FORsights

New Expense Details Coming for Public Companies?

On July 31, 2023, FASB issued an exposure draft that would require public business entities (PBEs) to disclose additional detailed information—on an annual and interim basis—about the types of expenses (including inventory and manufacturing expense, employee compensation, depreciation, and amortization) included within commonly presented expense line items—cost of sales, selling general and administrative (SG&A), and research and development (R&D).

Comments are requested by October 30, 2023.

Background

Investors have long lobbied for additional expense details in financial statements, prompting FASB to kick off this project in 2017. Currently, Accounting Standards Codification (ASC) 220, *Income Statement—Reporting Comprehensive Income*, does not mandate specific expense captions on the face of the income statement or require any disaggregation of expense captions. Certain income statement breakouts are required by industry-specific guidance or are triggered when a specific event occurs, *e.g.*, goodwill impairment. Other expenses, even when not required to be broken out on the face of the income statement, are required to be disclosed separately in the financial statement notes. For PBEs subject to the SEC's presentation requirements, Regulation S-X also contains certain industry-specific disclosures.

The proposal does not change or remove these existing presentation requirements. The proposal addresses where and how new additional information would appear in the financial statement notes. The proposal does not require any changes to the face of the income statement.

Scope

The proposal would apply to all PBEs. Private companies, nonprofits, and employee benefit plans are not in scope.

What Expenses Will Require Disaggregation?

The proposal would require a PBE to disclose—in tabular format—the amounts of the following expenses included in each **relevant** expense caption appearing on the face of the income statement in continuing operations:

Inventory[1] and manufacturing expense

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[1] The proposal defines inventory expense as: "An expense resulting from the derecognition of inventory due to sale to customers, consumption in the production of goods or services for such sale, or remeasurement (for example, an impairment) in accordance with Section 330-10-35 or any other Subsequent Measurement Section within an Industry Subtopic in Topic 330 on inventory."

- Employee compensation[2]
- Depreciation
- Intangible asset amortization
- Depreciation, depletion, and amortization (DD&A) recognized as part of oil- and gas-producing activities (ASC 932, *Extractive Activities, Oil and Gas*)

The proposal contains three detailed examples of the disclosures and presentation that would be required (manufacturing and service operations, service operations, and a bank). See Appendix for one example.

Relevant Expenses

FASB consciously elected not to include a prescriptive list of "relevant" expense captions. To be flexible and applicable across all industries, FASB focused on the expense captions disclosed on the face of the income statement. If an income expense caption in continuing operations contains any of the five expense types noted above, additional tabular disclosure would be required in the financial statement notes.

For each relevant expense caption, any amounts not covered by the five categories above must be accumulated in an "other" category with a qualitative description of their composition. An entity is not precluded from breaking out additional expense line items within a relevant expense caption and reducing the amount in the "other" category.

FASB expects that entities would generally identify cost of sales, SG&A, and R&D expenses as relevant expense captions subject to further disaggregation.

Inventory & Manufacturing Expense

On an annual basis, an entity must disclose how it defines other manufacturing expenses. Management judgment will be required and the proposal notes that this may include—but is not limited to—certain costs incurred as part of an entity's manufacturing activities that are not capitalizable, *e.g.*, unallocated manufacturing overhead related to abnormally low production.

The proposal mandates additional disaggregation of inventory and manufacturing expenses. Tabular disclosure will be required for any costs incurred that were capitalized to inventory during the current period and any manufacturing costs incurred that were directly expensed during the current period, with accompanying disclosure of captions for changes in inventories and other adjustments and reconciling items to reconcile the amounts of

[2] The proposal defines employee compensation as: "All forms of cash consideration (including deferred cash compensation), share-based payment arrangements, medical care benefits, pension benefits, postretirement benefits, and nonretirement postemployment benefits (including special or contractual termination benefits) given by an entity in exchange for service rendered by employees or for the termination of employment. This includes compensation cost arising from wages, salaries, social security contributions, profit-sharing, bonuses, one-time employee termination benefits, other postemployment benefits, employee stock ownership plans, employee share purchase plans, defined contribution plans, multiemployer plans, and any other compensation cost recognized in accordance with the guidance in Topic 710 on compensation. For defined benefit plans within the scope of Topic 715 on retirement benefits, employee compensation includes only the service cost component of net periodic pension cost and the service cost component of net periodic postretirement benefit cost."

costs incurred to the amounts of expenses recognized. This would include the following categories, which must reconcile to costs incurred and expenses recognized:

- Purchases of inventory
- Employee compensation
- Depreciation
- Intangible asset amortization
- DD&A
- Costs capitalized to inventory and manufacturing expenses not included in the preceding categories
- Changes in inventories. The amount of inventory and manufacturing expense recognized during a reporting period and the costs incurred that are either capitalized to inventory or expensed as incurred during the reporting period will generally not be equal. If this is the case, this line item would be used as a reconciling item
- Other adjustments and reconciling items

Compensation

The proposal includes a practical expedient that allows entities complying with Regulation S-X 9-04 to use that definition of salaries and employee benefits rather than the definition included in this proposed standard. An entity may elect—but is not required—to include amounts attributable to other transactions entered into for the benefit of employees, *e.g.*, the provision of subsidized goods or services, in employee compensation. The election should be disclosed as well as a description of the transactions included.

Selling Expenses

On an interim and annual basis, an entity must disclose in the financial statement notes the total selling expenses recognized in continuing operations. An entity shall make its own determination of what constitutes a selling expense and, on an annual basis, disclose how it defines selling expenses.

Condensed Income Statement for Interim Reporting

Entities complying with SEC Regulation S-X are allowed to present a condensed income statement for interim reporting, which may have different expense captions than annual reports. The proposal is carefully worded so that disaggregation requirements would apply to the captions presented in a given reporting period.

Integration With Existing Disclosure Requirements

The proposal would require an entity to use the proposed tabular format for certain existing disclosures. The items listed below would not cause an expense line item to be relevant, but an entity would be required to break out any of the below items into a separate line item in the tabular disclosure for the relevant expense it rolls up to in its entirety.

If cost of sales was a relevant expense caption (because cost of sales includes inventory and manufacturing expense) and if amortization of costs to fulfill a contract with a customer was recognized entirely **in cost of sales and not in multiple expense captions presented on the face of the income statement, then amortization of costs to fulfill a contract with a customer would be required to be included as a separate line item in the new tabular format disclosure in addition to the five categories noted above.**

For each relevant expense caption identified, an entity would disclose—in tabular format—each of the following expenses, gains, and losses and the amount recognized in each relevant expense caption, if applicable:

- The amount of R&D assets acquired in a transaction other than a business combination and written off (ASC 350, *Intangible Assets*)
- Impairment loss recognized related to an intangible asset (ASC 350)
- Impairment loss of long-lived assets classified as held and used (ASC 360, *Property, Plant, and Equipment*)
- Gain or loss recognized for long-lived assets classified as held for sale or disposed of (ASC 360)
- Each major type of cost associated with an exit or disposal activity (ASC 420, *Exit or Disposal Cost Obligations*)
- Bargain purchase gain recognized in a business combination (ASC 805, *Business Combinations*)
- Any gain or loss recognized upon the deconsolidation of a subsidiary or the derecognition of a group of assets (ASC 810, *Consolidation*)
- Gains and losses on derivative instruments and related hedged items (ASC 815, *Derivatives and Hedging*)
- Amortization/impairment of license agreements for program material (ASC 920, *Entertainment – Broadcasters*)
- Amortization/Impairment of film costs (ASC 926, *Entertainment – Films*)

The following amounts should be included in a tabular disclosure if those amounts are included entirely in one relevant expense line item:

- Provision for expected credit losses (ASC 326, *Financial Instruments—Credit Losses*)
- Losses on firm purchase commitments (ASC 330, *Inventory*)
- Amortization expense attributable to the expiration of an insurance or reinsurance coverage provided under a contract that transfers only significant underwriting risk (ASC 340, *Other Assets and Deferred Costs*)
- Amortization of costs to fulfill a contract with a customer (ASC 340)
- Impairment of costs to fulfill a contract with a customer (ASC 340)
- Amortization of costs to obtain a contract with a customer (ASC 340)
- Impairment of costs to obtain a contract with a customer (ASC 340)
- Amortization of capitalized implementation costs of hosting arrangements that are service contracts (ASC 350, *Intangibles—Goodwill and Other*)
- Asset retirement obligation accretion expense (ASC 410, *Asset Retirement and Environmental Obligations*)
- Loss contingencies recognized (ASC 450, *Contingencies*)
- Warranty expense (ASC 460, *Guarantees*)

- Expense related to counterparty default in own-share lending arrangements issued in contemplation of convertible debt issuance (ASC 470, *Debt*)
- Aggregate gain on restructuring of payable by a debtor with a troubled debt restructuring (ASC 470)
- Gains and losses upon consolidation of a variable interest entity that is not a business (ASC 810)
- Foreign currency transaction gains or losses (ASC 830, *Foreign Currency Matters*)
- Operating lease cost (ASC 842, *Lease Accounting*)
- Short-term lease cost (ASC 842)
- Variable lease cost (ASC 842)
- Net gain or loss recognized from sale and leaseback transactions (ASC 842)
- Gains and losses from nonmonetary transactions (ASC 845, *Nonmonetary Transactions*)

Transition & Effective Date

If approved, the changes would be implemented on a prospective basis along with an option to adopt retrospectively at the entity's option. The effective date will be determined after FASB reviews comment letter feedback.

Other Reporting Changes Coming – Segment Reporting

On July 26, 2023, FASB approved drafting of a final ASU that would require enhanced disclosures and increased frequency of reporting of a public entity's reportable segments. The final ASU is expected in September 2023 and closely follows the exposure draft. The ASU will be effective for fiscal years beginning after December 15, 2023 and interim periods beginning after December 15, 2024. Highlights include:

All annual disclosures about a reportable segment's profit or loss currently required by ASC 280 would now be required in interim periods (interest revenue and expenses, depreciation, depletion, and amortization expense)
On an annual and interim basis, disclose significant segment expenses that are regularly provided to the chief operating decision maker and included within each reported measure of segment profit or loss
On an annual and interim basis, disclose an amount for other segment items by reportable segment and a description of its composition
A public entity with a single reportable segment would be required to provide all the proposed disclosures and all existing segment disclosures in ASC 280

Conclusion

Forvis Mazars works with hundreds of publicly traded companies in the delivery of assurance, tax, or consulting services within the U.S. and globally. For more information, visit forvismazars.us.

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Appendix

The following example illustrates new disclosures for a manufacturing company that presents cost of products sold, cost of services, and SG&A on the face of its income statement. Additional detail on this illustrative example and other illustrative examples can be found in the proposal.

Cost of products sold

Cost of products sold	20X3	20X2	20X1
Inventory and manufacturing expense[a]	$ 53,688	$ 51,935	$ 48,680
Employee compensation	2,046	1,827	1,279
Depreciation	1,395	1,311	1,232
Warranty expense	4,394	3,952	3,894
Other cost of products sold[b]	1,933	1,873	2,159
Total cost of products sold	$ 63,456	$ 60,898	$ 57,244

(a) The company defines manufacturing expenses (other than inventory expense) as those that are incurred for the purpose of producing units of inventory, but are not capitalizable. Other manufacturing expenses include costs incurred related to idled manufacturing plants.

(b) Other cost of products sold consisted primarily of amounts paid to carriers for freight services related to contract fulfillment for the years ended December 31, 20X3, 20X2, and 20X1.

Cost of products sold: inventory and manufacturing expense			
Purchases of inventory	$ 20,213	$ 19,199	$ 16,319
Employee compensation	15,532	14,712	12,799
Depreciation	8,795	8,678	8,418
Intangible asset amortization	3,914	4,050	3,929
Other inventory and manufacturing costs (directly expensed or capitalized to inventory)[c]	5,619	5,733	5,834
Total inventory and manufacturing costs (directly expensed or capitalized to inventory)	54,073	52,372	47,299
Other adjustments and reconciling items[d]	(542)	424	538
Changes in inventories	157	(861)	843
Total inventory and manufacturing expense	$ 53,688	$ 51,935	$ 48,680

(c) Other inventory and manufacturing costs consisted primarily of power, fuel, and other utilities costs for the years ended December 31, 20X3, 20X2, and 20X1.

(d) Other adjustments and reconciling Items consisted of reconciling adjustments attributable to differences in the foreign exchange rates used to translate beginning inventory, ending inventory, and costs incurred from various functional currencies into the reporting currency for the years ended December 31, 20X3, 20X2, and 20X1. For the year ended December 31, 20X3, other adjustments and reconciling Items also included the carrying amount of inventory sold to noncustomers in connection with a disposal transaction.

Cost of services

Cost of services			
Employee compensation	$ 6,598	$ 5,654	$ 4,354
Depreciation	763	765	742
Intangible asset amortization	642	670	650
Other cost of services[e]	2,493	2,479	3,152
Total cost of services	$ 10,496	$ 9,568	$ 8,898

(e) Other cost of services consisted primarily of operating lease and travel costs for the years ended December 31, 20X3, 20X2, and 20X1.

Selling, general, and administrative

Selling, general, and administrative			
Employee compensation	$ 13,242	$ 11,379	$ 10,764
Depreciation	1,454	1,755	1,737
PP&E impairment	412	-	-
Intangible asset amortization	523	596	-
Other SG&A[f]	5,218	5,141	5,615
Total selling, general, and administrative	$ 20,849	$ 18,871	$ 18,116

(f) Other SG&A consisted primarily of professional services fees, operating lease expense, and the costs paid to third parties for printing, publications, and advertising for the years ended December 31, 20X3, 20X2, and 20X1.

Selling expenses

During the years ended December 31, 20X3, 20X2, and 20X1, selling expenses were $13,425, $12,123, and $11,585, respectively. The entity's selling expenses include those expenses related to marketing and promotional activities and client relationship management.