SFAS 130, REPORTING COMPREHENSIVE INCOME (1997)

In June, 1997, the FASB issued Statement 130; the exposure draft is described in the Analysis and Use of Financial Statements, 2nd edition (AUFS) on page 18. The only significant change from the exposure draft is that comprehensive income per share is not a required disclosure. The standard does not change any accounting method, only the way financial data are displayed.

Comprehensive income is defined as:
the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners.¹

Thus, comprehensive income includes both net income and direct-to-equity adjustments such as:

1. Cumulative translation adjustments under SFAS 52 (AUFS, Chapter 15)
2. Minimum pension liability under SFAS 87 (AUFS, Chapter 12)
3. Unrealized gains and losses on available-for-sale securities under SFAS 115 (AUFS, Chapter 13)

These adjustments are collectively known as other comprehensive income. The current FASB project on derivatives and hedging (AUFS, Box 16-2) is expected to result in additional adjustments that will be included in other comprehensive income.

The new standard requires that firms with items of other comprehensive income report:

1. The closing balance of each such item. Their total is reported as a separate component of equity called accumulated other comprehensive income.
2. The change (either pretax or post-tax) in each item; the change can be reported either gross (showing both additions and subtractions) or net.
3. Reclassification adjustments to avoid double counting. For example, realized investment gains that include unrealized gains from prior years would be double counted unless those unrealized gains are deducted from other comprehensive in the year of realization.²

¹ SFAC 6 (1985), paragraph 70, emphasis added.
2 Reclassification adjustments are not required for the minimum pension liability. Such adjustments for the cumulative translation adjustment are limited to translation gains and losses realized upon sale or liquidation of the investment in foreign subsidiaries. Reclassification adjustments in comparative statements provided for earlier periods are encouraged, but not required.

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(continued)

4. Total comprehensive income in condensed financial statements provided for interim periods.

Alternative displays are permitted. For example, firms can provide a separate statement of comprehensive income or can combine that statement with the income statement. Some data can be reported either on the statement face or in footnotes.

SFAS 130 is effective in calendar 1998 although earlier application is permitted. Financial statements for earlier years must be restated to conform to the new standard.

The new standard requires reporting firms to assemble all direct-to-equity adjustments in one place, enabling financial statement users to monitor changes in them, and better assess their significance for future income and cash flows.

_Illustration: Dow Chemical_

As DuPont did not report any elements of other comprehensive income over the 1992-1994 period, we use Dow to illustrate the new standard. First, we estimate other comprehensive income (in $millions):

<table>
<thead>
<tr>
<th>Change in</th>
<th>1992</th>
<th>1993</th>
<th>1994</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimum pension obligation</td>
<td>3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unrealized gains (losses)</td>
<td></td>
<td>107</td>
<td>(126)</td>
</tr>
<tr>
<td>Cumulative translation adjustment</td>
<td>(301)</td>
<td>(197)</td>
<td>(26 )</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>(298)</td>
<td>(90 )</td>
<td>(152)</td>
</tr>
<tr>
<td>Net income for common*</td>
<td>269</td>
<td>637</td>
<td>931</td>
</tr>
<tr>
<td>Comprehensive income*</td>
<td>29</td>
<td>547</td>
<td>779</td>
</tr>
</tbody>
</table>

* Before cumulative effect of accounting change in 1992

The components of other comprehensive income are obtained from the statements of stockholders’ equity from AUFS, page 1151.

As can be seen, both net income and comprehensive income rose sharply over the 1992 to 1994 period. Unusually, other comprehensive income is negative for all three years, and comprehensive income is below net income. For most firms, comprehensive income is more volatile, exceeding net income in some years but falling below net income in other years.
Our estimate is incomplete as Dow does not report reclassification adjustments, and they cannot be calculated from the available data.

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