Don’t roll the DISE on the FASB’s expense disaggregation project

September 2023

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Feedback from investors on our 2021 Agenda Consultation provided us with a fresh approach to providing more detailed information about a company’s expenses, which investors have said is critically important to understanding a company’s performance, assessing its prospects for future cash flows, and comparing its performance over time and with that of other companies.

FASB Chair Rich Jones
July 31, 2023

The need for additional disaggregated financial information was a resounding theme from investors weighing in on the FASB’s 2021 agenda consultation process. Today, there is little guidance on the expense categories that should be presented in a company’s income statement, unless otherwise prescribed by SEC guidance or industry-specific rules. Investors have consistently asked for additional details about income statement expenses, which they believe are important to understanding a company’s performance and forecasting future cash flows.

In response to this feedback, the FASB issued an exposure draft[1] on July 31, 2023 that would require additional disaggregation of income statement expenses (referred to as DISE). The scope and impact of the proposed amendments are far reaching. The proposal would not change or add to the expense captions a company currently presents in its income statement. However, it would require new tabular footnote disclosures that provide additional detail about the amounts included in existing expense captions. The proposed amendments would also require the separate disclosure of selling expenses.

The FASB designed the proposed amendments to be industry-agnostic by focusing on specific categories of expenses likely to be relevant for most companies, including employee compensation, depreciation, and amortization expense. The categories are also among those identified as the highest priority in investor feedback to the FASB and generally align with the expense categories that would be required by the new International Accounting Standards Board (IASB) standard on primary financial statements, expected to be issued in 2024.

Under the proposed amendments, the new disclosures would be required in both interim and annual financial statements. Companies would apply the new requirements on a prospective basis, with an option to apply them retrospectively by providing comparable information for prior periods.

The FASB has preliminarily determined that the scope of the proposed amendments would be limited to public business entities. However, depending on the feedback received on the proposal – especially from private company financial statement users – the FASB may revisit this scoping decision. Therefore, it is important for all companies to stay up to date on developments related to this project.

The comment period for the exposure draft closes on October 30. Given the scope of the proposed amendments, we encourage all stakeholders to get engaged in the standard setting process and to begin assessing the potential impacts now.

[1] FASB’s proposed Accounting Standards Update, Disaggregation of Income Statement Expenses.

Proposed disclosure requirements

1. **Disclose in a table in the financial statement footnotes the amount of the following categories of expenses included in each relevant expense caption presented in the income statement:[2]**

   (1-a) inventory and manufacturing expense

   (1-b) employee compensation

   (1-c) depreciation

   (1-d) intangible asset amortization

   (1-e) depreciation, depletion, and amortization recognized as part of oil- and gas-producing activities

2. **Include within the same table provided under (1) certain amounts that are already required to be disclosed under existing generally accepted accounting principles.**

3. **Disclose in a table in the financial statement footnotes a further disaggregation of inventory and manufacturing expense (1-a) into the following categories of costs incurred:[3]**

   (3-a) purchases of inventory

   (3-b) employee compensation

   (3-c) depreciation

   (3-d) intangible asset amortization

   (3-e) depreciation, depletion, and amortization recognized as part of oil- and gas-producing activities

4. **Provide a qualitative description of the amounts remaining ("other") in relevant expense captions or in inventory and manufacturing expense that are not separately disclosed quantitatively.**

5. **Disclose the total amount of selling expenses and, on an annual basis, an entity's definition of selling expenses.**

[2] A "relevant expense caption" is defined as an expense caption presented on the face of the income statement within continuing operations that contains at least one of the types of expenses listed in 1-a to 1-e below.
[3] Costs incurred would include those that are either capitalized in inventory or expensed as incurred during the current period. On an annual basis, an entity would disclose its definition of other manufacturing expenses.

> We used investor input to redefine and focus a path forward on our project on financial performance reporting, revising its objective and scope to focus on disaggregation of income statement expenses.
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> FASB 2021 Agenda Consultation Report

Key questions as you consider the potential impact

Because the FASB specifies the categories of expenses that would require disclosure, the impact of the proposed amendments will vary depending on the extent of current disaggregation presented by companies or industry practices. For example, a manufacturing company that currently presents income statement expense captions such as cost of goods sold and selling, general, and administrative expenses will likely be required to provide significantly more detailed expense information. Conversely, a financial institution that already separately presents salaries and employee benefits (or similar caption) pursuant to SEC requirements may not be significantly impacted.

Regardless of industry, we expect that all companies would be required to provide some level of additional disclosure. We have highlighted five questions that companies should consider as they evaluate the potential impact of the proposed amendments.

What data is currently available and what additional information would be needed to comply with the proposed amendments?

A first step in assessing the impact of the proposed amendments is taking stock of the data currently available and assessing whether changes will be needed to how data is collected and aggregated. Companies that do not currently aggregate data in the categories prescribed by the proposed amendments will need to assess the steps necessary to bridge those gaps. This may be more challenging for companies that will need to compile information from disparate systems or those with decentralized operations or significant intercompany transactions.

Companies that hold inventory or have significant manufacturing activities will need to further evaluate their ability to disaggregate costs incurred related to inventory and manufacturing expenses. The FASB decided to focus this disaggregation requirement on costs incurred during the period rather than a disaggregation of expenses recorded in the income statement in an attempt to make this requirement more operable. Despite the FASB's efforts, companies may find this aspect of the proposal particularly challenging.

What system and process changes would be required?

After evaluating the need for additional information, companies may find they will need to implement system changes or new automated solutions. The extent of system changes needed will vary across companies; however, for some it will be a time-consuming effort and could require coordination with other planned system updates. Further, all companies will need to consider the impact to their reporting processes and internal controls. Input from preparers on the extent of potential system and process changes and the expected time and effort required to make these changes will be important to inform the FASB's cost-benefit analysis as well as decisions about the effective date of the new requirements.

How would the new disclosures impact other communications with investors?

For many companies, the proposed amendments would require details of expenses that have not previously been provided to investors. This additional level of detail may impact how management describes its financial results within management's discussion and analysis (MD&A) in SEC filings as well as press releases and other communications with investors and analysts. Coordination with investor relations will be important to plan for any changes to communications, get in front of potential questions, and avoid surprises.

What transition method would the company choose to adopt the new requirements?

While the proposed amendments allow for prospective application of the new requirements, companies should consider stakeholder expectations when determining their adoption policy. Despite not being required, some companies may want to provide comparative information in anticipation of questions that may arise from users or as support for additional discussion with MD&A or other communications. As compiling data for comparative periods may require additional time and effort, companies should consider the implications to their implementation timeline. This will also be important feedback to the FASB as they finalize the effective date of the new requirements.

Are there alternatives the FASB could consider that achieve the objective of providing decision-useful information to investors?

Companies may also want to consider providing feedback to the FASB on alternatives they believe would make the proposed requirements more operable, while achieving the overall objectives of the project. In particular, the proposal asks for input on potential practical expedients that would simplify or reduce the costs associated with disaggregating inventory and manufacturing expense without significantly diminishing the decision usefulness of the information provided.

What's next?

The exposure draft will remain open for comment until October 30, followed by a public roundtable on December 13. The FASB will then consider stakeholders' feedback, make final decisions about the new requirements, and determine the effective date.

The FASB has set a clear objective to respond to investors' calls for additional disaggregation of income statement expenses. Companies should keep this goal in mind as they provide feedback on the proposal. Input from the preparer community will be important to inform the FASB's final decisions about the disclosure requirements as well as the effective date.

Companies should not wait for a final standard to begin assessing the steps needed to comply with the new requirements. Depending on a company's specific facts and circumstances, new system or process changes may be required, as well as coordination across geographies and business segments. Gaining an understanding of the implications early on will be key to planning for a successful implementation once the rules are finalized.

For more information about the DISE project, listen to our podcast, Getting ahead of the FASB project on expense disaggregation, DISE.

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