



FASB Proposes Changes to Presentation of Net Benefit Cost

To increase transparency, the FASB recently proposed changes to the financial statement presentation of net benefit cost.¹ The proposed changes may affect the reported amounts of cost of sales, gross profit, and operating income for some companies, and are intended to provide financial statement users with more decision-useful information.

Key Facts

- The FASB’s proposal would require entities to:
 - Report service cost in the same line item(s) as other compensation costs; and
 - Present other components of net benefit cost separately from service cost in the income statement and outside a subtotal of operating income, if presented.
- Service cost would be the only component of net benefit cost eligible for capitalization.
- The proposed guidance would apply to all entities, including not-for-profit entities, that offer defined benefit pension or other postretirement benefit plans.

Key Impacts

- The proposed changes may affect the amount of reported gross profit and operating income.
- Because only the service cost component is eligible for capitalization, the carrying amount of inventory and self-constructed assets may change.
- U.S. GAAP would align more closely with IFRS because the service cost component would be reported in the income statement separately from the other components of net benefit cost.

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¹ FASB Proposed Accounting Standards Update, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, January 26, 2016, available at www.fasb.org. Net benefit cost comprises defined benefit pension cost and postretirement benefit cost.



By including the service cost component with other compensation costs and presenting the other components of net benefit cost outside of operating income, volatility of certain financial metrics may be reduced, which would improve their predictive value to users.

How Would Financial Statement Information Improve?

FASB stakeholders have observed that presenting defined benefit cost on a net basis combines elements that are distinctly different. Service cost is the only component that originates from employee service exclusively and, therefore, generally is analyzed differently from other components of net benefit cost.

An increasing number of entities have elected a policy to recognize actuarial gains and losses immediately in the income statement, resulting in increased volatility in financial performance measures such as cost of sales, gross profit, selling, general and administrative (SG&A) expenses, and operating income. Presenting the other components of net benefit cost outside of operating income may reduce this volatility, and users may be able to perform a more cost-effective and predictive analysis of the financial performance measures during the reporting period.

Effect on Capitalized Assets

The proposal likely would change the carrying amount of inventory and self-constructed assets, because only the service cost component would be eligible for capitalization, thereby limiting the eligible amount to only those costs most closely associated with current operating activities.

Effect on U.S. GAAP and IFRS Comparisons

U.S. GAAP would align more closely with IFRS because the service cost component would be separated from other components of net benefit cost. Although limiting the amount eligible for capitalization to service cost would result in a difference between U.S. GAAP and IFRS, the changes would allow financial statement users to better compare the current period's operating activities.

Disclosures about Amounts Reclassified out of Accumulated Other Comprehensive Income

An entity would need to disclose each income statement line item affected by amounts related to pension and other postretirement benefits that are reclassified out of accumulated other comprehensive income. The amortized amounts no longer would be eligible for capitalization and would be reclassified to net income in their entirety in the same reporting period.

Proposed Transition

Retrospective Application

Presentation of components of net benefit cost in the income statement

Prospective Application

Capitalization of service cost component in assets

Entities would need to disclose the nature of, and reason for, the change in accounting principle in the first interim and annual reporting periods of adoption.

Looking Ahead

We encourage entities to consider the potential effects of the FASB's proposed changes on their financial statements, performance measures, and compensation arrangements tied to operating metrics; to evaluate the effect on financial statement users; and to provide comments to the FASB by the April 25 comment deadline.

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