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August 31, 2015

Susan M. Cosper, CPA
Technical Director
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PO Box 5116
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Re: June 8, 2015 Exposure Draft of a Proposed Accounting Standards Update (ASU), *Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* [File Reference No. 2015-270]

Dear Ms. Cosper:

One of the objectives that the Council of the American Institute of Certified Public Accountants (AICPA) established for the PCPS Executive Committee is to speak on behalf of local and regional firms and represent those firms' interests on professional issues in keeping with the public interest, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective. These comments, however, do not necessarily reflect the positions of the AICPA.

TIC has reviewed the ED and is providing the following comments for your consideration.

GENERAL COMMENTS

TIC is supportive of the simplification measures proposed in the ED. Although private companies will derive some relief from the amendments, TIC believes other simplifications are needed that would offer practical expedients for the share-based compensation accounting issues that are of most concern to private companies. However, TIC has decided to submit its comments on the current ED now and postpone further comments on additional alternatives until a later date, as discussed under Question 1 below.

SPECIFIC COMMENTS

Question 1: Do you agree that the proposed amendments result in a reduction (or potential reduction) of cost and complexity while maintaining or improving the usefulness of information provided to users of financial statements? If not, why?

Yes. TIC welcomes simplifications and improvements to accounting for share-based payments, especially for nonpublic companies. Frequently, nonpublic companies struggle with the high cost and complexity of accounting for these types of transactions as they often involve experts and a significant amount of resources in determining recognition and measurement. The proposed amendments will help simplify the accounting in certain areas while maintaining user relevance.

However, TIC believes that the Board and the Private Company Council (PCC) should provide additional relief for private companies in accounting for share-based payment transactions, including the related disclosures. TIC has reviewed the official minutes of the May 5, 2015 PCC meeting, which included two proposed accounting alternatives for private company transactions involving share-based compensation. Although TIC has started discussing the PCC alternatives, the committee will need more time to develop its recommendations for additional relief for private companies. TIC will continue to review these alternatives in the coming month and will report to the Board at a later date.

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 the benefit is realized through a reduction to taxes payable? If yes, why? [Issue 1: pages 8-48, pars. 3-20, and BC4-BC8]

Yes. TIC understands that current accounting requires the creation and recognition of additional paid-in capital (APIC) pools associated with excess tax benefits. Under the accounting principles in Topic 718, if the tax deduction taken on the company's income tax return for the award exceeds the cumulative amount of compensation cost recognized in the financial statements for that award, the company would recognize the excess tax benefit as an increase to APIC. On the contrary, if the tax deduction reported in the tax return for an individual award is less than the cumulative compensation cost recognized for financial reporting purposes for that award, the write-off of the related deferred tax asset in excess of the benefits of the tax deduction is recognized 1) in equity to the extent that APIC has been recognized for excess tax deductions from previous share-based payments, or 2) as income tax expense to the extent the write-off exceeds previous qualifying excess tax benefits recognized in equity.

TIC believes this guidance is somewhat counterintuitive; for example, the "build-up of APIC pools" creates arbitrary and inflated equity over the life of the pool that is only reduced by future stock based compensation transactions that may or may not occur. The APIC pools artificially inflate APIC and create an administrative burden for financial statement preparers without providing any useful information for financial statement users.

Therefore, TIC favors recognition of excess tax benefits and tax deficiencies in the income statement. The Board's proposal is more appropriate as the proposed accounting would better align with a change in estimate (i.e., estimated tax benefit vs. actual tax benefit) which would be accounted for at the date of the underlying transaction and recognized in earnings. As the Board noted, there would be volatility in the financial statements;

however, the volatility would be properly disclosed in the company's rate reconciliation disclosure. The Board's proposal also would simplify the accounting for share-based payments as it would effectively eliminate the need to track APIC pools which, as noted above, creates an unnecessary administrative burden for certain preparers.

TIC also supports the proposed elimination of the current requirement to delay recognition of a deferred tax asset for an excess tax benefit from a current-period tax deduction that cannot reduce taxes payable in that period. The Board's proposal to recognize the excess tax benefit (subject to a possible valuation allowance) would be conceptually consistent with current income tax accounting principles.

It should be noted, however, that the proposed tax simplifications would provide greater benefits for public companies than for private companies. As a general rule, private companies do not have APIC pools since options are not exercised on a regular basis. For example, a private start-up company will often attempt to incentivize employees with more and more options over time, but the options can't be sold until a triggering event occurs. Therefore, the pool of options would likely be exercised over a relatively short period of time rather than gradually over time based on market conditions, as is often the case with public companies.

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? [Issue 2, pages 48-52, pars. 21-24, and BC9]

Yes. As discussed in the response to Question 2 above, TIC believes the "true up" adjustment recognized at the date of exercise is an operating cash flow item. Such classification would be consistent with the accounting for the underlying tax impact of the equity award throughout the life of the award. TIC does not believe that a) these are separate and independent cash flows and b) it is appropriate to account for "hypothetical cash inflows and outflows" as financing activities, as the classification would be a misalignment with the underlying transactions.

Question 4: Should entities be permitted to make an accounting policy election either to account for forfeitures when they occur or to estimate forfeitures? If not, why? [Issue 3, pages 52-77, pars.25-38, and BC10-BC14]

Yes. As the Board noted in paragraph BC11, estimating the number of forfeitures can be highly subjective in certain circumstances. For example, it is not uncommon for private companies to issue awards to management or other employees to incentivize and retain those with significant talent. When the issuance of equity awards recurs infrequently, the process of estimating forfeitures is highly subjective because there is little history from which to draw. As a result, it is not uncommon for the preparer to estimate no forfeitures due to the lack of verifiable and supportable assumptions. Therefore, TIC believes, in these circumstances and others, permitting an accounting policy election to account for the forfeitures relating to service conditions as they occur would provide more reliable information to financial statement users and reduce complexity.

Question 5: Is the proposed expansion of the exception to liability classification related to the amount withheld for employee's taxes appropriate? If not, is there another exception that is more appropriate and why? [Issue 4, pages 77-79, pars. 39-41, and BC15-BC17]

In short, TIC agrees that the existing exception in U.S. GAAP is complex (i.e., the exception to liability classification when an employer uses a net settlement feature to withhold shares to meet an employer's tax-withholding requirements), since the employer must determine the minimum statutory withholding requirements on an employee-by-employee, jurisdiction-by-jurisdiction basis.

One example involves jurisdictions with marginal tax withholding rates (i.e., the tax rate that applies to a specific income tax bracket). A number of states in the U.S. require the use of different withholding rates based on an employee's income level, rather than a flat wage rate. When this is the case, an employer must determine minimum withholding requirements on an employee-by-employee basis, which can be a significant burden on a company. Another example would be mobile employees that work in multiple states and/or foreign countries.

Therefore, TIC believes that the proposed requirement to determine only one maximum rate in each jurisdiction rather than determining a rate for each employee would provide for adequate relief. However, this is another example of an amendment that will benefit primarily public companies, where exercising options is a frequent occurrence, employees are geographically dispersed and multiple jurisdictions are involved.

Question 6: Should the cash paid by an employer to the taxing authorities when directly withholding shares for tax-withholding purposes be classified as a financing activity on the statement of cash flows? If not, what classification is more appropriate and why? [See Issue 5, pages 79-81, pars. 42-44, and BC20]

Yes, TIC agrees with the proposed classification of the payments to reacquire shares as a financing activity, since, as discussed in paragraphs BC18-BC19, no cash flow classification guidance exists currently and the substance of these transactions is a share repurchase.

Question 7: When assessing the classification of an award with a repurchase feature that can only be exercised on the occurrence of a contingent event, should a contingent event within the employee's control be assessed in the same manner as a contingent event outside the employee's control? If not, why should there be a difference in the assessment? [See Issue 6, par. 45-page 81, BC21-BC25 and 718-10-25-9 and 718-10-55-137]

Yes. TIC believes that probability should be considered when determining the classification of awards with repurchase features. As noted in paragraph BC22, there is no specific guidance in Topic 718. As a result, the Board's proposal will provide consistent considerations and application to these types of instruments to align the classification

guidance between put and call rights that are contingent on an event within the employee's control.

Question 8: Is the practical expedient for nonpublic entities to estimate the expected term of all awards with performance conditions that affect vesting or service conditions appropriate? If not, are there other practical expedients that are more appropriate and why? Should the expedient be limited to nonpublic entities? [See Issue 7-pages 83-88, par. 48-51, BC26-BC30]

Yes. For awards with service conditions, it is common in practice for nonpublic entities to use the simplified method (i.e., the midpoint between the vesting date and the contractual term) in determining the expected term of the award. TIC believes this is generally acceptable and provides useful information to users of financial statements since the expected term used in valuing the award is required to be disclosed in the financial statements.

Question 9: Should nonpublic entities be allowed to make a one-time election to switch from measuring liability-classified awards at fair value to intrinsic value (current market price less exercise price)? If not, why? While not proposed, should the Board consider making the ability to elect intrinsic value an ongoing election alternative for nonpublic entities? [Issue 8: Intrinsic Value-pages 88-89 and par. BC31-32]

Yes. TIC believes nonpublic entities should be allowed to make a one-time election to change their accounting policies as of the effective date of the Improvements ASU from measuring liability-classified awards at fair value to intrinsic value without having to assess preferability for the change. As discussed in paragraph BC32, certain nonpublic entities and practitioners had not been aware of this election in the original standard and therefore measured their liability-classified awards at fair value instead of intrinsic value. Without the proposed amendment, which offers another election to make the switch, many entities may not be able to justify the change based on preferability. However, TIC believes the issue of ongoing elections should continue to be considered by the PCC as part of its preferability project relating to all PCC alternatives.

Question 10: Are the transition requirements for each area appropriate? If not, what transition approach is more appropriate? [BC36-BC39]

Yes. The transition requirements for each area seem appropriate.

Question 11: How much time will be necessary to adopt the amendments in this proposed Update? Should the amount of time needed to apply the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities?

For nonpublic entities, TIC believes the Board should allow early adoption to allow nonpublic companies to take advantage of the simplifications as soon as practicable. Otherwise, TIC believes the Board should allow a sufficient amount of time for financial

statement preparers and their auditors to understand the new guidance and should provide an additional one-year implementation period for nonpublic companies beyond the transition period allowed for public companies.

TIC appreciates the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely,

Scot Phillips, Chair
PCPS Technical Issues Committee

cc: PCPS Executive and Technical Issues Committees