



Disaggregation of income statement expenses (DISE)

Issues In-Depth

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Contents

Foreword.....	1
Acknowledgments	2
About this publication	3
1. Scope, overview and timing.....	5
2. Relevant expense captions	18
3. Natural expenses defined	26
4. How to apply the disaggregation requirements.....	52
5. Disclosure requirements and tabular disclosure.....	80
6. Selling expenses	94
7. Effective date and transition	99
8. Illustrative disclosures.....	109
Additional resources	119
KPMG Financial Reporting View	120

Expense disclosures, season 3

Continuing the FASB's recent efforts to enhance expense transparency for investors – starting with ASU 2023-07 on segment reporting and following with ASU 2023-09 on income tax disclosures – the third installment in this trilogy is upon us.

Enter ASU 2024-03, focused on expense disaggregation disclosures. While it does not alter the look of the income statement (no new line items or subtotals), it requires public business entities to peel back the layers of certain expense captions in the notes. The goal? Greater clarity into how companies operate and spend – driven by natural expense categories – with the intent to promote comparability across entities.

Calendar-year entities will premier these disclosures in their 2027 annual financial statements, with interim disclosures following in 2028.

In this publication, we provide an overview of the relevant accounting guidance and spotlight our preliminary views on some of the unique and challenging considerations and fact patterns that can arise when analyzing the expense disaggregation disclosure requirements.

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About this publication

The purpose of this Issues In-Depth is to assist public business entities in applying the requirements in ASU 2024-03, codified in Subtopic 220-40, relative to expense disaggregation disclosures.

Organization of the text

Each chapter of this Issues In-Depth includes excerpts from the *FASB Accounting Standards Codification*® (ASC) and overviews of the relevant FASB and SEC requirements for expense disaggregation disclosures. Our in-depth guidance is explained through Q&As that reflect the questions we encounter in practice. We include examples to explain key concepts.

Our commentary is referenced to the Codification, SEC regulations, FASB Accounting Standards Updates and to other literature, where applicable. The Codification refers to the FASB ASC, which excludes SEC regulations, whereas US GAAP refers to the FASB ASC and SEC regulations, collectively. The following are examples:

- 220-40-50-1 is paragraph 50-1 of ASC Subtopic 220-40.
- ASU 2024-03.BC125 is paragraph 125 of the basis for conclusions to ASU 2024-03.
- CON 8.D73 is paragraph D73 of FASB Concepts Statement No. 8.
- S-X Rule 210.9-04 is Rule 210.9-04 of SEC Regulation S-X.
- TQA 5210.02 is section 5210.02 of the AICPA's Technical Questions and Answers.

Pending content

This Issues In-Depth incorporates Codification amendments from Accounting Standards Update No. 2025-06, Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40). These amendments are applicable to all entities and are effective for annual and interim reporting periods in fiscal years beginning after December 15, 2027.

Abbreviations

We use the following abbreviations in this Issues In-Depth.

AICPA	American Institute of Certified Public Accountants
ARO	Asset retirement obligation
ASU	Accounting Standards Update
COGS	Cost of goods sold
DD&A	Depreciation, depletion and amortization
EGC	Emerging Growth Company
FIFO	First-in, first-out

FPI	Foreign private issuer
GAAP	Generally accepted accounting principles
IPO	Initial public offering
LIFO	Last-in, first-out
MD&A	Management's Discussion and Analysis
NCI	Noncontrolling interest
NFP	Not-for-profit (entity)
PBE	Public business entity
PP&E	Property, plant and equipment
PPV	Purchase price variance
R&D	Research and development
RIM	Retail inventory method
ROU	Right-of-use (asset)
SG&A	Selling, general and administrative expenses
USD	US dollar
VIE	Variable interest entity
WIP	Work in progress

1. Scope, overview and timing

Detailed contents

1.1 How the standard works

1.2 Scope

Question

Question 1.2.10 When might Subtopic 220-40 be relevant to a private company?

1.3 Main provisions

Questions

Question 1.3.10 What are the main provisions of Subtopic 220-40?

Question 1.3.20 Does Subtopic 220-40 establish any new income statement presentation requirements?

Question 1.3.30 How does Subtopic 220-40 interact with the segment reporting requirements?

Question 1.3.40 Does Subtopic 220-40 affect MD&A disclosure requirements?

1.4 Frequency

Questions

Question 1.4.10 What are the differences between the required disclosures for annual and interim periods?

Question 1.4.20 Are interim disclosures required for both quarter-to-date and year-to-date interim periods?

1.5 Change in display of the disclosures

Questions

Question 1.5.10 What happens when an entity changes the display of a disclosure?

Question 1.5.20 How are changes in display assessed in interim periods?

1.1 How the standard works

Subtopic 220-40 requires public business entities (PBEs) to disclose specific expense information in the notes to the financial statements. The Subtopic does not create new or modify existing presentation requirements and therefore is not intended to change the layout of the income statement.

Scope

Subtopic 220-40 applies to all PBEs, including small reporting companies and entities whose financial statements are included in another entity's SEC filings. It does not apply to private companies, not-for-profit entities and certain employee benefit plans. However, private companies that expect to become PBEs in the future may need to consider the effect of adopting these requirements.

Main provisions and frequency

Subtopic 220-40 requires two broad new financial statement disclosures:

- disaggregated information about specific types of expenses (called 'required natural expense categories') included in any income statement caption that meets the definition of a 'relevant expense caption'; and
- quantitative and qualitative information about selling expenses – a management-defined measure.

Main provisions	Annual financial statements	Interim financial statements
Relevant expense captions identified for disaggregation	Required	Required Condensed interim financial statements may produce different relevant expense captions than annual financial statements
Required natural expense categories disclosed separately for each relevant expense caption (in tabular format)	Required	Required
Additional categories disclosed and other US GAAP disclosures reported in same tabular format for each relevant expense caption (one-stop-shop approach)	Required	Required to the extent other US GAAP disclosures are required in interim periods
Selling expenses disclosed (amounts and description)	Required	Amounts: required Description: required only if changed during the interim period

Change in display of the disclosures

Although Subtopic 220-40 should be applied consistently for all periods presented, it explicitly addresses the following two types of changes:

- the election of an alternative provided by Subtopic 220-40 (e.g. the ability to choose to disaggregate inventory amounts under a cost-incurred or expense-incurred basis – see [section 4.5](#)); and
- the definition of a disclosure (e.g. change in the definition of selling expenses).

When making such changes, an entity discloses the reasons for the change and recasts prior periods presented for comparative purposes (unless impracticable).

Changes in display caused by changes in facts and circumstances do not require recasting but may need to be explained.

1.2 Scope

Excerpt from ASC 220-40

05-1 This Subtopic provides guidance on the disaggregation disclosure requirements for certain expense captions presented on the face of an entity's income statement. This Subtopic also provides guidance on the disclosure of selling expenses.

> Overall Guidance

15-1 This Subtopic has its own discrete scope, which is separate and distinct from the pervasive scope for this Topic as outlined in Section 220-10-15.

> Entities

15-2 The guidance in this Subtopic applies to all public business entities.

15-3 The guidance in this Subtopic does not apply to the following entities:

- a. **Private companies**
- b. **Not-for-profit entities**
- c. Employee benefit plans within the scope of any of the following Topics:
 1. Plan Accounting—Defined Benefit Pension Plans (Topic 960)
 2. Plan Accounting—Defined Contribution Pension Plans (Topic 962)
 3. Plan Accounting—Health and Welfare Benefit Plans (Topic 965).

20 Glossary

Public Business Entity

A public business entity is a business entity meeting any one of the criteria below. Neither a **not-for-profit entity** nor an employee benefit plan is a business entity.

- a. It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).
- b. It is required by the Securities Exchange Act of 1934 (the Act), as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency other than the SEC.
- c. It is required to file or furnish financial statements with a foreign or domestic regulatory agency in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer.
- d. It has issued, or is a conduit bond obligor for, **securities** that are traded, listed, or quoted on an exchange or an over-the-counter market.
- e. It has one or more securities that are not subject to contractual restrictions on transfer, and it is required by law, contract, or regulation to prepare U.S. GAAP financial statements (including notes) and make them publicly available on a periodic basis (for example, interim or annual periods). An entity must meet both of these conditions to meet this criterion.

An entity may meet the definition of a public business entity solely because its financial statements or financial information is included in another entity's filing with the SEC. In that case, the entity is only a public business entity for purposes of financial statements that are filed or furnished with the SEC.

The requirements of Subtopic 220-40 apply to all PBEs, including small reporting companies, EGCs, and nonissuers that are required to file or furnish financial statements with or to the SEC (e.g. broker dealers). [\[220-40-15-2, ASU 2024-03.BC32\]](#)

The term PBE also includes entities whose financial statements or financial information are included in another entity's SEC filings (e.g. S-X Rule 3-05 financial statements). [\[220-40 Glossary\]](#)

The requirements do not apply to private companies, not-for-profit entities, or employee benefit plans in the scope of Topics 960, 962 or 965. [\[220-40-15-3\]](#)

Question 1.2.10 When might Subtopic 220-40 be relevant to a private company?

Interpretive response: Although private companies are excluded from the scope, a private company that expects to meet the definition of a PBE in the future may need to consider the effects of adopting and complying with Subtopic 220-40's requirements. Significant time and effort may be required to comply with the requirements. This is particularly important for a private company that is:

- considering an initial public offering and would need to apply the requirements when preparing its registration statement;
- considering issuing public debt;
- acquired by an SEC registrant and is required to file or furnish financial statements with the SEC under S-X Rule 3-05; and
- an unconsolidated subsidiary or 50% or less owned by an SEC registrant and is required to file or furnish financial statements with the SEC under S-X Rule 3-09.

1.3 Main provisions

Excerpt from ASC 220-40

> Overall Guidance

50-1 The objective of the disclosure requirements in this Section is to provide disaggregated information about a **public business entity's** expenses to help investors:

- a. Better understand the entity's performance
- b. Better assess the entity's prospects for future cash flows
- c. Compare an entity's performance over time and with that of other entities.

In addition, the disclosure requirements are intended to provide information about the relative proportion and trends of each category of expense identified in paragraph 220-40-50-6 in relation to the corresponding income statement expense caption amount in order to meet the overall objective described above. An entity shall consider the level of detail necessary to satisfy the disclosure objective and specific requirements of this Subtopic. An entity may use estimates or other methods that produce a reasonable approximation of the amounts required to be disclosed by this Subtopic.

50-2 This Section includes the following (all of which apply only to expenses in continuing operations):

- a. Required expense categories to be disclosed, identification of relevant expense captions, and practical expedients (see paragraphs 220-40-50-6 through 50-20)
- b. Tabular integration of other disclosure requirements (see paragraphs 220-40-50-21 through 50-25)
- c. Disclosure of expense reimbursements included in a relevant expense caption (see paragraphs 220-40-50-26 through 50-29)
- d. An amount and qualitative description of the composition of other items remaining in relevant expense captions (see paragraph 220-40-50-30)
- e. Disclosure of the disaggregation of relevant expense captions that contain amounts within the scope of Topic 330 on inventory (see paragraphs 220-40-50-31 through 50-34)
- f. Requirements related to selling expenses (see paragraphs 220-40-50-35 through 50-36).

Subtopic 220-40 intends to help financial statement users navigate the diversity in practice regarding the composition and naming conventions of expense captions presented in the income statement, in order to better understand and assess entities' cost structures, performance and prospects for future cash flows. It does this by requiring disclosure of common operating expenses (i.e. required categories) that make up certain income statement expense captions. Subtopic 220-40 is a disclosure standard; therefore, it does not create new or modify existing income statement line items or presentation requirements and does not intend to change the layout of the income statement. [\[ASU 2024-03.BC2 – BC4, BC125\]](#)

Question 1.3.10 What are the main provisions of Subtopic 220-40?

Interpretive response: Subtopic 220-40 requires new financial statement disclosures in tabular format, disaggregating information about specific types of expenses (called 'required natural expense categories') presented in any 'relevant income statement expense caption'. Further, it integrates certain existing required disclosures under the Codification into the new tabular disclosure. Information about selling expenses is also required, separate from the tabular disclosure. [\[220-40-50-2\]](#)

The main provisions are summarized as follows.

Main provisions	Highlights
Relevant expense captions identified for disaggregation (see chapter 2)	A functional or natural expense line item in the income statement within continuing operations containing expenses from any required natural expense category
Required natural expense categories disclosed separately for each relevant expense caption (in tabular format) (see chapter 3)	• Purchases of inventory • Employee compensation • Depreciation • Intangible asset amortization • Depreciation, depletion and amortization (DD&A) for oil-and-gas producing activities or other amounts of depletion expense
Additional categories disclosed and other US GAAP disclosures reported in same tabular format for each relevant expense caption (see chapters 4 and 5)	• Certain expense reimbursements • Specific expenses, gains and losses required to be disclosed by other Codification Topics and Subtopics • Other items (residual amount and composition) • Changes in inventories, <i>if applicable</i> • Other adjustments and reconciling items (amount and composition), <i>if applicable</i>
Selling expenses disclosed (see chapter 6)	• Total amount of selling expenses • Description of the composition of this 'management' defined measure (annual only, unless changed during interim period)

Question 1.3.20 Does Subtopic 220-40 establish any new income statement presentation requirements?

Interpretive response: No.

Subtopic 220-40 does not create any new line items or subtotals and does not intend to change the functional categorization of line items. Instead, the incremental disaggregated expense information is disclosed in the notes to the financial statements and is considered an extension of an entity's income statement. [[220-40-50-1](#), [ASU 2024-03.BC125](#), [BC127](#)]

If an entity determines a change to its income statement presentation is warranted upon going through the process to adopt Subtopic 220-40, it should consider the guidance in Topic 250. See KPMG Handbook, [Accounting changes and error corrections](#).

Question 1.3.30 How does Subtopic 220-40 interact with the segment reporting requirements?

Interpretive response: These two sets of requirements are not designed to significantly interact unless the chief operating decision maker (CODM) is provided with natural expense categories or selling expenses by segment. Subtopic 220-40 and Topic 280 (segment reporting) both require disaggregated expense disclosures; however, the requirements differ in their scope and methods.

Topic 280 requires the disclosure of significant segment expenses that are regularly provided to the chief operating decision maker and included within each reported measure of a segment's profit or loss, using the management approach. See KPMG Handbook, [Segment reporting](#), for more information on Topic 280.

In contrast, Subtopic 220-40 requires the disclosure of specified natural expense categories included within relevant expense captions of the income statement (see [chapter 2](#)). Therefore, the disclosure is at the entity level rather than at the segment level. Further, these categories are based on Codification definitions, i.e. a management approach is not applied for this disclosure. A management approach is however applied for the disclosure of selling expenses (see [chapter 7](#)), which could therefore overlap with the segment disclosures, but only where selling expenses are provided to the CODM at the segment level and considered a significant segment expense under Topic 280. Accordingly, the expense information and amounts provided for segment reporting may differ from the expense information and amounts provided for Subtopic 220-40. [\[ASU 2024-03.BC150 – BC153\]](#)

Question 1.3.40 Does Subtopic 220-40 affect MD&A disclosure requirements?

Interpretive response: Not directly.

Subtopic 220-40 does not create any new MD&A disclosure requirements under SEC Regulation S-K Item 303. However, given the nature of the disaggregated information provided, the Subtopic 220-40 disclosures may be complementary or additive to an entity's MD&A disclosures by providing detailed and specific contextual information regarding certain expense components of the income statement and ultimately the entity's results of operations. [\[ASU 2024-03.BC5\]](#)

Given some of the interconnectedness between the disaggregated disclosures and MD&A, entities should ensure that the information is consistent, where appropriate, between the two sections and with other related information. Because of this, the new disclosures may affect what is discussed in MD&A over time.

1.4 Frequency

Excerpt from ASC 220-40

> Overall Guidance

50-3 The requirements in this Section apply to interim and annual reporting periods, except for the requirement to disclose how an entity defines selling expenses (see paragraph 220-40-50-36), which only applies to annual reporting periods (or interim reporting periods if the definition is changed). An entity is required to include the disclosures listed in paragraphs 220-40-50-21 through 50-22 in a tabular format disclosure for interim reporting purposes only if the disclosure requirements referenced in those paragraphs are required in interim reporting periods by the guidance in other Topics.

Subtopic 220-40 disclosure requirements apply in both interim and annual reporting periods. Providing the information this frequently and on a periodic basis affords users more visibility into an entity's performance and allows investors to update their expectations of an entity's major expense activity. [220-40-50-3, ASU 2024-03.BC25(e)]

Question 1.4.10 What are the differences between the required disclosures for annual and interim periods?

Interpretive response: The disclosures in Subtopic 220-40 are required in both annual and interim periods, with a few caveats as noted in the table below.

Main provisions	Required?		Clarification of interim period requirements
	Annual	Interim	
Relevant expense captions identified for disaggregation (see chapter 2)	✓	✓	If an entity presents condensed interim financial statements as permitted under S-X Rule 210.8-03 and Rule 210.10-01, the income statement line items may be different at interim and annual reporting periods. Determination of the relevant expense captions is based on the line items presented for the period and whether those expense captions include required natural expense categories. This may lead to different relevant expense captions between interim and annual periods. [220-40-50-5, ASU 2024-03.BC129]
Required natural expense categories disclosed separately for each relevant expense caption (in	✓	✓	

Main provisions	Required?		Clarification of interim period requirements
	Annual	Interim	
tabular format (see chapter 3)			
Additional categories disclosed and other US GAAP disclosures integrated in same tabular format for each relevant expense caption (see chapters 4 and 5)	✓	✓	The requirement to integrate other US GAAP disclosures applies <i>only</i> if the disclosure is required in interim reporting periods under other Topics or Subtopics (see Question 5.2.40). This may lead to a different display of the tabular disclosure between interim and annual periods. [220-40-50-3, 220-40-50-21 – 50-22]
Selling expenses disclosed (see chapter 6)			The description of the composition of selling expenses is provided in an interim reporting period <i>only</i> if the definition has changed in that period. [220-40-50-3, ASU 2024-03.BC121]
• Amounts	✓	✓	
• Description	✓	✗	

Question 1.4.20 Are interim disclosures required for both quarter-to-date and year-to-date interim periods?

Interpretive response: Yes.

Although not explicitly stated in Subtopic 220-40, we believe both the quarter-to-date and year-to-date periods are subject to the disclosure requirements for interim reporting periods. [220-40-50-3]

For example, for a calendar year-end entity, Q2 financial statements include an income statement for the three- and six-month periods ended June 30. The entity would present the disaggregated disclosures and the amount of selling expenses for both the three- and six-month periods ended June 30.

1.5 Change in display of the disclosures

Excerpt from ASC 220-40

> Overall Guidance

50-4 The disclosure requirements in this Section shall be applied consistently for all periods presented. If an entity changes its display of the disclosure requirements in the current reporting period as a result of a change in the election of an alternative or a change in a definition of a disclosure in this Section, the entity shall:

- Disclose the reason for the change in the period of the change (in the interim and annual reporting periods affected by the change)

- b. Recast the prior periods presented for comparative purposes, except for the requirements in paragraphs 220-40-50-22 through 50-23, unless it is impracticable to do so. If it is impracticable to do so, the entity shall disclose that fact and explain why it is impracticable to recast prior periods.

Changes described in this paragraph do not represent a change in accounting principle in accordance with Topic 250 on accounting changes and error corrections.

50-5 Some entities provide condensed statements for interim reporting periods and, therefore, present different expense captions on their income statements at annual and interim reporting periods. For an entity that provides condensed statements for interim reporting periods, the guidance in paragraph 220-40-50-4 is applicable in instances in which an entity changes its display of the disclosure requirements for the current interim reporting period compared with the prior interim reporting period or in instances in which the entity changes its display of the disclosure requirements for the current annual reporting period compared with the prior annual reporting period.

• > Tabular Integration of Other Disclosure Requirements

50-23 If there is a change in facts and circumstances that results in an item listed in paragraph 220-40-50-22 changing from being included in one relevant expense caption in the current reporting period and multiple relevant expense captions in a comparative period, or vice versa, an entity shall provide the disclosure required by paragraph 205-10-50-1.

Excerpt from ASC 205-10

> Changes Affecting Comparability

50-1 If, because of reclassifications or for other reasons, changes have occurred in the manner of or basis for presenting corresponding items for two or more periods, information shall be furnished that will explain the change. This procedure is in conformity with the well-recognized principle that any change in practice that affects comparability of financial statements shall be disclosed.

The disclosure requirements in Subtopic 220-40 apply consistently for all periods presented. However, an entity may need or elect to change its display of the disclosures in the current reporting period under specific circumstances. [\[220-40-50-4\]](#)

Subtopic 220-40 specifically states that the following two types of changes in display are not considered a change in accounting principle subject to the requirements of Topic 250: [\[220-40-50-4\]](#)

- the election of an alternative provided by Subtopic 220-40; and
- the definition of a disclosure.

Subtopic 220-40 also specifically addresses how certain changes in facts and circumstances may affect the disclosures and points to the general disclosure requirements in Subtopic 205-10 for changes affecting comparability. [\[220-40-50-23, 205-10-50-1\]](#)

Question 1.5.10 What happens when an entity changes the display of a disclosure?

Interpretive response: It depends.

An entity should first evaluate the reason for the change in display to understand whether Subtopic 220-40 provides specific guidance. This analysis is necessary to determine whether the change needs to be applied retrospectively to all periods presented.

Changes in display specifically addressed in Subtopic 220-40

Subtopic 220-40 specifically addresses the following changes in display. [220-40-50-4]

Nature of the change	Examples
Change in the election of an alternative provided by Subtopic 220-40	- Change between the two acceptable disclosure approaches for expense reimbursements received from another entity (see section 4.4). - Change between the two acceptable bases for disclosing the disaggregation of a relevant expense caption that contains amounts related to inventory (see section 4.5). [ASU 2024-03.BC69]
Change in the definition of a disclosure	Change in the definition of selling expenses (see Question 6.2.50). [ASU 2024-03.BC121]

These changes do not represent a change in accounting principle under Topic 250, because they represent a change in the display of a disclosure and are not a presentation, measurement or recognition change. Therefore, the entity does not need to demonstrate that the change is preferable. Instead, the following requirements apply. [220-40-50-4, ASU 2024-03.BC124]

- Disclose the reasons for any changes made in the period of the change.
- Recast prior periods presented for comparative purposes, unless it is impracticable to do so. If impracticable, disclose this fact and why it is impracticable to recast prior periods.

Changes in facts and circumstances

Nature of the change	Examples
Specified expenses, gains and losses already required for disclosure under US GAAP start or cease to be included in only one relevant expense caption and start or cease to be reported separately in the tabular disclosure for that caption as a result (see Question 5.2.30)	Loss contingency amounts recorded only in COGS in prior periods, which is determined to be a relevant expense caption (see chapter 2), but recorded across COGS and SG&A in the current period. Because loss contingencies are only required to be disclosed in the disaggregated disclosures if included entirely within one expense caption (see Question 5.2.20), this category ceases to be disclosed.

Nature of the change	Examples
Expense category starts or ceases to be present and starts or ceases to be disclosed as a result	R&D is determined to be a relevant expense caption (see chapter 2), and R&D activities are entirely outsourced in the period and employee compensation costs are no longer incurred. This required natural expense category ceases to be disclosed in the disaggregation of R&D.

Changes in facts and circumstances do not require recasting of prior periods presented. Subtopic 220-40 points to the general disclosure requirements in Subtopic 205-10 for changes affecting comparability, when the change relates to a change in facts and circumstances such as specified amounts disclosed under existing Codification requirements (see [Question 5.2.30](#)). As a result, an entity discloses the reasons for any changes made in the period of the change. [\[220-40-50-23\]](#)

Question 1.5.20 How are changes in display assessed in interim periods?

Interpretive response: The guidance explained in [Question 1.5.10](#) applies similarly to changes in display in annual and interim periods. However, assessing whether a change in display in an interim period requires specific recasting and/or disclosures may require more judgment than for annual periods when the entity issues condensed interim financial statements (see [Question 1.4.10](#)). In this case, the entity compares disclosures for relevant comparative periods – i.e. comparing the current and prior interim reporting periods instead of simply comparing the current interim period to the most recent annual reporting period. [\[220-40-50-5\]](#)

2. Relevant expense captions

Detailed contents

2.1 How the standard works

2.2 Relevant expense caption defined

Questions

Question 2.2.10 Are all income statement line items considered relevant expense captions?

Question 2.2.20 What expense captions in continuing operations are generally not expected to be relevant expense captions?

Question 2.2.30 Is an income statement line item a relevant expense caption solely because it contains items required to be disclosed under other Codification Topics or Subtopics?

2.3 Exceptions and practical expedients

Questions

Question 2.3.10 Is disaggregation required for line items related to equity method investments?

Question 2.3.20 Is disaggregation required if an expense caption consists entirely of one required natural expense category?

Question 2.3.30 Is disaggregation required if substantially all of an expense caption represents purchases of inventory?

Question 2.3.40 Are banks and bank holding companies that apply S-X Rule 210.9-04 required to disaggregate salaries and employee benefits?

2.1 How the standard works

The first step in complying with Subtopic 220-40 is to identify the relevant expense captions in the income statement that will require disaggregation in the note disclosure.

Relevant expense captions

Relevant expense captions are income statement line items in continuing operations that contain the following required natural expense categories:

- purchases of inventory;
- employee compensation;
- depreciation;
- intangible asset amortization; and
- DD&A or other depletion expense.

Common examples of relevant expense captions are cost of sales, SG&A and R&D. Relevant expense captions vary by entity and industry.

Exceptions

The following expense captions are exempt from the disaggregation requirements:

- an expense caption for the entity's share of profit or loss in an equity method investee; and
- expense captions consisting entirely of one required natural expense category (e.g. a depreciation line item that comprises only depreciation expense as defined by Topic 360 (PP&E)).

Practical expedients

Optional practical expedients are available for certain expense captions.

- When 'substantially' all of an expense caption comprises purchases of inventory, disaggregation is not required, but a qualitative description of the composition should be provided.
- Banking entities applying Reg S-X Rule 210.9-04 can use 'salaries and employee benefits' in lieu of the defined term 'employee compensation' for disaggregation purposes.

2.2 Relevant expense caption defined

Excerpt from ASC 220-40

> Overall Guidance

- > Expense Disaggregation Disclosures
- • > Identification of Relevant Expense Captions

50-12 For the purposes of applying the guidance in this Subtopic, a relevant expense caption is an expense caption presented on the face of the income statement in continuing operations that contains any of the expenses listed in paragraph 220-40-50-6 (including those described in paragraphs 220-40-50-10 through 50-11)....

- > Tabular Integration of Other Disclosure Requirements

50-24 The presence of the expenses, gains, and losses listed in paragraphs 220-40-50-21 through 50-22 would not cause an expense caption to be a relevant expense caption....

A relevant expense caption is an expense caption presented on the face of the income statement in continuing operations that contains any of the expense categories required by Subtopic 220-40 (i.e. the 'required natural expense categories'). These expense categories are: [\[220-40-50-6\]](#)

- purchases of inventory
- employee compensation
- depreciation
- intangible asset amortization
- depreciation, depletion and amortization of capitalized acquisition, exploration, and development costs recognized as part of oil- and gas-producing activities (DD&A) or other amounts of depletion expense.

The presence of ROU asset amortization for a finance lease or leasehold improvement amortization in an income statement expense caption will subject the caption to disaggregation because these amounts are a subset of either the depreciation or intangible asset amortization required category (see [Question 3.5.20](#)). [\[ASU 2024-03.BC38\]](#)

See [chapter 3](#) for more detailed information on the required natural expense categories. [\[220-40-50-12\]](#)

Question 2.2.10 Are all income statement line items considered relevant expense captions?

Interpretive response: No.

A relevant expense caption is only an income statement line item in continuing operations that contains any of the natural expense categories required for

disaggregation. Although relevant expense captions are not identified or defined by their name presented on the face of the income statement, it is generally expected that entities will identify cost of sales, SG&A and R&D (and similarly named expense captions in the income statement) as relevant expense captions due to the likely presence of at least one of the required natural expense categories. The determination of relevant expense captions will vary by entity and industry. [ASU 2024-03.BC39 – BC42]

Discontinued operations as a line item is not a relevant expense caption, because the requirements of Subtopic 220-40 only apply to line items in continuing operations. Discontinued operations are subject to the disclosure requirements in Subtopic 205-20. See chapter 7 in KPMG Handbook, [Discontinued operations and held-for-sale disposal groups](#). [220-40-50-2]

Question 2.2.20 What expense captions in continuing operations are generally not expected to be relevant expense captions?

Interpretive response: Examples of expense captions in continuing operations that are generally not expected to be relevant expense captions include interest expense and income tax expense, because these captions typically do not contain any of the required natural expense categories. Additionally, for banking entities, provision for credit losses, data processing and professional fees are not expected to be relevant expense captions due to their nature. However, the determination of relevant expense captions is ultimately dependent on an entity's specific facts and circumstances. [220-40-55-5, 55-15, 55-22]

Question 2.2.30 Is an income statement line item a relevant expense caption solely because it contains items required to be disclosed under other Codification Topics or Subtopics?

Interpretive response: No.

The existence in an income statement line item of expenses, gains and losses required to be disclosed by other Topics and Subtopics does not make the line item a relevant expense caption subject to disaggregation in the notes. This is true even if the item to be disclosed is listed by Subtopic 220-40 as an item that would be required to be reported separately in the tabular disclosure if the line item were a relevant expense caption (see [Question 5.2.20](#)). Instead, the determination is solely based on whether the income statement line item contains any of the required natural expense categories (see [Question 2.2.10](#)). [220-40-50-24]

2.3 Exceptions and practical expedients

Excerpt from ASC 220-40

> Overall Guidance

- > Expense Disaggregation Disclosures
- • > Identification of Relevant Expense Captions

50-12 ...A relevant expense caption that consists entirely of one expense category listed in paragraph 220-40-50-6 is not subject to the requirements of this Subtopic. For example, if depreciation is a relevant expense caption on the income statement and the caption consists entirely of depreciation in accordance with paragraph 220-40-50-6(c), no additional disclosure is required because the information in the income statement satisfies the disclosure requirements in this Subtopic. In contrast, if the relevant expense caption comprises depreciation and intangible asset amortization, an entity would be required to separately disclose depreciation and intangible asset amortization in accordance with paragraph 220-40-50-6(c) through (d), respectively. ...

50-13 An entity's share of earnings or losses from investments accounted for under the equity method in accordance with paragraph 323-10-45-1 is not a relevant expense caption for purposes of applying the guidance in this Subtopic. Additionally, an entity is not required to further disaggregate its disclosure of summarized information of results of operations of investments accounted for under the equity method in accordance with paragraph 323-10-50-3(c).

- • > Practical Expedient for Purchases of Inventory

50-19 As a practical expedient, when substantially all of an entity's income statement expense caption comprises purchases of inventory as described in paragraph 220-40-50-7, the entity is not required to apply the guidance in paragraph 220-40-50-6 to that caption. An entity that applies this practical expedient shall disclose a qualitative description of the composition of the expense caption in interim and annual reporting periods.

- • > Practical Expedient for Employee Compensation

50-20 As a practical expedient for determining what amounts are classified as employee compensation in paragraph 220-40-50-6(b), an entity that presents an expense caption for salaries and employee benefits (or a similarly named caption) on the face of its income statement to comply with the requirements in SEC Regulation S-X Rule 210.9-04, Statements of Comprehensive Income (see paragraph 942-220-S99-1), may use the amounts classified as salaries and employee benefits in accordance with SEC Regulation S-X Rule 210.9-04 rather than in accordance with the definition of employee compensation included in this Subtopic.

Subtopic 220-40 provides relief from the disaggregation requirements in the form of exceptions and practical expedients, as follows.

Exceptions	Entity's share of profit or loss in an equity method investee
	Expense caption that consists entirely of one required natural expense category
Practical expedients (optional)	Expense caption that consists of substantially all purchases of inventory
	Use of amounts classified as salaries and employee benefits under Reg S-X Rule 210.9-04 in lieu of the definition of employee compensation included in Subtopic 220-40

Question 2.3.10 Is disaggregation required for line items related to equity method investments?

Interpretive response: No.

Subtopic 220-40 states that an entity's share of earnings or losses from investments accounted for under the equity method (i.e. equity in earnings) is not a relevant expense caption and is therefore excluded from the disaggregation requirements. [220-40-50-12 – 50-13]

Based on the nature of this exception, we believe that related equity method investment income statement line items such as gain or loss on disposal of an equity method investment or impairments of an equity method investment also are not relevant expense captions and therefore are excluded from the disaggregation requirements.

The separate disclosure of summarized information of results of operations of equity method investments is also not subject to the disaggregation requirements. [220-40-50-12 – 50-13, ASU 2024-03.BC28(d)]

Question 2.3.20 Is disaggregation required if an expense caption consists entirely of one required natural expense category?

Interpretive response: No.

A relevant expense caption that consists entirely of one required natural expense category is not subject to the disaggregation requirements.

To illustrate, if 'depreciation' is a relevant expense caption on the face of the income statement and consists entirely of depreciation expense (see [section 3.5](#)), no further disaggregation is required. However, if this caption includes both depreciation expense *and* intangible asset amortization expense, disaggregation is required to separately disclose each of these required natural expense categories. [220-40-50-12]

Question 2.3.30 Is disaggregation required if substantially all of an expense caption represents purchases of inventory?

Interpretive response: No.

As a practical expedient, when substantially all of an income statement expense caption comprises purchases of inventory, that caption does not need to be disaggregated. Instead, a qualitative description of the composition of the expense caption is provided in both interim and annual reporting periods. [220-40-50-19]

The term 'substantially all' is not defined in Subtopic 220-40 but should be applied consistently with how it is applied in other areas of the Codification. 'Substantially all' is generally understood to mean approximately 90%. For example, Topic 842 (leases) provides guidance that 90% might be appropriate for evaluating 'substantially all' when performing the lease identification and classification evaluations (see section 3.3.3 of KPMG Handbook, [Leases](#)). [ASU 2024-03.BC80, 842-10-55-2(c)]

For example, in certain sectors entities present expense captions on the face of the income statement, such as 'purchases' or 'purchases of materials', that primarily comprise purchases of inventory (see [section 3.3](#)) but also include a small amount of other non-inventory purchases. If substantially all of the line item comprises purchases of inventory, the practical expedient is available to align with the exemption for a relevant expense caption comprising entirely one of the required natural expense categories (see [Question 2.3.20](#)). This practical expedient provides some relief for preparers as long as qualitative context is also disclosed regarding what is included in the expense caption, such as purchases of raw materials inventory, finished goods inventory and purchases of PP&E. [ASU 2024-03.BC79 – BC81]

This practical expedient is limited to purchases of inventory. For example, it would not provide relief if substantially all of a caption is inventoriable costs under Topic 330 (inventory), because inventoriable costs may include labor, depreciation and other expense categories that require disaggregation. The relationship between purchases of inventory and inventoriable costs is discussed in [Question 3.3.10](#).

Question 2.3.40 Are banks and bank holding companies that apply S-X Rule 210.9-04 required to disaggregate salaries and employee benefits?

Interpretive response: No.

Banking entities are generally required to comply with Reg S-X Rule 210.9-04 and present a caption on the face of the income statement for 'salaries and employee benefits' (or a similarly named caption). Given the SEC requirement, such entities that present 'salaries and employee benefits' (or a similarly named caption) are not required to apply the definition of employee compensation included in Subtopic 220-40 and therefore do not have to disaggregate this

caption. The amounts classified under each definition are not expected to be substantially different. [220-40-50-20, ASU 2024-03.BC96]

Use of this practical expedient is limited to those entities that apply S-X Rule 210.9-04 and should not be applied by analogy by entities not subject to S-X Rule 210.9-04.

See FASB Example 3 (reproduced in [section 8.3](#)). [220-40-55-21]

3. Natural expenses defined

Detailed contents

3.1 How the standard works

3.2 Overview

Questions

Question 3.2.10 What is the difference between 'natural' and 'functional' expense categorization?

Question 3.2.20 Can a required natural expense category be further disaggregated?

3.3 Purchases of inventory

Questions

Question 3.3.10 What is the relationship between purchases of inventory, inventoriable costs, inventory expenses and manufacturing expenses?

Question 3.3.20 What constitutes purchases of inventory under Subtopic 220-40?

Question 3.3.30 Are all amounts of inventory recognized from external transactions considered purchases?

Question 3.3.40 How are intercompany and intra-entity purchases considered?

Examples

Example 3.3.10 Inventory recognized through business combination

Example 3.3.20 Intercompany and intra-entity purchases

3.4 Employee compensation

Questions

Question 3.4.10 How is 'employee' defined under Subtopic 220-40?

Question 3.4.20 Do all individuals commonly referred to as employees meet the definition?

Question 3.4.30 How is employee compensation defined under Subtopic 220-40?

Question 3.4.40 Can subsidized goods or services provided to employees be included in employee compensation?

Question 3.4.50 Can one-time employee termination benefits be included in employee compensation?

Question 3.4.60 Can amounts provided to nonemployees be included in employee compensation?

Question 3.4.70 Is total employee compensation incurred in a period disaggregated in the tabular disclosure?

Example

Example 3.4.10 Disaggregation of employee compensation capitalized or accrued

3.5 Depreciation

Questions

Question 3.5.10 How is depreciation defined under Subtopic 220-40?

Question 3.5.20 Is the amortization of finance lease ROU assets and leasehold improvements included in depreciation or intangible assets amortization?

Question 3.5.30 Is depreciation of capitalized asset retirement costs associated with an ARO included in depreciation?

Question 3.5.40 Is total depreciation incurred in a period disaggregated in the tabular disclosure?

3.6 Intangible asset amortization

Questions

Question 3.6.10 How is intangible asset amortization defined under Subtopic 220-40?

Question 3.6.20 What are examples of assets outside Subtopic 350-30's scope?

Question 3.6.30 Is the amortization of capitalized internal-use software costs included in depreciation or intangible asset amortization?

Question 3.6.40 Is total intangible asset amortization incurred in a period disaggregated in the tabular disclosure?

3.7 DD&A

Questions

Question 3.7.10 How is DD&A defined under Subtopic 220-40?

Question 3.7.20 Are amounts for DD&A required to be disclosed separately from amounts for other depletion expense?

Example

Example 3.7.10 Disaggregation of DD&A

3.1 How the standard works

All relevant expense captions within continuing operations in the income statement are disaggregated into the natural expense categories listed in the table below. This disaggregation is through a tabular disclosure in the financial statement notes. To reconcile the aggregate required expenses with the totals in a relevant expense caption, any other expenses, gains or losses in the caption are either:

- reported separately in the table if subject to other US GAAP disclosure requirements (see [section 5.2](#));
- voluntarily disaggregated (see [section 5.3](#)); or
- aggregated into an 'other items' category in the table.

Required natural expense categories	Key requirements and definitions
Purchases of inventory	• Includes the cost of externally purchased materials and other tangible items that are in the scope of Topic 330, or the scope of an Industry Subtopic in Topic 330.
Employee compensation	• Includes compensation costs as outlined in Topics 710, 712, 715 and 718 (e.g. wages, bonuses, social security contributions, benefits and stock compensation). • 'Employee' is defined to align with Topic 718. It can be, but is not limited to, full-time, part-time, temporary or seasonal. • One-time employee termination benefits provided to employees who are involuntarily terminated are presented as a separate line item from regular employee compensation.
Depreciation	• Includes amounts recorded for long-lived assets under Topic 360.
Intangible asset amortization	• Includes amounts recorded for assets capitalized under Topic 350. • Excludes amortization of other capitalized assets (e.g. customer contract acquisition costs under Subtopic 340-40).
DD&A for oil-and-gas producing activities and depletion	• Includes amortization of costs of proved properties and costs of wells and related equipment and facilities recognized under Subtopic 932-360 for entities in the oil-and-gas industry. • Includes amounts not recognized as a part of oil-and-gas producing activities (e.g. mining entities subject to Topic 930).

Many income statements are presented using a functional categorization of expenses; therefore, there could be an extensive list of natural expenses for each relevant expense caption. To balance the cost and benefits of the disaggregation requirements, the FASB decided to limit the natural expense categories required to be disaggregated to five categories. Using a limited number allows for more standardized, consistent and comparable disclosures between PBEs.

3.2 Overview

Excerpt from ASC 220-40

> Overall Guidance

• > Expense Disaggregation Disclosures

50-6 For interim and annual reporting periods, an entity shall disaggregate, in a tabular format disclosure in the notes to financial statements, all relevant expense captions (see paragraphs 220-40-50-12 through 50-13 for guidance on identifying relevant expense captions) presented on the face of the income statement in continuing operations into the following expense categories:

- a. Purchases of **inventory** (see paragraph 220-40-50-7)
- b. **Employee compensation** (disclosing separately any **one-time employee termination benefits**, if applicable, see paragraph 220-40-50-21(e))
- c. Depreciation (for separate requirement to disclose depreciation expense for the period in total, see paragraph 360-10-50-1(a))
- d. **Intangible asset** amortization (for separate requirement to disclose intangible asset amortization expense for the period in total, see paragraph 350-30-50-2(a)(2))
- e. Depreciation, depletion, and amortization of capitalized acquisition, exploration, and development costs recognized as part of **oil- and gas-producing activities** (see Subtopic 932-360 on extractive activities—oil and gas—property, plant, and equipment) or other amounts of depletion expense (see paragraph 220-40-50-11).

20 Glossary

Natural Expense Classification

A method of grouping expenses according to the types of economic benefits received in incurring those expenses. Examples of natural expense classifications include salaries and wages, employee benefits, nonemployee professional services, supplies, interest expense, rent, utilities, and depreciation.

All relevant expense captions (see [chapter 2](#)) are disaggregated in a tabular note disclosure into the following required natural expense categories:

- purchases of inventory – see [section 3.3](#);
- employee compensation – see [section 3.4](#);
- depreciation – see [section 3.5](#);
- intangible asset amortization – see [section 3.6](#); and
- DD&A – see [section 3.7](#).

‘Employee’ and ‘employee compensation’ are defined terms in the ASC Master Glossary (see [section 3.4](#)). The other terms for required natural expense categories are not specifically defined in the ASC Master Glossary. Therefore, judgment may be needed, including looking to other existing disclosure requirements and other guidance, to determine which cost-generating activities are associated with these required natural expense categories. [\[ASU 2024-03.BC89 – BC90\]](#)

When a caption includes purchases of inventory, the entity can elect between two approaches to disaggregate amounts related to inventory in that caption (see [section 4.5](#)).

The disaggregation by natural expense categories is novel and intended to assist investors in understanding an entity's cost structure, as most entities categorize their expenses by function in their income statements, which often leads to multiple types of natural expenses being aggregated in one income statement line.

Question 3.2.10 What is the difference between 'natural' and 'functional' expense categorization?

Interpretive response: Natural expenses are categorized based on the types of economic benefits obtained from the expenditure. Said differently, natural expenses describe the type of cost incurred without consideration of the department or function such cost was incurred for. In contrast, functional expense categorization is done based on the purpose for which the expenses are incurred. Functional expenses describe where or why the expenditure was incurred. [\[ASU 2024-03.BC55 – BC58, BC133\]](#)

The following are examples of natural and functional expenses. [\[220-40 Glossary, ASU 2024-03.BC55 – BC58\]](#)

Natural expenses	Functional expenses
• Purchases of inventory • Employee compensation (i.e. salaries and wages, employee benefits) • Depreciation • Intangible asset amortization • Depletion • Non-employee professional services (i.e. subcontractor costs) • Supplies • Interest • Rent • Utilities • Maintenance	• Cost of services • Cost of goods sold • Cost of revenue • Manufacturing and production • Technology and development • Research and development • Sales and marketing • Selling, general and administrative • Customer care • Restructuring

Question 3.2.20 Can a required natural expense category be further disaggregated?

Interpretive response: Yes.

We believe an entity may voluntarily further disaggregate a required natural expense category within a relevant expense caption as long as the underlying components and total amount for the required natural expense category are clearly presented. For example, an entity may want to disclose the underlying components of employee compensation – e.g. salaries and wages, share-based

payment arrangements, medical benefits, pension benefits. This information may be provided within or outside of the tabular disclosure for the relevant expense caption. Regardless of where this information appears, the underlying components and the total for the required category need to be clearly labeled and presented so that the disaggregation by required category is still achieved and not obscured by the voluntary information.

This view aligns with the option for entities to provide additional voluntary disclosures for relevant expense captions as long as those disclosures are separate from the required expense information. Voluntary quantitative disclosures may provide users of the financial statements with decision-useful information; however, they do not replace and cannot be combined with the required expense amounts (see [Question 5.3.10](#)). [220-40-50-30, ASU 2024-03.BC92, BC115]

3.3 Purchases of inventory

Excerpt from ASC 220-40

> Overall Guidance

• > Expense Disaggregation Disclosures

50-7 Purchases of inventory shall include only amounts within the scope of Topic 330 or within the scope of an Industry Subtopic in Topic 330 (collectively, Topic 330) but shall not include (regardless of the basis selected in paragraph 220-40-50-31) the amounts recognized from any of the following:

- A **business combination** within the scope of Subtopic 805-10 on business combinations
- A **joint venture** formation within the scope of Subtopic 805-60 on joint venture formations
- The initial consolidation of a **variable interest entity** that is not a business combination within the scope of Subtopic 810-10 on consolidation.

Amounts excluded by this paragraph shall be included in the other items category, unless separately disclosed voluntarily (see paragraph 220-40-50-30). See paragraphs 220-40-50-31 through 50-34 for additional requirements for the disaggregation of relevant expense captions that contain amounts within the scope of Topic 330.

Purchases of inventory is one of the five required natural expense categories that is disaggregated for each relevant expense caption in the income statement. [220-40-50-6(a)]

Purchases of inventory is not a US GAAP defined term, but Subtopic 220-40 provides that for purposes of the expense disaggregation disclosures, purchases of inventory: [220-40-50-7]

- include only amounts related to externally purchased raw materials and other tangible items (external spend) in the scope of Topic 330 (inventory) or industry Subtopics – i.e. inventoriable costs (see [Question 3.3.20](#)); and

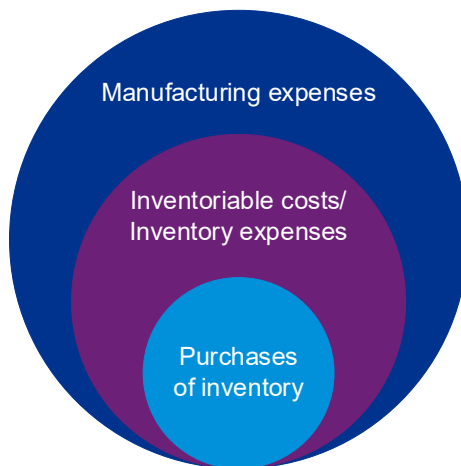
- exclude amounts of inventory recognized through certain nonrecurring transactions outside the ordinary course of business, such as business combinations (see [Question 3.3.30](#)).

As a result, judgment might be needed to identify which inventoriable costs qualify as purchases of inventory. Depending on the level of conversion and manufacturing necessary, purchases of inventory may or may not constitute a large portion of an entity's total inventoriable costs and cost of sales.

When substantially all of an income statement caption comprises purchases of inventory, an entity may elect to not apply the disaggregation requirements to that caption (see [Question 2.3.30](#)). [220-40-50-19]

Question 3.3.10 What is the relationship between purchases of inventory, inventoriable costs, inventory expenses and manufacturing expenses?

Interpretive response: Because purchases of inventory is not a defined term in the Codification, identifying the items and quantifying the amounts intended to be captured in this required natural expense category may be a new concept for some entities. To determine purchases of inventory in this context, it is helpful to distinguish between several different but interrelated terms.



This visualization may depict generally understood concepts for a manufacturing entity.

Manufacturing expenses

The FASB defined this term in the exposure draft for Subtopic 220-40 but later removed it from the final ASU. Manufacturing expense is a functional expense, generally understood to capture the costs of production. Such costs may relate to the production of inventory under Topic 330, and other manufacturing activities that do not generate inventoriable costs (e.g. unallocated fixed overhead and other abnormal costs). Accordingly, inventoriable costs and inventory expense may only represent a portion of total manufacturing expenses. [ASU 2024-03.BC82, BC85]

Inventoriable costs

Defined under Topic 330, inventoriable costs are the direct and indirect expenditures and charges incurred to bring inventory to its existing condition and location. Inventoriable costs typically comprise acquisition costs (e.g. price paid, sales tax, inbound delivery costs) and production costs (i.e. costs incurred in converting raw materials to WIP and finished goods), and represent total costs capitalized to the balance sheet as inventory under Topic 330. Therefore, inventoriable costs typically include several natural expense categories, not only purchases of inventory but also purchases of services, employee compensation, depreciation, amortization, depletion, etc. Inventoriable costs exclude costs incurred as part of an entity's manufacturing activities that are not capitalizable, e.g. unallocated manufacturing overhead related to abnormally low production). [\[330-10-30-1\]](#)

Inventory expenses

The FASB defined this term in the exposure draft for Subtopic 220-40 but later removed it from the final ASU. Inventory expense results from the derecognition of inventory assets due to sale to customers, consumption in the production of goods or services for such sale, or remeasurement (e.g. impairment). [\[ASU 2024-03.BC83\]](#)

Purchases of inventory

Purchases of inventory does not include all inventoriable costs (e.g. labor, overhead, etc.) or all manufacturing costs incurred, and therefore is narrowly defined. See [Question 3.3.20](#) for more context. [\[ASU 2024-03.BC76, BC78, BC81 – BC88\]](#)

For further guidance on inventory and inventoriable costs, see KPMG Handbook, [Inventory](#).

Question 3.3.20 What constitutes purchases of inventory under Subtopic 220-40?

Interpretive response: Identifying purchases of inventory as intended by Subtopic 220-40 involves two key terms: inventory and purchases, as well as defining elements of the purchase cost.

Inventory

Under Topic 330, an asset is inventory if it is a tangible asset that is: [\[330-10 Glossary\]](#)

- held for sale in the ordinary course of business;
- in process of production for such sale; or
- to be currently consumed in the production of goods or services to be available for sale.

Some costs, such as film costs and costs accumulated for long-term construction contracts, may be colloquially referred to as 'inventory' by an entity even though they are not considered inventory under Topic 330. Costs related

to assets that are not recognized as inventory under Topic 330 are not included in the purchases of inventory category (see [Question 4.2.10](#)). [ASU 2024-03.BC76]

Purchases

The term purchases is not defined in US GAAP. It is used in Subtopic 220-40 to distinguish amounts spent to acquire inventory items sourced from third parties from amounts related to activities like manufacturing, moving or storing the inventory even if costs related to these activities might also be inventoriable and expended with third parties. Further, certain external transactions with third parties are not considered purchases (see [Question 3.3.30](#)).

In this context, we believe purchases of inventory is intended to include only external spend for tangible items such as raw materials, supplies, WIP and finished goods. It does not include all inventoriable costs (e.g. labor, overhead), nor does it include all external spend (e.g. services purchased from third parties). [ASU 2024-03.BC78, BC81, BC83 – BC88]

Purchase cost

In our experience, some entities are taking a broad view of what comprises the purchase cost of inventory by planning to incorporate not only the price paid (net of rebates and discounts received) for the items but also all direct external acquisition costs incurred in procuring items of inventory – e.g. tariffs, taxes, inbound shipping costs. Other entities are taking a narrow view by planning to include only the price paid (net of rebates and discounts received) for the items in purchases of inventory; other direct acquisition costs are therefore reported as ‘other items’ in the tabular disclosure. In the absence of a clear definition in Subtopic 220-40, we believe either view is acceptable, as long as it is disclosed (if material) and consistently applied across reporting periods and similar types of inventory.

Question 3.3.30 Are all amounts of inventory recognized from external transactions considered purchases?

Interpretive response: No.

Purchases of inventory exclude amounts recognized from the following non-recurring transactions outside the ordinary course of business: [220-40-50-7, ASU 2024-03.BC77]

- business combinations (Subtopic 805-10) – see [Example 3.3.10](#);
- joint venture formations (Subtopic 805-60); and
- initial consolidation of a variable interest entity (VIE) that is not a business combination (Subtopic 810-10).

As a result of these exclusions, entities need to distinguish between similar items of inventory based on how these items were recognized on the balance sheet, e.g. through a regular purchase from an external supplier versus acquired in a business combination. This is because amounts recognized from the above excluded transactions are disclosed in the ‘other items’ category of an entity’s disaggregation table, unless separately disclosed voluntarily (see [section 5.3](#)).

This is illustrated in [Example 3.3.10](#). [220-40-50-7, 50-30, ASU 2024-03.BC77]

Conversely, amounts recognized from the following transactions are considered purchases of inventory, even though these transactions may also be non-recurring and outside the ordinary course of business: [\[ASU 2024-03.BC77\]](#)

- asset or asset group acquisition (Subtopic 805-50); and
- acquisition of a voting interest entity that does not meet the definition of a business (Subtopic 805-50).

Example 3.3.10 Inventory recognized through business combination

In the same reporting period, ABC Corp. directly purchases inventory from supplier Y for \$100 and acquires an entity with inventory of \$50 in a business combination.

ABC has no inventory at the beginning of the reporting period and sells all inventory during the reporting period.

The inventory rollforward is as follows (not a required disclosure).

Inventory	ABC	Acquiree	Consolidated totals
Opening inventory	-	-	-
Inventory directly purchased from suppliers	100	-	100
Inventory recognized through business combinations	-	50	50
Inventory sold	(100)	(50)	(150)
Closing inventory	-	-	-

ABC discloses the following to disaggregate the costs of goods sold relevant expense caption.

Cost of goods sold	Amount
Purchases of inventory	100
Other items	50
Total cost of goods sold	150

In its disclosure, ABC provides a qualitative description of the composition of the line 'Other items'. Alternatively, ABC can voluntarily report the amount of 50 on a separate line that more explicitly describes its composition (e.g. inventory recognized from business combination).

Question 3.3.40 How are intercompany and intra-entity purchases considered?

Interpretive response: Purchases of inventory is intended to capture only externally purchased inventory items. It is important to assess purchases from the standpoint of the reporting entity. When operations are vertically integrated, inventory may be sold between manufacturing sites, cost centers or subsidiaries (further referred as stand-alone entities). Therefore, what constitutes purchases of inventory for the group versus for each stand-alone entity might differ as illustrated in [Example 3.3.20](#). [ASU 2024-03.BC78]

Example 3.3.20 Intercompany and intra-entity purchases

Parent has two subsidiaries: A (manufacturer) and B (distributor). Subsidiary A purchases Part X from an external supplier for \$50, incurs \$100 of manufacturing costs to transform Part X into WIP Y, and then sells WIP Y to Subsidiary B for \$170 (i.e. with a margin of \$20).

Subsidiary B purchases Part Z from an external supplier for \$10, assembles Product A (comprised of WIP Y and Part Z) and resells Product A to Customer. Subsidiary B does not incur any other production costs associated with the assembly of Product A.

Parent and Subsidiaries A and B are all PBEs subject to Subtopic 220-40 disclosures. They disclose the following to disaggregate the costs of goods sold relevant expense caption in their respective financial statements.

Cost of goods sold	Subsidiary A	Subsidiary B	Parent
Purchases of inventory (limited to external purchases only)	50	180 ¹	60 ²
Other required natural expense categories (to be separately broken down as appropriate)	100 ³	-	100 ³
Total cost of goods sold	150	180	160
Notes:			
1. \$170 purchase of WIP Y from Subsidiary A + \$10 purchase of Part Z from external supplier.			
2. \$50 purchase of Part X by Subsidiary A + \$10 purchase of Part Z by Subsidiary B. Excludes \$170 sale of WIP Y by Subsidiary A to Subsidiary B.			
3. \$100 of manufacturing costs incurred by Subsidiary A in production of WIP X.			

3.4 Employee compensation

Excerpt from ASC 220-40

> Overall Guidance

• > Expense Disaggregation Disclosures

50-8 When applying the guidance in paragraph 220-40-50-6(b), an entity may elect, but is not required, to include amounts attributable to other transactions entered into for the benefit of employees (for example, the provision of subsidized goods or services) in employee compensation. For interim and annual reporting periods, an entity that includes other transactions entered into for the benefit of employees as part of employee compensation shall disclose both that those transactions have been included and a description of those transactions.

20 Glossary

Employee (second definition)

An individual over whom a reporting entity exercises or has the right to exercise sufficient control to establish an employer-employee relationship based on common law as illustrated in case law and currently under U.S. Internal Revenue Service (IRS) Revenue Ruling 87-41. A reporting entity based in a foreign jurisdiction would determine whether an employee-employer relationship exists based on the pertinent laws of that jurisdiction. Accordingly, an individual meets the definition of an employee if the reporting entity consistently represents that individual to be an employee under common law. The definition of an employee for payroll tax purposes under the U.S. Internal Revenue Code includes common law employees. Accordingly, a reporting entity that classifies an individual potentially subject to U.S. payroll taxes as an employee also must represent that individual as an employee for payroll tax purposes (unless the individual is a leased employee as described below). An individual that meets the definition of an employee includes, but is not limited to, a full-time, part-time, temporary, or seasonal employee. An individual does not meet the definition of an employee solely because the reporting entity represents that individual as an employee for some, but not all, purposes. For example, a requirement or decision to classify an individual as an employee for U.S. payroll tax purposes does not, by itself, indicate that the individual is an employee because the individual also must be an employee of the reporting entity under common law.

A leased individual is deemed to be an employee of the lessee if all of the following requirements are met:

- a. The leased individual qualifies as a common law employee of the lessee, and the lessor is contractually required to remit payroll taxes on the compensation paid to the leased individual for the services provided to the lessee.
- b. The lessor and lessee agree in writing to all of the following conditions related to the leased individual:
 1. The lessee has the exclusive right to grant compensation to the individual for the employee service to the lessee.

2. The lessee has a right to hire, fire, and control the activities of the individual. (The lessor also may have that right.)
3. The lessee has the exclusive right to determine the economic value of the services performed by the individual (including wages and the number of units and value of stock compensation granted).
4. The individual has the ability to participate in the lessee's employee benefit plans, if any, on the same basis as other comparable employees of the lessee.
5. The lessee agrees to and remits to the lessor funds sufficient to cover the complete compensation, including all payroll taxes, of the individual on or before a contractually agreed upon date or dates.

A nonemployee director does not satisfy this definition of employee.

Nevertheless, nonemployee directors acting in their role as members of a board of directors are treated as employees if those directors were elected by the employer's shareholders or appointed to a board position that will be filled by shareholder election when the existing term expires. However, that requirement applies only to awards and other compensation granted to nonemployee directors for their services as directors. Awards granted and compensation paid to those individuals for other services shall be accounted for as awards and compensation to nonemployees.

Employee Compensation

All forms of cash consideration (including deferred cash compensation), **share-based payment arrangements**, medical care benefits, **pension benefits**, **postretirement benefits**, and **nonretirement postemployment benefits** (including special or contractual **termination benefits**) given by an entity in exchange for service rendered by **employees** or for the termination of employment. This includes compensation cost arising from wages, salaries, profit-sharing, bonuses, **one-time employee termination benefits**, **other postemployment benefits**, **employee stock ownership plans**, employee share purchase plans, **defined contribution plans**, **multiemployer plans**, and any other compensation cost recognized in accordance with the guidance in Topic 710 on compensation, Topic 712 on nonretirement postemployment benefits, Topic 715 on retirement benefits, and Topic 718 on stock compensation. This also includes compulsory payments paid to the general government that confer entitlement to receive a (contingent) future social benefit, such as unemployment insurance benefits and supplements; accident, injury, and sickness benefits; old-age, disability, and survivors' pensions; and family allowances, reimbursements for medical and hospital expenses, or provision of hospital or medical services. For **defined benefit plans** within the scope of Topic 715, employee compensation includes only the **service cost component of net periodic pension cost** and the **service cost component of net periodic postretirement benefit cost**.

One-Time Employee Termination Benefits

Benefits provided to current employees that are involuntarily terminated under the terms of a one-time benefit arrangement.

Employee compensation is one of the five required natural expense categories that is disaggregated for each relevant expense caption in the income statement. [\[220-40-50-6\(b\)\]](#)

'Employee' and 'employee compensation' are defined terms in the Codification. 'Employee' is aligned with the definition used for accounting for stock compensation under Topic 718. The term 'employee compensation' under Subtopic 220-40 is intended to widely encompass the common types of consideration provided to employees in exchange for services provided. [220-40 Glossary, ASU 2024-03.BC90]

Banking entities required to comply with Reg S-X Rule 210.9-04 report an income statement caption for 'salaries and employee benefits' (or similarly named caption) and are not required to apply the definition of employee compensation included in Subtopic 220-40 (see [Question 2.3.40](#)). [220-40-50-20]

Question 3.4.10 How is 'employee' defined under Subtopic 220-40?

Interpretive response: There are two definitions of the term employee in the Codification. The first definition is used in Topic 960 for individuals who have rendered or are rendering services in the context of benefit plans. Subtopic 220-40 leverages the second definition, also used in the context of stock compensation under Topic 718. Under the second definition, employees are individuals over whom a reporting entity exercises or has the right to exercise sufficient control to establish an employer-employee relationship under common law based on requirements of the reporting entity's jurisdiction. [220-40 Glossary]

Employees include, but are not limited to, full-time, part-time, temporary, or seasonal individuals. It may also include inactive employees because Topic 712 (nonretirement postemployment benefits) is referenced in the definition of 'employee compensation' (see [Question 3.4.30](#)). [ASU 2024-03.BC92]

Question 3.4.20 Do all individuals commonly referred to as employees meet the definition?

Interpretive response: Not necessarily.

An individual does not meet the definition of an employee (see [Question 3.4.10](#)) solely because the entity represents the individual as an employee for some, but not all purposes (such as for US payroll taxes only). Instead, the individual must also be an employee of the entity under common law. US entities should consider case law and the factors provided in the IRS Revenue Ruling 87-41 in assessing whether an individual is an employee under common law. Similarly, foreign-based reporting entities should consider the pertinent laws of their jurisdiction to determine whether an employee-employer relationship exists. [220-40 Glossary]

Leased individuals and professional employer organizations

Leased individuals may meet the definition of an employee of the lessee if specific requirements are met (the employee leasing criteria). First, a leased individual must qualify as a common law employee of the lessee, and the individual's lessor must also be contractually required to remit payroll taxes on

the compensation provided to the leased individual for services provided to the lessee. Second, the lessor and lessee must agree in writing to five specific conditions related to the leased individual, which collectively demonstrate an employment-like relationship between the lessee and leased individual akin to a traditional employer-employee relationship. These conditions are reproduced in the Codification excerpt above defining the term 'employee'. [\[220-40 Glossary\]](#)

For example, assume an entity engages with a professional employer organization (PEO) that provides a comprehensive human resources solution through a co-employment model. The entity should consider the specific terms of the agreement in determining whether the employee leasing criteria are met. Although an individual may qualify as a common law employee of both employers, only one entity can qualify as the employer for financial reporting purposes as it relates to delivery of a single set of services. This determination hinges on whether the employee leasing criteria are met; if they are, the employer would be the lessee. However, this does not preclude an individual who is working part-time for two entities, providing separate services to each entity, from receiving compensation from both entities and the related amounts being accounted for as employee compensation by each entity.

Nonemployee directors

Nonemployee directors, elected by the shareholders, serving in their capacity and role as director, qualify for treatment as employees. However, any compensation to these individuals in a nonelected capacity or for services rendered outside of their role as a director is not considered employee compensation. [\[220-40 Glossary\]](#)

See section 1 of KPMG Handbook, [Share-based payment](#), for scoping considerations regarding employees and nonemployees, and in particular paragraphs 1.018 and 1.019 that discuss employee leasing arrangements.

Question 3.4.30 How is employee compensation defined under Subtopic 220-40?

Interpretive response: Employee compensation encompasses common significant forms of consideration provided by an entity in return for employees' services or for the termination of employment. It includes all forms of cash compensation and noncash consideration related to share-based payment arrangements, medical care benefits, pension benefits, postretirement benefits and nonretirement postemployment benefits. Employee compensation is defined broadly to eliminate potential complex judgments about the natural cost classification for common forms of consideration exchanged in an employer/employee relationship. [\[220-40 Glossary, ASU 2024-03.BC93 – BC95\]](#)

In evaluating which costs to include in employee compensation, entities need to consider the costs recognized under the following Topics: [\[220-40 Glossary\]](#)

- Topic 710 (compensation – general)
- Topic 712 (nonretirement postemployment benefits)

- Topic 715 (retirement benefits) (only the service cost component for net periodic pension and postretirement benefit costs for defined benefit plans)
- Topic 718 (stock compensation).

The following table lists common types of compensation and whether we believe they constitute employee compensation. This list is not exhaustive and other costs may qualify under the definition.

Compensation type	Included in employee compensation category?
Employee wages, salaries, profit-sharing and bonuses	Yes
Employee share-based payment arrangements, stock ownership plans and share purchase plans	Yes
Employee medical, pension, postretirement and nonretirement postemployment benefits	Yes
Employee defined contribution plans and multiemployer plans	Yes
Employee unemployment insurance benefits	Yes
Employee accident, injury and sickness benefits	Yes
Employee old-age, disability, and survivors' pensions	Yes
Employee family allowances, reimbursements for medical and hospital expenses, or provision of hospital or medical services	Yes
Employee payroll taxes	Yes
Compensation to directors in their elected capacity and role as directors	Yes (see Question 3.4.20)
Subsidized goods or services provided to employees	It depends (see Question 3.4.40)
Employee special or contractual termination benefits, including one-time employee termination benefits	No (see Question 3.4.50)
Nonemployee compensation	No (see Question 3.4.60)

Question 3.4.40 Can subsidized goods or services provided to employees be included in employee compensation?

Interpretive response: Yes, if an entity elects to do so.

Amounts attributable to other transactions entered into for the benefit of employees, such as subsidized goods or services, that are not explicitly in the scope of the compensation Topics listed by Subtopic 220-40 (see [Question 3.4.30](#)) may be included in employee compensation but are not required to be.

If an entity elects to include such amounts in employee compensation, it discloses that election and describes those transactions. [220-40-50-8, ASU 2024-03.BC115]

Question 3.4.50 Can one-time employee termination benefits be included in employee compensation?

Interpretive response: No.

Although one-time employee termination benefits provided to employees who are involuntarily terminated are a form of employee compensation, they represent exit or disposal activities under Topic 420 and are disclosed under that Topic. Therefore, they are reported separately from employee compensation in the tabular disclosure, meaning they are not included in the 'other items' line of the tabular disclosure (see [Question 5.2.10](#)). [220-40-50-6(b), 50-21(e)]

Further, in this instance, an entity discloses the fact that the employee compensation category excludes these benefits because they are reported as a separate line item. [220-40-55-16]

See FASB Example 2 (reproduced in [section 8.2](#)). [220-40-55-16]

Question 3.4.60 Can amounts provided to nonemployees be included in employee compensation?

Interpretive response: No.

Nonemployees, including contracted labor, subcontractors and professional service providers, do not meet the definition of employee (see [Question 3.4.10](#)). Accordingly, compensation amounts, cash or noncash, provided to such individuals are not categorized as employee compensation.

Nonemployee compensation can be voluntarily disclosed as a separate line item included within (see [Question 3.2.20](#)) or outside of the tabular disclosure as long as the amounts are not combined with the required employee compensation disaggregated amounts. If not voluntarily disclosed as a separate line item within the tabular disclosure, nonemployee compensation amounts are included in 'other items' and incorporated into the qualitative description of those other items (see [Question 5.3.20](#)). [ASU 2024-03.BC92, BC115]

Further, an entity is not precluded from disclosing a subtotal for total workforce costs that may include amounts that are separately disclosed for employee compensation and nonemployee costs (see [Question 5.3.10](#)). [ASU 2024-03.BC115]

Question 3.4.70 Is total employee compensation incurred in a period disaggregated in the tabular disclosure?**Interpretive response:** No.

Subtopic 220-40 only requires disaggregation of costs incurred that are either (a) expensed as incurred or (b) capitalized to inventory. [ASU 2024-03.BC141]

The sum of the amounts for employee compensation disaggregated across all relevant expense captions in the tabular disclosure may not always represent the total of employee compensation amounts incurred in the reporting period. There are several reasons for this situation.

- Employee compensation costs capitalized to assets other than inventory do not require disaggregation (e.g. PP&E under Topic 360, software under Subtopic 350-40, customer contract costs under Subtopic 340-40) (see [section 4.2](#)). [220-40-50-14]
- Certain liability-related expenses do not require disaggregation (e.g. provisions for losses on contracts, claims and claims adjustment expenses, or environmental obligations) (see [section 4.3](#)). [220-40-50-16]
- Disaggregated amounts for employee compensation may be net of expense reimbursement amounts (see [section 4.4](#)). [220-40-50-26]
- There are two available approaches to disaggregate costs included in a relevant expense caption that contains inventory amounts (see [section 4.5](#)). If the expense-incurred basis is applied (see [section 4.5.20](#)), the amount of employee compensation disclosed corresponds to amounts included in the cost-basis of the inventory sold in the period, not the employee compensation costs incurred in the period in relation to the activities in COGS. [220-40-50-31]

[Example 3.4.10](#) illustrates these requirements.

Example 3.4.10 Disaggregation of employee compensation capitalized or accrued

ABC Corp. incurs \$150 as total employee compensation for the services it received from its employees, and \$30 for services received from nonemployees (i.e. contractors) in the reporting period. It does not incur any other costs, and none of these costs relate to inventory in the scope of Topic 330. It accounts for the total \$180 as follows.

Amounts related to	Accounting treatment	Relevant expense caption	Amount
Services to customers provided by employees	Expensed as incurred	Costs of services	50
Services to customers provided by contractors	Expensed as incurred	Costs of services	10

Amounts related to	Accounting treatment	Relevant expense caption	Amount
Environmental obligation (employees)	Recognized against the environmental obligation		10
Sales commissions earned by employees on securing 6-month customer contracts	Expensed as incurred	SG&A	40
Sales commissions earned by contractors on securing 6-month customer contracts	Expensed as incurred	SG&A	20
Sales commissions earned on securing 24-month customer contracts (employees)	Recognized as a contract acquisition cost asset under Subtopic 340-40		30
Development of new internal-use software (employees)	Recognized within the cost of the software asset, under Subtopic 350-40		20
Total			180

In the reporting period, ABC reports the following amounts in its disaggregated disclosures for the costs of services and SG&A relevant expense captions.

Cost of services	Amount
Employee compensation	50
Other items	10
Total costs of services	60

SG&A	Amount
Employee compensation	40
Other items	20
Total SG&A	60

In its disclosure, ABC qualitatively describes that the two lines 'other items' are composed of costs for services rendered by contractors. Alternatively, ABC can elect to voluntarily disclose contractor costs separately in lieu of including them in the 'other items' category.

3.5 Depreciation

Excerpt from ASC 220-40

> Overall Guidance

• > Expense Disaggregation Disclosures

50-9 The amounts provided for depreciation in accordance with paragraph 220-40-50-6(c) and intangible asset amortization in accordance with paragraph 220-40-50-6(d) shall be consistent with the classification of amounts used to satisfy the disclosure requirements for the total depreciation expense and total intangible asset amortization expense disclosures in paragraphs 360-10-50-1(a) and 350-30-50-2(a)(2), respectively, and with the classification of amounts described in paragraph 220-40-50-10.

50-10 Amortization of a **right-of-use asset** for a **finance lease** recognized in accordance with paragraphs 842-20-35-7 through 35-8 and amortization of leasehold improvements recognized in accordance with paragraphs 842-20-35-12 through 35-13 shall be disclosed in a manner consistent with how an entity presents depreciation or amortization of similar assets (see paragraph 842-20-45-4(a)). That is, amounts shall be included as part of either depreciation in paragraph 220-40-50-6(c) or intangible asset amortization in paragraph 220-40-50-6(d).

Depreciation is one of the five required natural expense categories that is disaggregated for each relevant expense caption in the income statement. [220-40-50-6(c)]

The amounts disclosed for depreciation expense under Subtopic 220-40 are consistent with those disclosed under Topic 360. [220-40-50-9]

Question 3.5.10 How is depreciation defined under Subtopic 220-40?

Interpretive response: Depreciation as a required natural expense category is defined by reference to existing requirements in Topic 360 to disclose 'depreciation expense for the period', reflecting the systematic and rational allocation of tangible assets cost over their useful lives. [220-40-50-9, 360-10-50-1(a), ASU 2024-03.BC99,.BC103]

The following table lists common types of assets (non-exhaustive) that may be in the scope of Topic 360 for depreciation.

Asset types	In scope of Topic 360 for depreciation?
Long-lived tangible assets used to create and distribute and entity's products and services (e.g. buildings, machinery and equipment, and furniture and fixtures) [360-10-05-3]	Yes

Asset types	In scope of Topic 360 for depreciation?
Finance lease ROU assets and leasehold improvements	It depends (see Question 3.5.20)
Capitalized asset retirement costs associated with an ARO	Yes (see Question 3.5.30)
Capitalized internal-use software costs	It depends (see Question 3.6.30)

Question 3.5.20 Is the amortization of finance lease ROU assets and leasehold improvements included in depreciation or intangible assets amortization?

Background: Like depreciation of tangible assets, amortization of intangible assets is also a required natural expense category (see [section 3.6](#)). However, Topic 842 does not prescribe whether lease ROU assets are tangible or intangible assets. Similarly, it does not prescribe whether the amortization of finance lease ROU assets and leasehold improvements should be included as part of current disclosure requirements for depreciation and intangible asset amortization. It simply requires these amortization amounts to be presented in the income statement in a manner consistent with how an entity presents depreciation or amortization of similar assets. [\[842-20-45-4\(a\), ASU 2016-02.BC265, ASU 2024-03.BC102\]](#)

Interpretive response: It depends.

For Subtopic 220-40 disclosures purposes, amortization of finance lease ROU assets and leasehold improvements needs to be included in either depreciation or intangible asset amortization, in a manner consistent with how an entity presents depreciation or amortization of similar assets. As a result, the presence of such amounts in an income statement caption subjects the caption to the disaggregation requirements in Subtopic 220-40. An entity should consistently apply its classification election. In our experience entities often include finance lease ROU assets in PPE and in that case the amounts would be presented within depreciation. [\[220-40-50-10, ASU 2024-03.BC38, BC102\]](#)

Question 3.5.30 Is depreciation of capitalized asset retirement costs associated with an ARO included in depreciation?

Background: When recognizing an ARO liability under Subtopic 410-20, asset retirement costs are capitalized and increase the carrying amount of the related long-lived asset. Subsequently, capitalized asset retirement costs are allocated to expense using a systematic and rational method over the related long-lived asset's useful life. [\[410-20-25-5, 35-2\]](#)

Interpretive response: Yes.

The capitalized asset retirement costs are part of the total cost of the long-lived asset to which the ARO relates. Therefore, depreciation of capitalized asset retirement costs is included in depreciation expense. [410-20-25-5, 35-2]

Question 3.5.40 Is total depreciation incurred in a period disaggregated in the tabular disclosure?

Background: Subtopic 360-10 requires the amount of depreciation expense for the period to be disclosed in the notes. This amount represents depreciation charged to expense in the period but may also include depreciation capitalized as part of the cost of inventory in the period – i.e. total depreciation incurred in the period. [360-10-50-1, TQA 5210.02]

Interpretive response: Not necessarily.

As explained in [Question 3.4.70](#) for employee compensation, there are several reasons why the sum of the natural expense category (e.g. depreciation) amounts disaggregated across all relevant expense captions may not equal the total amounts incurred. Subtopic 220-40 only requires disaggregation of costs incurred that are either (a) expensed as incurred or (b) capitalized to inventory – e.g. depreciation capitalized to an asset other than inventory is not subject to disaggregation. See [Question 4.2.10](#) for examples of costs capitalized that do not require disaggregation. [ASU 2024-03.BC141]

For these reasons, and depending on how amounts disclosed under Subtopic 360-10 are calculated, these amounts may not equal the sum of the depreciation amounts disaggregated across all relevant expense captions under Subtopic 220-40. [ASU 2024-03.BC102]

3.6 Intangible asset amortization

Intangible asset amortization is one of the five required natural expense categories that is disaggregated for each relevant expense caption in the income statement. [220-40-50-6(d)]

The amounts disclosed for intangible asset amortization expense under Subtopic 220-40 are consistent with those disclosed under Subtopic 350-30. [220-40-50-9]

Question 3.6.10 How is intangible asset amortization defined under Subtopic 220-40?

Interpretive response: Intangible asset amortization is defined in Subtopic 220-40 by reference to existing requirements in Subtopic 350-30 to disclose the total amount of amortization expense for the period, reflecting the pattern in which the intangible assets' economic benefits are consumed. [220-40-50-9, 350-30-50-2(a)(2), ASU 2024-03.BC99, BC103]

The following types of assets are in the scope of Subtopic 350-30 and therefore their amortization amounts are classified as intangible asset amortization under Subtopic 220-40:

- capitalized costs of software to be sold, leased or marketed;
- intangible assets acquired individually or with a group of other assets; and
- costs of internally developing identifiable intangible assets that an entity recognized as assets.

Conversely, amortization of assets outside Subtopic 350-30's scope is excluded from the required natural expense category amount. See [Question 3.6.20](#) for consideration of other types of expenses classified as 'amortization' under separate Codification Topics. A potential exception to this exclusion relates to the amortization by a lessee of finance lease ROU assets and leasehold improvements under Topic 842 (see [Question 3.5.20](#)). [350-30-15-3, 220-40-50-10, ASU 2024-03.BC98, BC102]

Question 3.6.20 What are examples of assets outside Subtopic 350-30's scope?

Interpretive response: In practice, the term 'amortization' is used broadly to describe the systematic allocation of the cost of nonphysical assets over their useful lives. Subtopic 220-40 limits the required category of intangible asset amortization to assets in the scope of Subtopic 350-30 (see [Question 3.6.10](#)). Therefore, other types of amortization are excluded from the category. Examples of other types of amortization include the following. [220-40-50-9, 50-21 – 50-22, ASU 2024-03.BC57, BC104]

Amortization attributable to assets recognized for	Relevant Subtopic
The expiration of an insurance or reinsurance coverage provided under a contract that transfers only significant underwriting risk	340-30
Costs to obtain or fulfill a contract with a customer	340-40
Capitalized implementation costs of hosting arrangements that are service contracts (see Question 3.6.30 for considerations related to internal use software costs)	350-40
Debt issue costs	470-10
License agreements for program material	920-350
Film costs	926-20
Capitalized acquisition costs (insurance contracts)	944-30

Despite not being included in intangible asset amortization, certain of these amounts (e.g. amortization of license agreements for program material and film costs) are required to be reported separately in the tabular disclosure in certain cases (see [section 5.2](#)). Otherwise, the amounts are included in 'other items' in the tabular disclosure (see [section 5.3](#)). [220-40-50-21, 50-22, ASU 2024-03.BC104, BC105]

Question 3.6.30 Is the amortization of capitalized internal-use software costs included in depreciation or intangible asset amortization?

Background: There is diversity in practice regarding how internal-use software in the scope of Subtopic 350-40 is presented on the balance sheet (i.e. within PP&E or intangible assets) and how amortization amounts are disclosed within total depreciation expense or total amortization expense. This is because the disclosure guidance in Subtopic 350-40 refers to the guidance in Subtopic 360-10 for PP&E rather than the intangible assets disclosures in Subtopic 350-30. [350-40-50-1, ASU 2024-03.BC100]

ASU 2025-06 Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40), clarifies that the PP&E disclosures in Subtopic 360-10 are required for all capitalized software costs accounted for under Subtopic 350-40, regardless of how those costs are presented in an entity's financial statements. See KPMG Defining Issues, [FASB issues final ASU on software cost accounting](#), for more information about this ASU. [ASU 2025-06.BC94]

Interpretive response: It depends.

The Board decided not to address the classification of amortization of internal-use software in Subtopic 220-40, but expects corresponding amounts to be included in either depreciation or intangible asset amortization, in a manner consistent with how the underlying asset is presented on the balance sheet (i.e. PP&E or intangible assets) and how amortization amounts are disclosed. [ASU 2024-03.BC101]

The adoption of ASU 2025-06 is not expected to change the classification of these amounts. [ASU 2025-06.BC94]

Question 3.6.40 Is total intangible asset amortization incurred in a period disaggregated in the tabular disclosure?

Background: Subtopic 350-30 requires the total amount assigned to intangible asset amortization (i.e. total amortization incurred) for the period be disclosed in the notes. [350-30-50-1]

Interpretive response: Not necessarily.

As explained in [Question 3.4.70](#) for employee compensation, there are several reasons why the sum of the natural expense category (e.g. intangible asset amortization) amounts disaggregated across all relevant expense captions may not equal the total amounts incurred. Subtopic 220-40 only requires disaggregation of costs incurred that are either (a) expensed as incurred or (b) capitalized to inventory – e.g. amortization capitalized to an asset other than inventory is not subject to disaggregation. [ASU 2024-03.BC141]

For these reasons, intangible asset amortization amounts disaggregated under Subtopic 220-40 may not reconcile to the total amounts disclosed pursuant to Subtopic 350-30. [ASU 2024-03.BC102]

3.7 DD&A

Excerpt from ASC 220-40

• > Expense Disaggregation Disclosures

50-11 In determining the amounts to be disclosed in paragraph 220-40-50-6(e), an entity also shall include amounts for depletion expense that are not recognized as part of oil- and gas-producing activities in accordance with Subtopic 932-360 (such as depletion expense recognized by entities within the scope of Topic 930 on mining).

DD&A of capitalized acquisition, exploration and development costs recognized as part of oil- and gas-producing activities under Subtopic 932-360, together with other amounts of depletion expense, is one of the five required natural expense categories that is disaggregated for each relevant expense caption in the income statement. [\[220-40-50-6\(e\)\]](#)

Although DD&A and depletion expense are specific to certain industries, these natural expenses are included in a separate required natural expense category because they represent noncash expenses recognized systematically, similar to depreciation and intangible asset amortization. The separate category also provides disaggregation classification clarity for those industries with DD&A and depletion expense. [\[ASU 2024-03.BC63\]](#)

Question 3.7.10 How is DD&A defined under Subtopic 220-40?

Interpretive response: DD&A as a required natural expense category includes: [\[220-40-50-6\(e\), 50-11\]](#)

- DD&A of capitalized acquisition, exploration and development costs recognized as part of oil- and gas-producing activities under Subtopic 932-360; and
- other amounts of depletion expense recognized in extractive industries outside of oil and gas (e.g. mining entities in the scope of Topic 930).

Entities with extractive activities use depletion expense to reflect the reduction in their natural resource assets as those assets are consumed over time. Other amounts of depletion expense are included in the DD&A category to ensure consistent disclosure across all entities with extractive activities. [\[ASU 2024-03.BC47\]](#)

Example 3.7.10 Disaggregation of DD&A

ABC Corp. operates in both the oil-and-gas and chemical industries. ABC presents a caption 'depreciation, depletion and amortization' in its income statement and has determined this line item represents a relevant expense caption.

The 'depreciation, depletion and amortization' line item is \$4,000 and includes:

- depletion, depreciation and amortization (DD&A) expense from oil- and gas-producing activities, \$2,300;
- depreciation of an ARO related to oil- and gas-producing activities, \$200;
- depreciation related to the chemical plant equipment, \$750;
- depreciation related to the corporate headquarters, \$250; and
- amortization related to capitalized software, \$500.

ABC disaggregates the amounts based on their underlying nature and the applicable required expense categories. ABC provides the following tabular disclosure.

Depreciation, depletion, and amortization	Amount
DD&A (including ARO depreciation)	2,500
Depreciation (chemical plant equipment and corporate headquarters)	1,000
Amortization (capitalized software)	500
Total depreciation, depletion and amortization	4,000

Question 3.7.20 Are amounts for DD&A required to be disclosed separately from amounts for other depletion expense?

Interpretive response: No.

The required category DD&A captures the aggregate amount of both the DD&A recognized as a part of oil- and gas-producing activities and depletion expense not recognized as part of oil- and gas-producing activities. Separate disaggregation between the two components is not required but is permitted (see [Question 3.2.20](#)). [ASU 2024-03.BC103]

4. How to apply the disaggregation requirements

Detailed contents

4.1 How the standard works

4.2 Certain asset-related expenses

Question

Question 4.2.10 What are examples of costs capitalized to assets that do not require disaggregation?

4.3 Certain liability-related expenses

Questions

Question 4.3.10 Are all liability-related expenses that involve estimates exempt from disaggregation?

Question 4.3.20 Does the disaggregation exemption for qualifying liability-related expenses apply to initial recognition, subsequent measurement, or both?

Question 4.3.30 Can an entity elect to disaggregate qualifying liability-related expenses?

4.4 Expense reimbursements

Questions

Question 4.4.10 What are cost-sharing or cost-reimbursement arrangements?

Question 4.4.20 How are expense reimbursements received disclosed?

Question 4.4.30 How are expense reimbursements paid disclosed?

4.5 Disaggregation of relevant expense captions with inventory amounts

4.5.10 The cost-incurred basis

4.5.20 The expense-incurred basis

4.5.30 Practical considerations when electing a disaggregation basis

Questions

Question 4.5.10 How do the cost-incurred and expense-incurred bases compare?

Question 4.5.20 What is included in 'other items' in the disaggregation of COGS (or other relevant caption with inventory amounts)?

Question 4.5.30 In which category are inventory remeasurements included?

Question 4.5.40 In which category are standard cost variances included?

Question 4.5.50 How is the cost-incurred basis applied?

Question 4.5.60 What is included in the required natural expense categories when the cost-incurred basis is applied?

Question 4.5.70 What is included in the 'changes in inventory' category?

Question 4.5.80 What is included in the 'other adjustments and reconciling items' category?

Question 4.5.90 How is the expense-incurred basis applied?

Question 4.5.100 What considerations may be relevant in electing the cost-incurred basis or the expense-incurred basis?

Examples

Example 4.5.10 Cost-incurred vs expense-incurred basis

Example 4.5.20 Other items under cost-incurred vs expense-incurred basis

Example 4.5.30 Inventory impairment

Example 4.5.40 Standard cost variances

Example 4.5.50 Deconsolidation transaction under the cost-incurred basis

Example 4.5.60 Translation adjustments under the cost-incurred basis

Example 4.5.70 Cost-incurred vs expense-incurred basis, under FIFO vs LIFO

4.1 How the standard works

To reduce the operational reporting complexities and mitigate implementation costs for preparers in applying Subtopic 220-40, ASU 2024-03 provides additional guidance beyond prescribing required natural expenses categories.

Certain asset-related expenses

Expenditures (e.g. employee compensation) that are capitalized to an asset (other than to inventory) are not disaggregated when capitalized because they are not recorded in the income statement at that time. Instead, the expense amount related to the subsequent derecognition of the asset is disaggregated based on its nature when recorded in the income statement (e.g. depreciation) without regard to the initial nature of the costs (e.g. employee compensation) when capitalized to the asset.

Certain liability-related expenses

‘Qualifying liability-related expenses’ do not need to be disaggregated. To qualify for this treatment, an expense must relate to an estimated liability for which the timing of settlement is uncertain, and the expense cannot entirely be made up of one required natural expense category (e.g. employee compensation). This guidance is expected to provide relief for expenses related to liabilities such as provisions for losses on construction-type contracts, claims obligations for insurers or environmental obligations.

Expense reimbursements

Expense reimbursements relate to both amounts received from or paid to another entity under a cost-sharing or cost-reimbursement arrangement. Such amounts are generally not allocated to natural expenses.

- **Expense reimbursements received:** An entity that includes expense reimbursements in a relevant expense caption can report the reimbursements on a separate line of the tabular disclosure, or it can include the expenses in the tabular disclosure net of the reimbursement effects.
- **Expense reimbursements paid:** Expense reimbursements paid that are included in a relevant expense caption are reported separately as an expense category in the tabular disclosure for that caption.

Expense captions with inventory amounts

Unlike other asset-related expenses, amounts capitalized to inventory under Topic 330 (‘inventory amounts’) are disaggregated. Subtopic 220-40 provides two bases for disaggregation – the cost-incurred basis and the expense-incurred basis. The chosen approach is to be applied consistently.

- **Cost-incurred basis:** Under this basis, amounts are disaggregated in the reporting period in which they are capitalized to inventory.
- **Expense-incurred approach:** Under this basis, amounts previously capitalized to inventory are disaggregated in the reporting period the inventory is derecognized based on the natural expense category of the costs when they were initially incurred.

4.2 Certain asset-related expenses

Excerpt from ASC 220-40

> Overall Guidance

- > Expense Disaggregation Disclosures
- • > Identification of Relevant Expense Captions
- • • > Certain Asset-Related Expenses

50-14 With the exception of inventory disclosed under the cost-incurred basis described in paragraph 220-40-50-31(a), an entity is not required to further disaggregate costs capitalized as an asset, even if the costs capitalized include the categories listed in paragraph 220-40-50-6. In addition, when an expense amount relates to the derecognition of an asset other than inventory, an entity shall apply the guidance in paragraph 220-40-50-6 based on the nature of the expense at the time that it is recognized in the income statement.

50-15 To illustrate the application of the requirements in paragraph 220-40-50-14, an entity is not required to further disaggregate amortization of costs to fulfill a **contract** with a **customer** into the categories required by paragraph 220-40-50-6 (for example, employee compensation). As another example, an entity that capitalizes employee compensation when self-constructing new property, plant, and equipment for internal use is not required to further disaggregate the resulting depreciation into the categories listed in paragraph 220-40-50-6.

The expense disaggregation disclosure requirements do not apply to costs capitalized to assets other than inventory (e.g. PP&E), even if those costs include the required natural expense categories (e.g. employee compensation). Instead, the expense amount related to the subsequent derecognition of those assets is disaggregated based on its nature when recorded in the income statement (e.g. depreciation) without regard to the initial nature of the costs when capitalized to the asset. [220-40-50-14]

The disaggregation of costs capitalized to inventory is discussed in [section 4.5](#).

Question 4.2.10 What are examples of costs capitalized to assets that do not require disaggregation?

Interpretive response: The following table lists examples of costs capitalized to assets that do not require disaggregation into their natural expense categories. The third column indicates how to report the expense amount related to the subsequent derecognition of the asset in the tabular disclosure for a relevant expense caption that includes such amount. [220-40-50-15, ASU 2024-03.BC44, BC57, BC98, BC143]

Costs capitalized to the following assets	Relevant Topic/Subtopic	Expense from asset derecognition reported in tabular disclosure as follows
Direct loan origination costs incurred by a lender, deferred and recognized as a reduction in the yield of the loan	310-20	N/A - Reflected as reduction of interest income [ASU 2024-03.BC142]
Costs to obtain or fulfill a contract with a customer	340-40	Reported separately if entirely recorded in one relevant expense caption (see Question 5.2.20) or 'other items' (see section 5.3) if recorded in more than one relevant expense caption
Internal-use software	350-40	Intangible asset amortization or depreciation (see Question 3.6.30)
PP&E that is self-constructed for internal use	360-10	Depreciation
Film costs	926-20	Reported separately if recorded in a relevant expense caption (see Question 5.2.10)
Software to be sold, licensed, or marketed	985-20	Intangible asset amortization (see Question 3.6.10)

As explained in [Question 3.3.20](#), some costs may be capitalized to assets colloquially referred to as inventory even though these assets are not in the scope of Topic 330. Such costs do not require disaggregation when incurred.
[ASU 2024-03.BC76]

4.3 Certain liability-related expenses

Excerpt from ASC 220-40

> Overall Guidance

- > Expense Disaggregation Disclosures
- • > Identification of Relevant Expense Captions
- • • > Certain Liability-Related Expenses

50-16 An entity is not required to disaggregate an expense amount into the required expense categories as part of the disclosures required by paragraph 220-40-50-6 if all of the following criteria are met:

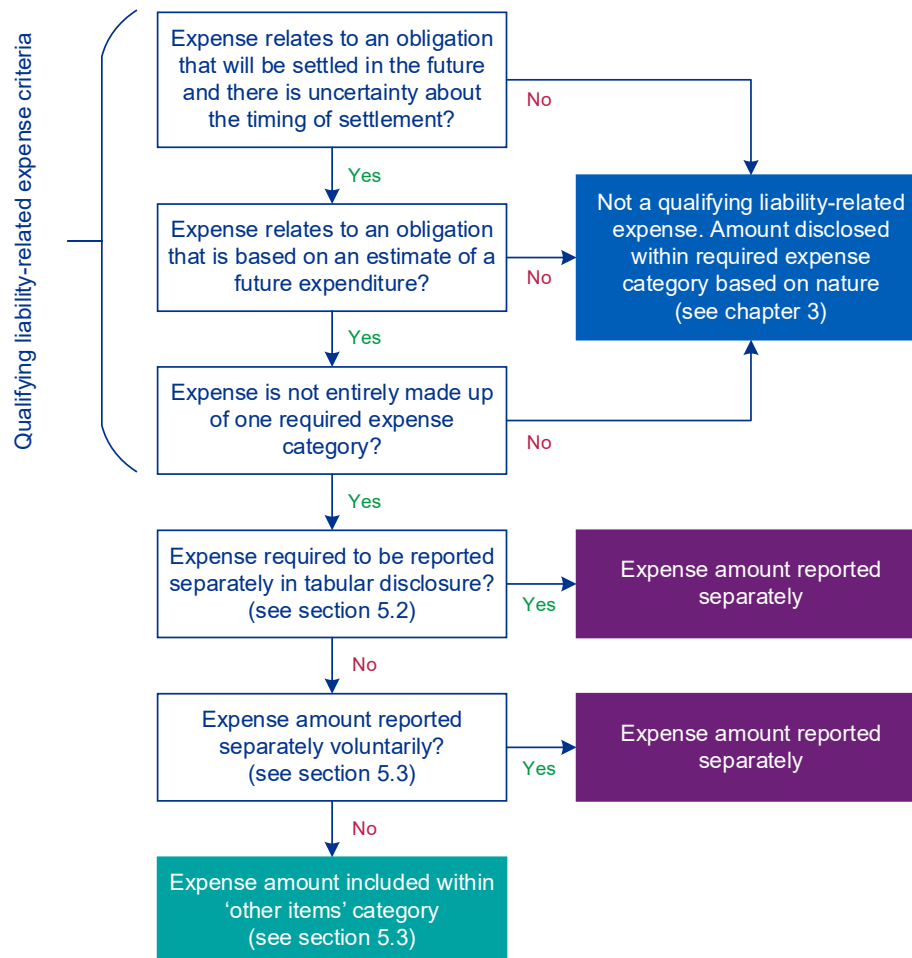
- a. The expense relates to an obligation that will be settled in the future and there is uncertainty about the timing of settlement.
- b. The expense relates to an obligation that is based on an estimate of a future expenditure.
- c. The expense is not entirely made up of one required expense category (for example, employee compensation).

An expense that meets the above criteria may be required to be disclosed in the same tabular format if it is listed in paragraphs 220-40-50-21 through 50-22.

50-17 Examples of expenses that meet the criteria in paragraph 220-40-50-16 include provision for losses on contracts (see Subtopic 605-35 on revenue recognition – construction-type and production-type contracts), claims and claims adjustment expenses, and asset retirement obligations, among others.

50-18 Examples of expenses that do not meet the criteria in paragraph 220-40-50-16 include expense amounts related to accruals for liabilities to pay for goods or services that have been received or supplied but have not been paid or invoiced, including amounts due to employees (for example, amounts relating to accrued bonuses, vacation pay, or pension obligations).

The expense disaggregation disclosure requirements do not apply to liability-related expense amounts that meet the first three criteria in the following decision tree (further referred to as 'qualifying liability-related expenses'). However, these expenses may still be subject to separate reporting in the tabular disclosure, under the requirements discussed in [section 5.2](#) or if the entity voluntarily elects to do so (see [Question 5.3.10](#)). Evaluating whether liability-related expenses are exempt from disaggregation requires judgment. [220-40-50-16]



Question 4.3.10 Are all liability-related expenses that involve estimates exempt from disaggregation?

Interpretive response: No.

The use of estimates to measure a liability is not sufficient by itself to exempt the related expenses from disaggregation.

For example, some liabilities for which the timing of settlement is known may involve the use of estimates in their measurement. Alternatively, the amount at which the liability will be settled is known although timing is uncertain. Further, certain liabilities with uncertainty as to when and at what amount they are ultimately expected to be settled may still need to be disaggregated if the liability represents a single required natural expense category. [220-40-50-18, ASU 2024-03.BC45]

The table below provides examples of liability-related expenses and whether they are disaggregated if included within a relevant expense caption, considering their nature and separate reporting requirements explained in [section 5.2](#). Expenses exempt from the disaggregation requirements that do not require separate reporting are included in 'other items' in the tabular disclosure, unless voluntarily disclosed separately (see [Question 5.3.10](#)).

Liability-related expense type	Exempt from disaggregation into the natural categories?	Separate reporting in the tabular disclosure required?
Accruals for liabilities to pay for goods or services that have been received or supplied but have not yet been paid or invoiced	No [220-40-50-18]	No
Amounts due to employees – accrued bonuses, accrued vacation pay	No [220-40-50-18]	No
Amounts due to employees – pension obligations	No [220-40-50-18]	Yes, components of net benefit cost recognized (other than service cost amounts included within employee compensation) need to be reported separately in the tabular disclosure. [220-40-50-21(f)] (see Question 5.2.10)
Qualifying liability-related expenses that do not require separate reporting		
Provision for losses on contracts recognized on construction-type and production-type revenue contracts under Subtopic 605-35	Yes [220-40-50-17, ASU 2024-03.BC45]	No

Liability-related expense type	Exempt from disaggregation into the natural categories?	Separate reporting in the tabular disclosure required?
Claims and claims adjustment expenses [944-40 Glossary]	Yes [220-40-50-17, ASU 2024-03.BC45]	No
Asset retirement obligations (AROs)	Yes [220-40-50-17, ASU 2024-03.BC45]	No, except for accretion expense if included entirely in one relevant expense caption [220-40-50-22(i)] (see Question 5.2.20)
Environmental obligations	Yes [220-40-55-10]	No
Qualifying liability-related expenses that require separate reporting		
Loss contingencies	Yes	Yes, if included entirely in one relevant expense caption [220-40-50-22(j)] (see Question 5.2.20)
Warranty accruals	Yes	Yes, if included entirely in one relevant expense caption [220-40-50-22(k)] (see Question 5.2.20)

FASB Example 1 (reproduced in [section 8.1](#)) illustrates the reporting of expenses related to an environmental obligation and a warranty obligation.

Question 4.3.20 Does the disaggregation exemption for qualifying liability-related expenses apply to initial recognition, subsequent measurement, or both?

Interpretive response: We believe that the disaggregation exemption for qualifying liability-related expenses applies to both the initial recognition and subsequent measurement of these liabilities. For example, if an entity records an expense amount to establish an environmental obligation and subsequently incurs additional expense amounts for the remeasurement of such obligation, the expense amounts for the initial recognition and remeasurement are not required to be disaggregated. Instead, the expense amounts are included in the 'other items' category in the respective period the expense is incurred. [220-40-55-10 – 55-11]

Question 4.3.30 Can an entity elect to disaggregate qualifying liability-related expenses?

Interpretive response: Yes.

We believe an entity is generally permitted to disaggregate qualifying liability-related expenses. The approach selected should be applied consistently to similar types of liabilities and to the initial recognition and remeasurement of the liability.

However, disaggregating the components of certain liability-related expenses may be challenging if the total amount expensed for that type of liability (e.g. warranty expense) is required to be reported separately as a whole in the tabular disclosure, under the requirements explained in [section 5.2. \[220-40-50-16\]](#)

4.4 Expense reimbursements

Excerpt from ASC 220-40

> Overall Guidance

• > Expense Reimbursements Included in a Relevant Expense Caption

50-26 For interim and annual reporting periods, an entity that presents a relevant expense caption that includes amounts that are recorded net of an expense reimbursement related to a cost-sharing or cost-reimbursement arrangement from another entity, in the same tabular format disclosure in which the disclosures required by paragraph 220-40-50-6 are provided, shall either:

- Separately disclose the amount of the expense reimbursement
- Disclose the amounts of the expense categories required by paragraphs 220-40-50-6 and 220-40-50-21 through 50-22 that are included in the relevant expense caption net of any reimbursement effects.

50-27 For interim and annual reporting periods, an entity shall disclose how expense reimbursements related to a cost-sharing or cost-reimbursement arrangement are included in the tabular format disclosure, as described in paragraph 220-40-50-26.

50-28 For interim and annual reporting periods, an entity that includes an expense reimbursement related to a cost-sharing or cost-reimbursement arrangement to another entity in a relevant expense caption shall separately disclose the amount of that expense reimbursement in the same tabular format disclosure in which the disclosures required by paragraph 220-40-50-6 are provided.

50-29 For interim and annual reporting periods, when applying the guidance in paragraph 220-40-50-26(a) or 220-40-50-28, an entity shall disclose qualitative descriptions of the expense categories (based on their **natural expense classification**) to which an expense reimbursement relates.

Expense reimbursements relate to both amounts received from or paid to another entity under a cost-sharing or cost-reimbursement arrangement. These amounts are subject to specific requirements, which differ for amounts received and paid, with some optionality. Expense reimbursement guidance is specifically provided because such amounts are generally not allocated to natural expenses. For example, entities that pay reimbursements do not typically receive detailed information about the natural expenses to which the reimbursements relate. [220-40-50-26 – 50-29, ASU 2024-03.BC28(g), BC112]

Question 4.4.10 What are cost-sharing or cost-reimbursement arrangements?

Interpretive response: The terms ‘cost-sharing’ and ‘cost-reimbursement’ arrangements are not defined. Therefore, judgment is needed to assess when the expense reimbursements guidance applies. We believe the guidance is generally not intended to apply to traditional customer-vendor arrangements, although some arrangements may be structured on a cost-plus basis and provide the vendor reimbursement for its costs incurred under the contract.

Conversely, we believe entities should assess whether the guidance is applicable to the following arrangements (not exhaustive):

- funded research and development cost-sharing arrangements; [220-40-55-18]
- management fees; [ASU 2024-03.BC112]
- government grants; and
- transition services agreements in acquisitions of businesses (see Question 4.3.90 in KPMG Handbook, [Financial statement presentation](#)).

This assessment may require judgment because whether the guidance applies may depend on the terms of the arrangements and how they are accounted for – e.g. for a cost reimbursement received it would depend on whether the amount is presented as income or contra expense in the income statement. This guidance may be relevant even if an arrangement provides for the reimbursement of only one type of cost (e.g. employee compensation).

Question 4.4.20 How are expense reimbursements received disclosed?

Interpretive response: When a relevant expense caption includes amounts that are net of an expense reimbursement received, the tabular disclosure for that caption may be presented in one of two ways: [220-40-50-26]

- Expense reimbursement amount as a separate line item – i.e. a gross approach; or
- Expenses net of any reimbursement effects – i.e. a net approach.

Depending on which approach is elected (i.e. gross or net), there are additional disclosure requirements, as follows.

Disclosure requirement for both interim and annual reporting periods	Expense reimbursement received	
	Gross approach	Net approach
Statement indicating how expense reimbursements are presented in the tabular disclosure [220-40-50-27]	✓	✓
Qualitative description of the nature of the expense to which the reimbursement relates [220-40-50-29]	✓	✗
Amounts of the expense categories required by paragraphs 220-40-50-6 (see chapter 2) and 220-40-50-21 to 50-22 (see section 5.2) that are included in the relevant expense caption net of any reimbursement effects [220-40-50-26(b)]	✗	✓

FASB Example 2 (reproduced in [section 8.2](#)) illustrates the reporting of expense reimbursements received and included in the R&D expense caption.

Question 4.4.30 How are expense reimbursements paid disclosed?

Interpretive response: Expense reimbursements paid that are included in a relevant expense caption are disaggregated separately as an expense category in the tabular disclosure for that caption. Similar to when expense reimbursements received are reported separately in the tabular disclosure (see the gross presentation in [Question 4.4.20](#)), the following disclosures are required. [220-40-50-28, 220-40-50-29, ASU 2024-03.BC112]

Disclosure requirement for both interim and annual reporting periods	Expense reimbursement received
Qualitative description of the nature of the expense to which the reimbursement relates [220-40-50-29]	✓

As a result of this requirement, expense reimbursements paid to another entity cannot be combined with other required natural expense categories in the tabular disclosure, even if the reimbursement is for one type of cost only. For example, the amount paid by an entity to reimburse a third party for employee compensation costs incurred by the third party does not meet the definition of employee compensation for the entity and therefore cannot be included in the employee compensation category (see [Questions 3.4.20](#) and [3.4.30](#)). The amount is reported separately in the tabular disclosure and the nature of the expense to which the reimbursement relates (i.e. employee compensation) is described. [ASU 2024-03.BC112]

4.5 Disaggregation of relevant expense captions with inventory amounts

Excerpt from ASC 220-40

> Overall Guidance

- > Expense Disaggregation Disclosures
- • > Identification of Relevant Expense Captions

50-12 ...Furthermore, in accordance with paragraph 220-40-50-31, when a relevant expense caption contains amounts within the scope of Topic 330, an entity shall apply its chosen basis for disaggregating amounts within the scope of Topic 330 to the expense categories listed in paragraph 220-40-50-6.

• > Disclosure of the Disaggregation of Relevant Expense Captions That Contain Amounts within the Scope of Topic 330

50-31 The following are two acceptable bases for disclosing the disaggregation of a relevant expense caption that contains expense amounts related to inventory within the scope of Topic 330:

- a. Cost-incurred basis. The amounts disclosed for the disaggregation of a relevant expense caption comprise costs incurred that were capitalized to inventory in accordance with Topic 330 during the current reporting period and any costs incurred that were directly expensed during the current reporting period (including costs that are capitalizable in accordance with Topic 330 but were directly expensed to the income statement). Under this basis, in interim and annual reporting periods, an entity shall disclose an amount for changes in inventories and an amount for other adjustments and reconciling items to reconcile the costs incurred to the total relevant expense caption (see paragraphs 220-40-50-32 through 50-34).
- b. Expense-incurred basis. The amounts disclosed for the disaggregation of a relevant expense caption comprise expense amounts related to the derecognition of inventory that was previously capitalized in accordance with Topic 330 and any costs incurred that were directly expensed during the current reporting period (including costs that are capitalizable in accordance with Topic 330 but were directly expensed to the income statement). Under this basis, an entity shall disclose the expense amounts related to the derecognition of inventory based on the natural expense category of the costs when they were initially incurred (for example, the expense from the derecognition of inventory may relate to purchases of inventory and employee compensation incurred in prior periods).

In many cases, an entity's chosen basis will result in disclosed amounts that are different than if the entity had chosen the alternative basis. An entity's chosen basis should be applied consistently to all expense categories listed in paragraph 220-40-50-6.

• • > Changes in Inventories When the Cost-Incurred Basis Is Applied

50-32 When the amounts disclosed in accordance with paragraph 220-40-50-6 include costs incurred that were capitalized to inventory in accordance with

Topic 330 during the reporting period (because an entity has applied the cost-incurred basis in paragraph 220-40-50-31(a)), those amounts often will not equal the amounts expensed as incurred during the reporting period. If the amount of expense recognized and the amount of costs incurred in the current reporting period are not equal, then an entity shall disclose in interim and annual reporting periods a category for the changes in inventories balances to reconcile the costs incurred (which shall include costs capitalized to inventory and costs expensed during the reporting period) to expenses recognized. The amount disclosed for changes in inventories in the current reporting period shall equal the difference between the amount of inventory included on the balance sheet at the end of the prior reporting period and the amount of inventory included on the balance sheet at the end of the current reporting period. As described in paragraph 220-40-50-33, a separate category that comprises any other adjustments and reconciling items shall be provided to reconcile costs incurred to expenses recognized during the reporting period.

• • > Other Adjustments and Reconciling Items When the Cost-Incurred Basis Is Applied

50-33 In addition to the changes in inventories category described in paragraph 220-40-50-32, for interim and annual reporting periods, under the cost-incurred basis (see paragraph 220-40-50-31(a)), an entity shall disclose the amount of other adjustments and reconciling items that include (to the extent not disclosed in a separate caption) other amounts that are necessary to reconcile costs incurred to expenses recognized. For example, those items would include, if applicable:

- a. The amount of inventory derecognized during the period that is not recognized as an expense (for example, inventory derecognized as part of derecognition transactions within the scope of Subtopic 810-10 on consolidation)
- b. The amount attributable to differences in the foreign currency exchange rates used to translate costs incurred, the beginning balance of inventory, and the ending balance of inventory in accordance with Subtopic 830-30 on foreign currency matters—translation of financial statements.

50-34 Consistent with the requirements in paragraph 220-40-50-30, for interim and annual reporting periods, an entity shall qualitatively describe the nature of amounts (based on their natural expense classification when applicable) included in other adjustments and reconciling items in accordance with paragraph 220-40-50-33.

Subtopic 220-40 requires disaggregation of amounts capitalized to inventory under Topic 330 (further referred to as 'inventory amounts'). This is an exception to other asset-related capitalized amounts, which do not require disaggregation (see [section 4.2](#)). This requirement is intended to provide financial statement users more visibility into the nature and type of costs included in COGS and similar expense captions. [\[ASU 2024-03.BC66\]](#)

Obtaining detailed information about natural expense categories (see [chapter 3](#)) can be challenging in practice. Once costs are capitalized to inventory, their original nature is often lost or obscured, as inventory balances are typically tracked in aggregate within reporting systems. As a result, it can be difficult to accurately identify the underlying nature of inventory amounts when they are

subsequently expensed to COGS or similar expense captions. [ASU 2024-03.BC67, BC72]

In light of these practical limitations, two options are provided for disaggregating relevant expense captions that contain inventory amounts. [220-40-50-31]

Cost-incurred basis	Expense-incurred basis
Amounts are disclosed based on amounts capitalized to inventory and directly expensed during the current period (see section 4.5.10).	Amounts are disclosed based on expenses related to the derecognition of inventory, including costs previously capitalized, and directly expensed during the current period (see section 4.5.20).

Although amounts disclosed can differ under each basis, the enhanced disclosures resulting from either basis are expected to provide more decision-useful expense information and transparency of inventory cost information. [220-40-50-31, ASU 2024-03.BC28(b), BC74 – BC75]

When a relevant expense caption contains inventory amounts, the selected basis for disaggregation is to be applied consistently to all required natural expense categories in that caption. [220-40-50-31]

While consistency is also expected across reporting periods, an entity may change its disaggregation basis. See [section 1.5](#) for the relevant requirements.

The following table summarizes the expected classification of various inventory amounts and inventory related transactions under the cost-incurred basis and expense-incurred basis. This table assumes no voluntary disclosures are provided (see [Question 5.3.10](#)).

Inventory amounts recognized from the following transactions	Expected classification under cost-incurred and expense-incurred bases
Direct acquisition from third party (i.e. external spend) of tangible items in the scope of Topic 330 (e.g. raw materials, supplies, WIP and finished goods) See Question 3.3.20 for considerations about the cost of purchases, relative to direct acquisition costs (e.g. external inbound shipping costs and associated tariffs)	Purchases of inventory
Intercompany transactions See Question 3.3.40	- Required natural expense category based on nature (e.g. employee compensation, depreciation, etc.) from the perspective of the reporting entity 'Other items', if not captured within a required natural expense category
Business combination (Subtopic 805-10) See Question 3.3.30	'Other items'

Inventory amounts recognized from the following transactions	Expected classification under cost-incurred and expense-incurred bases
Joint venture formation (Subtopic 805-60) See Question 3.3.30	'Other items'
Initial consolidation of a VIE (Subtopic 810-10) See Question 3.3.30	'Other items'
Purchases of items not in the scope of Topic 330 (i.e. items colloquially referred to as inventory) See Question 4.2.10	'Other items'
Capitalization of inventoriable labor, overhead or manufacturing costs See Question 4.5.40	- Required natural expense category based on nature (e.g. employee compensation, depreciation, etc.) 'Other items', if not captured within a required natural expense category
Standard cost variances See Question 4.5.40	- Required natural expense category based on nature (e.g. purchases of inventory, employee compensation, etc.) 'Other items', if not captured within a required natural expense category
Inventory remeasurement (e.g. impairment) See Question 4.5.30	'Other items' or - Changes in inventory (cost-incurred basis only)
Derecognition (e.g. deconsolidation) See Question 4.5.80	'Other adjustments and reconciling items' (cost-incurred basis only)
Foreign exchange translation effects See Question 4.5.80	'Other adjustments and reconciling items' (cost-incurred basis only)

Question 4.5.10 How do the cost-incurred and expense-incurred bases compare?

Interpretive response: The requirements of each basis are outlined in the following table. [220-40-50-31, ASU 2024-03.BC69]

Disclosure requirement	Acceptable bases	
	Cost-incurred	Expense-incurred
The amounts disclosed for each required natural expense in a relevant expense caption comprise the following:		
Costs incurred that are capitalized to inventory under Topic 330 during the current reporting period	✓	✗

Disclosure requirement	Acceptable bases	
	Cost-incurred	Expense-incurred
Expense amounts related to the derecognition of inventory that was previously capitalized under Topic 330, based on the natural expense category of the costs when they were initially incurred	✗	✓
Costs incurred that are directly expensed during the current reporting period (including costs that are capitalizable under Topic 330)	✓	✓
In addition, the tabular disclosure for the relevant expense caption includes the following:		
Amounts required to be reported separately (see section 5.2), or reported separately voluntarily (see Question 5.3.10)	✓	✓
'Other items' category, accompanied by a qualitative disclosure of the nature of the amounts included (see section 5.3 and Question 4.5.20) [220-40-50-30, 220-40-55-6, 55-11]	✓	✓
'Changes in inventory' category (see Question 4.5.70)	✓	✗
'Other adjustments and reconciling items' category, accompanied by a qualitative disclosure of the nature of the amounts included (see Question 4.5.80) [220-40-50-34]	✓	✗

Expenses presented in the income statement will not equal costs incurred during a given period. As a result, when the cost-incurred basis is used, two additional categories are required in the tabular disclosure ('changes in inventories' and 'other adjustments and reconciling items') to reconcile to the total amount of the expense caption. [220-40-50-31(a)]

The elected basis for disaggregation applies consistently to all inventory amounts in a relevant expense caption. For example, if an entity selects the cost-incurred basis, it would apply that basis to purchases of inventory, employee compensation, intangible asset amortization, and depreciation within the relevant expense caption. We believe the elected basis should also be applied consistently to inventory amounts that are included within the 'other items' category (see [Question 4.5.20](#)). [220-40-50-31, ASU 2024-03.BC69]

Example 4.5.10 Cost-incurred vs expense-incurred basis

In the reporting period, ABC Corp. purchases \$60 of parts (10 parts with a unit price of \$6) and incurs employee compensation for \$40 to manufacture 10 finished goods. ABC sells 8 finished goods (i.e. COGS is \$80). Opening inventory is zero and closing inventory is \$20.

ABC provides the following disclosure to disaggregate the COGS relevant expense caption depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred basis
Purchases of inventory	60	48 ¹
Employee compensation	40	32 ²
Changes in inventories	(20)	Category does not apply
Total cost of goods sold	80	80
Notes:		
1. 8 units sold × \$6 per unit of parts purchases		
2. \$40 employee compensation × 8/10 (units sold ÷ units produced)		

Question 4.5.20 What is included in ‘other items’ in the disaggregation of COGS (or other relevant caption with inventory amounts)?

Interpretive response: The ‘other items’ category is a concept that applies to the disaggregation of *all* relevant expense captions (see [Question 5.3.20](#)) and is therefore relevant under both the cost-incurred and the expense-incurred bases. It represents amounts recorded within a relevant expense caption that do not require disaggregation (i.e. do not represent a required natural category) or separate reporting in the tabular disclosure (see [section 5.2](#)).

Other items in COGS (or other relevant income statement caption with inventory amounts) may include purchased services or operating lease payments (if not required to be reported separately – see [Question 5.2.20](#)), whether inventoriable or not. FASB Example 1 (reproduced in [section 8.1](#)) illustrates this category labeled ‘other cost of product sold’ and being used for the effects of business combinations and similar transactions related to inventory amounts (see [Question 3.3.30](#)), outbound freight costs and remeasurement expenses on an environmental obligation liability. [\[220-40-55-11\]](#)

Although the ‘other items’ category is relevant under both bases and should theoretically capture the same types of items, its amount may not be the same. This is because ‘other items’ may include inventoriable costs whose amounts may vary depending on which basis is used. This is illustrated in [Example 4.5.20](#).

Example 4.5.20 Other items under cost-incurred vs expense-incurred basis

In the reporting period, ABC Corp. purchases \$60 of parts (10 parts with a unit price of \$6) and outsources assembly to a third-party contractor for \$40. Out of the 10 finished goods products manufactured, ABC sells 8 (i.e. COGS is \$80). Opening inventory is zero and closing inventory is \$20.

ABC provides the following disclosure to disaggregate the COGS relevant expense caption depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred basis
Purchases of inventory	60	48 ¹
Other items (purchased services)	40	32 ²
Changes in inventories	(20)	Category does not apply
Total cost of goods sold	80	80

Notes:

- 8 units sold × \$6 per unit of parts purchases
- \$40 paid to third-party contractor × 8/10 (units sold ÷ units produced)

Question 4.5.30 In which category are inventory remeasurements included?

Background: Remeasurements of inventory may be due to one of the following.

- **Impairment losses:** Inventory is generally carried at cost until it either becomes impaired or is sold or otherwise disposed of. [330-10-35-1A]
- **Remeasurement at net realizable value:** In exceptional cases, certain inventories are stated above cost – e.g. agricultural products. [330-10-35-16]

Interpretive response: Subtopic 220-40 is silent on where to include inventory remeasurements in the tabular disclosure. Under the expense-incurred basis, we believe including these effects in 'other items' is appropriate, because they do not belong to any of the required natural expense categories. We believe the same presentation is also appropriate under the cost-incurred basis, but alternatively these remeasurements can be presented in the 'changes in inventory' category.

Example 4.5.30 Inventory impairment

ABC Corp.'s opening inventory is \$100 and closing inventory is \$20. The change in inventory balance is due entirely to the inventory being impaired. The impairment loss of \$80 is recognized as an expense in COGS. No inventory was purchased, manufactured or sold in the reporting period.

ABC provides the following disclosure to disaggregate the COGS relevant expense caption depending on which approach it elects.

Cost of goods sold	Cost-incurred basis		Expense-incurred basis
	Option 1	Option 2	
Other items	80	-	80
Changes in inventories	-	80	Category does not apply
Total cost of goods sold	80	80	80

Question 4.5.40 In which category are standard cost variances included?

Background: Standard costing is used by certain entities to approximate the cost of inventory. An entity will establish a standard cost for a product based on a budget or forecast prior to the start of the fiscal year that encompasses its expectation of the unit cost of the product inclusive of material, labor and overhead cost components. For Subtopic 220-40 purposes, the cost components of the standard cost estimate are disaggregated based on their nature (e.g. purchased materials, labor, machinery depreciation, overhead, etc.) and presented within the applicable required natural expense category.

Topic 330 acknowledges that standard costing is an acceptable method to approximate the cost of inventory, regardless of the cost flow assumption used (i.e. first-in first-out (FIFO), average cost, or last-in first-out (LIFO)). However, standard costs are only acceptable if adjusted at reasonable intervals to reflect current conditions, so that at the reporting date standard costs reasonably approximate costs computed under the selected cost flow assumption. When variances between actual costs incurred and standard cost are identified (whether favorable or unfavorable) for inventory on hand at the reporting date, these normal variances are capitalized to ensure standard cost approximates actual inventory cost under one of the cost flow assumptions. [330-10-30-12]

For further guidance on inventory cost flow assumptions, see section 3.3 in KPMG Handbook, [Inventory](#).

Interpretive response: Subtopic 220-40 is silent on where to include standard cost variances. Because standard costing is only acceptable as a proxy for actual costs, we believe these variances should be allocated to the underlying cost nature they relate to (i.e. the same natural categorization as the related standard cost components), in order for inventoriable costs to be reflected at their actual amounts incurred. For example, pricing variances on raw materials should be categorized as purchases of inventory, but manufacturing variances may encompass several natural expense categories.

Example 4.5.40 Standard cost variances

In Year 1, ABC Corp. manufactures Product X and sells no inventory. In Year 2, all inventory is sold. ABC uses standard costing and adjusts the cost of

inventory on the balance sheet at the end of Year 1 to reflect actual conditions, as follows.

Costs capitalized to inventory	Standard cost set at beginning of Year 1	Cost variance	Cost adjusted at end of Year 1
Purchases of inventory	10	3	13
Employee compensation	5	(2)	3
Costs capitalized to inventory	15	1	16

In Year 1, ABC discloses the following to disaggregate the COGS relevant expense caption depending on which approach it elects.

Cost of goods sold	Cost-incurred basis ¹	Expense-incurred basis
Purchases of inventory	13	-
Employee compensation	3	-
Changes in inventory	(16)	Category does not apply
Total cost of goods sold	-	-

Note:

1. Any variances are classified based on their respective nature (i.e. the net cost variance of \$1 is reflected as follows: \$3 through purchases of inventory and \$(2) through employee compensation).

In Year 2, there are no further cost adjustments, and all inventory is sold. ABC discloses the following depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred basis
Purchases of inventory	-	13
Employee compensation	-	3
Changes in inventory	16	Category does not apply
Total cost of goods sold	16	16

4.5.10 The cost-incurred basis

The cost-incurred basis is one of the two acceptable bases that can be applied to disaggregate relevant expense captions that contain inventory. [220-40-50-31]

Question 4.5.50 How is the cost-incurred basis applied?

Interpretive response: The cost-incurred basis allows entities to disaggregate costs capitalized to inventory based on their nature when incurred. [220-40-50-14, ASU 2024-03.BC44]

It includes the following requirements. [220-40-50-31]

Disclosure requirement
The amounts disclosed for the disaggregation of a relevant expense caption comprise the following:
Costs incurred that are capitalized to inventory under Topic 330 during the current reporting period. Amounts are reflected based on their nature.
Costs incurred that are directly expensed during the current reporting period (including costs that are capitalizable under Topic 330). Amounts are reflected based on their nature.
In addition, the tabular disclosure for the relevant expense caption includes the following:
Amounts required to be reported separately (see section 5.2) or that are reported separately voluntarily (see Question 5.3.10).
'Other items' category, accompanied by a qualitative disclosure of the nature of the amounts included (see section 5.2 and Questions 4.2.10 and 5.3.20). [220-40-50-30, 220-40-55-6, 55-11]
'Changes in inventory' category (see Question 4.5.70).
'Other adjustments and reconciling items' category, accompanied by a qualitative disclosure of the nature of the amounts included (see Question 4.5.80). [220-40-50-34]

When elected, the cost-incurred basis applies consistently to all inventory amounts in a relevant expense caption (see [Question 4.5.10](#)). [220-40-50-31(a), ASU 2024-03.BC69]

Question 4.5.60 What is included in the required natural expense categories when the cost-incurred basis is applied?

Interpretive response: Under the cost-incurred basis, each required natural expense category comprises costs incurred that are either (1) capitalized to inventory or (2) directly expensed during the current period, whether related to inventory or not. The table below illustrates this requirement. [ASU 2024-03.BC69]

Required natural expense categories	Expected items included
Purchases of inventory (see section 3.3)	Purchases of inventory incurred that are capitalized or directly expensed during the current period
Employee compensation (see section 3.4)	- Inventoriable employee compensation costs – i.e. costs incurred that are capitalized in inventory - Inventory-related employee compensation costs directly expensed during the current period – e.g. unallocated fixed overhead due to abnormally low production or an idle plant - All other non-inventory employee compensation costs expensed during the current period

Required natural expense categories	Expected items included
Depreciation (see section 3.5)	• Inventoriable depreciation costs – i.e. costs incurred that are capitalized in inventory • Depreciation of inventory-related PP&E directly expensed during the current period – e.g. unallocated depreciation of manufacturing plant and equipment due to abnormally low production or an idle plant • All other non-inventory depreciation expenses during the current period
Intangible asset amortization (see section 3.6)	• Inventoriable intangible asset amortization costs – i.e. costs incurred that are capitalized in inventory • Amortization of inventory-related intangible assets directly expensed during the current period – e.g. unallocated amortization of patents used in the manufacturing process due to abnormally low production or an idle plant • All other non-inventory intangible asset amortization expenses during the current period

Question 4.5.70 What is included in the 'changes in inventory' category?

Interpretive response: The 'changes in inventory' category is used to reconcile the costs incurred (i.e. sum of costs capitalized and directly expensed) for the period to the expenses reported for the period within a relevant expense caption when these amounts are not equal. This category represents the change in the inventory balance from the beginning of the period to the end of the period and can be directly calculated from the balance sheet. [\[220-40-50-32, ASU 2024-03.BC68, BC70\]](#)

Question 4.5.80 What is included in the 'other adjustments and reconciling items' category?

Interpretive response: An 'other adjustments and reconciling items' category may be needed to reconcile the costs incurred (i.e. sum of costs capitalized and directly expensed) and the change in inventory (see [Question 4.5.70](#)) for the period to the total expenses reported for the period within a relevant expense caption. This category is accompanied by a qualitative description of the nature of the amounts included. [\[220-40-50-33 – 50-34, ASU 2024-03.BC70\]](#)

This category captures the effects of transactions that affect the beginning and ending balances of inventory but do *not* have an associated expense, such as: [\[220-40-50-33, ASU 2024-03.BC71\]](#)

- inventory derecognized during the current reporting period that is not recognized as an expense, such as inventory derecognized as a result of

the sale of a business or deconsolidation transactions accounted for under Subtopic 810-10 (see [Example 4.5.50](#)); and

- foreign currency exchange rate effects from translating beginning and ending inventory balances and costs incurred during the period determined under Subtopic 830-30. Such translation adjustments that result from translating a foreign functional currency into the reporting currency are recorded in other comprehensive income and therefore are not recognized as expenses within relevant expense captions (see [Example 4.5.60](#)). [830-30-45-12]

By contrast to the 'other items' category (see [Question 4.5.20](#)), the 'other adjustments and reconciling items' category is *only* applicable when the cost-incurred basis of disaggregation is selected for a relevant expense caption that contains inventory amounts. Therefore, the category is intended to capture reconciling items that only exist as a result of the application of the cost-incurred basis. [220-40-50-7, 50-33]

Example 4.5.50 Deconsolidation transaction under the cost-incurred basis

ABC Corp.'s opening inventory is \$100 and closing inventory is \$20. The change in inventory balance is due entirely to the inventory derecognized as a result of the sale of a business (deconsolidation transaction accounted for under Subtopic 810-10) that held \$80 of inventory. Aside from this deconsolidation transaction, ABC purchased and sold \$10 of inventory during the period.

ABC discloses the following to disaggregate the COGS relevant expense caption depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred basis
Purchases of inventory	10	10
Other adjustments and reconciling items (sale of business)	(80)	Category does not apply
Changes in inventories	80	Category does not apply
Total cost of goods sold	10	10

Example 4.5.60 Translation adjustments under the cost-incurred basis

ABC Corp. is domiciled in the US, and its reporting currency is the US dollar. ABC's wholly owned subsidiary, DEF Corp. is domiciled in the UK, and its functional currency is the Great British Pound (GBP).

Beginning inventory held by DEF is 100 GBP, and GBP = USD. Ending inventory is 110 USD and is entirely attributed to translation adjustments of \$10 recorded in other comprehensive income due to the change in exchange rates between

GBP and USD. Aside from DEF's inventory on hand, ABC purchased and sold \$5 of inventory during the period.

ABC discloses the following to disaggregate the COGS relevant expense caption depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred basis
Purchases of inventory	5	5
Other adjustments and reconciling items (foreign currency translation effect)	(10)	Category does not apply
Changes in inventories	10	Category does not apply
Total cost of goods sold	5	5

4.5.20 The expense-incurred basis

The expense-incurred basis is one of the two acceptable bases that can be applied to disaggregate relevant expense captions that include inventory. [220-40-50-31]

Question 4.5.90 How is the expense-incurred basis applied?

Interpretive response: The expense-incurred basis allows entities to disaggregate inventory-related amounts actually expensed during the current period.

It includes the following requirements. [220-40-50-31]

Disclosure requirement
The amounts disclosed for the disaggregation of a relevant expense caption comprise the following:
Expense amounts related to the derecognition of inventory that was previously capitalized under Topic 330, based on the natural expense category of the costs when they were initially incurred.
Costs incurred that are directly expensed during the current reporting period (including costs that are capitalizable under Topic 330). Amounts are reflected based on their nature.
In addition, the tabular disclosure for the relevant expense caption includes the following:
Amounts required to be reported separately (see section 5.2) or that are reported separately voluntarily (see Question 5.3.10).
'Other items' category, accompanied by a qualitative disclosure of the nature of the amounts included (see section 5.2 and Questions 4.2.10 and 5.3.20). [220-40-50-30, 55-6, 55-11]

When elected, the expense-incurred basis applies consistently to all inventory amounts in a relevant expense caption (see [Question 4.5.10](#)). [220-40-50-31(b), ASU 2024-03.BC69]

The cost of each item of sold inventory is disaggregated based on its initial nature prior to capitalization (e.g. purchases of inventory, employee compensation). This requirement may create practical challenges to track costs across several periods, which may be exacerbated by the cost flow assumption used. This is illustrated in [Example 4.5.70](#). [220-40-50-31(b), ASU 2024-03.BC69]

Similar to entities applying the cost-incurred basis, entities applying the expense-incurred basis may disclose an amount for ‘other items’ within a relevant expense caption along with a qualitative description of the nature of the amounts included (see [Question 4.5.20](#)). [220-40-50-30]

4.5.30 Practical considerations when electing a disaggregation basis

Question 4.5.100 What considerations may be relevant in electing the cost-incurred basis or the expense-incurred basis?

Interpretive response: Entity specific facts and circumstances are relevant in determining which basis to use when applying the disaggregation requirements to a relevant expense caption that contains inventory amounts. Example considerations (not exhaustive) that may be relevant to this decision are included in the following table.

Consideration	Basis of disaggregation expected to be selected		
	Cost-incurred	Expense-incurred	Rationale
Existing reporting systems have the ability to track natural expense information from initiation through the inventory production process and up until derecognition [ASU 2024-03.BC28(b), BC72]	✗	✓	Natural expense information is available to produce the required disclosure information.
Existing reporting systems only track information at an account level and nature is lost after capitalization [ASU 2024-03.BC28(b), BC67, BC72]	✓	✗	Natural expense information is <i>not</i> available to produce the required disclosure information.
Production and sales volumes are significantly different in a given period [ASU 2024-03.BC74]	✗	✓	The expense amounts disclosed under the expense-incurred basis more directly relate to the sales

Consideration	Basis of disaggregation expected to be selected		
	Cost-incurred	Expense-incurred	Rationale
			volume. The cost-incurred basis may be less intuitive in periods where production and sales volumes vary significantly.
Production and sales volumes are significantly different in a given period, but additional information is provided regarding inventory turnover, trends, seasonality or volatility [ASU 2024-03.BC74]	✓	✗	Separate insights provided may help users of the financial statements better understand expense information provided under the cost-incurred basis.
Inventory primarily consists of purchased finished goods for sale	✗	✓	Given the nature of the inventory balances may be primarily 'purchases of inventory', the expense-incurred basis may be practical to apply.
High inventory turnover	✗	✓	Given the shorter lag between when the inventory costs are incurred (capitalization) and expensed (derecognition), the expense-incurred basis may be practical to apply.
✓ – Expected to be selected. ✗ – Not expected to be selected.			

Inventory cost flow assumptions

Each inventory cost flow assumption (i.e. FIFO, LIFO, average cost, specific identification or RIM) introduces different practical challenges when disaggregating inventory-related cost information by natural expense category. The use of standard costing may further complicate that process. These challenges need to be considered when selecting which disaggregation basis to apply.

The operational application of these costing methods – whether inventory cost are tracked systematically and tagged to individual units or allocated periodically – directly affects both the availability and granularity of expense data. This in turn affects an entity's ability to trace costs back to their original natural expense categories. For example, under LIFO, applying the expense-incurred basis may present difficulties if a significantly aged layer is liquidated, as the nature of the original expense may no longer be identifiable. [ASU 2024-03.BC67, BC73]

Entities planning to change or upgrade their inventory accounting systems should carefully consider how such changes may affect their ability to comply with the requirements of Subtopic 220-40.

For a detailed discussion of inventory cost flow, see section 3.3 of KPMG Handbook, [Inventory](#).

Additional practical considerations for complying with disaggregation requirements are addressed in [section 7.3](#).

Example 4.5.70 Cost-incurred vs expense-incurred basis, under FIFO vs LIFO

In Year 1, ABC Corp. manufactures 30 units of Product X as follows:

- **Batch 1:** 10 units. Unit price is \$1.80 comprised of \$1 for parts and \$0.80 for labor.
- **Batch 2:** 20 units. Unit price is \$2 comprised of \$1.40 for parts and \$0.60 for labor.

No units were sold in Year 1 and various different scenarios are provided for sales in Year 2.

Costs capitalized for these products (reflected in inventory on the balance sheet at the end of Year 1) are as follows.

Costs capitalized to inventory	Batch 1	Batch 2	Total
Purchases of inventory	10	28	38
Employee compensation	8	12	20
Costs capitalized to inventory	18	40	58

In Year 1, ABC discloses the following to disaggregate the COGS relevant expense caption depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred basis
Purchases of inventory	38	-
Employee compensation	20	-
Changes in inventory	(58)	Category does not apply
Total cost of goods sold	-	-

Scenario 1: All units are sold in Year 2

In Year 2, ABC discloses the following depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred- basis
Purchases of inventory	-	38
Employee compensation	-	20

Cost of goods sold	Cost-incurred basis	Expense-incurred- basis
Changes in inventory	58	Category does not apply
Total cost of goods sold	58	58

Scenario 2: 25 units are sold in Year 2 – ABC applies FIFO to its inventory

In Year 2, ABC discloses the following depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred basis
Purchases of inventory ¹	-	31
Employee compensation ²	-	17
Changes in inventory	48	Category does not apply
Total cost of goods sold	48	48

Notes:

1. All 10 units from Batch 1 (parts cost of \$10), and 15 units from Batch 2 (parts cost of \$21, or unit cost of $\$1.40 \times 15$ units).
2. All 10 units from Batch 1 (labor cost of \$8), and 15 units from Batch 2 (labor cost of \$9, or unit cost of $\$0.60 \times 15$ units).

Scenario 3: 25 units are sold in Year 2 – ABC applies LIFO to its inventory

In Year 2, ABC discloses the following depending on which approach it elects.

Cost of goods sold	Cost-incurred basis	Expense-incurred basis
Purchases of inventory ¹	-	33
Employee compensation ²	-	16
Changes in inventory	49	Category does not apply
Total of cost of goods sold	49	49

Notes:

1. All 20 units from Batch 2 (parts cost of \$28), and 5 units from Batch 1 (parts cost of \$5, or unit cost of $\$1 \times 5$ units).
2. All 20 units from Batch 2 (labor cost of \$12), and 5 units from Batch 1 (labor cost of \$4, or unit cost of $\$0.80 \times 5$ units).

5. Disclosure requirements and tabular disclosure

Detailed contents

5.1 How the standard works

5.2 One stop shop table

Questions

Question 5.2.10 Which specific expenses, gains and losses are always reported separately in the tabular disclosure?

Question 5.2.20 Which specific expenses, gains and losses are reported separately in the tabular disclosure only if they are included entirely in one relevant expense caption?

Question 5.2.30 Does the tabular disclosure require recasting when a specific expense, gain or loss is no longer included entirely in one relevant expense caption (or vice versa)?

Question 5.2.40 Are the specific expenses, gains and losses required to be reported separately in the tabular disclosure at each interim and annual period?

Example

Example 5.2.10 Change in display of operating lease costs

5.3 Voluntary disclosures and other items

Questions

Question 5.3.10 What are the parameters regarding voluntary disclosure of additional expense categories?

Question 5.3.20 How are 'other items' remaining in relevant expense captions disclosed?

Example

Example 5.3.10 Voluntary disclosure of an incremental expense category and subtotal

5.1 How the standard works

Each relevant expense caption (see [chapter 2](#)) is disaggregated in a tabular format disclosure in the notes to the financial statements. The tabular disclosure not only disaggregates the amounts for the five required natural expense categories (see [chapter 3](#)), but also separately includes (as a separate line item) certain other items in a relevant expense caption that are required to be disclosed by Topics and Subtopics other than Subtopic 220-40. In this regard, Subtopic 220-40 introduces a ‘one-stop-shop’ approach that explains the nature and location of certain types of expenses, gains or losses included in the income statement and reduces the amounts disclosed as a part of ‘other items’.

Subtopic 220-40 provides a list of which items currently required to be disclosed under other Codification Topics or Subtopics need to be reported separately in the tabular disclosure. Some items are always reported separately if present in a relevant expense caption, and some items are only reported separately if the expense is entirely recorded in a single relevant expense caption.

As a result of the requirements explained earlier in [chapters 2 to 4](#) and the above requirements, the tabular disclosure for a single relevant expense caption may need to separately report all the following items, if relevant to the caption.

Items included in tabular disclosure	Details	Section or Question
Required natural expense categories	Purchases of inventory	Section 3.3
	Employee compensation	Section 3.4
	Depreciation	Section 3.5
	Intangible asset amortization	Section 3.6
	DD&A	Section 3.7
Expense reimbursements	Expense reimbursement amount received (optional)	Question 4.4.20
	Expense reimbursement amount paid	Question 4.4.30
Items relevant only if the caption includes inventory amounts and the cost-incurred basis is applied	Changes in inventory	Question 4.5.70
	Other adjustments and reconciling items	Question 4.5.80
Specific expenses, gains and losses already required to be disclosed under US GAAP	Items always reported separately	Question 5.2.10
	Items reported separately only if included entirely in one relevant expense caption	Question 5.2.20
Items voluntarily disclosed		Question 3.2.20 Question 5.3.10
Other items		Question 5.3.20

This section specifically addresses the requirements to report separately in the tabular disclosure certain expenses, gains and losses required to be disclosed under other Codification Topics or Subtopics. See the light blue highlighted rows in the above table. The existence of these specific expenses, gains and losses within an income statement caption does not make the caption 'relevant', i.e. subject to disaggregation under Subtopic 220-40.

Items that are not required to be reported separately in the tabular disclosure can be voluntarily disclosed or included in the 'other items' category. See the light green highlighted rows in the above table. This is addressed in [section 5.3](#).

5.2 One stop shop table

Excerpt from ASC 220-40

> Overall Guidance

• > Tabular Integration of Other Disclosure Requirements

50-21 An entity shall disclose, in the same tabular format disclosure in which the disclosures required by paragraph 220-40-50-6 are provided, each of the following expenses, gains, and losses and the amount recognized in each relevant expense caption (see paragraphs 220-40-50-12 through 50-13 for guidance on identifying relevant expense captions):

- a. The amount of research and development assets acquired in a transaction other than a business combination and written off (see paragraph 350-30-50-1(c))
- b. Impairment loss recognized related to an intangible asset (see paragraph 350-30-50-3)
- c. **Impairment** loss of long-lived assets classified as held and used (see paragraph 360-10-50-2)
- d. Gain or loss recognized in accordance with paragraphs 360-10-35-37 through 35-45 and 360-10-40-5 for long-lived assets classified as held for sale or disposed of (see paragraph 360-10-50-3)
- e. Each major type of cost associated with an exit or disposal activity (for example, one-time employee termination benefits, contract termination costs, and other associated costs) (see paragraph 420-10-50-1)
- f. Components of net benefit cost recognized (other than service cost amounts included within employee compensation) (see paragraph 715-20-50-1(h))
- g. Bargain purchase gain recognized in a business combination (see paragraph 805-30-50-1(f))
- h. Any gain or loss recognized upon the deconsolidation of a **subsidiary** or the derecognition of a group of assets in accordance with paragraph 810-10-40-3A (see paragraph 810-10-50-1B)
- i. Gains and losses on **derivative instruments** (and nonderivative instruments that are designated and qualify as hedging instruments in accordance with paragraphs 815-20-25-58 and 815-20-25-66) and related hedged items (see paragraph 815-10-50-4A)
- j. Amortization of **license agreements** for program material (see paragraph 920-350-50-2)
- k. Impairment of license agreements for program material (see paragraph 920-350-50-4)
- l. Amortization of **film costs** (see paragraph 926-20-50-4A)
- m. Impairment of film costs (see paragraph 926-20-50-4C).

These disclosures shall be included in the tabular format disclosure required by paragraph 220-40-50-6 using the same frequency (that is, whether the disclosure is required at interim and annual reporting periods or only annual reporting periods) as required by the corresponding Topic.

50-22 An entity shall disclose, in the same tabular format disclosure in which the disclosures required by paragraph 220-40-50-6 are provided, each of the

following amounts if those amounts are included entirely in one expense caption that also is a relevant expense caption (see paragraphs 220-40-50-12 through 50-13 for guidance on identifying relevant expense captions):

- a. Provision for expected credit losses (see paragraphs 326-20-50-13 and 326-30-50-9)
- b. Losses on firm purchase commitments (see paragraph 330-10-50-5)
- c. Amortization expense attributable to the expiration of an insurance or **reinsurance** coverage provided under a contract that transfers only significant **underwriting risk** (see paragraph 340-30-50-2)
- d. Amortization of costs to fulfill a contract with a customer (see paragraph 340-40-50-3)
- e. Impairment of costs to fulfill a contract with a customer (see paragraph 340-40-50-3)
- f. Amortization of costs to obtain a contract with a customer (see paragraph 340-40-50-3)
- g. Impairment of costs to obtain a contract with a customer (see paragraph 340-40-50-3)
- h. Amortization of capitalized implementation costs of **hosting arrangements** that are service contracts (see paragraph 350-40-50-3)
- i. **Asset retirement obligation accretion expense** (see paragraph 410-20-50-1)
- j. **Loss contingencies** recognized (see paragraph 450-20-50-1)
- k. **Warranty** expense (the total of expenses recognized related to aggregate changes in the liability for accruals related to product warranties issued during the reporting period and the aggregate changes in the liability for accruals related to preexisting warranties, including adjustments related to changes in estimates) (see paragraph 460-10-50-8)
- l. Expense related to counterparty default in own-share lending arrangements issued in contemplation of convertible debt issuance (see paragraph 470-20-50-2C)
- m. Aggregate gain on restructuring of payables by a debtor with a **troubled debt restructuring** (see paragraph 470-60-50-1)
- n. Gains and losses upon consolidation of a variable interest entity that is not a business (see paragraph 810-10-50-3)
- o. Foreign currency **transaction gains or losses** (see paragraph 830-20-50-1)
- p. **Operating lease** cost (see paragraph 842-20-50-4)
- q. **Short-term lease** cost (see paragraph 842-20-50-4)
- r. Variable lease cost (see paragraph 842-20-50-4)
- s. Net gain or loss recognized from sale and leaseback transactions (see paragraph 842-20-50-4)
- t. Gains and losses from nonmonetary transactions (see paragraph 845-10-50-1)
- u. Amortization of capitalized **acquisition costs** (see paragraph 944-30-50-1(c)).

These disclosures shall be included in the tabular format disclosure required by paragraph 220-40-50-6 using the same frequency (that is, whether the disclosure is required at interim and annual reporting periods or only annual reporting periods) as required by the corresponding Topic.

50-23 If there is a change in facts and circumstances that results in an item listed in paragraph 220-40-50-22 changing from being included in one relevant

expense caption in the current reporting period and multiple relevant expense captions in a comparative period, or vice versa, an entity shall provide the disclosure required by paragraph 205-10-50-1.

50-24 ...An entity only shall include the applicable expenses listed in paragraphs 220-40-50-21 through 50-22 in the tabular format disclosures if an expense caption is a relevant expense caption in accordance with paragraphs 220-40-50-12 through 50-13.

50-25 To illustrate the application of the requirements in paragraph 220-40-50-22, if cost of sales was a relevant expense caption (because cost of sales includes purchases of inventory described in paragraph 220-40-50-6(a)) and if amortization of costs to fulfill a contract with a customer was recognized entirely in cost of sales and not in multiple expense captions presented on the face of the income statement, then amortization of costs to fulfill a contract with a customer would be required to be included as a separate category in the tabular format disclosure in addition to the categories required by paragraph 220-40-50-6.

For purposes of the tabular disclosure, Subtopic 220-40 provides a list of which expenses, gains and losses are: [\[220-40-50-21, 50-22\]](#)

- always reported separately if present in a relevant expense caption (see [Question 5.2.10](#)); or
- only reported separately if the expense is entirely recorded in a single relevant expense caption (see [Question 5.2.20](#)).

Question 5.2.10 Which specific expenses, gains and losses are always reported separately in the tabular disclosure?

Interpretive response: Subtopic 220-40 provides a list of the expenses, gains and losses that need to be reported separately (i.e. as a separate line item) in the tabular disclosure for each relevant expense caption that includes these items. This list represents items whose amount and income statement caption require disclosure by other Codification Topics and Subtopics. [\[220-40-50-21, ASU 2024-03.BC104\]](#)

The list is based on other Codification Topics' and Subtopics' current requirements and is subject to change if these requirements change in the future. The list is as follows. [\[220-40-50-21\]](#)

Expenses, gains and losses always reported separately in the tabular disclosure	Source of the disclosure requirement
The amount of R&D assets acquired in a transaction other than a business combination and written off	350-30-50-1(c)
Impairment loss recognized related to an intangible asset	350-30-50-3
Impairment loss of long-lived assets classified as held and used	360-10-50-2

Expenses, gains and losses always reported separately in the tabular disclosure	Source of the disclosure requirement
Gain or loss recognized in accordance with paragraphs 360-10-35-37 to 35-45 and 360-10-40-5 for long-lived assets classified as held for sale or disposed of	360-10-50-3
Each major type of cost associated with an exit or disposal activity (e.g. one-time employee termination benefits, contract termination costs, and other associated costs)	420-10-50-1
Components of net benefit cost recognized (other than service cost amounts included within employee compensation)	715-20-50-1(h)
Bargain purchase gain recognized in a business combination	805-30-50-1(f)
Any gain or loss recognized upon the deconsolidation of a subsidiary or the derecognition of a group of assets in accordance with paragraph 810-10-40-3A	810-10-50-1B
Gains and losses on derivative instruments (and nonderivative instruments that are designated and qualify as hedging instruments in accordance with paragraphs 815-20-25-58 and 815-20-25-66)	815-10-50-4A
Gains and losses on related hedged items	815-10-50-4A
Amortization of license agreements for program material	920-350-50-2
Impairment of license agreements for program material	920-350-50-4
Amortization of film costs	926-20-50-4A
Impairment of film costs	926-20-50-4C

The existence of these specific expenses, gains or losses within an income statement caption does not make the caption 'relevant', i.e. subject to disaggregation under Subtopic 220-40 (see [Question 2.2.30](#)). If these items are included in a caption that is not otherwise required to be disaggregated under Subtopic 220-40, their disclosure can continue to be provided in other notes to the financial statements. [220-40-50-24, ASU 2024-03.BC104]

FASB Example 1 (reproduced in [section 8.1](#)) illustrates the separate presentation of a line item for impairment loss on long-lived assets in the tabular disclosure of SG&A.

Question 5.2.20 Which specific expenses, gains and losses are reported separately in the tabular disclosure only if they are included entirely in one relevant expense caption?

Interpretive response: Subtopic 220-40 provides a list of the expenses, gains and losses that need to be reported separately (i.e. as a separate line item) in the tabular disclosure for each relevant expense caption that includes these items, but only if recorded entirely within a single relevant expense caption. This list represents items required to be disclosed under other Codification

Topics and Subtopics with no accompanying requirement to also disclose the line item in the income statement where the amount is recorded. The list excludes functional expenses (e.g. R&D expenses) that may have overlap with the required natural expense categories. [220-40-50-22, 50-25, ASU 2024-03.BC105 – BC107]

The list is based on other codification Topics' and Subtopics' current requirements and is subject to change if these requirements change in the future. The list is as follows: [220-40-50-22]

Expenses, gains and losses reported separately in the tabular disclosure if included entirely in one relevant expense caption	Source of the disclosure requirement
Provision for expected credit losses	326-20-50-9, 50-13
Losses on firm purchase commitments	330-10-50-5
Amortization expense attributable to the expiration of an insurance or reinsurance coverage provided under a contract that transfers only significant underwriting risk	340-30-50-2
Amortization of costs to fulfill a contract with a customer	340-40-50-3
Impairment of costs to fulfill a contract with a customer	340-40-50-3
Amortization of costs to obtain a contract with a customer	340-40-50-3
Impairment of costs to obtain a contract with a customer	340-40-50-3
Amortization of capitalized implementation costs of hosting arrangements that are service contracts	350-40-50-3
ARO accretion expense	410-20-50-1
Loss contingencies recognized	450-20-50-1
Warranty expense (the total of expenses recognized related to aggregate changes in the liability for accruals related to product warranties issued during the reporting period and the aggregate changes in the liability for accruals related to preexisting warranties, including adjustments related to changes in estimates)	460-10-50-8
Expense related to counterparty default in own-share lending arrangements issued in contemplation of convertible debt issuance	470-20-50-2C
Aggregate gain on restructuring of payables by a debtor with a troubled debt restructuring	470-60-50-1
Gains and losses upon consolidation of a variable interest entity that is not a business	810-10-50-3
Foreign currency transaction gains or losses	830-20-50-1
Operating lease cost	842-20-50-4
Short-term lease cost	842-20-50-4
Variable lease cost	842-20-50-4
Net gain or loss recognized from sale and leaseback transactions	842-20-50-4

Expenses, gains and losses reported separately in the tabular disclosure if included entirely in one relevant expense caption	Source of the disclosure requirement
Gains and losses from nonmonetary transactions	845-10-50-1
Amortization of capitalized acquisition costs	944-30-50-1(c)

The existence of these specific expenses, gains or losses within an income statement caption does not make the caption 'relevant', i.e. subject to disaggregation under Subtopic 220-40 (see [Question 2.2.30](#)). [220-40-50-24, ASU 2024-03.BC105]

If any of these specific expenses, gains or losses are recorded in multiple income statement captions, there is no requirement to report them separately in the respective relevant expense caption tabular disclosures. Corresponding amounts are included in 'other items' or can be voluntarily reported separately (see [section 5.3](#)). Regardless of the option selected in the tabular disclosures, the disclosure requirements under other Topics or Subtopics still apply and may need to be satisfied in other notes to the financial statements. [ASU 2024-03.BC106, BC110]

FASB Example 1 (reproduced in [section 8.1](#)) illustrates the separate presentation of warranty expenses, as this expense is entirely recorded in one caption (cost of products sold). Conversely, in that example operating lease costs do not need to be reported separately because they are recorded in multiple relevant expense captions (cost of services and SG&A).

Question 5.2.30 Does the tabular disclosure require recasting when a specific expense, gain or loss is no longer included entirely in one relevant expense caption (or vice versa)?

Background: As explained in [Question 5.2.20](#), certain specific expenses, gains and losses are reported separately in the tabular disclosure only if they are included entirely in one relevant expense caption. Such an item might be included entirely in one relevant expense caption in one period and several captions the next period, or vice versa. See [Example 5.2.10](#).

Interpretive response: No.

This change in facts and circumstances may cause a change in display of the tabular disclosure between the prior and current period. However, recasting of prior periods to conform to the new display is not required. Because the change affects comparability, an entity discloses the reasons for the change in the period it occurs. [205-10-50-1, 220-40-50-23, ASU 2024-03.BC110 – BC111, BC124]

Example 5.2.10 Change in display of operating lease costs

In Year 1, ABC Corp., a manufacturer, incurs operating lease costs only for its manufacturing facilities. These costs are entirely included in COGS (a relevant expense caption) and therefore are required to be reported separately in the tabular disclosure for COGS for Year 1.

In Year 2, ABC enters into a new operating lease for its corporate headquarters and includes the associated cost in SG&A. ABC continues to record the operating lease costs associated with its manufacturing facilities in COGS. It is not required to include the operating lease costs as a separate category in the tabular disclosure for COGS and SG&A for Year 2, because operating lease costs are not entirely included within one relevant expense caption.

When presenting Year 2 tabular disclosures, ABC does not need to recast Year 1 information. However, the change in facts and circumstances and the effect on comparability needs to be explained. In Year 2, ABC also needs to provide the operating lease cost disclosure required by paragraph 842-20-50-4, outside the tabular disclosure.

Question 5.2.40 Are the specific expenses, gains and losses required to be reported separately in the tabular disclosure at each interim and annual period?

Interpretive response: No. Subtopic 220-40 does not intend to change the disclosure requirement frequency in other Codification Topics or Subtopics. Therefore, the specific expenses, gains and losses listed in [Questions 5.2.10](#) and [5.2.20](#) are only reported separately in the tabular disclosure for an interim period if their disclosure is required by the corresponding Topic or Subtopic for interim periods. [\[220-40-50-21 – 50-22\]](#)

For example, gains and losses on derivative instruments need to be reported separately in the tabular disclosure of any relevant expense caption that contains such amounts, for both interim and annual periods due to the disclosure frequency requirements of Topic 815 (derivatives). [\[815-10-50-4A\]](#)

Other specific expenses, gains and losses may occur infrequently, subject to certain events occurring (e.g. impairment, deconsolidation of a subsidiary, recognition of loss contingencies). They would be reported separately in the tabular disclosure for the periods in which they are recorded and disclosed in accordance with the relevant Codification Topics or Subtopics.

As a result of the above requirements, the format of the tabular disclosure may be different between interim and annual periods.

5.3 Voluntary disclosures and other items

Excerpt from ASC 220-40

> Overall Guidance

- > Other Items Remaining in Relevant Expense Captions

50-30 For interim and annual reporting periods, an entity, in the same tabular format disclosure in which the disclosures required by paragraph 220-40-50-6 are provided, shall disclose for each relevant expense caption an amount for other items. The amount for other items is the difference between the following:

- a. The amount of the relevant expense caption presented on the face of the income statement
- b. The aggregate amount of expense categories separately disclosed in accordance with paragraphs 220-40-50-6, 220-40-50-21 through 50-22, 220-40-50-26(a), and 220-40-50-28 that are included in the relevant expense caption.

For interim and annual reporting periods, an entity also shall disclose qualitative descriptions of the composition (based on their natural expense classification) of other items. The detail provided in those qualitative disclosures shall be commensurate with the significance of the amounts being described.

Notwithstanding that requirement, an entity is not precluded from further disaggregating relevant expense captions before applying the guidance in this paragraph to the remaining other items. Additional voluntary disclosures may be provided inside or outside the tabular disclosure if those disclosures are not combined with the disaggregated expense amounts required by paragraphs 220-40-50-6, 220-40-50-21 through 50-22, 220-40-50-26(a), and 220-40-50-28.

An entity has a choice in how to treat residual amounts in a relevant expense caption – i.e. amounts that are not required to be reported separately in the tabular disclosure (see [section 5.2](#)). Residual amounts can be either: [\[220-40-50-30\]](#)

- voluntarily reported separately in the tabular disclosure; or
- aggregated and presented as ‘other items’ in the tabular disclosure (accompanied by a qualitative description of the amounts composing ‘other items’). In this case, the amounts can also be voluntarily disclosed outside of the tabular disclosure.

Question 5.3.10 What are the parameters regarding voluntary disclosure of additional expense categories?

Interpretive response: Voluntary disclosure of additional expense categories is permitted as long as the amounts provided voluntarily are not combined with the required disaggregation amounts. The separation of voluntary amounts from required amounts is intended to preserve comparability of the disclosures between entities. As an exception to this rule, an entity may elect to include

amounts attributable to other transactions entered into for the benefit of employees (e.g. the provision of subsidized goods or services) in employee compensation (see [Question 3.4.40](#)).

Voluntary disclosures may be included either within or outside of the tabular disclosure. They do not replace required disclosures and must be clearly labeled. [\[220-40-50-30, ASU 2024-03.BC92, BC115\]](#)

For example, contractor costs may be a significant component of COGS for certain entities. Contractor costs are not a required natural expense category and cannot be combined with amounts for employee compensation. By default, contractor costs are therefore included in the reconciling line 'other items' in the tabular disclosure; however, they alternatively may be either reported separately in the tabular disclosure (on their own line) or disclosed outside the tabular disclosure.

Further, an entity is permitted to present subtotals that include required and voluntarily disclosed expense categories. For example, a subtotal for 'total workforce cost' comprising employee compensation and contractor costs may be voluntarily included in the tabular disclosure. See [Question 3.4.60](#). [\[ASU 2024-03.BC115\]](#)

[Question 3.2.20](#) addresses how a required natural expense in a relevant expense caption can be further disaggregated voluntarily (e.g. to disclose the underlying components of employee compensation – e.g. salaries and wages, share-based payment arrangements, medical benefits, pension benefits).

Example 5.3.10 Voluntary disclosure of an incremental expense category and subtotal

ABC Corp., a biopharma company, has identified R&D as a relevant expense caption in its income statement because the line includes employee compensation costs as well as depreciation.

ABC incurs significant R&D expenses associated with contracted services for a variety of purposes including regulatory consultants, clinical trial development, data scientist, manufacturing expansion and planning. The extent of these expenses vary year-over-year depending on the specific projects and stages of development. ABC believes that contracted services costs along with its own employee compensation costs are meaningful to understanding its total workforce costs.

In its tabular disclosure of R&D expenses, ABC elects to voluntarily report a separate expense category for contracted services as well as a subtotal for total workforce costs, comprising the employee compensation required natural expense category and the voluntary contracted services category, as shown below.

Research and development (R&D)	Amount
Employee compensation	1,500
Contracted services	500
Total workforce costs	2,000

Research and development (R&D)	Amount
Depreciation	100
Other R&D ¹	300
Total research and development	2,400
Note:	
1. Other R&D costs consist primarily of regulatory fees, license costs and operating lease expenses.	

If ABC does not elect to voluntarily report a separate expense category for contracted services and a subtotal for total workforce costs, amounts for contracted services are included in 'other items' (labeled as 'Other R&D' in this example), as shown below.

Research and development (R&D)	Amount
Employee compensation	1,500
Depreciation	100
Other R&D ¹	800
Total research and development	2,400
Note:	
1. Other R&D consists primarily of contracted services for regulatory consultants, clinical trial development, data scientist, manufacturing expansion and planning, regulatory fees, license costs and operating lease expenses.	

Question 5.3.20 How are 'other items' remaining in relevant expense captions disclosed?

Interpretive response: The 'other items' category aggregates residual amounts recorded within a relevant expense caption that do not require disaggregation and are not reported separately. This ensures that the tabular disclosure for each relevant expense caption reconciles to the caption amount in the income statement. The amount for other items is not necessarily small, given there are only five natural expense categories required to be disaggregated and an entity may incur significant costs outside of these categories. FASB Example 2 (reproduced in [section 8.2](#)) illustrates such a situation in the disaggregation of the caption 'cost of sales' by a service entity that has significant contractor expenses. Further, [Question 4.5.20](#) discusses the 'other items' category when disaggregating a relevant caption such as COGS that includes inventory amounts.

The composition of the amounts included in 'other items' needs to be qualitatively described, based on the natural classification of the expenses (see [Question 3.2.10](#)). The level of detail provided in this disclosure should correspond with the significance of the amounts being described and provide

context, especially when there are significant changes in the nature of costs incurred or expenses recognized. [\[220-40-50-30, ASU 2024-03.BC113 – BC115\]](#)

FASB Examples 1 to 3 (reproduced in [chapter 8](#)) illustrate the possible composition and qualitative disclosure of 'other items'.

6. Selling expenses

Detailed contents

6.1 How the standard works

6.2 Disclosure of selling expenses

Questions

Question 6.2.10 How are 'selling expenses' defined?

Question 6.2.20 Are advertising expenses included in selling expenses?

Question 6.2.30 What items do not qualify as selling expenses?

Question 6.2.40 Can the selling expenses quantitative disclosure requirement be satisfied through the tabular disclosure of natural expense categories for relevant expense captions?

Question 6.2.50 May an entity change its definition of selling expenses?

6.1 How the standard works

Subtopic 240-40 requires the following disclosures related to selling expenses.

Nature of the disclosure	Information required	Frequency
Quantitative	Total selling expenses recognized in continuing operations	Annual and interim
Qualitative	Description of the composition of selling expenses	Annual only (unless changed during the interim period)

‘Selling expenses’ is a management-defined measure. The absence of a prescribed definition gives latitude to preparers to provide information considering an entity’s specific facts and circumstances and is consistent with the discretion currently afforded to entities in classifying expenses within income statement captions such as COGS and SG&A expenses. This disclosure is intended to provide users of the financial statements with management’s view of the costs that are expected to vary with revenue trends, unlike the general and administrative costs that are often reported with selling expenses in an SG&A caption. [\[ASU 2024-03.BC25\(d\), BC28\(i\)\]](#)

6.2 Disclosure of selling expenses

Excerpt from ASC 220-40

> Overall Guidance

• > Selling Expenses

50-35 For interim and annual reporting periods, an entity shall disclose, in the notes to financial statements, the total selling expenses recognized in continuing operations.

50-36 An entity shall make its own determination of what constitutes a selling expense. An entity's definition of selling expenses shall include only items that are presented as expenses in the income statement. An entity shall disclose how it defines the term selling expenses in annual reporting periods (or in interim reporting periods if the definition is changed).

Subtopic 240-40 requires quantitative and qualitative disclosures related to selling expenses – a management-defined measure. [\[220-40-50-35 – 50-36\]](#)

Question 6.2.10 How are 'selling expenses' defined?

Interpretive response: Subtopic 220-40 does not define or prescribe specific examples of what constitutes selling expenses. Instead, the Board noted that the determination of which expenses to attribute to a selling function depends on each entity's facts and circumstances and that each entity has its own tailored definition of 'selling'. [\[220-40-50-36, ASU 2024-03.BC116-120\]](#)

We believe examples of potential selling expenses include: [\[220-40-55-12, 55-19, 55-25, ASU 2024-03.BC119\]](#)

- marketing and promotional activities
- client relationship management
- advertising (see [Question 6.2.20](#))
- customer acquisition costs (including amortization of costs to obtain a contract with a customer previously capitalized under Subtopic 340-40)
- market research
- business development
- fulfillment costs (including amortization of costs to fulfill a contract with a customer previously capitalized under Subtopic 340-40)
- costs associated with physical sales locations or websites
- allocation of management expenses.

FASB Examples 1 to 3 (reproduced in [chapter 8](#)) illustrate the composition of management's definition of selling expenses.

Question 6.2.20 Are advertising expenses included in selling expenses?

Background: Subtopic 720-35 (advertising costs) defines advertising as “the promotion of an industry, an entity, a brand, a product name, or specific products or services to create or simulate a positive entity image or a desire to buy the entity’s products or services, using forms of media to communicate with potential customers.” [720-35-05-4]

Interpretive response: It depends.

Whether advertising expenses are included in selling expenses is dependent on whether an entity considers such expenses to be representative of its selling function and within its definition of selling expenses (see [Question 6.2.10](#)). [ASU 2024-03.BC120]

Regardless of whether advertising expenses are included in selling expenses for the purpose of Subtopic 220-40, Subtopic 720-35 requires disclosure of the total amount charged to advertising expense for each income statement period presented. There is no accompanying requirement to disclose the specific income statement caption(s) in which advertising expenses are included. [720-35-50-1(b)]

Question 6.2.30 What items do not qualify as selling expenses?

Interpretive response: Subtopic 220-40 does not provide explicit examples of expenses that might be excluded from selling expenses. However, it limits selling expenses to items presented as expenses within continuing operations in the income statement. As a result, we believe the following types of transactions should not be included in an entity’s definition of selling expenses. [220-40-50-36, ASU 2024-03.BC116]

- Capitalized amounts (such as capitalized costs to obtain or fulfill a contract with a customer in the scope of Subtopic 340-40). However, amortization of these amounts may qualify as selling expense (see [Question 6.2.10](#)).
- Amounts presented as a reduction of revenue (such as marketing incentives accounted for as consideration payable to customers not in exchange for a distinct good or service transferred by the customer to the entity). [606-10-32-25]

Question 6.2.40 Can the selling expenses quantitative disclosure requirement be satisfied through the tabular disclosure of natural expense categories for relevant expense captions?

Background: There is diversity in practice in how selling expenses are presented in the income statement (e.g. as an individual ‘selling expenses’

caption, included within an SG&A expense caption, or spread across multiple expense captions that contain selling components).

Interpretive response: It depends.

The ability to combine the selling expenses quantitative disclosure within the tabular disclosures for relevant expense captions depends on the structure of the entity's income statement and management's definition of selling expenses. [ASU 2024-03.BC117 – BC120]

- If selling expenses (or a similarly named caption capturing selling expenses, such as 'sales and marketing') is its own individual caption in the income statement, the quantitative disclosure is directly satisfied. The qualitative description of the caption composition would still be required.
- If selling expenses are included in one caption in the income statement (e.g. SG&A), it might be challenging to display their amount in the tabular disclosure for that caption because selling expenses is generally a functional grouping of expenses (see [Question 3.2.10](#)), meaning that it may include several required natural expenses.
- If selling expenses are included in more than one caption, their total amount cannot be provided in one tabular disclosure only.

Question 6.2.50 May an entity change its definition of selling expenses?

Interpretive response: Yes.

Given that the amount of selling expenses is determined based on an entity's specific facts and circumstances using a management approach, it is possible for an entity's definition of selling expenses to evolve over time due to underlying changes to operations and business models. [220-40-50-4, ASU 2024-03.BC121]

If an entity changes its definition of selling expenses (e.g. to no longer include amounts relating to advertising expenses), the revised definition and the reasons for the change must be disclosed, and comparative amounts need to be recast in the current disclosure (assuming it is not impracticable to do so). [ASU 2024-03.BC121]

Changing the definition of selling expenses does not represent a change in accounting principle under Topic 250 (see [section 1.5](#)).

7. Effective date and transition

Detailed contents

7.1 How the standard works

7.2 Effective date and transition requirements

Questions

Question 7.2.10 How does the prospective application affect comparative information?

Question 7.2.20 When do off-calendar year-end entities first adopt Subtopic 220-40?

Question 7.2.30 Are EGC companies provided additional time to comply with the requirements?

Question 7.2.40 Can entities adopt Subtopic 220-40 during an interim reporting period prior to the first annual reporting period?

7.3 Transition considerations

Question

Question 7.3.10 What are some approaches for preparing to comply with Subtopic 220-40?

7.1 How the standard works

Effective date and transition requirements

Subtopic 220-40's expense disaggregation disclosure requirements become effective for:

- annual reporting periods beginning after December 15, 2026, and
- interim periods within fiscal years beginning after December 15, 2027.

Early adoption is permitted. Entities generally apply the standard prospectively but may elect retrospective application for any or all prior periods presented, provided the requirements are adopted in full.

In the first year of adoption, comparative disclosures are not required; instead, comparative periods build up progressively over subsequent years. Off-calendar year-end entities follow the same effective dates, and emerging growth companies (EGCs) are not granted additional time to comply.

Transition considerations

Implementation may require significant systems and process changes. The use of estimates and other methods is permitted as long as they produce a reasonable approximation of the amounts required to be disclosed. Judgment is required in determining when, where and how estimates may be applied.

7.2 Effective date and transition requirements

Excerpt from ASC 220-40

> Transition Related to Accounting Standards Updates No. 2024-03, *Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures (Subtopic 220-40): Disaggregation of Income Statement Expenses*, and No. 2025-01, *Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures (Subtopic 220-40): Clarifying the Effective Date*

65-1 The following represents the transition and effective date information related to Accounting Standards Updates No. 2024-03, *Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures (Subtopic 220-40): Disaggregation of Income Statement Expenses*, and No. 2025-01, *Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures (Subtopic 220-40): Clarifying the Effective Date*:

Effective date and early adoption

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

Transition method

- b. A public business entity shall apply the pending content that links to this paragraph prospectively to financial statements issued for reporting periods beginning after the effective date of the pending content that links to this paragraph. The disclosures required by the pending content that links to this paragraph do not need to be included in financial statements for reporting periods beginning before the effective date that are being presented for comparative purposes with financial statements issued for periods after the effective date.
- c. A public business entity may elect to apply the pending content that links to this paragraph retrospectively to any or all prior periods presented in the financial statements. If applied to financial statements for periods beginning before the effective date, those disclosures shall be prepared and presented in accordance with this Subtopic.

The effective date and transition requirements for Subtopic 220-40 are in ASU 2024-03, later clarified by ASU 2025-01, and are as follows. [\[220-40-65-1\]](#)

Effective date	• Annual reporting periods beginning after December 15, 2026. • Interim reporting periods within fiscal years beginning after December 15, 2027.
Early adoption	Early adoption is permitted.
Transition	Prospective, with retrospective application to any or all prior periods presented permitted.

Because certain entities may not have all of the information necessary to adopt the disaggregated disclosure requirements retrospectively, the adoption of Subtopic 220-40 is on a prospective basis. However, retrospective application is permitted for any or all prior periods presented as long as the requirements are adopted in full. [220-40-65-1, ASU 2024-03.BC156 – BC157]

Question 7.2.10 How does the prospective application affect comparative information?

Interpretive response: Prospective application of Subtopic 220-40 will result in the build-up of comparative disclosures over time, from no comparatives required in the initial year of adoption to a full set of comparative disclosures three years later.

For example, Subtopic 220-40 disclosures in a calendar year-end entity's first annual financial statements after adoption (i.e. 12/31/2027) and first interim financial statements (i.e. 3/31/2028) will stand alone with no comparative disclosures required. Comparative periods disclosed will build progressively in subsequent reporting periods. [220-40-65-1(b)]

This is further illustrated in the following table.

Fiscal year	Subtopic 220-40 disclosures are provided for the following periods:			
	Annual periods		Interim periods	
	Current period	Comparative periods	Current period	Comparative periods
2027	Yes (2027)	No (2026) No (2025)	No (2027 Q1-Q3)	No (2026 Q1-Q3)
2028	Yes (2028)	Yes (2027) No (2026)	Yes (2028 Q1-Q3)	No (2027 Q1-Q3)
2029	Yes (2029)	Yes (2028) Yes (2027)	Yes (2029 Q1-Q3)	Yes (2028 Q1-Q3)

Question 7.2.20 When do off-calendar year-end entities first adopt Subtopic 220-40?

Interpretive response: Absent early adoption, off-calendar year-end entities adopt Subtopic 220-40 in their annual periods beginning after December 15, 2026 and interim reporting periods beginning after December 15, 2027. For example, if an entity's year-end is January 31st, the entity is required to adopt Subtopic 220-40 for:

- the annual reporting period ended January 31, 2028; and
- interim periods starting after January 31, 2028 – i.e. the first interim information is provided for the quarter ended April 30, 2028.

Question 7.2.30 Are EGC companies provided additional time to comply with the requirements?

Interpretive response: No.

EGCs are PBEs and the adoption timing is the same for all PBEs. EGCs are not provided additional time to comply with the requirements. [220-40-15-2, ASU 2024-03.BC32]

Question 7.2.40 Can entities adopt Subtopic 220-40 during an interim reporting period prior to the first annual reporting period?

Interpretive response: Yes.

Given early adoption is permitted, adopting the requirements in an interim period prior to the first annual reporting period is permitted. However, whenever possible, entities should generally adopt any accounting changes during the first interim period of a fiscal year. Further, the disclosures should comply with all of the requirements of Subtopic 220-40, including those needed in the first period of adoption (e.g. defining selling expenses). [220-40-65-1(c), 270-10-45-15]

For example, a calendar year-end entity may elect to adopt the requirements starting with its Q1 interim reporting period in 2027, i.e. before it is required to adopt the requirements for the annual reporting period ended December 31, 2027. The entity does not need to include comparative information in the Q1 interim reporting period, but it does need to comply with all requirements of Subtopic 220-40 starting in Q1 2027.

7.3 Transition considerations

Excerpt from ASC 220-40

> Implementation Guidance

• > Disaggregation of Expenses

55-2 Application of the guidance in this Subtopic might cause an entity to pursue a degree of detail in recordkeeping and computations that could be burdensome as well as unnecessary to produce a reasonable approximation of the results. Accordingly, an entity may use estimates or other methods that produce a reasonable approximation of the amounts required to be disclosed by this Subtopic.

The ability to successfully adopt and comply with the requirements of Subtopic 220-40 requires an upfront readiness assessment. A key element to this readiness assessment includes identifying the sources of data that will be used to derive the required disclosures. Depending on the data availability or lack

thereof and identified gaps in existing system configurations, significant time and resources may be needed to comply with the Subtopic 220-40 requirements. Potential changes that may result from this readiness evaluation include: [\[ASU 2024-03.BC154\]](#)

- system scoping, integration and configuration changes and expanded reporting tools;
- updates to the financial reporting processes and internal controls;
- expanded coordination and training for accounting and financial reporting personnel and across operations, governance functions, business segments and geographies; and
- additional personnel and resource needs.

Estimates or other systematic and rational methods may be used to produce a reasonable approximation of the amounts required to be disclosed. Judgment is required in determining when, where and how estimates may be applied. When applied, careful consideration should be given to the methods, assumptions and data used in the estimates and any resulting changes to the financial reporting process and controls. [\[220-40-50-1, 55-2, ASU 2024-03.BC28\(j\), BC50, BC53\]](#)

Question 7.3.10 What are some approaches for preparing to comply with Subtopic 220-40?

Interpretive response: Anticipated approaches for preparing to comply with the requirements of Subtopic 220-40 include a systems-based approach, an estimates approach and a combination of the two. There may be other approaches as well.

Systems-based approach

Often the data necessary to comply with the disaggregation requirements will be sourced from different levels, including:

- the consolidation and financial reporting system;
- various ERP systems;
- inventory systems; and
- non-accounting systems with key data elements (e.g. HR systems or payroll systems).

Depending on the current scoping and configurations of these systems, significant updates may be needed.

Employee compensation

For example, companies with a workforce comprising employees and nonemployees may need to evaluate the following.

Key data element	Source	Considerations
Employee, as defined , see Question 3.4.10	The employee designation and related information likely sources from an HR or payroll system.	HR or payroll systems may be out of scope for financial reporting purposes. However, given that the employee designation (i.e. employee versus nonemployee) and department coding are critical for determining the amount of employee compensation to be disaggregated across relevant expense captions, changes to system scoping and integration (including related processes and controls) may be necessary. These changes will help to accurately incorporate the needed data into the financial reporting process.
Employee compensation, as defined , see Question 3.4.30	The various components of employee compensation are likely recorded within various accounts across ERP systems.	ERPs may need to be evaluated to identify all of the components comprising employee compensation (e.g. salaries, stock compensation, medical benefits, pensions) and the accounts each component is mapped to. Additional accounts/subaccounts and/or updated account mapping may be necessary to track the compensation components by employee versus nonemployee and by department coding to ensure all applicable compensation components are captured and mapped to accounts consistently across ERP systems.
Employee compensation reported within a relevant expense caption	The disaggregated disclosure will likely be derived from the consolidation and financial reporting system.	Consolidation and financial reporting systems may need to be assessed to determine whether their current configurations and reporting capabilities can provide the necessary information, such as required categories like employee compensation, for each relevant expense caption. For example, if both COGS and SG&A include employee compensation, it is important to confirm that the system can separately extract employee compensation data for each caption, rather than aggregating the amounts together.

Additional complexities may exist for entities that operate in multiple jurisdictions. For example, different locations may not maintain employee or employee compensation information consistently and employment laws may differ across jurisdictions, which can affect the employee designation and the types of compensation to be included (see [section 3.4](#)).

Inventory amounts

A systems-based approach may be necessary for some entities to comply with the requirements of Subtopic 220-40. The specific system requirements and capabilities will depend on whether the entity applies the cost-incurred or expense-incurred disaggregation basis to relevant expense captions that include inventory amounts (see [section 4.5](#)). Regardless of the chosen basis, it is essential that entities maintain visibility into the original nature of capitalized inventory transactions when first recorded. This ensures that the underlying expense categories can be accurately identified and reported in accordance with the standard.

Key data element	Source	Considerations
Natural classification of inventory transactions	The supporting documentation for inventory-related transactions – whether capitalized or directly expensed – will vary by cost type. For example, external purchases of materials may be supported by invoices paid, capitalized labor by payroll reports or timecards, and depreciation by fixed asset reports.	To accurately disaggregate inventory costs by their natural classification, inventory accounting or ERP systems may need to be configured to tag and track each cost component at the time it is capitalized or expensed. Under the cost-incurred basis, tagging and tracking must cover current-period activity. Under the expense-incurred basis, tagging and tracking may need to extend across multiple periods (e.g. depending on inventory turnover) to ensure that, as inventory is derecognized, the original nature of the costs can still be identified and reported.
Intercompany inventory transactions	Intercompany inventory transactions that require elimination upon consolidation are typically sourced from the consolidation and financial reporting system.	Consolidation and financial reporting systems may need to be assessed to determine whether their current configurations and reporting capabilities can provide the necessary information, such as amounts for each required natural expense category, after elimination of intercompany transactions. Disclosures are prepared from the perspective of the reporting entity, not from the entity within the group that last sold the inventory in the period or holds it at the reporting date (see Question 3.3.40). As a result, systems must be able to look through intercompany transactions and trace the natural expense classification back to the nature of the costs as initially incurred by the originating group entity (see Example 3.3.20).

Estimates approach

For some entities, the use of estimates may help in complying with the requirements of Subtopic 220-40. Using estimates requires careful judgment to ensure they provide a reasonable approximation of the amounts required for disclosure. Developing such estimates involves careful consideration of the relevance and reliability of underlying data, the methods and assumptions applied, and the related processes and controls.

Employee compensation

Practical example	Considerations
Entities with both employees and nonemployees cannot combine amounts related to nonemployees within the employee compensation category. As a result, organizations with a workforce comprising employees and nonemployees may need to estimate the portion of compensation attributable solely to employees within each relevant expense caption if this information is not directly accessible.	One approach is to calculate the percentage of the workforce that represents employees versus nonemployees and apply that percentage to compensation components common to both groups (e.g. salaries, wages, bonuses). Components unique to employees (e.g. pensions, payroll taxes) should not be allocated using this method. Data for these estimates (e.g. employee versus nonemployee headcount) may come from nonfinancial systems that lack the same level of internal controls as accounting systems, so the reliability of these inputs should be carefully assessed. Further, the chosen percentage must be sufficiently precise. For example, the proportion of nonemployees may vary significantly between functions (e.g. sales versus manufacturing) or across geographies. Applying a simple headcount percentage to total compensation amounts may not accurately reflect actual costs if compensation levels differ between groups.

Inventory amounts

The use of estimates and related considerations may vary based on the inventory cost flow assumptions applied.

Practical examples	Considerations
Allocation of cost pools	
Some entities allocate costs to inventory using underlying cost pools. When inventory allocation methods or systems are used to assign inventoriable costs to inventory and COGS, detailed data by natural expense category may not be available at the transactional level. This affects both the	Estimates may be needed to assign costs to the appropriate natural expense categories. For example, entities might estimate the percentage of total costs attributable to categories such as purchases of inventory, employee compensation, or depreciation. The reliability of these estimates depends on

Practical examples	Considerations
unit value of inventory on hand and the amounts derecognized upon sale.	the quality of the underlying data and assumptions. Inputs (e.g. depreciation included in inventoriable costs) may not be easily traceable to their natural classification, so careful evaluation of cost pool inputs is essential.
Periodic inventory systems	
Entities using a periodic inventory system calculate COGS at period-end based on the changes in inventory balances and purchase activity, rather than tracking costs in real time.	Similar to cost pool allocations, estimates may be needed to assign costs to the appropriate natural expense categories. The accuracy of these estimates relies on the availability and reliability of supporting data and the appropriateness of the allocation methods used.
Standard costing	
Under standard costing, a predetermined cost per unit is assigned to inventory. Actual costs often differ from standard costs, so entities must track and recognize variances that capture the difference between standard and actual costs. Standard costs and variances typically include multiple components (e.g. materials, labor costs, manufacturing overhead, etc.) that span several required natural expense categories.	Standard cost components and related variances must be disaggregated by their nature (e.g. raw materials as purchases of inventory, employee labor costs as employee compensation, machinery depreciation as depreciation). Entities may need to enhance their standard cost estimation processes to ensure each component and variance is properly classified. The level of estimation may vary depending on the disaggregation basis selected. • Under the cost-incurred basis, entities may need to estimate the composition of variances capitalized to inventory still on hand at period-end. • Under the expense-incurred basis, entities may need to estimate the composition of variances recognized in COGS for inventory sold during the period.

See [Question 4.5.100](#) for further discussion regarding inventory cost flow assumptions.

8. Illustrative disclosures

Detailed contents

- 8.1 FASB Example 1: Disaggregation of income statement expenses by an entity with manufacturing and service operations**
- 8.2 FASB Example 2: Disaggregation of income statement expenses by an entity with service operations**
- 8.3 FASB Example 3: Disaggregation of income statement expenses by a bank**

8.1 FASB Example 1: Disaggregation of income statement expenses by an entity with manufacturing and service operations

FASB Example 1 illustrates one type of tabular format disclosure that an entity with manufacturing and service operations could use to meet the disaggregation requirements in Subtopic 220-40 discussed in [chapters 2 to 5](#).

This example also illustrates the disclosure of selling expenses discussed in [chapter 6](#).

Excerpt from ASC 220-40

> Illustrations

- > Example 1: Disaggregation of Income Statement Expenses by an Entity with Manufacturing and Service Operations

55-3 This Example illustrates one type of tabular format disclosure that an entity could use to disclose disaggregated expense amounts in accordance with paragraphs 220-40-50-1 through 50-34. This Example also illustrates the disclosure of selling expenses in accordance with paragraphs 220-40-50-35 through 50-36.

55-4 For the year ended December 31, 20X4, Entity X, which is a manufacturer with significant service operations, presents the following comparative income statement

Entity X			
Consolidated Income Statement			
For the Years Ended December 31, 20X4, 20X3, and 20X2			
	20X4	20X3	20X2
Revenue:			
Products	\$82,144	\$79,137	\$75,180
Services	26,132	23,146	21,989
Total revenues	108,276	102,283	97,169
Operating expenses:			
Cost of products sold	63,456	60,898	57,244
Cost of services	10,496	9,568	8,898
Selling, general, and administrative	20,849	18,871	18,116
Total operating expenses	94,801	89,337	84,258
Operating income	13,475	12,946	12,911
Interest expense	4,971	4,213	4,297
Income before income taxes	8,504	8,733	8,614
Income tax expense	1,786	1,834	1,809
Net income	\$6,718	\$6,899	\$6,805

55-5 Entity X provides a disclosure that disaggregates the cost of products sold; cost of services; and selling, general, and administrative expense captions into the categories listed in paragraph 220-40-50-6. Those expense captions were identified as relevant expense captions because those captions contain one or more of the expense categories listed in paragraph 220-40-50-6. Even though Entity X presents other expense captions on the face of its consolidated income statement, such as interest expense and income tax expense, those expense captions do not contain any of the expense categories listed in paragraph 220-40-50-6 (including those described in paragraphs 220-40-50-10 through 50-11); therefore, those expense captions do not need to be disaggregated.

55-6 Because cost of products sold contains amounts related to inventory within the scope of Topic 330, Entity X may elect to disclose the amounts under a cost-incurred basis or expense-incurred basis. In this Example, Entity X chooses to disclose the disaggregation of cost of products sold on a cost-incurred basis (that is, the amounts disclosed include costs incurred that were capitalized to inventory during the current reporting period and costs incurred that were directly expensed during the current reporting period) in accordance with paragraph 220-40-50-31(a). Because Entity X discloses the required expense categories using a cost-incurred basis, the entity discloses the changes in inventories caption and the other adjustments and reconciling items caption in accordance with paragraphs 220-40-50-32 through 50-33. In accordance with paragraph 220-40-50-34, Entity X qualitatively describes the nature of amounts included in other adjustments and reconciling items. If Entity X had instead disclosed the required expense categories on an expense-incurred basis (that is, the amounts disclosed comprise expense amounts related to the derecognition of inventory that was previously capitalized in accordance with Topic 330 and any costs incurred that were directly expensed during the current reporting period) in accordance with paragraph 220-40-50-31(b), then the changes in inventories caption and the other adjustments and reconciling items caption would not be necessary in the disaggregation disclosure.

55-7 Entity X also recognizes **impairment** of property, plant, and equipment classified as held and used in selling, general, and administrative expenses and, therefore, includes that impairment as a separate category in the tabular format disclosure in accordance with paragraph 220-40-50-21(c).

55-8 Entity X recognizes expenses associated with **warranty** accruals entirely within cost of products sold and, therefore, includes warranty expense as a separate category in accordance with paragraph 220-40-50-22(k).

55-9 Entity X recognizes **operating lease** costs in both cost of services and selling, general, and administrative expenses. Therefore, in accordance with paragraph 220-40-50-22, Entity X is not required to separately disclose the amounts of cost of services and selling, general, and administrative expenses that are attributable to operating lease cost. Instead, those expenses are included in the amount for other items for each relevant expense caption in accordance with paragraph 220-40-50-30.

55-10 Entity X recognizes amounts related to the initial recognition and subsequent measurement of a liability for an environmental obligation in cost of products sold (see Subtopic 410-30 on asset retirement and environmental

obligations). In accordance with paragraph 220-40-50-16, Entity X is not required to disaggregate that amount into the expense categories listed in paragraph 220-40-50-6. Instead, that expense is included in the amount for other items in accordance with paragraph 220-40-50-30.

55-11 Entity X provides the following disclosure.

Disaggregation of Relevant Expense Captions			
	20X4	20X3	20X2
Cost of products sold			
<i>Cost of products sold</i>			
Purchases of inventory	\$20,213	\$19,199	\$16,319
Employee compensation	17,578	16,539	14,078
Depreciation	10,190	9,989	9,650
Intangible asset amortization	3,914	4,050	3,929
Warranty expense	4,394	3,952	3,894
Other cost of products sold ^(a)	7,552	7,606	7,993
Changes in inventories	157	(861)	843
Other adjustments and reconciling items ^(b)	(542)	424	538
Total cost of products sold	\$63,456	\$60,898	\$57,244
(a) Other cost of products sold consists primarily of amounts paid to carriers for outbound freight services related to contract fulfillment and amounts related to the measurement of a liability for an environmental obligation for the years ended December 31, 20X4, 20X3, and 20X2. Year ended December 31, 20X4, also includes inventory amounts recognized as part of a business combination.			
(b) Other adjustments and reconciling items consist of reconciling adjustments attributable to differences in the foreign exchange rates used to translate beginning inventory, ending inventory, and costs incurred from various functional currencies into the reporting currency for the years ended December 31, 20X4, 20X3, and 20X2.			
Cost of services			
<i>Cost of services</i>			
Employee compensation	\$6,598	\$5,654	\$4,354
Depreciation	763	765	742
Intangible asset amortization	642	670	650
Other cost of services ^(c)	2,493	2,479	3,152
Total cost of services	\$10,496	\$9,568	\$8,898
(c) Other cost of services consists primarily of operating lease and travel expenses for the years ended December 31, 20X4, 20X3, and 20X2.			
Selling, general, and administrative			
<i>Selling, general, and administrative (SG&A)</i>			
Employee compensation	\$13,242	\$11,379	\$10,764
Depreciation	1,454	1,755	1,737
Property, plant, and equipment impairment	412	-	-
Intangible asset amortization	523	596	-

Other SG&A ^(d)	5,218	5,141	5,615
Total SG&A	\$20,849	\$18,871	\$18,116

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

55-12 In addition to the tabular format disclosure illustrated in paragraph 220-40-55-11, Entity X disclose its selling expenses and how it defines selling expenses in accordance with paragraphs 220-40-50-35 through 50-36.

Selling Expenses

During the years ended December 31, 20X4, 20X3, and 20X2, selling expenses were \$13,425, \$12,123, and \$11,585, respectively. The entity's selling expenses include those expenses related to marketing and promotional activities and client relationship management.

8.2 FASB Example 2: Disaggregation of income statement expenses by an entity with service operations

FASB Example 2 illustrates one type of tabular format disclosure that an entity with only service operations could use to meet the disaggregation requirements in Subtopic 220-40 discussed in [chapters 2 to 5](#).

This example also illustrates the disclosure of selling expenses discussed in [chapter 6](#).

Excerpt from ASC 220-40

> Illustrations

- > Example 2: Disaggregation of Income Statement Expenses by an Entity with Service Operations

55-13 This Example illustrates one type of tabular format disclosure that an entity could use to disclose disaggregated expense amounts in accordance with paragraphs 220-40-50-1 through 50-34. This Example also illustrates the disclosure of selling expenses in accordance with paragraphs 220-40-50-35 through 50-36.

55-14 For the year ended December 31, 20X4, Entity X, which is a services provider, presents the following comparative income statement.

Entity X			
Consolidated Income Statement			
For the Years Ended December 31, 20X4, 20X3, and 20X2			
	20X4	20X3	20X2
Revenue:	\$737,132	\$710,146	\$694,180
Cost of sales (exclusive of depreciation and amortization shown separately below)	140,055	170,435	145,778

Depreciation and amortization related to cost of sales	31,578	26,178	23,628
Selling, general, and administrative expenses	497,962	458,215	471,626
Research and development expenses	57,235	52,174	48,898
Operating income	10,302	3,144	4,250
Interest expense	3,145	2,665	2,297
Income before income taxes	7,157	479	1,953
Income tax expense	1,503	101	410
Net income	\$5,654	\$378	\$1,543

55-15 Entity X provides a disclosure that disaggregates the cost of sales; depreciation and amortization; selling, general, and administrative expenses; and research and development expenses captions into the categories listed in paragraph 220-40-50-6. Those expense captions were identified as relevant expense captions because those captions contain one or more of the expense categories listed in paragraph 220-40-50-6. Even though Entity X presents other expense captions on the face of its consolidated income statement, such as interest expense and income tax expense, those expense captions do not contain any of the expense categories listed in paragraph 220-40-50-6 (including those described in paragraphs 220-40-50-10 through 50-11); therefore, those expense captions do not need to be disaggregated.

55-16 Entity X also recognizes **one-time employee termination benefits** in cost of sales; selling, general, and administrative expenses; and research and development expenses and, therefore, includes this amount as a separate category in the tabular format disclosure in accordance with paragraph 220-40-50-21. Paragraph 220-40-50-21(e) requires that an entity disclose the amount of each major type of cost associated with an exit or disposal activity (for example, one-time employee termination benefits) that is recognized in each relevant expense caption in the same tabular format in which the disclosures required by paragraph 220-40-50-6 are provided. Because one-time employee termination benefits are a form of employee compensation, Entity X discloses that its employee compensation category excludes one-time employee termination benefits because one-time employee termination benefits are disclosed as a separate category.

55-17 Entity X has a funded research and development cost-sharing arrangement with a strategic partner. Entity X recognizes an expense reimbursement from the strategic partner in research and development expenses and, in accordance with paragraph 220-40-50-26(a), elects to separately disclose the amount of that expense reimbursement. If Entity X had elected to present a relevant expense caption net of an expense reimbursement from another entity, it would have been required to disclose the amount of the expense categories that are included in each relevant expense caption. Additionally, in accordance with paragraph 220-40-50-29, Entity X qualitatively describes the expense categories to which the reimbursement relates.

55-18 Entity X provides the following disclosure.

Disaggregation of Relevant Expense Captions			
	20X4	20X3	20X2
Cost of sales			
<i>Cost of sales</i>			
Employee compensation (exclusive of one-time employee termination benefits)	\$86,336	\$83,903	\$100,009
One-time employee termination benefits	7,434	39,298	-
Other cost of sales ^(a)	46,285	47,234	45,769
Total cost of sales	\$140,055	\$170,435	\$145,778
(a) Other cost of sales consist primarily of subcontractor costs and travel expenses for the years ended December 31, 20X4, 20X3, and 20X2.			
Depreciation and amortization related to cost of sales			
<i>Depreciation and amortization related to cost of sales</i>			
Depreciation	\$19,126	\$17,984	\$17,893
Intangible asset amortization	12,452	8,194	5,735
Total depreciation and amortization related to cost of sales	\$31,578	\$26,178	\$23,628
Selling, general, and administrative expenses			
<i>Selling, general, and administrative expenses (SG&A)</i>			
Employee compensation (exclusive of one-time employee termination benefits)	\$278,859	\$238,272	\$301,841
One-time employee termination benefits	19,243	60,635	-
Other SG&A ^(b)	199,860	159,308	169,785
Total SG&A	\$497,962	\$458,215	\$471,626
(b) Other SG&A consists primarily of professional services fees and the costs paid to third parties for printing, publications, and advertising for the years ended December 31, 20X4, 20X3, and 20X2.			
Research and development expenses			
<i>Research and development expenses (R&D)</i>			
Employee compensation (exclusive of one-time employee termination benefits)	\$46,242	\$41,379	\$40,764
One-time employee termination benefits	1,454	1,855	-
Other R&D ^(c)	17,836	16,845	15,890
Cost reimbursements ^(d)	(8,297)	(7,905)	(7,756)
Total R&D	\$57,235	\$52,174	\$48,898
(c) Disaggregation of Relevant Expense Captions Other R&D consists primarily of payments to third parties for professional services and licenses of intellectual property for the years ended December 31, 20X4, 20X3, and 20X2.			
(d) Cost reimbursements consist of payments from a strategic partner for employee compensation and materials costs related to R&D incurred as part of a funded research and development arrangement for the years ended December 31, 20X4, 20X3, and 20X2.			

55-19 In addition to the tabular format disclosure illustrated in paragraph 220-40-55-18, Entity X also must disclose its selling expenses and how it defines selling expenses in accordance with paragraphs 220-40-50-35 through 50-36.

Selling Expenses

During the years ended December 31, 20X4, 20X3, and 20X2, selling expenses were \$224,536, \$223,493, and \$231,892, respectively. The entity's selling expenses include those expenses related to advertising and certain customer acquisition-related costs.

8.3 FASB Example 3: Disaggregation of income statement expenses by a bank

FASB Example 3 illustrates one type of tabular format disclosure that a bank could use to meet the disaggregation requirements in Subtopic 220-40 discussed in [chapters 2 to 5](#).

This example also illustrates the disclosure of selling expenses discussed in [chapter 6](#).

Excerpt from ASC 220-40

> Illustrations

- > Example 3: Disaggregation of Income Statement Expenses by a Bank

55-20 This Example illustrates one type of tabular format disclosure that an entity could use to disclose disaggregated expense amounts in accordance with paragraphs 220-40-50-1 through 50-34. This Example also illustrates the disclosure of selling expenses in accordance with paragraphs 220-40-50-35 through 50-36.

55-21 For the year ended December 31, 20X4, Entity X, which is a bank, presents the following comparative income statement.

Entity X			
Consolidated Income Statement			
For the Years Ended December 31, 20X4, 20X3, and 20X2			
	20X4	20X3	20X2
Interest income			
Loans	\$2,795,052	\$2,142,873	\$2,072,997
Investment securities	628,887	442,550	465,842
Other	209,629	116,461	79,193
Total interest income	3,633,568	2,701,884	2,618,032
Interest expense			
Deposits	302,797	30,280	151,399
Borrowed funds	279,505	83,852	167,703
Total interest expense	582,302	114,132	319,102

Net interest income	3,051,266	2,587,752	2,298,930
Provision for (recapture of) credit losses	116,461	(186,337)	372,674
Net interest income after provision for (recapture of) credit losses	2,934,805	2,774,089	1,926,256
Noninterest income			
Service charges on deposit accounts	201,702	171,062	151,969
Other service charges and fees	282,383	239,487	212,757
Total noninterest income	484,085	410,549	364,726
Noninterest expense			
Salaries and employee benefits	1,464,608	1,176,183	1,365,443
Occupancy and depreciation	376,587	279,875	349,679
Data processing	166,111	146,308	161,046
Advertising and marketing	56,876	30,555	28,192
Professional fees	73,230	61,459	74,473
Other	30,513	21,399	24,804
Total noninterest expense	2,167,925	1,715,779	2,003,637
Income before income taxes	1,250,965	1,468,859	287,345
Income tax expense	262,703	308,460	60,342
Net income	\$988,262	\$1,160,399	\$227,003

55-22 Entity X provides a disclosure that disaggregates the occupancy and depreciation expense and other expense captions into the categories listed in paragraph 220-40-50-6. Those expense captions were identified as relevant expense captions because those captions contain one or more of the expense categories listed in paragraph 220-40-50-6. In this Example, even though Entity X also presents separate expense captions on the face of its consolidated income statement for interest expense, provision for (recapture of) credit losses, data processing, advertising and marketing, professional fees, and income tax expense, those expense captions do not contain any of the expense categories listed in paragraph 220-40-50-6 (including those described in paragraphs 220-40-50-10 through 50-11); therefore, those expense captions do not need to be further disaggregated. Entity X applies the practical expedient for employee compensation described in paragraph 220-40-50-20 and elects to not repeat the amount presented on the face of the income statement in the notes to financial statements.

55-23 Entity X recognizes operating lease cost entirely within occupancy and depreciation expense and, therefore, includes operating lease cost as a separate category in accordance with paragraph 220-40-50-22(p).

55-24 Entity X provides the following disclosure.

Disaggregation of Relevant Expense Captions			
	20X4	20X3	20X2
Occupancy and depreciation expense			
<i>Occupancy and depreciation expense</i>			
Depreciation	\$164,232	\$146,403	\$145,907

Operating lease expense	152,445	103,239	149,842
Other occupancy expenses ^(a)	59,910	30,233	53,930
Total occupancy and depreciation expense	\$376,587	\$279,875	\$349,679
(a) Other occupancy expenses consist primarily of repair and maintenance expense for the years ended December 31, 20X4, 20X3, and 20X2.			
Other			
<i>Other</i>			
Intangible asset amortization	\$13,139	\$10,980	\$10,068
Other ^(b)	17,374	10,419	14,736
Total other	\$30,513	\$21,399	\$24,804

(b) Other consists primarily of regulatory licensing fees and charitable contributions for the years ended December 31, 20X4, 20X3, and 20X2.

55-25 In addition to the tabular format disclosure illustrated in paragraph 220-40-55-24, Entity X also must disclose its selling expenses and how it defines selling expenses in accordance with paragraphs 220-40-50-35 through 50-36.

Selling Expenses

During the years ended December 31, 20X4, 20X3, and 20X2, the entity defined selling expenses to be the same as its advertising and marketing expenses, which are presented on the face of its consolidated income statement. The entity's advertising and marketing expenses include costs incurred for advertising, market research, and business development.

Additional resources

There is a page on KPMG Financial Reporting View with all of our existing guidance on expense disaggregation disclosures. Resources include our [Defining Issues](#), [Rolling the DISE: FASB issues final ASU](#), various podcasts including [Rolling the DISE](#) and [Disaggregation of income statement expenses](#), and our webcast, [Disaggregation of Income Statement Expenses \(DISE\)](#).

See KPMG Handbook, [Financial statement presentation](#), for financial statement presentation matters.

See KPMG Handbook, [Segment reporting](#), for segment reporting matters.

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- Business combinations
- Business combinations (SEC reporting)
- Climate risk in the financial statements
- Consolidation
- Contingencies, commitments and guarantees
- Credit impairment
- Debt and equity financing
- Derivatives and hedging
- Discontinued operations and held-for-sale disposal groups
- Earnings per share
- Employee benefits
- Equity method of accounting
- Fair value measurement
- Financial statement presentation
- Foreign currency
- GHG emissions reporting
- Going concern
- IFRS® compared to US GAAP
- Impairment of nonfinancial assets
- Income taxes
- Internal control over financial reporting
- Inventory
- Investment companies
- Investments
- Leases
- Long-duration contracts
- Reference rate reform
- Research and development
- Revenue recognition
- Revenue: Real estate
- Revenue: Software and SaaS
- Segment reporting
- Service concession arrangements
- Share-based payment
- Software and website costs
- Statement of cash flows
- Tax credits
- Transfers and servicing of financial assets

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