



LETTER OF COMMENT NO. 35

Accountants and Management Consultants  
The US Member Firm of  
Grant Thornton International  
National Office  
175 West Jackson Blvd.  
Chicago, IL 60604-2615

Grant Thornton

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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

*Via E-Mail to director@fasb.org*

Re: File Reference Proposed FSP APB 14-a

Grant Thornton LLP appreciates the opportunity to comment on the proposed FASB Staff Position APB 14-a, "Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)."

We believe that the guidance in APB Opinion 14, *Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants*, does not properly reflect the economic effects of many convertible debt instruments that have recently been issued. Therefore, we support the Board's decision to address the accounting for certain of these instruments. In our view, the guidance in the proposed FSP will significantly improve the accounting for many existing convertible debt instruments that are currently accounted for under APB Opinion 14.

#### **Expansion of scope of proposed FSP**

Optimally, we would support a more comprehensive review of APB Opinion 14 that would consider recognition of an equity component associated with the conversion feature of all convertible debt instruments. We believe that approach would better reflect the economic effects of these instruments in an entity's financial statements and would result in more consistent treatment of the debt component in all convertible debt instruments. It would also align with the guidance in International Accounting Standards 32, *Financial Instruments: Presentation*.

We recognize that a comprehensive reconsideration of APB Opinion 14 would demand a significant amount of the Board's time and would deplete the resources invested in its liabilities and equity project. As an alternative, we think it is possible to broaden the scope of the proposed FSP to cover

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the vast majority of convertible debt instruments that are currently outstanding. We suggest that the Board expand the scope of the proposed FSP to include all convertible debt instruments other than conventional convertible debt instruments, as defined in EITF Issue.05-2, "The Meaning of 'Conventional Convertible Debt Instrument' in Issue No. 00-19."

By clarifying that only conventional convertible debt instruments containing "standard" antidilution provisions would meet the requirement in paragraph 3 of APB Opinion 14, the proposed FSP would allow the recognition of an equity component for the vast majority of convertible debt instruments that are currently outstanding. In our view, APB Opinion 14 currently provides a basis for this approach. For instance, paragraph 18 states that APB Opinion 14 is not meant to cover all convertible debt transactions, as follows:

The Board recognizes that it is not practicable in this Opinion to discuss all possible types of debt with conversion features, debt issued with stock purchase warrants, or debt securities with a combination of such features. Securities not explicitly discussed in this Opinion should be dealt with in accordance with the substance of the transaction. For example, when convertible debt is issued at a substantial premium, there is a presumption that such premium represents paid-in capital.

In addition, paragraph 3 states that convertible debt securities discussed in APB Opinion 14 are convertible at a specified price at the option of the holder and that the terms of such securities include "...a conversion price which does not decrease except pursuant to antidilution provisions." We believe that the proliferation of convertible debt instruments since the issuance of APB Opinion 14 requires further clarification about antidilution provisions. We also believe that EITF Issue 05-2 provides a definition of "standard" antidilution provisions that can be consistently applied in determining whether a conversion price does not decrease except pursuant to antidilution provisions.

## **Questions for respondents**

### ***Measurement***

Recognizing the fair value of the equity component is consistent with measurement criteria found elsewhere in generally accepted accounting principles (GAAP). We do not believe that valuation of the debt component will require sufficiently less effort than valuation of the equity component to justify using a measurement standard that is inconsistent with similar measurement standards for similar instruments that already exist in GAAP. For example, embedded conversion features that are accounted for under Statement 133, *Accounting for Derivative Instruments and Hedging Activities*, are recognized at the fair value of the equity component. Using the same measurement standard would result in consistent accounting for the debt component of instruments subject to Statement 133 and instruments subject to the proposed FSP.

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In addition, EITF Issue 06-6, "Debtor's Accounting for a Modification (or Exchange) of Convertible Debt Instruments," calls for measuring the changes in fair value of an embedded conversion option to determine whether a substantial change occurs in the terms of a debt instrument and to measure additional debt discount if the change in fair value of the embedded conversion option does not result in a substantial change in terms. EITF Issue 06-7, "Issuer's Accounting for a Previously Bifurcated Conversion Option in a Convertible Debt Instrument When the Conversion Option No Longer Meets the Bifurcation Criteria in FASB Statement No. 133," requires using the fair value of the embedded conversion option at the extinguishment date to measure the reacquisition of the equity component upon extinguishment of an instrument.

**References to GAAP**

The accounting guidance on convertible debt instruments is interspersed throughout existing accounting literature. Therefore, we believe it would help constituents if references to other applicable GAAP, such as guidance for modifications, are included in the final FSP.

**Illustrative example**

Because accounting for convertible debt instruments can be challenging, we suggest including the illustrative example in Appendix A in the final FSP, to help improve constituents' comprehension of these accounting practices.

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We appreciate the opportunity to comment on the proposed FSP and would be pleased to discuss our comments with Board members or the FASB staff. If you have any questions, please contact Joseph Graziano at (732) 516-5560 or Mark Scoles at (312) 602-8780.

Very truly yours,

/s/ Grant Thornton LLP