

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 08-06: FSP EITF 00-19-2: Accounting for Registration Payment Arrangements

ISSUE NULLIFIED BY SSAP NO. 5R

INT 08-06 Dates Discussed

May 31, 2008; September 22, 2008

INT 08-06 References

SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets (SSAP No. 5R)

INT 08-06 Issue

1. *FASB Staff Position EITF 00-19-2: Accounting for Registration Payment Arrangements (FSP EITF 00-19-2)*, issued in December 2006, addresses an issuer's accounting for registration payment arrangements. FSP EITF 00-19-2 specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision of a financial instrument or other agreement, should be separately recognized and measured in accordance with *FASB Statement No. 5, Accounting for Contingencies* (FAS 5). Furthermore, FSP EITF 00-19-2 clarifies that a financial instrument subject to the registration payment arrangement should be accounted for in accordance with other applicable generally accepted accounting principles (GAAP) without regard to the contingent obligation to transfer consideration pursuant to the registration payment arrangement.

2. For registration payment arrangements that are outstanding prior to the issuance of FSP EITF 00-19-2, and that continue to be outstanding at the beginning of the period of adoption, GAAP transition shall be achieved by reporting a change in accounting principle through a cumulative-effect adjustment to the opening balance of retained earnings, or other appropriate components of equity or net assets in the statement of financial position.

3. As noted within FSP EITF 00-19-2:

4. This FSP applies to the issuer of a registration payment arrangement. For purposes of this FSP, a registration payment arrangement is an arrangement with both of the following characteristics:

- a. The arrangement specifies that the issuer will endeavor (1) to file a registration statement for the resale of specified financial instruments and/or for the resale of equity shares that are issuable upon exercise or conversion of specified financial instruments and for that registration statement to be declared effective by the SEC (or other applicable securities regulator if the registration statement will be filed in a foreign jurisdiction) within a specified grace period, and/or (2) to maintain the effectiveness of the registration statement for a specified period of time (or in perpetuity); and
- b. The arrangement requires the issuer to transfer consideration to the counterparty if the registration statement for the resale of the financial instrument or instruments subject to the arrangement is not declared effective or if effectiveness of the registration statement is not maintained. That consideration

may be payable in a lump sum or it may be payable periodically, and the form of the consideration may vary. For example, the consideration may be in the form of cash, equity instruments, or adjustments to the terms of the financial instrument or instruments that are subject to the registration payment arrangement (such as an increased interest rate on a debt instrument).

5. This FSP applies to a registration payment arrangement regardless of whether it is issued as a separate agreement or included as a provision of a financial instrument or other agreement. An arrangement that requires the issuer to obtain and/or maintain a listing on a stock exchange, instead of, or in addition to, obtaining and/or maintaining an effective registration statement, is within the scope of this FSP if the remaining characteristics set forth in paragraph 4 are met.
4. As outlined in FSP EITF 00-19-2, because of the potential significance of the consideration that may become payable under registration payment arrangements, questions have arisen as to the accounting for such arrangements. Questions also have arisen about whether the existence of a registration payment arrangement affects the accounting for the financial instrument(s) subject to the registration payment arrangement, particularly when the financial instrument or instruments are accounted for in accordance with *EITF Issue No. 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, an Company's Own Stock* (EITF 00-19).
5. FASB staff issued the following guidance in paragraphs 7-11 of FSP EITF 00-19-2:
 7. The contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement shall be recognized and measured separately in accordance with Statement 5 and FASB Interpretation No. 14, Reasonable Estimation of the Amount of a Loss.
 8. The financial instrument(s) subject to the registration payment arrangement shall be recognized and measured in accordance with other applicable GAAP (for example, APB Opinion No. 21, Interest on Receivables and Payables, Statement 133, and Issue 00-19) without regard to the contingent obligation to transfer consideration pursuant to the registration payment arrangement. That is, an entity should recognize and measure a registration payment arrangement as a separate unit of account from the financial instrument(s) subject to that arrangement.
 9. If the transfer of consideration under a registration payment arrangement is probable and can be reasonably estimated at inception, the contingent liability under the registration payment arrangement shall be included in the allocation of proceeds from the related financing transaction using the measurement guidance in Statement 5. The remaining proceeds shall be allocated to the financial instrument(s) issued in conjunction with the registration payment arrangement based on the provisions of other applicable GAAP. For example, if the financial instruments issued concurrently with the registration payment arrangement are a debt instrument and an equity-classified warrant, the remaining proceeds after recognizing and measuring a liability for the registration payment arrangement under Statement 5 would be allocated on a relative fair value basis between the debt and the warrant pursuant to paragraph 16 of APB Opinion No. 14, Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants. A financial instrument issued concurrently with a registration payment arrangement might be initially measured at a discount to its principal amount under this allocation methodology. For purposes of determining whether a convertible instrument contains a beneficial conversion feature under Issues 98-5 and 00-27, an entity shall use the effective conversion price based on the proceeds allocated to the convertible instrument to compute the intrinsic value, if any, of the embedded conversion option.

10. If the transfer of consideration under a registration payment arrangement becomes probable and can be reasonably estimated subsequent to the inception of the arrangement or if the measurement of a previously recognized contingent liability increases or decreases in a subsequent period, the initial recognition of the contingent liability or the change in the measurement of the previously recognized contingent liability shall be recognized in earnings.

11. If (a) an entity would be required to deliver shares under a registration payment arrangement, (b) the transfer of that consideration is probable, and (c) the number of shares to be delivered can be reasonably estimated, the issuer's share price at the reporting date shall be used to measure the contingent liability under Statement 5.

INT 08-06 Discussion

6. The Working Group reached a consensus to adopt the guidance in paragraphs 7-11 of FSP EITF 00-19-2 with the following modifications:

- a. Registration payment arrangements meet the definition of a loss contingency in accordance with paragraph 6 of SSAP No. 5R.
- b. Financial instruments shall be accounted for in accordance with the statutory accounting principles for that specific asset type. Registration payment arrangement obligations shall be separate from the measurement and recognition of financial instruments subject to such arrangements.
- c. Transition revisions resulting from application of this guidance shall be accounted for as a change in accounting principle pursuant to *SSAP No. 3—Accounting Changes and Corrections of Errors* (SSAP No. 3). In accordance with SSAP No. 3, the cumulative effect of changes in accounting principles shall be reported as adjustments to unassigned funds in the period of the change in the accounting principle.

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7. No further discussion planned.