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To Whom It May Concern:

We have identified certain items that we believe require technical corrections. We therefore recommend that the Board consider the following amendments as part of its next Technical Corrections and Improvements document. We appreciate the opportunity to bring these to your attention and would be pleased to discuss our comments with Board members or the FASB staff at your convenience.

Thank you,

Ernst & Young LLP

Classification of options and similar instruments that allow for cash settlement upon the occurrence of a contingent event

Paragraphs 32 and A229 of FAS 123R, *Share-Based Payment*, require options or similar instruments to be classified as liabilities if "the entity can be required under any circumstances to settle the option or similar instrument by transferring cash or other assets." FSP FAS 123R-4 amended these paragraphs to specify that a cash settlement feature that can be exercised only upon the occurrence of a contingent event that is outside the employee's control does not meet the condition in paragraphs 32 and A229 until it becomes probable that the event will occur. This guidance was codified in ASC 718-10-25-11(b).

Paragraph 7 of the FSP states: "The guidance in this FSP is applicable only for options or similar instruments issued as part of employee compensation arrangements. That is, the guidance included in this FSP is not applicable, by analogy or otherwise, to instruments outside employee share-based payment arrangements." This limited application note was codified in ASC 718-10-35-15 but was reworded so that the limitation refers only to the modification accounting codified from Paragraph 6 of the FSP (also in ASC 718-10-35-15), not to the guidance codified in ASC 718-10-25-11(b).

ASC 505-50 provides guidance for classifying equity-based payments to nonemployees. ASC 505-50-25-10 states that "[a] grantor shall recognize either a corresponding equity or a liability, depending on whether the instruments granted satisfy the equity or liability classification criteria established in paragraphs 718-10-25-6 through 25-19." This requires grantors to apply by analogy the guidance in ASC 718-10-25-11(b) when they classify options or similar instruments issued as part of nonemployee share-based arrangements. Without a clear link to the guidance from paragraph 7 of FSP FAS 123R-4, the guidance in ASC 718-10-25-11(b) may be applied incorrectly, resulting in an inappropriate classification of a nonemployee award of options or similar instruments that an entity can be required under any circumstances to settle by transferring cash or other assets.

We suggest that the limiting guidance from paragraph 7 of the FSP (i.e., codified in ASC 718-10-35-15) be added to both paragraphs ASC 505-50-25-10 and ASC 718-10-25-11(b) for clarity. We believe this is most consistent with the guidance as originally adopted.

Loans insured under an FHA or VA program

EITF 87-9, *Profit Recognition on Sales of Real Estate with Insured Mortgages or Surety Bonds*, was codified in ASC 360-20, *Property, Plant, and Equipment — Real Estate Sales*. However, the final paragraph of EITF 87-9, which amended previous discussions, does not appear to have been codified. As a result, ASC 360-20-55-3 (see excerpt below) allows the initial and continuing investment tests to be evaluated using Federal Housing Administration (FHA) or Veterans Administration (VA) criteria rather than the criteria set out in ASC 360-20-55-1 (i.e., the minimum initial investment criteria) provided the loan is *fully insured* under these programs. However, the Task Force ultimately concluded (see excerpt below) that such loans did not need to be *fully insured* and amended EITF 87-9 to reflect that conclusion. ASC 360-20 does not reflect that decision to amend the guidance. We suggest that the term "fully" should be deleted to conform ASC 360-20-55-3 with the subsequent EITF discussions permitting profit recognition under the full accrual method for all loans insured under the current FHA or VA programs.

Excerpt: ASC 360-20-55-3 A seller of owner-occupied single-family residential homes that finances a sale under an Federal Housing Administration or Veterans Administration government-insured program may use the normal down payment requirements or loan limits established under those programs as a surrogate for the down payment criteria set forth in paragraphs 360-20-55-1 through 55-2 and may record profit under the full accrual method provided that the mortgage receivable is **fully** [emphasis added] insured from loss under the Federal Housing Administration or Veterans Administration program. In that specific circumstance, departure from the minimum initial investment criteria of this Section is justified because all of the credit risk associated with the receivable from the sale is transferred to the governmental agency. However, in all other circumstances (for example, Federal Housing Administration or Veterans Administration programs that provide for less than full insurance or seller financing using private mortgage insurance) the minimum initial investment criteria set forth in this Section shall be followed.

Excerpt: EITF 87-9 On the second issue, the Task Force reached a consensus that mortgage insurance should *not* be considered the equivalent of an irrevocable letter of credit in the determination of whether it is appropriate to recognize profit under the full accrual method because the purchase of mortgage insurance is not deemed to demonstrate a commitment by the buyer to honor its obligation to pay for the property.

With respect to the subissue, the Task Force reached a consensus that a seller of owner-occupied single-family residential homes that finances a sale under an FHA or VA government-insured program may use the normal down payment requirements or loan limits established under those programs as a surrogate for the down payment criteria set forth in paragraphs 53 and 54 of Statement 66 and may record profit under the full accrual method provided that the mortgage receivable is *fully insured* from loss under the FHA or VA program. In that specific circumstance, the Task Force believes that departure from the minimum initial investment criteria of Statement 66 is justified because all of the credit risk associated with the receivable from the sale is transferred to the governmental agency. However, the Task Force emphasized that in all other circumstances (for example, FHA or VA programs that provide for less than full insurance or seller financing using private mortgage insurance) the minimum initial investment criteria set forth in Statement 66 should be followed.

Subsequently, several Task Force members indicated that they did not recall the consensus being limited to transactions that are *fully* insured under the FHA and VA programs. Some Task Force members indicated their belief that the consensus should be applied to all sales of residential property for which the seller provides financing under the FHA or VA program and the buyer has complied with the normal lending terms for those programs in the specific location of the property, irrespective of whether the mortgage is *fully* insured. Others suggested that they are uncomfortable addressing transactions that are not fully insured under those programs without a better understanding of how the programs insure the seller in the event of a default by the buyer.

At a subsequent meeting, the Task Force discussed the FHA mortgage insurance program and the VA loan guarantee program with representatives from the FHA and the VA. An FHA representative confirmed that the FHA program normally insures 100 percent of the outstanding mortgage principal, and a VA representative stated that the VA program generally provides first-dollar loss coverage of either 40 or 50 percent of the qualified loan amount, but coverage of not more than $36,000. Coverage under the VA program is reduced on a pro rata basis as the principal of the loan is paid off. Neither program provides for split coverage with private insurers. Also, in the event of a default by the borrower, both the FHA and the VA programs provide for recourse against the borrower.

The Task Force reached a consensus that the term *fully* should be deleted from the consensus reached above, thus permitting profit recognition under the full accrual method for all loans insured under the current FHA or VA programs. Task Force members noted that the consensus applies only to FHA and VA coverage and not to private mortgage insurance.

Newly acquired business or nonprofit activity classified as held for sale on acquisition following the adoption of ASU 2014-08, *Reporting Discontinued Operations and Disclosure of Disposals of Components of an Entity*

ASC 205-20-45-1D, added by ASU 2014-08, *Reporting Discontinued Operations and Disclosure of Disposals of Components of an Entity*, states: "A business or nonprofit activity that, on acquisition, meets the criteria in paragraph 205-20-45-1E to be classified as held for sale is a discontinued operation." The criteria in paragraph 205-20-45-1E are:

Excerpt: 205-20-45-1E A component of an entity or a group of components of an entity, or a business or nonprofit activity (the entity to be sold), shall be classified as held for sale in the period in which **all** [emphasis added] of the following criteria are met:

a. Management, having the authority to approve the action, commits to a plan to sell the entity to be sold.

b. The entity to be sold is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such entities to be sold. (See Examples 5 through 7 [paragraphs 360-10-55-37 through 55-42], which illustrate when that criterion would be met.)

c. An active program to locate a buyer or buyers and other actions required to complete the plan to sell the entity to be sold have been initiated.

d. The sale of the entity to be sold is **probable**, and transfer of the entity to be sold is expected to qualify for recognition as a completed sale, within one year, except as permitted by paragraph 205-20-45-1G. (See Example 8 [paragraph 360-10-55-43], which illustrates when that criterion would be met.)

e. The entity to be sold is being actively marketed for sale at a price that is reasonable in relation to its current fair value. The price at which an entity to be sold is being marketed is indicative of whether the entity currently has the intent and ability to sell the entity to be sold. A market price that is reasonable in relation to fair value indicates that the entity to be sold is available for immediate sale, whereas a market price in excess of fair value indicates that the entity to be sold is not available for immediate sale.

f. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

We believe that the language in ASC 205-20-45-1D and 45-1E changes existing practice for the evaluation of the criteria to be classified as held for sale for newly acquired businesses and nonprofit activities from the current requirements in ASC 360-10-45-12 for a newly acquired asset held for sale.

ASC 360-10-45-12 states: "A long-lived asset (disposal group) that is newly acquired and that will be sold rather than held and used shall be classified as held for sale at the acquisition date only if the one-year requirement in paragraph 360-10-45-9(d) is met (except as permitted by the preceding paragraph) and any other criteria in paragraph 360-10-45-9 that are not met at that date are probable of being met within a short period following the acquisition (usually within three months)."

The one-year requirement in ASC 360-10-45-9(d) is reflected in ASC 205-20-45-1E(d) (and the exception referred to parenthetically in ASC 360-10-45-12 is reflected in 205-20-45-1G). However, the language in ASC 360-10-45-12 that provides relief from the other criteria (i.e., "and any other criteria in paragraph 360-10-45-9 that are not met at that date are probable of being met within a short period following the acquisition (usually within three months)") was not included or referenced in ASC 205-20 with the issuance of ASU 2014-08. Accordingly, upon adoption of ASU 2014-08, a newly acquired business or nonprofit activity does not appear to have relief from meeting the other held for sale criteria upon acquisition in order to be classified as a discontinued operation.

Based on discussion with certain members of the FASB staff, we understand that the Board did not intend to change the evaluation of the held for sale criteria for newly acquired businesses and nonprofit activities and that the criteria in ASC 360-10-45-12 should continue to be applied. If the FASB staff's understanding of the Board's intent is correct, we suggest that the Board amend ASC 205-20-45-1D and/or 45-1E to either include or reference the guidance in ASC 360-10-45-12 for purposes of defining a newly acquired business or nonprofit activity as a discontinued operation.