



Fitch Ratings

LETTER OF COMMENT NO. 25

One State Street Plaza
New York, NY 10004

T 212 908 0500 / 800 75 FITCH
www.fitchratings.com

October 15, 2007

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

File Reference: Proposed FSP APB 14-a
Accounting for Convertible Debt Instruments That May Be Settled in
Cash upon Conversion (Including Partial Cash Settlement)

Dear Mr. Golden:

We appreciate the opportunity to comment on the Financial Accounting Standards Board's (FASB or Board) Proposed Staff Position APB 14-a, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)*, (hereafter referred to as the "Proposed FSP"). Fitch has been a strong advocate of the FASB's and the International Accounting Standards Board's (IASB) efforts to achieve global convergence of accounting standards. We have concerns that implementation of the Proposed FSP prior to the completion of the liabilities and equity project of the joint Boards will add more confusion to an already complex area of accounting and not benefit the convergence process. We believe that the proposed accounting modification for these convertible debt instruments will also add undue complexity to the financial statements from a credit analysis perspective. Fixed income investors, creditors, and credit rating agencies focus primarily on the cash interest expense and the full, undiscounted value of the debt of the issuer. Should this proposal be adopted, we would encourage transparent disclosure requirements to ensure financial statement users, and in particular the very large number of fixed income investors and creditors, understand the nature of the balance sheet and non-cash income statement adjustments the Proposed FSP would require them to make.

Overview

Fitch Ratings (Fitch) is a leading global rating agency committed to providing the world's credit markets with independent, timely and prospective credit opinions. Fitch's corporate finance ratings make use of both qualitative and quantitative analyses to assess the business and financial risks of fixed-income issuers. Therefore, Fitch directly relies on

Fitch Ratings

the financial statements and that reliance places us in an informed position to comment on information we believe is useful and crucial in the credit evaluation process, which is a critical component of efficient capital markets.

Interim Changes to US GAAP

The accounting for convertible debt instruments has been modified by the FASB and its Emerging Issues Task Force a number of times in the past several years. The accounting complexity faced by issuers of these convertible debt instruments has resulted in a significant number of restatements. It has been widely reported that over 20% of all restatements in 2006 were the result of misclassification of liabilities and equity with many of these instances specifically related to beneficial conversion features.

Fitch appreciates the efforts being made by the FASB, together with the IASB, to address the distinction between liabilities and equity and understands that a discussion paper is expected on this project during the forth quarter of 2007. It does not make sense to us to be adjusting accounting for debt/equity instruments before the principles of establishing what is debt and what is equity are refreshed and clearly established.

Additionally, we understand that one of the main reasons for the Proposed FSP is to establish accounting for these instruments so that appropriate net income and earnings per share (EPS) measurements can be derived. Again this does not make sense to us. From the credit analyst perspective the Proposed FSP would be adjusting the financial statements in a way that is unhelpful to us in order to "fix" metrics that will no longer be required by the standards in the future anyway, according to the current direction of the FASB and the IASB joint Financial Statement Presentation Project.

We view the Proposed FSP as an interim fix to US GAAP for the convenience of equity investors at the inconvenience of credit investors. Ultimately, we expect that the two projects discussed above will yet again change the accounting and reporting for these convertible debt instruments. We question whether another interim fix to what is obviously a complicated and evolving area of accounting will best serve the users of financial information.

Credit Analyst Perspective

While we understand the argument for requiring that the issuer of a convertible debt instrument within its scope separately account for the liability and equity components in a manner that will reflect the entity's nonconvertible borrowing rate, Fitch credit analysts and other fixed income investors and creditors will often need to reverse the adjustments to the balance sheet and income statement required by the Proposed FSP in order to produce financial ratios that are relevant to creditors' interests.

Fitch Ratings

The Proposed FSP does not address the frequency with which instruments of this type become in-the-money, resulting in exercise of the conversion option, versus the frequency with which these instruments remain out-of-the-money and therefore are never exercised. Whenever the latter is the case, the cash interest expense is in fact a better representation of the cost of the instrument, and the stated principal is a better representation of the balance sheet value of the liability than the values that would result from application of the FSP. If the Proposed FSP is adopted, the FASB should explain why it is of greater importance to make the financial statements less accurate for those cases in which the instruments ultimately will not convert and perform in all regards like straight debt, albeit with a lower cash interest cost.

Should the Proposed FSP be adopted in its current form, credit analysts would have to reverse from the balance sheet the i) debt discount; ii) deferred tax liability; and iii) adjustments to additional paid-in capital for the equity component of the instrument and deferred taxes. Also, analysts will in most cases reverse from the income statement the non-cash portion of interest expense, net of any deferred tax provisions. For the periods during which these instruments are settled or extinguished, analysts may also reverse any gain or loss that was recorded as a result of changes in the fair value of the liability from the initial measurement date to the settlement or extinguishment date.

Thus, just about all of the adjustments required by this Proposed FSP would most likely be reversed as part of Fitch's credit analysis process.

Disclosure Requirements

Given how fragmented the guidance is for convertible debt instruments, we strongly believe that transparent disclosure requirements are critical for credit analysis.

There should be disclosure included in the footnotes to the financial statements of the par value along with carrying value of the convertible debt issuance.

An additional item that is of great interest to fixed income investors that is not addressed by the FSP is the potential value of the obligation if the convertible security is in the money at the time of its exercise; in the case of securities like Instrument C, the issuer may at its option settle the conversion spread above par with either shares or cash. A footnote disclosure of the value of the consideration in excess of par that would be owed at the date of the close of the financial statements would be helpful.

Since most of these convertible debt issues are long-term in nature, disclosing the amount that is allocated to additional paid-in capital only in the statement of stockholders' equity would result in the information being difficult to ascertain in later years. Therefore, there should also be disclosure *in the footnotes* as to how much of the issuance has been allocated to additional paid-in capital due to the imputed interest rate/ conversion feature.

Fitch Ratings

The footnotes should also include information regarding the income statement impact of the debt discount amortization under the proposed interest method. We suggest disclosures similar in nature to the requirements under the Reconciliation of the Statements of Comprehensive Income and Cash Flows being proposed in the Financial Statement Presentation Project. Our example below utilizes the assumptions and data from the implementation guidance (which we find useful) and is for “Year 1”:

(\$ 000)	Cash Interest	Amortization of Debt Discount	Pre-tax Income Statement Impact
Interest on Convertible Debt Issues	2,000	2,779	3,106

We will be happy to answer any questions on our comments and look forward to discussing these comments with the Board at the appropriate time.

Yours sincerely,

Ellen Lapson
Managing Director
Corporate Finance
Fitch Ratings
New York

Dina M. Maher
Senior Director
Credit Policy
Fitch Ratings
New York

Note: Fitch employs a methodology for allocating equity credit for hybrids and other capital securities, including convertible debt instruments. Equity credit is an analytical concept that expresses the extent to which Fitch views a security as containing debt-like or equity-like qualities in a risk-adjusted evaluation of an issuer’s capital structure and financial leverage. Securities like Instrument C are typically classified by Fitch as Class A (that is, allocated 100% to debt.) Thus, we consider Fitch’s adjustments for equity-like hybrids to be irrelevant to the matter in this letter.