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Mr. Larry Smith
Director of Technical Application & Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

March 29, 2004

Dear Mr. Smith:

Thank you for the opportunity to comment on the consensus reached by the Emerging Issues Task Force (EITF) in Issue No. 03-6, "Participating Securities and the Two-Class Method under FASB Statement No. 128, *Earnings per Share*." We have numerous clients whose financial statements could be materially impacted by the guidance in Issue 03-6 and we are concerned by the confusion among constituents and the accounting firms regarding the application of Issue 03-6 to Variable Share Forward (VSF) contracts. We understand there are conflicting views among the Big Four accounting firms on this issue.

As we understand the consensus reached by the EITF in Issue 2b(i), a reduction to the conversion price or an increase to the conversion ratio of a convertible security that is triggered by a dividend payment on common stock is not a participation right. Similarly, reductions to the exercise price of options or warrants on the issuer's shares also are not considered participation rights. We fully support these conclusions. However, a similar provision in a forward contract to issue common stock, where the forward contract provides for an adjustment to the exercise price that is tied to the declaration of dividends by the issuer, would be deemed a participating security subject to the two-class method under Statement 128.

At issue is whether a VSF should be analyzed as an optional security or a forward security based on the guidance in Issue 03-6. This determination could result in *materially* different Basic EPS figures, depending on the specific terms of the transaction being analyzed.

We believe that a VSF should be analyzed as an optional contract because it is, in fact, a combination of options in a single contract. As such, we do not believe that the inclusion of a provision which adjusts the settlement rates (or strike prices) on a VSF triggered by a dividend payment on common stock should cause the VSF to be deemed a participating security subject to the two-class method under Statement 128.

A typical VSF is issued to investors with the following terms:

- There is no value exchanged at inception.
- At maturity of the VSF, the investor delivers \$100 in cash or permitted financial instruments.
- If the stock price at maturity is below \$100, the company delivers 1.00 shares to the investor. Economically, the issuer has purchased a put at \$100 on 1.00 shares from the investor.
- If the stock price at maturity is above \$125, the company delivers 0.80 shares to the investor. Economically, the issuer has written a call at \$125 on 0.80 shares to the investor.
- If the stock price is between \$100 - \$125, commonly referred to as “the dead zone”, the company delivers as many shares (between 1.00 – 0.80) as needed to deliver \$100 of value to the investor. Economically, this is a spot market transaction at maturity.

We would acknowledge that settlement rate adjustment features for dividends may vary among transactions. However, in the transactions we reviewed the investor only benefited from a settlement rate adjustment triggered by a dividend payment on common stock when the stock price at maturity was outside the dead zone. Put another way, the investor *only* participates either when the purchased put option is in the money or the written call option is in the money. They do not participate when the stock price at maturity is between the put option strike price and call option strike price (i.e. in the dead zone).

For example, assume the VSF described above had a 3-year life. Due to an interim dividend payment the dead zone was adjusted from the original \$100-\$125 range down to \$99-\$124. If the stock price at maturity was \$110, the issuer would deliver 0.9091 shares worth \$100 whether or not the VSF had a settlement rate adjustment provision triggered by dividends.

It is our understanding that the EITF believes that securities in which it is certain that the investor will participate from an adjustment to the exercise price that is tied to the declaration of dividends, such as a fixed-price, fixed-share forward, should be deemed participating securities subject to the two-class method. A VSF is not such a contract. As described above, in a VSF, it is not certain that an investor will benefit from a settlement rate adjustment because the investor will not benefit when the stock price at maturity is between the put option strike price and call option strike price.

Based on this understanding of the consensus reached by EITF in Issue 2b(i) of Issue 03-6 we do not believe that the inclusion of a provision which adjusts the settlement rates on a VSF triggered by a dividend payment on common stock should cause the VSF to be deemed a participating security subject to the two-class method under Statement 128. However, we would urge the EITF or the FASB to clarify that the consensus reached in Issue 2b(i) of Issue 03-6 does not apply to a VSF.

If you would like to discuss our comments or any other issues further you can contact me at 212-902-7052 or Nora Dougherty at 212-357-8391.

Sincerely,

Timothy J. Bridges
Managing Director

Copy: Nora Dougherty
Matt Schroeder

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Mr. Lawrence W. Smith
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March 30, 2004

Dear Mr. Smith:

We would like the opportunity to comment on the consensus reached by the Emerging Issues Task Force (“EITF”) at its meeting held on March 17-18, 2004 regarding Issue 03-6 “Participating Securities and the Two-Class Method under FAS 128”. We understand that Issue 03-6 addresses a number of questions regarding the calculation of basic earnings-per-share (“EPS”) by companies that have issued securities other than common stock that participate in dividends and earnings (“participating securities”) of the issuing entity. The issue is also intended to provide further guidance in applying the two-class method of calculating EPS once it is determined that a security is participating.

It is our understanding that the FASB staff raised an additional issue at the meeting concerning the treatment of forward contracts with dividend (or dividend-equivalent) rights that would adjust the settlement amount when the forward contract settled and that the EITF reached a consensus that these forward contracts would be considered participating securities for the purpose of applying Issue 03-6. However, it is not clear whether the EITF meant for this guidance to include Variable Share Forward Sales Contracts (VSF), such as the contract illustrated in Example 4 of FSP No. FAS 150-1, “Issuer’s Accounting for Freestanding Financial Instruments Composed of More than One Option or Forward Contract Embodying Obligations under FASB Statement No 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*”.

Certain of these VSF contracts have anti-dilution adjustments which effectively adjust the settlement rate or number of shares to be delivered under the contract. This adjustment is contingent upon the issuer increasing its dividend rate or taking other actions that are within the control of the issuer that have a dilutive effect. For example, in order for the VSF to participate

in the undistributed earnings with common shareholders, the issuer would have to increase its dividend rate (i.e. from \$0.49 to \$0.50 per share) and its share price would have to be above or below the \$50 to \$60 share price range (based on the amounts used in Example 4 of FSP No. FAS 150-1). Therefore, the payment of dividends on common shares by itself does not result in the VSF participating by way of an adjustment to the settlement rate. There is a “dual trigger” event that must occur before this participation comes into effect. The two-class method gives rise to application issues for these types of contracts because i) the VSF may not ultimately participate in dividends and earnings and ii) the number of shares that will ultimately be delivered under the contract is not know until the VSF settlement date.

For the reasons noted above, we believe that the two-class method for determining EPS should not apply to VSF contracts with anti-dilution adjustments that are contingent upon both i) the issuer increasing its dividend rate or taking other actions that are within the control of the issuer that have a dilutive effect and ii) the share price of the issuer being above or below a specified range.

If you would like to discuss our comments further, please contact me at (441) 294-7392.

Sincerely,

Derrick A. Irby
Vice President

cc: Jerry de St. Paer
Michael Siese