Pfizer Inc
235 East 42nd Street
New York, NY 10017-5755

August 14, 2015

Technical Director
File Reference Nos. 2015-270
FASB
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Subject: Proposed Accounting Standards Update (ASU), *Compensation–Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*

Dear Technical Director:

Pfizer Inc. is a research-based, global biopharmaceutical company headquartered in New York. We discover, develop, manufacture and market leading medicines and vaccines, as well as many of the world's best-known consumer healthcare products. In 2014, we reported revenues of $50 billion and total assets of $169 billion.

Pfizer supports the intent underlying the Board's broad Simplification Initiative; that is, to reduce the cost and complexity in U.S. GAAP, while maintaining or improving the usefulness of the information provided to users of financial statements. As we explain more fully in the responses to the Questions for Respondents, we believe some elements of this proposed Update achieve that goal, while other provisions do not. We are also concerned that some of the proposed changes go beyond the scope of the Board's Simplification Initiative.

General Comments

- We concur with the Board's conclusion, as incorporated into current U.S. GAAP, that a share-based payment arrangement is comprised of two transactions: a compensation arrangement (equity consideration for services) and an equity transaction (upon exercise of options or vesting of shares). [SFAS 123R, B209]
- We believe that the income statement should continue to reflect only the grant date Fair Value and the corresponding tax effect on that pretax amount. We believe that this approach provides the most decision-useful information to users of financial statements.
- We are concerned about any "simplification" proposal that introduces new volatility into the income statement and we are especially concerned when that volatility is the result of an equity transaction. Such an action seems beyond the scope of the Board's Simplification Initiative.
- The extraordinary effort associated with the APIC pool was primarily attributable to the *development* of the pool upon adoption of SFAS 123R. In our experience, there is no significant ongoing effort involved in the continued monitoring of the pool.
- We would support a simplification proposal that requires all tax deficiencies to be recorded in APIC, regardless of the status of any existing APIC pool.

Please also see our responses to Questions for Respondents.

Questions for Respondents

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?

No. See our responses to the following Questions for Respondents.

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?

- We do <u>not</u> agree that excess tax benefits and tax deficiencies should be recognized in the income statement.

  Under U.S. GAAP, when accounting for a share-based payment arrangement, the arrangement is comprised of two transactions: a compensation arrangement (equity consideration for services) and an equity transaction (upon exercise of options or vesting of shares). We do not believe that effects of the equity transaction should result in an income statement impact.

  When accounting for a share-based payment arrangement, the compensation portion of the arrangement ends on the grant date and, therefore, the compensation cost is fixed on that date. This accounting reflects the concept that subsequent changes in the fair value of the awards are not considered part of the compensation arrangement; rather they are gains/ losses of the employees as shareholders and are not related to the compensation arrangement. We believe that the tax impact should follow the same concept where the tax impact related to the employer's tax deduction as a result of the exercise of the option or vesting of the shares in excess of the compensation cost recognized should not be recognized in the income statement. As this additional net tax deduction (i.e., cumulative excess tax benefits net of cumulative tax deficiencies) directly results from the exercise of the options or vesting of the shares and reflects the subsequent changes in the fair value of the awards after the grant date, it should be treated as additional proceeds received from the issuance of the shares and, as such, should be recognized in APIC.

  Furthermore, the **tax** effects of the deductible compensation cost in excess of the compensation cost recognized for financial reporting purposes results from changes in the market value of the equity award (capital). Generally, under U.S. GAAP, changes in the market value of the company's capital are not recognized in the income statement. We believe that is because such changes do not represent the historical performance of the company, but rather the market's perception of the company's *expected* performance. Therefore, we do not believe it is appropriate to recognize the excess tax benefits in the income statement; rather, as these benefits are a direct result of the change in the market value of the company's equity, we believe these should be recorded in APIC.

  Also, the income tax effects recognized in the income statement generally represent the tax impacts related to the pre-tax income. Accordingly, as there is no pre-tax income or expense recognized in the income statement for the difference between the fair value at grant date for book purposes and the intrinsic value at settlement date, it is our view that the related tax effects of such difference should not be recognized in the income statement.

  In addition to the conceptual basis for our disagreement with the proposed amendment, we do not think recognizing all excess tax benefits and tax deficiencies in the income statement would maintain or improve the usefulness of information provided to users of financial statements. As the Board noted in BC5, the proposed amendment may make an entity's reported income tax expense more volatile and as such we believe it would introduce complexity and variability, making it more difficult for financial statement users to understand reported results. That is, since the tax provision in the income statement would include tax impacts not related to any pre-tax income or the entity's ongoing business but rather it would include impacts associated with the market price of a company's stock.

- We <u>would</u> support a simplification proposal that requires all tax deficiencies to be recorded in APIC, regardless of the status of any existing APIC pool.

- With regards to the Board's proposal to eliminate the APIC pool as a simplification initiative, it is our experience that the cost and complexity around the APIC pool was significantly greater when the APIC pool was first established and less so for its ongoing maintenance and related tax calculations. We see no simplification benefits from the proposal to eliminate the APIC pool. In other words, if this simplification initiative had been introduced at the same time as the current standard, we might have considered it differently, but given that we have set up the pool and the processes supporting it, we find no substantive benefit to the simplification initiative at this point, to either preparers or to users of the financial statements.

- Under the proposed guidance (an income statement model), we agree that an entity should not delay recognition of an excess tax benefit until the benefit is realized through a reduction to taxes payable since this would not align with the guidance related to all other tax impacts in the income statement. However, as described, we do not support this proposed amendment.

  Under an APIC model (our proposal), while we agree that removing the requirement to delay recognition of an excess tax benefit until the tax benefit is realized through the reduction of taxes payable would achieve simplification (the calculations are onerous). We also recognize that, in an equity transaction, if the proceeds are not received in cash, recording an increase to equity against a deferred asset, that may at times be a noncurrent asset, would not be conceptually appropriate. As such, we are unclear, under an APIC model, how the removal of the requirement to delay recognition of an excess tax benefit until the tax benefit is realized through the reduction of taxes payable would maintain or improve decision-useful information.

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?

We respectfully request the Board not approve the proposed amendment to recognize all excess tax benefits and tax deficiencies in the income statement, based on our above view that in essence these adjustments reflect capital transactions. However, if that proposal is approved, we would not object to classifying, as a matter of consistency, excess tax benefits as an operating activity.

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?

We respectfully request the Board not approve the proposed amendment to change the current accounting for forfeitures. In our view, and as observed by the Board in BC13, estimating forfeitures generally provides a more accurate reflection of periodic compensation cost.

Also, by allowing a policy election, we are concerned this proposed amendment would reduce comparability among companies with economically similar equity awards, which we believe does not maintain or improve the usefulness of the information provided to users of financial statements.

Finally, we observe that the Board concluded that, regardless of whether an entity estimates the effects of forfeitures in its initial accrual of compensation cost or accounts for forfeitures in compensation cost when they occur, the entity will ultimately recognize compensation cost for all awards that vest. While we agree that ultimately the cumulative compensation cost recognized will be the same regardless of the policy elected, the costs per period will differ over the vesting period, which is usually a number of years. As such, we do not believe that a policy election should be granted, as it does not maintain or improve decision-usefulness.

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?

Yes, we believe the proposed approach to change the threshold for an award to qualify for equity classification to permit withholding up to the employee's maximum individual statutory tax rate in the applicable jurisdictions achieves the intentions of the Board's Simplification Initiative.

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?

Although it is our view, as expressed below, that these cash payments have more relevance as part of operating activities, we would not object to the proposed amendment to classify such payments as a financing activity as we also appreciate the conceptual view to account for these cash payments as an "in substance" repurchase of shares and to thus present them as part of financing activities.

Notwithstanding, we support the Board's intention to provide guidance in this area where some believe currently there is none; although a supportable basis for classifying tax withholding payments as an operating activity can be found by the literal requirement to classify cash payments to governments for taxes, duties, fines, and other fees or penalties as operating activities (ASC 230-10-45-17-c) and the absence of actual cash flows for the purchase of stock.

In our view, rather than considering these cash payments to the taxing authorities as repurchases of an equity instrument, we effectively view these cash payments as the fulfillment of a company's obligation to withhold taxes from the employees' compensation and pay it to the government, and, as such, we believe they should be presented as part of operating activities. Furthermore, as the taxing authorities will not accept payment in the form of company shares, effectively, employee compensation awards will always trigger a payment of cash by the entity for the portion withheld (i.e., in other words, effectively, a portion of the award will always need to be converted into cash). We recognize the Board's observations in BC20 about the definition of operating activities; however, these particular withholding cash payments are, as explained above, a direct result of compensation provided to employees and cannot be avoided, akin to cash paid for cash payroll taxes withheld, and, therefore, we believe that they are a "... cash effect of transactions and other events that enter into the determination of net income."

As such, we request the Board reconsider its conclusion and treat cash paid by an employer to a taxing authority as part of operating activities on the statement of cash flows, consistent with the presentation of cash payroll tax withholdings.

Question 10: Are the transition requirements for each area appropriate? If not, what transition approach is more appropriate?

We do not object to the transition requirements for each area as described in the proposed Update.

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 entities be different from the amount of time needed by public business entities?

We would need a reasonable amount of time after issuance to make any necessary adjustments to third party vendor system calculations and to evaluate the transition requirements where they may require cumulative effect adjustments to equity and/or retrospective presentation.

***

We appreciate the opportunity to provide our comments on the amendments in the proposed Update. We would be happy to discuss our comments with you further or to meet with you if it would be helpful.

Loretta V. Cangialosi
Senior Vice President and Controller

cc: Frank D'Amelio
Executive Vice President and Chief Financial Officer