Statutory Accounting Principles (E) Working Group

**Maintenance Agenda Submission Form**

**Form A**

## **Issue: ASU 2019-08, Codification Improvements to Topic 718 and Topic 606**

**Check (applicable entity):**

 P/C Life Health

Modification of existing SSAP [x]  [x]  [x]

New Issue or SSAP [ ]  [ ]  [ ]

Interpretation [ ]  [ ]  [ ]

Description of Issue: In November 2019, FASB issued *ASU 2019-08 Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer,* which includes amendments to Topics 718 and 606. The changes to Topic 718 include share-based payment transactions for acquiring goods and services from nonemployees and in doing so superseded guidance in Subtopic 505-50, Equity—Equity-Based Payments to Non-Employees. The changes to Topic 606 expand the scope of the codification to include share-based payment awards granted to a customer in conjunction with selling goods or services.

The amendments in ASU 2019-08 require that an entity measure and classify share-based payment awards granted to a customer by applying the guidance in Topic 718. The amount recorded as a reduction of the transaction price is required to be measured on the basis of the grant-date fair value of the share-based payment award in accordance with Topic 718. The grant date is the date at which a grantor (supplier) and a grantee (customer) reach a mutual understanding of the key terms and conditions of a share-based payment award. The classification and subsequent measurement of the award are subject to the guidance in Topic 718 unless the share-based payment award is subsequently modified and the grantee is no longer a customer.

For statutory accounting assessments, prior U.S. GAAP guidance related to share-based payments has been predominantly adopted with modification in *SSAP No. 104R—Share-Based Payments*. Statutory accounting modifications to the U.S. GAAP guidance have mostly pertained to statutory terms and concepts. (For example, statutory reporting lines, nonadmittance of prepaid assets, etc.)

Existing Authoritative Literature:

Stock Compensation is covered by *SSAP No. 104R—Share-Based Payments* and *SSAP No. 95—Nonmonetary Transactions*.

The ASUs related to ASC Topic 606 have been rejected in *SSAP No. 47—Uninsured Plans.*

**Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups**):

Agenda item 2018-35 adopted with modification *ASU 2018-07,* *Improvements to Nonemployee Share-Based Payment Accounting* and incorporated the U.S. GAAP amendments from that project into SAP.

Agenda items 2016-19 and 2017-37 address the main ASUs related to *ASC Topic 606* and there have been several other agenda items for minor updates to revenue recognition guidance, all of which have been rejected in SSAP No. 47.

**Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:**

None.

**Convergence with International Financial Reporting Standards (IFRS):**

None.

Staff Recommendation:

## **Staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to adopt with modification *ASU 2019-08 Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer* for statutory accounting. These revisions would add language to include share-based consideration payable to customers under SSAP No. 104R guidance in the same manner as U.S. GAAP. With the revisions proposed to SSAP No. 104R, revisions are also proposed to *SSAP No. 95—Nonmonetary Transactions* to update previously adopted U.S. GAAP guidance. In addition, proposed revisions to *SSAP No. 47—Uninsured Plans*, reject Topic 606 guidance in ASU 2019-08. The proposed revisions to SSAP No. 95, SSAP No. 104R, and *SSAP No. 47—Uninsured Plans*, are illustrated in the Form A.**

***Proposed Revisions to SSAP No. 95—Nonmonetary Transactions***

**Accounting for a Convertible Instrument Granted or Issued to a Nonemployee for Goods or Services or Services and Cash (in combination or individually), or as Consideration Payable to a Customer**

17. The guidance in paragraph 18 addresses a convertible instrument that is issued or granted to a nonemployee in exchange for goods or services or a combination of goods or services and cash or consideration payable to a customer. The convertible instrument contains a nondetachable conversion option that permits the holder to convert the instrument into the issuer's stock.

19. To determine the fair value of a convertible instrument granted as part of a share-based payment transaction to a nonemployee in exchange for goods or services or as consideration payable to a customer that is equity in form or, if debt in form, that can be converted into equity instruments of the issuer, the entity shall first apply SSAP No. 104R.

*Proposed Revisions to SSAP No. 104R—Share-Based Payments*

## **SUMMARY OF ISSUE**

2. The objective of accounting for transactions under share-based payment arrangements is to recognize in the financial statements the goods or services received in exchange for equity instruments granted or liabilities incurred and the related cost to the entity as those goods or services are received. This statement uses the terms “compensation” and “payment” in their broadest senses to refer to the consideration paid for goods, services, or the consideration paid to a customer.

**Scope and Scope Exceptions**

4. This statement applies to all share-based payment transactions in which a grantor acquires [goods](http://asc.fasb.org/glossarysection%26trid%3D2229119%26id%3DSL2258986-113943) or services to be used or consumed in the grantor’s own operations or provides consideration payable to a customer by issuing (or offering to issue) its shares, share options, or other equity instruments or by incurring liabilities to an employee or nonemployee that meet either of the following conditions:

* 1. The amounts are based, at least in part, on the price of the entity’s shares or other equity instruments.
	2. The awards require or may require [settlement](http://asc.fasb.org/glossarysection%26ioid%3D7485812%26id%3DSL2296969-113906) by issuing the entity’s equity shares or other equity instruments.

5. Share-based payments awarded to a grantee by a related party or other holder of an [economic interest in the entity](http://asc.fasb.org/glossarysection%26ioid%3D6415400%26id%3DSL2300834-113901) as compensation for goods or services provided to the reporting entity are share-based payment transactions to be accounted for under this statement unless the transfer is clearly for a purpose other than compensation for goods or services to the reporting entity. The substance of such a transaction is that the economic interest holder makes a capital contribution to the reporting entity, and that entity makes a share-based payment to the grantee in exchange for services rendered or goods received. An example of a situation in which such a transfer is not compensation is a transfer to settle an obligation of the economic interest holder to the grantee that is unrelated to goods or services to be used or consumed in a grantor’s own operations.

6. The guidance in this statement does not apply to:

* 1. Equity instruments held by an employee stock ownership plan. Such equity instruments shall follow the guidance in SSAP No. 12—Employee Stock Ownership Plans.
	2. Transactions involving equity instruments granted to a lender or investor that provides financing to the issuer.
	3. Transactions involving equity instruments granted in conjunction with selling goods or services to customers as part of a contract (for example, sales incentives). If consideration payable to a customer is payment for a distinct good or service from the customer, then the entity shall account for the purchase of the good or service in the same way it accounts for other purchases from suppliers. Therefore, share-based payment awards granted to a customer for a distinct good or service to be used or consumed in the grantor’s own operations are accounted for under this statement.

Recognition

11. This guidance does not address the period(s) or the manner (that is, capitalize versus expense) in which an entity granting the share-based payment award (the purchaser or grantor) to a nonemployee shall recognize the cost of the share-based payment award that will be issued, other than to require that a nonadmitted prepaid asset or expense be recognized (or previous recognition reversed) in the same period(s) and in the same manner as if the grantor had paid cash for the goods or services instead of paying with or using the share-based payment award.

Initial Measurement

35. An entity shall account for the compensation cost from share-based payment transactions in accordance with the fair-value-based method set forth in this statement. That is, the cost of goods obtained or services received in exchange for awards of share-based compensation generally shall be measured based on the grant-date fair value of the equity instruments issued or on the fair value of the liabilities incurred. The cost of goods obtained or services received by an entity as consideration for equity instruments issued or liabilities incurred in share-based compensation transactions with employees shall be measured based on the fair value of the equity instruments issued or the liabilities settled. The portion of the fair value of an instrument attributed to goods obtained or services received is net of any amount that a grantee pays (or becomes obligated to pay) for that instrument when it is granted. For example, if a grantee pays $5 at the grant date for an option with a grant-date fair value of $50, the amount attributed to goods or services provided by the grantee is $45.

Measurement Objective – Fair Value at Grant Date

38. The measurement objective for equity instruments awarded to grantees is to estimate the fair value at the grant date of the equity instruments that the entity is obligated to issue when grantees have delivered the good or rendered the service and satisfied any other conditions necessary to earn the right to benefit from the instruments (for example, to exercise share options). That estimate is based on the share price and other pertinent factors, such as expected [volatility](http://asc.fasb.org/glossarysection%26ioid%3D6889852%26id%3DSL2301365-113897), at the grant date.

* 1. Measurement Objective and Measurement Date for Awards Classified as Liabilities: At the [grant date](http://asc.fasb.org/glossarysection%26ioid%3D6415241%26id%3DSL2301017-113899), the measurement objective for liabilities incurred under [share-based compensation arrangements](http://asc.fasb.org/glossarysection%26ioid%3D6415241%26id%3DSL2301021-113899) is the same as the measurement objective for equity instruments awarded to [g](http://asc.fasb.org/glossarysection%26trid%3D2229012%26id%3DSL2276460-113911)rantees as described in paragraph 38. However, the [measurement date](http://asc.fasb.org/glossarysection%26ioid%3D7485812%26id%3DSL2297005-113906) for liability instruments is the date of [settlement](http://asc.fasb.org/glossarysection%26ioid%3D6415241%26id%3DSL2301033-113899).
	2. Intrinsic Value Option for Awards Classified as Liabilities: A reporting entity shall make a policy decision of whether to measure all of its liabilities incurred under share-based payment arrangements (for employee and nonemployee awards) issued in exchange for goods or services at [fair value](http://asc.fasb.org/glossarysection%26trid%3D2228950%26id%3DSL2301124-113895) or at [intrinsic value](http://asc.fasb.org/glossarysection%26ioid%3D6743629%26id%3DSL2300956-113898). However, the reporting entity shall initially and subsequently measure awards determined to be consideration payable to a customer at fair value.

52. A reporting entity may not be able to reasonably estimate the fair value of its equity share options, nonemployee awards and similar instruments because it is not practicable for the reporting entity to estimate the expected volatility of its share price. In that situation, the entity shall account for its equity share options, nonemployee awards and similar instruments based on a value calculated using the historical volatility of an appropriate industry sector index instead of the expected volatility of the entity’s share price (permitted value). A reporting entity’s use of permitted value shall be consistent between employee share-based payment transactions and nonemployee share-based payment transactions. Throughout the remainder of this statement, provisions that apply to accounting for share options, nonemployee awards and similar instruments at fair value also apply to calculated value.

*Staff Note: Paragraph 98 references “permitted value in accordance with paragraph 52”, but terminology was not consistent between paragraphs. NAIC staff changed "calculated value" to “permitted value” to allow for easier cross-referencing.*

54. A reporting entity that elects to apply the practical expedient in paragraph 53 shall apply the practical expedient to a share option or similar award that has all of the following characteristics:

* 1. The share option or similar award is granted at the money.
	2. The grantee has only a limited time to exercise the award (typically 30-90 days) if the grantee no longer provides goods, terminates service after vesting, or ceases to be a customer.
	3. The grantee can only exercise the award. The grantee cannot sell or hedge the award.
	4. The award does not include a market condition.

Subsequent Measurement

68. The total amount of compensation cost recognized for share-based payment awards to nonemployees shall be based on the number of instruments for which a good has been delivered or a service has been rendered. To determine the amount of compensation cost to be recognized in each period, an entity shall make an entity-wide accounting policy election for all nonemployee share-based payment awards, including share-based payment awards granted to customers, to do either of the following:

* 1. Estimate the number of forfeitures expected to occur. The entity shall base initial accruals of compensation cost on the estimated number of nonemployee share-based payment awards for which a good is expected to be delivered or service is expected to be rendered. The entity shall revise that estimate if subsequent information indicates that the actual number of instruments is likely to differ from previous estimates. The cumulative effect on current and prior periods of a change in the estimates shall be recognized in compensation cost in the period of the change.
	2. Recognize the effect of forfeitures in compensation cost when they occur. Previously recognized compensation cost for a nonemployee share-based payment award shall be reversed in the period that the award is forfeited.

80. A freestanding financial instrument issued to a grantee that is subject to initial recognition and measurement guidance within this statement shall continue to be subject to the recognition and measurement provisions of this statement throughout the life of the instrument, unless its terms are modified after a grantee vests in the award and is no longer providing goods or services, a grantee vests in the award and is no longer a customer, or a grantee is no longer an employee. Only for purposes of this paragraph, a modification does not include a change to the terms of an award if that change is made solely to reflect an equity restructuring provided that both of the following conditions are met:

* 1. There is no increase in fair value of the award (or the ratio of intrinsic value to the exercise price of the award is preserved, that is, the holder is made whole) or the antidilution provision is not added to the terms of the award in contemplation of an equity restructuring.
	2. All holders of the same class of equity instruments (for example, stock options) are treated in the same manner.

81. Other modifications of that instrument that take place after a grantee vests in the award and is no longer providing goods or services, is no longer a customer, or is no longer an employee shall be subject to the modification guidance in paragraph 83. Following modification, recognition and measurement of the instrument shall be determined through reference to other applicable statutory accounting principles.

Subsequent Measurement - Awards Classified as Liabilities

97. Changes in the fair value (or intrinsic value for a reporting entity that elects that method) of a liability incurred under a share-based payment arrangement issued in exchange for goods or services that occur during the employee’s requisite service period or the nonemployee’s vesting period shall be recognized as compensation cost over that period. The percentage of the fair value (or intrinsic value) that is accrued as compensation cost at the end of each period shall equal the percentage of the requisite service that has been rendered for an employee award or the percentage that would have been recognized had the grantor paid cash for the goods or services instead of paying with a nonemployee award at that date. Changes in the fair value (or intrinsic value) of a liability issued in exchange for goods or services that occur after the end of the employee’s requisite service period or the nonemployee’s vesting period are compensation costs of the period in which the changes occur. Any difference between the amount for which a liability award issued in exchange for goods or services is settled and its fair value at the settlement date as estimated in accordance with the provisions of this statement is an adjustment of compensation cost in the period of settlement.

98. Reporting entities shall measure a liability award under a share-based payment arrangement based on the award’s fair value (or permitted value in accordance with paragraph 52) remeasured at each reporting date until the date of settlement. Compensation costs for each period until settlement shall be based on the change (or a portion of the change, depending on the percentage of the requisite service that has been rendered for an employee award or the percentage that would have been recognized had the grantor paid cash for the goods and services instead of paying with a nonemployee award at the reporting date) in the fair value of the instrument for each reporting period. A reporting entity shall subsequently measure awards determined to be consideration payable to a customer at fair value.

Effective Date and Transition

132. Since the initial adoption of SSAP No. 104, subsequent revisions were effective as follows:

* 1. *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer.*

## **References**

### Other

* *SSAP No. 12—Employee Stock Ownership Plans*

***Proposed Revisions to SSAP No. 47—Uninsured Plans***

## **Relevant Literature**

15. This statement rejects *ASU 2014-09, Revenue from Contracts with Customers; ASU 2015-14, Revenue From Contracts With Customers; ASU 2016-08, Revenue From Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net); ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing; ASU 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients; ASU 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers; ASU 2018-18, Collaborative Arrangements (Topic 808), Clarifying the Interaction between Topic 808 and Topic 606,* the Topic 606 guidance included in *ASU 2019-08, Codification Improvements to Stock Compensation (Topic 718) and Share-Based Consideration Payable to a Customer (Topic 606), ASU 2021-02, Franchisors—Revenue from Contracts with Customers, ASU 2021-08, Business Combinations, Accounting for Contract Assets and Contract Liabilities from Contracts with Customers*

Staff Review Completed by:

NAIC Staff – William Oden, February 2023

Status:

On March 22, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification, and exposed revisions to SSAP No. 95, SSAP No. 104R, and SSAP No. 47 to adopt, with modification, *ASU 2019-08 Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer*, as illustrated above.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2023/3-22-23 - Spring/Exposures/23-07 - ASU 2019-08 - Stock Comp.docx