

SEC Regulations Committee
October 14, 2008 - Joint Meeting with SEC Staff
SEC Offices – Washington DC

Discussion Document B

Topic: *Applying the Transition Provisions of FSP APB 14-1, “Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement).”*

Background: FSP APB 14-1, “Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)” (“FSP APB 14-1” or “the FSP”) addresses the accounting for convertible debt instruments that, by their terms, may be settled in cash or other assets upon conversion, including partial cash settlement. The FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years.

As adopted, FSP APB 14-1 requires retrospective application to all periods presented for instruments within its scope that were outstanding during any of the periods that will be presented in the annual financial statements for the period of adoption. Paragraph 36 states,

The guidance in this FSP shall not be applied retrospectively to instruments within its scope that were not outstanding during **any** of the periods that will be presented in the annual financial statements for the period of adoption but were outstanding during an earlier period. Therefore, an entity shall not reclassify amounts between its opening equity accounts in those circumstances.

The cumulative effect of the change in accounting principle on periods prior to those presented is recognized as of the beginning of the earliest period presented with an offsetting adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets).

Questions have been raised about how the transition provisions apply to an SEC registrant. In Form 10-K, an SEC registrant must present three years of comparative income statements and two years of comparative balance sheets (for a smaller reporting company, two years of comparative income statements and balance sheets). In addition, the Form 10-K of an SEC registrant that is not a smaller reporting company must include a table of selected financial data for the past five years (or an even longer period at the registrant’s option).

The Committee requests that the SEC staff provide clarification on whether the FSP applies retroactively to instruments outstanding at anytime during the period covered by the audited financial statements, or to instruments outstanding at anytime during the period covered by the table of selected financial data?

Staff Response: The SEC staff indicated that they generally expect all periods presented in the selected financial data to be presented on basis consistent with the annual financial statements. For example, if a company adopts a new accounting standard that requires retroactive application or disposes of a business that is accounted for as a discontinued operation, the staff will expect the years prior to the annual financial statements – generally years 4 and 5 - to be presented on the same basis as the annual financial statements. However, given the unique transition guidance in FSP APB 14-1, which should not be analogized to other situations, the SEC staff indicated that it will not object to either of the following transition elections:

- Alternative A: A registrant may apply the FSP to those instruments that were outstanding during the periods presented in the annual financial statements that will be included in its

Form 10-K (e.g., two years for a smaller reporting company or three years for any other SEC registrant).

- Alternative B: A registrant may apply the FSP to those instruments that were outstanding during the annual periods that will be presented in the selected financial data table in its Form 10-K (e.g., the past five years required to be presented or such longer period as the registrant elects to present in the table).

In either case, if material, the SEC staff expects the notes to the financial statements to disclose how the registrant has adopted the transition provisions of the FSP.

To the extent a registrant elects Alternative A, the company should disclose that the selected financial data for the earlier periods is not comparable to the periods for which the audited financial statements are provided.