

**Statement of  
Financial Accounting Standards  
No. 8**

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**Financial Accounting Standards Committee**

**Statement of Financial Accounting Standards No.8**

**Accounting Policies,  
Changes in Accounting Estimates and Errors**

**I Introduction**

- (1) This Statement establishes the accounting standards for processing accounting changes and prior period adjustments of a business.
- (2) Deleted

**II Explanation**

**Accounting changes**

- (3) Accounting changes include changes in accounting principles and changes in accounting estimate.
- (4) A change in accounting principle refers to the transfer from the originally adopted accounting principle to another. A change from an unaccepted accounting principle to a generally accepted one is a correction of an error instead of a change in accounting principle.

There are numerous circumstances calling for a change in accounting principle, including a change in the method of inventory valuation, such as from the weighted average cost method to the first-in-first-out (FIFO) method.

- (5) The following two circumstances do not constitute a change in accounting principle: (a) adoption of an appropriate accounting principle necessitated by transactions that previously were immaterial in substance; and (b) adoption of an appropriate accounting principle necessitated by transactions that are different in substance from those previously occurring.
- (6) A change in accounting estimate refers to the modification of a previous estimate when more justifiable and reasonable information is accumulated, additional information is obtained, or new events occur. 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 useful lives of, or expected pattern of consumption of the future economic benefits embodied in, depreciable assets; and
  - (d) warranty obligations.
- (7) Deleted.
- (8) Businesses should adopt accounting principles carefully and consistently from one accounting period to the next in order to facilitate the comparability of accounting data. An accounting principle once adopted should not be changed unless there is a change in the environment or the business can justify the use of a new accounting principle.

#### **Prior period adjustments**

- (9) Prior period adjustments refer to corrections of errors that result in financial statements being presented unfairly because of errors of calculation, recording, and identification (eg, misidentifying capital expenditure as revenue expenditure), as well as mis-adoption of accounting principles and methods. Such errors are limited to those

discovered after the issuance date of the financial statements, and those arising as a result of new accounting standards.

### **III Accounting standards**

#### **Accounting changes**

##### ***Change in accounting principle***

- (10) A change in accounting principle, except for those described in Paragraph 18, should be recognized on the following basis:
- (a) The amount of the cumulative effect resulting from the change to a new accounting principle should be calculated, and shown in the income statement between the captions *Extraordinary items* and *Net income*. The cumulative effect indicated above refers to the difference between (i) the amount of retained earnings at the beginning of the period of a change and (ii) the amount of retained earnings that would have been reported at that date if the new accounting principle had been applied retroactively for all prior periods.
  - (b) The effect of adopting the new accounting principle on income before extraordinary items and on net income of the period of the change should be disclosed.
  - (c) Financial statements for prior periods included for comparative purposes should be presented as previously reported. However, income before extraordinary items and net income computed on a pro forma basis should be shown on the face of the income statement for all periods presented as if the newly adopted accounting principle had been applied during all periods affected.
  - (d) The nature of the change in accounting principle and the reason that the new principle is preferable to the original

should be disclosed in the footnotes.

- (11) If a change in accounting principle does not result in the cumulative effect, the effect of the change on the income before extraordinary items and on the net income for the period should be disclosed. The nature of the change in method should also be described.
- (12) When calculating the cumulative effect of a change in accounting principle is impracticable, the cumulative effect may not be calculated. However, the effect of the change on the net income for the period in which the change occurred and the reason for omitting the accounting for the cumulative effect should be disclosed.

#### ***Change in accounting estimate***

- (13) The effect of a change in accounting estimate should be recognized as follows:
  - (a) If the change affects one period only (eg, the overstatement or the understatement of allowance for doubtful accounts), the effects should be recognized in that period, and there should be no prior period adjustment.
  - (b) If the change affects both the period of change and future periods (eg, a change in service lives of depreciable assets), the effects should be recognized in that period and the following periods. There should be no prior period adjustment, and no cumulative effect should be calculated. However, the effect on the income that results from the change in accounting estimate should be disclosed.
- (14) If a change in an accounting estimate and a change in an accounting principle occur simultaneously, and their effects are separable, then the change in the accounting principle should be processed first and the change in the accounting estimate should be processed second.
- (15) When distinguishing between a change in an accounting principle and a change in an accounting estimate is difficult, such change should be considered as changes in estimates.

#### ***Change in the reporting entity***

- (16) Deleted.

#### **Prior period adjustments**

- (17) When errors of prior period income items are discovered, corrections of errors should be treated as prior period adjustments, be recorded in the year in which the error was discovered, and be reported in the amount net of tax in the financial statements as an adjustment to the beginning balance of retained earnings. The related accounts on the balance sheet should also be adjusted. If comparative statements are prepared, the prior statements effected should be restated and the nature of the error, as well as its effect on the income of the year in which the error occurs, should be disclosed.
- (18) The situations that require adjustment of prior period income and restatement of all prior period financial statements are:
  - (a) a change in the method of accounting for long-term construction-type contracts;
  - (b) a change to or from the full-cost method of accounting in the extractive industries;
  - (c) issuance of financial statements by a business for the first time to obtain additional equity capital;
  - (d) a change in accounting principles to comply with newly issued accounting principles. However, other regulations should be observed if the committee has made other announcements;

#### **IV Notes**

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(19) If conditions stated in Paragraphs 10, 11, 12, 13, or 17 occur, then publicly-held companies should disclose the effect of accounting changes on prior period adjustments and on earnings per share.

(20) This Statement was issued on June 30, 1986. This Statement was first revised on July 20, 2006.

The first revision of this Statement shall be effective for financial statements with fiscal years beginning on or after January 1, 2007.

Early adoption is encouraged.

Those financial statements that had been originally prepared in accordance with the provisions of this Statement should not be restated retroactively to follow the first revision of this Statement.

The provisions of this Statement need not be applied to immaterial items.