Project **Financial Statement Presentation**

Topic **Remeasurement definition and display**

Introduction and background

1. As mentioned in WG Paper 4, in October 2009, the boards agreed to eliminate the reconciliation schedule and present information about remeasurements in the SCI or the notes. At the working group meeting, we would like to get input on the definition and display of a remeasurement. The definitional issues raised in this paper will be addressed at the February joint meeting.

2. At the joint meeting in October 2009, the FASB tentatively agreed to require disaggregation of remeasurements on the statement of comprehensive income (SCI) in a columnar format. The IASB expressed a preference for presenting information about remeasurements in a single note to financial statements. Both boards also agreed that the notes to financial statements should include a description or explanation of the remeasurement information presented on the SCI/in the notes.

3. Both boards seem to agree that providing this type of information could help users understand and assess an entity's performance, but there remains a lack of agreement on what exactly to disaggregate as a remeasurement.

Definition of a remeasurement

4. In February, the staff will ask the boards to agree on a definition to be included in the exposure draft. In the materials for that meeting, the staff recommend the following definition:

> A *remeasurement* is an amount recognised in comprehensive income that reflects the effects of a change in the net carrying amount of an asset or liability and is the result of:

a. a change in (or transacting at) a current price or value,

b. a change in an estimate of a current price or value, or

c. *a change in any estimate or method used to measure the carrying amount of an asset or liability*.

5. In addition, the staff recommend that the sale of ordinary inventory (including the realised income from the market-making activities of broker-dealers) should **not** be presented as a remeasurement.

6. In thinking about this issue, the staff considered whether to exclude from the presentation of remeasurements other remeasurements that arise as a result of selling or holding ordinary inventory (e.g., reassessments of the collectability of receivables or the write down of inventory to lower-of-cost-or-market). Although there are reasonable arguments for excluding these types of items, for the reasons explained below, the staff decided to recommend that these items **be included** in the presentation of remeasurements.

Changes in estimates

7. One of the main questions for the boards in February is whether estimates should be considered remeasurements. Part (c) of the definition in paragraph 4 brings in the effect on current period income arising from changes in any estimate or method used to measure the carrying amount of an asset or liability.

8. One reason for including changes in estimates is that the staff agree with the concern expressed by some board members that it could be misleading to present as remeasurements only those changes that are tied to prices, thereby implying that the changes in *market* expectations somehow have different implications for the future than changes in *management* expectations. Unbiased changes in management estimates, just like unbiased changes in market expectations, should have a relatively low correlation with the changes in those same prices or estimates in future periods. Therefore, providing feedback on how both types of expectations have evolved during the period is likely to be useful to users of financial statements.

9. In addition, the staff agree with feedback received at a recent meeting with members of the FASB Investors Technical Advisory Committee (ITAC). When asked about this issue, ITAC members said that users can better analyse an

entity's performance when they understand how changes in management's estimates have impacted the carrying value of its assets and liabilities from one period to the next, as noted above.

Possible exclusions

10. Although the sale of ordinary inventory at an amount different than carrying amount meets the definition of a remeasurement, these remeasurements are fundamentally different in character than other types of realised remeasurements (e.g., the sale of PP&E). In fact, current reporting requirements already highlight the results of these transactions by showing the realised "remeasurement" (that is, the gross margin on sales) on the SCI. Therefore, the staff see little reason for including the gross margin from the sale of inventory with other remeasurements and is recommending that the sale of ordinary inventory (including the realised income from the market-making activities of broker-dealers) not be presented as a remeasurement.

11. As with the selling of inventory, the decrease in value of inventory due to factors such as breakage, shrinkage, spoilage, or obsolescence also meet the proposed definition of a remeasurement. However, for many firms, inventories are routinely manufactured or otherwise produced on a large scale, repetitive basis, and so regularly experience predictable amounts of breakage, shrinkage, spoilage, and/or obsolescence. Some board members have expressed concern that capturing these costs as remeasurements offers little informational benefit to justify the cost of doing so. Similar arguments can be made for the cost of bad debt arising from trade receivables.

12. While the staff agree that such remeasurements are likely to be highly predictable for some firms, variation in these amounts (either between firms or for the same firm across time) can provide useful information to users about how firms manage their inventory and collections processes. In addition, allowing exceptions for these items would introduce subjectivity into the presentation of remeasurements. Therefore, the staff is recommending that an entity not be permitted to exclude these "ordinary" remeasurements from presentation.

Staff analysis

13. The staff think that the definition proposed in paragraph 4 and related guidance (see the Appendix) will result in the presentation of information useful in assessing the persistence of comprehensive income components.

14. In particular, disaggregation of comprehensive income in this manner would help users identify those portions of current period income that are not the result of routine allocations (which affect future earnings in predictable ways) and help users identify those portions of current period income that are, instead, the result of changes in market prices, revisions in management's estimates, or the realisation of amounts that are different from the previously reported carrying value of an asset or liability.

15. This information is important because changes in prices and estimates, if unbiased, should have a relatively low correlation with the changes in those same prices or estimates in future periods. In addition, this information is likely to be useful to users of financial statements because it provides feedback on how management's expectations (or, for fair values, market expectations) have evolved during the period.

Discussion questions—remeasurement definition
1a. Should the definition of a remeasurement include "a change in any estimate or method used to measure the carrying amount of an asset or liability"? Why or why not? 1b. If not, should the boards limit the definition to "changes in a current price or value or an estimate of a current price or value"? 2. Is the definition in paragraph 4 and related guidance in the appendix clear? Is it operational? If not, why not. 3. Ignoring the definition in paragraph 4, what items from the list in the Appendix would you like to see included/excluded from presentation? Is there a unifying theme around the items you want in or out?

Discussion question—remeasurement display
4. The FASB thinks the most transparent way to present remeasurement information is on the SCI in the context of the other components of comprehensive income. The IASB does not support a multi-column SCI and thinks presentation in a single note along with narrative explanation will provide users with the information they are seeking without cluttering the SCI. Should remeasurements be presented on the SCI or in the notes?

Appendix

Related guidance on the definition of a remeasurement

A1. The following paragraphs provide an additional explanation of the remeasurement definition described in this working group paper.

A2. A remeasurement includes (but is not limited to) changes in fair value (e.g., financial instruments), changes in the method of estimating an allowance for items measured at net realisable value (e.g., accounts receivable), asset impairments, including inventory impairments, and the realised gain/loss on the sale of property, plant, and equipment (PP&E).

A3. A remeasurement does not include the initial recognition of an asset or liability, a change in an asset or liability attributable to the passage of time (e.g., the accretion of a liability), or routine allocations (e.g. depreciation, amortization).

A4. A remeasurement also does not include the initial recognition of, or changes in, a provision or allowance associated with an asset or liability when that provision or allowance is recognized or changed as part of the initial measurement of the underlying asset or liability (e.g., the initial recognition of a reserve, or adjustments to an existing reserve, to reflect newly originated or acquired loans).

A5. Similarly, the initial recognition of a net contract position would not be a remeasurement. However, adjustments to current period revenue arising from a reassessment of prior period performance would be disaggregated as a remeasurement. Similarly, the loss recognized on an onerous contract would constitute a remeasurement.

A6. A remeasurement also does not include amounts that are “partially realised” during a period (e.g., the receipt of cash related to debt securities, dividends on equity securities, or rental income on investment properties). In such cases, the recorded values of the underlying assets or liabilities will decline, but not necessarily because expectations about future cash flows have changed.

Examples of remeasurements

A7. Below is a table that illustrates, for some common assets and liabilities, the changes in carrying amounts that would be disaggregated as a remeasurement (that is, included in the remeasurement column on the SCI or in the notes) and the changes that would not using the definition and guidance in paragraph 4.

	Presented as a remeasurement?	
Item	**Yes**	**No**
Revenues	• Gains/losses on derivatives to fix the sales price of anticipate sales • Adjustments to revenue arising from re-estimation of the contract receivable • Losses on onerous contracts	• Gross margin earned on sale of goods • Spread earned by broker dealers • Initial recognition of and adjustments to allowance for sales returns
Costs of goods sold	• Gains/losses on derivatives hedging the purchase price of inventory • Changes in the market price of inventories measured at estimated market value • Write down of inventory to lower-of-cost-or-market • Adjustments to methods of estimating inventory value and COGS	• Cost of sales
Bad debt expense (or other similar provisions)	• Revisions of existing allowance due to changes in the character of the receivable/portfolio such as deteriorating credit quality • Other income/expense arising from changes in the method of estimating allowance	• Initial recognition of allowance for an individual account or portfolio, if recognized as part of the initial measurement of the associated asset • Routine changes in allowance
Pension expense / pension liability adjustment	• Return on plan assets • Settlements/curtailments • Actuarial gain/loss on obligations	• Service cost • Prior service costs • Interest cost
Depreciation and other gains/losses related to fixed assets	• Revaluation • Impairment • Disposal gains/losses • Change in depreciation estimates	• Depreciation expense
Amortization and other gains/losses related to intangible assets	• Impairment • Disposal gains/losses • Change in amortization estimates	• Amortization expense

	Presented as a remeasurement?	
Item	**Yes**	**No**
Income/expense and other gains/losses related to financial investments	• OTTI • Holding gains/losses • Realized gains/losses	• Interest income • Dividend income
Income/expense and other gains/losses related to financial liabilities	• Changes in fair value • Realized gain/loss on retirement	• Interest expense
Investment property	• Changes in property values	• Rent
Income taxes	• Changes in tax rates • Revisions to valuation allowance on deferred tax asset/liability	• Current period income tax expense
Foreign currency gain/loss	• All income/expense	