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To the Point

FASB — final guidance

FASB requires public business entities to disaggregate certain income statement expenses

The guidance addresses investors' requests for more detailed information about certain income statement expenses.

What you need to know

- The FASB issued final guidance requiring public business entities to disclose, on an annual and interim basis, disaggregated information about certain income statement expense line items.
- Public business entities are required to disclose purchases of inventory, employee compensation, depreciation, intangible asset amortization and depletion for each income statement line item that contains those expenses.
- Specified expenses, gains or losses that are already disclosed under existing US GAAP are required to be included in the disaggregated income statement expense line item disclosures, and any remaining amounts need to be described qualitatively. Separate disclosures of total selling expenses and an entity's definition of those expenses are also required.
- Public business entities are required to apply the guidance prospectively and may apply it retrospectively. The guidance is effective for fiscal years beginning after 15 December 2026, and interim periods within fiscal years beginning after 15 December 2027. Early adoption is permitted.

Overview

The Financial Accounting Standards Board (FASB or Board) issued a final Accounting Standards Update (ASU)[1] requiring a public business entity to provide disaggregated disclosures, in the notes to the financial statements, of certain categories of expenses that are included in expense line items[2] on the face of the income statement. The disclosures are required on an annual and interim basis.

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The guidance requires an entity to disclose the total amount of selling expenses and, on an annual basis, how it defines selling expenses. An entity may use estimates or other methods that produce a reasonable approximation of amounts required to be disclosed. The guidance does not change what an entity presents on the face of its income statement.

The FASB issued the guidance in response to investors' requests for more detailed expense information, which they said is critical to understanding an entity's performance, assessing its prospects for future cash flows and comparing its performance both over time and with that of other entities.

Key considerations

Required expense categories

The guidance requires disclosure, in a tabular format, of each relevant expense line item on the face of the income statement in continuing operations disaggregated into the following categories:

- Purchases of inventory in the scope of Accounting Standards Codification (ASC) 330, *Inventory*
- Employee compensation
- Depreciation
- Intangible asset amortization
- Depreciation, depletion and amortization (DD&A) of capitalized acquisition, exploration and development costs recognized as part of oil- and gas-producing activities or other amounts of depletion expense

A relevant expense line item is one that is presented on the face of the income statement in continuing operations that contains any of the above expense categories (e.g., income tax expense is not a relevant expense line item because it does not contain any of these expense categories). A relevant expense line item that consists entirely of one expense category listed above is not required to be disaggregated.

Purchases of inventory

Purchases of inventory include amounts in the scope of ASC 330, except for inventory amounts recognized from a business combination, joint venture formation and the initial consolidation of a variable interest entity that is not a business combination.

The guidance provides an entity with two acceptable bases for disclosing the disaggregation of a relevant expense line item that contains expense amounts related to inventory in the scope of ASC 330 (e.g., cost of products sold):

- **Cost-incurred basis**: Costs incurred that were capitalized to inventory in accordance with ASC 330 and any costs incurred that were directly expensed during the current reporting period[3]
- **Expense-incurred basis**: Expense amounts related to the derecognition of inventory that were previously capitalized in accordance with ASC 330 and any costs incurred that were directly expensed during the current reporting period[3]

An entity's chosen basis needs to be applied to all required expense categories listed above. Under the cost-incurred basis, an entity is required to disclose categories for changes in inventories and other adjustments and reconciling items to reconcile the costs incurred to the relevant expense line item. The amount disclosed in changes in inventories equals the difference between the amount of inventory included on the balance sheet at the end of the prior reporting period and the amount at the end of the current reporting period. See the Appendix for an illustration of the disclosures under the cost-incurred basis.

The guidance provides a practical expedient allowing an entity to disclose a qualitative description of the composition of an income statement expense line item when substantially all of it comprises purchases of inventory, instead of disclosing disaggregated amounts for that expense line item.

Employee compensation

The guidance includes a new definition of employee compensation and amends the existing definition of employee used in ASC 718, *Compensation — Stock Compensation*. Under the guidance, employee compensation[4] includes all forms of cash consideration (including deferred cash compensation), share-based payment arrangements and various other benefits (e.g., medical care, pension, postretirement, nonretirement postemployment) given by an entity in exchange for service rendered by employees or for the termination of employment. One-time employee termination benefits under ASC 420, *Exit or Disposal Cost Obligations*, are required to be disclosed separately from employee compensation.

Depreciation and intangible asset amortization

Certain existing disclosures are included in the same tabular disclosure under the guidance.

The amounts provided separately for depreciation and intangible asset amortization need to be consistent with those reported under the requirements in ASC 360, *Property, Plant, and Equipment*, and ASC 350, *Intangibles — Goodwill and Other*, respectively. Additionally, the amortization of a right-of-use asset for a finance lease and the amortization of leasehold improvements recognized in accordance with ASC 842, *Leases*, need to be included in either the depreciation or intangible asset amortization expense category.

DD&A and depletion

In paragraph BC63 of the ASU's Background Information and Basis for Conclusions, the Board said that DD&A is an industry-specific expense, but it was included as an expense category that is required to be disclosed because "it represents a potentially significant noncash expense that is recognized systematically, like depreciation and intangible asset amortization." Depletion expense recognized by entities for activities other than oil and gas acquisition, exploration and development (e.g., mining activities) is required to be separately disclosed.

Tabular integration of other disclosure requirements

The guidance requires certain amounts already disclosed under existing US GAAP to also be disclosed as a separate category in the disaggregated expense table(s) if those amounts are recognized in the relevant expense line item. These include:

- Specified expenses, gains and losses for which there is an existing requirement to disclose both the amount and expense line item in the income statement where they are included[5]
- Specified expenses, gains and losses for which there is an existing requirement to disclose the amount, but no requirement to disclose the expense line item in the income statement where they are included if the amount is recorded entirely in one expense line item[5]

To illustrate the second bullet, if cost of sales is a relevant expense line item and operating lease costs are included entirely in cost of sales, the entity is required to include operating lease costs as a separate category in the disaggregated expense table for cost of sales. Alternatively, disclosure as a separate category is not required if operating lease costs are included in multiple line items, such as selling, general and administrative (SG&A) and cost of sales.

Expense reimbursements included in relevant expense line items

Entities presenting a relevant expense line item that includes amounts that are reimbursements related to a cost-sharing or cost-reimbursement arrangement from or to another entity are required to provide incremental quantitative and qualitative details in the expense disaggregation disclosures.

Qualitative disclosures about any remaining amounts

The guidance requires qualitative disclosures about any remaining amounts in relevant expense line items. The detail provided in such disclosures needs to be commensurate with the significance of the amounts described.

Selling expenses

The guidance requires disclosure of the total amount of selling expenses recognized in continuing operations on an annual and interim basis and disclosure of an entity's definition of selling expenses on an annual basis (or in interim reporting periods if the definition is changed).

How we see it

Entities should evaluate whether their existing systems are capable of capturing the data required and whether additional processes and controls are necessary.

Effective date and transition

Entities are required to apply the guidance prospectively and may apply it retrospectively. The guidance is effective for fiscal years beginning after 15 December 2026, and interim periods within fiscal years beginning after 15 December 2027. Early adoption is permitted.

Endnotes:

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[1] ASU 2024-03, *Income Statement — Reporting Comprehensive Income — Expense Disaggregation Disclosures (Subtopic 220-40): Disaggregation of Income Statement Expenses.*

[2] Line items are also referred to as captions.

[3] Costs incurred that were directly expensed during the current reporting period include costs that are capitalizable in accordance with ASC 330 but were directly expensed to the income statement.

[4] As a practical expedient for determining what amounts are classified as employee compensation, an entity that presents an expense line item for salaries and employee benefits (or a similarly named line item) on the face of its income statement to comply with Securities and Exchange Commission Regulation S-X Rule 210.9-04, *Statements of Comprehensive Income* (ASC 942-220-S99-1), may use those amounts rather than amounts calculated using the definition of employee compensation included in this guidance.

[5] ASC 220-40-50-21 and ASC 220-40-50-22, respectively.

Appendix: Illustration of disclosures under the cost-incurred basis

The following illustration, which is included in the ASU, shows one type of tabular format an entity could use to make the disclosures.

For the year ended 31 December 20X4, Entity X, a manufacturer with significant service operations, presents the following comparative income statement and related disclosures in the notes to the financial statements. This example assumes the use of the cost-incurred basis for disaggregating cost of products sold. For illustration purposes related to the tabular integration of other disclosure requirements, assume Entity X recognizes the following expenses: (1) impairment of property, plant and equipment (PP&E) in SG&A,[1] (2) warranty expense entirely within cost of products sold[2] and (3) operating lease cost in both cost of services and SG&A.[2] This example also assumes Entity X recognizes amounts related to the initial recognition and subsequent measurement of a liability for an environmental obligation in cost of products sold:

Consolidated Income Statement

	20X4	20X3	20X2
Revenues:			
Products	$ 82,144	$ 79,137	$ 75,180
Services	26,132	23,146	21,989
Total revenues	108,276	102,283	97,169
Operating expenses:			
Cost of products sold	63,456	60,898	57,244
Cost of services	10,496	9,568	8,898
Selling, general, and administrative	20,849	18,871	18,116
Total operating expenses	94,801	89,337	84,258
Operating income	13,475	12,946	12,911
Interest expense	4,971	4,213	4,297
Income before income taxes	8,504	8,733	8,614
Income tax expense	1,786	1,834	1,809
Net income	$ 6,718	$ 6,899	$ 6,805

Relevant expense line items

Cost of products sold			
Cost of products sold	20X4	20X3	20X2
Purchases of inventory	$ 20,213	$ 19,199	$ 16,319
Employee compensation	17,578	16,539	14,078
Depreciation	10,190	9,989	9,650
Intangible asset amortization	3,914	4,050	3,929
Warranty expense	4,394	3,952	3,894
Other cost of products sold[(a)]	7,552	7,606	7,993
Changes in inventories	157	(861)	843
Other adjustments and reconciling items[(b)]	(542)	424	538
Total cost of products sold	$ 63,456	$ 60,898	$ 57,244

(a) Other cost of products sold consists primarily of amounts paid to carriers for outbound freight services related to contract fulfillment and amounts related to the measurement of a liability for an environmental obligation for the years ended December 31, 20X4, 20X3 and 20X2. Year ended December 31, 20X4, also includes inventory amounts recognized as part of a business combination.

(b) Other adjustments and reconciling items consist 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, 20X4, 20X3 and 20X2.

Cost of services			
Cost of services	20X4	20X3	20X2
Employee compensation	$ 6,598	$ 5,654	$ 4,354
Depreciation	763	765	742
Intangible asset amortization	642	670	650
Other cost of services[(c)]	2,493	2,479	3,152
Total cost of services	$ 10,496	$ 9,568	$ 8,898

(c) Other cost of services consists primarily of operating lease and travel expenses for the years ended December 31, 20X4, 20X3, and 20X2.

Selling, general, and administrative			
Selling, general, and administrative	20X4	20X3	20X2
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[(d)]	5,218	5,141	5,615
Total selling, general, and administrative	$ 20,849	$ 18,871	$ 18,116

(d) Other SG&A consists primarily of professional services fees and operating lease expense for the years ended December 31, 20X4, 20X3, and 20X2.

Example footnote disclosure: Selling expenses

During the years ended December 31, 20X4, 20X3 and 20X2, 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.

1 This is an expense for which there is an existing requirement to disclose the amount and expense line item in the income statement where it is included (ASC 220-40-50-21).

2 These are expenses for which there is an existing requirement to disclose the amounts, but no requirement to disclose the line items in the income statement where they are included. The warranty expense is recorded entirely in one expense line item and, therefore, included in the cost of products sold disaggregated expense table. The operating lease cost is not recorded entirely in one expense line item and, therefore, not included as a separate category in the disaggregated expense tables but is included in other SG&A and other cost of services (ASC 220-40-50-22).