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Ms. Suzanne Bielstein  
Director of Major Projects and Technical Activities  
File Reference 1200-200  
Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, CT 06856-5116

Letter of Comment No: /7  
File Reference: 1200-200  
Date Received: 4/13/04

Dear Ms. Bielstein:

BDO Seidman, LLP is pleased to offer comments on the Proposed FASB Statement, *Earnings per Share*.

We support issuance of the Proposed Statement, because we believe that it is consistent with the stated objective of harmonizing with the IASB with standards that are equivalent, or superior, to existing U.S. GAAP. However, we strongly object to the proposed change related to mandatorily convertible securities.

#### Year-to-date Computations

We agree with the proposed change to compute year-to-date earnings per share (EPS) based on the total period, so that year-to-date EPS is not affected by the frequency of reporting. The proposed amendment specifically affects the treasury stock method for options and warrants. We recommend that the Board make a similar change to the computations involving contingent shares

#### Transactions That Can Be Settled in Cash or Shares

We agree with the requirement to assume settlement in shares if such settlement is more dilutive.

#### Mandatorily Convertible Securities

We are strongly opposed to the requirement that shares to be issued upon conversion of a mandatorily convertible security be included in the computation of basic EPS from the date that conversion becomes mandatory. We believe that presentation is not representationally faithful of the economic substance during the period that the



mandatorily convertible security is outstanding and not yet converted. Following is a description of a form of mandatorily convertible preferred stock issued in substantial amounts by U.S. companies in the past 10 years to help illustrate our point:

Preferred stock is issued with a three-year life and a mandatory conversion into common stock at the end of three years. The number of common shares varies depending on the market price of the common stock at the end of three years, with a minimum of 5/6th of a common share per share of preferred and a maximum of 1 common share per share of preferred. During its three-year life, the preferred pays a dividend substantially higher than the dividend on common shares, either a fixed dividend or a formula dividend that changes with money market conditions. In the event of liquidation of the issuer prior to the mandatory conversion date, the preferred stock has a preference over common stock.

The assumed conversion of the security will almost always be anti-dilutive, because the dividend on a preferred share normally exceeds the earnings per if-converted common share. Assuming conversion for basic EPS obscures the real economic return that the preferred shareholders receive during the three-year life of the preferred stock and overstates the earnings available to the common shareholders during that period. We believe the appropriate presentation for basic EPS in this circumstance is to subtract the dividend on the preferred shares from net income to derive income available to common shareholders.

Prior to the mandatory conversion date, the convertible security should affect basic EPS in a manner similar to a class of common stock with dividend rights that are different from the rights on other outstanding common shares. Under Statement 128, that circumstance would require the use of the two-class method to determine basic EPS. We also note that the EITF recently reached a consensus on Issue No. 03-6, "Participating Securities and the Two-Class Method under FASB Statement No. 128, *Earnings per Share*," that all participating securities, whether or not convertible, should be included in the computation of basic EPS using the two-class method. That consensus resulted in the FASB staff agreeing to rescind EITF Abstracts, Topic No. D-95, "Effect of Participating Convertible Securities on the Computation of Basic Earnings per Share," which permitted entities to make an accounting policy decision as to how participating convertible securities were to be included in the computation of basic EPS (using either the two-class method or the if-converted method, if the dilutive effect is greater than using the two-class method). Requiring the use of the if-converted method for mandatorily convertible securities seems inconsistent with the consensus on Issue 03-6 and the staff's decision to withdraw the guidance in Topic D-95.

Further, we do not believe mandatorily convertible preferred shares meet the intent of paragraph 10 of Statement 128. Paragraph 10 states that, "Shares issuable for little or no

cash consideration upon the satisfaction of certain conditions (contingently issuable shares) shall be considered outstanding common shares and included in the computation of basic EPS as of the date that all necessary conditions have been satisfied (in essence, when issuance of the shares is no longer contingent).”

The preferred shareholder is required to pay substantial non-cash consideration to obtain the common shares by giving up the preferred shares with their valuable dividend and liquidation preference rights. Although the preferred shareholders have no choice in the matter, from the company's point of view, the common shares will be issued in exchange for valuable consideration. As a result, we believe that the common shares should be included in basic EPS only at the time that they are issued. In the rare case in which conversion would be dilutive, the dilution will be captured in diluted EPS.

We would be pleased to discuss our comments with the Board or staff. Please direct questions to Ben Neuhausen at 312-616-4661.

Very truly yours,

s/ BDO Seidman, LLP