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EITF Provides Guidance on Accounting for Stock Compensation When a Performance Target Can Be Achieved After the Service Vesting Period

The Emerging Issues Task Force (EITF) on September 13, 2013 reached a tentative consensus on how companies should account for stock compensation in which a performance-vesting condition may be satisfied after completion of a service-vesting condition. The issue, referred to as EITF Issue No. 13-D, relates to equity awards that include a performance target that must be met to earn the awards, and the performance target can be met (and the awards earned) after the service-vesting period (if any) is satisfied. An example would be a stock option or restricted stock award with a 3-year service-vesting condition and the requirement that a specified performance target must be attained with the next 10 years for the awards to be earned, regardless of whether the grant recipients are still employed at that time. Examples of such performance targets could include an initial public offering (IPO), regulatory approval, or a financial target. The EITF decided to take up the issue as there is apparent diversity in accounting treatment among companies.

> The EITF tentatively decided that equity awards with a performance target that may be attained after completion of an underlying service-vesting period (if any) should be accounted for as a performance condition that affects the vesting of the award. Thus, compensation cost is recognized over the vesting period when attainment of the performance target becomes "probable," which could be subsequent to the service vesting period when the award recipient is no longer employed or never if the performance target is not attained. This represents a favorable conclusion as the alternatives considered but rejected by the EITF included treating the performance target as a non-vesting condition that affects the grant date fair value of the award similar in concept to a market condition, or as a liability award with variable accounting until the performance target is attained or forfeited.

The EITF further decided that no additional disclosures are required and the new guidance should be applied prospectively to new awards that are granted or modified on or after the effective date of a final consensus, with earlier application permitted. The EITF's tentative conclusion must be issued for public comment and ratified by Financial Accounting Standards Board (FASB) prior to becoming a final consensus.

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General questions about this letter 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 letter and other published materials are available on our website at www.fwcook.com.