

## STAFF PAPER

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## Introduction

1. This paper presents our analysis of, and recommendations on, the project direction for the amendments to IAS 8 *Accounting Policies, Changes in Accounting Estimates and Error* proposed in the Exposure Draft *Accounting Policies and Accounting Estimates* (Proposed amendments to IAS 8) (Exposure Draft).
2. This paper reflects feedback received from Board members in April 2019 on project direction ([Agenda Paper 26D](#) for the Board's April 2019 meeting (April Board paper)). Appendix B to this paper summarises that feedback and our analysis of that feedback.

## Structure of the paper

3. This paper includes:
  - (a) summary of staff recommendations; and
  - (b) staff analysis and recommendations.
4. There are three appendices to this paper:
  - (a) Appendix A—re-exposure;
  - (b) Appendix B—summary and analysis of feedback from Board members; and

- (c) Appendix C—consideration of other alternatives for project direction.

## Summary of staff recommendations

5. We recommend that the Board:
- (a) finalise the amendments with the modifications set out in agenda paper 26A for this meeting; and
  - (b) not re-expose the amendments.

## Staff analysis and recommendations

### *Proceeding with the amendments<sup>1</sup>*

6. Many respondents raised concerns about particular aspects of the proposed amendments and asked for additional clarity in particular areas. We think that our analysis and recommendations in Agenda Papers 26B and 26C for this meeting would address many of those concerns.
7. Although many respondents agreed with the direction of the project, some asked whether the expected benefits of proceeding with the amendments (expected benefits) would outweigh the cost of standard-setting (cost). In assessing whether the Board should proceed with the amendments, we think it is necessary to consider whether the expected benefits would outweigh the cost.

### *Expected benefits*

8. We think proceeding with the amendments would help clarify the distinction between accounting policies and accounting estimates by specifying how accounting policies relate to accounting estimates. It would also reduce diversity in accounting for changes in estimation techniques and valuation techniques. Several respondents said these explanations and clarifications were helpful. We think these clarifications would

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<sup>1</sup> Throughout this paper, we have used the term ‘proceed with the amendments’ to refer to proceeding with the amendments as proposed in the Exposure Draft subject to the modifications set out in Agenda Paper 26A for this meeting.

lead to greater consistency in the application of the definitions, thereby improving the overall quality of financial reporting.

9. IAS 8 does not define accounting estimates. It defines *accounting policies* and a *change in accounting estimate*. Several respondents said providing a definition of accounting estimates is helpful and would clarify the distinction between accounting policies and estimates. The recommended definition of accounting estimates (as proposed in Agenda Paper 26B for this meeting) builds on concepts from the *Conceptual Framework for Financial Reporting* issued by the Board in March 2018 (Conceptual Framework) and, in our view, represents an improvement from the existing requirements in IAS 8.

10. However, we acknowledge that the amendments would not solve all identified application questions. In particular, we think the amendments may not address some situations in which an IFRS Standard does not clearly set out a measurement objective. In such situations, it might not always be clear whether a change results from a change in the underlying measurement objective (in which case it would be a change in accounting policy) or a change in a measurement technique designed to achieve the same underlying measurement objective (in which case it would be a change in an accounting estimate).

*Cost*

11. Proceeding with the amendments will introduce a new definition of accounting estimates. Stakeholders would incur cost in understanding and applying that definition, even if the new definition does not ultimately result in changes. Local jurisdictional authorities would also incur costs in incorporating the amendments into local laws and regulations (e.g. when endorsing the amendments).

12. The Exposure Draft proposed that an entity would apply the proposed amendments prospectively to all changes in accounting policies and all changes in accounting estimates that occur on or after the effective date of the proposed amendments. Although the Board has not yet redeliberated the transition requirements, we think that if the Board were to confirm the transition requirements proposed in the Exposure Draft, this would further limit the cost of applying the amendments.

13. The use of estimates is pervasive and affects several areas of financial reporting under IFRS Standards. For example, the term estimate(s) is used more than 1,000 times in IFRS Standards. Consequently, we think that any attempt to define accounting estimates inherently carries a risk of unintended consequences. We think it might not be possible to identify all possible situations in which there could be unintended consequences until the revised definitions are applied in practice. Nonetheless, we think the risk of any unintended consequences has been mitigated to some extent through consultations with the Accounting Standards Advisory Forum (ASAF) and the IFRS Interpretations Committee (Committee) members—these consultations have not highlighted any particular unintended consequence that might arise from proceeding with the amendments.
14. Additional cost (in particular time and resources) would be incurred by stakeholders and the Board if the Board decides to re-expose the amendments before it finalises them. Appendix A to this paper presents our analysis and views on this matter. Based on our analysis in Appendix A, we think the Board does not need to re-expose the amendments.

*Feedback from ASAF and Committee members*

15. Many Committee members and some ASAF members suggested that the Board proceed with the amendments. Some Committee members also said the cost would not be significant. However, some ASAF members questioned whether the expected benefits were substantial enough for the Board to proceed with the amendments.

*Staff conclusion and recommendation*

16. We think that, on balance, the expected benefits outweigh the cost. We also think that the Board does not need to re-expose the amendments.
17. Accordingly, we recommend that the Board finalise the amendments.

***Alternative for project direction***

18. The amendments to IAS 8 would help clarify the distinction between accounting policies and estimates. As discussed in paragraph 10 of this paper, we think the amendments would not address all identified application questions. If the Board is of

the view that the expected benefits would not outweigh the cost, it could decide not to proceed with the proposed amendments and do no further work on this project.

19. However, several respondents to the Exposure Draft said it was helpful to clarify that selecting an estimation technique or a valuation technique constitutes making an accounting estimate. At the April 2019 Board meeting, some Board members said tis clarification, by itself, would bring sufficient benefits to justify proceeding with the amendments.
  
20. Accordingly, we think that the Board could decide not to proceed with the amendments, but instead, amend IAS 8 only to clarify that selecting an estimation technique or a valuation technique constitutes making an accounting estimate. Applying this approach, the Board would not proceed with any of the other proposed amendments that were included in the Exposure Draft. This approach would resolve a known application problem and would not involve significant costs.
  
21. If the Board is of the view that the expected benefits of proceeding with the amendments do not outweigh the cost, we would recommend that the Board apply this approach (ie amend IAS 8 only to clarify that selecting an estimation technique or a valuation technique constitutes making an accounting estimate).
  
22. We also considered, but do not recommend, some other alternatives suggested by respondents to the Exposure Draft. Appendix C to this paper includes our analysis of those alternatives.

**Staff recommendation**

23. We recommend that the Board:
  - (a) finalise the amendments with the modifications set out in Agenda Paper 26A for this meeting; and
  - (b) not re-expose the amendments.

**Question for the Board**

Does the Board agree with the recommendation set out in paragraph 23?

## Appendix A—re-exposure

A1. If the Board decides to proceed with the amendments, it would need to assess whether the modifications to the proposals included in the Exposure Draft warrant re-exposing the amendments.<sup>2</sup> This appendix presents our analysis and recommendation on this matter.

A2. Paragraphs 6.25–6.28 of the IFRS Foundation’s [\*Due Process Handbook\*](#) (Handbook) set out the criteria the Board considers when assessing the need for re-exposure.

These paragraphs state:

6.25 In considering whether there is a need for re-exposure, the IASB:

- (a) identifies substantial issues that emerged during the comment period on the Exposure Draft and that it had not previously considered;
- (b) assesses the evidence that it has considered;
- (c) determines whether it has sufficiently understood the issues, implications and likely effects of the new requirements and actively sought the views of interested parties; and
- (d) considers whether the various viewpoints were appropriately aired in the Exposure Draft and adequately discussed and reviewed in the Basis for Conclusions.

6.26 It is inevitable that the final proposals will include changes from those originally proposed. The fact that there are changes does not compel the IASB to re-expose the proposals. The IASB needs to consider whether the revised proposals include any fundamental changes on which respondents have not had the opportunity to comment because they were not contemplated or discussed in the Basis for Conclusions accompanying the Exposure Draft. The IASB also needs to consider whether it will learn anything new by re-exposing the proposals. If the IASB is satisfied that the revised proposals respond to the feedback received and that it is unlikely that re-exposure will reveal any new concerns, it should proceed to finalise the proposed requirements.

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<sup>2</sup> See agenda paper 26A for this meeting for a summary of the proposed modifications.

6.27 The more extensive and fundamental the changes from the Exposure Draft and current practice the more likely the proposals should be re-exposed. However, the IASB needs to weigh the cost of delaying improvements to financial reporting against the relative urgency for the need to change and what additional steps it has taken to consult since the Exposure Draft was published. The use of consultative groups or targeted consultation can give the IASB information to support a decision to finalise a proposal without the need for re-exposure.

6.28 The IASB should give more weight to changes in recognition and measurement than disclosure when considering whether re-exposure is necessary.

- A3. We acknowledge that some might say the Board should re-expose the proposed amendments, particularly because applying our recommendations would result in:
- (a) using terminology that is different from that proposed in the Exposure Draft (for example, the use of ‘measurement uncertainty’ rather than ‘estimation uncertainty’);
  - (b) removing some of the clarifications initially proposed (such as the proposed changes to the definition of accounting policies and clarification relating to the inventory cost formula) which changes the ‘package’ of proposed amendments included in the Exposure Draft; and
  - (c) including some examples illustrating the application of the proposed definition of accounting estimates.
- A4. Although we did not specifically seek feedback from ASAF and Committee members on the need to re-exposure, the ASAF member from the Accounting Standards Board of Japan suggested considering re-exposure in the light of the modifications<sup>3</sup>. One Committee observer also suggested that the Board (a) consider whether to re-expose the amendments, or (b) undertake extended outreach with stakeholders to help identify possible unintended consequences that might arise from the modifications.

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<sup>3</sup> The ASAF member from the Asian-Oceanian Standard-Setters Group also said one of its members suggested the Board consider re-exposure in the light of the modifications.

- A5. We think the modifications only address matters raised by respondents and do not constitute fundamental changes on which respondents have not had the opportunity to comment. In particular:
- (a) the substance of the definition of accounting estimates would not change from the proposal in the Exposure Draft. Although the definition would no longer define accounting estimates as judgements and assumptions themselves, but rather as the output of measurement techniques used in applying accounting policies, it would retain the key aspects of the definition included in the Exposure Draft—ie that accounting estimates (i) are used in applying an accounting policy; and (ii) involve the use of judgements and assumptions. The examples would simply illustrate the application of the definition.
  - (b) our proposals not to proceed with some of the clarifications that were initially proposed (such as the proposed changes to the definition of accounting policies and clarification relating to the inventory cost formula) are simply because we think those clarifications (a) raised more questions than answers, and (b) are not required to achieve the objectives of this project. We also think that our proposal not to proceed with changing the definition of accounting policies (eg to retain the terms rules and conventions in the definition of accounting policies) would not create any new overlap with the recommended definition of accounting estimates.
- A6. We also think it is unlikely that re-exposure will reveal any new concerns or identify unintended consequences. We have consulted with the Committee and the ASAF on our preliminary views. Feedback received from Committee and ASAF members was useful in confirming our understanding and analysis of the feedback and did not highlight any significant new concerns. Therefore, we think the consultation with Committee and ASAF members (a) provides information to support the Board in a decision to finalise the amendments without re-exposure, and (b) indicates that re-exposure may not reveal any new concerns.
- A7. On the basis of our analysis, we think the Board does not need to re-expose the amendments.

## **Appendix B—summary and analysis of feedback from Board members**

- B1. Most Board members supported finalising the proposed amendments and said the proposals improved IAS 8. In particular, some Board members said the clarification that a change in an estimation technique or a valuation technique is part of a change in an accounting estimate would, in itself, bring sufficient benefits to justify proceeding with the amendments. However, one Board member said, in his view, the expected benefits did not outweigh the costs.
- B2. [Agenda Paper 26D](#) for the Board’s April 2019 meeting acknowledged that the proposed amendments would not solve all identified application questions. One Board member asked for more information about the type of application questions that would remain unsolved. Paragraph 10 of this paper discusses this further.

## **Appendix C—consideration of other alternatives for project direction**

- C1. Some respondents suggested that the Board could develop specific requirements to address only particular identified application questions. Although this approach would lead to consistent application for those particular questions, we think doing so would require the Board to develop specific rules that would apply only in those particular situations. This would be contrary to the principles-based nature of IFRS Standards. This approach would also require significant additional time and cost to develop. Accordingly, we have not considered this approach further.
- C2. Some respondents suggested other alternative approaches the Board could consider. In particular, some respondents said the Board could:
- (a) revisit the requirements in IAS 8 for retrospective application by considering whether and when retrospective application provides useful information;
  - (b) define either an accounting policy or an accounting estimate and use a residual approach for all other changes; or
  - (c) remove the requirement for retrospective application of changes (ie entities would apply all changes prospectively), and permit changes only if they provide more relevant information. One respondent said the Board could also strengthen disclosure requirements for all changes.
- C3. We think considering the alternative approaches in paragraph C2 of this paper is beyond the scope of these narrow-scope amendments and would require a more fundamental review of IAS 8. Accordingly, we have not considered these approaches further.