

October 14, 2016

FASB TO ISSUE AN ACCOUNTING STANDARDS UPDATE ON THE SCOPE OF MODIFICATION ACCOUNTING IN TOPIC 718

The Financial Accounting Standards Board (FASB) on October 5, 2016 directed its staff to draft a proposed Accounting Standards Update (ASU) for vote by written ballot that would narrow the scope of modification accounting in FASB Accounting Standards Codification (ASC) Topic 718 (Topic 718). The proposed change would be beneficial for companies and compensation professionals because it would permit some changes to outstanding share-based payment awards to escape the complexities and potential incremental costs of accounting for modifications under Topic 718.

Topic 718 broadly defines a modification as “...a change to *any* of the terms or conditions of a share-based payment award...” The proposed ASU would narrow this definition to exclude from its scope changes to outstanding share-based payment awards that do not affect the total current fair value, vesting requirements, or equity/liability classification of the awards. Nonpublic companies would be able to substitute calculated value or intrinsic value for fair value in the preceding sentence if such an alternative measurement method is used. The revised definition of modification would be applied prospectively to changes to outstanding share-based payment awards beginning in the period of adoption of the final ASU. The proposed ASU will be subject to a comment period of at least 30 days before a final ASU is issued.

The FASB decided to add this project to its agenda on August 31, 2016 after receiving technical inquiries from companies as to whether a change to outstanding share-based payment awards to increase the maximum permissible stock-for-tax withholding provision from (1) the minimum required tax withholding rate to (2) the maximum marginal tax withholding rate constituted a modification. A number of companies are considering making this change after the release in March 2016 of ASU 2016-09, *Improvement to Employee Share-Based Payment Accounting*.¹ The FASB staff’s response to this inquiry was that an amendment to outstanding share-

¹ Refer to our most recent alert letter on this topic dated April 6, 2016 on our website at http://www.fwcook.com/content/documents/publications/04-06-16_Improvements_to_Employee_Share-Based_Payment_Accounting-FASB_ASU.pdf Additional alert letters on this topic are dated December 21, 2015, June 15, 2015, February 20, 2015, and November 7, 2014, and can be found on our website.

based payment awards or plan documents to increase the maximum permissible tax withholding rate does not constitute a modification requiring modification accounting provided the awards or plan documents already included a net settlement feature. However, the FASB staff cautioned that their view only relates to amendments as a result of ASU 2016-09 and should not be applied by analogy to other circumstances. Because of this narrow application and the perceived overly broad definition of modification in Topic 718, the FASB decided to add this project to their agenda.

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. A complete summary of Topic 718 can be found on our website at [http://www.fwcook.com/content/documents/publications/04-06-16_\(ORIGINALLY_4-29-05\)_-_Accounting_for_Stock_Compensation_Under_FASB_ASC_Topic_718.pdf](http://www.fwcook.com/content/documents/publications/04-06-16_(ORIGINALLY_4-29-05)_-_Accounting_for_Stock_Compensation_Under_FASB_ASC_Topic_718.pdf)