

October 15, 2007

LETTER OF COMMENT NO. 54

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

Re: Proposed FASB Staff Position No. APB 14-a "Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)"

Sent by FAX to 203-849-9714 and mailed separately

Dear Technical Director:

We appreciate the opportunity to comment on proposed FASB Staff Position No. APB 14a "Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)" ("FSP No. APB 14a").

ON Semiconductor Corporation is a world-wide provider of power semiconductor devices with a market capitalization of approximately \$3.6 billion dollars. We have issued approximately \$839 million in convertible debt during the last three years to reduce our cash interest expense, all of which would fall under this proposed FSP No. APB 14a. We believe the current accounting treatment for convertible debt instruments that may be settled in cash upon conversion (including partial cash settlement) is sound and appropriate since such convertible debt is structurally different than traditional convertible debt. We believe the current accounting treatment appropriately captures the cash cost of the debt interest and the dilutive effect of potential share issuance over the life of the debt. We therefore do not support the issuance of this FSP that requires convertible debt instruments within the scope of FSP No. APB 14a to be separated into their liability and equity components at initial recognition by (a) recording the liability component at the fair value of a similar liability that does not have an associated equity component and (b) attributing the remaining proceeds from issuance to the equity component. Nor do we support separation by (a) recording the embedded conversion feature (equity component) at its fair value and (b) attributing the remaining proceeds from issuance to the liability component.

The sophisticated investing public predominately uses our financial statements to assess the cash flow capacity of the corporation and with it determine an implied enterprise valuation. The primary means to determine this has been to analyze the statement of operations since over a long period of time it should closely equal operating cash flows. FAS 123R and this proposed pronouncement would create charges in the statement of operations that would not affect operating cash flow which could be misunderstood by an unsophisticated financial statement user. About 50% of the analysts that follow our company pro-forma out the stock option expense from our statement of operations. We believe most analysts will want the information needed to proforma out the non-cash debt amortization related interest expense also. That only discourages the use of generally accepted accounting principle ("GAAP") based financial statements and encourages the use of pro-forma numbers. Our preliminary analysis indicates our GAAP net income would be reduced by about 15% with the adoption of this new pronouncement, which is more than triple the impact that FAS 123R had on our statement of operations. If this

pronouncement would take effect as planned, it will not allow us sufficient time to communicate these material accounting changes to all of our shareholders. An unsophisticated investor might interpret the reduction in income as one that should reduce the market valuation of the company even though the operating cash flows have not changed. We want to ensure the net income reduction caused by this pronouncement does not have a corresponding reduction of approximately \$500 million in our market capitalization. Therefore at a minimum, an adoption window of January 1, 2009 for calendar corporations we believe would be more in line with more recent pronouncements that had even less impact. There are several other pitfalls we would like to point out about the shortcomings of bifurcation accounting which include:

- Understatement of debt levels,
- Increasing leverage over the life of the convertible,
- Distortions in net income, earnings per share ("EPS") and return on equity ("ROE"),
- Subjectivity in determining the straight debt rate, credit spreads, volatility, and option duration.

## Recognition and Initial Measurement

We are not supportive of the recognition and initial measurement required by paragraphs 8 through 13 of the proposed FSP No. APB 14a for convertible debt within the scope of this FSP. Separately accounting for the liability and equity components of such convertible debt instruments would lead to significant understatement of debt levels and overstatement of equity levels prior to the expected maturity of the bond. By incorporating a net-share settlement feature in convertible debt, the issuer is taking on a permanent debt obligation on the par amount of a convertible bond. The issuer of such convertible debt does not have the flexibility to convert debt into equity (via a call exercise or at maturity) that an issuer of typical convertible debt has. This makes recognition of the par amount as debt on the balance sheet appropriate. The proposed accounting in this FSP will result in debt amounts on the balance sheet that do not reflect the true liability. We know of several debt issuers that would suddenly have positive equity or a 100% increase in equity value due to this proposed pronouncement. This FSP does not promote a conservative balance sheet, which will be problematic for rating agencies, the banking industry, and the investment community as it will foster variability in many standard metrics like enterprise value and return on equity calculations.

## Subsequent Measurement

We are not supportive of the subsequent measurement required by paragraphs 14 through 15 of this proposed FSP, which require the excess of the principal amount of the liability component over its initial fair value to be amortized to interest cost using the interest method. Over time, the interest cost recognized in subsequent periods that is accrued to the debt component results in debt levels that increase over time while in reality no additional debt is issued by the company. This will cause leverage ratios to be different over the life of the security and also lower than the true leverage ratios based on debt obligation recognized at par. Furthermore, the non-cash interest expense, also referred to as "phantom interest", causes distortions and volatility in reported net income, earnings per share and return on equity causing GAAP financial statements not to reflect the true economic reality of a company's operations.

## Impact to Earnings Per Share

The proposed FSP creates more questions than it answers with regard to the calculation of earnings per share for convertible debt within its scope. The proposed FSP does not address whether the impact to diluted earnings per share from such convertible debt should be calculated

by the treasury stock method or the if-converted method. Under current accounting treatment, the treasury stock method of determining the dilutive impact of convertible debt within the scope of this FSP is appropriate because the issuer of such debt is only obligated to issue stock for the value above par. Hence, the issuer will only issue stock in an amount by which the security is inthe-money. The accounting proposed in this FSP introduces a contradiction by negatively impacting the numerator of both basic and dilutive earnings per share through increased interest expense, but not allowing an add-back of interest expense under the treasury stock method that would otherwise be allowed for normal convertible debt under the if-converted method. In other words, not only is diluted earnings per share negatively impacted by the treasury stock method if the debt is in-the-money at the end of a period, but both basic and diluted earnings per share are also negatively impacted by phantom interest that will never be a cash charge and that would otherwise be added back to net income to calculate diluted earnings per share under the ifconverted method. In addition, under this proposal a straight debt issuance will be less dilutive than a net share settled convertible that is in the money because the interest expense and the stock dilution would be included in the earnings per share calculation. As a result, comparability of results will differ between issuers with different flavors of convertible debt and straight debt.

## Assumption Variability

There are many assumptions that can change the relative amount of the debt discount significantly namely the choice of the liability or equity option value methodology and assumptions like the expected life, the first call window, the volatility and the credit spread. Aggressive use or conservative use of these variables can lead to debt discounts that regularly vary by more than 5% of the debt face value. We have seen some cases where it can be as high as 18%. It is clear with this kind of variability; there will be reduced comparability and transparency. A well thought out adoption plan would help to reduce some but not all of the variability.

In summary, we would like to state our objection the proposed FSP No. APB 14a as it has the potential to infuse a high degree of subjectivity that would negatively affect comparability and transparency from the investor's point of view. If the proposal does get implemented, we would at a minimum request a later effective date in order to properly plan, execute and communicate the dramatic effect this would have on our financial statements.

We appreciate your consideration of our views and as you deliberate this FSP, feel free to contact me at 602-244-7362 if you have any questions or observations.

Sincerely.

Donald Colvin

Executive Vice President, Chief Financial Officer

ON Semiconductor Corporation.