

## Accounting & Auditing Update

# FASB Issues New ASU on Improvements to Nonemployee Share-Based Payment Accounting

By Bryan Decker, CPA, Senior Manager

As part of its simplification initiative, the Financial Accounting Standards Board (FASB or Board) recently issued Accounting Standards Update (ASU) 2018-07—Compensation—Stock Compensation (Topic 718): **Improvements to Nonemployee Share-Based Payment Accounting**.

Areas of simplification in this ASU pertain to accounting for nonemployee share-based payments such as transactions involving the acquisition of goods and services from nonemployees. However, some of the changes apply only to nonpublic entities.

In order to preserve operating cash flows, some entities often times issue share-based payments to procure goods or services that are used by the entity in its operations. Previously, share-based payments to nonemployees were covered by Accounting Standards Codification (ASC) Topic 505-50: **Equity-Based Payments to Non-Employees**. ASU 2018-07 supersedes Topic 505-50 by amending Topic 718 to apply to all share-based payment transactions where an entity acquires goods or services for its operations.

ASU 2018-07 amends Topic 718 to make it clear that it does not apply to share-based payments used in financing to the issuer or in awards granted in conjunction with selling goods or services to a customer pursuant to a contract accounted for under Topic 606: **Revenue from Contracts with Customers**.

### Summary of Changes

|                                      | Current GAAP  | Summary of Amendments   |
|--------------------------------------|---|---|
| <b>Overall Measurement Objective</b> | 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 requirement for employee share-based payment awards, nonemployee share-based payment awards within the scope of Topic 718 are measured at grant-date fair value of the equity instruments that an entity is obligated to issue when 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. |
| <b>Measurement Date</b>              | 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 <i>grant date</i> is amended to generally state the date at which a <i>grantor</i> and a <i>grantee</i> reach a mutual understanding of the key terms and conditions of a share-based payment award.  |

|  | Current GAAP   | Summary of Amendments  |
|--|--|--|
| <b>Awards with Performance Conditions</b>                              | Nonemployee share-based payment awards with performance conditions are measured at the <i>lowest aggregate fair value</i> .  | Consistent with the accounting for employee share-based payment awards, an entity considers the probability of satisfying performance conditions when nonemployee share-based payment awards contain such conditions.  |
| <b>Classification Reassessment of Certain Equity-Classified Awards</b> | <p>Generally, the classification of equity-classified nonemployee share-based payment awards is subject to other GAAP (for example, 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.</p> <p>This often results in the need to reassess the classification of such awards.</p> | <p>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, the 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.</p> <p>This eliminates the requirement to reassess classification of such awards upon vesting.</p> |
| <b>Nonpublic Entity-Specific Amendments</b>                            |  |  |
| <b>Calculated Value</b>  | Inputs to the valuation of equity share options and similar instruments issued to nonemployees include an estimate of the expected volatility.   | Historical volatility of an appropriate industry-sector index is used by nonpublic entities for expected volatilities as inputs to the valuation of share options and similar instruments issued to nonemployees when it is not practicable for the nonpublic entity to estimate the expected volatility of its share price.   |
| <b>Intrinsic Value</b>   | Entities are required to measure liability-classified nonemployee share-based payment awards at fair value.  | A nonpublic entity can make a onetime election to switch from measuring liability-classified nonemployee share-based payment awards at fair value to intrinsic value. Regardless of the election, liability-classified awards would be subject to remeasurement until exercise.  |

### Remeasurement at Time of Adoption

An entity 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 entity is required to measure these nonemployee awards at fair value as of the adoption date. The entity must not remeasure assets that have already been recorded.

### Effective Dates

ASU 2018-07 effective dates are as follows:

- Public entities: for annual reporting periods beginning after December 15, 2018, including interim periods within that fiscal year.
- Other entities: for annual reporting periods beginning after December 15, 2019, and for interim periods within fiscal years beginning after December 15, 2020.

Early adoption is permitted, but no earlier than an entity's adoption date of Topic 606.

## Contact Us

If you have any questions about this new ASU or about accounting and auditing in general, please contact either of the individuals below or a member of your PKF O'Connor Davies client service team.

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