FINANCIAL ACCOUNTING SERIES

ACCOUNTING STANDARDS UPDATE

No. 2015-11
July 2015

# Inventory (Topic 330)

## Simplifying the Measurement of Inventory

An Amendment of the *FASB Accounting Standards Codification*®

Financial Accounting Standards Board

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FASB

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# Accounting Standards Update 2015-11

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# Simplifying the Measurement of Inventory

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# Summary

## Why Is the FASB Issuing This Accounting Standards Update (Update)?

The Board is issuing this Update as part of its Simplification Initiative. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of generally accepted accounting principles (GAAP) for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements.

The Board heard from stakeholders that the guidance on the subsequent measurement of inventory is unnecessarily complex because there are several potential outcomes. Topic 330, Inventory, currently requires an entity to measure inventory at the lower of cost or market. Market could be replacement cost, net realizable value, or net realizable value less an approximately normal profit margin.

## Who Is Affected by the Amendments in This Update?

The amendments in this Update do not apply to inventory that is measured using last-in, first-out (LIFO) or the retail inventory method. The amendments apply to all other inventory, which includes inventory that is measured using first-in, first-out (FIFO) or average cost. The Board received feedback from stakeholders that the proposed amendments would reduce costs and increase comparability for inventory measured using FIFO or average cost but potentially could result in significant transition costs that would not be justified by the benefits for inventory measured using LIFO or the retail inventory method due to the complexity inherent in those methods. Therefore, the Board decided to limit the scope of the simplification to exclude inventory measured using LIFO or the retail inventory method.

## What Are the Main Provisions?

An entity should measure inventory within the scope of this Update at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. Subsequent measurement is unchanged for inventory measured using LIFO or the retail inventory method.

The amendments in this Update more closely align the measurement of inventory in GAAP with the measurement of inventory in International Financial Reporting Standards (IFRS).

The Board has amended some of the other guidance in Topic 330 to more clearly articulate the requirements for the measurement and disclosure of inventory. However, the Board does not intend for those clarifications to result in any changes in practice. Other than the change in the subsequent measurement guidance from the lower of cost or market to the lower of cost and net realizable value for inventory within the scope of this Update, there are no other substantive changes to the guidance on measurement of inventory.

## When Will the Amendments Be Effective and What Are the Transition Requirements?

For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. For all other entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017. The amendments in this Update should be applied prospectively with earlier application permitted as of the beginning of an interim or annual reporting period.

# Amendments to the *FASB Accounting Standards Codification*®

## Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–25. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is <u>underlined</u>, and deleted text is ~~struck out~~.

## Amendments to Master Glossary

2. Amend the Master Glossary term *Direct Effects of a Change in Accounting Principle,* with a link to transition paragraph 330-10-65-1, as follows: **[Note: The term *Net Realizable Value* is shown for convenience.]**

**Direct Effects of a Change in Accounting Principle**

Those recognized changes in assets or liabilities necessary to effect a change in accounting principle. An example of a direct effect is an adjustment to an inventory balance to effect a change in inventory valuation method. Related changes, such as an effect on deferred income tax assets or liabilities or an impairment adjustment resulting from applying the <u>subsequent measurement guidance in Subtopic 330-10</u> ~~lower-of-cost-or-market test~~ to the adjusted inventory balance, also are examples of direct effects of a change in accounting principle.

**Net Realizable Value**

Estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation.

## Amendments to Subtopic 330-10

3. Supersede paragraph 330-10-35-1 and its related heading and paragraph 330-10-35-6, add paragraphs 330-10-35-1A through 35-1C and 330-10-35-7A and their related headings, and amend paragraphs 330-10-35-2 and 330-10-35-8 through 35-11, with a link to transition paragraph 330-10-65-1, as follows:

# Inventory—Overall

## Subsequent Measurement

~~**> Adjustments to Lower of Cost or Market**~~

**330-10-35-1** Paragraph superseded by Accounting Standards Update 2015-11. ~~A departure from the cost basis of pricing the **inventory** is required when the utility of the goods is no longer as great as their cost. Where there is evidence that the utility of goods, in their disposal in the ordinary course of business, will be less than cost, whether due to physical deterioration, obsolescence, changes in price levels, or other causes, the difference shall be recognized as a loss of the current period. This is generally accomplished by stating such goods at a lower level commonly designated as **market**.~~ **[Content amended and moved to paragraph 330-10-35-1C]**

**330-10-35-1A** The subsequent measurement of **inventory** depends on the cost method and is different for the following:

a. Inventory measured using any method other than last-in, first-out (LIFO) or the retail inventory method (see paragraph 330-10-35-1B)
b. Inventory measured using LIFO or the retail inventory method (see paragraphs 330-10-35-1C through 35-7).

Paragraphs 330-10-35-7A through 35-11 apply to all inventory.

**> Inventory Measured Using Any Method Other Than LIFO or the Retail Inventory Method**

**330-10-35-1B** Inventory measured using any method other than LIFO or the retail inventory method (for example, inventory measured using first-in, first-out (FIFO) or average cost) shall be measured at the lower of cost and **net realizable value**. When evidence exists that the net realizable value of inventory is lower than its cost, the difference shall be recognized as a loss in earnings in the period in which it occurs. That loss may be required, for example, due to damage, physical deterioration, obsolescence, changes in price levels, or other causes.

**> Inventory Measured Using LIFO or the Retail Inventory Method**

**330-10-35-1C** A departure from the cost basis of pricing ~~the~~ **{remove glossary link}inventory{remove glossary link}** measured using LIFO or the retail inventory method is required when the utility of the goods is no longer as great as their cost. Where there is evidence that the utility of goods, in their disposal in the ordinary course of business, will be less than cost, whether due to damage, physical deterioration, obsolescence, changes in price levels, or other causes, the difference shall be recognized as a loss of the current period. This is generally accomplished by stating such goods at a lower level commonly designated as **market**. **[Content amended as shown and moved from paragraph 330-10-35-1]**

**330-10-35-2** The cost basis of recording inventory ordinarily achieves the objective of a proper matching of costs and revenues. However, under certain circumstances cost may not be the amount properly chargeable against the revenues of future periods. A departure from cost is required in these circumstances because cost is satisfactory only if the utility of the goods has not diminished since their acquisition; a loss of utility shall be reflected as a charge against the revenues of the period in which it occurs. Thus, in accounting for inventories, a loss shall be recognized whenever the utility of goods is impaired by damage, deterioration, obsolescence, changes in price levels, or other causes. The measurement of such losses for inventory measured using LIFO or the retail inventory method shall be accomplished by applying the rule of pricing inventories at the lower of cost or market. This provides a practical means of measuring utility and thereby determining the amount of the loss to be recognized and accounted for in the current period.

**330-10-35-3** The rule of lower of cost or market is intended to provide a means of measuring the residual usefulness of an inventory expenditure. The term *market* is therefore to be interpreted as indicating utility on the inventory date and may be thought of in terms of the equivalent expenditure which would have to be made in the ordinary course at that date to procure corresponding utility.

**330-10-35-4** As a general guide, utility is indicated primarily by the current cost of replacement of the goods as they would be obtained by purchase or reproduction. In applying the rule, however, judgment must always be exercised and no loss shall be recognized unless the evidence indicates clearly that a loss has been sustained. There are therefore exceptions to such a standard. Replacement or reproduction prices would not be appropriate as a measure of utility when the estimated sales value, reduced by the costs of completion and disposal, is lower, in which case the realizable value so determined more appropriately measures utility.

**330-10-35-5** Furthermore, when the evidence indicates that cost will be recovered with an approximately normal profit upon sale in the ordinary course of business, no loss shall be recognized even though replacement or reproduction costs are lower. This might be true, for example, in the case of production under firm sales contracts at fixed prices, or when a reasonable volume of future orders is assured at stable selling prices.

**330-10-35-6** Paragraph superseded by Accounting Standards Update 2015-11. ~~If inventory has been the hedged item in a fair value hedge, the inventory's cost basis used in the lower of cost or market accounting shall reflect the effect of the adjustments of its carrying amount made pursuant to paragraph 815-25-35-1(b).~~ **[Content amended and moved to paragraph 330-10-35-7A]**

**330-10-35-7** Because of the many variations of circumstances encountered in inventory pricing, the definition of **market** is intended as a guide rather than a literal rule. It shall be applied realistically in light of the objectives expressed in this Subtopic and with due regard to the form, content, and composition of the inventory. For example, the retail inventory method, if adequate markdowns are currently taken, accomplishes the objectives described herein. It is also recognized that, if a business is expected to lose money for a sustained period, the inventory shall not be written down to offset a loss inherent in the subsequent operations.

**> Subsequent Measurement Guidance Applicable to All Inventory**

**330-10-35-7A** If inventory has been the hedged item in a fair value hedge, the inventory's cost basis for purposes of subsequent measurement ~~used in the lower of cost or market accounting~~ shall reflect the effect of the adjustments of its carrying amount made pursuant to paragraph 815-25-35-1(b). **[Content amended as shown and moved from paragraph 330-10-35-6]**

**330-10-35-8** Depending on the character and composition of the inventory, the guidance in paragraphs 330-10-35-1A through 35-7 that is applicable to the inventory being measured ~~the rule of lower of cost or market~~ may properly be applied either directly to each item or to the total of the inventory (or, in some cases, to the total of the components of each major category). The method shall be that which most clearly reflects periodic income.

**330-10-35-9** The purpose of reducing the carrying amount of inventory ~~to market~~ is to reflect fairly the income of the period. The most common practice is to apply the applicable subsequent measurement guidance ~~lower of cost or market rule~~ separately to each item of the inventory. However, if there is only one end-product category, the ~~category the cost utility of the total stock—the~~ application of the applicable subsequent measurement guidance to inventory in its ~~entirety—~~entirety may have the greatest significance for accounting purposes. Accordingly, the remeasurement ~~reduction~~ of individual items ~~to market~~ may not always lead to the most useful result if the ~~utility~~ market value (for inventory measured using LIFO or the retail inventory method) or net realizable value (for all other inventory) of the total inventory ~~to the business~~ is not below its cost. This might be the ~~case~~ case, for example, if selling prices are not affected by temporary or small fluctuations in current costs of purchase or manufacture.

**330-10-35-10** Similarly, where more than one major product or operational category exists, the application of the applicable subsequent measurement guidance ~~lower of cost or market rule~~ to the total of the items included in such major categories may result in the most useful determination of income. When no loss of income is expected to take place as a result of a reduction of cost prices of certain goods because others forming components of the same general categories of finished products have a market value (for inventory measured using LIFO or the retail inventory method) or net realizable value (for all other inventory) equally in excess of cost, such components need not be adjusted ~~to market~~ to the extent that they are in balanced quantities. Thus, in such cases, the guidance on subsequent measurement ~~rule of lower of cost or market,~~ may be applied directly to the totals of the entire inventory, rather than to the individual inventory items, if they enter into the same category of finished product and if they are in balanced quantities, provided the procedure is applied consistently from year to year.

**330-10-35-11** To the extent, however, that the stocks of particular materials or components are excessive in relation to others, the more widely recognized procedure of applying the guidance on subsequent measurement ~~lower of cost or market~~ to the individual items constituting the excess shall be followed. This would also apply in cases in which the items enter into the production of unrelated products or products having a material variation in the rate of turnover. Unless an effective method of classifying categories is practicable, the rule shall be applied to each item in the inventory.

4. Amend paragraph 330-10-50-2 and its related heading, with a link to transition paragraph 330-10-65-1, as follows:

## Disclosure

**> Losses from the Subsequent Measurement of Inventory~~Application of Lower of Cost or Market~~**

**330-10-50-2** ~~When substantial~~ Substantial and unusual losses that result from the subsequent measurement of **inventory** (see paragraphs 330-10-35-1A through 35-11) should be disclosed in the financial statements. ~~application of the rule of lower of cost or **market** it will frequently be desirable to disclose the amount of the loss in the income statement as a charge separately identified from the consumed **inventory** costs described as cost of goods sold.~~

5. Amend paragraph 330-10-55-2, with a link to transition paragraph 330-10-65-1, as follows:

## Implementation Guidance and Illustrations

**> Implementation Guidance**

**> > Market Decline in Interim Period**

**330-10-55-2** If near-term price recovery is uncertain, a decline in the **market** ~~price~~ value (for inventory measured using LIFO or the retail inventory method) or **net realizable value** (for all other inventory) of inventory below cost during an interim period shall be accounted for consistent with annual periods, except as described in paragraph 270-10-45-6.~~as follows. Paragraph 270-10-45-6 requires that the inventory be written down to the lower of cost or market unless either of the following conditions is met:~~

a. Subparagraph superseded by Accounting Standards Update 2015-11. ~~Substantial evidence exists that market prices will recover before the inventory is sold.~~
b. Subparagraph superseded by Accounting Standards Update 2015-11. ~~In the case of last-in, first-out (LIFO) inventory, substantial evidence exists that inventory amounts will be restored by year-end.~~

~~A write-down is generally required unless the decline is due to seasonal price fluctuations.~~

6. Add paragraph 330-10-65-1 and its related heading as follows:

**> Transition Related to Accounting Standards Update No. 2015-11, *Inventory (Topic 330): Simplifying the Measurement of Inventory***

**330-10-65-1** The following represents the transition and effective date information related to Accounting Standards Update No. 2015-11, *Inventory (Topic 330): Simplifying the Measurement of Inventory:*

a. For **public business entities**, the pending content that links to this paragraph shall be effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years.
b. For all other entities, the pending content that links to this paragraph shall be effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017.
c. An entity shall apply the pending content that links to this paragraph prospectively to the measurement of inventory after the date of adoption. If an entity has written down inventory measured using any method other than last-in, first-out (LIFO) or the retail inventory method below its cost before the adoption of the pending content that links to this paragraph, that reduced amount is considered the cost upon adoption.
d. Earlier application is permitted as of the beginning of an interim or annual reporting period.
e. An entity is required only to disclose the nature of and reason for the change in accounting principle in the first interim and annual period of adoption.

## Amendments to Subtopic 270-10

7. Amend paragraph 270-10-45-6, with a link to transition paragraph 330-10-65-1, as follows:

### Interim Reporting—Overall

### Other Presentation Matters

**270-10-45-6** Practices vary in determining costs of inventory. For example, cost of goods produced may be determined based on standard or actual cost, while cost of inventory may be determined on an average, first-in, first-out (FIFO), or last-in, first-out (LIFO) cost basis. While entities ~~shall~~ generally shall use the same inventory pricing methods and make provisions for writedowns ~~to market~~ at interim dates on the same basis as used at annual inventory dates, the following exceptions are appropriate at interim reporting dates:

a. Some entities use estimated gross profit rates to determine the cost of goods sold during interim periods or use other methods different from those used at annual inventory dates. These entities shall disclose the method used at the interim date and any significant adjustments that result from reconciliations with the annual physical inventory.
b. Entities that use the LIFO method may encounter a liquidation of base period inventories at an interim date that is expected to be replaced by the end of the annual period. In ~~such~~ those cases the inventory at the interim reporting date shall not give effect to the LIFO liquidation, and cost of sales for the interim reporting period shall include the expected cost of replacement of the liquidated LIFO base.
c. Inventory losses from ~~market declines~~ the application of the guidance on subsequent measurement in Subtopic 330-10 shall not be deferred beyond the interim period in which the decline occurs. Recoveries of such losses on the same inventory in later interim periods of the same fiscal year through market ~~price~~ value recoveries (for inventory measured using LIFO or the retail inventory method) or **net realizable value** recoveries (for all other inventory) shall be recognized as gains in the later interim period. Such gains shall not exceed previously recognized losses. Some ~~market~~ declines in the market value (for inventory measured using LIFO or the retail inventory method) or net realizable value (for all other inventory) of inventory at interim dates, however, can reasonably be expected to be restored in the fiscal year. Such temporary ~~market~~ declines need not be recognized at the interim date since no loss is expected to be incurred in the fiscal year.
d. Entities that use standard cost accounting systems for determining inventory and product costs should generally follow the same procedures in reporting purchase price, wage rate, usage, or efficiency variances from standard cost at the end of an interim period as followed at the end of a fiscal year. Purchase price variances or volume or capacity cost variances that are planned and expected to be absorbed by the end of the annual period, should ordinarily be deferred at interim reporting dates. The effect of unplanned or unanticipated purchase price or volume variances, however, shall be reported at the end of an interim period following the same procedures used at the end of a fiscal year.

# Amendments to Subtopic 275-10

8. Amend paragraph 275-10-05-7, with a link to transition paragraph 330-10-65-1, as follows:

## Risks and Uncertainties—Overall

## Overview and Background

**275-10-05-7** Estimates inherent in the current financial reporting process inevitably involve assumptions about future events. For example, accruing income for the current period under a long-term contract requires an estimate of the total profit to be earned on the contract. For another example, carrying inventories measured using first-in, first-out (FIFO) at the lower of cost and **net realizable value** ~~or market~~ is based on an assumption that there will be sufficient demand for that product in the future to be able to sell the quantity on hand without incurring losses on the sales or, if net realizable value ~~market~~ is used, that it can be estimated. Making reliable estimates for those ~~such~~ matters is often difficult even in periods of economic stability; it is more so in periods of economic volatility. Although many users of financial statements are aware of that aspect of financial reporting, others often assume an unwarranted degree of reliability in financial statements. The disclosure required by this Subtopic should help dispel any of those ~~such~~ erroneous assumptions.

**Transition Date:** *(P) December 15, 2016; (N) December 15, 2017* | **Transition Guidance: 606-10-65-1**

**275-10-05-7** Estimates inherent in the current financial reporting process inevitably involve assumptions about future events. For example, estimating and constraining estimates of variable consideration to be included in the **transaction price** for a **contract** with a **customer** in accordance with paragraphs 606-10-32-5 through 32-14 and measuring progress toward complete satisfaction of a **performance obligation** in accordance with paragraphs 606-10-25-31 through 25-37. For another example, carrying inventories measured using first-in, first-out (FIFO) at the lower of cost and **net realizable value** ~~or market~~ is based on an assumption that there will be sufficient demand for that product in the future to be able to sell the quantity on hand without incurring losses on the sales or, if net realizable value ~~market~~ is used, that it can be estimated. Making reliable estimates for those ~~such~~ matters is often difficult even in periods of economic stability; it is more so in periods of economic volatility. Although many users of financial statements are aware of that aspect of financial reporting, others often assume an unwarranted degree of reliability in financial statements. The disclosure required by this Subtopic should help dispel any of those ~~such~~ erroneous assumptions.

# Amendments to Subtopic 360-10

9. Amend paragraph 360-10-55-21, with a link to transition paragraph 330-10-65-1, as follows:

## Property, Plant, and Equipment—Overall

## Implementation Guidance and Illustrations

### Impairment or Disposal of Long-Lived Assets

#### > Illustrations

#### > > Example 1: Allocation of Impairment Loss

**360-10-55-21** An entity owns a manufacturing facility that together with other assets is tested for recoverability as a group. In addition to long-lived assets (Assets A–D), the asset group includes inventory measured using first-in, first-out (FIFO), which is reported at the lower of cost and **net realizable value** ~~or market~~ in accordance with Topic 330, and other current assets and liabilities that are not covered by this Subtopic. The $2.75 million aggregate carrying amount of the asset group is not recoverable and exceeds its fair value by $600,000. In accordance with paragraph 360-10-35-28, the impairment loss of $600,000 would be allocated as shown below to the long-lived assets of the group.

| Asset Group | Carrying Amount (in $ 000s) | Pro Rata Allocation Factor | Allocation of Impairment (Loss) (in $ 000s) | Adjusted Carrying Amount (in $ 000s) |
|---|---|---|---|---|
| Current assets | $ 400 | - | $ - | $ 400 |
| Liabilities | (150) | - | - | (150) |
| Long-lived assets: | | | | |
| Asset A | 590 | 24% | (144) | 446 |
| Asset B | 780 | 31 | (186) | 594 |
| Asset C | 950 | 38 | (228) | 722 |
| Asset D | 180 | 7 | (42) | 138 |
| Subtotal—long-lived assets | 2,500 | 100 | (600) | 1,900 |
| Total | $ 2,750 | 100% | $ (600) | $ 2,150 |

# Amendments to Subtopic 705-10

10. Amend paragraph 705-10-25-2, with a link to transition paragraph 330-10-65-1, as follows:

## Cost of Sales and Services—Overall

## Recognition

**> Inventory**

**705-10-25-2** See paragraphs ~~330-10-35-1~~ 330-10-35-1A through 35-11 for adjustments affecting cost of sales and services resulting from ~~remeasuring~~ the subsequent measurement of inventory ~~to the lower of cost or market~~.

# Amendments to Subtopic 830-10

11. Amend paragraphs 830-10-55-8 through 55-9, 830-10-55-15, and 830-10-55-18 through 55-19 and their related headings and supersede paragraphs 830-10-55-17 and 830-10-55-20 through 55-22 and their related headings, with a link to transition paragraph 330-10-65-1, as follows:

## Foreign Currency Matters—Overall

## Implementation Guidance and Illustrations

**> Implementation Guidance**

**> > Remeasuring Inventory Not Recorded in the Functional Currency**

**830-10-55-8** The ~~rule of cost or market, whichever is lower (as described in Subtopic 330-10),~~ guidance on the subsequent measurement of inventory in Subtopic 330-10 requires special application when the books of record are not kept in the functional currency. Inventories carried at cost in the books of record in another currency should be first remeasured to cost in the functional currency using historical exchange rates. Then, historical cost in the functional currency should be evaluated for impairment under the subsequent measurement guidance using ~~is compared with market as stated in~~ the functional currency. Application of the subsequent measurement guidance ~~rule~~ in functional currency may require a write-down ~~write-downs to market~~ in the functional currency statements even though no write-down has been made in the books of record maintained in another currency. Likewise, a write-down in the books of record may need to be reversed if the application of the subsequent measurement guidance in the functional currency does not require a write-down ~~market exceeds historical cost as stated in the functional currency~~. If inventory has been written down ~~to market~~ in the functional currency statements, that functional currency amount shall continue to be the carrying amount in the functional currency financial statements until the inventory is sold or a further write-down is necessary. An asset other than inventory may sometimes be written down from historical cost. Although different measurement guidance may be used to determine that write-down, ~~that write-down~~

~~is not under the rule of cost or market, whichever is lower,~~ the approach described in this paragraph might be appropriate. That is, a write-down may be required in the functional currency statements even though not required in the books of record, and a write-down in the books of record may need to be reversed before remeasurement to prevent the remeasured amount from exceeding functional currency historical cost.

**830-10-55-9** Literal application of the subsequent measurement guidance in Subtopic 330-10 ~~rule of cost or market, whichever is lower,~~ may require an inventory write-down in functional currency financial statements for locally acquired inventory if the value of the currency in which the books of record are maintained has declined in relation to the functional currency between the date the inventory was acquired and the date of the balance sheet. ~~Such~~ However, such a write-down may not be necessary, ~~however,~~ for example, for inventory measured using the first-in, first out (FIFO) methodology, if the ~~replacement costs or selling prices~~ **net realizable value** expressed in the currency in which the books of record are maintained ~~have~~ has increased sufficiently so that ~~market~~ net realizable value exceeds historical cost as measured in functional currency. Cases A and B in Example 2 (see paragraphs 830-10-55-15 through 55-16 and 830-10-55-18 through 55-19~~55-22~~) illustrate this situation. This paragraph is not intended to preclude recognition of gains in a later interim period to the extent of inventory losses recognized from ~~market~~ net realizable value declines in earlier interim periods if losses on the same inventory are recovered in the same year, as provided by paragraph 270-10-45-6(c). An inventory write-down also may be required for imported inventory.

**> Illustrations**

**> > Example 2: Remeasuring Inventory Not Recorded in the Functional Currency**

**830-10-55-15** The following Cases illustrate this Section's implementation guidance on remeasurement of inventory that is measured using first-in, first-out (FIFO) and is not recorded in the functional currency (see paragraphs 830-10-45-18 and 830-10-55-8 through 55-9):

a. Historical cost in functional currency exceeds net realizable value in functional currency (Case A)~~Market based on current replacement cost (Case A)~~
   1. Subparagraph superseded by Accounting Standards Update 2015-11.~~Historical cost exceeds market based on current replacement cost (Case A1).~~
   2. Subparagraph superseded by Accounting Standards Update 2015-11.~~Market based on current replacement cost exceeds historical cost (Case A2).~~

b. Net realizable value in functional currency exceeds historical cost in functional currency (Case B)~~Market based on net realizable value reduced by normal profit margin (Case B)~~ .

**830-10-55-16** Cases A and B share all of the following assumptions:

a. BR is the currency in which the books of record are maintained.
b. FC is the functional currency.
c. When the rate is BR 1 = FC 2.40, a foreign subsidiary of a U.S. entity purchases a unit of inventory at a cost of BR 500 (measured in functional currency, FC 1,200).
d. At the foreign subsidiary's balance sheet date, the current rate is BR 1 = FC 2.00.

**~~> > > Case A: Market Based on Current Replacement Cost~~**

**830-10-55-17** Paragraph superseded by Accounting Standards Update 2015-11.~~Cases A1 and A2 share both of the following additional assumptions:~~

~~a. Net realizable value is BR 630 (measured in functional currency, FC 1,260).~~
~~b. Net realizable value reduced by an allowance for an approximately normal profit margin is BR 550 (measured in functional currency, FC 1,100).~~

**~~> > > > Case A1~~> > > Case A: Historical Cost in Functional Currency Exceeds Net Realizable Value in Functional Currency ~~Market Based on Current Replacement Cost~~**

**830-10-55-18** Assume the ~~current replacement cost~~ net realizable value of the unit of inventory is BR 560 (measured in functional currency, FC 1,120). Because ~~current replacement cost~~ net realizable value as measured in the functional currency (FC 1,120) is less than historical cost as measured in the functional currency (FC 1,200), an inventory write-down of FC 80 is required in the functional currency financial statements.

**~~> > > > Case A2~~> > > Case B: ~~Market Based on Current Replacement Cost~~ Net Realizable Value in Functional Currency Exceeds Historical Cost in Functional Currency**

**830-10-55-19** Assume the ~~current replacement cost~~ net realizable value at the foreign subsidiary's balance sheet date is ~~of~~ BR 620. Because ~~market~~ net realizable value as measured in the functional currency (BR 620 x FC 2.00 = FC 1,240) exceeds historical cost as measured in the functional currency (BR 500 x FC 2.40 = FC 1,200), an inventory write-down is not required in the functional currency financial statements.

**~~> > > Case B: Market Based on Net Realizable Value Reduced by Normal Profit Margin~~**

**830-10-55-20** Paragraph superseded by Accounting Standards Update 2015-11.~~Assume the current replacement cost of the unit of inventory is BR 560 and that selling prices in terms of the currency in which the books of record are maintained have increased so that both of the following conditions exist:~~

a. ~~Net realizable value is BR 720.~~
b. ~~Net realizable value reduced by an allowance for an approximately normal profit margin is BR640.~~

**830-10-55-21** Paragraph superseded by Accounting Standards Update 2015-11.~~In that situation, because replacement cost measured in functional currency (BR 560 x FC 2.00 = FC 1,120) is less than net realizable value reduced by an allowance for an approximately normal profit margin measured in functional currency (BR 640 x FC 2.00 = FC 1,280), market is FC 1,280.~~

**830-10-55-22** Paragraph superseded by Accounting Standards Update 2015-11.~~Because market as measured in the functional currency (FC 1,280) exceeds historical cost as measured in the functional currency (BR 500 x FC 2.40 = FC 1,200), an inventory write-down is not required in the functional currency financial statements.~~

# Amendments to Subtopic 905-330

12. Amend paragraphs 905-330-35-1 through 35-3 and 905-330-35-5, with a link to transition paragraph 330-10-65-1, as follows:

## Agriculture—Inventory

## Subsequent Measurement

### General

#### > Growing Crops

**905-330-35-1** Costs of growing **crops** shall be accumulated until the time of harvest. Growing crops shall be measured using the guidance in Subtopic 330-10 ~~reported at the lower of cost or market~~.

#### > Developing Animals

**905-330-35-2** Developing animals to be held for sale shall be measured using the guidance in Subtopic 330-10 ~~valued at the lower of cost or market~~.

#### > Animals Available and Held for Sale

**905-330-35-3** Animals held for sale shall be valued at either of the following:

a. The amount determined using the measurement guidance in Subtopic 330-10 ~~lower of cost or market~~
b. **Net realizable value**, ~~At sales price less estimated costs of disposal,~~ if all the following conditions exist:

1. The product has a reliable, readily determinable, and realizable market price.
2. The product has relatively insignificant and predictable costs of disposal.
3. The product is available for immediate delivery.

~~Inventories of harvested crops and **livestock** held for sale and commonly referred to as valued at market are actually valued at **net realizable value**.~~

**> Harvested Crops**

**905-330-35-4** Inventories of harvested crops shall be valued using the same criteria as animals held for sale in the preceding paragraph.

## Cooperatives

**905-330-35-5** The inventories for a **pooling cooperative** shall be accounted for at either of the following:

a. The amount determined using the measurement guidance in Subtopic 330-10 ~~the lower of cost or market or at~~
b. **Net ~~net~~ realizable value**.

When **assigned amounts** are used, they should approximate estimated ~~market~~ net realizable value of unprocessed products delivered by patrons. See Example 1 (paragraph 905-330-55-1) for an illustration.

13. Amend paragraphs 905-330-55-2 through 55-4, with a link to transition paragraph 330-10-65-1, as follows:

# Implementation Guidance and Illustrations

## Cooperatives

**> Illustrations**

**> > Example 1: Accounting by Pooling Cooperatives for Products Received from Patrons**

**905-330-55-1** This Example illustrates the guidance in paragraphs 905-330-25-6 through 25-7 and 905-330-35-5.

**905-330-55-2** ~~This Example~~ In this Example, inventory is measured using first-in, first-out (FIFO) and ~~has~~ the following assumptions apply:

| | |
|---|---|
| Sales | $ 129,630 |
| Beginning inventory | |
| Net realizable value | 31,128 |
| Lower of cost ~~or market~~and net realizable value | 28,380 |
| Assigned value of ~~patron's~~patrons' raw product received | 56,500 |
| Ending inventory | |
| Net realizable value | 35,596 |
| Lower of cost ~~or market~~and net realizable value | 32,360 |
| Income taxes | 1,250 |
| Other costs and expenses | 56,580 |
| Amounts paid to ~~patron's~~patrons, retains, and nonpatronage earnings | 74,430 |
| Amounts due patrons at beginning of year | |
| Lower of cost ~~or market~~and net realizable value method | 8,910 |
| Net realizable value method | 11,748 |

**905-330-55-3** The following tables illustrate the statement of net earnings prepared under each of two possible methods of accounting for inventories (columns A and B), the statement of net proceeds prepared under the **net realizable value** method (column C), and the respective statements of amounts due patrons, if such latter statement is included in the financial statements. Column A demonstrates the lower of cost and net realizable value ~~or market~~ method with patrons' raw product being charged to cost of production at **assigned amounts**. Column B demonstrates the net realizable value method with patrons' raw product being charged to cost of production at assigned amounts. Column C demonstrates the net realizable value method when no amounts are assigned to patrons' raw product; therefore, there is no charge to cost of production for patrons' raw product.

| | Inventories Valued At | | | | | |
|---|---|---|---|---|---|---|
| | Lower of Cost ~~or Market~~and Net Realizable Value (Column A) | | Net Realizable Value (Column B) | | Net Realizable Value (Column C) | |
| Sales | $ | 129,630 | $ | 129,630 | $ | 129,630 |
| Costs and expenses (I) | | 109,100 | | 108,702 | | 52,202 |
| Earnings before income taxes | | 20,530 | | 20,928 | | - |
| Proceeds before income taxes | | - | | - | | 77,428 |
| Income taxes | | 1,250 | | 1,250 | | 1,250 |
| Net earnings | $ | 19,280 | $ | 19,678 | | |
| Net proceeds | | | | | $ | 76,178 |
| I. Beginning inventory | $ | 28,380 | $ | 31,218 | $ | 31,218 |
| Assigned value of patrons' raw product received | | 56,500 | | 56,500 | | - |
| Ending inventory | | (32,360) | | (35,596) | | (35,596) |
| Other costs and expenses | | 56,580 | | 56,580 | | 56,580 |
| | $ | 109,100 | $ | 108,702 | $ | 52,202 |

**Statement of Amounts Due Patrons**

| | Inventories Valued At | | | | | |
|---|---|---|---|---|---|---|
| | Lower of Cost ~~or Market~~and Net Realizable Value (Column A) | | Net Realizable Value (Column B) | | Net Realizable Value (Column C) | |
| Amounts due patrons at beginning of year | $ | 8,910 | $ | 11,748 | $ | 11,748 |
| Net earnings | | 19,280 | | 19,678 | | - |
| Net proceeds | | - | | - | | 76,178 |
| Assigned value of patrons' raw product received | | 56,500 | | 56,500 | | - |
| | | 84,690 | | 87,926 | | 87,926 |
| Less amounts paid to patrons, retains, and nonpatronage earnings | | 74,430 | | 74,430 | | 74,430 |
| Amounts due patrons at end of year | $ | 10,260 | $ | 13,496 | $ | 13,496 |

**905-330-55-4** Under the two inventory methods presented, the difference in amounts due patrons at the end of the year results from the difference in the ending inventory valuations, illustrated as follows.

| | |
|---|---|
| Inventories of finished goods and goods in process at: | |
| Net realizable value | $ 35,596 |
| Lower of cost ~~or market~~and net realizable value | (32,360) |
| | 3,326 |
| Amounts due patrons at end of year on lower of cost ~~or market~~and net realizable value basis | 10,260 |
| Amounts due patrons at end of year on net realizable value basis | $ 13,496 |

# Amendments to Subtopic 905-360

14. Amend paragraphs 905-360-30-1 through 30-2, with a link to transition paragraph 330-10-65-1, as follows:

## Agriculture—Property, Plant, and Equipment

## Initial Measurement

### > Developing Animals

**905-360-30-1** All direct and indirect costs of developing animals shall be accumulated until the animals reach maturity and are transferred to a productive function. All direct and indirect development costs of animals raised for sale shall be accumulated, and the animals shall be accounted for in accordance with the measurement guidance in Subtopic 330-10 ~~at the lower of cost or market~~ until they are available for sale.

### > Animals Available and Held for Sale

**905-360-30-2 Agricultural producers** shall report animals available and held for sale either:

a. In accordance with the measurement guidance in Subtopic 330-10 ~~At the lower of cost or market~~
b. In accordance with established industry practice at **net realizable value** ~~sales price, less estimated costs of disposal~~, if all of the following conditions exist:
   1. There are reliable, readily determinable, and realizable market prices for the animals.
   2. The costs of disposal are relatively insignificant and predictable.
   3. The animals are available for immediate delivery.

# Amendments to Subtopic 905-405

15. Amend paragraph 905-405-25-1, with a link to transition paragraph 330-10-65-1, as follows:

## Agriculture—Liabilities

## Recognition

### Cooperatives

#### > Pooling Cooperatives

**905-405-25-1** If the boards of directors of agricultural marketing cooperatives operating on a pooling basis with no obligation to pay **patrons** fixed prices (pooling cooperatives) assign amounts that approximate estimated ~~market~~ **net realizable value** to unprocessed products received from patrons, the **assigned amounts** shall be credited to amounts due patrons. When assigned amounts are used, they should approximate estimated ~~market~~ net realizable value of unprocessed products delivered by patrons (an example of inventories at lower of cost ~~or market~~ and net realizable value is provided in Example 1 (see paragraph 905-330-55-1)).

16. Amend paragraph 250-10-00-1, by adding the following item to the table, as follows:

**250-10-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| **Direct Effects of a Change in Accounting Principle** | Amended | 2015-11 | 07/22/2015 |

17. Amend paragraph 270-10-00-1, by adding the following items to the table, as follows:

**270-10-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| **Net Realizable Value** | Added | 2015-11 | 07/22/2015 |
| 270-10-45-6 | Amended | 2015-11 | 07/22/2015 |

18. Amend paragraph 275-10-00-1, by adding the following items to the table, as follows:

**275-10-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| **Net Realizable Value** | Added | 2015-11 | 07/22/2015 |
| 275-10-05-7 | Amended | 2015-11 | 07/22/2015 |

19. Amend paragraph 330-10-00-1, by adding the following items to the table, as follows:

**330-10-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| **Direct Effects of a Change in Accounting Principle** | Amended | 2015-11 | 07/22/2015 |
| 330-10-35-1 | Superseded | 2015-11 | 07/22/2015 |
| 330-10-35-1A through 35-1C | Added | 2015-11 | 07/22/2015 |
| 330-10-35-2 | Amended | 2015-11 | 07/22/2015 |
| 330-10-35-6 | Superseded | 2015-11 | 07/22/2015 |
| 330-10-35-7A | Added | 2015-11 | 07/22/2015 |
| 330-10-35-8 through 35-11 | Amended | 2015-11 | 07/22/2015 |
| 330-10-50-2 | Amended | 2015-11 | 07/22/2015 |
| 330-10-55-2 | Amended | 2015-11 | 07/22/2015 |
| 330-10-65-1 | Added | 2015-11 | 07/22/2015 |

20. Amend paragraph 360-10-00-1, by adding the following items to the table, as follows:

**360-10-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| **Net Realizable Value** | Added | 2015-11 | 07/22/2015 |
| 360-10-55-21 | Amended | 2015-11 | 07/22/2015 |

21. Amend paragraph 705-10-00-1, by adding the following item to the table, as follows:

**705-10-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| 705-10-25-2 | Amended | 2015-11 | 07/22/2015 |

22. Amend paragraph 830-10-00-1, by adding the following items to the table, as follows:

**830-10-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| **Net Realizable Value** | Added | 2015-11 | 07/22/2015 |
| 830-10-55-8 | Amended | 2015-11 | 07/22/2015 |
| 830-10-55-9 | Amended | 2015-11 | 07/22/2015 |
| 830-10-55-15 | Amended | 2015-11 | 07/22/2015 |
| 830-10-55-17 | Superseded | 2015-11 | 07/22/2015 |
| 830-10-55-18 | Amended | 2015-11 | 07/22/2015 |
| 830-10-55-19 | Amended | 2015-11 | 07/22/2015 |
| 830-10-55-20 through 55-22 | Superseded | 2015-11 | 07/22/2015 |

23. Amend paragraph 905-330-00-1, by adding the following items to the table, as follows:

**905-330-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| 905-330-35-1 through 35-3 | Amended | 2015-11 | 07/22/2015 |
| 905-330-35-5 | Amended | 2015-11 | 07/22/2015 |
| 905-330-55-2 through 55-4 | Amended | 2015-11 | 07/22/2015 |

24. Amend paragraph 905-360-00-1, by adding the following items to the table, as follows:

**905-360-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| **Net Realizable Value** | Added | 2015-11 | 07/22/2015 |
| 905-360-30-1 | Amended | 2015-11 | 07/22/2015 |
| 905-360-30-2 | Amended | 2015-11 | 07/22/2015 |

25. Amend paragraph 905-405-00-1, by adding the following items to the table, as follows:

**905-405-00-1** The following table identifies the changes made to this Subtopic.

| Paragraph | Action | Accounting Standards Update | Date |
|---|---|---|---|
| **Net Realizable Value** | Added | 2015-11 | 07/22/2015 |
| 905-405-25-1 | Amended | 2015-11 | 07/22/2015 |

*The amendments in this Update were adopted by the affirmative vote of five members of the Financial Accounting Standards Board. Messrs. Linsmeier and Siegel dissented.*

Messrs. Linsmeier and Siegel dissent from the issuance of this Accounting Standards Update because they believe that while the Board's decision reduces *costs* for *some* preparers, it introduces additional complexity for users, preparers, auditors, and students of accounting when compared with the current reporting model. Specifically, they believe that retaining the original inventory impairment guidance only for entities using the last-in, first-out method (LIFO) and the retail inventory method will increase complexity rather than simplify GAAP, which contradicts the stated objective of a project that was added to the agenda as part of the Board's Simplification Initiative.

Messrs. Linsmeier and Siegel believe that introducing two different impairment models for inventory will cause users of financial statements to be faced with an additional layer of noncomparability in reported numbers that will further hinder comparisons of one entity to another. While paragraph BC9 indicates that the Board believes that current inventory guidance yields noncomparable results when reporting entities avail themselves of different inventory measurement approaches, Messrs. Linsmeier and Siegel judge this Update to further exacerbate this noncomparability rather than to maintain or reduce it. While it is true that in current guidance there are different methods for measuring inventory at cost, there is no difference in the guidance for writing down inventory to market. This Update introduces a difference in the approach to measuring the impaired value of inventory that depends on the method used to measure the inventory at cost, thereby introducing further variations in the subsequent accounting for inventory at cost or market and making it difficult for Messrs. Linsmeier and Siegel to see the proposed change as simplifying the analyses users must undertake to compare outcomes of different entities.

Messrs. Linsmeier and Siegel also believe that preparers and auditors will experience more complexity by having to consider and potentially implement or audit two different models for the subsequent measurement of impaired inventory. They believe that those complexities will be greatest when entities elect to use LIFO or the retail inventory method for one class of inventory or type of product and another inventory method to measure the cost of inventory for other classes of inventory or product types. In those cases, the impaired value of inventory sometimes will be consistently measured at net realizable value for a subset of inventory, while for the other subset of inventory it will be measured by comparing net realizable value to replacement cost and net realizable value minus an approximately normal profit margin and measuring the impaired value at the middle of those three amounts.

Messrs. Linsmeier and Siegel further believe that this Update will not result in any simplification for students preparing to be accounting professionals. They believe that while there already are several inventory costing methods for complying with current GAAP, the bifurcation of the impairment model into two different approaches will reduce the understandability of the overall accounting for inventory and make learning more difficult, which they believe adds complexity and contradicts the objective of this Simplification project.

Finally, Messrs. Linsmeier and Siegel believe that each of these problems may further highlight the diversity in current practice in how entities using LIFO or the retail inventory method consider net realizable value, replacement cost, and net realizable value less an approximately normal margin when measuring inventory at the lower of cost or market (LOCOM). Messrs. Linsmeier and Siegel believe that continuing to include within current GAAP consideration of each of these three amounts when determining market for entities using LIFO or the retail inventory method could introduce additional challenges in complying with current GAAP for those entities that measure inventory at the lower of cost or market, especially to the extent that those entities do not currently explicitly consider all three amounts in determining market.

In summary, Messrs. Linsmeier and Siegel believe that this Update does not represent a simplification. They conclude that while the amendments provide a cost reduction for *some* preparers, the Update introduces additional complexity for users, preparers, auditors, and students for all the reasons outlined above. Messrs. Linsmeier and Siegel believe that the only approach that would represent a simplification for those using, preparing, auditing, and studying accounting information would be to change the measurement of impaired inventory to net realizable value for each different method of measuring inventory at cost. This approach also would have the added benefit of converging with IFRS, which would simplify accounting globally. Given that this approach was found unacceptable by the Board because it introduces one-time costs for entities using LIFO or the retail inventory method, Messrs. Linsmeier and Siegel prefer that the Board do nothing rather than add complexity to the accounting in a project undertaken by the Board under its Simplification Initiative.

*Members of the Financial Accounting Standards Board:*

Russell G. Golden, *Chairman*
James L. Kroeker, *Vice Chairman*
Daryl E. Buck
Thomas J. Linsmeier
R. Harold Schroeder
Marc A. Siegel
Lawrence W. Smith

# Background Information and Basis for Conclusions

## Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

BC2. The Board is issuing this Update as part of its Simplification Initiative. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of GAAP for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements.

## Scope and Measurement

BC3. To simplify the measurement of inventory, the Board issued the July 2014 proposed Accounting Standards Update, *Inventory (Topic 330): Simplifying the Measurement of Inventory,* which proposed that inventory should be measured at the lower of cost and net realizable value. *Net realizable value* is defined in the Master Glossary as the "estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation." The amendments in the proposed Update would have eliminated the guidance in Topic 330 that requires a reporting entity measuring inventory at the lower of cost or market to consider the replacement cost of inventory and the net realizable value of inventory less an approximately normal profit margin along with net realizable value in determining the market value.

BC4. The proposed Update was open for public comment for 75 days, and the Board received 31 comment letters. A substantial majority of respondents to the proposed Update expressed support for the proposed amendments, citing that the amendments would (a) reduce cost and complexity, (b) provide users of financial statements with more comparable information, and (c) increase convergence of GAAP and IFRS. IAS 2, *Inventories*, requires inventory to be measured at the lower of cost and net realizable value. The term *net realisable value* is defined in IAS 2 as "the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale," which is similar to the Codification Master Glossary definition.

BC5. However, some respondents indicated that for entities that measure inventory using LIFO or the retail inventory method, the proposed amendments would result in potentially significant costs, particularly upon transition, and would not simplify their subsequent measurement of inventory. This view also was expressed by entities during outreach performed after the comment letter process.

BC6. Under some approaches to applying the retail inventory method, the cost of inventory is estimated by multiplying the retail price of inventory by a margin that excludes the effect of permanent markdowns, which is similar to valuing inventory using net realizable value less an approximately normal profit margin (commonly referred to as the “floor” in practice). The floor was one of the measures that would have been eliminated by the proposed Update. Thus, some stakeholders were concerned that this approach to applying the retail inventory method no longer would be permitted. Those stakeholders indicated that requiring permanent markdowns to be included in the margin used to estimate the cost of inventory would result in costly and complex changes to their processes and inventory systems.

BC7. Some entities that apply LIFO and previously recognized lower of cost or market adjustments (which in practice are accounted for as an allowance by those entities) indicated that the proposed amendments could result in significant increases in their inventory balances upon transition unless the Board clarified that any previously recognized write-downs of inventory should be part of the cost basis upon transition. However, even if the Board decided to make that clarification, some entities indicated that it would be challenging to allocate those write-downs to each LIFO layer. Other entities said that replacement cost is a relevant measurement of impairment when LIFO is used. Still other entities indicated that even if no previous write-downs have been recognized, the benefits of the proposed amendments to U.S. Securities and Exchange Commission (SEC) registrants that measure inventory using LIFO would be limited because of the SEC requirement to disclose the replacement cost of LIFO inventory. Those stakeholders also noted that private companies often provide a similar disclosure.

BC8. In response to certain of the stakeholders’ concerns (principally concerns about whether the overall benefits of the change justify potentially significant implementation costs for certain entities), the Board decided to limit the scope of the proposed amendments to exclude inventory measured using LIFO or the retail inventory method. That is, the subsequent measurement guidance is unchanged for inventory measured using LIFO or the retail inventory method. All other inventory will be measured at the lower of cost and net realizable value.

BC9. The Board did not want entities that measure inventory using LIFO or the retail inventory method to incur potentially significant transition costs because the amendments may not result in significantly more useful information for users of financial statements. The amendments also might not simplify the accounting for those entities because of the inherent complexities involved in estimating cost under LIFO and the retail inventory method and the related complexities involved in estimating impairment. In addition, the Board noted that inventory is not comparable under existing GAAP across entities that use different inventory methods; therefore, the Board concluded that making subsequent measurement consistent across all methods would not improve comparability meaningfully. However, the Board also did not want to forgo an opportunity to reduce costs and improve comparability among the large group of stakeholders that would be within the scope of the amendments because of the concerns of a small subset of comment letter respondents. The Board noted that the simplification would apply to a substantial majority of entities with inventory.

## Disclosure

BC10. The Board considered whether to change disclosure requirements about the subsequent measurement of inventory. The Board noted that Topic 330 requires disclosures about the basis for stating inventories, losses from the application of lower of cost or market (amended in this Update to refer to losses from the subsequent measurement of inventory), goods stated above cost, stating inventories at sales prices, losses on firm purchase commitments, and significant estimates applicable to inventory. In addition, there are disclosures about estimates in Topic 275, Risks and Uncertainties. Instead of amending the disclosure requirements within this project, the Board decided to consider the adequacy of disclosures in Topic 330 more broadly as part of the project on the disclosure framework.

## Other Codification Amendments

BC11. Some of the other guidance in Topic 330 is amended in this Update to more clearly articulate the requirements for the measurement and disclosure of inventory. However, the Board does not intend for those clarifications to result in any change in practice. Other than the change in the subsequent measurement guidance from the lower of cost or market to the lower of cost and net realizable value for inventory within the scope of this Update, the Board has made no other substantive changes to the guidance on measurement of inventory in this Update.

## Effective Date and Transition

BC12. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. For all other entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017. Earlier application is permitted by all entities as of the beginning of an interim or annual reporting period. The Board delayed the proposed effective date by one year as a result of additional research and outreach performed by the staff, which delayed the issuance of this Update.

BC13. Additionally, the Board decided to delay the effective date for interim reporting periods for entities other than public business entities because it recognizes that those entities often do not become aware of changes in financial reporting requirements until fiscal year-end. This is consistent with the *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies* (the Framework), which states that private companies generally should not be required to adopt amendments during an interim period within the initial fiscal year of adoption. Because earlier application is allowed, entities other than public business entities will still have the ability to benefit from the amendments in this Update at an earlier date, if desired. The Framework also states that, generally, the amendments in an Update should be effective for private companies one year after the first annual period for which public entities are required to adopt them. However, respondents indicated that no delay was necessary for private companies; therefore, the Board decided to align the annual period of adoption for all entities.

BC14. The Board decided that an entity should apply the amendments in this Update prospectively to the measurement of inventory after the date of adoption. If an entity has written down inventory measured using any method other than LIFO or the retail inventory method below its cost before the adoption of the amendments in this Update, that reduced amount is considered the cost upon adoption.

BC15. The Board concluded that the costs of requiring or permitting retrospective application of the guidance would not justify the benefits. Additionally, retrospective application might require the use of hindsight, which would reduce some of the benefits of restating prior periods. Furthermore, retrospective application may not result in a significant change to the previous measurement of inventory for some entities.

BC16. The Board decided that the only disclosures required at transition should be the nature of and reason for the change in accounting principle. The Board concluded that the costs of a quantitative disclosure about the change from the lower of cost or market to the lower of cost and net realizable value would not justify the benefits because a reporting entity would be required in the year of adoption to measure inventory using both existing requirements and the amendments in this Update, and because the change would not be significant for some entities.

## Benefits and Costs

BC17. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC18. The amendments in this Update will reduce the cost of measuring inventory within this Update's scope because the current guidance on inventory measurement involves estimating replacement cost, net realizable value, and net realizable value less an approximately normal profit margin; in contrast, the amendments in this Update require only an estimate of net realizable value. Furthermore, for inventory within the scope of this Update, the amendments more closely align the measurement of inventory in GAAP with the measurement of inventory in IFRS.

BC19. The amendments in this Update should not increase cost and complexity for any entity because estimating net realizable value is necessary to apply the current guidance, and inventory measured using LIFO or the retail inventory method is excluded from the scope of this Update partially because of concerns about the cost of application. The Board specifically considered whether limiting the scope of this Update would add some measure of complexity to the Codification. The Board observed that the majority of entities with inventory use costing methods that are included in this Update's scope and that the benefits of this Update to those entities justify the costs associated with some measure of increased complexity in the Codification.

BC20. The Board acknowledges that this Update may appear to decrease comparability by requiring different subsequent measurement models for inventory measured using different methods. However, the Board observed that inventory balances based on different costing methods are not comparable under current GAAP and, as a result, the Board believes that an incremental difference in subsequent measurement guidance will not meaningfully affect comparability between inventory reported using LIFO or the retail inventory method and all other inventory.

BC21. The amendments in this Update will increase the consistency of the measurement of inventory within its scope because, at present, the application of the subsequent measurement guidance can result in three different measures of market. The amendments in this Update are expected to increase comparability for the majority of entities because most entities measure inventory using methods other than LIFO or the retail inventory method.

# Amendments to the XBRL Taxonomy

The amendments to the *FASB Accounting Standards Codification*® in this Accounting Standards Update require changes to the U.S. GAAP Financial Reporting Taxonomy (Taxonomy). Those changes, which will be incorporated into the proposed 2016 Taxonomy, are available for public comment through ASU Taxonomy Changes provided at www.fasb.org, and finalized as part of the annual release process starting in September 2015.