

**FASB Emerging Issues Task Force**

**Issue No.** 09-E

**Title:** Accounting for Stock Dividends, Including Distributions to Shareholders with Components of Stock and Cash

**Document:** Issue Summary No. 1, Supplement No. 1\*

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**Previously distributed EITF materials:** Issue Summary No. 1, dated August 26, 2009

**References:**

FASB Accounting Standards Codification Topic 250, *Accounting Changes and Error Corrections* (Topic 250)

FASB Accounting Standards Codification Topic 260, *Earnings per Share* (Topic 260)

FASB Accounting Standards Codification Topic 480, *Distinguishing Liabilities from Equity* (Topic 480)

FASB Accounting Standards Codification Topic 505, *Equity* (Topic 505)

FASB Accounting Standards Codification Topic 855, *Subsequent Events* (Topic 855)

FASB Statement No. 128, *Earnings per Share* (now under Topic 260) (Statement 128)

FASB Statement No. 165, *Subsequent Events* (now under Topic 855) (Statement 165)

AICPA Accounting Research Bulletin No. 43, *Restatement and Revision of Accounting Research Bulletins* (now under Topic 260 and Topic 505) (ARB 43)

IAS 33, *Earnings Per Share* (IAS 33)

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**\* The alternative views presented in this Issue Summary Supplement are for purposes of discussion by the EITF. No individual views are to be presumed to be acceptable or unacceptable applications of Generally Accepted Accounting Principles until the Task Force makes such a determination, exposes it for public comment, and it is ratified by the Board.**

## **Background**

1. At the September 9–10, 2009 EITF meeting, the Task Force reached consensus-for-exposure on this Issue and on September 23, 2009, the Board ratified those consensus-for-exposure and approved the issuance of a proposed Accounting Standards Update (proposed Update) for public comment. The proposed Update was posted to the website on September 30, 2009, with a comment period that ended on October 26, 2009. Four comment letters were received on the proposed Update and have been distributed to Task Force members. At the November 19, 2009 EITF meeting, the Task Force will have the opportunity to consider the comment letters and informal comments as it redeliberates the consensus-for-exposure. The Task Force will then be asked whether it agrees with the staff recommendations for the proposed changes to the amendments to the FASB Accounting Standards Codification<sup>TM</sup> (the Codification) to be included in the final Update and whether it would like to affirm its consensus-for-exposure (as amended) on this Issue as a final consensus.

## **Summary of Comment Letters Received and FASB Staff Analysis**

2. Four comment letters were received on the draft abstract, two from accounting firms and two from preparers. The staff also received several informal comments. The staff has identified and analyzed the significant comments in the sections that follow.

### ***Stock dividend versus share issuance***

3. All four comment letter respondents opposed the consensus-for-exposure that the stock portion of a distribution to shareholders that contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) should be considered a stock dividend. In their view, a distribution of stock and cash that allows shareholders the ability to select the form of the distribution with a limit on the amount of cash that will be distributed in total does not meet the definition of a stock dividend in the Codification because the proportional interest of each shareholder will not remain the same unless all shareholders make the same election. The respondents supported the alternative view presented in the proposed Update that such a distribution should be accounted for and included in EPS calculations as a share issuance. The following comment from an accounting firm (CL #4) is representative of the comments received:

We support the notion that the constant proportional interest measurement should be at the individual shareholder level. Accordingly, we believe that the stock portion of the distribution should not be considered a stock dividend for EPS purposes, but should rather be treated as a stock issuance.

4. Several respondents also expressed concern that accounting for these types of distributions as a stock dividend would unduly add to financial reporting complexity and would be confusing to investors and administratively burdensome to preparers. The following comment from a preparer (CL#3) is representative of such comments received:

Many REITs, such as Simon, have established a long history of paying quarterly distributions to their shareholders. Therefore, if the ED is passed as drafted, we would be restating our prior year historical quarterly amounts every quarter we report our results. We believe this would be burdensome and not provide meaningful disclosure. Moreover, we believe this would be confusing to investors and would serve to dilute the usefulness of the metric to the end users of our financial statements.

5. One comment letter respondent (CL#3) indicated that because a REIT is required to distribute at least 90 percent of its taxable income to its shareholders, the ability to pay out a portion of that amount in shares preserves cash and reduces the entity's borrowing costs. However, the benefit of the reduced borrowing costs is not reflected in earnings (and EPS) until the period in which the shares are issued. As a result, if EPS is retroactively restated for prior periods in which the required distribution was paid in cash with no reduction in borrowing costs, trends in EPS will show larger growth than if the distribution was accounted for as a share issuance. In the respondent's view, that result is "an 'artificial' growth that could lead investors to believe that the company's growth profile is actually stronger than it is in the underlying operations."

6. The FASB staff notes that concerns raised by respondents about this type of distribution not being proportionate for each individual shareholder were considered by the Task Force at the September EITF meeting and were documented in View A of Issue 1 in Issue Summary No. 1. However, some concerns raised by respondents, including the administrative burden to preparers and the effect of potential interest savings on EPS, were not previously considered by the Task

Force. As noted in the proposed Update, Task Force members who supported the consensus-for-exposure believe that the aggregate value of the distribution (in the form of stock, cash, or both) is distributed to each shareholder proportionately based on the shareholder's relative ownership interests. Because there is a limitation on the total amount of cash that will be distributed, those Task Force members view the shareholder elections of their preferred form of the distribution as an entity's distributing a fixed ratio of cash and shares for each share of stock and subsequently facilitating exchanges of cash and shares among the shareholders, rather than an entity's changing the relative ownership interests.

7. At the September EITF meeting, the Task Force was also provided with information about the FASB staff's outreach to investors. Investors that responded to the staff's inquiry generally indicated that they would prefer that EPS not be restated for this type of distribution. However, some concerns raised by respondents, including the administrative burden to preparers and the effect of potential interest savings on EPS, were not previously considered by the Task Force.

**Question 1 – Does the Task Force want to reconsider its consensus-for-exposure that the stock portion of a distribution to shareholders that contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) should be considered a stock dividend?**

8. If the Task Force decides that these types of distributions should be considered share issuances, the staff recommends the following amendments to the Codification (added text is underlined and deleted text is ~~struck out~~):

**505-20-15-3** The guidance in this Subtopic does not apply to the accounting for a distribution or issuance to shareholders of any of the following:

- a. Shares of another corporation held as an investment
- b. Shares of a different class
- c. Rights to subscribe for additional shares
- d. Shares of the same class in cases in which each shareholder is given an election to receive cash or shares, including cases in which there is a potential

limitation on the total amount of cash that all shareholders can elect to receive in the aggregate.

These proposed amendments would be in lieu of the amendments to Topic 505 and Topic 260 of the Codification included in the proposed Update.

***Portion of distribution accounted for and included in EPS calculations as a stock dividend***

9. One respondent disagreed with the Task Force consensus-for-exposure that only the minimum portion of the distribution that will be issued in shares should be accounted for and included in EPS calculations as a stock dividend. Under the consensus-for-exposure, if the cash available to be distributed is limited to 40 percent of the total value of the distribution, only 60 percent of the total value of that distribution would be considered a stock dividend. The remaining 40 percent of the total value of the distribution that is available to be distributed in cash would not be considered a stock dividend, even if fewer than 40 percent of shareholders elect to receive cash and, therefore, more than 60 percent of the distribution is in shares. That is because for 40 percent of the total value, the shareholder has the option to receive stock or cash.

10. The respondent who disagreed with that consensus-for-exposure expressed a view that if a distribution is required to be accounted for and included in EPS calculations as a stock dividend, the actual amount of the shares issued, not the minimum number that could be issued, should be accounted for as a stock dividend.

11. At the September meeting, one Task Force member noted that certain of these types of arrangements include clauses that allow entities to pay the entire dividend in cash if certain conditions are met (for example, if there is a significant change in the stock price). The Task Force did not discuss those types of clauses in detail but asked the FASB staff to research those types of arrangements further to determine whether there are attributes of those arrangements that could affect the Task Force's decisions.

12. The FASB staff subsequently received an informal comment indicating that entities that offer those types of distributions frequently reserve the right to distribute the entire dividend in cash or to increase the maximum amount that will be paid in cash at their discretion. For a REIT

to qualify for taxable dividend treatment under IRS Revenue Procedure 2008-68, any increase in the maximum amount that will be paid in cash by the entity would be required to be distributed proportionately to all shareholders electing to receive cash. That informal commenter questioned whether such an option would result in an entity concluding that the minimum portion of the distribution that will be paid in shares is zero, and therefore, any shares issued would be considered a share issuance. The FASB staff also received an informal comment that some entities might communicate to their shareholders that they retain the right to limit the portion of the dividend that will be paid in cash, but might not reach a final determination of the maximum amount (or communicate that maximum to the shareholders) until shortly before the dividend is paid.

13. The FASB staff reviewed filings of eight different entities that declared dividends in 2008 and 2009 that allowed shareholders to receive payment of the dividend all in cash or all in stock with a limit on the amount of cash that would be distributed. The review was not an exhaustive review of all of these types of distributions. For six of those transactions, the entities had the right to pay the entire dividend in cash or to increase the maximum amount of cash paid at their sole discretion. For two transactions, the entities did not have the sole discretion to increase the amount of cash paid, but if the payment of shares would cause a disqualification of the entity as a REIT (for example, if the distribution would result in a shareholder owning more than 9.9 percent of the total number of shares outstanding), the shareholder would receive cash to the extent required to ensure that the entity continued to qualify as a REIT.

**Question 2 – If the Task Force affirms its consensus-for-exposure that the stock portion of a distribution to shareholders that contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) should be considered a stock dividend, what portion of the distribution should be considered the stock portion and accounted for as a stock dividend?**

*View A: Only the minimum portion of the distribution that will be issued in shares should be accounted for and included in EPS calculations as a stock dividend. If there is an option to pay*

*the entire distribution in cash, the minimum portion of the distribution that will be issued in shares is zero and any shares issued should be considered a share issuance for EPS purposes.*

14. Proponents of View A believe that when a distribution to shareholders contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) only the minimum portion of the distribution that will be in shares should be considered a stock dividend. Those proponents believe that if an entity has an unconditional right to distribute the entire dividend in cash regardless of the elections made by the shareholders, the minimum portion of the distribution that will be in shares is zero.

15. Proponents of View A note that the only information that is known at the time the distribution is declared is the minimum amount of cash that will be distributed if enough shareholders elect to receive cash for that limit to be reached. However, the amount of cash that is actually distributed could be more or less depending on shareholder elections and the entity's actions. Shareholders have the ability to decrease the amount of cash distributed based on their elections and the entity has the ability to increase the amount of cash distributed. The entity may decide to pay the entire dividend in cash or to increase the amount of cash distributed based on shareholder elections. Because of the uncertainty involved, proponents of View A believe that these types of arrangements will not result in a proportional distribution of shares to shareholders and should not be considered a stock dividend. Instead, proponents of View A believe that any shares issued should be accounted for and included in EPS calculations as a share issuance and should not be retroactively reflected in EPS.

16. Opponents of View A note that the exception to stock dividend treatment in paragraph 505-20-13-5 relates to shareholders' rights to elect to receive a distribution in cash or shares not an entity's right to pay a dividend in shares or cash. Those opponents note that if an entity declares a 100 percent stock dividend and retains the right to pay the dividend in cash rather than shares but ultimately issues a 100 percent stock dividend, the distribution would be accounted for and included in EPS calculations as a stock dividend because the shareholder is not given the option to elect to receive cash or shares. Opponents of View A note that the option to pay cash does not

affect the stock dividend treatment in those situations and they do not believe an entity's option to pay additional cash in situations in which a distribution to shareholders contains components of cash and stock and allows shareholders to select their preferred form of the distribution should affect the treatment of the portion of the distribution that is paid in shares.

17. The FASB staff believes that a large percentage of distributions to shareholders that allow shareholders to select their preferred form of the distribution include a clause that gives the entity the right to make the entire distribution in cash. Therefore, if the Task Force decides that the stock portion of those types of distributions should not be considered a stock dividend, this Issue may only apply in limited situations.

*View B: Only the portion of the distribution that will be issued in shares if the maximum amount of cash that all shareholders have the option to receive is distributed should be accounted for and included in EPS calculations as a stock dividend.*

18. Proponents of View B believe that when a distribution to shareholders contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) an entity's ability to pay the entire distribution in cash should not affect whether the portion of the dividend that is issued in shares should be considered a stock dividend. Those proponents believe that the entity's right to pay the entire dividend in cash instead of shares is generally only a protective right that is included to ensure that the entity retains its REIT status or to protect the entity's share price.

19. Proponents of View B note that the entity has the right to distribute all cash prior to making the decision to allow shareholders to select their preferred form of distribution. The purpose of these arrangements is to allow a REIT to conserve cash while still meeting its obligations to distribute income. Therefore, it is unlikely that an entity would declare a distribution that would limit the amount of cash that would be distributed and then subsequently decide to distribute cash in excess of that amount. Proponents of View B note that because the Task Force reached a consensus-for-exposure that stock dividends should be retroactively reflected in EPS on the later of the ex-dividend date or the date the number of shares to be issued is known, only the shares

actually issued, if any, would be reflected as a stock dividend. Therefore, if there are situations in which an entity decides to pay the entire dividend in cash or increase the amount paid in cash, the entity would not be required to restate EPS.

20. Proponents of View B believe that this issue can be resolved by revising the words in the proposed Update to focus on the number of shares that would be issued if the maximum amount of cash that shareholders have the option to receive is distributed.

21. If the Task Force selects View B, the FASB staff recommends the following revisions to the amendments in the proposed Update (only the changes from the proposed Update are shown) (added text is underlined and deleted text is ~~struck out~~):

**505-20-05-3A** In certain situations, shareholders are given an election to receive their entire dividend distribution in either cash or shares of equivalent value, with a limitation placed on the total amount of cash that ~~will be distributed in the aggregate to~~ all shareholders can elect to receive in the aggregate (for example, the ~~total~~ amount of cash ~~available to be distributed that all shareholders can elect to receive in total~~ may be limited to 40 percent of the total distribution). If too many shareholders elect to receive cash, each shareholder electing to receive cash receives a pro rata amount of cash corresponding to its proportionate interest in the distribution. In those situations, although the proportional interest of each individual shareholder may not remain the same, the ~~minimum~~ portion of the distribution that will be issued in shares if the maximum amount of cash that all shareholders can elect to receive is distributed shall be accounted for and included in EPS calculations as a stock dividend. For example, if an entity with 1 million shares outstanding declares a \$10 per-share dividend to be issued in cash or shares at the election of the shareholder, but the total cash available to be distributed that all shareholders can elect to receive is limited to 40 percent (\$4 million) of the total value of the distribution, 60 percent (\$6 million in shares) of the total value of the distribution shall be considered a stock dividend. The remaining 40 percent of the distribution would be considered a cash dividend or stock issuance on the basis of the elections of the shareholders.

**505-20-15-3** The guidance in this Subtopic does not apply to the accounting for a distribution or issuance to shareholders of any of the following:

- a. Shares of another corporation held as an investment
- b. Shares of a different class
- c. Rights to subscribe for additional shares

d. Shares of the same class in cases in which each shareholder is given an election to receive cash or shares. However, if a limitation is placed on the total amount of cash available to be distributed in the aggregate to all shareholders can elect to receive in the aggregate, this Subtopic applies to the ~~minimum~~ portion of the distribution that will be issued in shares if the maximum amount of cash that all shareholders can elect to receive is distributed. For example, if the total cash available to be distributed that all shareholders can elect to receive is limited to 40 percent of the total value of the distribution, this Subtopic applies to the 60 percent of the total value of the distribution that will be distributed in shares unless the entity decides to increase the amount of cash paid, because each shareholder's option to receive greater than 40 percent in cash is contingent upon the outcome of elections made by other shareholders or the entity's discretion. This Subtopic does not apply to the 40 percent that may be distributed in cash at the shareholders' election, even if all or a portion of that amount is ultimately distributed in shares.

*View C: All shares that are ultimately issued when a distribution to shareholders contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) should be considered a stock dividend for EPS purposes.*

22. Proponents of View C agree with proponents of View B that when a distribution to shareholders contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) an entity's ability to pay the entire distribution in cash should not affect whether the portion of the dividend that is issued in shares should be considered a stock dividend. However, if shareholders do not elect to receive the maximum amount of cash available to be distributed, proponents of View C do not believe it is appropriate for a portion of the shares distributed to be accounted for as a stock dividend and a portion to be accounted for as a share issuance. Proponents of View C believe that because the number of shares to be issued is known at the time the stock dividend is recorded, all of the shares issued should be reflected as a stock dividend.

### ***Timing and diluted EPS guidance***

23. At the September meeting, the Task Force reached a consensus-for-exposure that an entity should reflect a stock dividend in EPS in its financial statements on the later of the ex-dividend

date or the date the number of shares to be issued is known. The Task Force decided that this guidance should not be limited to stock dividends described in Issue 1 but should apply to all stock dividends.

24. The Task Force also reached a consensus-for-exposure that for the stock dividend portion of a distribution to shareholders described in this Issue that has not yet been retroactively reflected in EPS for all periods presented, an entity shall not include the shares to be distributed in the computation of diluted EPS. The Task Force did not specifically discuss whether its decision related to the computation of diluted EPS should apply to all stock dividends. One informal commenter questioned why this guidance would not also apply to all other types of stock dividends.

25. Comment letter respondents generally agreed that an entity should reflect a stock dividend in EPS in its financial statements on the later of the ex-dividend date or the date the number of shares to be issued is known. However, as discussed above, those respondents did not agree that the stock portion of a distribution to shareholders that contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) should be considered a stock dividend.

26. Two of those respondents provided their views on how a distribution that is considered a share issuance should be reflected in EPS. One respondent (CL#1) indicated that because the distributions will be settled in a variable number of shares, the distributions should be recognized as a liability in accordance with the guidance in Topic 480 for distinguishing liabilities from equity. That respondent further indicated that the shares should be considered potentially issuable until paid and should be reflected in diluted EPS in accordance with the guidance in Topic 260 for how contracts that may be settled in stock or cash should be reflected in the computation of EPS. Another respondent (CL #3) indicated that shares issued in that manner should be included in EPS from the date of declaration (or ex-dividend date) because that is the date the entity is committed to issuing the shares. That respondent indicated that "[t]his is the date the company is committed to issuing the shares and though the final number is not yet

known at that date, it generally will be by the time the financial statements for the most recent period are issued."

27. The FASB staff received an informal comment recommending that the final consensus clarify that the number of shares that could be required to settle the portion of the dividend obligation in excess of the minimum cash portion but less than the maximum cash portion would be included in diluted EPS calculations pursuant to the guidance in paragraphs 260-10-45-45 (contracts that may be settled in stock or cash) and 45-48 (contingently issuable shares). The FASB staff observes that the consensus-for-exposure indicates that a stock dividend that has **not yet** been retroactively reflected in EPS should not be included in the computation of diluted EPS. Because the contingently issuable shares representing the portion of the dividend above the minimum cash amount and below the maximum cash amount will not be treated as a stock dividend and will not be retroactively included in EPS, the diluted EPS guidance in the consensus-for-exposure does not apply to those shares.

**Question 3 – Does the Task Force want to allow an entity to exclude the shares to be distributed in a stock dividend from the computation of diluted EPS when the dividend has not yet been retroactively reflected in EPS for all periods presented even if the distribution does not contain components of cash and stock and allows shareholders to select their preferred form of the distribution?**

*View A: Exclude the shares to be distributed in a stock dividend from the computation of diluted EPS when the dividend has not yet been retroactively reflected in EPS even if the distribution does not contain components of cash and stock and allows shareholders to select their preferred form of the distribution.*

28. Proponents of View A note that in a standard stock dividend, an entity declares a dividend of a certain number of shares (that is, the number of shares to be issued is known at the declaration date) and the period between the declaration date and ex-dividend date is fairly short. Therefore, the question about whether to include the shares in diluted EPS if the dividend has not yet been retroactively reflected in EPS generally would not apply to these types of dividends

because the entity would be required to retroactively adjust EPS shortly after the dividend was declared. The question would only apply if the number of shares to be issued in a stock dividend is not known (for example, if an entity declares a stock dividend of \$5 million to be paid in shares).

29. Proponents of View A believe that the Task Force decided to exclude from diluted EPS distributions that contain components of cash and stock and allow shareholders to select their preferred form of distribution because it would be burdensome for preparers and confusing to investors for the entity to include the shares in diluted EPS in one period and then retroactively adjust EPS for all periods presented to reflect the distribution in basic EPS. Proponents of View A believe that this same issue applies to other types of stock dividends for which the number of shares to be issued is not yet known and, therefore, the guidance should be extended to all stock dividends.

*View B: Do not exclude the shares to be distributed in a stock dividend from the computation of diluted EPS when the dividend has not yet been retroactively reflected in EPS if the distribution does not contain components of cash and stock and allows shareholders to select their preferred form of the distribution.*

30. Proponents of View B believe that if the number of shares to be issued in a stock dividend is not known, the dividend should be accounted for in accordance with the guidance for contingently issuable shares in Topic 260, which requires that shares whose issuance is contingent upon satisfaction of certain conditions be considered outstanding and included in the computation of diluted EPS. If all necessary conditions have not been satisfied by the end of the period, Topic 260 requires that the number of contingently issuable shares included in diluted EPS be based on the number of shares, if any, that would be issuable if the end of the reporting period were the end of the contingency period (for example, the number of shares that would be issuable based on current period earnings or the period-end market price) and if the result would be dilutive.

31. Proponents of View B believe that a special exception is being provided if a distribution contains components of cash and stock and allows shareholders to elect their preferred form of distribution because of the uncertainty surrounding shareholders' elections. However, in cases in which the number of shares to be issued is not known simply because the number of shares to be issued is dependent on the share price on a certain date, proponents of View B believe that the guidance in Topic 260 on contingently issuable shares should be applied.

**Question 4 – If the Task Force decides that the stock portion of a distribution to shareholders that contains components of cash and stock and allows shareholders to select their preferred form of the distribution (with a limit on the amount of cash that will be distributed in total) should be accounted for and included in EPS calculations as a share issuance, does the Task Force still want to provide guidance on the timing and, if the Task Force selects View A in Question 3, the dilutive effects of stock dividends?**

32. As noted in Issue Summary No. 1, currently there is diversity in practice on when a stock dividend is recorded. Some believe that a stock dividend should be reflected in EPS on the date the dividend is declared. Others believe that a stock dividend should be reflected in EPS when the trading price of the shares has been adjusted to reflect the effects of the stock dividend, which some believe is the record date while others believe it is the day after the distribution date.

#### ***Transition and Effective Date***

33. The Task Force consensus-for-exposure states that the amendments in the proposed Update would be effective for interim and annual periods ending on or after December, 15, 2009, and would be applied on a retrospective basis. One respondent recommended that the effective date be changed to the first reporting period beginning after March 15, 2010. The other three respondents, including the two preparer respondents indicated that the proposed effective date is operational. The FASB staff believes that entities should have the information readily available to apply this consensus immediately and recommends that the Task Force affirm its consensus-for-exposure.

**Question 5 – Does the Task Force want to affirm its consensus-for-exposure that the amendments in the proposed Update should be effective for interim and annual periods ending on or after December 15, 2009, and should be applied on a retrospective basis?**