LEHMAN BROTHERS

October 15, 2007

Mr. Russell G. Golden
Director of Technical Application & Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116



LETTER OF COMMENT NO. $/ \mathcal{F}$

File Reference: Proposed FSP APB 14-a

Dear Mr. Golden,

Lehman Brothers appreciates the opportunity to comment on FSP ABP 14-a, Accounting for Convertible Debt Instruments That May Be Settled in Cash Upon Conversion (Including Partial Cash Settlements) (the "Proposed FSP"). We do not believe that such a significant amendment to APB Opinion No. 14, Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants ("ABP 14"), should be made through a FASB Staff Position (FSP) because the due process and related comment period associated with an FSP is more limited in scope than that required for a Statement of Financial Accounting Standards. In addition, and as explained more fully below:

- We do not support the proposed principle that requires separating the conversion option from a convertible debt instrument solely because it may be settled in cash (including partial cash settlement) upon conversion. We believe the economics of substantially all convertible debt instruments issued in the public markets are the same and therefore we believe that accounting for convertible debt instruments that settle in a fixed number of shares as well as those that permit or require the issuer to settle a portion of the if-converted value in cash (upon conversion) should be accounted for in the same manner.
- We believe a more comprehensive approach to accounting for equity-linked securities and derivatives is needed.
- We are also concerned about the effective date and transition rules of the Proposed FSP.

We recommend that the Proposed FSP not be issued or, failing that, we recommend the new rules be applicable only for instruments in existence at adoption date and those issued subsequently, and the effective date be changed to fiscal years beginning after December 15, 2008.

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In addition to the comments and concerns expressed in this letter, we have participated in the preparation of the comment letter submitted by the International Swaps and Derivatives Association and endorse the views and positions expressed in that letter.

A Comprehensive Approach is Needed

We believe that accounting for equity-linked securities and derivatives requires a comprehensive reassessment and we strongly recommend any change to the current accounting for such instruments to be undertaken comprehensively as part of the FASB's Liabilities and Equity project. We are concerned that without broad principles in place which can be used to address accounting for all equity-linked securities and derivatives there will be unforeseen consequences and inconsistent accounting for similar or like instruments. We are concerned that issuance of the Proposed FSP and discussion of other related issues (for example EITF Issue 07-5, Determining Whether an Instrument (or an Embedded Feature) Is Indexed to an Entity's Own Stock) is a piecemeal approach to setting generally accepted accounting principles ("GAAP"). As noted above, we do not believe making such a significant amendment to APB 14 in such a short time frame through an FSP is appropriate due process.

In addition, the Proposed FSP is not entirely in line with current IFRS accounting for convertibles and we believe this divergence needs to be comprehensively addressed.

Current Accounting is Correct

We believe that convertible debt instruments that, by their stated terms, may be settled in cash (or other assets) upon conversion, including partial cash settlement ("Net-Share Settled Converts") are within the scope of APB 14. The key analytical factor in APB 14 is the inseparability of the debt and conversion option. The fact that a holder of a Net-Share Settled Convert receives both cash and shares upon conversion does not mean that the debt and conversion option are separable. Inseparability is maintained with Net-Share Settled Converts because:

- The conversion option cannot be separated and traded.
- A holder of a Net-Share Settled Convert has two choices: (i) redeem the instrument prior to or at maturity for the principal amount, or (ii) convert the instrument. The holder can not settle the debt and equity components separately and at different times.
- Upon exercise of the conversion option, the convertible investor forgoes the benefits
 of redemption because regardless of the currency received, the investor gives up the
 right to future interest payments, has an equity claim in bankruptcy and receives only
 the value of the underlying shares.

The partial cash settlement upon conversion is not a repayment of the debt. A converting holder forever extinguishes the debt claim with no guaranty of receiving the par amount

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back because the holder only receives the value of the conversion shares, regardless of whether it is more or less than par.

We believe that current accounting for Net-Share Settled Converts is more accurate than the Proposed FSP's requirement that the debt and option components of a Net-Share Settled Convert be bifurcated. We believe the Proposed FSP's treatment would be inaccurate and potentially misleading in several respects:

- The proposed balance sheet treatment understates the debt claim since holders have a claim for the full par amount in bankruptcy. This understates leverage at a time when leverage has become an increasingly important tool for issuers and remains an important metric for investors in evaluating companies.
- Upon any early retirement of a Net-Share Settled Convert, under the Proposed FSP, the issuer would record a one-time loss equal to the difference between the fair value of the debt amount (calculated at the time of retirement) and the accreted debt value recorded on the balance sheet.
- The equity amount on the balance sheet would be overstated. Investors, rating
 agencies and regulators may not be able to easily distinguish between real equity and
 the phantom equity created by bifurcation. Issuers could either be penalized (via a
 lower return on equity) or benefited (through the ability to further increase leverage)
 by this phantom equity. Either way, the financial statements would not accurately
 reflect the economics of the transaction.

Separation Methodology

We do not agree with the method of separation in the Proposed FSP. We believe that the methodology for separating the debt and equity components is inconsistent with the way market participants price convertible bonds because it requires the issuer to disregard the terms of the embedded conversion option when determining the expected life and fair value of the debt component. The valuation of the separate bond and option components can be difficult and complex. Whether the debt or the option is first valued, assumptions must be made about things such as comparable debt rates (which can be difficult to determine for issuers without other debt outstanding) and volatility (which is a subjective determination with limited market benchmarks given the size and duration of most convertible instruments). Leaving aside the practical difficulties this may create for issuers, the complexity and subjectivity of different separation/valuation methodologies will make apples to apples comparisons of issuers with similar securities more difficult.

In addition, we believe the proposed separation methodology will increase the complexity and judgment required to properly apply the Proposed FSP and that is counter to FASB's stated intention of moving to principles-based accounting standards and reducing complexity when setting GAAP.

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In response to Question 1, we do not believe the proposed FSP would be easier to apply if separation were achieved by recording the embedded conversion feature at its fair value and then attributing the remaining proceeds to the liability component because we fundamentally disagree that separation is the correct accounting answer.

In response to Questions 2 and 3, we agree that inclusion of references to other applicable GAAP and the illustrative example in Appendix A both will aid in the understandability of the final FSP.

Fair Value Measurement

Paragraph 12 of the FSP indicates that Net-Share Settled Converts are not eligible for fair a value election in accordance with the scope exception in paragraph 8(f) of SFAS 159, The Fair Value Option of the Financial Assets and Financial Liabilities ("SFAS 159"). The majority of Net-Share Settled Converts are not issued with a beneficial conversion feature. In addition, the FASB's view is that Net-Share Settled Converts are akin to debt issued with separately detachable and exercisable warrants; therefore we believe the debt component of a Net-Share Settled Convert should be eligible for a fair value election. Failing that, given that paragraph 8(f) of SFAS 159 applies only to convertible bonds that contain a beneficial conversion feature; we believe the final FSP should provide the basis for not permitting a fair value election under SFAS 159.

Effective Date and Transition

The current proposal is the final FSP, which is to be issued in November or early December 2007, be effective for fiscal years beginning after December 15, 2007 and require retrospective application to all periods presented. Further, the Proposed FSP requires retrospective application to convertible debt instruments regardless of whether they still exist at adoption date or still permit cash settlement.

We believe there will be insufficient time for companies to assess the effects of the final FSP on existing convertibles and lending arrangements between when it is issued and the date it must be adopted. Many lending arrangements contain covenants/ratios based on the amount of debt on balance sheet and interest coverage ratios (which is typically calculated as GAAP income before interest and taxes / GAAP interest expense). We are seriously concerned that it may simply not be possible for many convertible issuers to be able to discuss with their lenders both technical breaches of covenants that occur due to retroactive application of the Proposed FSP as well as potential amendments to lending agreements. Even if there was sufficient time, in the current market environment many issuers will be reticent to have discussions with lenders regardless of whether the new accounting under the final FSP will lead to "better" ratios.

Further, issuers will be required to restate prior financials regardless of whether a convertible is still outstanding at the time the final FSP is adopted. This could lead to the unfortunate result that for convertibles that were modified after their original issuance

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date, but prior to the adoption of the new rules, a company must restate its financials based on historical data that may not be easily obtainable, for a security that no longer exists. These are not insignificant or isolated issues. There is currently over \$300 billion of convertible debt securities outstanding in the US market, of which approximately \$200 billion is impacted by the Proposed FSP because they require or permit cash settlement.

As noted above, we strongly recommend that the Proposed FSP not be issued or, failing that, we recommend the new rules be applicable only for instruments in existence at adoption date and those issued subsequently, and the effective date be changed to fiscal years beginning after December 15, 2008.

We appreciate the opportunity to submit our views and would be pleased to discuss our comments with you at your convenience.

Sincerely,

Edward S. Grieb

Managing Director and Financial Controller, Lehman Brothers Holdings Inc.