June 20, 2018

FASB In Focus

ACCOUNTING STANDARDS UPDATE NO. 2018-07

Compensation—Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting

On June 20, 2018, the Financial Accounting Standards Board (FASB) issued an Accounting Standards Update (ASU) intended to reduce cost and complexity and to improve financial reporting for share-based payments issued to nonemployees (for example, service providers, external legal counsel, suppliers, etc.).

Why Is the FASB Issuing This ASU?

The Board is issuing this ASU as part of its Simplification Initiative. The objective of the Simplification Initiative is to maintain or improve the usefulness of the information provided to the users of financial statements while reducing cost and complexity in financial reporting.

The ASU expands the scope of Topic 718, Compensation—Stock Compensation, which currently only includes share-based payments issued to employees, to also include share-based payments issued to nonemployees for goods and services.

Consequently, the accounting for share-based payments to nonemployees and employees will be substantially aligned. The ASU supersedes Subtopic 505-50, Equity—Equity-Based Payments to Non-Employees.

The accounting for nonemployee share-based payment transactions was identified as an area for simplification through:

1. Outreach for the Simplification Initiative
2. Ongoing dialogue with the Private Company Council (PCC) about making improvements to the accounting for share-based payments, and
3. The August 2014 Post-Implementation Review Report on FASB Statement No. 123 (revised 2004), Share-Based Payment.

Stakeholders recommended that the FASB improve the accounting for nonemployee share-based payments to reduce cost and complexity to apply the guidance, while improving the financial reporting for these transactions.

How Will the Changes Improve Accounting for Nonemployee Share-Based Payments?

The existing guidance on nonemployee share-based payments is significantly different from current guidance for employee share-based payments. This ASU expands the scope of the employee share-based payments guidance to include share-based payments issued to nonemployees. By doing so, the FASB improves the accounting of nonemployee share-based payments issued to acquire goods and services used in its own operations.

A company should apply the requirements of Topic 718 to nonemployee awards except for specific guidance on inputs to an option pricing model and the attribution of cost (that is, the period of time over which share-based payment awards vest and the pattern of cost recognition over that period).

The amendments specify that Topic 718 applies to all share-based payment transactions in which a grantor acquires goods or services to be used or consumed in a grantor's own operations by issuing share-based payment awards.

The amendments also clarify that Topic 718 does not apply to share-based payments used to effectively provide:

1. Financing to the issuer, or
2. Awards granted in conjunction with selling goods or services to customers as part of a contract accounted for under Topic 606, Revenue from Contracts with Customers.

How Do the Amendments Improve Current Generally Accepted Accounting Principles (GAAP)?	
Current GAAP	**Summary of Amendments**
Overall Measurement Objective: Nonemployee share-based payment awards are measured at the fair value of the consideration received or the fair value of the equity instruments issued, whichever can be more reliably measured.	Consistent with the accounting for equity-classified awards issued to employees, equity-classified nonemployee awards within the scope of Topic 718 will be measured at grant-date fair value.
Measurement Date: The measurement date for equity-classified nonemployee share-based payment awards is the earlier of the date at which: ■ A commitment for performance by the counterparty is reached, and ■ The date at which the counterparty's performance is complete.	Equity-classified nonemployee share-based payment awards are measured at the grant date. The definition of the term *grant date* is amended to generally state the date at which *a grantor* and *a grantee* reach a mutual understanding of the key terms and conditions of a share-based payment award.
Awards with Performance Conditions: Nonemployee share-based payment awards with performance conditions are measured at the *lowest aggregate fair value.*	Consistent with the accounting for employee share-based payment awards, a company considers the probability of satisfying performance conditions when nonemployee share-based payment awards contain such conditions.
Classification Reassessment of Certain Equity-Classified Awards: Generally, the classification of equity-classified nonemployee share-based payment awards is subject to other GAAP (ex. Topic 815, Derivatives and Hedging) once the good has been delivered or the service has been rendered and any other conditions necessary to earn the right to benefit from the instruments have been satisfied. This often results in the need to reassess the classification of such awards.	Generally, the classification of equity-classified nonemployee share-based payment awards will continue to be subject to the requirements of Topic 718 unless modified after: ■ The good has been delivered and/or service has been rendered ■ Any other conditions necessary to earn the right to benefit from the instruments have been satisfied, and ■ The nonemployee is no longer providing goods or services. This eliminates the requirement to reassess classification of such awards upon vesting.

Who Will Be Affected by the New Guidance?

The amendments in this ASU affect all companies that enter into share-based payment transactions for acquiring goods or services from nonemployees.

When Will the ASU Be Effective?

The amendments in this ASU are effective for public companies for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. For all other companies, the amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early adoption is permitted, but no earlier than a company's adoption date of Topic 606.

What About Transition?

A company should only remeasure liability-classified awards that have not been settled by the date of adoption and equity-classified awards for which a measurement date has not been established through a cumulative-effect adjustment to retained earnings as of the beginning of the fiscal year of adoption.

Upon transition, the company is required to measure these nonemployee awards at fair value as of the adoption date. The company must not remeasure assets that are completed. For example, finished goods inventory or equipment that has begun amortization should not be remeasured upon transition.

Disclosures required at transition include the nature of and reason for the change in accounting principle and, if applicable, quantitative information about the cumulative effect of the change on retained earnings or other components of equity.

For more information about the project, please visit the FASB's website at www.fasb.org.

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