

Appendix D

AMENDMENTS TO EXISTING PRONOUNCEMENTS

D1. This Statement supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and the following related interpretations of Opinion 25:

- a. AICPA Accounting Interpretation 1, “Stock Plans Established by a Principal Stockholder”
- b. FASB Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*
- c. FASB Interpretation No. 38, *Determining the Measurement Date for Stock Option, Purchase, and Award Plans Involving Junior Stock*
- d. FASB Interpretation No. 44, *Accounting for Certain Transactions involving Stock Compensation*.

D2. This Statement supersedes FASB Statement No. 148, *Accounting for Stock-Based Compensation—Transition and Disclosure*.

D3. All references to FASB Statement No. 123, *Accounting for Stock-Based Compensation*, are replaced by *FASB Statement No. 123, Share-Based Payment*.

D4. ARB No. 43, Chapter 13B, “Compensation Involved in Stock Option and Stock Purchase Plans,” is amended as follows:

- a. Paragraph 2, as amended by Statement 123:

For convenience, this section will discuss primarily the problems of compensation raised by stock option plans. However, the committee feels that substantially the same problems may be encountered in connection with stock purchase plans made available to employees, and the discussion below is applicable to such plans also. FASB Statement No. 123, *Accounting for Stock-Based Compensation—Share-Based Payment*, ~~specifies~~ establishes a fair-value-based method of accounting for ~~stock share-based compensation plans payment arrangements~~ and ~~encourages~~ requires public entities to ~~adopt~~ apply that method in accounting for all share-based payment transactions with employees (except for transactions involving employee stock ownership plans and transactions in which it is not reasonably possible to estimate fair value [paragraphs 21 and 22 of Statement 123]). That Statement also establishes the fair-value-based method of accounting as preferable for nonpublic entities but permits those entities to account for their share options and similar instruments using Statement 123’s intrinsic value method. ~~arrangements under which employees receive shares of stock or other equity instruments of the employer or the employer incurs liabilities to employees in amounts based on the price of the employer’s stock. However, Statement 123 permits an employer in determining its net income to continue to apply the accounting provisions of this section and Opinion 25 to all its stock-based employee compensation arrangements. Entities that continue to~~

~~apply this section and Opinion 25 shall comply with the disclosure requirements of Statement 123.~~

D5. APB Opinion No. 29, *Accounting for Nonmonetary Transactions*, is amended as follows:

a. Footnote 4, as amended by Statement 123:

~~FASB Statement No. 123, *Accounting for Stock Based Compensation—Share-Based Payment*, applies to all transactions in which (a) one or more suppliers of goods or services receive awards of equity shares, share options, or other equity instruments or (b) the entity incurs liabilities to suppliers (1) in amounts based, at least in part, on the price of the entity’s shares or other equity instruments or (2) that require or may require settlement by issuance of the entity’s shares or other equity instruments—*an entity acquires goods or services by issuing equity instruments or by incurring liabilities to the supplier in amounts based on the price of the entity’s common stock or other equity instruments.*~~

D6. FASB Statement No. 109, *Accounting for Income Taxes*, is amended as follows:

a. Paragraph 36(e), as amended by Statement 123:

~~Expenses for employee stock options recognized differently for financial reporting and tax purposes (refer to paragraphs 41–44 of FASB Statement No. 123, *Accounting for Stock Based Compensation—Share-Based Payment* and paragraph 17 of APB Opinion No. 25, *Accounting for Stock Issued to Employees*).~~

D7. FASB Statement No. 128, *Earnings per Share*, is amended as follows:

a. Paragraph 20 and the heading preceding it:

~~***Stock-based compensation arrangements***~~ **Share-based payment arrangements**

~~Fixed awards and nonvested stock~~ Awards of share options and nonvested shares (as defined in FASB Statement No. 123, *Accounting for Stock Based Compensation—Share-Based Payment*) to be issued to an employee¹² under a ~~stock~~ share-based compensation arrangement are considered options for purposes of computing diluted EPS. Such ~~stock~~ share-based awards shall be considered to be outstanding as of the grant date for purposes of computing diluted EPS even though their exercise may be contingent upon vesting. Those ~~stock~~ share-based awards are included in the diluted EPS computation even if the employee may not receive (or be able to sell) the stock until some future date. Accordingly, all shares to be issued shall be included in computing diluted EPS if the effect is dilutive. The dilutive effect of ~~stock~~ share-based compensation arrangements shall be computed using the treasury stock method. If the ~~stock~~ share-based awards were granted during the period, the shares

issuable must be weighted to reflect the portion of the period during which the awards were outstanding.

b. Paragraph 21:

In applying the treasury stock method described in paragraph 17, the assumed proceeds shall be the sum of (a) the amount, if any, the employee must pay upon exercise, (b) the amount of compensation cost attributed to future services and not yet recognized,¹³ and (c) the amount of excess tax benefits (both deferred and current), if any, that would be credited to additional paid-in capital assuming exercise of the options. Assumed proceeds shall not include compensation ascribed to past services. The excess tax benefit is the amount resulting from a tax deduction for compensation in excess of compensation expense recognized for financial reporting purposes. That deduction arises from an increase in the market price of the stock under option between the measurement date and the date at which the compensation deduction for income tax purposes is determinable. The amount of the tax benefit shall be determined by a “with-and-without” computation. ~~Paragraph 17 of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, states that in some instances the tax deduction for compensation may be less than the compensation expense recognized for financial reporting purposes. If the resulting difference in income tax will be deducted from capital in accordance with that paragraph, such taxes to be deducted from capital shall be treated as a reduction of assumed proceeds.~~

c. Footnote 13:

This provision applies only to those ~~stock~~-share-based awards for which compensation cost will be recognized in the financial statements in accordance with ~~APB Opinion No. 25, *Accounting for Stock Issued to Employees*, or Statement 123.~~

d. Paragraph 23:

Awards with a market condition, a Pperformance condition, or any combination thereof awards (as defined in Statement 123) shall be included in diluted EPS pursuant to the contingent share provisions in paragraphs 30–35 of this Statement. ~~As discussed in paragraph 26 of Statement 123, targeted stock price options are not considered to be a performance award. However, because options with a target stock price have a market price contingency, the contingent share provisions of this Statement shall be applied in determining whether those options are included in the computation of diluted EPS.~~

e. Illustration 8—“Application of the Treasury Stock Method for Stock Appreciation Rights and Other Variable Stock Option Award Plans,” paragraphs 157–159, is deleted because the accounting illustrated is based on Opinion 25 and its related interpretations, which are superseded by this Statement.

D8. FASB Statement No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*, is amended as follows:

a. Paragraph 17:

This Statement does not apply to obligations under ~~stock~~share-based compensation arrangements if those obligations are accounted for under ~~APB Opinion No. 25, Accounting for Stock Issued to Employees~~, FASB Statement No. 123, ~~Accounting for Stock-Based Compensation—Share-Based Payment~~, AICPA Statement of Position (SOP) 93-6, *Employers' Accounting for Employee Stock Ownership Plans*, or related guidance. However, this Statement does apply to a freestanding financial instrument that was issued under a ~~stock~~share-based compensation arrangement but is no longer subject to ~~Opinion 25~~, Statement 123, SOP 93-6, or related guidance. For example, this Statement applies to mandatorily redeemable shares issued upon an employee's exercise of an employee ~~stock~~ share option.

b. Paragraph D1:

Nonpublic entity

Any entity other than one (a) whose equity securities trade in a public market either on a stock exchange (domestic or foreign) or in the over-the-counter market, including securities quoted only locally or regionally, (b) that makes a filing with a regulatory agency in preparation for the sale of any class of equity securities in a public market, or (c) that is controlled by an entity covered by (a) or (b). [Statement 123, paragraph ~~395-E1~~.]

D9. FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, is amended as follows:

a. Footnote 18:

The term *public entity* is defined in paragraph ~~395-E1~~ of FASB Statement No. 123, ~~Accounting for Stock-Based Compensation—Share-Based Payment~~.

b. Footnote 23:

The term *nonpublic entity* is defined in paragraph ~~395-E1~~ of Statement 123.

D10. FASB Technical Bulletin No. 97-1, *Accounting under Statement 123 for Certain Employee Stock Purchase Plans with a Look-Back Option*, is amended as follows:

a. The Reference:

FASB Statement No. 123, ~~Accounting for Stock-Based Compensation—Share-Based Payment~~, paragraphs 23 and ~~24~~, ~~232-242-B168-B176-348-356~~.

b. Paragraph 1:

The accounting guidance in this Technical Bulletin addresses the accounting under Statement 123 for certain employee stock purchase plans (ESPPs) with a look-back option. An example of a *look-back option* is a provision in an ESPP that establishes the purchase price as an amount based on the lesser of the stock's market price at the grant date or its market price at the exercise (or purchase) date. ~~This Technical Bulletin does not address the accounting for those plans under APB Opinion No. 25, *Accounting for Stock Issued to Employees*. It also~~ This Technical Bulletin does not address the effect of those plans on earnings per share calculations.¹

c. Paragraph 2:

Paragraph 23 of Statement 123 establishes the criteria under which an ESPP should be evaluated to determine whether it qualifies for noncompensatory treatment. If a plan does not meet *all* of those criteria, the fair value method of accounting must be used. ~~Paragraph 24 notes that a plan provision such as a look back option is one feature that causes an ESPP to be considered compensatory. Paragraph 239 explains in part the Board's rationale:~~

~~The Board considered respondents' requests that broad-based plans with look back options be considered noncompensatory and noted that a look back option can have substantial value because it enables the employee to purchase the stock for an amount that could be significantly less than the market price at date of purchase. A look back option is not an essential element of a broad-based plan aimed at promoting broad employee stock ownership; a purchase discount also provides inducement for participation. The Board concluded that broad-based plans that contain look back options cannot be treated as noncompensatory.~~

d. All references to *Illustration 9* of Statement 123 in paragraphs 3, 5, 6, 9, 10, 12–15, and 21 and footnote 7 are replaced by *Illustration 18*.

e. Footnote 2:

The examples in Illustration 9–18 of Statement 123 and this Technical Bulletin illustrate the use of the Black-Scholes-Merton option pricing ~~model formula (a closed-form model)~~. It also may be acceptable to use a binomial option pricing lattice model to value an award under an ESPP with a look-back option.

f. Paragraph 7:

Although many ESPPs with a look-back option initially limit the maximum number of shares of stock that the employee is permitted to purchase under the plan (Type A plans), other ESPPs (Type B plans) do not fix the number of

shares that the employee is permitted to purchase if the exercise date stock price is lower than the grant date stock price. In effect, an ESPP that does not fix the number of shares that may be purchased has guaranteed that the employee can always receive the value associated with *at least* 15 percent of the stock price at the grant date (the employee can receive much more than 15 percent of the grant date value of the stock if the stock appreciates during the look-back period). That provision provides the employee with the equivalent of a put option on 15 percent of the shares with an exercise price equal to the stock price at the grant date. In contrast, an employee who participates in a Type A plan is only guaranteed 15 percent of *the lower of* the stock price as of the grant date or the exercise date, which is the equivalent of a call option on 85 percent of the shares (as described more fully in paragraph ~~352~~B172 of Statement 123). A participant in a Type B plan receives the equivalent of both a put option and a call option.

- g. The following footnote is added at the end of the first sentence in paragraph 8:

*The assumptions used for the numerical calculations in this Technical Bulletin are not intended to be the same as those in Illustration 18 of Statement 123. Rather, they are independent and designed to illustrate how the component measurement approach in Illustration 18 would be modified to reflect various features of employee stock purchase plans.

- h. Paragraph 17:

Likewise, although not a change to the terms of the ESPP, an election by an employee to increase withholding amounts (or percentages) for future services (Type F through Type H plans) is a modification of the terms of the award to that employee, which, in substance, is similar to an exchange of the original award for a new award with different terms. Accordingly, the fair value of an award under an ESPP with variable withholdings should be determined at the grant date (using the Type A, Type B, or Type C measurement approach, as applicable) based on the estimated amounts (or percentages) that a participating employee initially elects to withhold under the terms of the plan. Subsequent to the grant date (~~except as noted in paragraph 23~~), any increases in withholding amounts (or percentages) for future services should be accounted for as a plan modification in accordance with the guidance in paragraph 35 of Statement 123.

- i. Paragraph 18:

Paragraph 35 of Statement 123 explains the approach that should be used to account for a modification of the terms of an award as follows:

A modification of the terms or conditions of an award that ~~makes it more valuable~~ increases its fair value shall be treated as an exchange of the original award for a new award. In substance, the entity repurchases the original instrument by issuing a new

instrument of greater fair value, incurring additional compensation cost for that incremental value. ~~The incremental value shall be measured by the difference between (a) the fair value of the modified option determined in accordance with the provisions of this Statement and (b) the value of the old option immediately before its terms are modified, determined based on the shorter of (1) its remaining expected life or (2) the expected life of the modified option.~~ The effects of a modification shall be measured as follows:

- a. Incremental compensation shall be measured as the excess, if any, of the fair value of the modified award determined in accordance with the provisions of this Statement over the fair value of the original award immediately before its terms are modified. The effect of the modification on the number of instruments expected to vest also shall be reflected. The estimate at the modification date of the portion of the award expected to vest shall be subsequently adjusted, if necessary, in accordance with paragraph 26 of this Statement.
 - b. Total recognized compensation cost for an award rarely will be less than the fair value of the award at the grant date unless at the date of the modification the performance or service conditions of the original award are not expected to be satisfied. Thus, the total compensation cost measured at the date of a modification shall be (1) the portion of the grant-date fair value of the original award for which the requisite service is expected to be rendered (or has already been rendered) at that date plus (2) the incremental cost resulting from the modification. Compensation cost shall be subsequently adjusted, if necessary, in accordance with paragraph 26 of this Statement.
 - c. A change in compensation cost from the modification of an award measured at intrinsic value in accordance with either paragraph 20A or paragraph 22 of this Statement shall be measured by comparing the intrinsic value of the modified award, if any, with the intrinsic value of the original award, if any, immediately before the modification.
- j. Paragraph 20:

Any decreases in the withholding amounts (or percentages) should be disregarded for purposes of recognizing compensation cost unless the employee services that were valued at the grant date will no longer be provided to the employer due to a termination. However, no compensation cost should be recognized for awards that an employee forfeits because of failure to satisfy a service requirement for vesting. The accounting for decreases in withholdings is consistent with the requirement in paragraph 26 of Statement 123 that the total amount of compensation cost that must be recognized for an award is based on the number of instruments ~~that vest rather than the number of instruments that are either granted or exercised~~ for which the requisite service is rendered (that is, for which the requisite service period is completed).

k. Paragraph 24:

In some circumstances, applying the measurement approaches described in this Technical Bulletin at the grant date may not be practicable for certain types of ESPPs. For example, an entity may not have access at a reasonable cost to the modeling capabilities needed to determine the fair value of plans with features in addition to or different from those described in this Technical Bulletin. If it is *not practicable* to reasonably estimate fair value at the grant date, the guidance in paragraph 22 of Statement 123 would apply.¹³ Paragraph 22 of Statement 123 states:

~~If it is not possible to reasonably estimate the fair value of an-a share option or other equity instrument at the grant date, the final measure of compensation cost shall be the fair intrinsic value of the instrument at the date it is settled-based on the stock price and other pertinent factors at the first date at which it is possible to reasonably estimate that value. Compensation cost for each period until settlement shall be based on the change (or pro rata change, depending on the percentage of the requisite service that has been rendered at the reporting date) in intrinsic value of the instrument for each reporting period, based on the current share price and other pertinent factors at the reporting date. The entity shall continue to use that accounting method for those awards even if it subsequently concludes that it is possible to reasonably estimate their fair value—for example, if the terms of the award are modified or a new valuation technique is developed. Generally, that is likely to be the date at which the number of shares to which an employee is entitled and the exercise price are determinable. Estimates of compensation cost for periods during which it is not possible to determine fair value shall be based on the current intrinsic value of the award, determined in accordance with the terms that would apply if the option or similar instrument had been currently exercised.~~