

October 31, 2002

Ms. Suzanne Q. Bielstein  
Director of Major Projects and Technical Activities  
Financial Accounting Standards Board  
401 Merritt 7  
Norwalk, Connecticut 06856-5116

**Letter of Comment No:** 15  
**File Reference:** 1101,001  
**Date Received:** 10/31/02

Re: Comments on Proposed Standard, *Accounting for Stock-Based Compensation – Transition and Disclosure, an amendment of FASB Statement No. 123* (File Reference No. 1101-001)

Dear Ms. Bielstein:

PricewaterhouseCoopers LLP appreciates the opportunity to comment on the proposed standard, *Accounting for Stock-Based Compensation – Transition and Disclosure, an amendment of FASB Statement No. 123* (the ED).

In light of the recent movement towards wider adoption of the fair value method of accounting for stock options, we agree with the Board's efforts to facilitate companies' adoption by providing multiple transition alternatives. We therefore support issuance of the proposed standard. While we acknowledge the concerns expressed by certain users of financial statements that this approach may not result in comparability – at least in the near term – among adopters, we also observe that we do not currently have comparability among companies, due to the decision of many to continue to apply the intrinsic value method of APB Opinion No. 25, *Accounting for Stock Issued to Employees*. We believe, however, that the proposed disclosures will prove useful, as they provide users with the data they require in order to make meaningful comparisons among companies.

#### Disclosures

While we agree that the additional disclosures proposed in the ED provide useful information, we do not agree with the Board's conclusion that the tabular disclosures should be embedded within a company's Significant Accounting Policies footnote. We do not believe such quantitative information is consistent with the disclosures envisioned by APB Opinion No. 22,

*Disclosure of Accounting Policies.* We suggest the Board require disclosure of this tabular data in a company's footnotes, but provide preparers with the flexibility to determine where that data should be included. It would seem to us that inclusion in a Stockholders' Equity or Stock Compensation Plans footnote would be a more appropriate location.

**Fiscal 2002 Adopters**

We believe that the Board should allow companies that have previously adopted FAS 123 in fiscal 2002 under the current prospective transition provisions, but have not yet issued annual financial statements, to amend the transition approach to follow either the modified prospective or retroactive approaches permitted under the ED.

**Implementation Issues**

We are aware of a significant number of implementation issues that exist in practice relative to the provisions of FAS 123. We believe it would be beneficial for the Board to address those issues through standard setting, FASB staff implementation guidance, or by referring them to the Emerging Issues Task Force. We would welcome the opportunity to assist in the identification and resolution of such issues.

**Other Matters**

We have a number of other comments that are largely editorial in nature and intended to enhance the clarity of the ED. Those comments are included in Appendix I.

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We appreciate the opportunity to express our views in this letter. If you have any questions regarding our comments, please feel free to contact Paul R. Kepple at (973) 236-5293 or Mark S. Neagle at (973) 236-7204.

Sincerely,

PricewaterhouseCoopers LLP

A. Proposed changes to description of the application of the modified prospective method:

We observe that there are inconsistencies within the document in the discussion of this transition provision. For example, in paragraph A10, that method is described as being applied to “the unvested portion of previously issued as well as new awards.” We observe that there may be awards that may be vested under FAS 123 for which there has not been a final measurement date. We therefore believe the language in paragraph 2.a.b. should be substituted for that currently in A10. We have a similar comment with respect to paragraphs A6.c., A12, A13, A14, B3, B4 and B7.

B. Proposed changes to paragraph 2 of the ED

We believe the language in paragraph 2 could be clarified by making the following revisions:

2. Statement 123 is amended as follows:

b. The following new paragraph 52A is inserted after paragraph 52:

An entity that elects the transition method in paragraph 52(b) or 52(c) may need to report an adjustment to additional paid-in capital as of the beginning of the first period for which stock-based employee compensation cost is accounted for in accordance with the fair value method. ~~For awards that are unvested or, in the case of certain variable awards, unexercised as of the beginning of that period,~~ That adjustment shall be determined as follows:

- a. The carrying amounts of unearned or deferred compensation (contra-equity accounts), stock-based compensation liabilities, and the related deferred tax balances recognized under Opinion 25, if any, shall be reversed.
  - b. The additional paid-in capital, stock-based compensation liabilities, and related deferred tax balances determined under this Statement shall be recognized.
- c. The difference between the amounts reversed in (a) and the amounts recognized in (b) shall be reported as an adjustment to additional paid-in capital as of the beginning of the period. No cumulative effect of a change in accounting principle shall be presented.
- c. The following sentence is added to the end of paragraph 44:

If an entity that continued to apply Opinion 25 subsequently adopts the fair value based method in this Statement, only the additional paid-in capital recognized from excess tax deductions for awards accounted for under the fair value method pursuant to the transition provisions of paragraph 52 is available to absorb any such write-offs.

**Amendments to Disclosure Provisions**

- d. Paragraph 45 of Statement 123 is replaced by the following:

Regardless of the method used to account for stock-based employee compensation arrangements, the financial statements of an entity shall include the disclosures specified in paragraphs 46-48. All entities shall disclose prominently, in the "Summary of Significant Accounting Policies" or its equivalent, the following information:

- a. The method used -- either the intrinsic value method or the fair value method -- to account for stock-based employee compensation in each period presented
- b. For an entity that adopts the fair value recognition provisions of this Statement, for all financial statements in which the period of adoption is presented, a description of the method of reporting the change in accounting principle
- c. If unvested awards of stock-based employee compensation were outstanding and accounted for under the intrinsic value method of Opinion 25 for any period for which an income statement is presented, a tabular presentation, for all periods, of the following information:

C. Proposed revisions to paragraph 4 of the ED

We observe that the introductory language in paragraph 3 differs from that used in paragraph 2.d.c. We believe that using similar language will avoid potential confusion. In addition, we are concerned that use of the phrase "any period presented [that] includes the effects of stock-based compensation under Opinion 25" might prove confusing because the majority of those awards may not result in an accounting consequence (i.e., those awards that were granted at-the-money and therefore had no intrinsic value).

**Amendment to Opinion 28**

3. The following is added to the list of disclosures in paragraph 30 of Opinion 28:

- j. ~~If any period presented includes the effects of stock-based compensation accounted for under the intrinsic method, the following information about stock-based employee compensation expense under the provisions of FASB Statement No. [14X], *Accounting for Stock-Based Compensation—Transition and Disclosure*, shall be disclosed prominently in tabular form: If awards of stock-based compensation were outstanding and accounted for under the intrinsic value method of Opinion No. 25 for any period for which an income statement is presented, a tabular presentation, for all periods, of the following information shall be prominently disclosed:~~

- (1) Net income and basic and diluted earnings per share as reported
- (2) The stock-based employee compensation cost, net of related tax effects, included in the determination of net income as reported
- (3) The stock-based employee compensation cost, net of related tax effects, that would have been included in the determination of net income if the fair value method had been applied to all awards\*
- (4) Pro forma net income as if the fair value method had been applied to all awards
- (5) Pro forma basic and diluted earnings per share as if the fair value method had been applied to all awards.

D. Proposed revision to paragraph a 13 of the ED

We believe the clarity of this paragraph could be improved by making the following revisions:

**Accumulated Opinion 25 Balances**

A13. The prospective recognition method for unvested awards (alternative (b) in paragraph 2(a) of this Statement) and the retroactive restatement method (alternative (c) in paragraph 2(a)) raise the issue of accounting for the accumulated deferred compensation, if any, and related deferred income tax balances that arose under the application of Opinion 25. The Board concluded that the carrying amounts of those items should be reversed and that any required beginning balances under Statement 123 relating to unvested awards should be recorded with the effect recognized in paid-in capital. The Opinion 25 balances and Statement 123 balances both ultimately increase paid-in capital for the value of the employee services received. However, because the two accounting models under which those balances arise are fundamentally different, the Board decided not to require reclassifications between retained earnings (either directly or through the income statement) and paid-in capital. The Board believed that to require such a reclassification because doing so would be tantamount to reporting the adoption of the fair value method as the cumulative effect of a change in accounting principle, that the Board concluded that permitting transition through a cumulative effect adjustment believes would not provide readers of financial statements with useful information.

E. Proposed revision to paragraph A8 of the ED

We observe that modifications or settlements of stock-based awards subsequent to December 15, 1994 would also be within the scope of the retroactive restatement provisions of the ED. We suggest the following clarification:

A8. *Retroactive restatement*, as used in this Statement, refers to the restatement of prior periods' reported net income to give effect to the fair value method of accounting for employee awards granted, modified or settled to employees in fiscal years beginning after December 15, 1994. Retroactive application to awards made in periods before that date involves the problems cited by the Board in originally rejecting retroactive application and would likely result in restated amounts different from those previously disclosed in financial statements.

We observe that a similar change should be made throughout Appendix B.

F. Proposed revisions to per share data in Appendix B:

Finally, we observe that in the earnings per share data included in Appendix B, the denominator of the diluted calculation appears to be the same for the "as reported" and "pro forma" disclosures. Because unearned compensation will almost always differ between the intrinsic value and fair value methods, for entities that choose not to retroactively restate, the effect of applying the treasury stock calculation described in paragraph 17 of FASB Statement No. 128, *Earnings per Share*, would result in a different number of potential common shares. This does not appear to be the case in those examples.