FASB EXPOSURE DRAFT

Proposed Accounting Standards Update

Issued: January 10, 2017
Comments Due: March 13, 2017

Inventory (Topic 330)

Disclosure Framework—Changes to the Disclosure Requirements for Inventory

The Board issued this Exposure Draft to solicit public comment on proposed changes to Topic 330 of the *FASB Accounting Standards Codification*®. Individuals can submit comments in one of three ways: using the electronic feedback form on the FASB website, emailing comments to director@fasb.org, or sending a letter to "Technical Director, File Reference No. 2017-210, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

Financial Accounting Standards Board

Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update

The Board invites comments on all matters in this Exposure Draft until March 13, 2017. Interested parties may submit comments in one of three ways:

- Using the electronic feedback form available on the FASB website at Exposure Documents Open for Comment
- Emailing comments to director@fasb.org, File Reference No. 2017-210
- Sending a letter to "Technical Director, File Reference No. 2017-210, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

All comments received are part of the FASB's public file and are available at www.fasb.org.

The *FASB Accounting Standards Codification*® is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective. A copy of this Exposure Draft is available at www.fasb.org.

FASB FINANCIAL ACCOUNTING STANDARDS BOARD

Proposed Accounting Standards Update

Inventory (Topic 330)

Disclosure Framework—Changes to the Disclosure Requirements for Inventory

January 10, 2017

Comment Deadline: March 13, 2017

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Summary and Questions for Respondents

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

The Board is issuing this proposed Update as part of the disclosure framework project. The objective and primary focus of the disclosure framework project are to improve the effectiveness of disclosures in the notes to financial statements by facilitating clear communication of the information required by generally accepted accounting principles (GAAP) that is most important to users of each entity's financial statements. Achieving the objective of improving the effectiveness of the notes to financial statements includes:

1. The development of a framework that promotes consistent decisions by the Board about disclosure requirements
2. The appropriate exercise of discretion by reporting entities.

In March 2014, the Board issued a proposed FASB Concepts Statement, *Conceptual Framework for Financial Reporting—Chapter 8: Notes to Financial Statements.* The proposed Concepts Statement is intended to identify a broad range of possible information for the Board to consider when deciding on the disclosure requirements for a particular Topic. From that intentionally broad set, the Board would identify a narrower set of disclosures about that Topic to be required on the basis of an evaluation of whether the benefits of entities providing the information justify the costs. The Concepts Statement, when finalized, would be used by the Board as a basis for establishing disclosure requirements in future accounting standards as well as for evaluating current disclosure requirements.

The Board decided to test the guidance in the proposed Concepts Statement and improve the effectiveness of disclosure requirements on inventory, income taxes, fair value measurements, and defined benefit pension and other postretirement benefit plans by using those proposed concepts. The amendments in this proposed Update are the result of the Board's consideration of the concepts in the proposed Concepts Statement as they relate to inventory disclosures in Topic 330, Inventory. The project does not extend to disclosures related to cost of goods sold.

Who Would Be Affected by the Amendments in This Proposed Update?

The amendments in this proposed Update would apply to all entities that are required to follow Topic 330.

Certain of the disclosures that would be required by the amendments in this proposed Update would not be required for entities that are not public business entities. The Board is seeking input on the application of the proposed amendments to private companies and not-for-profit organizations.

What Are the Main Provisions?

The amendments in this proposed Update would modify the disclosure requirements for inventory. The following additional disclosures would be required by Topic 330 for all entities on the basis of the proposed Concepts Statement and cost and benefit considerations:

1. Inventory disaggregated by component (for example, raw materials, work-in-process, finished goods, and supplies)
2. Inventory disaggregated by measurement basis
3. Changes to the inventory balance that are not specifically related to the purchase, manufacture, or sale of inventory in the ordinary course of business
4. A qualitative description of the types of costs capitalized into inventory
5. The effect of last-in, first-out (LIFO) liquidations on income
6. The replacement cost for LIFO inventory.

Entities that report some or all of their inventory using the retail inventory method (RIM) also would be required to provide qualitative and quantitative information about the critical assumptions used in the calculation of inventory under the RIM.

In addition, entities that are subject to disclosing segment information in Topic 280, Segment Reporting, would be required to disclose, in both annual and interim periods, inventory by reportable segment and by component for each reportable segment to the extent that information is regularly provided to the chief operating decision maker.

When Would the Amendments Be Effective?

The amendments in this proposed Update would be applied prospectively.

The effective date will be determined after the Board considers stakeholder feedback on the proposed amendments.

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

Question 1: Would the amendments in this proposed Update result in more effective, decision-useful information about inventory? Please explain why or why not.

Question 2: Are the proposed disclosure requirements operable and auditable? If not, which aspects pose operability or auditability concerns and why?

Question 3: Would any of the proposed disclosures impose significant incremental costs? If so, please describe the nature and extent of the additional costs.

Question 4: Paragraph 330-10-50-7 proposes a requirement to disclose certain specific changes in the inventory balance. Is this requirement sufficiently operable? Why or why not? Would a requirement to include a rollforward of inventory impose significantly greater costs? If so, please describe the nature and extent of the additional costs. Would the informational benefit of a rollforward be sufficient to justify the additional costs? Are there other ways to provide users with this information without imposing significant incremental costs, and, if so, what are they?

Question 5: The proposed amendments would apply to all entities, except for the requirements in paragraphs 280-10-50-25 and 280-10-50-32, which apply only to those public entities subject to the guidance in Topic 280. Is it appropriate to exclude entities that are not public business entities from this guidance? Are there other disclosures for which entities other than public business entities should be allowed a modification?

Question 6: Paragraph 330-10-50-11 proposes a requirement to disclose a qualitative description of types of costs that an entity capitalizes into inventory. Would this requirement provide useful information to users?

Question 7: Paragraph 330-10-50-12 proposes a requirement for entities that record inventory using the RIM to disclose qualitative and quantitative information about the critical assumptions used under that method. Is this disclosure requirement incremental to existing guidance for critical accounting estimates and significant accounting policies? Would it be operable and provide useful information to users?

Question 8: Are there any other disclosures that should be required by Topic 330 on the basis of the proposed Concepts Statement or for other reasons? Please explain why.

[Note: To see how the Board applied the decision questions from the proposed Concepts Statement to Topic 330, see *Decision Questions Considered in Establishing Disclosure Requirements* on this project's summary page on the FASB's website (www.fasb.org).]

Question 9: Should the proposed disclosures be required only for the fiscal year in which the requirements are effective and years after that fiscal year, or should prior periods be restated in the year in which the requirements are effective? Please explain why.

Question 10: How much time would be needed to implement the proposed amendments? Should the amount of time needed to implement the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities? Should early adoption be permitted? Please explain why.

Public Roundtable Meetings

The Board plans to hold public roundtable meetings on the amendments in this proposed Update in conjunction with the overall disclosure framework project in the first quarter of 2017. The purpose of roundtable meetings is to listen to the views of, and obtain information from, interested stakeholders about the proposed amendments.

Amendments to the *FASB Accounting Standards Codification*®

Summary of Proposed Amendments to the Accounting Standards Codification

1. The following table provides a summary of the proposed amendments to the Accounting Standards Codification.

Codification Paragraphs	**Action**	**Description of Changes**
330-10-30-12 Inventory—Overall—Initial Measurement	Amended	The proposed amendments would remove the disclosure on standard costs.
330-10-50-1 through 50-6 Disclosure	Superseded	The proposed amendments would replace current disclosure requirements.
330-10-50-1A through 50-1B and 330-10-50-7 through 50-14 Disclosure	Added	The proposed amendments would outline additional inventory disclosures.
330-10-55-8 through 55-10 Implementation Guidance and Illustrations	Amended	The proposed amendments would update the example.
330-10-55-14 through 55-17 Implementation Guidance and Illustrations	Added	The proposed amendments would add examples illustrating proposed inventory disclosures.
330-10-65-2 Transition and Open Effective Date Information	Added	The proposed amendments would add information on transition and effective date.

Codification Paragraphs	Action	Description of Changes
270-10-50-1 Interim Reporting—Overall—Disclosure	Amended	The proposed amendments would add a proposed inventory disclosure requirement to the interim guidance.
280-10-50-25 and 280-10-50-32 Segment Reporting—Overall—Disclosure	Amended	The proposed amendments would amend certain segment disclosures to include inventory.
280-10-55-53 through 55-54 Implementation Guidance and Illustrations	Added	The proposed amendments would add examples illustrating proposed inventory disclosures.

Introduction

2. The Accounting Standards Codification is amended as described in paragraphs 3–9. 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 underlined, and deleted text is ~~struck out~~.

Amendments to Subtopic 330-10

3. Amend paragraph 330-10-30-12, with a link to transition paragraph 330-10-65-2, as follows:

Inventory—Overall

Initial Measurement

> Determination of Inventory Costs

330-10-30-12 Standard costs are acceptable if adjusted at reasonable intervals to reflect current conditions so that at the balance-sheet date standard costs reasonably approximate costs computed under one of the recognized bases. ~~In such cases descriptive language shall be used which will express this relationship, as, for instance, “approximate costs determined on the first-in first-out basis,” or, if~~

~~it is desired to mention standard costs, "at standard costs, approximating average costs."~~

4. Supersede paragraphs 330-10-50-1 through 50-6 and the related headings and add paragraphs 330-10-50-1A through 50-1B and 330-10-50-7 through 50-14 and the related headings, with a link to transition paragraph 330-10-65-2, as follows:

[Note: Paragraph 330-10-50-1A contains paragraph references from the proposed Accounting Standards Update, *Notes to Financial Statements (Topic 235): Assessing Whether Disclosures Are Material*.]

Disclosure

~~> Basis for Stating Inventories~~

330-10-50-1 Paragraph superseded by Accounting Standards Update No. 201X-XX. ~~The basis of stating inventories shall be consistently applied and shall be disclosed in the financial statements; whenever a significant change is made therein, there shall be disclosure of the nature of the change and, if material, the effect on income. A change of such basis may have an important effect upon the interpretation of the financial statements both before and after that change, and hence, in the event of a change, a full disclosure of its nature and of its effect, if material, upon income shall be made. See paragraph 210-10-50-1.~~

330-10-50-1A This Section provides guidance on the financial statement disclosure requirements relating to **inventory** applicable to all entities. A reporting entity does not need to provide individual disclosures required by this Subtopic if the disclosures are immaterial. See paragraphs 235-10-50-7 through 50-9 for additional guidance on determining whether disclosures are material.

330-10-50-1B The objective of the following disclosures is to provide users of financial statements with information that is useful in assessing the following:

a. How different types of inventory may affect prospects for future cash flows
b. How inventory recorded using different measurement methods may affect the decision usefulness of information for projecting future cash flows
c. How transactions, events, and circumstances outside the normal course of business affect the inventory balance.

~~> Losses from the Subsequent Measurement of Inventory~~

330-10-50-2 Paragraph superseded by Accounting Standards Update No. 201X-XX. ~~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.~~

~~**> Goods Stated Above Cost**~~

330-10-50-3 Paragraph superseded by Accounting Standards Update No. 201X-XX. ~~Where goods are stated above cost this fact shall be fully disclosed.~~

~~**> Stating Inventories at Sales Prices**~~

330-10-50-4 Paragraph superseded by Accounting Standards Update No. 201X-XX. ~~Where such inventories are stated at sales prices, the use of such basis shall be fully disclosed in the financial statements.~~

~~**> Losses on Firm Purchase Commitments**~~

330-10-50-5 Paragraph superseded by Accounting Standards Update No. 201X-XX. ~~The amounts of net losses on firm purchase commitments accrued under paragraph 330-10-35-17 shall be disclosed separately in the income statement.~~ **[Content moved to paragraph 330-10-50-14]**

~~**> Disclosure of Significant Estimates**~~

330-10-50-6 Paragraph superseded by Accounting Standards Update No. 201X-XX. ~~See Example 1 (paragraph 330-10-55-8) for an illustration of the disclosure of significant estimates applicable to inventories as required by Section 275-10-50.~~ **[Content moved to paragraph 330-10-50-11]**

> Changes in Inventory

330-10-50-7 An entity shall disclose changes in the **inventory** balance during the period that are from transactions, circumstances, or events outside the normal course of purchasing, manufacturing, or selling inventory for each period presented. Examples of items that meet this principle may include, but are not limited to, increases or decreases in the inventory balance for any of the following, if applicable:

a. Atypical losses from the subsequent measurement of inventory or shrinkage, spoilage, or damage and a description of the facts and circumstances leading to those losses
b. Balance sheet reclassifications
c. Inventory obtained through a business combination
d. Inventory disposed of through a divestiture
e. Unrealized gains and losses for inventories recorded above cost or at selling prices.

See Example 2 (paragraph 330-10-55-14) for an illustration of the disclosure of changes in inventory.

> Composition of Inventory

330-10-50-8 An entity shall disclose the major components of inventory such as raw materials, work-in-process, finished goods, and supplies for each period presented. If it is not practical to assign amounts to major components of inventory using the last-in, first-out (LIFO) cost flow assumption, the major components may be disclosed under cost flow assumptions other than LIFO with the excess of such total amount over the aggregate LIFO amount shown as a deduction to arrive at the amount of the aggregate LIFO inventory.

330-10-50-9 An entity shall disclose the measurement bases for its inventory, such as LIFO, first-in, first-out (FIFO), LIFO retail inventory method, or weighted average and the amount recorded under each basis.

330-10-50-10 An entity shall disclose a qualitative description of the types of costs it capitalizes into inventory.

330-10-50-11 See Example 1 (paragraph 330-10-55-8) for an illustration of the disclosure of significant estimates applicable to inventories as required by Section 275-10-50. **[Content moved from paragraph 330-10-50-6]**

> Inventory Reported under the Retail Inventory Method

330-10-50-12 An entity that records any portion of its inventory using the retail inventory method of accounting shall disclose qualitative and quantitative information about the critical assumptions used to measure that portion of inventory under the retail inventory method at the end of each annual period presented. See Example 3 (paragraphs 330-10-55-15 through 55-17) for an illustration of the disclosure of information about the critical assumptions used to measure inventory under the retail inventory method.

> Inventory Reported under the LIFO Cost Flow Assumption

330-10-50-13 An entity applying the LIFO cost flow assumption to all or a portion of its inventory shall disclose the following:

a. Excess of replacement cost or current cost over the reported inventory amount
b. Effect on net income of the liquidation of a portion of an entity's LIFO inventory.

> Losses on Firm Purchase Commitments

330-10-50-14 The amounts of net losses on firm purchase commitments accrued under paragraph 330-10-35-17 shall be disclosed separately in the income statement. **[Content moved from paragraph 330-10-50-5]**

5. Amend paragraphs 330-10-55-8 through 55-10 and add paragraphs 330-10-55-14 through 55-17 and their related headings, with a link to transition paragraph 330-10-65-2, as follows:

Implementation Guidance and Illustrations

330-10-55-1 This Section, which is an integral part of the requirements of this Topic, provides general guidance to be used in accounting for **inventory**. Certain assumptions have been made to simplify the computations and focus on the issue at hand in each illustration.

> Illustrations

> > Example 1: Disclosure of Significant Estimates

330-10-55-8 This Example illustrates the guidance in paragraph ~~330-10-50-6~~330-10-50-12 regarding the disclosure of significant estimates related to inventory. Entity A manufactures high technology video game~~stereo~~ equipment. In June 20X7~~19X7~~, one of Entity A's competitors introduced a new model video game~~stereo~~ system with the same features as Entity A's Model A. The competitor's version sells for significantly less than Entity A's suggested retail price for Model A. The introduction of this product resulted in a sharp decrease in the sales volume of Model A. As of December 31, 20X7~~19X7~~, Entity A has accumulated significant inventory quantities beyond its ~~normal~~anticipated short-term needs of its Model A system. Inventory for Model A ($6 million) represents approximately 20 percent of Entity A's inventory at that date. The remaining 80 percent of Entity A's inventory consists of products experiencing only normal competitive pressures. Entity A has established provisions for obsolescence for this latter group of products in the normal course of business.

330-10-55-9 Management has developed a program to provide substantial dealer incentives on purchases of the Model A, which it expects will result in the sale of this inventory in the near term. Because of the existing high profit margin on its video game~~stereo~~ systems, Entity A would continue to earn a marginal profit on sales of the Model A under the new program. It is also reasonably possible, however, that the program will not be wholly successful, and, accordingly, a material loss could ultimately result on the disposal of the inventory.

330-10-55-10 The entity would disclose the following.

> As of December 31, 20X7~~19X7~~, some portion of $6 million of inventory of one of the entity's products is in excess of Entity A's current requirements based on

the recent level of sales. Management has developed a program to reduce this inventory to desired levels over the near term and believes no loss will be incurred on its disposition. No estimate can be made of a range of amounts of loss that are reasonably possible should the program not be successful.

330-10-55-11 This situation meets the criteria for disclosure under paragraph 275-10-50-8 because circumstances that existed at the date of the financial statements, including the decreasing sales volume and excessive quantities of inventory of Model A, make it at least reasonably possible that management's plan to liquidate its excess inventory without a loss will be less than fully successful and that such an outcome would have a near-term material effect on the entity's financial statements.

330-10-55-12 In this Example, Entity A discloses the existence of potentially excess quantities of inventory at the date of the financial statements and indicates that the uncertainty is expected to be resolved in the near term. The disclosure is intended to provide users with insight into management's assessment of recoverability of the cost of inventories existing at the date of the financial statements. Although disclosure of the $6 million carrying amount of the inventory of Model A is not required because, based on the facts presented, $6 million does not constitute a reasonable estimate of loss on the disposal of the inventory or the maximum amount in an estimated range of loss, disclosure of this amount is not misleading and may provide useful information.

330-10-55-13 Discussion of Entity A's provision for obsolescence for the remaining 80 percent of its inventory is not required because it is not considered reasonably possible that additional material losses on this inventory will occur.

> > Example 2: Disclosure of Changes in Inventory

330-10-55-14 This Example illustrates the guidance in paragraph 330-10-50-7 on the disclosure of changes in inventory. Entity B manufactures home-use and industrial tools and acquired Company Z in 20X8. Additionally, some of Entity B's inventory was damaged in a natural disaster during 20X8. Entity B also reclassified certain assets, including some inventory, to assets held for sale. Entity B discloses the following changes in inventory:

a. Impairment of $0.5 million of certain raw materials damaged in a flood
b. Inventory of $2 million obtained through Entity B's acquisition of Company Z
c. Inventory of $0.7 million reclassified to assets held for sale because of the pending sale of Entity B's drill product line.

> > Example 3: Retail Inventory Method

330-10-55-15 This Example illustrates both a narrative description of an entity's application of the retail inventory method and a tabular disclosure of the retail inventory calculation of ending inventory.

330-10-55-16 The following includes a narrative example of the required disclosure of the critical assumptions used in applying the retail inventory method:

> Under the Company's retail inventory method, the valuation of inventories at cost is estimated by applying a calculated cost-to-retail inventory ratio to the retail value of ending inventory at a department level. The Company's average cost-to-retail inventory ratio applied to ending inventory as of December 31, 20X8, and December 31, 20X7, respectively, was 72.4 percent and 72.3 percent. There are certain judgments and estimates inherent in the retail inventory method calculation that may affect the ending inventory valuation at cost, as well as the gross profit recognized. Those judgments include the approach to grouping products into departments, recording estimated shrinkage in physical inventories, and timely recording of markdowns taken.
>
> Permanent markdowns designated for clearance activity are recorded when the utility of the inventory has diminished. Permanent markdowns used in the retail inventory calculation were $1.0 million and $1.2 million at December 31, 20X8, and December 31, 20X7, respectively. Factors considered in the determination of permanent markdowns include current and anticipated demand, customer preferences, and merchandise age. When a decision is made to permanently mark down merchandise, the resulting gross margin reduction is recognized in the period in which the markdown is recorded.
>
> Physical inventories generally are taken within each merchandise department annually, and inventory records are adjusted accordingly, resulting in the recording of actual shrinkage. The retail value of shrinkage included in the retail inventory calculation as of December 31, 20X8, and 20X7, was $0.3 million and $0.4 million, respectively.

330-10-55-17 The following is a tabular example, with qualitative information provided separately, of the required disclosure of the critical assumptions used in applying the retail inventory method.

[For ease of readability, the new table is not underlined.]

	20X8		20X7	
(in millions)	**Cost**	**Retail**	**Cost**	**Retail**
Beginning retail inventory method inventory at January 1,	$ 9.8	$ 13.5	$ 10.2	$ 15.1
Purchases	22.2	31.7	21.4	29.8
Markdowns		(1.0)		(1.2)
Goods available for sale	32.0	44.2	31.6	43.7
Sales		(32.9)		(29.7)
Shrinkage		(0.3)		(0.4)
Total reductions		(33.2)		(30.1)
Other		0.1		(0.1)
Ending retail inventory method inventory at December 31,	$ 8.1	$ 11.2	$ 9.8	$ 13.5

Under the Company's retail inventory method, the valuation of inventories at cost are estimated by applying a calculated cost-to-retail inventory ratio to the retail value of ending inventory at a department level. There are certain judgments and estimates inherent in the retail inventory method calculation that may affect the ending inventory valuation at cost, as well as the gross profit recognized. Those judgments include the approach to grouping products into departments, recording estimated shrinkage in physical inventories, and timely recording of markdowns taken.

Permanent markdowns designated for clearance activity are recorded when the utility of the inventory has diminished. Factors considered in the determination of permanent markdowns include current and anticipated demand, customer preferences, and merchandise age. When a decision is made to permanently mark down merchandise, the resulting gross margin reduction is recognized in the period in which the markdown is recorded.

Physical inventories generally are taken within each merchandise department annually, and inventory records are adjusted accordingly, resulting in the recording of actual shrinkage.

6. Add paragraph 330-10-65-2 and its related heading as follows:

Transition and Open Effective Date Information

> Transition Related to Accounting Standards Update No. 201X-XX, *Inventory (Topic 330): Disclosure Framework—Changes to the Disclosure Requirements for Inventory*

330-10-65-2 The following represents the transition and effective date information related to Accounting Standards Update No. 201X-XX, *Inventory (Topic 330): Disclosure Framework—Changes to the Disclosure Requirements for Inventory:*

a. The pending content that links to this paragraph shall be effective [date to be determined after exposure period].
b. Early adoption of the pending content that links to this paragraph [shall/shall not be] permitted.
c. An entity shall apply the pending content that links to this paragraph prospectively.

Amendments to Subtopic 270-10

7. Amend paragraph 270-10-50-1(i), with a link to transition paragraph 330-10-65-2, as follows:

Interim Reporting—Overall

Disclosure

> Disclosure of Summarized Interim Financial Data by Publicly Traded Companies

270-10-50-1 Many **publicly traded companies** report summarized financial information at periodic interim dates in considerably less detail than that provided in annual financial statements. While this information provides more timely information than would result if complete financial statements were issued at the end of each interim period, the timeliness of presentation may be partially offset by a reduction in detail in the information provided. As a result, certain guides as to minimum disclosure are desirable. (It should be recognized that the minimum disclosures of summarized interim financial data required of publicly traded companies do not constitute a fair presentation of financial position and results of operations in conformity with generally accepted accounting principles [GAAP].) If publicly traded companies report summarized financial information at interim dates (including reports on fourth quarters), the following data should be reported, as a minimum:

i. All of the following information about reportable operating segments determined according to the provisions of Topic 280, including provisions related to restatement of segment information in previously issued financial statements:
    1. Revenues from external customers
    2. Intersegment revenues
    3. A measure of segment profit or loss
    4. Total assets for which there has been a material change from the amount disclosed in the last annual report

4a. Inventory in total and by major component if it meets the criteria in paragraph 280-10-50-25
5. A description of differences from the last annual report in the basis of segmentation or in the measurement of segment profit or loss
6. A reconciliation of the total of the reportable segments' measures of profit or loss to the entity's consolidated income before income taxes and discontinued operations. However, if, for example, an entity allocates items such as income taxes to segments, the entity may choose to reconcile the total of the segments' measures of profit or loss to consolidated income after those items. Significant reconciling items shall be separately identified and described in that reconciliation.

Amendments to Subtopic 280-10

8. Amend paragraphs 280-10-50-25 and 280-10-50-32, with a link to transition paragraph 330-10-65-2, as follows:

Segment Reporting—Overall

Disclosure

> Operating Segments

> > Disclosure Requirements

> > > Information about Profit or Loss and Assets

280-10-50-25 A public entity shall disclose ~~both of~~ the following about each reportable segment if the specified amounts are included in the determination of segment assets reviewed by the chief operating decision maker or are otherwise regularly provided to the chief operating decision maker, even if not included in the determination of segment assets unless otherwise noted below~~assets~~:

a. The amount of investment in equity method investees
b. Total expenditures for additions to long-lived assets other than any of the following (see Example 3, Case B [paragraph 280-10-55-48]):
   1. Financial instruments
   2. Long-term customer relationships of a financial institution
   3. Mortgage and other servicing rights
   4. Deferred policy acquisition costs
   5. Deferred tax assets.
c. **Inventory,** only if such information is reviewed by or regularly provided to the chief operating decision maker by segment (see Example 4 in paragraphs 280-10-55-53 through 55-54):

1. In total. If any portion of inventory is not allocated to a segment, that amount shall be classified as unallocated.
2. By major component (such as raw materials, work-in-process, finished goods, and supplies). If any portion of inventory is not allocated to a segment or to a component, that amount shall be classified as unallocated.

> > > Interim Period Information

280-10-50-32 A public entity shall disclose all of the following about each reportable segment in condensed financial statements of interim periods:

a. Revenues from external customers
b. Intersegment revenues
c. A measure of segment profit or loss
d. Total assets for which there has been a material change from the amount disclosed in the last annual report
dd. Inventory in total and by major component if it meets the criteria in paragraph 280-10-50-25
e. A description of differences from the last annual report in the basis of segmentation or in the basis of measurement of segment profit or loss
f. A reconciliation of the total of the reportable segments' measures of profit or loss to the public entity's consolidated income before income taxes and discontinued operations. However, if a public entity allocates items such as income taxes to segments, the public entity may choose to reconcile the total of the segments' measures of profit or loss to consolidated income after those items. Significant reconciling items shall be separately identified and described in that reconciliation.

9. Add paragraphs 280-10-55-53 through 55-54 and their related headings, with a link to transition paragraph 330-10-65-2, as follows:

Implementation Guidance and Illustrations

> Illustrations

> > Example 4: Inventory Disclosure

> > > Case A: Disaggregation by Component Reviewed by Chief Operating Decision Maker

280-10-55-53 Company X has two reportable segments—Segment A and Segment B. The chief operating decision maker of Company X regularly reviews the inventory balances for each segment, disaggregated by major component. Company X discloses the following.

[For ease of readability, the new table is not underlined.]

	As of December 31, 20X3			
(in thousands)	**Segment A**	**Segment B**	**Unallocated**	**Total**
Raw materials	$ 77	$ 99	$ 15	$ 191
Work-in-process	39	40	1	80
Finished goods	21	51	12	84
Supplies	10	11	3	24
Total inventory	$ 147	$ 201	$ 31	$ 379

> > > Case B: Disaggregation by Segment Only Reviewed by Chief Operating Decision Maker

280-10-55-54 Company H has two reportable segments—Segment Y and Segment Z. The chief operating decision maker of Company H regularly reviews the inventory balances in total for each segment but does not receive or review information about inventory components by segment. The following is an example of the disclosure of segment information that Company H includes in its annual financial statements (in thousands).

> Company H had $170 and $202 of inventory in Segment Y and Segment Z, respectively, as of December 31, 20X3. In addition, Company H had $21 of inventory that was not allocated to either segment as of December 31, 20X3.

The amendments in this proposed Update were approved for publication by five members of the Financial Accounting Standards Board. Messrs. Buck and Smith voted against publication of the amendments. Their alternative views are set out at the end of the basis for conclusions.

Members of the Financial Accounting Standards Board:

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

Background Information, Basis for Conclusions, and Alternative Views

Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this proposed 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 the amendments in this proposed Update as part of the disclosure framework project. The objective and primary focus of the disclosure framework project are to improve the effectiveness of disclosures in the notes to financial statements by facilitating clear communication of the information required by GAAP that is most important to the users of each entity's financial statements. Achieving the objective of improving the effectiveness of the notes to financial statements includes:

a. The development of a framework that promotes consistent decisions by the Board about disclosure requirements
b. The appropriate exercise of discretion by reporting entities.

BC3. In March 2014, the Board issued a proposed Concepts Statement on Chapter 8, *Notes to Financial Statements.* The proposed Concepts Statement is intended to identify a broad range of possible information for the Board to consider when deciding on the disclosure requirements for a particular Topic. From that intentionally broad set, the Board would identify a narrower set of disclosures about that Topic to be required on the basis of an evaluation of whether the benefits to users of financial information justify the costs to entities providing that information. The Concepts Statement, when finalized, would be used by the Board as a basis for establishing disclosure requirements in future accounting standards as well as for evaluating current disclosure requirements.

BC4. The Board decided to test the guidance in the proposed Concepts Statement and improve the effectiveness of disclosure requirements for inventory, income taxes, fair value measurements, and defined benefit pension and other postretirement benefit plans by using those proposed concepts. Proposed guidance on income taxes, fair value measurements, and defined benefit pension and other postretirement benefit plans have been previously exposed for comment. The amendments in this proposed Update are the result of the Board's consideration of the concepts in the proposed Concepts Statement as they relate to inventory disclosures.

BC5. The Board anticipates that entities would incur moderate costs as a result of implementing the amendments in this proposed Update, while the proposed amendments would provide users with beneficial information that would justify those costs. An entity's decision to omit immaterial disclosures (if it had not done so previously) may reduce the entity's total cost of complying with the disclosure requirements, although in certain cases there may be costs incurred to assess whether a disclosure is immaterial.

Background Information

BC6. The current inventory disclosure requirements have developed over time, although there has been little change in recent years. Most of the requirements were established by ARB No. 43, Chapter 4, "Inventory Pricing," and its predecessor standards including ARB No. 29, *Inventory Pricing*. ARB 43 was issued in 1953 and sets forth the general principles applicable to inventories of mercantile and manufacturing enterprises. In addition, the following pronouncements established disclosure requirements specific to certain industries:

a. FASB Statement No. 66, *Accounting for Sales of Real Estate*
b. AICPA Statement of Position 85-3, *Accounting by Agricultural Producers and Agricultural Cooperatives*
c. AICPA Statement of Position 04-2, *Accounting for Real Estate Time-Sharing Transactions*
d. AICPA Audit and Accounting Guide, *Audits of Federal Government Contractors.*

BC7. Cost is a pervasive constraint on information that can be provided by financial reporting. It is important that the benefits of reporting financial information justify the costs. This basis for conclusions explains the reasons why the Board decided that the benefits would justify the costs for certain disclosures, but not for other disclosures.

BC8. In December 2013, the Board issued the *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies*, which assists the Board and the Private Company Council in determining, among other things, whether and in what circumstances to provide alternative disclosure requirements for private companies reporting under GAAP. The Board used the Private Company Decision-Making Framework in conjunction with feedback received from the Private Company Council on the amendments in this proposed Update to determine whether the disclosures discussed as part of the disclosure framework review of inventory should be applied to private companies.

Disclosure Objectives and Immaterial Disclosures

BC9. In September 2015, the Board issued proposed Accounting Standards Update, *Notes to Financial Statements (Topic 235): Assessing Whether Disclosures Are Material,* which is intended to promote the appropriate use of discretion by reporting entities when evaluating disclosure requirements set forth by the Board. Application of the amendments in that proposed Update is intended to result in an entity providing material information while allowing the entity to exclude immaterial information. The amendments in that proposed Update would, among other things, clarify that reporting entities may consider materiality when assessing disclosure requirements for both quantitative and qualitative information similar to any other accounting requirement. The amendments in that proposed Update have been considered by the Board in developing the amendments in this proposed Update. That is, the amendments in this proposed Update:

a. State that an entity need not provide required disclosures if they are immaterial
b. Exclude phrases like *an entity shall disclose at a minimum,* which make it difficult to justify omitting immaterial disclosures
c. Refer readers to Topic 235 (as would be amended by the guidance in the proposed Update on that Topic) for a discussion of the appropriate exercise of discretion.

While included in this proposed Update, those specific amendments are subject to redeliberations following the comment period for the proposed Update on Topic 235.

BC10. In addition, the Board developed the objectives for inventory disclosures in this proposed Update using the relevant decision questions from the proposed Concepts Statement. The objectives are intended to provide insight into why the disclosures were deemed by the Board to be relevant and may assist preparers in exercising discretion when complying with the disclosure requirements.

Scope

BC11. The Board decided to exclude Topic 705, Cost of Sales and Services, from the scope of this project. Although the Board acknowledged that disclosures on cost of sales are linked to inventory disclosures, the Board concluded that a narrow-scope project focusing only on inventory would enable the timelier completion of testing the guidance in the proposed Concepts Statement. Concerns were raised by some Board members, however, that isolating the balance sheet disclosures related to inventory from the corresponding income statement effects is challenging. Furthermore, some Board members raised concerns that many financial statement users would be more interested in improved disclosures on the profit and loss metrics, such as cost of sales, as opposed to improved disclosures on the inventory balance. The Board has a broad project on its current research agenda on inventory and cost of sales that is not limited to disclosures. The Board acknowledges that some of the proposed disclosures also would address the effects of inventory valuation on costs of sales, such as some changes in inventory and last-in, first-out (LIFO) liquidations. However, those proposed disclosures were included from the perspective of their effect on the inventory balance.

BC12. In December 2013, the Board issued Accounting Standards Update No. 2013-12, *Definition of a Public Business Entity—An Addition to the Master Glossary*. The primary purpose of that Update was to amend the Master Glossary of the Codification to include one definition of the term *public business entity* for future use in GAAP. All entities with inventory are within the scope of Topic 330. The Board decided that certain inventory disclosures would be included in Topic 280, which does not use the definition of a public business entity. The Board decided that the segment disclosures for inventory would only apply to those entities within the scope of Topic 280. The Board also decided not to allow any disclosure modifications in Topic 330 for entities that are not public business entities.

Changes in Inventory

BC13. Decision Question L7 of the proposed Concepts Statement indicates that the Board should consider disclosure requirements that provide financial statement users with information about the causes of the changes in an entity's line item, which are not easily understood. The proposed Concepts Statement notes that the cause of changes from the prior period could be summarized in a detailed rollforward. Accordingly, the Board considered a proposed requirement to disclose an annual rollforward of the inventory balance. The Board also considered an approach that would require only specific changes (the specific changes approach) in the inventory balance to be disclosed rather than rolling forward the balance.

BC14. Financial statement users noted there is minimal information available from current disclosure requirements to help them understand the change in an entity's inventory balance from a prior period. To fill this void, some users supported a rollforward of the beginning to ending inventory balance because a rollforward would provide them with helpful information in assessing the inventory balance. Some analysts, particularly those focused on retail entities, were especially supportive of a full rollforward disclosure, stating that a rollforward would provide them with helpful information for refining their analyses of margins and inventory turnover.

BC15. Some other users, generally those who put less emphasis on inventory information, suggested that a full rollforward would be unnecessary and, instead, suggested the specific changes approach. Those users explained that the more incrementally beneficial line items in a rollforward are those that relate to changes in the inventory balance because of events or circumstances outside the normal course of business, which may include inventory acquired in a business combination or the reclassification of inventory to other balance sheet accounts and certain noncash charges such as atypical impairment charges or loss of inventory from significantly higher than normal shrinkage.

BC16. Some Board members stated that a full rollforward of the inventory balance would be the best way to provide the broadest base of financial statement users with information about the causes of the change in the inventory line item. Those Board members noted that a full rollforward would be straightforward and would alleviate concerns about enumerating the specific changes in the balance that should be disclosed in the absence of a full rollforward. They noted that providing only pieces of the change in inventory would place significant costs and burdens on those users that do focus on inventory.

BC17. The Board considered whether to require an inventory rollforward when inventory is significant, since there is a substantial divide between entities for which inventory is core to their business operations and those for which it is not. Some Board members stated that by not requiring a rollforward for these entities, the Board would be disregarding the needs of a significant portion of the user community. However, other Board members noted that creating a rule to define when inventory is important or when a rollforward would be required would be challenging. Furthermore, on the basis of the mixed user input and lack of a clear cost-benefit analysis, the Board was not persuaded to mandate a rollforward.

BC18. Board members who did not support disclosing a full rollforward raised concerns about the potential costs as compared with the anticipated benefits of preparing a rollforward. Many financial statement preparers indicated that their management does not prepare or review inventory by rolling forward the balance. In addition, some Board members raised concerns that discretion would be necessary in determining which line items to include if a full rollforward were required and that such discretion could reduce comparability of the information across companies.

BC19. Although the Board acknowledged that a full rollforward may provide financial statement users with helpful information to refine their inventory analyses, the Board does not have sufficient information to support a conclusion that the expected benefits of a rollforward would benefit a broad enough base of financial statement users to justify the potential costs and decided to require disclosure of certain changes in inventory. However, some Board members recognize that in situations where inventory is a significant asset and changes in inventory are closely monitored by investors, the benefits of a rollforward would likely justify the costs. In those situations, the objective in paragraph 330-10-50-1B could be better met by an entity providing a full rollfoward.

BC20. The Board considered three approaches to refine the wording of the specific changes approach. The first approach would be to impose a principles-based requirement. This could be, for example, a requirement to disclose items that are significant and unusual, noncash, or outside the normal purchase, manufacture, or sale of inventory. Some Board members noted that this principles-based language would prevent important changes in the inventory balance from being excluded from disclosure simply because they are not included in a defined list. However, some Board members expressed concerns about this approach, specifically noting that developing sufficiently broad language to capture the pertinent changes for all companies across all industries could be challenging. In addition, some Board members raised the concern that a principles-based approach may be difficult to implement.

BC21. The second approach would be to list the types of changes in the inventory line item that should be disclosed. Board members supporting this approach said that a specified list of items to be disclosed would enhance comparability across companies and would be more operable than applying principles-based language. Some Board members expressed concern that important changes in the inventory balance may be excluded solely because they are not included on the prescribed list.

BC22. The third approach is a hybrid of the first two approaches. Under this approach, the disclosure requirement would (a) include a principles-based requirement to disclose items that are outside the normal purchase, manufacture, or sale of inventory and (b) provide a list of specific items that should be disclosed if applicable to the entity. Board members supporting this approach stated that it would alleviate some of the implementation concerns by making clear those items that are expected to be disclosed, while also providing for the disclosure of relevant changes in the inventory balance not explicitly included on the prescribed list. In addition, some Board members believe that it would be easier to apply this approach to a broader range of scenarios. The Board decided to propose the hybrid approach and has included a list of potential transactions, circumstances, and events that should be considered for disclosure but does not limit disclosure to these items.

BC23. The Board also decided that the changes disclosed under this requirement would be those that are outside the ordinary course of business. For example, estimates of loss because of slow moving inventory or shrinkage, which are consistent with experience in the ordinary course of business, would not need to be disclosed. However, losses because of an abnormally large drop in demand or amount of shrinkage would be considered for disclosure.

Disaggregation of Inventory

BC24. Decision Question L4 of the proposed Concepts Statement indicates that the Board should consider disclosure when a line item includes components of different natures that could affect prospects for net cash flows differently. Additionally, the proposed Concepts Statement states that the Board should consider disclosure when a line item includes individual items (or groups) that are measured differently. The Board considered the following possible ways to disaggregate inventory in the notes to the financial statements:

a. By segment
b. By component
c. By age
d. By geographical location
e. By measurement basis.

Segment and Component

BC25. The Board considered user feedback that disaggregation of inventory by component can be informative when there are increases or decreases in certain components of inventory. The Board noted that the costs of this disclosure requirement should be minimal because public companies are required to disaggregate inventory by class (similar to component) under Rule 5-02 of Regulation S-X of the U.S. Securities and Exchange Commission (SEC). In addition, feedback from financial statement preparers indicated that most public and some private companies already disaggregate inventory by component or in a similar manner.

BC26. The Board also considered a proposed requirement to disclose inventory disaggregated by segment. The Board agreed with financial statement users that disaggregation of inventory by segment would be helpful because it could (a) provide greater insight into gross margins, (b) help users analyze a company's inventory in a manner similar to how management does so, and (c) focus on specific areas or products that may be of interest to a user. Furthermore, the Board agreed with financial statement users that inventory by segment disclosures would be even more useful if further disaggregated by component.

BC27. The Board acknowledged financial statement preparers' concerns that some products or components might not be specifically identified with a particular segment, necessitating allocation or disclosure of an unallocated amount. The Board proposes to address this issue by requiring disclosure of the unallocated amount.

BC28. The Board considered two approaches to disclose inventory disaggregated by segment and component. The first approach would require disclosure only if reviewed by, or otherwise regularly provided to, the chief operating decision maker. Under this approach, the disclosure requirements would be added to Topic 280 rather than to Topic 330. Board members who favored this approach stated that when the chief operating decision maker focuses on these items, the information also is more likely to be decision useful to financial statement users. Board members opposed to this approach expressed the concern that comparability across entities would be reduced.

BC29. The second approach would require that all entities disclose inventory disaggregated by segment and component. Board members preferring this approach believe that it would improve comparability across entities. Board members opposing this approach expressed concern about the potential added cost to entities whose chief operating decision maker does not already review or regularly receive that information.

BC30. The Board decided that it would be most meaningful to users and least costly to preparers to require disclosure of inventory by segment (and further by component within each segment) only if this information is reviewed by, or regularly provided to, the chief operating decision maker as outlined in Topic 280.

Age

BC31. The Board considered a requirement to disclose inventory disaggregated by age because some users indicated that inventory age is critical to their inventory analyses, particularly in the retail industry. Although the Board recognized the potential usefulness of this information to financial statement users for certain types of inventory, some Board members acknowledged that crafting guidance capable of yielding a disaggregation of inventory by age, which is meaningful within and across companies and industries, would be challenging. Furthermore, allowing companies discretion in how to disaggregate their inventory by age would substantially reduce comparability and the usefulness of the disclosure for financial statement users. In addition, some Board members expressed concern that such a disaggregation might not be operable for many types of inventory. Certain items with exceptionally short or long lives, for example, would be difficult if not impossible to track and record by age. Finally, some Board members believe that requiring the disaggregation of inventory by age would not provide broadly relevant information and would, therefore, be unduly burdensome.

Geographical Location

BC32. The Board also considered a requirement to disclose inventory disaggregated by geographical location and noted the following:

a. Some public and private company financial statement users said that knowledge of the geographical location of inventory could help confirm management assertions about the source of inventory problems and identify potential backlog in the supply chain.
b. Some users stated that an “in transit” category in such a disaggregation could provide useful information about inventory buildups, changes in shipping terms, or increases in purchases to address growth prospects.
c. Some private company users expressed that geographical location information is important in lending decisions because the ability to liquidate inventory upon default may vary depending on its physical location.

BC33. Board members had mixed views about the potential usefulness of the disclosure of inventory disaggregated by geography but agreed that disaggregating inventory by segment and component provides more useful information. One Board member noted that if geographical location is critically important, that information may already be provided in the company's segment disclosures. Some Board members also raised concerns about the operability of the requirement; for example, it could be difficult to identify the level of granularity of the geographical breakdown.

BC34. Several Private Company Council members noted, and the Board acknowledged, that lenders likely demand more timely information outside the financial statements about inventory used as collateral. They also noted that inventory held outside the United States might not be used as collateral if concerns exist about access.

Measurement Basis

BC35. The Board decided to require disclosure of the measurement basis used, as well as the amount of inventory measured, under each different basis. Topic 235, which requires disclosure of a description of significant accounting policies, specifies that inventory pricing is a disclosure that commonly would be required, but a requirement to disclose the amount of inventory measured under each method does not currently exist. Outreach indicated that some users may not be aware that an individual company may use different inventory methods for various portions of its inventory.

BC36. Requiring companies to disclose the amount measured under each basis may facilitate users' evaluation of the comparability of inventory balances across companies. The Board expects that this information is generally readily available to management because it is integral to operating an entity.

BC37. Topic 330 currently requires disclosure of inventories stated above cost or at sales prices. The Board noted that the guidance is broad and provides no incremental information beyond the Topic 235 requirement to state the basis of measuring inventories. Furthermore, measuring inventory above cost or at selling price is a measurement basis, which would be included in the proposed disclosure of the measurement bases used and amounts of inventory under each measurement basis. Accordingly, the Board eliminated the existing Topic 330 disclosure requirement.

Retail Inventory Method (RIM)

BC38. Another area of inventory that the Board considered under Decision Question L7 of the proposed Concepts Statement is the RIM. Additionally, decision Question L14 of the proposed Concepts Statement indicates that the Board should consider disclosure when the carrying amount of the line item is an estimate that requires assumptions, judgments, or other internal inputs that could reasonably have been different. The calculation of inventory under the RIM is not directly based on the cost of inventory, and changes in the inventory balance may not be easily understood without further disclosure of the assumptions used in the RIM calculation. The Board also noted that the mechanics of the RIM calculation are not as well understood as some other inventory costing methods.

BC39. Some users noted that the complexity and subjectivity of the RIM calculations complicate users' analyses of RIM inventory. Users in the retail industry said that more insight into the RIM may be useful, but some users acknowledged that any disclosure sufficient for understanding a company's application of the RIM may be too complex and detailed to be practical.

BC40. The Board noted that the type of RIM applied is useful information for users and should be included in the proposed requirement to disclose inventory disaggregated by measurement basis.

BC41. The Board acknowledged that detailed information about the RIM would likely be useful to only those users with a deep understanding of the model. The Board also acknowledged concern from preparers that some information included in the RIM calculation was proprietary. However, the Board noted that disclosing the critical assumptions included in the calculation of ending inventory under the RIM would enhance transparency. Additionally, qualitative information about those assumptions would help users understand how managements' assumptions affect the inventory balance.

BC42. The Board considered requiring disclosure of only certain pieces of the retail inventory calculation but ultimately decided that more complete qualitative and quantitative disclosure of the critical assumptions would be more beneficial to users. The Board decided not to prescribe a disclosure format but to allow management to choose an appropriate format for its entity. The disclosure could take the form of a presentation of the entire RIM calculation or a description of the critical components of the calculation.

BC43. The Board noted that this disclosure is not expected to change an entity's application of the RIM but should reflect the specifics of that application. The Board acknowledged that entities may use different assumptions or calculations in their application of the RIM. For example, one entity may define shrinkage as only missing products, while another may include damaged or spoiled goods or price changes in the shrinkage amount. These nuances in how an entity is calculating the cost of inventory under the RIM should be considered for disclosure.

Capitalized Costs

BC44. The Board decided to require qualitative disclosure of the types of costs capitalized in inventory. Some users pointed out that the lack of information currently available on the types of costs capitalized in inventory hinders their ability to analyze, compare, and ask questions of entities. Some users indicated that a qualitative description of the costs capitalized could address the deficiency.

BC45. Some Board members raised the concern that the disclosure might become “boilerplate” and be of limited use, but other Board members believe it would be a useful starting point for comparison analysis. Such analysis could serve as a catalyst for users to ask questions of management, particularly if the nature of capitalized costs changed over time or differed across companies in the same industry. Additionally, Board members agreed that the proposed required disclosure should not be unduly burdensome to prepare because the information should be readily available to management.

LIFO Liquidation

BC46. Another requirement considered in light of Decision Question L7 is disclosure of the effect of a LIFO inventory liquidation on income.

BC47. Disclosure of the effect of a LIFO liquidation is required by the SEC, but many non-SEC filing entities follow the recommendations in the November 30, 1984 AICPA Issues Paper, *Identification and Discussion of Certain Financial Accounting and Reporting Issues Concerning LIFO Inventories* (AICPA LIFO Paper) and disclose this information as well. The Board decided to require the disclosure for all entities, because many entities already provide this disclosure and the information is important to users.

Replacement Cost for Inventories Measured Using LIFO

BC48. Decision Question L15 of the proposed Concepts Statement indicates that the Board should consider disclosure when an alternative measure or way of applying a measurement is clearly incrementally useful in assessing prospects for cash flows. This led the Board to consider a requirement to disclose the replacement cost of inventories measured at LIFO.

BC49. Because the LIFO inventory cost reported in a company’s balance sheet often does not represent the current cost of the inventory, Regulation S-X already requires public companies to disclose the excess of replacement cost over LIFO cost. The AICPA LIFO Paper also discusses whether companies should disclose the difference (often represented by the “LIFO reserve”) between LIFO cost and cost determined by some other acceptable inventory costing method (such as first-in, first-out [FIFO] or average cost). The Board decided to require this disclosure for all entities, because many public and nonpublic companies already disclose the information and this disclosure would provide insight into an entity’s prospects for future cash flows.

BC50. While this proposed requirement would create redundancy with SEC guidance, adding the requirement to Topic 330 would extend the requirement to all companies applying GAAP and would enhance the decision usefulness of inventory disclosures. The Board agreed with those users that noted that this disclosure would be appropriate as a required disclosure in Topic 330.

Disclosure of Significant Estimates

BC51. Inventory balances can include a number of estimates, such as estimated selling prices for lower of cost and net realizable value adjustments, estimated impairment because of the deterioration or obsolescence of goods, estimated shrinkage, and markup or markdown estimates used in the RIM calculations. This led the Board to evaluate existing and potential new disclosure requirements of estimates and judgments under Decision Question L14 of the proposed Concepts Statement.

BC52. Existing guidance on significant estimates in Topic 330 (which is moved from paragraph 330-10-50-6 to paragraph 330-10-50-11 in this proposed Update) references Topic 275, Risks and Uncertainties, and requires the disclosure of significant estimates. Topic 330 also provides an example of how to apply the risk and uncertainty disclosure guidance to inventory. During staff outreach, many financial statement preparers stated that the disclosure requirements in Section 275-10-50 are sufficient to ensure adequate disclosure of situations and circumstances giving rise to risk and uncertainty and significant estimates. The financial statement users that commented on the disclosure of significant estimates did not identify any additional information that would be useful for their analyses. The Board concluded that the example on the application of risks and uncertainties provided in Topic 330 is helpful and that no additional disclosure requirements are necessary.

Losses on Firm Purchase Commitments

BC53. Topic 330 includes a requirement for separate income statement presentation of losses on firm purchase commitments. Acknowledging that it was outside the scope of this project, the Board discussed whether separate presentation on the face of the income statement was necessary and concluded that the existing requirement provides useful information for financial statement users. The Board noted that the elimination of this requirement could reduce transparency and visibility into the location of such losses within the income statement. The Board decided to leave the existing requirement unchanged.

Other Disclosures Considered but Not Proposed by the Board

Inventory Subject to Royalty and Other Arrangements

BC54. Decision Question O3 of the proposed Concepts Statement indicates that the Board should consider disclosure when contractual rights or obligations arising from past transactions and events or current conditions and circumstances exist that are expected to meet the criteria for recognition in the future. This led the Board to consider disclosure of the existence of royalty or other arrangements that will obligate the entity to incur expenses upon the sale of items in inventory subject to those arrangements.

BC55. Some Board members raised a concern that such a requirement might equally pertain to other arrangements (for example, sales commission arrangements), which also obligate the entity to incur expenses upon sale of items in inventory subject to those arrangements. Relatedly, some Board members said that such a requirement pertains to cost of goods sold rather than inventory and is, therefore, beyond the scope of this project.

BC56. Some Board members also contemplated whether royalty and other similar arrangements should be considered for disclosure under Topic 440, Commitments; however, they acknowledged that no explicit guidance exists in that Topic for royalty arrangements.

Inventory on Consignment

BC57. Decision Question L3 of the proposed Concepts Statement indicates that the Board should consider disclosure when the existence or ownership of the rights and obligations underlying the line item could be uncertain. The Board acknowledged that such rights could be uncertain when consignment arrangements are present. Various types of consignment arrangements exist and each counterparty's rights and obligations with respect to the inventory could vary depending on the arrangement. In addition, inventory on consignment is physically located with the consignee, and the timing of recognition or derecognition by the consignor often depends on actions of the consignee. Accordingly, there could be uncertainties about its existence. This led the Board to consider a requirement to disclose the amount of inventory on consignment and the nature of the consigned inventory.

BC58. The Board questioned the pervasiveness and materiality of consignment arrangements. Some Board members also questioned the usefulness of the disclosures because they believe that the information would be most useful when consigned inventory is used as collateral, in which case lenders would be expected to have alternative means of obtaining more timely information directly from the entity. Consequently, the Board decided against requiring this disclosure.

Inventory Pledged As Collateral

BC59. The Board noted that the SEC requires disclosure of all assets subject to lien; however, GAAP only requires disclosure of certain financial assets pledged as collateral. As such, the Board considered whether to add a requirement to disclose inventory pledged as collateral. The Board decided not to add a specific requirement for inventory because this would not fully address the broader issue of assets pledged as collateral.

Alternative Inventory Measurement Methods

BC60. The Board considered a requirement to disclose inventory measured at fair value, net realizable value, or market value as another potential alternative measure that would be useful in assessing prospects for future cash flows (see Decision Question L15 of the proposed Concepts Statement).

BC61. The Board received conflicting feedback from stakeholders. Some analysts said that such alternative inventory measures may be helpful in estimating an entity's future cash flows and making assumptions about future margins. Nevertheless, other users and some financial statement preparers expressed reservations about the reliability of the information, since the alternative measurements would necessitate the use of broad subjective estimates. Some users and preparers also noted the potential for competitive harm, although the Board observed that any potential effect would be mitigated by the level of aggregation of the disclosure.

BC62. The Board concluded that while a proposed disclosure of inventory measured under other methods may yield information useful in assessing prospects for future cash flows, the potential benefits to users would not justify the perceived costs—both in terms of preparation costs and potential loss of proprietary data. The Board, therefore, decided not to require this disclosure.

Modifications to Existing Inventory Disclosures

Consistent Application of the Measurement Basis

BC63. The Board decided to supersede paragraph 330-10-50-1 (as it appears in current GAAP), which requires that an entity apply the basis of stating inventories consistently. The Board noted that this guidance pertains to the measurement of inventory and not to its disclosure and is redundant with paragraph 330-10-30-15 in the Initial Measurement Section of Topic 330. The Board also noted that any inconsistencies in the application of the measurement basis would be apparent through the requirement in paragraph 330-10-50-9 of this proposed Update to disclose inventory disaggregated by the measurement basis.

Changes in Measurement Basis

BC64. The Board superseded the current guidance in Topic 330 relating to a change in measurement basis because it is redundant with guidance in Topic 250, Accounting Changes and Error Corrections. The Board also noted that other Topics within the Codification that are subject to accounting changes do not have similar disclosure requirements about changes to the measurement basis. Additionally, the guidance in Topic 250 is more robust than the current Topic 330 disclosure requirement.

Standard Costs

BC65. The Board noted that, by definition, standard costs must reasonably approximate costs computed under one of the recognized bases. The Board also noted that whether an entity uses standard costs was not identified as an area of concern by users. Accordingly, the Board determined that the current requirement to use "descriptive language" to express the relationship between standard costs and one of the recognized bases is unnecessary and could be eliminated.

Interim Disclosures

BC66. The Board considered which of the proposed disclosures, if any, should be required on an interim basis. For all proposed disclosures, other than disaggregation of inventory by segment and component, the Board determined that the provisions for interim disclosures in Topic 270, Interim Reporting, and in paragraphs D63 and D64 of the proposed Concepts Statement should apply such that an entity should disclose the following on an interim basis:

a. Differences from the most recent annual financial statements in the recognition, measurement, or presentation of inventory
b. How the financial position and results of operations for the interim period relate to the entire year (for example, seasonal inventory levels)
c. Significant changes in financial position that are unclear.

BC67. The Board considered user feedback indicating that inventory disaggregated by segment and component would be important on an interim basis for user trend and turnover analyses. Although some Board members believe that a requirement to disaggregate inventory in this manner at interim periods would be inconsistent with the principles in the proposed Concepts Statement and those established in Topic 280, the Board decided that if information about inventory is used by the chief operating decision maker, the segment disclosure should be made for both interim and annual periods.

Considerations for Entities Other Than Public Business Entities

BC68. The Board evaluated each of the proposed disclosure requirements under the Private Company Decision-Making Framework to assess whether any differences in disclosure requirements were warranted for private companies. The Board noted that not-for-profit companies with inventory would likely face similar resource constraints and that users of their financial statements would have similar needs to those of private companies. Additionally, the Board noted that employee benefit plans generally do not have inventory. Therefore, the Board concluded that disclosure differences determined using the Private Company Decision-Making Framework, if any, should apply to all entities other than public business entities to which Topic 330 applies.

BC69. The Board determined that entities not subject to the existing guidance in Topic 280 should not be required to apply the segment guidance for inventory. The Board noted that because most entities other than public business entities are not subject to the segment reporting requirements in Topic 280, such a disclosure would be costly to those entities to prepare. Furthermore, the Board acknowledged feedback from some users of private company financial statements that said that they would not find this information useful.

BC70. The Board also considered whether disclosure of current factors affecting the cost, availability, or utility of inventory should only be required for entities other than public business entities. Feedback, specifically from the users of private company financial statements, indicated that additional information on inventory risks and uncertainties would be useful. The Board noted, however, that much of the requested information should be provided under Topic 275. Moreover, some of that information might be included in a public business entity’s Management Discussion and Analysis and would not be appropriate for inclusion in the notes to financial statements.

Effective Date and Transition

BC71. The amendments in this proposed Update would be applied prospectively. Retrospective application would improve the comparability of financial information across all periods presented; however, the Board concluded that the benefit of greater comparability would not justify the additional cost.

BC72. The Board will determine the effective date and whether early adoption should be permitted after it considers stakeholder feedback on the amendments in this proposed Update.

How Do the Proposed Provisions Compare with International Financial Reporting Standards (IFRS)?

BC73. IAS 2, *Inventories*, outlines the inventory disclosure requirements for companies reporting under IFRS. The amendments in this proposed Update would result in differences in disclosures between GAAP and IFRS. The International Accounting Standards Board did not base its disclosures on the application of the concepts in the proposed Concepts Statement.

Benefits and Costs

BC74. The objective of financial reporting is to provide information useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. 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.

BC75. The Board anticipates that most entities would incur moderate costs to implement the amendments in this proposed Update and that the beneficial information provided to users would justify those costs. An entity's decision to omit immaterial disclosure (if it had not done so previously) may reduce the entity's total cost in complying with the disclosure requirements, although there may be costs incurred to assess whether a disclosure is immaterial. In many cases, the proposed disclosures are expected to utilize readily available information, further mitigating the cost in those situations.

Alternative Views

BC76. While Messrs. Buck and Smith agree with many of the improvements in disclosures about inventory included in the amendments in this proposed Update, they disagree with the issuance of the proposed amendments because they disagree with the proposed disclosures specifically targeted to the RIM. Messrs. Buck and Smith do not believe that the benefits of providing the disclosures about the RIM justify the costs because they do not believe that the Board has adequately identified the benefits. While they acknowledge that the RIM disclosures will provide users with more information, it is unclear how that information will be used.

BC77. Messrs. Buck and Smith are particularly concerned about the requirement to disclose the cost-to-retail margin, which, in turn, would enable users to determine the gross margin expected to be earned on the future sales of inventory recorded under the RIM. Entities that use other methods of inventory are not required to disclose expected gross margins, and Messrs. Buck and Smith do not believe that it is appropriate to require entities using the RIM to make that disclosure. Board members who support the issuance of the amendments in this proposed Update support the disclosure because it is a key determination of the recorded value of inventory. Messrs. Buck and Smith believe that the RIM is simply a mechanism to estimate the cost of the inventory, just as there are estimates used in valuing inventory at FIFO, average cost, LIFO, and so on, yet the details of those calculations used in the other methodologies are not required to be disclosed. Messrs. Buck and Smith believe that any proposed disclosures of expected gross margin would be more suitable for Management's Discussion and Analysis rather than footnotes to the financial statements, mainly because of the potential for unintended litigation consequences if reporting entities fail to achieve those margins upon the eventual sale of the inventory.

Amendments to the XBRL Taxonomy

The provisions of this Exposure Draft, if finalized as proposed, would require changes to the U.S. GAAP Financial Reporting Taxonomy (Taxonomy). We welcome comments on these proposed changes to the Taxonomy through ASU Taxonomy Changes provided at www.fasb.org. After the FASB has completed its deliberations and issued a final Accounting Standards Update, proposed amendments to the Taxonomy will be made available for public comment at www.fasb.org and finalized as part of the annual release process.