error, depreciation expense for 2017:

Scenario 2 - was understated by Rs. 70,000.

Underestimate of depreciation is a prior period error—the misstatement in the entity's 2017 financial statements arose from the misuse (mathematical error) of reliable information that was available when financial statements for those periods were authorised for issue.

Downward restatement of retained earnings at 1 January 2018 (the beginning of the current reporting period) is required.

Test your knowledge……

Question 01

Prospective application of a change in accounting policy means:

(a) applying the new accounting policy to transactions, other events and conditions occurring after the date as at which the financial statements are authorised for issue.

(b) applying the new accounting policy to transactions, other events and conditions occurring between the date as at which the policy is changed and the date when the financial statements are authorised for issue.

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

(d) applying a new accounting policy to transactions, other events and conditions as if that policy had always been applied.

Test your knowledge……

Question 02

Retrospective application of a change in accounting policy means:

(a) applying a new accounting policy to transactions, other events and conditions, identified before the date when the financial statements are authorised for issue, as if that policy had always been applied.

(b) applying the new accounting policy to transactions, other events and conditions occurring between the date as at which the policy is changed and the date when the financial statements are authorised for issue.

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

(d) applying a new accounting policy to transactions, other events and conditions as if that policy had always been applied.

Test your knowledge……

Question 03

Which of the following statements is true?

(a) The effect of a change in accounting estimate is recognised retrospectively.

(b) To the extent practicable, an entity must correct a prior period error prospectively in the first financial statements authorised for issue after its discovery.

(c) When an entity discovers an error in its financial statements of a prior period, it must immediately withdraw those financial statements and reissue them with the error corrected.

(d) To the extent practicable, an entity must correct a prior period error retrospectively in the first financial statements authorised for issue after its discovery.

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Thank you.