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FASB Continues Deliberations on Project to Improve and Simplify Accounting for Stock Compensation under FASB ASC Topic 718

Directs Staff to Prepare an Exposure Draft for Public Comment

On February 4, 2015 the Financial Accounting Standards Board (FASB) continued deliberations on its narrow-scope fast-track project to improve and simplify accounting for stock compensation under FASB Accounting Standards Codification (ASC) Topic 718. The topics for improvement and simplification were identified based on recently completed outreach efforts by the FASB staff as well as the Financial Accounting Foundation's (FAF) post-implementation review of the overall effectiveness of ASC Topic 718.[(1)]

The agenda for the February 4 meeting was dominated by the deliberation of transition and disclosure requirements for the proposed changes, which are summarized below. The FASB directed its staff to prepare an Exposure Draft of an Accounting Standards Update (ASU), which is expected to be issued during the second quarter of 2015 followed by a 60-day public comment period. The FASB decided to hold off on determining an effective date for the ASU until feedback is received from the comment period. However, a tentative date suggested by the FASB's staff was for fiscal years beginning after December 15, 2016, with a 1-year deferral for nonpublic companies.

Topic	Tentative Decision	Tentative Transition
1. Minimum Statutory Withholding Requirements	Increase the permissible stock-for-tax withholding limitation for equity awards from "required minimum statutory" to "maximum statutory" tax rates	Modified retrospective application with a cumulative-effect adjustment applied to outstanding liability awards at the date of adoption. In effect, the adjustment would reverse previous liability award accounting (due to withholding above the required minimum statutory tax rate) and establish grant date fair value equity award accounting. Prior periods are not adjusted

(1) Refer to our alert letter dated November 7, 2014 on our website at http://www.fwcook.com/alert_letters/11-7-14_FASB_Commences_Project_to_Improve_and_Simplify_Accounting_for_Stock_Compensation_under_FASB_ASC_Topic_718.pdf

2. Presentation of Employee Taxes Paid on the Statement of Cash Flows	Report all stock-for-tax withholding transactions as a financing activity on the statement of cash flows, because the substance of the transaction is a repurchase of shares from employees	Retrospective application with all presented prior periods restated
3a. Accounting for Income Taxes Upon Settlement of Award	Require all excess tax benefits and deficiencies to be recognized on the income statement, rather than as credits and debits to additional paid-in capital on the balance sheet	Prospective application to all excess tax benefits and tax deficiencies occurring after the date of adoption
3b. Accounting for Income Taxes Upon Settlement of Award	Eliminate the requirement to delay recognition of an excess tax benefit until the tax benefit is realized	Modified retrospective application with a cumulative-effect adjustment. Prior periods are not adjusted
4. Recognition of Award Forfeitures	Allow companies to make an entity-level accounting policy election for awards with service vesting conditions to either estimate forfeitures and true-up, or to recognize forfeitures as they occur. This election would not apply to awards with performance vesting conditions	Modified retrospective application with a cumulative-effect adjustment. Prior periods are not adjusted
5. Presentation of Excess Tax Benefits on the Statement of Cash Flows	Eliminate the presentation of excess tax benefits on the statement of cash flows	Retrospective application with all presented prior periods restated
6. Classification of Awards with Repurchase Features	Clarify the determination of whether an award with put and call rights that are contingent on an event is an equity or liability award based on the probability of the event occurring, regardless of whether the event is within the employee's control	Modified retrospective application with a cumulative-effect adjustment applied to outstanding liability awards at the date of adoption. Prior periods are not adjusted

7. Expected Term of Stock Option Award for Nonpublic Companies	Allow companies to elect an alternative to estimating the expected term of a stock option. For awards with only a service-vesting condition and awards with a performance-vesting condition that is probable of occurring, calculate the expected term as the midpoint between the vesting date and the maximum contractual term. For awards with a performance-vesting condition that is not probable of occurring, use the maximum contractual term	Prospective application to all awards measured at fair value after the date of adoption
8. Using Intrinsic Value Rather Than Fair Value for Liability Awards for Nonpublic Companies	Provide a one-time election for a finite period of time to switch from measuring liability awards at fair value to intrinsic value	Modified retrospective application with a cumulative-effect adjustment applied to outstanding liability awards at the date of adoption. Prior periods are not adjusted

For companies that elect to recognize forfeitures as they occur, FASB tentatively decided to modify language in Topic 718 that would require footnote disclosure about "unvested awards" rather than awards that are "expected to vest." In addition, the FASB tentatively decided to codify previous guidance that requires an award granted for past or future employee services to remain subject to the measurement and recognition provisions of Topic 718 for the entire existence of the award, unless the award is subsequently modified when the holder is no longer an employee.

The proposed amendments dealing with stock-for-tax withholding, award forfeitures, repurchase features, and nonpublic company simplifications are likely to be favorably received by companies. The proposal to run all income tax effects through the income statement could be controversial and draw adverse reaction during the comment period, however, due to the potential increase in the variability of reported income tax expense from period to period.

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General questions about this summary can be addressed to Thomas M. Haines in our Chicago office at 312-332-0910 or by email at tmhaines@fwcook.com. Specific questions should be referred to the company's professional accountants. Copies of this summary and other published materials are available on our website at www.fwcook.com.