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EITF Roundup

Audit and Enterprise Risk Services

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This issue of *EITF Roundup* covers the March 17, 2005, meeting of the Emerging Issues Task Force (EITF or the "Task Force"). EITF consensuses are not final until ratified by the Financial Accounting Standards Board (FASB). Official EITF minutes are posted to the Deloitte Accounting Research Tool (DART) Web site. EITF meeting materials distributed to the Task Force prior to the meeting and final meeting minutes are available on the FASB's Web site.

The Task Force discussed the following topics:

Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights"

STATUS: Tentative Conclusion Reached

IMPACT: All companies that serve as a general partner in limited partnerships, especially real estate and investment limited partnerships and managing members of limited liability companies governed like partnerships. A consensus would not apply if the partnership or similar entity is a variable interest entity (VIE) accounted for under FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*.

NEXT STEPS: Further discussion and a final consensus expected at the June meeting.

Little accounting guidance exists in determining when a general partner (GP) should or should not consolidate a limited partnership. AICPA Statement of Position 78-9, *Accounting for Investments in Real Estate Ventures*, provides specific guidance for investments in real estate limited partnerships, but investors in other types of partnerships have analogized to this guidance. SOP 78-9 provides that a GP should not consolidate a limited

partnership if limited partners (LPs) have certain "important rights." Issue 04-5 was added to the agenda due to inconsistent application by GPs when determining whether to consolidate a limited partnership.

A limited partnership is formed by one or more GPs and one or more LPs. Under partnership law, a typical LP is not liable for the obligations of a limited partnership (unless it is also a GP) because of limitations on the LP's participation in the operations of the limited partnership. In contrast, a GP generally has wide discretion over partnership operations and often is liable for its obligations.

Under GAAP, when an entity controls another entity, it is usually the accounting parent of the controlled entity. Thus, the GP's wide discretion in the operations of the partnership often constitutes **control**, and could make a sole GP the accounting parent of a limited partnership, requiring consolidation.[1]

Nonetheless, many GPs do not consolidate their limited partnerships, because the limited partners have **kick-out rights**, provisions in the partnership agreement under which the limited partners can remove the general partner. The percent of limited partner support needed to exercise kick-out rights vary from partnership to partnership, as do other key rights held by the limited and general partners.

At the March meeting, the Task Force considered constituent comments received on a draft abstract proposed at the November meeting. The Task Force reached a tentative conclusion that a general partner group of a limited partnership **is presumed to control the limited partnership**, unless either (both of these rights are discussed in detail below):

1. The limited partners have the substantive ability to dissolve[2] (liquidate) the limited partnership or otherwise remove the general partner (kick-out rights) without cause,[3] or
2. The limited partners have "substantive participating rights."

The Task Force believes the presumption of control by the GP(s) is appropriate because the consolidation-based-on-control model under GAAP typically requires a company, which controls the resources of another entity to consolidate that entity — even if the parent's economic interest is small. As discussed above, the nature of a limited partnership is such that the GP appears to have the control rights of the limited partnership.

Example 1

A limited partnership (a non-VIE) is established by three LPs (each owning 33 percent) and a one percent GP. The GP manages the partnership and makes all decisions. The LPs do not have the substantive ability to dissolve (liquidate) the limited partnership. In addition, the LPs have no rights to participate in the decisions or initiate actions of the limited partnership.

The GP would not overcome the presumption of control because the LPs do not have either of the rights required by Issue 04-5. Therefore, the GP should include in its consolidated financial statements the assets, liabilities, and revenues and expenses of the limited partnership. The LP's rights to the profits and losses of the partnership would be recorded as minority interest in the consolidated statements of the GP in accordance with Accounting Research Bulletin (ARB) No. 51, *Consolidated Financial Statements*.

1. Substantive Kick-Out Rights

The Task Force discussed comment letters questioning the threshold needed to determine whether limited partner kick-out rights are substantive. The Task Force considered the following alternatives:

[1] A different accounting analysis applies if the partnership is a variable interest entity (VIE) under Interpretation 46(R). Issue 04-5 does not apply to partnerships that are VIEs.

[2] The limited partners' unilateral right to withdraw from the partnership in whole or in part (withdrawal right) that does not require dissolution or liquidation of the entire limited partnership would not overcome the presumption that general partners control the limited partnership (that is, the withdrawal right is not deemed to be a kick-out right).

[3] *Without cause* means that no reason need be given for the dissolution (liquidation) of the limited partnership or removal of the general partner. *With cause* generally restricts the limited partners' ability to dissolve (liquidate) the limited partnership or remove the general partner in situations that include, but that would not be limited to, fraud, illegal acts, gross negligence, and bankruptcy of the general partner.

- View A — A simple majority (or a lower percentage) of the limited partnership voting interests are needed to exercise kick-out rights. These rights must be held by limited partners other than the general partner(s), entities under common control with the general partner(s), or other parties acting on behalf of the general partner(s).
- View B — A super majority of the limited partnership voting interests are needed to exercise kick-out rights (e.g., 66 2/3 percent of the limited partners would need to vote to exercise the kick-out right) for it to be substantive.
- View C — Kick-out rights must be able to be exercised upon a **reasonable vote** of the limited partners.

The Task Force concluded that limited partner kick-out rights are substantive (thus overcoming the presumption of control by the GP) if the limited partners can dissolve (liquidate) the entity or remove the general partner(s) by a vote of **a simple majority** (or a lower percentage) of the interests held by the limited partners other than the general partner(s) (View A). For these rights to be substantive, limited partners cannot face barriers to the exercise of the rights (see paragraph B20(b) of Interpretation 46(R)).

Example 2

A limited partnership (a non-VIE) is established by 99 LPs (each with a one percent interest) and a one percent GP. The GP manages the partners. The LPs have the ability to remove the GP by a vote of 66 2/3 percent of the LPs; however, they have no rights to participate in the decisions or initiate actions of the limited partnership.

The GP **could not overcome the presumption of control** because the LPs do not have either of the rights required by Issue 04-5. The LPs have kick-out rights; however, the right is not substantive because greater than a simple majority vote of the LPs is required for removal of the GP. See proposed transition below for guidance on when the GP may need to change these rights if they wish to avoid consolidation.

Example 3

A limited partnership (a non-VIE) is established by two LPs and a one percent GP. The GP manages the partnership and makes all decisions. The LPs have the ability to remove the general partner by a simple majority vote of the LPs; however, they have no rights to participate in the decisions or initiate actions of the limited partnership.

The GP **would overcome the presumption of control** because the LPs have substantive kick-out rights. That is, even though there are only two LPs (indicating that currently all of the limited partners would have to vote to kick the GP out), the right is substantive because it only requires a simple majority vote.

2. Substantive Participating Rights

A GP may not control a limited partnership even if kick-out rights do not exist or lack substance. Control depends on an analysis of other important rights that the LPs may have.

Virtually the same question was posed (in the context of corporate entities) in the deliberations of Issue No. 96-16, "Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights." The issue discussed when rights held by minority investors in a corporation were sufficiently significant that a majority investor would not consolidate. Participating rights, as defined in Issue 96-16, preclude consolidation by the majority investor, while protective rights do not.

In its deliberations of Issue 04-5, the Task Force concluded that there should not be substantive differences between limited partnerships and corporations for purposes of determining consolidation by a GP (Issue 04-5) or a majority investor (Issue 96-16). Participating rights, precluding consolidation by the GP, are those that provide the limited partners with the right to participate effectively in significant decisions that would be expected to be made in the ordinary course of the limited partnership's business. Protective rights, which do not preclude consolidation by the GP, might be used to forestall decisions that put the LPs' interest in jeopardy; however, these decisions would not be expected to be made in the ordinary course of business.

The following list, not all-inclusive, illustrates participating rights:

- Selecting, terminating, and setting the compensation of management responsible for implementing the limited partnership's policies and procedures.

- Establishing operating policies and making capital decisions of the limited partnership, including budgets, in the ordinary course of business.

The Task Force also agreed that the LPs' ability to block acquisitions and dispositions of assets may be protective or participating based on facts and circumstances. Issue 96-16 established a 20 percent limit (approval requirements above 20 percent of the fair value of the partnership's assets are classified as protective).

Editor's Note: Many GPs will seek amendments to partnership agreements to avoid consolidation after Issue 04-5 is effective. It may be more practical to achieve this outcome by creating substantive kick-out provisions rather than granting participating rights to LPs. True participating rights need to be evaluated carefully to determine that they do not jeopardize the LPs' limited liability status.

If the EITF reaches a final consensus and it is ratified by the FASB (actions expected at their respective June meetings), Issue 04-5 would be effective immediately following ratification for all **new** limited partnership agreements and for pre-existing limited partnership agreements that are **modified**.

For pre-existing limited partnership agreements that are not modified, Issue 04-5 would be effective in fiscal years beginning after December 15, 2005. Preparers can choose one of the following two methods for transition:

- Method A — Record the cumulative effect, if any, at the beginning of the period in which Issue 04-5 is first applied.
- Method B — Restate prior period financial statements.

Further discussion of this Issue is expected to occur at the June EITF meeting to (1) reaffirm its tentative conclusion and (2) consider conforming changes to Issue 96-16 to remove the 20 percent "bright-line" regarding LP approval of asset acquisitions and dispositions. The FASB staff is planning to draft a proposed change to Issue 96-16 and post it to its Web site for public comment.

Note: The FASB has proposed changes to SOP 78-9 through an FSP.[4] The FSP will ensure that SOP 78-9 and Issue 04-5 conform their guidance on the rights of limited partners that preclude consolidation by a general partner.

Issue No. 04-6, "Accounting for Stripping Costs in the Mining Industry"

STATUS: Final Consensus Reached

IMPACT: Mining enterprises that capitalize post-production stripping costs or expense these costs as incurred.

NEXT STEPS: FASB ratification expected in March.

Mining companies incur costs to remove overburden and other mine waste material (referred to as stripping costs) in order to access mineral deposits. During the development stage of a mine (before production begins), these costs are capitalized as part of the cost of the mine and frequently are amortized over the productive life of the mine using the units of production method.

Once production begins, should ongoing stripping costs be expensed or capitalized? Conceptually, stripping costs may benefit both current period production (because removal of the waste is necessary to extract the material mined in the current period), as well as future periods (because the costs facilitate access to additional minerals to be mined in the future). Currently, most mining companies expense stripping costs as incurred or capitalize and attribute the costs based on a "life of mine stripping ratio."[5]

[4] Proposed FASB Staff Position (FSP) No. SOP 78-9-a, "Interaction of AICPA Statement of Position 78-9, *Accounting for Investments in Real Estate Ventures*, and EITF Issue No. 04-5, 'Investor's Accounting for an Investment in a Limited Partnership When the Investor Is the Sole General Partner and the Limited Partners Have Certain Rights,'" amends paragraphs 7 and 9 of SOP 78-9 to provide guidance consistent with Issue 04-5 to determine when a general partner group does not control a limited partnership. Discussion of this FSP has been delayed until Issue 04-5 is finalized in June; it is expected to have the same effective date and transition as Issue 04-5.

[5] The life of mine stripping ratio is the predominant method of attribution used by mining companies that capitalize their stripping costs incurred during production. Unlike the units of production method which can make the minerals extracted in later periods bear a disproportionately large amount of stripping costs, the life of mine striping ratio results in a more consistent amount of stripping costs being allocated to each unit of reserves extracted.

At previous meetings, the Task Force reached a tentative conclusion that stripping costs incurred during production are mine-development costs that should be capitalized as an investment in the mine. Further, the costs should be attributed to proved and probable reserves in a systematic and rational manner.

At the March meeting, the Task Force reversed its previous conclusions; it reached a consensus that stripping costs incurred during production are **variable production costs** that should be considered a **component of inventory** in each period. That is, production stripping costs incurred in a given period should be associated with the activities of that period, without consideration of future potential benefits. For mining companies that keep relatively little mineral inventory on hand at the end of a financial reporting period, the consensus effectively requires them to expense the bulk of each period's stripping costs. Why? Because only a minor amount of current period stripping costs will be associated with period-end inventory.

This guidance is effective for financial statements issued for fiscal years beginning after December 15, 2005, with early adoption permitted. Entities will recognize the cumulative effect of initially applying this consensus in a manner similar to APB Opinion No. 20, *Accounting Changes* (pro-forma disclosures of the effect on previous financial statements would not be required). Restatement of previously issued financial statements is permitted.

No further discussion of this Issue is expected.

Issue No. 04-7, "Determining Whether an Interest Is a Variable Interest in a Potential Variable Interest Entity"

STATUS: Unable to reach a consensus. See Next Steps.

IMPACT: Many companies who are counterparties on forward contracts or forward-like derivative contracts with variable interest entities (VIEs), including financial entities, operating entities, and securitization vehicles that are not qualifying special-purpose entities (QSPEs). Also, the Issue may affect the accounting analysis of potential VIEs without forward or derivative contracts.

NEXT STEPS: FASB to consider whether to address the topic. If so, the EITF would drop the Issue from its agenda.

This Issue was added to the agenda due to inconsistent methods used to identify whether certain derivatives or forward contracts are variable interests under Interpretation 46(R). The issue is important; if a contract is not a variable interest, then the VIE's counterparty to the contract cannot be the primary beneficiary. Derivative dealers, particularly, are interested in the issue because of the large size of their derivative portfolios.

Under Interpretation 46(R), variability is the measure of the risks and rewards associated with a VIE. Interpretation 46(R) provides that contracts that create variability are not variable interests and contracts that absorb variability are variable interests. However, a derivative or forward contract can be viewed as both creating and absorbing variability. The issue is how risks should be evaluated in determining whether the contract or instrument is absorbing variability, and thus, is a variable interest.

The Task Force has discussed two fundamental approaches in determining whether an instrument is a variable interest:

- Fair Value — Based on whether the interest absorbs variability in the **fair value** of the net assets of an entity. This approach, for example, causes a **fixed rate** debt instrument issued by the potential VIE to absorb variability based on the fact that changes in interest rates cause the debt to change in fair value.
- Cash Flow — Based on whether the interest absorbs variability in the **cash flows** of an entity. This approach, for example, causes a **variable rate** debt instrument potentially to absorb variability based on its receipt of interest.

At the November meeting, the Task Force agreed, in general, that an enterprise should determine the predominant variability based solely on the **nature of the operations of the VIE**. That is, there is a **presumption** that (1) the cash flow approach should be applied for an "operating" entity, and (2) the fair value approach should be applied for a "financial" entity. The Task Force instructed the FASB staff and the Working Group to develop further this "Presumption Approach."

At the March meeting, the Task Force discussed the Presumption Approach and a second approach based on selected risks. Each is discussed below.

- Presumption Approach (summarized above) — The discussion also included under what conditions an entity might overcome the presumption — "in circumstances in which the application of the presumed method results in the consideration of variability that the potential VIE was not *clearly designed* to be exposed to."

- Risk Approach — Focuses on the variability that disproportionately affects and creates significant risk(s) to the entity's subordinated interest(s) holders. This approach excludes any other risk from the analysis (usually, interest rate risk). The risk approach avoids a possible conclusion that a senior interest holder should consolidate an entity due to interest rate risk. This conclusion might be reached if entity-wide interest rate risk was larger than other risks to which the VIE is exposed (e.g., credit risk). Since senior interests can be large in relation to subordinated interests, a senior interest holder could be viewed as the primary beneficiary of the VIE. Some believe that this result is illogical and inconsistent with the aim of Interpretation 46(R).

The Task Force could not reach agreement on either approach, with some members expressing the view that Interpretation 46(R) does not appear to support explicitly the exclusion of certain risks (an element of both approaches). As a result, the Task Force recommended that the FASB deal with the issue. If so, the EITF will drop Issue 04-7 from its agenda.

Issue No. 04-13, "Accounting for Purchases and Sales of Inventory With the Same Counterparty"

STATUS: Tentative Conclusion Reached

IMPACT: Companies that (1) maintain finished goods inventories and (2) buy and sell (or exchange) inventories with the same counterparty.

NEXT STEPS: Additional Discussion at a Future Meeting.

An entity may buy and sell inventory from (to) another entity that operates in the same line of business. The purchase and sale transactions may be documented as a single contractual arrangement (e.g., an inventory exchange) or documented in separate contractual arrangements. While this inventory practice is common in the oil and gas industry (e.g., oil for oil swaps), similar inventory issues arise in many industries. The inventory purchased or sold may consist of raw materials, work-in-process, or finished goods. The following questions have been raised regarding the accounting:

- Under what circumstances should two or more transactions with the same counterparty (counterparties) be viewed as a single nonmonetary transaction within the scope of APB Opinion No. 29, *Accounting for Nonmonetary Transactions*?
- If nonmonetary transactions within the scope of Opinion 29 involve inventory, are there any circumstances under which the transactions should be recognized at fair value rather than at recorded amounts?

At the March meeting, the Task Force discussed the second question. Opinion 29 requires that the accounting for a nonmonetary exchange that **essentially** is not the **culmination of an earning process** be based on the recorded amount of the nonmonetary asset relinquished. Paragraph 21(a) of Opinion 29 states, in part, that the following nonmonetary exchange transaction does not culminate an earning process:

> "An exchange of a product . . . **held for sale** in the ordinary course of business for a product . . . **to be sold** in the same line of business to **facilitate sales** to customers other than the parties to the exchange" [Emphasis added]

FASB Statement No. 153, *Exchanges of Nonmonetary Assets*, recently amended Opinion 29; however, paragraph 20(b) of Statement 153 carries forward the guidance cited above.

The Task Force considered the following alternatives:

- View A — There are no circumstances under which exchanges of inventory within the same line of business should be recognized at fair value.
- View B — A company should recognize an exchange of finished goods for raw material/work-in-process within the same line of business at fair value.
- View C — All nonmonetary exchanges of inventory should be recognized at fair value if fair value is determinable and the transaction has commercial substance.

The Task Force reached a tentative conclusion on View B — exchanges of inventory in the same line of business should be accounted for as shown in the following table.

Sold	Received		
	Raw Material	Work-in-Process	Finished Good
Raw Material	Recorded amount	Recorded amount	Recorded amount
Work-in-Process	Recorded amount	Recorded amount	Recorded amount
Finished Good	Fair value*	Fair value*	Recorded amount

* The other requirements of paragraph 20 of Opinion 29, as amended by Statement 153, also must be considered in order to record a nonmonetary transaction at fair value: fair value must be determinable within reasonable limits and the transaction must have commercial substance. Further, the Task Force observed that this Issue does not address whether these transactions qualify for revenue recognition.

The basis of the tentative conclusion is that a company that gives up a finished good in return for a component of producing inventory (i.e., raw materials or work-in-process) has culminated the earning process. As the inventory classification is critical to the application of the tentative conclusion, the EITF considered whether further guidance on classification should be included in the Issue. However, the Task Force concluded that a company should use its own entity-specific criteria to classify inventory for financial reporting purposes in accordance with Accounting Research Bulletin No. 43, Chapter 4, "Inventory Pricing." SEC Regulation S-X, Rule 5-02, "Balance Sheets," requires public companies to disclose their inventory classification.

At the June 2005 EITF meeting, the Task Force will revisit this tentative conclusion. It will also discuss the complex question of when two or more inventory transactions with the same counterparty should be viewed as a single nonmonetary transaction.

Issue No. 05-1, "The Accounting for the Conversion of an Instrument That Becomes Convertible Upon the Issuer's Exercise of a Call Option"

STATUS: Tentative Conclusion Reached

IMPACT: Issuers of contingently convertible debt instruments and other issuers of instruments that can become convertible upon the exercise of a call option.

NEXT STEPS: Additional discussion at a future meeting, and consideration of the earnings per share (EPS) effects of the tentative conclusion.

Issue No. 04-8, "The Effect of Contingently Convertible Instruments on Diluted Earnings per Share," required contingently convertible instruments (CoCos) to be included in diluted earnings per share regardless of whether the contingency had been met. An example of a CoCo follows:

On January 1, 2005, Company B (B) issues a CoCo for $1,000. The instrument is convertible into 10 shares of B's underlying common stock (implying a conversion price of $100). However, the investor does not have the right to convert unless the market price of the issuer's stock exceeds $120 for a specified consecutive number of days.

In addition to being convertible once the market price contingency has been met, the instrument includes a provision that allows B (the issuer) to call the CoCo anytime between 2009 and the maturity date. If B exercises the call, the holder has the option to receive cash of $1,000 as settlement of the debt or receive 10 shares. Accrued interest is ignored for purposes of this example.

This Issue addresses the accounting if B calls the CoCo when, absent the call, it cannot otherwise be converted (i.e., the market price contingency has not been met) and the holder elects to receive the 10 shares. For example, B calls the CoCo and the holder elects to receive shares when the stock price is $110 per share. APB Opinion No. 14, *Accounting for Convertible Debt and Debt Issued With Stock Purchase Warrants*, specifically does not address the complex convertible instruments that currently exist.

Note: This Issue also applies to instruments other than CoCos (e.g., an instrument that is never convertible except when the issuer exercises its call option).

At the March meeting, the Task Force considered the following views:

- View A — Account for conversion of the instrument in the same way as other conversions of a convertible instrument under Opinion 14. That is, the carrying amount of the debt should be credited to equity and no gain or loss would be recognized.
- View B — Account for conversion of the instrument as an induced conversion under FASB Statement No. 84, *Induced Conversions of Convertible Debt*.
- View C — Account for conversion of the instrument as a debt extinguishment under APB Opinion No. 26, *Early Extinguishment of Debt*. That is, on the date the holder converts the instrument, a gain or loss should be calculated as the difference between the carrying amount of the debt and the fair value of the stock issued. In the example above, B would recognize an extinguishment loss of $100 [$1,100 of stock issued (10 shares × $110) less $1,000 carrying value of debt].

The Task Force reached a tentative conclusion that no gain or loss should be recognized (View A) because the conversion is pursuant to the instrument's original terms, which provided for the possibility that an issuer will exercise its call option. However, certain Task Force members expressed a different view — the conversion right, while contemplated in the original terms of the instrument, does not exist until the issuer calls; therefore, value is being conveyed to the issuer and should be accounted for as an early extinguishment of debt (View C).

The SEC observer expressed concern about whether the EPS treatment would be consistent with View A. View A appears to rest on the conclusion that the instrument is always a convertible instrument regardless of the outcome of the contingency. While the EITF has resolved the EPS issue for CoCos (Issue 04-8 states that the CoCos always should be considered in the calculation of diluted EPS regardless of the market price of the stock), the EPS treatment should be ironed out in the context of other instruments (e.g., an instrument that is only convertible upon an issuer call).

Some FASB Board members also were skeptical about the tentative conclusion, expressing that it might be an unwarranted expansion of the scope of Opinion 14. Further discussion of this Issue is expected at a future meeting.

Agenda Committee Report

Added to EITF Agenda for discussion at a future meeting — The Effect of Registration Rights With Liquidated Damages Provisions for Financial Instruments Subject to EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock"

The issuance of a registration rights agreement that includes a liquidated damages clause is a relatively common occurrence when equity instruments, stock purchase warrants, and financial instruments that are convertible into equity securities are issued. Typically, the agreement requires the issuer to use its "best efforts" to file a registration statement (for the resale of equity instruments, shares of stock underlying a stock purchase warrant, or a convertible financial instrument) and have it declared effective by the end of a specified grace period. If the issuer fails to have the registration statement declared effective within the grace period (or, as the case may be, if effectiveness is not maintained), the issuer is required to pay liquidated damages to the investor each month until the registration statement is declared effective.

Should the registration rights agreement cause the issuer to account for the instrument (e.g., a stock purchase warrant) as a liability rather than equity under the provisions of Issue 00-19?

Added to EITF Agenda for discussion at a future meeting — The Meaning of "Conventional Convertible Debt Instrument" in EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock"

Issue 00-19 is used (among other purposes) to evaluate whether an issuer is required to bifurcate a conversion option that is embedded in convertible debt under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended. Paragraph 4 of Issue 00-19 provides an exception to applying some of its specific requirements if the contract is a "**conventional convertible debt instrument** in which the holder only may realize its value of the conversion option by exercising the option and receiving the entire proceeds in a fixed number of shares or the equivalent amount of cash (at the discretion of the issuer)." [Emphasis added]

At issue is when should a convertible debt instrument be considered "conventional"?

Added to EITF Agenda for discussion at a future meeting — Accounting for *Altersteilzeit* Early Retirement Programs

Altersteilzeit (ATZ) is a German early retirement program designed to create an incentive for employees, within a certain age group, to leave their employers before the legal retirement age. The ATZ program allows employees to retire early and still receive their salary, as well as a bonus, paid over a certain period of time. When certain criteria are met, ATZ plans are subsidized by the German government.

This Issue was added to the agenda to address the accounting for the salary component of the program, the bonus component, any subsidy received from the government, and the effect on the service credit for existing retirement plans. In addition, the FASB staff will explore whether other early retirement programs have similar terms and expand the scope of this Issue accordingly.

Item requiring further Agenda Committee discussion — Offsetting of a Right to Receive or an Obligation to Return Cash Collateral With a Net Derivative Position Under a Master Netting Arrangement

A company may enter into a master netting arrangement related to its derivative contracts with a counterparty. If the company is in a net receivable derivative position, the company may require collateral to be posted (e.g., the counterparty provides the company with cash or securities as collateral for the derivative contract). If the company is in a net payable derivative position, it may be required to post collateral with the counterparty.

Currently, there is diversity in practice on whether companies offset in the balance sheet receivables or obligations related to the collateral against the net derivative asset or liability. This diversity exists because of differences in how preparers apply FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts*.

No decision was reached on whether to add this issue to the agenda. The FASB staff will research the terms of master netting arrangements with the objective of further developing the issue. The Agenda Committee will reconsider this issue at the next Agenda Committee meeting.

Not added to EITF Agenda (FSP likely) — Accounting for Minimum Revenue Guarantees

Entities may enter into contracts whereby one party will guarantee to a third party (the guaranteed party) that the guaranteed party will attain a specified amount of revenue during a certain period. There is diversity in practice as to whether these contracts are within the scope of FASB Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. Although these arrangements may arise in many industries, it is common in contracts between a company that operates healthcare centers and non-employee physicians (e.g., the healthcare company guarantees that non-employee physicians will be able to bill a minimum amount of revenue from their physician practice).

This issue was not added to the EITF's Agenda. However, the Agenda Committee asked the FASB staff to consider providing guidance through the issuance of a FASB Staff Position (FSP). At the EITF meeting, the FASB staff indicated that an FSP is being prepared for the Board's consideration. The FSP is expected to require companies to account for this type of guarantee under Interpretation 45.

Upcoming EITF Events

The next EITF meeting is scheduled for June 15-16, 2005. On June 21, 2005, Deloitte & Touche will host a *Dbriefs* webcast on the topics discussed at the meeting. Join *Dbriefs* to be notified of this and other upcoming webcasts.

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On May 17 at 2:00 PM EDT, we will host a 120-minute webcast on frequently asked questions about FASB Statement No. 123(R), *Share-Based Payment*. Register for this webcast today.

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