FINANCIAL ACCOUNTING STANDARDS BOARD

Board Meeting Handout

PCC Issue No. 2018-01, "Practical Expedient to Measure Grant-Date Fair Value of Equity-Classified Share-Based Awards"

August 4, 2021

Meeting Purpose

1. At the June 2021 Private Company Council (PCC) meeting, PCC members and the Board continued discussions of a practical expedient for a private company to determine the current price input of equity-classified share-based awards issued to both employees and nonemployees (the practical expedient). The PCC voted to direct the staff to proceed with the issuance of a final Update for the practical expedient subject to FASB endorsement. The practical expedient describes the characteristics of a reasonable application of a reasonable valuation method, and those characteristics are the same characteristics provided in the U.S. Treasury Regulations related to Section 409A of the Internal Revenue Code (Section 409A). Therefore, a valuation performed in accordance with those Treasury Regulations would be an example of a valuation that would be reasonable under the practical expedient.

2. The August 4, 2021 Board meeting is a decision-making meeting. The Board will discuss the practical expedient. The staff will ask the Board to decide whether it endorses the PCC's decision to proceed with the issuance of a final Update. If the Board endorses the PCC's decision, the staff will proceed with the balloting process.

Question for the Board
1. Does the Board endorse the PCC's decision to proceed with the issuance of a final Update for a practical expedient for a private company to determine the current price input of equity-classified share-based awards issued to both employees and nonemployees that describes the characteristics of a reasonable application of a reasonable valuation method?

PCC Decision 1: Aligning with Section 409A

3. During initial deliberations leading to exposure of the proposed Update on August 17, 2020, the PCC decided that the practical expedient should allow a nonpublic entity to determine the current price input in accordance with certain valuation procedures described in paragraph 1.409A-1(b)(5)(iv)(B)(2) of Section 409A.

4. In redeliberations, the PCC decided that it would not directly reference paragraph 1.409A-1(b)(5)(iv)(B)(2), and would instead (a) include certain language from Section 409A describing the characteristics of the reasonable application of a reasonable valuation method and when previously calculated values are considered reasonable, and (b) indicate that valuations performed in accordance with paragraph 1.409A-1(b)(5)(iv)(B) of Section 409A would be examples of valuation approaches having the described characteristics.

5. Consistent with Section 409A, the practical expedient states that the following factors should be considered to evaluate the reasonable application of a reasonable valuation on the measurement date:

    a. The value of tangible and intangible assets of the nonpublic entity

    b. The present value of anticipated future cash-flows of the nonpublic entity

    c. The market value of stock or equity interests in similar corporations and other entities engaged in trades or businesses substantially similar to those engaged in by the nonpublic entity the stock of which is to be valued, the value of which can be readily determined through nondiscretionary, objective means (such as through trading prices on an established securities market or an amount paid in an arm's length private transaction)

    d. Recent arm's length transactions involving the sale or transfer of such stock or equity interests

    e. Other relevant factors such as control premiums or discounts for lack of marketability and whether the valuation method is used for other purposes that have a material economic effect on the nonpublic entity, its stockholders, or its creditors

    f. The nonpublic entity's consistent use of a valuation method to determine the value of its stock or assets for other purposes, including for purposes unrelated to compensation of service providers.

    Consistent with Section 409A, the practical expedient also states that the use of a valuation method is not reasonable if it does not consider all relevant information when applying its methodology and that a previously calculated value is not reasonable at a later date if the valuation is either older than 12 months or fails to reflect information that would materially change the value of the nonpublic entity.

Basis for the PCC's Decisions

6. The PCC approved the practical expedient on the basis that it would reduce costs associated with determining the current price input associated with a share-based award albeit for a limited population of nonpublic entities. The PCC expected that the cost reduction would arise primarily from a potential reduction in the number of valuations that nonpublic entities are required to obtain when a reasonable valuation having the characteristics described in the practical expedient was obtained within the last 12 months and when that valuation was updated to reflect information after the date of the calculation that may have a material effect on the value of the entity. The PCC also expected that in more limited circumstances the cost reduction would arise because:

    a. Nonpublic entities currently obtaining two independent valuations (one for GAAP and one for tax requirements) would be able to obtain just one to satisfy both purposes.

    b. An acceptable practice for determining the current price input using only one valuation would be codified in GAAP.

PCC Decision 2: Scope

7. During initial deliberations of the proposed Update, the PCC limited the scope of the practical expedient to equity-classified share-option awards for both employees and non-employees of nonpublic business entities. In redeliberations, the PCC decided to expand the scope of the practical expedient beyond just share-option awards to include all equity-classified awards within the scope of Topic 718.

PCC Decision 3: Application

8. During initial deliberations of the proposed Update, the PCC decided that the practical expedient could be elected on an award-by-award basis. In redeliberations, the PCC decided that the practical expedient should be applied on a measurement-date-by-measurement-date basis.

PCC Decision 4: Disclosure

9. During initial deliberations of the proposed Update, the PCC did not consider a disclosure requirement for the practical expedient. In redeliberations, the PCC decided to require a nonpublic entity to disclose that it has elected to apply the practical expedient.

PCC Decision 5: Transition and Effective Date

Transition

10. The PCC decided that the practical expedient should be applied prospectively.

Effective Date

11. The PCC decided that the practical expedient would apply to qualifying awards granted or modified during fiscal years beginning on or after December 15, 2021, and interim periods in the following year, with early adoption, including adoption within an interim period, permitted for financial statements that have not yet been issued or made available for issuance as of the issuance date of the final Update.

FINANCIAL ACCOUNTING STANDARDS BOARD

Board Meeting Handout

Joint Venture Formations

August 4, 2021

Meeting Purpose

1. The purpose of the August 4, 2021 Board meeting is to continue initial deliberations on the project.

2. At the February 17, 2021 Board meeting, the Board asked the staff to research areas in which differences, including equity method basis differences, could arise from misalignments between (a) the initial accounting by the venturer for its equity method investment in a joint venture and (b) the accounting upon formation by the joint venture based on the Board's tentative decisions on this project. The staff will ask the Board if it wants to expand the project's scope and objective to address those areas of differences and misalignments.

Questions for the Board
1. Would the Board like to expand the scope and objective of the project to include eliminating sources of venturer basis differences and other misalignments between the joint venture's accounting for its net assets and the venturer's equity method investment in the joint venture at formation? 2. If the answer to question 1 is "no," does the Board believe that the expected benefits of requiring a joint venture to initially recognize and measure the contribution of assets at fair value in its financial statements at formation (under the Board's tentative decisions to date) would justify the expected costs? 3. If the answer to question 2 is "no," would the Board like to remove the project from the technical agenda?

Issue Background

3. During the July 22, 2020 Board meeting, the Board tentatively decided to require a joint venture, upon formation, to account for contributions by the venturers as though the joint venture was the acquirer of a business within the scope of Subtopic 805-10, Business Combinations—Overall. That Subtopic requires that the acquirer recognize and measure the identifiable assets acquired and liabilities assumed at fair value (with certain exceptions).

4. The guidance in Subtopic 610-20, Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets, and Subtopic 810-10, Consolidation—Overall, require a venturer to initially measure its equity method investment in a joint venture at fair value. Topic 323, Investments—Equity Method and Joint Ventures, requires that an equity method investor—when calculating its equity method income based on the earnings of the investee—adjust the investee's earnings for any basis differences each period. Therefore, the measurement basis used in a joint venture's financial statements affects how significant the basis differences at formation would be for the venturer entity.

5. At the August 4, 2021 meeting, the staff will ask the Board whether it wants to proceed with the current project scope and objective or if it wants to expand the project scope and objective to eliminate all formation date basis differences that must be tracked by an equity method investor in a joint venture (venturer).