



30 Cannon Street, London EC4M 6XH, United Kingdom
Phone: +44 (0)20 7246 6410 Fax: +44 (0)20 7246 6411
Email: iasb@iasb.org Website: <http://www.iasb.org>

**International
Accounting Standards
Board**

This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.

These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting/Joint Meeting: 17/24 October 2006, London/Norwalk

Project: Financial Statement Presentation

Subject: Presenting Information about the Short and Long-term Nature of Assets and Liabilities (Agenda Paper 6B/44B) (Also issued as observer note for Joint IASB/FASB meeting)

-
1. In July, both Boards tentatively agreed that assets and liabilities in the operating category should be classified into short-term and long-term sub-categories on the face of the statement of financial position. In addition, the Boards agreed that information about the liquidity of all assets and liabilities should be presented in the notes to the financial statements. The following related issues are addressed in this memo:
 - a. The basis for determining whether an asset or liability is classified as short-term for presentation purposes.
 - b. What information about liquidity, including the short-term and long-term nature of assets and liabilities not included in the operating category, should be included in the notes to financial statements and how should that information be presented.
 - c. How the short and long-term components of deferred taxes should be determined (this is needed for providing liquidity information. FASB Statement No. 109, *Accounting for Income Taxes*, and IAS 1, *Presentation of Financial Statements*, have different requirements for determining the short and long-term portion of deferred taxes).

Issue 1: Short-Term Classification for Assets and Liabilities

2. Entities that apply IAS 1 are required to present a classified balance sheet *except when a presentation based on liquidity provides information that is reliable and is more relevant*. While U.S. GAAP does not require the presentation of a classified balance sheet, it provides guidance as to how to classify assets and liabilities (that is, segregate assets and liabilities into *current* and *noncurrent*) whenever an entity chooses to do so. The classification of assets and liabilities into current and noncurrent is generally considered to present information about the relative liquidity of an entity.
3. While both Boards tentatively agreed that only the assets and liabilities in the operating category should be further classified into short-term and long-term sub-categories, the Boards differed on how *short-term* should be defined. The IASB tentatively agreed with the staff recommendation that the short-term subcategory should be based on whether the expected realization or settlement of the asset or liability is within the current operating cycle (*operating cycle* approach). The staff recommended that *operating cycle* be defined as the “average time between the acquisition of materials or services entering the process and their final conversion to cash.” The FASB disagreed with the staff recommendation, as classification based on the operating cycle notion is considered outdated and not strictly followed in practice. The FASB tentatively agreed that the short-term subcategory should be based on one-year to conversion or settlement (*one-year* approach). The FASB asked the staff to address whether the *one year* approach should be based on contractual maturities or on expected realization.
4. Both U.S. GAAP and IFRS currently distinguish between *current* and *non-current* assets and liabilities by referring to the *operating cycle* concept (as described below).
 - a. ARB No. 43, Chapter 3A, “Working Capital—Current Assets and Current Liabilities,” defines the *operating cycle* as “the average time intervening between the acquisition of materials or services entering [the] process and the final cash realization” (paragraph 5). When there are several operating cycles occurring within a year, a one-year time period is used as a basis for segregating current assets; however, when the operating cycle is more than twelve months, the longer period is used. Where a particular business has no clearly defined operating cycle, the one-year rule governs.
 - b. IAS 1, *Presentation of Financial Statements*, defines the *operating cycle* as “the time between the acquisition of assets for processing and their realization in cash or cash

equivalents” (paragraph 59). When the entity’s normal operating cycle is not clearly identifiable, its duration is assumed to be twelve months.

5. As the operating cycle for some entities is longer than one year, some assets are classified as current even though they cannot be converted to cash within a year. For example, a distillery may classify its work-in-process as inventory (a current asset) for more than 20 years. Conversely, some assets are classified as current because they are expected to be converted to cash within a year even though their original maturity was longer than one year (such as the short-term portion of long-term loans). Other long-term assets are considered current because IAS 1 requires assets and liabilities held primarily for the purpose of being traded to be accounted for as current, regardless of whether they relate to the operating cycle. This is consistent with the notion that assets and liabilities used for the purpose of trading are expected to be converted to or settled with cash within one year.
6. This issue was discussed at the September 2006 JIG meeting. JIG members had differing views on whether the operating cycle or one year should be used to determine what is classified as short-term; however, the staff notes that the discussion focused on assets (inventory in particular) not on liabilities. It appears that if inventory that was not expected to be utilized (converted into cash) within one year could be classified as long-term, most would not be opposed to the one-year approach. The staff notes that if short-term were determined to be one year, accounting guidance related to inventories could be amended to require the presentation of short-term inventory and long-term inventory.
7. The staff further notes that the difference in the Board’s views is only relevant when an entity’s operating cycle is longer than one year. IASB members indicated a willingness to consider the *one-year* approach. At the October joint meeting, the staff would like the Boards to reach a common answer on this issue.

Staff Analysis

8. If *short-term* is to be defined based on an entity’s *operating cycle*, the result may be a varied presentation of short-term operating assets and liabilities which may undermine the comparability of the information presented in the financial statements. In addition, application of an *operating cycle* approach could be difficult for an entity that has one or

more operations with an operating cycle longer than one year and could result in a presentation in the financial statements that is less than transparent.

9. The staff notes that, while the *operating cycle* approach may be considered to be more consistent with how items will be classified in the various categories, (that is, based on how the entity manages its business), the operating cycle approach has not been strictly applied in practice. For example, most entities that have an operating cycle longer than one year classify their inventory as current but classify their liabilities based on the one year approach.
10. As noted during the FASB and JIG meetings, if information is needed about the length of an entity's operating cycle, it can be provided in the notes. The staff's preference is the *one-year* approach.
11. From the perspective of the user of the financial statements, the *one-year* approach is objective and straight-forward because a one year time period is objective; a user does not necessarily know how long an entity's operating cycle is. Further, many entities operate on multiple operating cycles, which adds complexity and decreases comparability of liquidity information. In addition, the resulting information will allow a user of the financial statements to assess the ability of an entity to settle its liabilities due within a year, with the assets to be converted into cash within a year.
12. One year is an arbitrary cut-off to determine which assets and liabilities are considered short-term and which are considered long-term. While it may be arbitrary, one year is consistent with the time frame in which information is reported in annual financial statements.

One Year Based on What?

13. As for whether the *one-year* approach should be based on contractual maturities or expected realization or settlement, the staff looks to ARB 43, which states that current assets "are those which are reasonably expected to be realized in cash or sold or consumed during the normal operating cycle of the business" and that current liabilities are "obligations whose liquidation is reasonably expected to require the use of existing resources properly classifiable as current assets, or the creation of other current liabilities." IAS 1 contains a similar expectations-based definition.

14. The staff notes that if the one-year classification is based on expected realization and does not consider contractual maturity, it is possible to have an outstanding note payable expected to be refinanced with a contractual maturity of 6 months classified as long-term because an entity intends (expects) to make payment on the debt after 12 months. The staff recommends that, for purposes of determining whether an asset or liability is short-term, the one-year approach be based on the *shorter* of the asset or liability's (a) contractual maturity or (b) expected realization or settlement. That is, a note payable with a contractual maturity of 6 months must be classified as short-term and a note payable with a contractual maturity of 12 months or more can be classified either as short-term or long-term, depending on the expectation (intent) of the entity.
15. The staff notes that the "shorter of" approach is consistent with the FASB's decision in the short-term convergence project to converge with IAS 1 related to the classification of short-term obligations expected to be refinanced and obligations that are callable because of a violation in a covenant.
16. Under existing guidance, some line items that have both short and long-term components, (for example, inventory), are classified entirely as current or noncurrent. According to the *operating cycle* approach, inventory would be considered short-term as it is considered part of an entity's *operating working capital*. If the inventory is to be converted to cash in the operating cycle, inventory would be classified as short-term, regardless of the actual time expected to cash realization of that inventory. In contrast, according to the *one-year* approach, inventory expected to be realized in cash within 12 months of the balance sheet date would be considered short-term and inventory expected to be realized more than 12 months from the balance sheet date would be considered long-term. (That staff notes that this change is not one of recognition or measurement, only one of presentation.) The staff believes that classifying only items that are expected to be converted to cash within 12 months of the balance sheet date as short-term gives a more accurate and informative view of an entity's liquidity position. This would suggest that the one-year approach be used for short-term and long-term classification on the statement of financial position.
17. While the Boards only discussed classifying operating assets and liabilities into short-term and long-term categories, the staff would like to clarify that the short-term definition should

apply to **all** assets and liabilities. The staff notes that the concept similar to working capital as defined in ARB 43 would be **all** short-term assets less **all** short-term liabilities (not just those in the operating category); therefore the agreed-upon definition should apply to all assets and liabilities for presentation purposes. (Determining the short-term portion of assets and liabilities may be necessary for presenting information about liquidity as addressed in Issue 2).

Staff Recommendation

18. The staff recommends that an entity be required to present short-term and long-term subcategories in the operating category on the statement of financial position. An asset or liability would be classified as short-term if the shorter of (a) the contractual maturity or (b) the expected realization or settlement of the asset or liability is within one year. Otherwise, the asset or liability should be classified as long-term. In addition, the staff recommends that an entity with an operating cycle longer than one year be encouraged to describe its operating cycle in the notes to financial statements.
19. The staff also recommends that the Boards confirm that the operating category is the only category or section that should be further classified into short-term and long-term subcategories on the face of the statement of financial position. The main reason for this is to keep that statement as uncluttered as possible. As noted at the July Board meetings and as discussed in the following issue, information about the short-term and long-term nature of the other categories can be provided in the notes to financial statements.

Question 1.a: *Should an entity be required to present operating assets and liabilities in short- and long-term categories on the face of the statement of financial position? If so, should assets and liabilities be classified as “short-term” if the shorter of (a) the contractual maturity or (b) the expected realization or settlement of the asset or liability is within one year?*

Question 1.b: *Should assets and liabilities in any category or section other than the operating category be classified into short-term and long-term subcategories on the face of the statement of financial position? If so, which category or section?*

Question 1.c: *Should working capital be defined in the financial statement presentation standard? If so, should it be defined as all short-term assets less all short-term liabilities?*

Issue 2: Information about Liquidity

Background

20. In July, the Boards agreed that information about the liquidity of an entity's assets and liabilities should be presented in the notes to financial statements. This additional information would be provided in support of the project working principle that states that the financial statements should provide information in a manner that will help a user of those financial statements assess the liquidity of an entity's assets and liabilities.
21. The FASB noted at their July meeting that identifying the short-term and long-term operating assets and liabilities on the face of the statement of financial position using a one-year approach will provide liquidity information about assets and liabilities in the operating category. Those Board members were open to presenting other information about liquidity in the notes to the financial statements with a leaning toward disclosure of assets and liabilities in order of liquidity.
22. At their July meeting, the IASB agreed with the staff recommendation that **all** assets and liabilities (not just those in the operating category) be presented in the **notes** in short-term (within one year) and long-term categories. However, IASB members expressed their concern that this supplemental information (as illustrated in the July memo) appeared to be repetitive and duplicative of the information presented on the statement of financial position. In addition, IASB members suggested that the notes include information regarding the maturities of assets and liabilities.

Possible Alternatives

23. Based on Board member input at the July meetings and discussions with JIG members in September, the staff developed the following possible alternatives for disclosing information about liquidity in financial statements. These alternatives are based on the presumption that the operating category is the only category that is further classified into short- and long-term subcategories on the statement of financial position. Because the statement of financial position will no longer be presented based on asset/liability classifications with subtotals for current and noncurrent assets and liabilities, and totals for assets and liabilities, each of the following alternatives will provide that information.

- a. **Alternative A**—Information about short and long-term assets and liabilities would be presented **by line item in order of liquidity** as follows: Asset line items would be presented in order of liquidity in two sections—short-term and long-term, followed by a number for total assets. Similarly, liabilities would be presented in order of liquidity in two sections—short-term and long-term, followed by total liabilities. Alternative A is illustrated in paragraph 27.
 - b. **Alternative B**—Information about short and long-term asset and liabilities would be presented **by category** as follows: the total amount of short-term assets for each category would be presented followed by a total for short-term assets. The same would be done for long-term assets, followed by a total for long-term assets and then total assets. The same presentation would be done for short and long-term liabilities. Alternative B is illustrated in paragraph 25.
 - c. **Alternative C**—Information about short and long-term asset and liabilities would be presented **by line item for all but the operating category** as follows: the total amount of short-term assets for the operating category would be presented along with the short-term line items for all the other categories, followed by a total for short-term assets. The same would be done for long-term assets, followed by a total for long-term assets and then total assets. The same presentation would be done for short and long-term liabilities. Alternative C is illustrated in paragraph 26.
24. In addition, details of the long-term maturities or expected cash flows for certain liabilities (pension and lease obligations and long-term debt) would be required in columnar format as illustrated following alternative disclosures. (Note that the following examples are based on the statement of financial position illustrated in Memorandum 44D/Agenda Paper 6D.)

25. The following illustrates the disclosure suggested in Alternative A:

Short and Long-term Assets and Liabilities by Line Item in Order of Liquidity

	<u>2006</u>	<u>2005</u>	<u>2004</u>
ASSETS			
<i>Short-term assets</i>			
Cash and cash equivalents	180	100	110
Accounts receivable	140	120	125
Inventory	50	40	40
Short-term portion of deferred tax asset	90	70	110
Short-term discontinued operation assets	35	-	-
Total short-term assets	<u>495</u>	<u>330</u>	<u>385</u>
<i>Long-term assets</i>			
Long-term inventory	20	20	20
Long-term portion of deferred tax asset	25	10	10
PP&E	530	510	445
Identifiable intangible assets	30	20	10
AFS securities	20	15	10
Equity method investment	80	70	90
Goodwill	90	90	90
Long-term discontinued operation assets	30	-	-
Total long-term assets	<u>825</u>	<u>735</u>	<u>675</u>
Total assets	<u><u>1,320</u></u>	<u><u>1,065</u></u>	<u><u>1,060</u></u>
LIABILITIES			
<i>Short-term liabilities</i>			
Accounts payable	120	80	100
Income tax payable	25	20	15
Commercial paper payable	80	60	74
Short-term portion of deferred tax liability	5	10	15
Short-term discontinued operation liabilities	105	-	-
Total short-term liabilities	<u>335</u>	<u>170</u>	<u>204</u>
<i>Long-term liabilities</i>			
Long-term portion of deferred tax liability	45	40	105
Bank loan payable	240	300	360
Pension liabilities	170	130	86
Total long-term liabilities	<u>455</u>	<u>470</u>	<u>551</u>
Total liabilities	<u>790</u>	<u>640</u>	<u>755</u>
EQUITY			
Total liabilities and equity	<u><u>1,320</u></u>	<u><u>1,065</u></u>	<u><u>1,060</u></u>

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Thereafter</u>	<u>Total</u>
Bank loan payable	60	30	30	30	30	60	240
Pension obligation	15	20	25	30	35	125	

26. The following illustrates the disclosure suggested in Alternative B:

Disclosure: Short-term and Long-term Assets and Liabilities by Category

	2006	2005	2004
ASSETS			
<i>Short-term assets</i>			
Business assets	190	160	165
Financing assets	180	100	110
Discontinued operation assets	35	-	-
Income taxes, including deferred	90	70	110
Total short-term assets	<u>495</u>	<u>330</u>	<u>385</u>
<i>Long-term assets</i>			
Business assets	770	725	665
Financing assets	-	-	-
Discontinued operation assets	30	-	-
Income taxes, including deferred	25	10	10
Total long-term assets	<u>825</u>	<u>735</u>	<u>675</u>
Total assets	<u><u>1,320</u></u>	<u><u>1,065</u></u>	<u><u>1,060</u></u>
LIABILITIES			
<i>Short-term liabilities</i>			
Business liabilities	120	80	100
Financing liabilities	-	-	-
Discontinued operation liabilities	105	-	-
Income taxes, including deferred	30	30	30
Total short-term liabilities	<u>255</u>	<u>110</u>	<u>130</u>
<i>Long-term liabilities</i>			
Business liabilities	170	130	86
Financing liabilities	320	360	434
Income taxes, including deferred	45	40	105
Total long-term liabilities	<u>535</u>	<u>530</u>	<u>625</u>
Total liabilities	<u>790</u>	<u>640</u>	<u>755</u>
EQUITY			
Total liabilities and equity	<u><u>1,320</u></u>	<u><u>1,065</u></u>	<u><u>1,060</u></u>

	2007	2008	2009	2010	2011	Thereafter	Total
Bank loan payable	60	30	30	30	30	60	240
Pension obligation	15	20	25	30	35	125	

27. The following illustrates the disclosure suggested in Alternative C:

**Disclosure: Short-term and Long-term Assets and Liabilities by Line Item
(operating assets and liabilities aggregated on one line)**

	<u>2006</u>	<u>2005</u>	<u>2004</u>
ASSETS			
<i>Short-term assets</i>			
Cash and cash equivalents	180	100	110
Short-term investments	-	-	-
Operating assets	190	160	165
Short-term portion of deferred tax asset	90	70	110
Short-term discontinued operation assets	35	-	-
Total short-term assets	<u>495</u>	<u>330</u>	<u>385</u>
<i>Long-term assets</i>			
Operating assets	670	640	565
Long-term portion of deferred tax asset	25	10	10
Investing assets	100	85	100
Long-term discontinued operation assets	30	-	-
Total long-term assets	<u>825</u>	<u>735</u>	<u>675</u>
Total assets	<u><u>1,320</u></u>	<u><u>1,065</u></u>	<u><u>1,060</u></u>
LIABILITIES			
<i>Short-term liabilities</i>			
Operating liabilities	120	80	100
Income tax payable	25	20	15
Commercial paper payable	80	60	74
Short-term portion of deferred tax liability	5	10	15
Short-term discontinued operation liabilities	105	-	-
Total short-term liabilities	<u>335</u>	<u>170</u>	<u>204</u>
<i>Long-term liabilities</i>			
Long-term portion of deferred tax liability	45	40	105
Bank loan payable	240	300	360
Operating liabilities	170	130	86
Total long-term liabilities	<u>455</u>	<u>470</u>	<u>551</u>
Total liabilities	<u>790</u>	<u>640</u>	<u>755</u>
EQUITY	<u>530</u>	<u>425</u>	<u>305</u>
Total liabilities and equity	<u><u>1,320</u></u>	<u><u>1,065</u></u>	<u><u>1,060</u></u>

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Thereafter</u>	<u>Total</u>
Bank loan payable	60	30	30	30	30	60	240
Pension obligation	15	20	25	30	35	125	

Staff Analysis

28. **Alternative A** provides information on the relative liquidity of all assets and liabilities on the statement of financial position without regard to which category they are included in. While presenting information in order of liquidity might appear to be providing users with useful information, there are instances in which it might not. For example, there are long-term line items on a statement of financial position that are an aggregation of items that have varying conversion or maturity dates (for example, PP&E and long-term debt). If the line items are to be presented in order of liquidity some “averaging” would need to be done for those items. If the weighted average for long-term debt is 8 years while some debt matures in 2 years and some in 15 years, presenting the long-term debt line as being “liquid” in 8 years could be very misleading.
29. Current accounting standards require disclosure of maturity information or expected cash flow information for certain long-term liabilities (pensions, debt, and leases). Thus more detailed information about the liquidity of items that tend to be aggregated on the face of the statement of financial position is available in the notes. The staff is of that view that that information should be presented in the same note disclosure as the liquidity information. Even if the aggregation issue described in the above paragraph was not a problem for an entity, the Alternative A disclosure might be more than users need as it repeats what is on the face of the statement of financial position.
30. **Alternative B** provides short-term and long-term asset and liability amounts for each category on the statement of financial position. Except for operating assets and liabilities that are presented on the face of the statement of financial position, a user would not be able to determine whether the specific assets and liabilities in other categories are short or long-term in nature by referring to this liquidity note. Alternative B would allow users to analyze liquidity by categories only—it does not provide information about the relative liquidity of line items presented on the statement of financial position. However, as discussed above, that may not necessarily be very useful information.
31. **Alternative C** provides information about the short and long-term nature of the line items on the statement of financial position other than the operating category (as that information is on the face of the statement). While this information is not in order of liquidity (because of the

aggregation issue), it does provide users with information similar to what is presented today in a classified balance sheet.

32. In the materials for discussion at the September 2006 JIG meeting, two other possible alternatives were included. One would have presented assets and liabilities disaggregated according to their expected maturity, using a columnar format with different time intervals (for example, within 1 year, 1 to 2 years, 2 to 5 years, and after 5 years). In discussing that alternative, some JIG members noted that providing a liquidity schedule that attempts to provide maturity information for each line item is impractical. The other alternative would have disaggregated assets and liabilities into two columns based on whether expected maturity was more or less than one year. For certain assets and liabilities, details of the long-term maturities by various time intervals would be required in columnar format. JIG members noted that the additional maturity information provided should focus on liabilities rather than assets.

Staff Recommendation

33. The staff recommends Alternative B—presenting short-term and long-term assets and liabilities by category as described in paragraph 23b and illustrated in paragraph 26. Line items presented on the face of the statement of financial position oftentimes aggregate assets or liabilities with varying maturities. Therefore, the staff is of the view that liquidity information provided by classifying line items in order of liquidity (Alternative A) represents relative liquidity at best and, therefore, disclosure of short- and long-term assets and liabilities at the category level would be sufficient. Because of the various categories on the face of the statement of financial position, the staff is of the view that the additional information in Alternative C (information about short- and long-term assets and liabilities presented by line item for all but the operating category) is not necessary.
34. For specific line items that aggregate the same asset or liability with varying maturities for which detailed information regarding those maturities would be useful, the staff recommends that maturity schedules be presented. Such information is currently required in U.S. GAAP for pensions, leases, and long-term debt.
35. If the Boards are of the view that users need information about the short and long-term nature of **all** assets and liabilities, the staff recommends that that information be provided on the

face of the statement of financial position, otherwise information in the notes would be almost duplicative of information on the face. In that case, in order to present total short-term assets and total short-term liabilities (that is, relative liquidity), the staff is of the opinion that a note disclosure would still need to be presented. The staff notes that Alternative C in combination with the statement of financial position would provide that information.

Question 2a: Should the notes to financial statements include information about the relative liquidity of each category (that is, short- and long-term asset and liabilities by category) as well as the totals for short- and long-term assets and liabilities and total assets and total liabilities?

Question 2b: Should details of long-term maturities be required to be presented for a liability presented on the statement of financial position that is an aggregation of similar liabilities with varying maturities (such as lease and pension obligations and long-term debt)?

Issue 3: Short and Long-term Components of Deferred Taxes

36. FASB Statement No. 109, *Accounting for Income Taxes*, requires that, in a classified statement of financial position, an entity separate deferred tax liabilities and assets into a current amount and a noncurrent amount. The classification of deferred tax liabilities as current or noncurrent should be based on the classification of the related asset or liability for financial reporting. IAS 1, *Presentation of Financial Statements*, requires that, when an entity presents a classified balance sheet, deferred tax assets and liabilities be presented as noncurrent.

37. In Issue 1 of this memo, the staff recommends that *operating* assets and liabilities be the only assets and liabilities classified into short- or long-term subcategories on the face of the statement of financial position. However, in order to provide liquidity information under Alternative A, B, or C in the prior issue, the short-term and long-term nature of deferred taxes will need to be determined. The question is what approach should be used to determine that short- and long-term split. The choices would be as follows:

- a. The short-term portion of a deferred tax liability or asset would be the deferred tax consequences of timing differences that will result in taxable or deductible amounts during the following year. This is the approach adopted in FASB Statement No. 96, *Accounting for Income Taxes*, the predecessor to Statement 109.
- b. Deferred taxes would be classified as short-term or long-term based on the classification of the related asset or liability. This is the approach adopted in Statement 109. A deferred tax liability or asset that is not related to an asset or liability for financial reporting purposes would be classified according to the expected reversal date of the temporary difference pursuant to FASB Statement No. 37, *Balance Sheet Classification of Deferred Income Taxes*. Valuation allowances for a particular tax jurisdiction would be allocated to short-term and long-term deferred assets on a pro-rata basis.
- c. All deferred taxes would be classified as long-term. This is the approach adopted in IAS 12. This could be viewed as a practical exception to the presentation required for all other assets and liabilities.

38. The FASB decided not to adopt approach (a) in Statement 109 because it required a detailed analysis to determine the amount of next year's reversing temporary differences. In particular, Statement 96 required that the **current** portion of a deferred tax liability or asset should be the deferred tax consequences of temporary differences that will result in taxable or deductible amounts during the following year or operating cycle if longer than one year. The FASB decided to adopt approach (b) because it would be easier to understand and apply, and would not create the impression that detailed scheduling was required, while the results from (b) would not differ significantly from (a).

Staff Recommendation

39. The staff recommends that the short-term and long-term portion of deferred taxes be disclosed in the notes to the financial statements in the same manner as other assets and liabilities and, therefore, does not support approach (c). The staff recommends that the short-term portion of deferred taxes be determined based on the classification of the related asset or liability (approach (b)). The staff is of the view that while approach (a) seems to be superior in concept, approach (b) is a reasonable compromise.

Question 3: *Should the short-term portion of deferred taxes be determined based on the classification of the related asset or liability?*