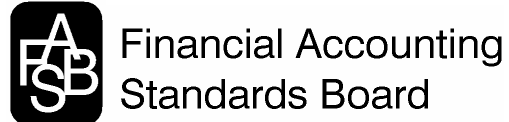


MINUTES



To: Board Members

From: Short-Term Convergence—Phase 1
Varian (ext. 353)

Subject: Minutes of the November 24, 2004 Board Meeting **Date:** December 3, 2004

cc: Bielstein, Smith, Leisenring, Swift, Polley, Gabriele, Intranet (email),
Project Team (J. Johnson, McKenna, Varian, Vincent), McGeachin
(IASB via e-mail)

The Board meeting minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue a final Statement or Interpretation.

Topic: Earnings per Share

Basis for Discussion: Memorandum EPS 2, Memorandum EPS 4, Memorandum
EPS 5

Length of Discussion: 10:50 a.m.to 11:30 a.m.

Attendance:

Board members present: Herz, Batavick, Crooch (by phone),
Schieneman, Schipper, Seidman, and Trott

Board members absent: None

Staff in charge of topic: J. Johnson

Other staff at Board table: Bielstein, Cassel, Varian

Outside participants: Leisenring

Summary of Decisions Reached:

The Board discussed issues related to the proposed Statement on earnings per share (EPS). The Board decided that when applying the treasury stock method to an instrument classified as a liability but potentially settled in shares, the extinguishment of the liability upon issuance of the shares should be included as proceeds in the computation of incremental shares. This decision does not affect the EPS computation for instruments that are currently accounted for using the if-converted method under FASB Statement No. 128, *Earnings per Share*. The Board also decided that any potential broader impact of this decision will be considered within the context of the liabilities and equity project. The Board directed the staff to maintain communication with other project teams dealing with EPS issues, such as the Application and Implementation project team and the liabilities and equity project team.

Objective of Meeting:

There were two objectives of this meeting; first, to determine whether the extinguishment of a liability upon issuance of shares should be included as proceeds in the computation of incremental shares when applying the treasury stock method to an instrument classified as a liability but potentially settled in shares, and second, to determine what impact that decision would have on the status of the project on EPS.

Matters Discussed and Decisions Reached:

1. Mr. Johnson began by stating that the first question to be addressed is when applying the treasury stock method to an instrument classified as a liability but potentially settled in shares, should the extinguishment of the liability upon issuance of the shares be included as proceeds in the computation of incremental shares? He stated that, conceptually, the staff's view is that the

extinguishment of a liability should be included as proceeds (View A).

However, he stated that Statement 128 does not view the extinguishment of a liability as proceeds (View B) for convertible debt and certain options and warrants.

2. Mr. Johnson stated that the more important question was what impact would answering the first question have on the status of this project? He stated that in considering the paragraph 29 amendment to Statement 128, View A is consistent with the objective of closing the window opened in EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock," that allowed a certain instrument to get equity treatment on the financial statements and no dilution in the EPS computation. He stated that View B is also consistent with that objective, but there is a lot of collateral damage. For example, if an instrument is classified as a liability, and changes in the value of that liability are reflected in the income statement, then the numerator in the EPS computation reflects the effects of an increasing underlying share price. As the underlying share price increases, the issuing entity recognizes expense for the increasing obligation to the holder of the instrument. If that same liability is potentially share-settled, View B would require that the denominator be adjusted for the effects of the increasing underlying share price as well.
3. More broadly, Mr. Johnson stated that if View B is found to have some flawed logic, then the if-converted method may also be found to have some flawed logic. He stated that companies have structured instruments to avoid the if-converted method in order to achieve a more desirable EPS treatment, and he discussed a few EPS maintenance projects that have specifically dealt with this issue, such as paragraph 51 of Statement 128 and EITF Issue No. 04-8, "The Effect of Contingently Convertible Instruments on Diluted Earnings per Share."
4. Mr. Johnson stated that the Board had three choices on how to approach this project. Option 1 is a View A approach that would consider amending

Statement 128 more broadly and perhaps changing the if-converted method. Option 2 is a View A approach that would not change the accounting for instruments currently accounted for using the if-converted method, and this approach would also consider any potential broader impact of this decision within the context of the liabilities and equity project. Option 3 is a View B approach with consideration of a potential reversal of the amendment to paragraph 29 of Statement 128.

5. Mr. Trott stated that if the Board decided to follow Option 3, then the amendment to Statement 128 would accomplish convergence with IAS 33, *Earnings per Share*, on year-to-date calculations and mandatorily convertible securities only.
6. Mr. Herz questioned whether IAS 33 includes the if-converted method. Mr. Johnson stated that the if-converted method is in IAS 33, but he did not know whether it got applied in practice. Mr. Schieneman stated that he had seen it applied in some Latin American companies.
7. Mr. Schieneman stated that he never thought that EPS should be a topic for short-term convergence and that he strongly supports Option 1. He stated that EPS is a very important metric and that the Board should not avoid the consideration metrics.
8. Mr. Leisenring stated that he was not confident that the IASB is willing or even able to reconsider IAS 33. He stated Option 1 may result in IAS 33 and Statement 128 being less converged than when this project began. Mr. Johnson stated that Option 1 might potentially decrease the use of the if-converted method. He stated that since balance sheet classification of convertible debt under IFRS is different from that under US GAAP, the effect on EPS is not the same regardless of the similarity of the EPS guidance.
9. Ms. Schipper stated that Option 2 would have the best potential to result in convergence in the long run. She stated the the Board would need to make sure that this particular issue is discussed in the liabilities and equity project in

order to get full convergence. Mr. Johnson stated that Option 2 might result in less convergence than Option 1 because the EITF might decide on questions of maintenance differently than the IFRIC would.

10. Ms. Seidman asked whether viewing the extinguishment of a liability as proceeds results in no dilution, assuming the liability is carried at fair value? Mr. Johnson stated that since the average share price over the period is used in the computation, and the liability amount used as proceeds is a point in time amount, there could potentially be some dilution in certain circumstances.
11. Ms. Seidman asked whether the Board would needed to expose an Option 2 decision? Mr. Johnson stated that he believes that this decision would need to be exposed.
12. Ms. Seidman stated that she would like to see more coordination between the liabilities and equity project and the EPS project. Mr. Trott stated that he hopes to see coordination between all project teams dealing with EPS issues. Mr. Johnson stated that his team would coordinate with any other teams dealing with EPS issues.
13. Six Board members agreed to Option 2; Mr. Schieneman objected. The Board directed the staff to maintain open communication with other project teams dealing with EPS issues.

Follow-up Items:

None.

General Announcements:

None