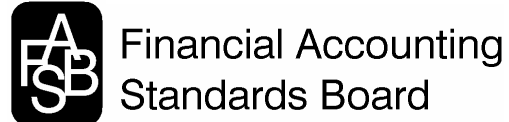


MINUTES



**To:** Board Members  
**From:** Kapko (ext. 317)  
**Subject:** Minutes of the April 27, 2005 FVM Board Meeting **Date:** May 4, 2005  
**cc:** Bielstein, L. Smith, Petrone, Fair Value Team, Revenue Recognition Team, Business Combinations Team, Larson, Polley, Gabriele, Getz, Mahoney, Sutay, Leisenring (IASB), J. Paul (IASB), G. Ryltsova (IASB), P. Martin (CICA), FASB Intranet

*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: Proposed FASB Statement, *Fair Value Measurements*: disclosures, block discounts, and scope

Basis for Discussion: Memorandums 1,2, and 3 dated April 8, 2005, and 1A dated April 19, 2005, and audience handout (attached)

Length of Discussion: 9:15 a.m. to 12:15 p.m.

Attendance:

Board members present: Batavick, Crooch, Herz, Schipper, Seidman, Trott, and Young

Board members absent: None

Staff in charge of topic: MacDonald

Other staff at Board table: Bielstein, Kapko, Lott, McBride, Sogoloff, Thuener, Todorova, and E. Smith

Outside participants: None

## **Summary of Decisions Reached**

The Board continued redeliberations of the proposed FASB Statement, *Fair Value Measurements* (FVM), focusing on issues relating to the scope of the Statement, block measurements, and disclosures. The Board reached the following decisions:

1. The Board decided to include in the scope of the FVM Statement FASB Statement No. 13, *Accounting for Leases*, and other pronouncements that address leasing transactions and FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan*.
2. The Board decided that the fair value of large positions of unrestricted securities that trade in active markets (blocks) should be measured within Level 1 of the fair value hierarchy as the product of the quoted price times the quantity held, except as follows. The Board decided that the fair value of a block held by a broker-dealer that both buys and sells in blocks as part of its regular, ongoing business activities may be measured within a lower level of the fair value hierarchy using a blockage factor, subject to further discussion of related disclosures. The Board discussed disclosures relating to an entity's policies for defining and measuring blocks, fair value amounts measured as the product of the quoted price times the quantity held, and information about gains or losses, if any, on the sale of securities that are initially acquired and held in a block but that are not sold in a block. Further discussion of disclosures is planned for a future Board meeting.
3. The Board revised aspects of the proposed disclosure requirements as follows:
  - a. For each major category of assets and liabilities remeasured at fair value during the period, the disclosures should segregate fair value amounts into three disclosure levels, that is, fair value amounts at the end of the period determined using quoted prices for identical assets or liabilities (Level 1), other market information (Level 2 and Level 3), and entity information (Level 4), and include information about the valuation techniques used. The Board eliminated the related guidance in paragraph 8 of the FVM ED, which would have required that those valuation techniques be consistently applied. Instead, the Board decided to emphasize the valuation objective, that is, to use the valuation technique(s) that provide the best estimate of fair value in the circumstances.

- b. Gains or losses should be disclosed in total (unrealized and realized) for each major category of assets and liabilities remeasured at fair value during the period, segregating amounts included in earnings and in other comprehensive income. Unrealized gains or losses related to those assets and liabilities still held at the reporting date should be separately disclosed for each disclosure level other than Level 1 whenever that information is available.
- c. Quantitative disclosures using a tabular format are required for interim and annual periods. Other disclosures (for example, information about the valuation techniques used) are required only for annual periods.
- d. The fair value information disclosed under the FVM Statement should include the fair value information disclosed under FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, and other pronouncements in the periods in which those disclosures are required, if practicable.

### **Objective of Meeting**

The principal objective of the meeting was to discuss issues raised by respondents relating to disclosures, blocks, and scope.

### **Matters Discussed and Decisions Reached**

#### **DISCLOSURES**

1. Ms. MacDonald said that in its deliberations, the Board decided that having established guidance focusing on how to develop fair value measurements, the FVM Statement should include enhanced disclosures about those measurements (a project objective). Those disclosures fall into two broad categories—measurement disclosures and earnings disclosures—and would apply for assets and liabilities recognized in the statement of financial position that are remeasured at fair value, whether on a recurring basis (financial instruments) or nonrecurring basis (impaired assets).

#### **Measurement Disclosures**

2. Ms. MacDonald explained that the measurement disclosures focus on how the fair value amounts are determined. She said that many respondents generally agreed with those disclosures, subject to clarifications and revisions.

### **Valuation Inputs/Techniques**

3. Ms. MacDonald said that many respondents referred to the need to clarify the disclosures about the inputs used to estimate fair value in the context of the fair value hierarchy (as revised) and include disclosures about the valuation techniques within which those inputs are used (as in many existing pronouncements). Some respondents also referred to the related guidance in paragraph 8 of the FVM ED, which states that valuation techniques used to estimate fair value should be “consistently applied.” In particular, they said that the consistency constraint indicated by that guidance would be overly restrictive.

4. Ms. MacDonald said that in response, the staff recommends that the Board establish three disclosure levels that would segregate fair value amounts determined using quoted prices for identical assets and liabilities in active markets (Level 1), significant other market inputs (Levels 2 and 3), and significant entity inputs (Level 4). She said that the staff also recommends that the Board require disclosure of the valuation technique(s) within which those inputs are used and eliminate the related guidance in paragraph 8 of the FVM ED. Instead, the FVM Statement should emphasize the valuation objective (to use the valuation technique or combination of valuation techniques that provides the best estimate of fair value in the circumstances).

5. All Board members agreed with that staff recommendation, subject to clarification (below).

6. With respect to the guidance in paragraph 8 of the FVM ED, Ms. Seidman said that consistency in the use of valuation techniques is important. Accordingly, the FVM Statement should emphasize the valuation objective, that is, to consistently apply a policy of using the valuation technique or combination of valuation techniques that provides the best estimate of fair value in the circumstances, as recommended by the staff. All other Board members agreed.

7. Ms. Seidman further observed that paragraph 8 of the FVM ED also clarifies that a change in the valuation technique(s) used to estimate fair value should be accounted for as a change in estimate under APB Opinion No. 20,

*Accounting Changes.* She said that guidance should be retained. Mr. Trott disagreed. He pointed out that Opinion 20 requires incremental disclosures about the effect of a change in estimate. He said that those disclosures should not be required under the FVM Statement, largely because in many cases, the information necessary to make those disclosures might not be available.

8. Ms. Seidman and Mr. Trott discussed an alternative approach where the FVM Statement would clarify that a change in the valuation technique(s) used to estimate fair value is not a change in accounting principle under Opinion 20 (to convey that the incremental reporting requirements under Opinion 20 for a change in estimate do not apply). All other Board members agreed.

#### **Discount Rates/Significant Assumptions**

9. Ms. MacDonald said that some respondents referred to the need for disclosures about discount rates and/or significant assumptions used in valuation techniques to estimate fair value. She said that in its deliberations, the Board decided not to standardize those disclosures in the FVM Statement because in many cases (in particular, for many nonfinancial assets and liabilities) the sheer volume of information that would need to be disclosed in order for that information to be meaningful would exceed any potential benefits. Instead, the Board decided to consider the need for those disclosures on a project-by-project basis. She said that the staff recommends that the Board affirm its earlier decision.

10. All Board members agreed with that staff recommendation.

#### **Statement 107**

11. Ms. MacDonald said that a few respondents questioned the interaction between the disclosures in FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, and the FVM Statement, in particular, whether those disclosures should be consolidated within the FVM Statement. She explained that in its deliberations, the Board decided to keep those disclosure requirements separate. In contrast to the FVM Statement, Statement 107 establishes the requirement to disclose the fair value of financial instruments (as

defined), regardless of whether a financial instrument is recognized in the statement of financial position and, if so, measured at fair value. Also, the disclosures in Statement 107 extend beyond the measurements themselves. Ms. MacDonald said that in view of those differences, the staff recommends that the Board affirm its earlier decision to keep the disclosure requirements separate, but amend Statement 107 to encourage but not require entities to provide the disclosures in the FVM Statement for all financial instruments disclosed at fair value (including loans carried at cost).

12. All Board members agreed with the staff's recommendation.

13. Mr. Trott emphasized that for now, the disclosure requirements in Statement 107 should remain separate but that the Board should consider ways to consolidate those disclosure requirements in other projects (for example, the derivatives disclosure project and the fair value option project). Having those disclosures available in one place would make the related information easier for users to understand. In the intervening period, the FVM Statement should amend Statement 107 to encourage but not require entities to provide the disclosures in the FVM Statement for all financial instruments disclosed at fair value.

14. Ms. Seidman agreed with Mr. Trott. She added that as a practical matter, by encouraging entities to combine the fair value disclosures in the FVM Statement with the fair value disclosures in Statement 107 (and other pronouncements), the disclosures in the FVM Statement likely would be provided for all financial instruments disclosed at fair value under Statement 107 (absent an amendment).

#### **Entities Subject to Disclosure Requirements**

15. Ms. MacDonald stated that in the context of measurement disclosures, some respondents referred to similar information that some entities in certain industries (for example, registered funds) provide in accordance with SEC and other regulatory requirements. They indicated that for those entities, the incremental and potentially overlapping measurement disclosures in the FVM

Statement would not necessarily be useful and, in some cases, might be confusing. She said that the staff acknowledges that concern, but that for the most part, the disclosures referred to by those respondents are made outside the financial statements (for example, in MD&A). Consistent with the Board's codification initiatives in this project and elsewhere, the staff recommends that the Board affirm its earlier decision (to require the measurement disclosures for all entities).

16. All Board members agreed with that staff recommendation.

### **Earnings Disclosures**

17. Ms. MacDonald explained that the earnings disclosures focus on the effect of fair value remeasurements on earnings for the period and, for recurring fair value remeasurements, would require disclosures of unrealized gains or losses. She said that many respondents disagreed with those disclosures. In particular, they emphasized that information about unrealized gains or losses does not provide meaningful information about the quality of earnings and, further, could convey to users that unrealized gains or losses are of a lesser quality than realized gains or losses, which is not the case.

18. Ms. MacDonald said that in response, the staff further considered whether to retain those disclosures (approach a), eliminate those disclosures (approach b), or require expanded disclosures detailing all changes in fair value (approach c). She said that having done so, the staff believes that earnings disclosures would be useful but is concerned about standardizing those disclosures in the FVM Statement (for all financial instruments and entities) without considering further the interaction between those disclosures and the disclosures in other existing pronouncements and users needs. She said that the staff recommends that the Board eliminate the earnings disclosures from the FVM Statement.

19. Mr. Trott generally agreed with that staff recommendation. He said that in his view, the distinction between realized and unrealized gains or losses is not important. Moreover, disclosure of unrealized gains or losses alone does not

provide information about the reasons for the remeasurements. He said that instead, the FVM Statement should require that entities disclose the line item(s) in the income statement in which the earnings effects of fair value remeasurements are reported, whether recurring or nonrecurring.

20. Mr. Young disagreed with that staff recommendation. He said that the distinction between realized and unrealized gains or losses is important and that the related disclosures (focusing on unrealized gains or losses) would provide important information to users. Accordingly, the FVM Statement should retain the disclosures in the FVM ED.

21. Mr. Herz disagreed with that staff recommendation. He said that the distinction between realized and unrealized gains or losses is important, especially with respect to those gains or losses that relate to fair value amounts determined within disclosure levels other than Level 1. He said that the FVM Statement should retain the disclosures in the FVM ED, as clarified and if practicable (where the information is available). In that regard, he referred to respondents' concerns that many entities would not be able to obtain that information from the systems in place currently.

22. Ms. Seidman disagreed with that staff recommendation. She explained that in speaking to constituents about the FVM project, she has conveyed that the earnings disclosures in the FVM ED represent a significant improvement over current reporting and that the measurement disclosures, alone, would be inadequate. She acknowledged that under existing pronouncements those disclosures would apply principally to financial instruments, but said that under proposed pronouncements (for example, in the business combinations project) those disclosures would (and should) apply more broadly. At the same time, however, Ms. Seidman said that she is sympathetic to concerns that many entities would not be able to obtain that information from the systems in place currently. She emphasized that she did not intend to require systems enhancements to comply with the disclosure requirements under the FVM Statement.

23. Ms. Seidman proposed an alternative approach, which would require that all entities disclose the effect of fair value remeasurements in total, that is, total gains or losses (unrealized and realized), preferably by disclosure level, while segregating amounts included in earnings and in other comprehensive income (approach d).

24. All other Board members agreed with approach d, subject to clarification (below).

25. In particular, Ms. Schipper said that in many cases, the distinction between realized and unrealized gains or losses is important because it distinguishes between what has been converted to cash (realized) and what could be converted to cash (unrealized). At the same time, however, Ms. Schipper said that like Ms. Seidman, she did not intend to require systems enhancements to comply with the disclosure requirements under the FVM Statement and is reluctant to do so now. She said that rather than wait until other agenda projects are completed to address this disclosure issue, she would support approach d, provided that the disclosures are only required for each major class of assets and liabilities remeasured at fair value (not by disclosure level).

26. Mr. Herz said that he, too, would support approach d, as clarified by Ms. Schipper, but together with disclosures of unrealized gains or losses, as previously clarified.

27. All Board members generally agreed with approach d, as clarified (to require disclosure of total gains or losses for each major category of assets or liabilities remeasured, segregating amounts included in earnings and in accumulated other comprehensive income), together with the disclosure of unrealized gains or losses relating to disclosure levels other than Level 1 when that information is available.

### **Interim-Period Disclosure Requirements**

28. Ms. MacDonald explained that in the FVM ED, the Board decided to require fair value disclosures in all interim periods and amend APB Opinion No. 28, *Interim Financial Reporting*, accordingly. She said that some respondents disagreed with that decision. In particular, they emphasized that those disclosures, in all interim periods, would not be cost beneficial and referred to constraints caused by accelerated filing requirements.

29. Ms. MacDonald said that with respect to the measurement disclosures, the staff believes that those disclosures, in all interim periods, would provide timely information to users about the remeasurements and factors affecting the relative reliability of the remeasurements during the year. Moreover, they should entail minimal cost, relying largely on the information used to develop the remeasurements. She asked the Board for its views on interim-period reporting, given its decision to retain earnings disclosures.

30. Ms. Seidman said that the FVM Statement should require disclosures in annual periods only, noting that the “feeder” Statements (that is, the Statements that require the fair value measurements that would be disclosed) require disclosures in annual periods only. She said that interim-period disclosures should be limited to material changes, as currently required under Opinion 28. Mr. Batavick agreed.

31. Mr. Young said that the FVM Statement should require interim-period disclosures, but that those disclosures should be limited to quantitative disclosures. The FVM Statement should require other disclosures, in particular, disclosure of the valuation techniques used to estimate fair value, in annual periods only.

32. Mr. Crooch, Mr. Herz, Ms. Schipper, and Mr. Trott said that the FVM Statement should require interim-period disclosures in all cases, but that they would support interim-period disclosures of quantitative information only, as suggested by Mr. Young. In particular, Mr. Trott noted the need for interim-

period disclosures to help educate and communicate to users information about fair value.

33. All Board members generally agreed that quantitative disclosures should be made in all interim and annual periods and that other qualitative disclosures should be made in annual periods only.

#### **Related Codification Initiatives**

34. Ms. MacDonald said that the FVM ED emphasized that consistent with the Board's related codification initiatives in this project and elsewhere, all fair value disclosures should be combined and disclosed together in a single location within the notes to the financial statements. She said that the staff recommends that the Board retain that guidance, as previously discussed (with respect to the disclosures in Statement 107), if practicable.

35. All Board members agreed with that staff recommendation.

#### **Presentation**

36. Ms. MacDonald said that in the FVM ED, the Board decided to encourage but not require tabular presentation of the fair value information disclosed under the FVM Statement, separately for each major class of assets and liabilities remeasured at fair value during the period. She said that the staff recommends that the Board affirm its earlier decision, allowing for narrative disclosures as appropriate to facilitate related codification initiatives.

37. Ms. Seidman and Mr. Trott agreed with that staff recommendation. Mr. Trott emphasized that allowing narrative disclosures would facilitate related codification efforts. In that regard, he referred to disclosures relating to servicing rights as disclosures that might not fit into a table. Other Board members disagreed with that staff recommendation. In particular, they emphasized that because tabular presentation would put all fair value information in one place, it would make it easier for users to understand.

38. The Board generally agreed to require tabular presentation of the fair value disclosures.

## **BLOCKS**

39. Ms. MacDonald explained that in the FVM ED, the majority of the Board at that time decided to allow broker-dealers and certain investment companies to measure large positions of unrestricted securities with quoted prices in active markets (blocks) using blockage factors, as allowed under the AICPA Audit and Accounting Guides for entities in those industries, rather than as the product of the quoted price times the quantity held (PxQ), as required under FASB Statements.

40. She said that nearly all respondents agreed with that decision for broker-dealers, emphasizing the relevance of the resulting measurements (using blockage factors). Other respondents clarified that for investment companies, the exception to PxQ applies only for those investment companies that are not subject to SEC reporting requirements and, even then, only if those investment companies had a practice of using blockage factors prior to May 31, 2000. In that regard, respondents referred to the standstill provision on the use of blockage factors included in the AICPA Audit and Accounting Guide for investment companies.

41. Ms. MacDonald said that at this time, given the change in the Board, the threshold question is whether to affirm the earlier Board decision. She said that respondents did not raise new issues not previously considered by the Board, except, perhaps, with respect to the clarifications for investment companies. Given respondents' overwhelming support for the Board's earlier decision, the staff believes that the Board should continue to allow an exception to PxQ, but only for broker-dealers that both buy and sell blocks as part of their regular ongoing business activities (as indicated in the FVM ED). With respect to investment companies, she said that the staff recommends that the Board eliminate the May 31, 2000, standstill provision included in the AICPA Audit and Accounting Guide and require all investment companies to use PxQ in measuring blocks. In the staff's view, an industry-based exception should similarly apply to all entities within that industry or to none at all.

42. Ms. MacDonald added that a related question for the Board's consideration is whether the FVM Statement should require disclosures about block measurements, whether using PxQ or blockage factors.

43. Mr. Young said that he would prefer to prohibit the use of blockage factors by all entities, referring to definitional and measurement concerns. He further noted that not all such measurements result in discounts; some might result in premiums. He said that block values using blockage factors could be disclosed.

44. Ms. Seidman said that she would prefer to allow the use of blockage factors as a general principle focusing on an entity's business activities, but that she would support the staff recommendation, which is generally consistent with current practice. In that regard, she acknowledged that investment companies have been precluded from using blockage factors since May 31, 2000. However, because prohibiting all investment companies from using blockage factors (including those with a practice of using blockage factors before May 31, 2000) would represent a change to the FVM ED, she asked the staff to discuss the issue with others, in particular, hedge funds, in advance of a final Statement.

45. Mr. Herz said that like Ms. Seidman, he would prefer to allow the use of blockage factors as a general principle focusing on an entity's business activities. At the same time, however, he agreed that the use of blockage factors, without limitation, could lead to abuse (earnings manipulation). Therefore, he also would support the staff's recommendation.

46. Mr. Crooch said that he previously objected to the use of blockage factors because he could not see a way to otherwise limit abuse (earnings manipulation). In retrospect, however, he observed that similar provisions included in other FASB Statements (to limit abuse) add undue complexity. Thus, he would support the staff recommendation and include related disclosures.

47. Mr. Trott agreed with Mr. Crooch, but emphasized that the use of blockage factors is an exception and that the use of blockage factors should be limited as indicated by the staff. He added, however, that his support for the staff recommendation is conditioned upon related disclosures.

48. In that regard, Mr. Trott said that the FVM Statement should require that an entity (broker-dealer) disclose its policies for defining and measuring blocks and the blockage factors used in measuring blocks (amount of any discount or premium). Also, in situations in which an entity sells securities previously held in a block separately (not as a block), the FVM Statement should require that the entity disclose the gain or loss realized on the sale as well as the gain or loss that would have been realized had the entity sold the securities in a block.

49. Ms. Schipper said that she, too, previously objected to the use of blockage factors to measure blocks and that she continues to believe PxQ is the appropriate measure for blocks. She added, however, that she would not object to a Board decision to accept the staff recommendation (allowing the limited use of blockage factors), provided that the exception does not create a treatment alternative, where non-comparability is mitigated through two-way disclosures. Accordingly, her support for the staff recommendation is conditioned on the one-way disclosures suggested by Mr. Trott.

50. Mr. Herz agreed that related disclosures are important, but disagreed with the disclosure of gains or losses on sales of securities separate from a block suggested by Mr. Trott. In particular, he expressed concerns about the incremental record-keeping requirements and complexity that disclosure would impose.

51. Ms. Seidman agreed with disclosure of gains or losses that are realized on sales of securities separate from a block, but not the incremental “what if” disclosures of gains or losses that would have been realized had the securities been sold in a block suggested by Mr. Trott. She said that in her view, such disclosures would not be cost-beneficial.

52. The Board generally agreed to affirm its earlier decision to allow the use of blockage factors, but only for blocks held by a broker-dealer that both buys and sells in blocks as part of its regular, ongoing business activities, subject to further discussion of related disclosures. In that regard, the Board discussed whether the FVM Statement should require that an entity (broker-dealer) disclose its policies for defining and measuring blocks and the blockage factors used in measuring blocks (the amount of any discount or premium). The Board agreed to consider at a future meeting additional disclosures focusing on gains or losses on sales of securities separate from a block (securities that are not subsequently sold as a block). Mr. Herz asked the staff to put together a disclosure package for the Board's review prior to that meeting.

### **SCOPE EXCLUSIONS**

53. Ms. MacDonald said that in its deliberations, the Board decided to exclude from the scope of the FVM Statement pronouncements that (a) specify a fair value measurement objective that is different from the fair value measurement objective in the FVM Statement or (b) otherwise provide related application guidance specific to the assets or liabilities under those pronouncements that might conflict with the related guidance in the FVM Statement. Ms. MacDonald said that few respondents commented on scope. However, those who did said that in a Statement that applies broadly, there should be few, if any, scope exclusions. She said that the staff agreed and, in response, further considered the scope exclusions in the FVM Statement.

### **Share-Based Payment Transactions**

54. Ms. MacDonald explained that in the FVM ED, the Board decided to exclude FASB Statement No. 123, *Accounting for Stock-Based Compensation* and other related pronouncements that address share-based payment transactions from the scope of the FVM Statement because, at that time, the Board had a project on its agenda to reconsider Statement 123. She said that in the intervening period, the Board issued a final Statement that revises Statement 123 and under FASB Statement No. 123 (revised 2004), *Share-Based Payment*, a fair value measure that relies on a definition of fair value generally

consistent with the definition of fair value in the FVM Statement is used as a basis for the measurements required under that Statement. However, its application to share-based payment transactions with employees results in a fair-value-based measure at the grant date that differs from the fair value measure in the FVM Statement. Ms. MacDonald said that largely for that reason, the staff recommends that the Board affirm that scope exclusion. She noted that as a practical matter, the fair-value-based measure in Statement 123(R) is specific to share-based transactions with employees, that those transactions are the principal focus of Statement 123(R), and Statement 123(R) provides extensive detailed guidance for applying its fair-value-based measure to those transactions.

55. All Board members agreed with that staff recommendation.

### **Revenue Transactions**

56. Ms. MacDonald explained that in the FVM ED, the Board decided to exclude pronouncements that require a vendor specific objective evidence (VSOE) of fair value measure for revenue transactions. She said that for the liabilities measured at VSOE of fair value under those pronouncements, the measurement is entity-specific. Further, the “default” to a VSOE of fair value measure allowed under EITF Issue No. 00-21, “Revenue Arrangements with Multiple Deliverables,” emphasizes the use of customer retail prices. In contrast, the FVM Statement would clarify that for liabilities measured at fair value, the measurement is market-based and requires the use of third-party “layoff” prices. She said that largely for that reason, the staff recommends that the Board affirm that scope exclusion.

57. All Board members agreed with that staff recommendation.

### **Leasing Transactions**

58. Ms. MacDonald explained that in the FVM ED, the Board decided to exclude FASB Statement No. 13, *Accounting for Leases*, and other related leasing pronouncements. She said that at that time, the Board was concerned that applying the fair value measure as clarified in the FVM Statement to leasing transactions could have unintended consequences when considered together

with long-standing valuation practices common within the leasing industry. However, some respondents indicated that the fair value measure used for leasing transactions is generally consistent with the fair value measure in the FVM Statement and that the related pronouncements should be included in the scope of the FVM Statement. Ms. MacDonald said that in response, the staff discussed the measurement requirements of those leasing pronouncements with leasing experts, who affirmed that view. She said that based largely on that input received, the staff recommends that the Board eliminate that scope exclusion and include pronouncements for leasing transactions in the scope of the FVM Statement.

59. All Board members agreed with that staff recommendation.

#### **Statement 114**

60. Ms. MacDonald explained that in the FVM ED, the Board decided to exclude FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan*, from the scope of the FVM Statement to distinguish its present value measure for impaired loans from other present value measures used to estimate fair value. She said that respondents acknowledged that those present value measures are different, but that Statement 114 allows a measure that is a fair value measure (fair value of collateral) as a practical expedient and the FVM ED indicates that where the practical expedient is used, the guidance in the FVM Statement would apply. For that reason, respondents said that Statement 114 should be included in the scope of the FVM Statement. Ms. MacDonald said that the staff agrees. Therefore, the staff recommends that the Board eliminate that scope exclusion and include Statement 114 in the scope of the FVM Statement, referring to the different present value measures in the basis for conclusions.

61. All Board members agreed with that staff recommendation.

#### **ARB 43**

62. Ms. MacDonald explained that in the FVM ED, the Board decided to exclude ARB No. 43 Chapter 4, "Inventory Pricing" from the scope of the FVM Statement to distinguish the market value measure that results when measuring

inventories at lower of cost or “market” from a fair value measure. She said that respondents agreed that those measures are different. For that reason, communicating ARB 43 as a scope exclusion is confusing. Ms. MacDonald said that the staff agrees. Therefore, the staff recommends that the Board eliminate that scope exclusion, referring to the different market value measure in ARB 43 in the basis for conclusions.

63. All Board members agreed with that staff recommendation, subject to further clarification. In that regard, Ms. Schipper suggested that in the summary, the FVM Statement communicate that it does not apply to other similar but different measurements (measurements that are not intended to be fair value measurements) under other pronouncements (market value measurements specific to inventories and certain present value measurements). All other Board members agreed.

#### **Practicability Exceptions to Fair Value Measurements**

64. Ms. MacDonald explained that in the FVM ED, the Board decided not to reconsider the practicability exceptions to fair value measurements in other existing pronouncements. She said that at that time, the Board acknowledged the inconsistencies created by those practicability exceptions, particularly with respect to financial instruments, but concluded that those exceptions raise issues about what to measure at fair value that go beyond the scope of the FVM Statement. Ms. MacDonald said that for that same reason, the staff recommends that the Board affirm that scope exclusion.

65. All Board members agreed with that staff recommendation

#### **Follow-up Items:**

66. The Board asked the staff to put together a disclosure package reflecting the decisions reached at the meeting for further consideration at a future meeting (with particular emphasis on blocks and gains or losses on sales of securities previously held in blocks that are sold separately, not in blocks).

#### **General Announcements:**

67. None.



**Board Meeting Handout**

ATTACHMENT

**FAIR VALUE MEASUREMENT PROJECT  
April 27, 2005 Board Meeting**

The Board will continue redeliberations of the proposed FASB Statement, *Fair Value Measurements* (FVM), focusing on issues raised by respondents relating to disclosures, blocks, and scope.

**DISCLOSURES**

In its deliberations, the Board decided that having developed guidance focusing on how to measure fair value, the FVM Statement should include enhanced disclosures about those measurements. For practical reasons, the Board decided to limit the disclosures to fair value remeasurements in periods subsequent to initial recognition, whether on a recurring basis (for example, financial instruments) or nonrecurring basis (for example, impaired assets and assets held for sale).

**1. Measurement Disclosures**

The FVM ED includes disclosures to convey information about how those fair value amounts are determined, indicating the relative reliability of the amounts. Many respondents generally agreed with those disclosures, subject to clarifications and revisions. In response, the Board will discuss whether to:

- a. Establish three disclosure levels that would segregate fair value amounts determined using quoted prices for identical assets and liabilities in active markets (Level 1), other market inputs (Level 2 and Level 3), and entity inputs (Level 4).
- b. Require disclosures about the valuation techniques in which the inputs are used to estimate fair value so that information about the valuation inputs and related valuation techniques are disclosed together within each disclosure level, including Level 1 (indicating where a matrix pricing or other data aggregation technique is used as a practical expedient).
- c. Eliminate the related guidance in paragraph 8 of the FVM ED, which states that valuation techniques used to estimate fair value should be “consistently applied” and, instead, emphasize the valuation objective as previously clarified (to use the valuation technique or combination of valuation techniques that provides the best estimate of fair value in the circumstances).
- d. Affirm its decision to consider the need for disclosures about discount rates and/or significant assumptions used to estimate fair value on a project-by-project basis and not standardize those disclosures in the FVM Statement.

- e. Affirm its decision to keep the disclosure requirements in FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, separate from the disclosure requirements in the FVM Statement.
- f. Affirm its decision that the measurement disclosures in the FVM Statement should be made by all entities that hold assets or liabilities that are recognized in the statement of financial position and remeasured at fair value.

## **2. Earnings Disclosures**

The FVM ED includes disclosures to convey information about the effect of fair value remeasurements on earnings for the period, indicating the “quality” of earnings broadly. With respect to recurring fair value remeasurements (for financial instruments), the related disclosures would segregate unrealized gains or losses relating to those assets and liabilities held at the reporting period and apply for all entities. Many respondents disagreed with those disclosures. In particular, they emphasized that information about unrealized gains or losses does not provide meaningful information about the quality of earnings and, further, could convey to users that unrealized gains or losses are of a lesser quality than realized gains or losses, which is not the case. In response, the Board will discuss whether to:

- a. Retain disclosure of unrealized gains or losses.
- b. Require expanded disclosures that, for each major class of assets and liabilities remeasured at fair value, would reconcile period-to-period changes in fair value, showing changes attributable to purchases, sales, realized gains/losses (segregating realized gains/losses previously unrealized in earnings, previously unrealized in OCI), and realized during the period), unrealized gains/losses (segregating unrealized gains/losses included in earnings and OCI), amortization/accretion, and impairment.
- c. Eliminate earnings disclosures.

### **3. Interim-Period Disclosure Requirements**

The FVM ED would require the fair value disclosures in all interim periods for which a statement of financial position is presented and amend APB Opinion No. 28, *Interim Financial Reporting*, accordingly. Some respondents disagreed with that requirement. In particular, they emphasized that those disclosures, in all interim periods, would not be cost-effective. The Board will discuss whether to affirm that requirement in the context of the fair value disclosures, as revised.

### **4. Related Codification Initiatives**

The FVM ED emphasized that consistent with related codification initiatives, fair value (and other similar) disclosures should be combined and disclosed together in a single location within the notes to the financial statements. The Board will discuss whether to retain that guidance, clarifying that the “other” fair value disclosures include those under Statement 107 and that all fair value disclosures should be combined and disclosed together in a single location within the notes to the financial statements, if practicable.

### **5. Presentation**

The FVM ED would encourage but not require tabular presentation of the fair value information disclosed under the FVM Statement. While some respondents agreed with that decision, others did not. In response, the Board will discuss whether to encourage or require tabular presentation of all or some of the fair value information disclosed under the FVM Statement, as revised.

## **BLOCKS**

In its deliberations, the Board considered measurement issues specific to large positions of unrestricted securities that trade in active markets (blocks) held by broker-dealers and certain investment companies.

Specifically, the Board considered whether the appropriate unit of account is (1) the individual trading unit, where the block is measured as the product of the quoted price times the quantity held (PxQ), as required under existing FASB Statements, which preclude the use of blockage factors or (2) the block, where the block is measured using a blockage factor (at a discount to the quoted price), as allowed under the AICPA Audit and Accounting Guides for broker-dealers and investment companies. The majority of the Board decided that the appropriate unit of account is the block and that the FVM Statement should continue to allow an exception to the requirement to use PxQ in measuring a block, leaving current practice under the AICPA Audit and Accounting Guides unchanged until such time as the Board resolves unit-of-account and other related issues broadly, at the concepts level.

For broker-dealers, many respondents agreed with that decision, emphasizing the relevance of the resulting measurements. For investment companies, however, some respondents clarified that the exception to the requirement to use PxQ in measuring a block applies only for investment companies that are not subject to SEC reporting requirements and, even then, only if those investment companies had a practice of using blockage factors prior to May 31, 2000, referring to the standstill provision on the use of blockage factors included in the AICPA Audit and Accounting Guide for investment companies.

In response, the Board will discuss:

- a. Whether to affirm the exception for broker-dealers, clarifying that the exception for block measurements only applies for those broker-dealers that both buy and sell blocks as part of their regular, ongoing business activities.
- b. Whether to affirm the exception for investment companies that are not subject to SEC requirements or otherwise affected by the May 31, 2000 standstill provision or, alternatively, whether to eliminate the May 31, 2000, standstill provision and require the use of PxQ for block measurements by all investment companies.
- c. Whether to require disclosures about block measurements.

## SCOPE EXCLUSIONS

Few respondents commented on scope. Those that did, however, said that in a Statement that applies broadly, there should be few, if any, scope exclusions. In response, the Board will discuss whether to affirm all or some of the scope exclusions identified in the FVM ED, focusing on the following:

- a. Pronouncements that address share-based payment transactions, in particular, FASB Statement No. 123 (revised 2004), *Share-Based Payment*.
- b. Pronouncements that require a vendor-specific objective evidence (VSOE) of fair value measure for revenue transactions, in particular, AICPA Statement of Position 97-2, *Software Revenue Recognition*, as modified by AICPA Statement of Position 98-9, *Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*, and EITF Issues No. 00-3, "Application of AICPA Statement of Position 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware," and No. 00-21, "Revenue Arrangements with Multiple Deliverables."
- c. Pronouncements that use a fair value measure in accounting for leasing transactions, in particular, FASB Statements No. 13 and 98, *Accounting for Leases*, FASB Interpretations No. 23, *Leases of Certain Property Owned by a Governmental Unit or Authority*, and No. 24, *Lease Involving Only Part of a Building*, and FASB Technical Bulletins No. 86-2, *Accounting for an Interest in the Residual Value of a Leased Asset*, and No. 88-1, *Issues Relating to Accounting for Leases*.
- d. FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan*.
- e. ARB No. 43, Chapter 4, "Inventory Pricing."
- f. Practicability exceptions to fair value measurements in other pronouncements, in particular, APB Opinion No. 29, *Accounting for Nonmonetary Transactions*, FASB Statements No. 87, *Employers' Accounting for Pensions*, No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*, No. 140, *Accounting for Transfers and Servicing of financial Assets and Extinguishments of Liabilities*, and Statement 107, and EITF Issues No. 99-17, "Accounting for Advertising Barter Transactions," and No. 85-40, "Comprehensive Review of Sales and Marketable Securities with Put Arrangements."