

Board Meeting Handout

Disaggregation—Income Statement Expenses: Clarifying the Effective Date December 18, 2024

Meeting Purpose

1. The purpose of this meeting is for the Board to redeliberate on the amendment in proposed Accounting Standards Update, *Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures (Subtopic 220-40): Clarifying the Effective Date*, which was issued for comment on November 25, 2024, with a 15-day comment period.

Questions for the Board

1. Does the Board want to affirm its decision to clarify the effective date for interim reporting periods?
2. Has the Board received sufficient information and analyses to make informed decisions on the issues presented? If not, what other information or analyses does the Board need?
3. Does the Board think that the expected benefits of the change would justify the expected costs? If so, does the Board give the staff permission to draft a final Accounting Standards Update for vote by written ballot?

Background and Summary of Comment Letter Feedback

2. Following the issuance of Accounting Standards Update No. 2024-03, *Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures (Subtopic 220-40): Disaggregation of Income Statement Expenses*, the Board was asked to clarify the initial effective date for entities that do not have an annual reporting period that ends on December 31 (referred to as non-calendar year-end entities). Subsequently, the Board issued a proposed Update that includes one amendment to paragraph 220-40-65-1(a), which states the following:

The pending content that links to this paragraph shall be effective for public business entities for annual reporting periods beginning after December 15, 2026, and interim reporting periods within annual reporting periods beginning after December 15, 2027. Early adoption is permitted.

3. Four comment letters were received, three from practitioners and one from a state CPA society, on the amendment in the proposed Update. All stakeholders agreed that the proposed amendment would clarify the initial adoption date for non-calendar year-end entities.

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Board Meeting Handout
Agenda Prioritization
December 18, 2024

Meeting Purpose

1. The December 18, 2024 agenda prioritization meeting is for the staff to provide the Board with information and the staff's research for a potential project to reconsider the last-in, first-out (LIFO) inventory costing method that is currently allowed under Topic 330, Inventory, and for the Board to consider adding that project to its technical agenda.
2. The Board will evaluate the potential project based on the following agenda-decision criteria:
 - (a) Is there an identifiable and sufficiently pervasive need to improve generally accepted accounting principles (GAAP)?
 - (b) Are there technically feasible solutions, and are the expected benefits of those solutions likely to justify the expected costs of change?
 - (c) Does the issue have an identifiable scope?

LIFO Inventory Costing Method

The questions for the Board on this potential project are as follows:

Questions for the Board

1. Does the Board want to add a project to its technical agenda to reconsider whether the LIFO costing method should be an allowable inventory cost flow assumption under Topic 330?
2. If the answer to Question 1 is yes, does the Board:
 - (a) Have feedback on the project's objective or scope?
 - (b) Request that the staff conduct additional research or outreach on certain potential solutions?

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Issue Background

3. The Board received an [agenda request](#) asking that the Board reconsider the LIFO costing method as an acceptable inventory costing method in GAAP. The agenda request included several issues that the requestors suggested that the Board consider when assessing whether the LIFO costing method should remain an acceptable inventory costing method under GAAP. Those issues included (a) convergence with International Financial Reporting Standards (IFRS Accounting Standards) and a potential reduction of accounting alternatives, (b) conceptual concerns, (c) revenue and expense matching concerns, (d) deferred holding gains concerns, and (e) the LIFO conformity rule within the Internal Revenue Code.
4. As a result of those issues, the agenda request asks that the Board consider one of the following potential updates to GAAP:
 - (a) Disallow the LIFO costing method for financial statement reporting, consistent with IFRS Accounting Standards
 - (b) Limit the use of the LIFO costing method to those entities for which the LIFO cost flow assumption matches the physical flow of inventory units
 - (c) If the LIFO costing method is retained for financial reporting purposes, make the following updates to the guidance in Topic 330:
 - (i) Require that all entities disclose the difference between the book value of LIFO inventory and its current or replacement cost, when material
 - (ii) Require that all entities disclose the effect of LIFO liquidations on reported income when the effect of the liquidation is material
 - (iii) If an entity applies the LIFO costing method differently for book and tax reporting, require that the entity separately disclose the resulting deferred tax asset or deferred tax liability from other deferred taxes in its footnote disclosures
 - (iv) Update the guidance in paragraph 330-10-30-9 to reflect the objective of general purpose financial reporting in the Conceptual Framework.

Accounting for Inventory

Inventory Measurement

5. Topic 330 provides guidance for how an entity accounts for and reports inventory. Paragraph 330-10-30-1 establishes that the primary basis for the measurement of inventories is cost, which is generally defined as either the price paid or consideration given to acquire an asset. When applied to inventory, cost includes acquisition costs and production costs that are

incurred to bring the inventory item to its existing condition and location. Determining the cost for individual inventory items can be challenging because an entity must allocate its cost to all units produced and sold during each period.

6. Topic 330 allows for different cost flow assumptions or methods to be used to measure an entity's inventory costs (that is, the entity's ending inventory capitalized on the balance sheet and its cost of goods sold recognized on the income statement). For example, as noted by paragraph 330-10-30-9, inventory costs may be determined under any one of several cost flow assumptions, including the first-in, first-out (FIFO), average cost, and LIFO costing methods. However, there are also other costing methods that are allowable under Topic 330, including specific identification and the retail inventory method. Paragraph 330-10-30-9 states that the major objective in selecting a cost flow assumption should be to choose the one that most clearly reflects periodic income.
7. Some entities may have the ability to identify costs specific to an inventory item that is sold to a customer. For example, an entity with a low volume of distinct inventory items may be able to identify the specific cost of each item of inventory sold. However, the use of cost flow assumptions other than the specific identification costing method may be necessary if similar items of inventory are purchased at different times and different prices, and the identity of those inventory items is lost between the time of acquisition or production and the time of sale. In those instances, cost flow assumptions provide practical bases for the allocation of costs to inventory when specific identification may not be practical.

LIFO Cost Flow Method

8. The LIFO costing method measures cost of goods sold using the cost of the items of inventory last acquired or produced. In periods of rising prices, this results in a larger reported amount of cost of goods sold and a lower reported amount of ending inventory than would be the case using the FIFO costing method or average costing method.
9. There are two broad methods for applying the LIFO cost flow assumption, which include the specific identification costing method and the dollar-value costing method. Furthermore, there are several techniques in practice used to calculate the LIFO index for the dollar-value costing method, including (a) the double-extension method, (b) the link-chain method, (c) the index method, and (d) the retail inventory method. Generally, the specific identification costing method is the simplest to understand conceptually but, in practice, many entities use the dollar-value costing method because the specific identification costing method can be burdensome to apply.

Required Inventory Disclosures

10. Topic 330, specifically paragraphs 330-10-50-1 through 50-6, requires that an entity make certain disclosures, including the basis used for stating inventories and the nature of any changes in the basis of stating inventories, losses from the subsequent measurement of inventory, goods stated above cost, inventories stated at sales prices, the amount of losses on firm purchase commitments, and significant estimates applicable to inventory.
11. In addition to those GAAP disclosures described in paragraph 10, the Securities and Exchange Commission also requires several inventory related disclosures, including two disclosures that are specific to the LIFO costing method. First, Regulation S-X Rule 5-02.6(c) requires that an entity disclose, either parenthetically on the face of the balance sheet or in a footnote, the excess of replacement or current cost over the stated LIFO value of inventory (that is, the “LIFO reserve” amount).¹ In addition, Staff Accounting Bulletin (SAB) Topic 11.F, “Miscellaneous Disclosure: LIFO Liquidations,” provides interpretive guidance noting that a registrant that uses the LIFO costing method must sufficiently disclose, either parenthetically on the face of the income statement or in a footnote, the effect of any LIFO liquidations on income.²

¹ Paragraph 210-10-S99-1

² Paragraph 330-10-S99-3