Interpretation of the Emerging Accounting Issues Working Group

INT 02-19: EITF 01-1: Accounting for a Convertible Instrument Granted or Issued to a Nonemployee for Goods or Services or a Combination of Goods or Services and Cash

ISSUE NULLIFIED BY SSAP NO. 95

INT 02-19 Dates Discussed

September 10, 2002; December 8, 2002

INT 02-19 References

SSAP No. 28—Nonmonetary Transactions (SSAP No. 28)
SSAP No. 95—Exchange of Nonmonetary Assets, A Replacement of SSAP No. 28—Nonmonetary Transactions (SSAP No. 95)

INT 02-19 Issue

1. Questions sometimes arise about the appropriate recognition and measurement by an issuer for a convertible instrument that is issued to a nonemployee in exchange for goods or services or a combination of goods or services and cash. The convertible instrument contains a nondetachable conversion option that permits the holder to convert the instrument into the issuer's stock.

2. *APB Opinion 14, Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants* (APB No. 14), *EITF No. 98-5, Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios* (EITF 98-5), and *EITF No. 00-27, Application of Issue No. 98-5 to Certain Convertible Instruments* (EITF 00-27) address an issuer's accounting for a conversion option for which the issuer's stock is the underlying when that conversion option is embedded in a debt or preferred stock instrument that is issued in a financing transaction. *FASB Statement No. 123, Accounting for Stock-Based Compensation* and *.curities w-ions*

cash) should be recognized as a financing cost (that is, interest expense or dividends) or as a cost of the goods or services received or receivable from the counterparty

Issue 4 – A company issues a convertible instrument for cash proceeds that indicate that the instrument includes a beneficial conversion option. The purchaser of the instrument also provides (receives) goods or services to (from) the issuer that are the subject of a separate contract. The issue is whether any goods or services provided (received) by the purchaser should be accounted for as an adjustment to the consideration for the convertible instrument.

INT 02-19 Discussion

4. The working group reached a consensus to adopt the consensus positions of *EITF 01-1, Accounting for a Convertible Instrument Granted or Issued to a Nn4,employeefor tGods o-5(r)68*

c. On Issue 3, the EAIWG reached a consensus that once the instrument is considered "issued" for accounting purposes, distributions paid or payable should be characterized as financing costs. Prior to that time, distributions paid or payable under the instrument should be characterized as a cost of the underlying goods or services. The EAIWG observed that the accretion of a discount on a convertible instrument resulting from a beneficial conversion option does not begin until the instrument is issued for accounting purposes.

d. On Issue 4, the EAIWG reached a consensus that the terms of both the agreement for goods or services and the convertible instrument should be evaluated to determine whether their separately stated pricing is equal to the fair value of the goods or services and convertible instrument. If that is not the case, the terms of the respective transactions should be adjusted. The convertible instrument should be recognized at its fair value with a corresponding increase or decrease in the purchase or sales price of the goods or services. The EAIWG acknowledged the difficulty in evaluating whether the separately stated pricing of a convertible instrument is equal to its fair value. The EAIWG noted that if an instrument issued to a goods or services provider (or purchaser) is part of a larger issuance, a substantive investment in the issuance by unrelated investors (who are not

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