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Ms. Hillary Salo  
Technical Director  
Financial Accounting Standards Board  
801 Main Avenue  
PO Box 5116  
Norwalk, CT 06856-5116

File Reference No. 2023-ED600

Dear Ms. Salo:

RSM US LLP is pleased to provide feedback on the Financial Accounting Standards Board's (FASB or Board) proposed Accounting Standards Update (ASU), *Debt—Debt with Conversion and Other Options (Subtopic 470-20): Induced Conversions of Convertible Debt Instruments* (proposed Update or proposal).

We support the Board's efforts to improve the application of the induced conversion guidance in Subtopic 470-20 and reduce the diversity in practice in determining whether a settlement of convertible debt at terms other than the original conversion provisions should be accounted for as an induced conversion or as an extinguishment.

Overall, we agree with the proposed amendments to clarify the requirements for determining whether the induced conversion guidance is applicable. We also concur with the proposed guidance that would specify an inducement offer must provide the same form and amount of consideration as the contractual conversion privileges, including the additional guidance related to a volume-weighted average price (VWAP) formula. However, as discussed further in our response to Question 4 below, we are concerned that the proposed amendment that states the induced conversion guidance can be applied to a convertible note that is not currently convertible may lead to more complexity for private companies that often issue convertible debt instruments with multiple contingent and noncontingent conversion terms.

Our responses to the questions posed in the proposed Update are included in the remainder of this letter.

### Responses to Questions for Respondents

**Question 1:** Do you agree with the proposed amendments to the induced conversion criterion in paragraph 470-20-40-13(b) that would require that an inducement offer preserve the consideration (in form and amount) issuable pursuant to conversion privileges provided in the terms of the debt instrument? Please explain why or why not.

Yes, we agree with the proposed amendment to the induced conversion criterion that would require an inducement offer to preserve the form and amount of consideration provided in the terms of the debt instrument. The proposed amendments effectively address the treatment of the settlement of a convertible debt instrument with a cash conversion feature, which should reduce or eliminate diversity in practice in this regard. Further, the proposed requirement is consistent with the existing provisions in paragraphs 470-20-40-4 and 40-5 on a contractual conversion, including the underlying principle that a conversion pursuant to a contractual conversion produces no gain or loss.

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**Question 2:** Do you agree that the proposed induced conversion criterion in paragraph 470-20-40-13(b) should be assessed as of the date the inducement offer is accepted by the convertible debt holder? Please explain why or why not.

Yes, we agree that the induced conversion criterion in paragraph 470-20-40-13(b) should be assessed as of the date the inducement offer is accepted by the convertible debt holder, which is consistent with the existing guidance on measurement of expense for an induced conversion.

**Question 3:** Do you agree with the proposed amendments in paragraph 470-20-40-13A(c) that, if the debt has been exchanged or modified (without being deemed to be substantially different) within the one-year period preceding the offer acceptance date, then the conversion privileges provided in the debt terms that existed one year before the offer acceptance date (rather than the conversion privileges provided in the terms of the debt instrument) should be used for the induced conversion assessment? If not, please explain why and state which alternative approach you would support (see paragraph BC52 for other approaches considered by the Task Force, including a principle-based approach).

Yes, we agree with the proposed amendments in paragraph 470-20-40-13A(c) that specify if the debt has been exchanged or modified (without being deemed to be substantially different) within the one-year period preceding the offer acceptance date, the conversion privileges that existed one year before the offer acceptance date should be used for the induced conversion assessment. This approach is similar to the one-year look-back used in the 10 percent cash flow test to evaluate a modification or exchange of a debt instrument under Subtopic 470-50.

**Question 4:** Do you agree that all convertible debt instruments, including convertible debt instruments that are not currently convertible, should be eligible for induced conversion accounting if they contained a substantive conversion feature at issuance and the other criteria in paragraph 470-20-40-13 are met? Please explain why or why not.

We do not support the Board's proposal to make convertible debt instruments that are not currently convertible eligible for induced conversion accounting based on whether the conversion feature was determined to be substantive at issuance. We believe that this proposed amendment would (1) not reflect the economic substance of the transaction, (2) result in a significant change to existing practice and (3) add complexity to the accounting model.

We question whether the proposed application of induced conversion accounting is appropriate when a convertible debt instrument is not currently convertible. In these circumstances, we believe the economic substance of the conversion may align more with a negotiated settlement and, therefore, extinguishment accounting, given any preexisting contract between the issuer and the debt holder is effectively voided, and the debt is extinguished pursuant to newly negotiated terms.

We recognize that the existing guidance in paragraph 470-20-40-5 requires an instrument's original conversion terms to be considered substantive at the time of issuance for a conversion under those terms to be treated as a contractual conversion with no gain or loss recognized upon the debt instrument's conversion. However, unlike the proposed Update, current GAAP requires the debt instrument to be currently convertible (i.e., convertible upon the issuer's exercise of a call option, not just when the instrument was originally issued). That's why at least some preparers and practitioners currently do not believe induced conversion accounting applies when the original debt instrument was not convertible as of the date of settlement or inducement offer.

We believe the proposed amendment may result in unintended consequences and added complexity for private companies that issue convertible debt. In practice, we often encounter private company debt that may include a conversion option for some or all of the following:

- Next round of preferred stock issued in a qualified financing
- Next round of preferred stock issued in a non-qualified financing
- An existing class of preferred stock upon a sale of the issuer or change in control
- Common stock, either throughout the term of the debt or only at its maturity

By requiring that each of the conversion features be considered, regardless of whether a contingency has or will be met, we believe the proposed induced conversion accounting assessment will be difficult to apply.

For the reasons discussed above, we recommend that the FASB eliminate or modify the proposed amendment that would require an entity to assess whether a conversion feature is substantive at the time of issuance. Instead, we believe the assessment should be made as of the date the inducement offer is accepted by the holder.

If the amendment is retained as proposed, we suggest the FASB provide additional guidance and illustrative examples to address:

- Consideration of an expired conversion feature that was considered substantive at issuance (i.e., reasonably possible of being exercised). For example, a conversion option that expired because a qualified financing did not occur by a stated date or a non-qualified financing conversion option whose exercise period lapsed unexercised.
- Consideration of a conversion feature for which the shares do not currently exist (e.g., the next round of preferred stock issued in a qualified financing). In particular, when evaluating whether the nature and amount criterion is satisfied, how should an entity assess such a provision if the shares have not been issued or do not exist and the rights and privileges of such shares have not been defined?
- When multiple substantive conversion features exist, how should a company consider each contingent and noncontingent conversion feature in assessing whether an induced conversion has occurred?
- When multiple substantive conversion features exist, how should a company measure the expense of the induced conversion (e.g., based on the feature determined to be an induced conversion, based on the feature that provides the highest number or amount of the same form)?

**Question 5:** Would the proposed amendments provide decision-useful information? Are the proposed amendments clear and operable? Please explain why or why not.

We defer to the users of financial statements as to whether the proposed amendments would provide decision-useful information. Please refer to our response to Question 4 regarding our concerns about the operability of some of the proposed amendments.

**Question 6:** The proposed transition requirements would allow entities to apply the proposed amendments on either a prospective or a retrospective basis. Would the information required to be disclosed under the proposed transition method be decision useful? Please explain why or why not. Are the proposed transition requirements operable? If not, why not and what transition method would be more appropriate and why?

We defer to the users of financial statements as to whether the transition disclosures would provide decision-useful information. We believe the proposed transition requirements would be operable since entities can elect to adopt them either prospectively or retrospectively.

**Question 7:** In evaluating the effective date, how much time would be needed to implement the proposed amendments? Should the effective date for entities other than public business entities be different from the effective date for public business entities? Should early adoption be permitted? Please explain why or why not.

We generally defer to the preparers of financial statements regarding the time needed to implement the proposed Update. We believe that entities other than public business entities (PBEs) should have an extra year to adopt the proposed Update because they often do not have the same level of resources and processes as PBEs and because the proposed amendments may be more challenging for them to implement. We also believe that all entities should be allowed to adopt the proposed Update early, because we do not see any significant drawbacks to doing so.

**Other matters for the Board's consideration**

In general, we believe the Case C and D examples in paragraphs 470-20-55-9A through 55-9G of the proposed Update are helpful for illustrating how to determine whether the accounting for induced conversion applies when there have been eliminations of or modifications to a VWAP formula. However, we recommend the Board expand these examples to also show how to measure the induced conversion expense, as well as the entries needed to record the induced conversion. This would prevent any possible misunderstanding related to the application of the proposed changes that deal with the inclusion, elimination or modification of a VWAP formula.

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We appreciate this opportunity to provide feedback on the proposed Update and would be pleased to respond to any questions the Board or its staff may have concerning our comments. Please direct any questions to Ginger Buechler at 612.455.9411 or Joseph Cascio at 212.372.1139.

Sincerely,

*RSM US LLP*

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