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Technical Director  
Financial Accounting Standards Board  
401 Merritt 7  
PO Box 5116  
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Sent via email to: [director@fasb.org](mailto:director@fasb.org), File Reference No. 2019-730

**Re: FASB Exposure Draft (ED) Proposed Accounting Standards Update issued July 31, 2019, Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity’s Own Equity (Subtopic 815-40) [File Reference No. 2019-730]**

Dear Technical Director:

CliftonLarsonAllen LLP appreciates the opportunity to comment on the Financial Accounting Standards Board’s July 31, 2019, Proposed Accounting Standards Update (ED), *Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity’s Own Equity (Subtopic 815-40)*.

The majority of our clients are private companies and not-for-profit entities. As such, our comments are focused on the ED questions and provisions related to private companies; therefore, we have not responded to every question in the ED.

We have provided our responses to the questions for respondents included in the exposure draft in the attachment to this letter.

Sincerely,

**CliftonLarsonAllen LLP**

**FASB Exposure Draft (ED) Proposed Accounting Standards Update issued July 31, 2019, *Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity’s Own Equity (Subtopic 815-40)***

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**Convertible Instruments**

- 1. Should convertible instruments be accounted for as a single unit of account, except in circumstances in which the conversion features are required to be bifurcated by guidance in Topic 815? Please explain why or why not. Under this simplification, would any specific information about convertible instruments be missing in order to understand an entity's financial position and financial performance? If so, please explain what information would be missing and how that information is used.***

We agree with the proposed amendment that states for conversion features that are not required to be accounted for as derivatives under Topic 815, the embedded conversion features would no longer be separated from the host contract. Consequently, a convertible debt instrument would be accounted for as a single liability measured at its amortized cost and a convertible preferred stock would be accounted for as a single equity instrument measured at its historical cost as long as no other features require bifurcation and recognition as derivatives.

We agree that this would provide financial statement users with a simpler and more consistent starting point to perform analyses across entities, consistent with feedback received from users. We agree with the FASB that the proposed amendments would improve the operability of the guidance and reduce, to a large extent, the complexities in the accounting for convertible instruments and the difficulties with the interpretation and application of the relevant guidance.

- 2. Do the disclosure amendments in this proposed Update for convertible debt instruments in paragraphs 470-20-50-1A through 50-1I and for convertible preferred stock in paragraphs 505-10-50-12 through 50-18 provide decision-useful information? Should any of these disclosures be required for every annual and interim period for which a statement of financial position and a statement of financial performance are presented? Should any other disclosures for convertible instruments be required? Please explain why or why not.***

We believe, based on stakeholder and user feedback in the Basis for Conclusions section of the exposure draft, current disclosure requirements for convertible debt are adequate to provide decision-useful information.

### **Derivatives Scope Exception for Contracts in an Entity's Own Equity**

**3. *Should remote settlement features be disregarded for purposes of determining the classification of a contract in an entity's own equity (for both indexation and settlement)? Is remote an operable threshold? Please explain why or why not.***

Yes, we agree that disregarding remote settlement features for purposes of determining the classification of a contract in an entity's own equity would improve the understandability of the guidance and allow the focus to be more on the economic substance of the transaction rather than the form.

As it pertains to the use of "remote" as an operable threshold, we believe that to achieve its objective of simplification and cost reduction, the FASB should provide further guidance in applying this term as a qualitative threshold. For example, the FASB could provide examples of what would be considered "remote" events.

Additionally, we suggest the FASB also consider the impact the use of the remote threshold would have on auditing standards and more specifically what evidential matter auditors will need to support a company's assessment of "remote."

**4. *Should a requirement to settle a contract in registered shares not affect the classification of a contract in the entity's own equity? Please explain why or why not.***

We agree with the FASB that a requirement to settle a contract with registered shares should not affect the classification of a contract in an entity's own equity because such a requirement is not necessarily indicative of whether an entity is able to share settle an instrument.

Additionally, as noted in the Basis for Conclusions section of the exposure draft, stakeholders told the FASB in their outreach that the unregistered share settlement condition is the most difficult aspect of the guidance to apply when determining an entity's ability to settle in shares. To evaluate this condition, an entity typically had to engage legal counsel to determine whether a contract could be settled with unregistered shares. Stakeholders further told the FASB that there was often disagreement between lawyers and accountants about conclusions, especially considering that likelihood could not be factored into this evaluation for accounting purposes but generally was factored into this evaluation for legal purposes.

We also appreciate the fact that removing the requirement would further align ASC 815 with ASC 718. More specifically, a requirement for a contract to be settled in registered shares does not imply that an entity does not have the ability to deliver shares and would not prevent equity classification, which is similar to the guidance in paragraph 718-10-25-15.

**5. Should a requirement to post collateral not affect the classification of a contract in an entity's own equity? Please explain why or why not.**

We agree with the FASB's conclusion that although posting collateral requires using assets in the short term, the nature of collateral is that it may be returned, so it may not be considered cash settlement.

**6. Should the hierarchy of a counterparty's rights or shareholder rights not affect the classification of a contract in an entity's own equity? Please explain why or why not.**

We agree with FASB's conclusion that including this condition in the guidance is unrelated to whether the contract will be cash settled or share settled. We further acknowledge that the notion of shareholders' rights is not defined in the Master Glossary (other than as described in Section 815-40-25), which makes this condition difficult to apply in practice.

**7. Are the proposed amendments about reassessment of the derivatives scope exception operable? Should reassessment of the derivatives scope exception occur only upon a reassessment event (as defined in paragraph 815-40-35-8)? If not, should the reassessment be performed more frequently even if a reassessment event has not occurred, for example, on an annual basis? If performed annually, should the likelihood threshold be remote or should a different threshold be applied? Please explain your rationale for each of the answers provided.**

Though dependent on how successful the FASB is in adding clarity to the remote threshold, we support reassessment only upon the occurrence of a reassessment event and recommend adding to ASC 815-40-35-8a that when an event deemed remote at inception occurs that this would also be considered a reassessment event. This approach would align with the impairment analysis of goodwill under the Private Company Council accounting alternative, which requires an analysis of goodwill upon the occurrence of a triggering event. Further, we recommend reassessing in situations when a contract is amended.

**8. Do the proposed disclosure amendments for contracts in an entity's own equity in paragraph 815-40-50-5(f) through (g) provide decision-useful information? Please explain why or why not. Should any other disclosures for contracts in an entity's own equity be required? Please explain which disclosures should be required and why.**

Yes, we believe the proposed disclosure amendments provide decision-useful information allowing users to understand how conversion or exercise prices or the number of shares used to calculate settlement could change as per the contract terms or if there was a change to conversion or exercise prices or the number of shares used to calculate settlement during the reporting period.

**Transition and Effective Date**

**13. Should the proposed amendments that affect classification, recognition, and measurement be applied on a modified retrospective basis, with an option for full retrospective application? Do you agree with the Board's proposed transition expedient? Please explain why or why not.**

We agree with the proposed transition guidance of applying the standard on a modified retrospective basis with an option for full retrospective application. While the modified retrospective method allows

for consistent presentation within the year of adoption, the full retrospective application provides preparers an option for consistency in all periods presented.

We further agree the proposed transition expedient, which allows the assessment of the consideration of likelihood (that is, contingent events in the indexation and settlement evaluations) at the date of adoption rather than at contract inception. This would reduce cost and complexity of adoption by the avoidance of developing an assessment which may no longer be relevant.

**15. How much time would be needed to implement the proposed amendments? Should the amount of time needed to implement the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities? Should early adoption be permitted? Please explain your response.**

To allow private companies the option to learn from public company implementation efforts, we recommend adopting an effective date strategy similar to that outlined in the FASB's August 15, 2019, exposure draft, *Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates*, which would permit private companies two years from the effective date for larger public business entities to adopt the standard. If early application is permitted, private entities can always adopt earlier if they are ready.

**Overall**

**16. The proposed amendments would affect all entities that issue convertible instruments and/or contracts in an entity's own equity. Are there any specific private company considerations, in the context of applying the Private Company Decision Making Framework, that the Board should be aware of?**

We believe the proposed amendments in the exposure draft will help reduce complexity and add more consistency in accounting for certain financial instruments with characteristics of liabilities and equity.

**17. The proposed amendments would supersede various areas of guidance (such as the guidance on certain accounting models for convertible instruments). Do you expect that superseding that guidance will result in any unintended consequences? For example, is there guidance that is currently analogized in practice to account for transactions for which there is no explicit guidance under current GAAP? Please explain what those unintended consequences are and potential solutions, if applicable.**

We recommend that if the FASB includes the remote threshold in the final standard, that the FASB apply the same remote threshold to contracts in an entity's own equity that are in the scope of ASC 480-10-25-8 (e.g., a warrant that requires gross settlement but is also puttable for cash upon a remote event or a warrant on shares that are redeemable only upon the occurrence of a remote event).