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SOUTHERN COMPANY

August 14, 2015

Ms. Susan M. Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Submitted via electronic mail to director@fasb.org

Re: File Reference: No. 2015-270, Proposed Accounting Standards Update, *Compensation – Stock Compensation (Topic 718)*

Dear Ms. Cosper:

We appreciate the opportunity to provide our views on the Proposed Accounting Standards Update, **Compensation – Stock Compensation (Topic 718), Improvements to Employee Share-Based Payment Accounting**. We respectfully ask the FASB to consider our comments and revise the proposed guidance accordingly.

Southern Company is a leading U.S. producer of electricity, and owns retail regulated electric utilities in four states, a growing competitive whole generation company, as well as fiber optics and wireless communications. Southern Company has 4.5 million customers and more than 46,000 megawatts of generating capacity.

Overall

We continue to support the efforts to simplify U.S. GAAP and appreciate the FASB considering such proposals. We support the FASB's proposed changes related to the policy election of forfeitures, the minimum statutory tax withholding requirements threshold to qualify for equity classification, and the cash flow classification of employee taxes paid. However, we do not agree with the proposed changes to reflect excess tax benefits in earnings or as an operating activity within the statement of cash flows. We believe this proposal represents a significant change in accounting principle and not just a simplification of U.S. GAAP.

Responses to Questions

Question 2: Should excess tax benefits and tax deficiencies be recognized in the income statement? If not, why, and are there other alternatives that are more appropriate? Should an entity delay recognition of an excess tax benefit until benefit is realized through a reduction to taxes payable? If yes, why?

We believe the proposed changes do not recognize the two distinct events that create the tax deductions. The first event is the rendering of services by an employee for the stock based compensation award. The second event is an equity transaction that relates solely to the change in intrinsic value of the award that is exercised or vests.

Our response to the current proposal is consistent with the FASB's original conclusion in **FASB Statement 123 (revised 2004) - *Share Based Payment*** where the Board rejected the option of recording excess tax benefits in the income statement.

> B209. The Board concluded that tax deductions in excess of recognized compensation costs that result from increases in intrinsic value after the grant date (that is, excess tax deductions) are due to changes in the price of an equity instrument. Therefore, the related tax effect (or excess tax benefit) should be an adjustment of paid-in capital. The result of that accounting is that the tax effects of an award of share-based employee compensation that qualifies as equity affect both the income statement and paid-in capital because the total tax deduction pertains to two separate transactions or events:
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> a. A transaction in which employees render services as consideration for an award of equity shares, equity share options, or other equity instruments. Use of those services in the entity's operations results in compensation cost, which is an income statement item.
> b. An equity transaction, such as the exercise of share options or the vesting of shares. Changes in the share price after the grant date affect the amount of that equity transaction.
>
> B213. The Board rejected recognizing both excess tax benefits and tax deficiencies in the income statement because that view is consistent with viewing the entire tax deduction as the result of a single transaction in which employees render service in exchange for compensation in the form of equity instruments. As noted in paragraph B209, the Board concluded that the tax deduction results from both a compensatory transaction and a separate transaction in which the employer issues equity instruments to employees (or the award is otherwise settled, such as by expiration of a share option).

We believe recognizing in earnings the tax effect of an item that was never recognized as expense in earnings is not appropriate. Again, we reference the FASB's language in **FASB Statement 123 (revised 2004) - *Share Based Payment*** below:

> B207. Consistent with the original provisions of Statement 123, the Board concluded that compensation cost recognized in the financial statements should be accounted for as a temporary difference under FASB Statement No. 109, *Accounting for Income Taxes.* Any deferred tax asset that is recognized for that temporary difference is not remeasured during the period that an award is outstanding for changes in the amount that would be deductible for tax purposes at subsequent balance sheet dates due to changes in the entity's share price but that are not recognized in measuring compensation cost.

Generally, when a temporary difference reverses and is reflected in earnings, the related tax expense is also reflected in earnings. Compensation expense related to share-based compensation does not, and should not, follow this pattern; because the difference between the compensation expense recognized for financial reporting purposes and the fair value of the stock award on the exercise date recognized for tax purposes is never recognized in book earnings. Recognizing the

tax expense without the corresponding compensation results in a mismatch that would create significant volatility in a company's earnings and require additional discussion in the reconciliation of the company's effective tax rate.
An additional consequence resulting from the proposed change in accounting principle is the impact on a company's budgeting and forecasting processes. The timing of a stock option exercise and the resulting recognition of tax expense is likely to be unpredictable and difficult, if not impossible, to forecast. The volatility that the proposed accounting creates could be significant and could result in additional complexities for a company to address in the management of its business.

Question 3: Should the effect on tax cash flows related to excess tax benefits be classified as an operating activity on the statement of cash flows? If not, what classification is more appropriate and why?

Consistent with our position that excess tax benefits on stock option exercises relate to an equity transaction, we agree with the current guidance in **Accounting Standards Codification 230 – *Statement of Cash Flows***, that these excess tax benefits should be classified as a cash inflow from financing activities. However, for simplicity and in recognition that the tax effects of other cash flows not considered operating are still classified within operating activities, we would not object to that classification here.

Conclusion

We appreciate the opportunity to provide our views on the proposed standards.

Sincerely,

Ann P. Daiss

Ann P. Daiss
Senior Vice President, Comptroller and
Chief Accounting Officer