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Mr. Lawrence Smith  
Director TA&I--FSP  
Financial Accounting Standards Board  
401 Merritt 7  
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LETTER OF COMMENT NO. 9

Dear Mr. Smith:

BDO Seidman, LLP is pleased to offer comments on the Proposed FASB Staff Position (FSP) EITF 00-19-b.

We commend the FASB staff for issuing this proposed FSP to address accounting for registration payment arrangements, an area in which there has been much diversity in practice. In the future we would like to see additional guidance that addresses the complexity and diversity in other areas of EITF Issue No. 00-19, not just registration payment arrangements.

We agree with the provisions of the proposed FSP that registration payment arrangements should be separately recognized and measured in accordance with FASB Statement No. 5, *Accounting for Contingencies*. We further agree that instruments subject to a registration payment arrangement should be accounted for under other applicable GAAP without regard to the registration payment arrangement.

Our comments below provide recommendations to improve the proposed guidance.

#### Scope

We agree with the definition of registration payment arrangements provided by the FSP and that the accounting should be the same whether a registration payment arrangement is issued as a separate agreement or included as a provision of another agreement. Further, we agree that the provisions of the FSP also should apply to arrangements requiring an issuer to obtain and/or maintain a listing on a stock exchange. Listing requirements are commonly included in registration payment arrangements and should be accounted for in the same manner. We also have seen agreements that require a company to comply with filing requirements so that holders of the company's securities can sell them under Rule 144. We believe the scope should be broadened to encompass these filing requirements as well as requirements to file registration statements.

In paragraph 5, it is not clear to us what the term “remaining characteristics” in the final sentence means.

Since the scope of the FSP is limited to registration payment arrangements, paragraphs 6, 11 and B10 appear to imply that commercial arrangements with similar characteristics are derivatives that should be accounted for under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. We do not believe that other commercial arrangements are derivatives, nor do we think they are treated as derivatives in current practice. Consequently, we recommend that the language in the final FSP, particularly B10, be modified to state that the Board has not deliberated other commercial arrangements and that this FSP is not intended to express or imply a view about whether other commercial arrangements are derivatives.

We believe that the FSP should include in its scope registration payment arrangements that are silent as to consideration payable. Paragraph 17 of Issue 00-19 states that if “the contract does not specify how the contract would be settled in the event that the company is unable to deliver registered shares, then net-cash settlement is assumed if the company is unable to deliver registered shares....Consequently, the derivative must be classified as an asset or a liability....” The interaction of the FSP and paragraph 17 is not clear for an arrangement that is silent about consideration, and staff guidance would be helpful.

#### Recognition and Measurement

As noted above, we agree with the recognition and measurement provisions of the proposed FSP. We further agree with the Board’s reasons in paragraph B7 for requiring measurement under Statement 5 rather than requiring that the liability be recorded at fair value.

We agree with the accounting for registration payment arrangements associated with debt instruments under paragraph 8 and 9 of the FSP. However, we are concerned about the application of this accounting for registration payment arrangements associated with equity instruments. If an entity recorded a contingent liability for a registration payment arrangement associated with an equity instrument at issuance, and the liability were subsequently reversed or reduced, then the entity would record income on a transaction in its own equity. Consequently, we believe that entities should record the consideration payable under an arrangement associated with equity instruments, and any change in that consideration, as an adjustment to equity. As a result, registration payment arrangements associated with debt instruments would affect earnings whether accrued at inception or later, and registration payment arrangements associated with equity instruments would not affect earnings whether accrued at inception or later. We also note that for equity instruments, the consideration payable often is characterized as additional dividends, for example, an increase in the dividend rate on preferred stock if the issuing company fails to meet its obligations under a registration payment arrangement. If the FASB accepts

this recommendation, we recommend specifying that the adjustments to equity affect earnings applicable to common shareholders for purposes of earnings per share computations.

The FSP applies regardless of the form of consideration transferred under a registration payment arrangement. We believe that the FSP should expand the guidance in paragraph B5 as follows. We agree that consideration payable based on a fixed dollar amount with a variable number of shares should be classified as a liability in accordance with FASB Statement No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*. However, we believe that consideration payable in a fixed number of shares (which we have seen in practice) should be measured at the date the registration payment arrangement is entered into and should be recorded if and when payment becomes probable. This accounting is based on the commitment date accounting of EITF Issue No. 00-27, "Application of Issue No. 98-5 to Certain Convertible Instruments."

#### Disclosures

We agree with the required disclosures.

#### Transition and Effective Date

We agree that the FSP should apply to all new arrangements that are entered into after the effective date of the FSP.

Regarding transition, we believe that further guidance is needed as follows:

1. Registration payment arrangements that were modified prior to the FSP effective date or are modified after issuance of the FSP – It is not clear whether the analysis required for implementation should be based on the modification date or the issuance date of the arrangement. We recommend that the analysis should be performed as of the date of the most recent modification. However, it is not clear to us how to analyze and compute adjustments for a modified award. We recommend that the FASB provide more guidance on how to compute the adjustments for a modified award.
2. With respect to modifications, we believe that the FSP should be effective immediately only for arrangements that are substantively modified subsequent to issuance. A non-substantive modification should not accelerate the applicability of the FSP.
3. Financial instruments that will no longer be accounted for as derivative instruments and will be recombined as if the embedded derivative had never been separated – If the reconstituted instrument is determined to have a beneficial conversion feature (BCF) at issuance, we believe that it is incorrect to record the entire cumulative catch up entry to retained earnings. An entity in that situation also should adjust additional paid-in capital. We recommend that Example 9 be



expanded to illustrate the entries if a BCF would have existed at issuance (discussed further below).

Implementation Guidance

For all examples, please note that income tax effects have not been considered to avoid confusion.

Example 1

As discussed above, we believe that an accrual for registration payment arrangements associated with common stock should be charged to equity, not income. Consequently, we believe that the \$13.5 million should be recorded as a liability and as a reduction of equity.

We note that in Example 2, the accrual for the registration payment arrangement was charged against equity in the initial allocation. We agree with this conclusion and believe that the classification of the debit in Examples 1 and 2 should be consistent.

Example 4

This example is straightforward and we agree with the conclusion. However, an example of a registration payment arrangement entered into in conjunction with the issuance of convertible preferred stock and warrants or convertible notes and warrants would have been more helpful.

Example 9

Example 9 of the FSP provides guidance for an instrument with an embedded derivative that was bifurcated, but upon adoption of the FSP would be recombined. Paragraph 17 of the FSP states that the “instrument should be recombined and adjusted to the carrying amount that would have been recognized at the adoption date of this FSP if the embedded derivative were not previously separated.” While the Example 9 does show recombination, it does not show recombination and entries for an instrument with a BCF at issuance.

If at inception, the instrument described in Example 9, was convertible at \$40/share when the market price of the common stock was \$45/share, there would have been a \$125 BCF. Included below is Example 9a that shows what we believe the recombination and transition entries for such an instrument would be. For purposes of the example we assume that if the debt had been initially recorded at \$875 in accordance with EITF Issue No. 00-27, the debt would have accreted to \$935 at transition date.

Example 9a

Derivative liability – conversion option	350	
Convertible debt instrument		35



APIC - BCF	125
Contingent liability	20
Beginning retained earnings	170

To further expand this illustration, assume the same facts as above with the following changes. The instrument was issued with warrants having a fair value of \$250 that would have been accounted for as equity but for the registration payments agreement. The fair value of the warrants increased to \$275 at transition date. The relative fair values allocation at inception would have been \$200 for the warrants and \$800 for the debt. As a result, the debt would have had a BCF of \$325. The debt has accreted to \$725 at transition date. Included below is Example 9b that shows what we believe the recombination and transition entries for such an instrument would be.

Example 9b

Derivative liability – conversion option	350
Warrant liability	275
Convertible debt instrument	175
APIC - BCF	325
APIC – Warrants	200
Contingent liability	20
Beginning retained earnings	255

Editorial Suggestion

We suggest two changes to the second sentence of paragraph 7:

1. State that the financial instrument shall be “recognized, measured, and classified” in accordance with other applicable GAAP. We believe that classification is encompassed in recognition, but suggest being as clear and explicit as possible.
2. Add Statement 150 to the examples of other applicable GAAP.

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

Very truly yours,

s/ BDO Seidman, LLP