Australian Accounting Standard **AAS 6**
March 1999

Accounting Policies

Prepared by the
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on behalf of the **Australian Society of Certified Practising Accountants** and **The Institute of Chartered Accountants in Australia**

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Defined words appear in *italics* the first time they appear in a section. The definitions are in Section 9. Standards are printed in **bold** type and commentary in light type.

MAIN FEATURES OF THE STANDARD

The Standard:

(a) requires accounting policies to be selected and applied in a manner which ensures that the resultant financial information:

    (i) satisfies the concepts of relevance and reliability

    (ii) is comparable and understandable, without sacrificing relevance and reliability

(b) permits a change in an accounting policy to be made only when

    (i) it is necessary in order to comply with another Australian Accounting Standard or an Urgent Issues Group Consensus View; or

    (ii) no specific Australian Accounting Standard applies and the change will result in an overall improvement in the relevance and reliability of financial information about the financial performance, financial position and cash flows of the entity; or

    (iii) an Australian Accounting Standard permits alternative accounting policies and the change from one permitted accounting policy to another permitted accounting policy will result in an overall improvement in the relevance and reliability of financial information about the financial performance, financial position and cash flows of the entity

(c) requires a change in an accounting policy on the initial adoption of another Australian Accounting Standard or an Urgent Issues Group Consensus View to be accounted for in accordance with the specific transitional provisions in that Australian Accounting Standard or Urgent Issues Group Consensus View

(d) requires the cumulative financial effect of a change in an accounting policy that is not a change on the initial adoption of another Australian Accounting Standard or an Urgent Issues Group Consensus View to be calculated as if the new accounting policy had always been applied, except where it is not practicable to determine the cumulative effect of the change in accounting policy, in which case the new accounting policy must be applied from the beginning of the current reporting period

(e) requires an entity's financial report to be prepared on a going concern basis unless it is intended to either liquidate the entity or to otherwise wind up its operations, or there is no realistic alternative but to liquidate the entity or to otherwise wind up its operations

(f) requires an entity to prepare its statement of financial performance and its statement of financial position on an accrual basis

(g) requires specific disclosures in relation to accounting policies, including disclosures about changes in accounting policies.

AUSTRALIAN ACCOUNTING STANDARD

AAS 6 "ACCOUNTING POLICIES"

1 Application

1.1 This Standard applies to:

(a) *general purpose financial reports* of each *reporting entity* to which Accounting Standards operative under the Corporations Law do not apply; or

(b) financial reports that are held out to be general purpose financial reports by an *entity* which is not a reporting entity, and to which Accounting Standards operative under the Corporations Law do not apply.

1.1.1 Accounting Standards operative under the Corporations Law apply to companies and to other entities required by legislation, ministerial directive or other government authority to apply such Standards. Reporting entities which are not required to apply Accounting Standards operative under the Corporations Law are required to apply this Standard.

1.1.2 The standards specified in this Standard apply to the financial report where information resulting from their application is material in accordance with Australian Accounting Standard AAS 5 "Materiality".

2 Operative Date

2.1 This Standard applies to reporting periods ending on or after 31 December 1999.

2.2 This Standard may be applied to reporting periods ending before 31 December 1999.

2.2.1 Australian Accounting Standard AAS 6 "Accounting Policies", as issued in September 1995, continues to apply to reporting periods that end before 31 December 1999. However, where an *entity* elects to apply this Standard early in accordance with paragraph 2.2, it will not also be obliged to comply with AAS 6, as issued in September 1995, for the reporting periods to which the election applies.

2.3 When operative, this Standard supersedes Australian Accounting Standard AAS 6 "Accounting Policies", as issued in October 1998.

3 Purpose of Standard

3.1 The purpose of this Standard is to:

(a) prescribe the concepts that guide the selection, application and disclosure of *accounting policies*

(b) require specific disclosures to be made in relation to the accounting policies adopted in the preparation and presentation of the financial report.

4 Criteria for Selection and Application of Accounting Policies

4.1 To ensure that the substance of the underlying transactions or other events is reported in the financial report, *accounting policies* must be selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of *relevance* and *reliability*.

4.1.1 Statement of Accounting Concepts SAC 3 "Qualitative Characteristics of Financial Information" identifies relevance and reliability as the primary qualitative characteristics that financial information should possess if it is to be useful to users in making and evaluating decisions about the allocation of scarce resources. Accordingly, the concepts of relevance and reliability are central to the selection of accounting policies.

4.1.2 The accounting policies to be applied to many transactions or other events are specified in Australian Accounting Standards, other authoritative pronouncements of the Public Sector Accounting Standards Board (PSASB) and/or the Australian Accounting Standards Board (AASB), or Urgent Issues Group (UIG) Consensus Views. In the absence of a specific Australian Accounting Standard, other authoritative pronouncement of the PSASB and/or the AASB or UIG Consensus View, judgement is used in selecting an accounting policy that provides the most useful information to users of the *entity's* financial report. In making this judgement, other pronouncements that are considered, in order of preference, are:

(a) the requirements and guidance in other Australian Accounting Standards or other authoritative pronouncements of the PSASB and/or the AASB dealing with similar or related issues

(b) the requirements and guidance in UIG Consensus Views dealing with similar or related issues

(c) the definitions and recognition criteria for assets, liabilities, equity, revenues and expenses set out in Statement of Accounting Concepts SAC 4 "Definition and Recognition of the Elements of Financial Statements"

(d) International Accounting Standards and Interpretations of the Standing Interpretations Committee of the International Accounting Standards Committee (only to the extent that these are consistent with (a), (b) and (c) of this paragraph)

(e) the pronouncements of other national accounting standard setting bodies and accepted industry practices (only to the extent that these are consistent with (a), (b) and (c) of this paragraph).

Relevance

4.1.3 Relevant financial information assists users in making and evaluating decisions about the allocation of scarce resources. It assists them in making predictions about future situations and in forming expectations, or it plays a confirmatory role in respect of their past evaluations.

4.1.4 Financial information may be relevant because of its nature, its nature and magnitude, or because of its magnitude in relation to its nature. Additional guidance on relevance is provided in SAC 3.

Reliability

4.1.5 Reliable financial information faithfully conveys to users the underlying transactions and other events that have occurred.

4.1.6 For financial information to be reliable, it needs to be free from bias. Reliable financial information does not lead users to conclusions that serve particular needs, desires or preconceptions of the preparers of financial reports.

4.1.7 To be reliable, financial information also needs to be free from undue error. Because of the inherent difficulties in identifying the economic phenomena to be measured or in devising or applying measurement or presentation techniques, financial information is subject to some risk of error. The impact of this risk on the usefulness of financial information can be offset in some cases by disclosure of the uncertainties relating to the information. Additional guidance on reliability is provided in SAC 3.

Substance

4.1.8 For financial information to satisfy both the relevance and reliability concepts, it is necessary that the substance rather than the form of a transaction or other event be reported where substance and form differ.

4.1.9 Reporting the substance of a transaction or other event requires that the information reported reflects its economic effect. In financial reporting, the substance of a transaction or other event is reflected in the assets, liabilities, equity, revenues and expenses (the elements of financial statements) resulting from or altered by the transaction or other event. Since such elements are often derived from legal rights and obligations, these rights and obligations are often important in determining the substance of a transaction or other event.

4.1.10 However, where the substance of certain transactions or other events is not adequately expressed by their legal form, it is inappropriate to account for them in accordance with their form. For example, an entity may transfer legal ownership of an asset to another party but have arrangements in place which ensure that it continues to enjoy future economic benefits embodied in that asset. If the entity were to account for such a transfer as a disposal of the future economic benefits embodied in that asset, its financial report would be unreliable as it would not faithfully represent the economic effect of the transaction.

4.1.11 Determining the substance of a transaction or other event involves identifying all of its aspects and implications, and considering the position of each of the parties to it, including their expectations and motivations for entering into the transaction or other event. For example, where goods are sold subject to retention of title pending settlement, the buyer or the seller is not prevented from *recognising* the transaction as a purchase or sale at the time of delivery where it is probable that the transaction will be settled in the normal course of business.

4.1.12 The notion of accounting for the substance of transactions is identified in numerous Australian Accounting Standards. For example, Australian Accounting Standard AAS 24 "Consolidated Financial Reports" requires an *economic entity*, comprising the *parent entity* and each of the entities that it controls, to prepare consolidated financial reports. Adoption of the criterion of control ensures that all the resources under the control of the parent entity are reflected in the consolidated financial report, irrespective of whether an ownership interest is held. This approach enables a number of individual but related entities to be identified as a single entity, so as to reflect the substance of the economic entity as a single economic unit.

4.1.13 Similarly, Australian Accounting Standard AAS 17 "Leases" requires a finance lease asset and liability to be recognised in the financial report of the lessee. Although the legal form of the lease agreement is such that the lessee does not acquire legal title to the leased property, the substance is that the lessee acquires the rights to most of the future economic benefits from the use of the leased property.

4.1.14 Australian Accounting Standard AAS 15 "Revenue" also reflects the notion of accounting for the substance of a transaction. Where an entity sells an asset to another entity and has in place arrangements under which the payment is deferred for some time, the economic effect of the transactions is that the vendor entity has sold an asset and also financed the other entity's purchase. Accordingly, the vendor accounts for the two separate transactions as a sale transaction and a financing transaction. This ensures that the sales revenue is not misstated and that information about the interest revenue implicit in the financing arrangement is properly reflected in the financial report.

5 Consistency of Application of Accounting Policies

5.1 ***Accounting policies* must be applied in a manner which ensures that the resulting financial information is *comparable* and *understandable*, without sacrificing its *relevance* and *reliability*.**

Comparability

5.1.1 The users of financial reports need to be able to compare aspects of an *entity* over time and compare aspects between entities at one time and over time. This implies that the *recognition*, measurement and presentation of transactions or other events need to be carried out in a consistent manner throughout an entity and over time for that entity, and that there needs to be consistency between entities in these regards. However, consistency should not impede the introduction of improved financial reporting. It is not acceptable for an entity to retain its accounting policies to the detriment of the concepts of relevance and reliability. Additional guidance on comparability is provided in SAC 3.

Understandability

5.1.2 Information should be presented in financial reports in the most understandable manner, without sacrificing its relevance and reliability. It is assumed that users possess the proficiency necessary to comprehend the significance of contemporary financial reporting practices. Additional guidance on understandability is provided in SAC 3.

6 Changes in Accounting Policies

6.1 A change in an *accounting policy* must be made only when:

(a) it is necessary in order to comply with another Australian Accounting Standard or an Urgent Issues Group Consensus View; or

(b) no specific Australian Accounting Standard applies and the change will result in an overall improvement in the *relevance* and *reliability* of financial information about the financial performance, financial position and cash flows of the *entity*; or

(c) an Australian Accounting Standard permits alternative accounting policies and the change from one permitted accounting policy to another permitted accounting policy will result in an overall improvement in the relevance and reliability of financial information about the financial performance, financial position and cash flows of the entity.

6.1.1 Users need to be able to compare the financial report of an entity over a period of time to identify trends in its financial performance, financial position and cash flows. Therefore, the same accounting policies are normally adopted in each reporting period.

Adoption of an Australian Accounting Standard or an Urgent Issues Group Consensus View

6.2 A change in an accounting policy that is made on the initial adoption of another Australian Accounting Standard or an Urgent Issues Group Consensus View must be accounted for in accordance with the specific transitional provisions in that Australian Accounting Standard or Urgent Issues Group Consensus View.

6.2.1 When the entity is allowed to, but elects not to, adopt a new Australian Accounting Standard prior to its operative date, the entity is encouraged to disclose the nature of the future change in accounting policy and an estimate of the effect of the change on its financial performance and financial position.

Other Changes in Accounting Policies

6.3 Subject to paragraph 6.5, the cumulative financial effect of a change in an accounting policy that is not a change arising on the initial adoption of another Australian Accounting Standard or an Urgent Issues Group Consensus View must be calculated as if the new accounting policy had always been applied. The cumulative financial effect up to the end of the *preceding reporting period*, including any adjustment to deferred income tax balances, must be *recognised* as a *revenue* or an *expense* in the statement of financial performance in the reporting period in which the change is made.

6.3.1 The cumulative financial effect up to the end of the preceding reporting period recognised as a revenue or an expense in the statement of financial performance in accordance with paragraph 6.3 comprises those amounts that would have been recognised as a revenue or an expense in previous reporting periods had the new accounting policy always applied.

6.4 Comparative information on the face of the financial statements must not be restated where the cumulative financial effect up to the end of the preceding reporting period of a change in accounting policy is recognised in accordance with paragraph 6.3.

6.5 When it is not practicable to determine the cumulative financial effect up to the end of the preceding reporting period of a change in an accounting policy that is not a change arising on

the initial adoption of another Australian Accounting Standard or an Urgent Issues Group Consensus View, the new accounting policy must be applied from the beginning of the *current reporting period.*

7 Going Concern and Accrual Bases of Accounting

Going Concern Basis

7.1 When preparing the financial report, an assessment must be made of the *entity's* ability to continue as a going concern. The financial report must be prepared on a *going concern basis* unless it is intended to either liquidate the entity or to otherwise wind up its operations, or there is no realistic alternative but to liquidate the entity or to otherwise wind up its operations.

7.1.1 In assessing whether the going concern basis is appropriate, it is necessary to consider all available information for the foreseeable future, which is at least, but is not limited to, twelve months from the *reporting date*. Each case is assessed on its own merit. Where an entity has a history of profitable operations and ready access to financial resources, a conclusion that the going concern basis of accounting is appropriate may be reached without detailed analysis. In other cases it may be necessary to consider a wide range of factors including current and expected profitability, debt repayment schedules and potential sources of replacement financing before it can be established that the going concern basis is appropriate.

7.1.2 In the public sector there may be circumstances where an entity is to be abolished or restructured after the reporting date pursuant to legislation, ministerial directive or other externally imposed requirement, and the assets and liabilities of the entity will be transferred to another entity after the reporting date, even at no cost or for nominal consideration. In such circumstances, the abolition or restructuring of itself does not mean that the entity is not a going concern at the reporting date.

7.1.3 Where, at the reporting date, it is intended that the entity be liquidated or its operations otherwise wound up, or there is an expectation that there will be no alternative but to liquidate the entity or otherwise wind up its operations, the financial report is not prepared on a going concern basis. Similarly, where an event occurring after the reporting date provides evidence that the entity was not a going concern at the reporting date, the financial report is not prepared on a going concern basis. However, where an event occurring after the reporting date provides evidence that the going concern basis is not appropriate after the reporting date, the financial effect of the event is disclosed but not *recognised* in the financial report. This is consistent with Australian Accounting Standard AAS 8 “Events Occurring After Reporting Date”.

7.1.4 Where it is apparent that the going concern basis is not appropriate, the financial report is generally prepared on a liquidation basis.

Accrual Basis

7.2 The entity must prepare its statement of financial performance and its statement of financial position on an *accrual basis*.

7.2.1 The accrual basis recognises the financial effects of transactions or other events in the reporting periods in which they occur, to the extent that those financial effects can be recognised, irrespective of whether cash has been received or paid. Accrual accounting provides information about assets, liabilities, equity, revenues and expenses, and changes in them, that cannot be obtained by accounting only for cash receipts and payments. The cash basis of accounting, which recognises the financial effects of transactions or other events only when cash has been received or paid, provides information of limited use for decision making. Such information is insufficient for assessing or identifying the assets the entity controls, the liabilities it is obliged to meet, and the revenues and expenses resulting from increases or decreases in those assets and liabilities. Accordingly, the accrual basis is the required *accounting basis*.

8 Disclosures

General

8.1 A summary of *accounting policies* must be presented in the initial section of the notes in the financial report. The following items must be disclosed in that summary:

(a) a statement that the financial report is a *general purpose financial report*

(b) a statement as to whether the financial report has been prepared in accordance with:

(i) Australian Accounting Standards

(ii) **other authoritative pronouncements of the Public Sector Accounting Standards Board and/or the Australian Accounting Standards Board**

(iii) **Urgent Issues Group Consensus Views**

(c) **a description of the measurement basis or bases used in preparing the financial report**

(d) **a description of each specific accounting policy that is necessary for an *understanding* of the financial report.**

8.1.1 The financial reporting framework applied in the preparation of the financial report is identified in the summary of accounting policies so that users understand the basis on which the financial report has been prepared. In addition to stating whether the financial report has been prepared in accordance with Australian Accounting Standards, other authoritative pronouncements of the Public Sector Accounting Standards Board and/or the Australian Accounting Standards Board, and Urgent Issues Group Consensus Views, it may also be appropriate to indicate the relevant statutory and other requirements adopted in the preparation of the financial report.

8.1.2 It is also important for users to be aware of the measurement basis or bases used in preparing the financial report. The different measurement bases that may be used include, but are not limited to, historical cost, current cost, net market value, or present value. Where more than one measurement basis is used, for example where certain non-current assets are revalued, it is sufficient to disclose a description of the class of assets and liabilities to which each measurement basis is applied.

8.1.3 In making judgements about the detail to be disclosed about an *entity's* accounting policies, consideration is given to the likely users of the financial report and their information needs. Therefore, it is necessary to consider the nature of the entity's operations and the policies which a user would expect to be disclosed for that type of entity. For example, where an entity has significant foreign operations or transactions in foreign currencies, the accounting policy adopted for foreign currency translation is disclosed.

8.1.4 To facilitate users' understanding of the accounting policies applied, it is useful to disclose information about the assumptions made in determining the policies and the methods adopted in applying them. These disclosures are a matter of judgement.

8.1.5 Where there is no Australian Accounting Standard, other authoritative pronouncements of the Public Sector Accounting Standards Board and/or the Australian Accounting Standards Board, or Urgent Issues Group Consensus View which specifies an accounting policy for a particular transaction or other event, the disclosures focus on explaining why the policy applied ensures that *relevant* and *reliable* information is presented in the financial report.

Material Uncertainty as to the Going Concern Basis

8.2 Where the financial report is prepared on a *going concern basis*, but material uncertainties exist in relation to events or conditions which cast doubt upon the entity's ability to continue as a going concern, those uncertainties must be disclosed in the summary of accounting policies.

8.2.1 An example of a material uncertainty related to an event or condition casting doubt upon an entity's ability to continue as a going concern is where the entity's fixed term borrowings are approaching maturity, and the entity's capacity to renew those fixed term borrowings or to obtain alternative sources of finance is uncertain.

8.2.2 The disclosure required by paragraph 8.2 includes, but is not limited to, disclosure of each of the following:

(a) a description of the events or conditions and the nature of the uncertainties

(b) the entity's plans for addressing those uncertainties and any mitigating factors.

Financial Report Prepared Other than on a Going Concern Basis

8.3 Where the financial report is prepared otherwise than on a going concern basis, the following must be disclosed in the summary of accounting policies:

(a) the fact that the going concern basis has not been applied

(b) the reasons for not applying the going concern basis

(c) the basis on which the financial report has been prepared.

Changes in Accounting Policies

8.4 Where a change in an accounting policy from that applied in the *preceding reporting period* has an effect in the *current reporting period* or any prior reporting periods presented in the financial report, or is expected to have an effect in a subsequent reporting period, the following must be disclosed in the summary of accounting policies or in a note referred to in the summary of accounting policies:

(a) the nature of the change

(b) the reasons for the change

(c) the amount of the adjustment, if any, *recognised* as a revenue or an expense in the statement of financial performance for the reporting period

(d) the amount of the adjustment, if any, to the opening balance of retained profits (surplus) or accumulated losses (deficiency) of the current reporting period

(e) the amount of the adjustment relating to prior reporting periods, including:

(i) where practicable, the restatement of comparative information for each prior reporting period presented in the financial report to show the information that would have been disclosed in the prior reporting period had the new accounting policy always been applied. If it is impracticable to restate the comparative information for each prior reporting period presented, that fact must be disclosed

(ii) the amount of the adjustment relating to reporting periods prior to those presented in the financial report.

8.4.1 Adjustments resulting from a change in an accounting policy are accounted for in accordance with the specific transitional provisions in the relevant Australian Accounting Standard or Urgent Issues Group Consensus View or, where the change does not relate to the initial adoption of an Australian Accounting Standard or an Urgent Issues Group Consensus View, are recognised in the statement of financial performance in the reporting period in which the change is made. Additional information is presented to show the statement of financial performance for the reporting period and any prior reporting periods presented in the financial report as if the new accounting policy had always been applied. These disclosure requirements are illustrated in the Appendix to this Standard.

8.5 Where a change in an accounting policy made in the preceding reporting period did not have a material effect in that reporting period but has a material effect in the current reporting period, the following must be disclosed in the summary of accounting policies or in a note referred to in the summary of accounting policies:

(a) the nature of the change

(b) the reasons for the change

(c) that the change was made in the preceding reporting period

(d) the financial effect of the change in the current reporting period.

8.5.1 The financial effect disclosed in accordance with paragraph 8.5(d) is determined by comparing the result of applying the new accounting policy for the entire reporting period and the result of applying the old accounting policy for the entire reporting period.

9 Definitions

9.1 In this Standard:

***accounting basis* means the general basis of accounting underlying the financial report, including, but not limited to, the historical cost basis, the current cost basis, the *going concern basis*, the *accrual basis* and the cash basis of accounting**

***accounting policies* means the specific accounting principles, bases or rules adopted in preparing and presenting the financial report**

***accrual basis* means the *accounting basis* where the assets, liabilities, equity, revenues and expenses are *recognised* in the reporting periods to which they relate, regardless of when cash is received or paid**

***comparability* means that quality of financial information which exists when users of that information are able to discern and evaluate similarities in, and differences between, the nature and effects of transactions or other events, at one time and over time, either when assessing aspects of a single *reporting entity* or of a number of reporting entities**

***current reporting period* means the reporting period of an *entity* to which the financial report relates**

economic entity* means a group of entities comprising the *parent entity* and each of its *subsidiaries

***entity* means any legal, administrative, or fiduciary arrangement, organisational structure or other party (including a person) having the capacity to deploy scarce resources in order to achieve objectives**

***general purpose financial report* means a financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs**

***going concern basis* means the accounting basis whereby in the preparation of the financial report the entity is viewed as a going concern, that is, the entity is expected to**

(a) be able to pay its debts as and when they become due and payable; and

(b) continue in operation without any intention or necessity to liquidate or otherwise wind up its operations

***parent entity* means an entity which controls another entity**

***preceding reporting period* means the reporting period of an entity immediately preceding the reporting period to which the financial report relates**

***recognised* means reported on, or incorporated in amounts reported on, the face of the statement of financial performance or the statement of financial position (whether or not further disclosure of the item is made in the notes)**

relevance **means that quality of financial information which exists when that information influences decisions by users about the allocation of scarce resources by:**

(a) **helping them form predictions about the outcomes of past, present or future events; or**

(b) **confirming or correcting their past evaluations**

and which enables users to assess the discharge of accountability by the management or governing body of the entity

reliability **means that quality of financial information which exists when that information can be depended upon to represent faithfully, and without bias or undue error, the transactions or other events that either it purports to represent or could reasonably be expected to represent**

reporting date **means the end of the reporting period to which the financial report relates**

reporting entity **means an entity (including an *economic entity*) in respect of which it is reasonable to expect the existence of users dependent on *general purpose financial reports* for information which will be useful to them for making and evaluating decisions about the allocation of scarce resources**

statement of financial performance **means profit and loss statement or other operating statement as referred to in other Australian Accounting Standards**

subsidiary **means an entity which is controlled by a parent entity**

understandability **means that quality of financial information which exists when users of that information are able to comprehend its meaning.**

CONFORMITY WITH INTERNATIONAL AND NEW ZEALAND ACCOUNTING STANDARDS

Conformity with International Accounting Standards

As at the date of issue of this Standard, compliance with this Standard will ensure conformity with International Accounting Standard IAS 1 "Presentation of Financial Statements" to the extent that IAS 1 addresses accounting policies.

As at the date of issue of this Standard, compliance with this Standard will also ensure conformity with International Accounting Standard IAS 8 "Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies" to the extent that IAS 8 addresses changes in accounting policies.

Conformity with New Zealand Accounting Standards

As at the date of issue of this Standard, compliance with this Standard will ensure conformity with Financial Reporting Standard FRS-1 "Disclosure of Accounting Policies".

APPENDIX

CHANGES IN ACCOUNTING POLICY

This Appendix forms part of the commentary. Its purpose is to illustrate the disclosures required in accordance with paragraph 8.4 of the Standard.

DATA

During 20X2, Gamma Entity changed its accounting policy for computer software development costs. In previous reporting periods Gamma capitalised such costs. Gamma has now decided that the development of computer software has evolved such that the future economic benefits in respect of these costs cannot be reliably determined and that the costs should therefore be expensed.

Gamma capitalised computer software development costs of $2,600 during 20X1 and $5,200 in periods prior to 20X1. Computer software development costs for 20X2 totalled $3,000.

In addition, Gamma became a reporting entity during 20X2 and is therefore required to prepare its general purpose financial report in accordance with Australian Accounting Standards. As a result, Gamma changed its accounting policy for employee sick leave entitlements to ensure that it complies with the requirements of AAS 30 “Accounting for Employee Entitlements”. The sick leave entitlements of Gamma’s employees accumulate and vest in a similar manner to annual leave entitlements. In previous reporting periods Gamma recognised sick leave entitlements as an expense only to the extent that the entitlements had been used by and/or paid to employees during the reporting period. AAS 30 requires employee sick leave entitlements which accumulate with the provision of services by employees to be recognised as an expense in the reporting period in which the employer consumes the employees’ services. The transitional provisions of AAS 30 require adjustments arising on the initial application of the Standard to be made to the opening balance of retained profits (surplus) or accumulated losses (deficiency) in the reporting period in which the Standard is first applied.

Employee entitlements to sick leave arising from services provided during 20X2 totalled $2,500. Gamma expensed sick leave of $1,500 during 20X1, however employee entitlements to sick leave arising from services provided during that period totalled $2,300. The unpaid sick leave entitlements owing to Gamma employees as at 31 December 20X0 was $2,800.

Gamma’s tax rate for 20X1 and 20X2 was 30%.

Gamma Entity
Statement of Financial Performance
for the reporting period ended 31 December 20X2

	20X2 **$**	**20X1** **$**
Profit/result from ordinary activities before the effect of change in accounting policy for computer software development costs and income tax expense	27,000	18,000
Cumulative effect of change in accounting policy for computer software development costs	(7,800)	–
Profit/result from ordinary activities before income tax expense	19,200	18,000
Income tax expense	(5,760)	(5,400)
Profit/result from ordinary activities after income tax expense	13,440	12,600

Note X Changes in Accounting Policies

An adjustment of $7,800 (before income tax benefit of $2,340) has been made in the statement of financial performance for 20X2, representing the effect of a change in accounting policy for the treatment of computer software development costs. These costs are now expensed rather than capitalised as they do not meet the criteria for recognition as assets.

As a result of adopting the requirements of AAS 30 "Accounting for Employee Entitlements", an adjustment of $3,600 (before tax benefit of $1,080) has been made to the opening balance of retained profits (surplus) for 20X2, representing the effect of a change in accounting policy for employee sick leave entitlements. Employee sick leave is now recognised as an expense in the reporting period in which the entitlement to sick leave accumulates to the employee rather than the reporting period in which the entitlements are used by and/or paid to employees.

The pro forma statement of financial performance and the restatement of retained profits (surplus) below show the information that would have been disclosed had the new accounting policies always been applied. Retained profits (surplus) as at the beginning of 20X1 have been reduced by $5,600, comprising an adjustment of $3,640 ($5,200 less tax benefit of $1,560) for computer software development costs relating to periods prior to 20X1, and an adjustment of $1,960 ($2,800 less tax benefit of $840) for employee sick leave entitlements relating to periods prior to 20X1.

Pro Forma Statement of Financial Performance

	20X2 $ (restated)	**20X1 $ (restated)**
Profit/result from ordinary activities before computer software, employee sick leave and income tax expenses	32,500	19,500
Computer software expense	(3,000)	(2,600)
Employee sick leave expense	(2,500)	(2,300)
Profit/result from ordinary activities before income tax expense	27,000	14,600
Income tax expense	(8,100)	(4,380)
Profit/result from ordinary activities after income tax expense	18,900	10,220

Restatement of Retained Profits (Surplus)

Previously reported retained profits (surplus) at the end of the previous reporting period	32,600	20,000
Change in accounting policy for computer software expense (net of income tax expense of $2,340 for 20X2 and $1,560 for 20X1)	(5,460)	(3,640)
Change in accounting policy for employee sick leave expense (net of income tax expense of $1,080 for 20X2 and $840 for 20X1)	(2,520)	(1,960)
Restated retained profits (surplus) at the beginning of the reporting period	24,620	14,400
Net profit/result from ordinary activities	18,900	10,220
Restated retained profits (surplus) at the end of the reporting period	43,520	24,620

BACKGROUND TO REVISION

This section does not form part of the Standard. It is a summary of the reasons for the current revision to the Standard.

1 The reissue of the Standard is part of a program being undertaken by the Public Sector Accounting Standards Board of the Australian Accounting Research Foundation and the Australian Accounting Standards Board (the Boards) to achieve greater harmony between Australian accounting standards and those of the International Accounting Standards Committee.

2 The reissue of the Standard follows consideration of the responses received on Exposure Draft ED 93 "Statement of Financial Performance and Ancillary Amendments", which was prepared by the Boards and released in July 1998. ED 93 included proposals aimed at harmonising Australian Accounting Standard AAS 6 and Accounting Standard AASB 1001 "Accounting Policies" with International Accounting Standard IAS 8 "Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies" to the extent that IAS 8 addresses changes in accounting policies.

Principal Changes from the Previous Standard

3 Consistent with the proposals in ED 93, the Standard:

(a) permits a change in an accounting policy to be made only when

(i) it is necessary in order to comply with another Australian Accounting Standard or an Urgent Issues Group Consensus View; or

(ii) no specific Australian Accounting Standard applies and the change will result in an overall improvement in the relevance and reliability of financial information about the financial performance, financial position and cash flows of the entity; or

(iii) an Australian Accounting Standard permits alternative accounting policies and the change from one permitted accounting policy to another permitted accounting policy will result in an overall improvement in the relevance and reliability of financial information about the financial performance, financial position and cash flows of the entity

(b) requires a change in an accounting policy on the initial adoption of another Australian Accounting Standard or an Urgent Issues Group Consensus View to be accounted for in accordance with the specific transitional provisions in that Australian Accounting Standard or Urgent Issues Group Consensus View

(c) requires the cumulative financial effect of a change in an accounting policy that is not a change on the initial adoption of another Australian Accounting Standard or an Urgent Issues Group Consensus View to be calculated as if the new accounting policy had always been applied, except where it is not practicable to determine the cumulative effect of the change in accounting policy, in which case the new accounting policy must be applied from the beginning of the current reporting period

(d) requires the following information to be disclosed where a change in an accounting policy has an effect in the current reporting period or any prior reporting periods presented in the financial report, or is expected to have an effect in a subsequent reporting period:

  (i) the nature of the change

  (ii) the reasons for the change

  (iii) the amount of the adjustment, if any, recognised as a revenue or an expense in the statement of financial performance for the reporting period

  (iv) the amount of the adjustment, if any, to the opening balance of retained profits (surplus) or accumulated losses (deficiency) of the current reporting period

  (v) the amount of the adjustment relating to prior reporting periods, including, where practicable, the restatement of comparative information for each prior reporting period presented in the financial report, and the amount of the adjustment relating to reporting periods prior to those presented in the financial report.

Noteworthy Differences from ED 93

4 The Standard retains the basic structure and content of the proposals in ED 93.