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Director, Technical Application and Implement
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

LETTER OF COMMENT NO. 5

RE: Proposed FASB Staff Position EITF No. 00-19-b, "Accounting for Registration Payment Arrangements"

Dear Director:

We appreciate the opportunity to provide our comments on proposed FASB Staff Position EITF No. 00-19-b, "Accounting for Registration Payment Arrangements." We support the Board's efforts to provide guidance on the accounting for registration payment arrangements and, in order to address diversity in practice, we agree with the Board's decision that registration payment arrangements should be recognized and measured under FASB Statement 5, "Accounting for Contingencies". We view the FSP as a short-term solution and encourage the Board to take steps in the future to address the complexities that are inherent in applying the provisions of EITF 00-19 which lead to many difficulties in practice. The following paragraphs include our recommendations to clarify provisions of the proposed FSP.

Best Efforts versus Obligatory Arrangements

Paragraphs B1 and B9 of the Basis for Conclusions explain that arrangements that obligate an entity to deliver registered shares upon exercise or conversion are not within the scope of the FSP and would continue to preclude equity classification for freestanding derivatives and embedded features analyzed under EITF 00-19. We believe that the Background and Scope sections of the FSP should address that point and emphasize the fact that a contract that obligates an issuer to use "best efforts" or "commercially reasonable efforts" to register the equity shares that are issuable upon exercise or conversion of a financial instrument does not require the issuer to deliver registered shares in the context of EITF 00-19. Additionally, we believe that the Board should clarify whether registration payment arrangements that do not specifically contain "best efforts" or "commercially reasonable efforts" clauses, but do not prohibit net-share settlement or physical settlement by delivery of unregistered shares are within the scope of the FSP.



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Scope

While the proposed FSP indicates that “commercial arrangements” are not within the scope of the FSP, it is unclear how a commercial arrangement is defined and whether it was the Board’s intention to restrict the application of the FSP to specific types of financial instruments. We note the absence of a statement that analogies are prohibited. Because of a general lack of accounting guidance for arrangements similar to the registration payment arrangements discussed in the proposed FSP, we would expect entities to attempt to analogize to the conclusion in the proposed FSP. We therefore believe the Board should clarify the scope of the FSP, and if, since the proposed FSP is an exception to the definition of a derivative under Statement 133, it believes analogies are not appropriate to specifically prohibit them as has been done in other pronouncements.

Recognition and Measurement

The Board should clarify that a registration payment arrangement recognized at issuance of a convertible debt is a liability separate and apart from the convertible debt. As such, it (1) reduces the proceeds used to determine the effective conversion price as described in Issue 1 of EITF 00-27, “Application of Issue No. 98-5 to Certain Convertible Instruments”; (2) affects the analysis under paragraph 13(b) of Statement 133 (i.e. the double-double test) and DIG B-16 “Calls and Puts in Debt Instruments”; and (3) its subsequent changes, if any, recognized in earnings are not part of the interest expense on the convertible debt.

Transition

The transition guidance described in the proposed FSP is confusing. We believe the Board should premise transition in the form of the fundamental concepts as follows:

- Outstanding registration payment arrangements as of the date of adoption should be recognized and measured under Statement 5 as of that date without consideration to information previous to that date;
- If a financial instrument, except for those originally issued together with a registration payment arrangement that was separately recognized and measured at fair value, was originally analyzed in combination with a registration payment arrangement, an entity



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should determine how it would have accounted for the financial instrument under applicable GAAP at the date of the instrument's issuance ignoring the effect of the registration payment arrangement and roll forward the revised accounting to the date of adoption; and

- Reverse, as of the date of adoption, the balances of the registration payment arrangements and related financial instruments previously recorded, except for those originally issued together with a registration payment arrangement that was separately recognized and measured at fair value, recognize the above amounts, and any differences should be accounted for as a cumulative effect adjustment to retained earnings.

Once the underlying concepts are explained, more detailed guidance can be provided for particular facts and circumstances as necessary.

Examples

Amounts allocated to a registration payment arrangement upon issuance of a convertible debt will have the effect of reducing the effective conversion price of the convertible debt and thereby increasing the likelihood that a beneficial conversion feature exists at the commitment date. We believe that an example that illustrates a situation where a beneficial conversion feature is present as a result of recording a Statement 5 obligation for a registration payment arrangement at issuance of a convertible security would be helpful.

We also recommend including a transition example (rather than a footnote reference to the applicable literature as currently done in paragraph A16 of the proposed FSP) of a situation where separation of an embedded conversion option would no longer be required as of the date of issuance of convertible debt when analyzed without the registration payment arrangement, but a beneficial conversion feature would exist.

Examples 7 and 8 indicate that the fair value of the entire arrangement (i.e. the warrant and the registration payment arrangement) at inception was \$100. However the description of the entry to be recorded upon adoption indicates that the warrant should be recorded at fair value by itself and the amount is also \$100. We believe that the technically correct description to the entry would be to indicate that the fair value of the entire arrangement should be ascribed to the warrant.



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Other

Certain registration payment arrangements may be within the scope of the proposed FSP as well as may be required to be accounted as a liability at fair value by paragraph 12 of Statement 150. The Board should include a scope exclusion for these types of contracts as an amendment to Statement 150.

If you have questions about our comments, please contact Enrique Tejerina at (212) 909-5530 or Mark Bielstein at (212) 909-5419.

Sincerely,

KPMG LLP