

# FASB and IASB Accounting Treatment Comparison

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To: Management and the Finance Committee

From: Accounting Adviser

Subject: Comparison of FASB and IASB Accounting Treatments for Selected Transactions

## Introduction

This memorandum evaluates the accounting treatment of prepaid insurance, research and development, advertising, employee injury claims, sale-and-leaseback arrangements, voluntary redundancies, customer advances, and litigation involving faulty software under U.S. GAAP and IFRS Accounting Standards. The two frameworks share important principles but do not always produce identical timing, measurement, terminology, or presentation. The Financial Accounting Standards Board organizes U.S. GAAP through the Accounting Standards Codification, while the International Accounting Standards Board issues IFRS standards such as IAS 37, IAS 38, IFRS 15, and IFRS 16. A reliable conclusion therefore begins by identifying the reporting framework, the contractual facts, the reporting date, materiality, and the evidence supporting management's estimates. Conservatism does not justify recording every possible loss, and legal form does not automatically determine economic substance. The journal entries below are illustrative rather than mechanical because actual account names, measurement, classification, and disclosure depend on the company's contracts, estimates, useful lives, probabilities, and whether a transaction satisfies the specific recognition criteria in the governing standard.

## Prepayments, Research, Development, and Advertising

Insurance paid for coverage extending into future periods is initially recognized as a prepaid asset under both frameworks because the entity has not yet consumed the entire service. As time passes, the amount applicable to the expired coverage period becomes insurance expense; a multi-year policy may require current and noncurrent classification. Research expenditure is generally expensed as incurred under both U.S. GAAP and IAS 38 because the entity cannot yet demonstrate an identifiable intangible asset capable of producing probable future economic benefits. Development

creates the most important difference. IAS 38 requires capitalization after all specified criteria are demonstrated, including technical feasibility, intention and ability to complete the asset, probable future benefits, adequate resources, and reliable measurement of cost. U.S. GAAP generally expenses research and development, subject to specialized guidance for areas such as software. Ordinary advertising is usually expensed when the goods or services are received or first used, while advance payments remain assets until the advertising service occurs. These distinctions affect both current profit and reported assets.

Illustrative entries should follow the economic event rather than an informal label. When an annual insurance premium is paid, the entity debits prepaid insurance and credits cash; each period it debits insurance expense and credits the prepaid asset as coverage expires. Research costs are normally debited to research expense with credits to cash, payroll, materials, or payables. Under IFRS, development expenditure that has passed the IAS 38 recognition threshold is debited to a development intangible asset and later amortized when available for use, whereas qualifying criteria not yet met require immediate expense and previously expensed amounts cannot simply be reinstated. An advertising payment made before the campaign runs is debited to prepaid advertising and later reclassified to expense when the service is delivered. Materiality can simplify accounting for genuinely insignificant items, but a company should use a consistent policy rather than manipulating timing. The practical lesson is that expected future benefit alone does not create an asset; the applicable definition and recognition criteria must be demonstrably satisfied.

## Employee Injury Claims, Litigation, and Contingencies

An employee injury claim or faulty-software lawsuit is not accrued merely because a claim exists, nor should management create a vague “contingent account” to build a cushion against future accidents. Under IAS 37, a provision is recognized when a past event creates a present legal or constructive obligation, an outflow of resources is probable, and a reliable estimate can be made. Under U.S. GAAP, a loss contingency is accrued when it is probable that a liability has been incurred and the amount can be reasonably estimated; probability terminology and measurement of ranges differ from IFRS. If recognition criteria are met, the illustrative entry debits injury or legal expense and credits a provision or accrued liability. If the loss is only possible or reasonably possible, disclosure rather than recognition may be appropriate, while remote risks generally require neither, subject to specific exceptions. Legal counsel’s assessment is important evidence, but management retains responsibility for the accounting conclusion. Going concern becomes relevant only if the claim contributes to material uncertainty about the entity’s ability to continue operating.

Measurement should reflect the best estimate required by the reporting framework rather than automatically using the claimant’s stated amount. Under IFRS, expected-value techniques can be appropriate for a large population of similar obligations, while a single obligation may emphasize the

most likely outcome adjusted for other possible results. Under U.S. GAAP, when a loss falls within a range and no amount is a better estimate than another, the minimum amount in the range is generally accrued with additional exposure disclosed as required. The accounting file should document the incident, claim status, insurance recovery, legal advice, comparable settlements, assumptions, and management approval. A settlement occurring after year-end can be an adjusting event if it provides evidence about a condition that existed at the reporting date; a new event arising afterward may be non-adjusting but still require material disclosure. Neutral reporting is important in both directions: deliberately understating a probable obligation misleads users, but deliberately overstating liabilities in the name of prudence also distorts performance and financial position.

## Sale-and-Leaseback and Subsequent Property Accounting

A transfer of a building followed by a leaseback cannot be recorded automatically as a simple sale followed by ordinary rent. Under IFRS 16 and ASC Topic 842, the first question is whether control of the asset has genuinely transferred under the relevant revenue guidance. Legal title alone is insufficient if contractual rights, repurchase provisions, or other terms prevent the buyer-lessor from obtaining control. If the transfer fails the sale test, the seller-lessee generally keeps the property on its books and records the cash proceeds as a financing liability, with later payments allocated according to the financing arrangement. If a sale qualifies, the seller-lessee records the sale and lease consequences required by its framework, including a right-of-use asset and lease liability. IFRS recognizes only the gain or loss associated with rights transferred to the buyer-lessor, and off-market terms can represent financing or prepayment. A later repurchase must be analyzed in light of whether a repurchase option existed from the beginning because that option can affect the original sale conclusion.

## Redundancies, Subsequent Events, and Customer Advances

Voluntary redundancies require evidence that an obligation has become sufficiently committed under the applicable employee-benefit and restructuring guidance. A board discussion or preliminary intention does not automatically create a liability. Timing depends on facts such as whether a detailed plan exists, whether employees have accepted a voluntary offer, whether the entity can realistically withdraw it, and whether the obligating event occurred before or after the reporting date. Those facts also determine whether an event after year-end adjusts the financial statements or is instead disclosed as a material non-adjusting event. Customer advances for software follow a different principle. Under IFRS 15 and ASC 606, cash received before the company satisfies its performance obligations is generally a contract liability rather than revenue. The entry at receipt is debit cash and credit contract liability; revenue is recognized as the promised license, hosting, implementation,

updates, support, training, or other distinct obligations transfer according to the contract. Refund rights, cancellation provisions, financing components, commissions, and foreign-currency terms may change measurement or classification and therefore require contract-level review.

## Framework Differences and Documentation

The selected transactions show why a company reporting under both frameworks cannot rely on one universal set of entries. Prepaid insurance and customer advances often produce similar basic outcomes, and research and ordinary advertising are commonly expensed, but qualifying development costs create a major IFRS-U.S. GAAP difference. Provisions and loss contingencies differ in recognition thresholds and measurement of uncertain ranges, while lease presentation and sale-and-leaseback accounting require framework-specific application even though both systems place most leases on the balance sheet. These timing differences can alter profit, assets, liabilities, ratios, debt covenants, tax calculations, and management performance measures. Every material conclusion should therefore identify the transaction, governing standard, relevant facts, alternatives considered, judgments, calculations, journal entry, disclosure, and approval. Legal contracts should be read directly instead of summarized informally, and estimates should be updated when better evidence becomes available. High-quality accounting is not the most conservative number or the most optimistic number; it is the treatment that best satisfies the definitions, recognition criteria, measurement requirements, and faithful-representation principles of the applicable framework.

## Conclusion

FASB and IASB requirements converge on many basic ideas but differ enough that management must analyze each transaction under the correct framework. Prepaid insurance remains an asset until coverage is consumed. Research is generally expensed, while IFRS capitalizes qualifying development expenditure after IAS 38 criteria are satisfied and U.S. GAAP usually expenses research and development except under specialized guidance. Advertising is normally expensed when received or first used, with advance payments deferred. Injury claims and faulty-software litigation depend on present obligation, probability, and reliable measurement rather than the mere existence of a claim. Sale-and-leaseback accounting requires a genuine transfer of control and recognition of continuing lease rights and obligations. Redundancy liabilities depend on when commitment becomes unavoidable, and customer advances remain contract liabilities until promised performance occurs. The safest reporting process is therefore evidence-based and transaction-specific: apply current authoritative standards, obtain legal and valuation support when necessary, document judgments, assess materiality, and update estimates so the financial statements represent economic substance rather than managerial preference.

## References

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