

MINUTES



To: Board Members

From: Servicing Rights Team (Varian, ext. 353)

Subject: Minutes of the April 13, 2005 Board Meeting (Servicing Rights) **Date:** April 19, 2005

cc: Bielstein, L. Smith, Petrone, Wilkins, Lott, E. Smith, Laurenzano, Varian, Bullen, Donoghue, Lusniak, Bergstrom, Kapko, Thompson, Gabriele, Sutay, 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: Comment period and effective date for measurement issues related to the Servicing Rights, Beneficial Interests and QSPE projects and transition issues related to the Servicing Rights project.

Basis for Discussion: Servicing Rights Memorandums 8 and 9, and QSPE Memorandum 48

Length of Discussion: 9:00 am to 11:15 am

Attendance:

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

Board members absent: Herz

Staff in charge of topic: Laurenzano

Other staff at Board table: L. Smith, Lott, E. Smith, Donoghue, Lusniak, Bergstrom, Kapko, Varian

Outside participants: Leisenring

Summary of Decisions Reached:

At today's meeting, the Board completed deliberations on the issues presented in the servicing rights, beneficial interests, and QSPE projects.

The Board decided for all three projects—

1. To expose the Exposure Drafts for a comment period of 60 days.
2. To require that the application of the measurement provisions be effective at the earlier of fiscal years beginning after December 15, 2005, or fiscal years that begin during the quarter in which the final Statement is issued.

Specifically, the Board decided for the servicing rights project—

3. To require that the initial measurement of all servicing rights at fair value be applied prospectively to new servicing rights recognized.
4. To require that the option to subsequently measure servicing rights at fair value be applied prospectively to all new servicing rights recognized after the election to subsequently measure at fair value is made and to all existing servicing rights on the date the election is made with a cumulative effect adjustment to reflect existing servicing rights at fair value upon election.
5. To include in the Exposure Draft's notice to recipients a request that asks constituents whether they believe entities should be permitted in conjunction with the adoption of the final Statement to transfer all securities from the available-for-sale category to the trading category without calling into question an entity's treatment of such securities under FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*.

Objective of Meeting:

The objective of the meeting was for the Board to decide on the effective date, transition, and comment period for the Exposure Drafts to amend FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, as well as the other Statement 140-related Exposure Draft.

Matters Discussed and Decisions Reached:

1. The staff presented a joint recommendation for the comment period and the effective dates for decisions related to measurement that will be used in each project's Exposure Draft. In regard to the length of comment period, the staff recommended a comment period of 60 days. In making this recommendation, the staff asked the Board to reconsider the staff's previous recommendation in the QSPE project for a 45-day comment period. The staff noted that the longer comment period is recommended because (a) three separate Exposure Drafts amending Statement 140 will be issued concurrently and (b) additional guidance has been provided for the isolation requirement, the requirements for transferring portions of financial assets, and the accounting for portions of transferred assets held by the transferor. Six Board members agreed to a 60-day comment period. Mr. Herz was not present and did not provide Mr. Trott with his proxy on this issue.

2. The staff recommended that the measurement provisions that will be included in each of the three Exposure Drafts be drafted as follows:

The application of the measurement provisions will be effective at the earlier of fiscal years beginning after December 15, 2005, or fiscal years that begin during the quarter in which a final Statement is issued.

3. The staff indicated that while this recommendation could make the measurement guidance applicable soon after or even before the expected issuance date of the final Statements, the staff believes that the application of

the measurement provisions should not be overly burdensome because the fair value information is already required to be obtained for initial recognition and subsequent impairment analysis and disclosure. The staff noted that some constituents have already indicated that they would like to apply the measurement provisions as soon as possible. All of the Board members present agreed with the staff's proposed effective date for the measurement provisions included in the three Exposure Drafts. Mr. Herz had provided Mr. Trott with an affirmative proxy on this issue.

4. Mr. Laurenzano then began discussing issues related to the servicing rights project. He presented the following decisions, which the Board had previously decided in this project:
 - a. Servicing rights should be initially measured at fair value.
 - b. Entities have the option of subsequently measuring servicing rights at fair value or lower of cost or carrying amount, as long as this option is applied to all servicing rights in a class of servicing rights.
 - c. The election to use fair value may be made at any time subsequent to the adoption of the statement, but each election may not be reversed.
 - d. Additional qualitative and quantitative disclosures are required to breach the comparability gap that the option to use fair value causes.
5. In regard to the decision to measure all servicing rights at fair value, Mr. Laurenzano presented the following three alternatives:
 - A. Prospective for new servicing rights recognized
 - B. Prospective for new and existing servicing rights recognized, with a cumulative effect adjustment to reflect the existing servicing rights as if they were initially measured at fair value
 - C. Retrospective application.
6. Mr. Laurenzano stated that the staff recommends Alternative A as it is the most practical approach given that the cumulative effect adjustment is expected to be minimal and that Alternatives B and C would require significant effort for little impact. Six members agreed with the staff

recommendation. Mr. Herz was not present and did not provide Mr. Trott with his proxy on this issue.

7. In regard to the option to subsequently measure servicing rights at fair value, Mr. Laurenzano presented the following three alternatives:
 - A. Prospective for all new servicing rights recognized after the election to subsequently measure at fair value is made.
 - B. Prospective for all new servicing rights recognized after the election is made and servicing rights that exist on the date of initial election, including the cumulative effect adjustment to reflect existing servicing rights at fair value.
 - C. Retrospective application.
8. Mr. Laurenzano recommended Alternative B as that alternative is consistent with the requirement to apply the measurement attribute to all servicing rights in each class. He stated that this alternative ensures that all servicing rights in each class are measured consistently on a prospective basis. He noted that this alternative also avoids earnings distortion associated with servicing rights by not allowing unrealized gains on existing servicing rights to be reflected as part of the mark to market adjustment in the first period after election as part of operations.
9. Mr. Trott asked the Board to discuss the transition requirements related to the election of the option upon issuance of the final Statement separately from the transition requirements for the election of the option any time subsequent to the issuance of the final Statement. Six Board members agreed with Alternative B with regard to the transition requirements for the initial election of the option upon issuance of the final Statement. Mr. Herz was not present and did not provide Mr. Trott with his proxy on this issue. Mr. Batavick asked the staff to consider including a simple example in the Exposure Draft that illustrates the proposed transition provisions.
10. Mr. Laurenzano also recommended Alternative B for the transition requirements related to the election of the option subsequent to the initial

adoption of the Statement. He observed that the retrospective application alternative (Alternative C) is consistent with the guidance expected to be provided for voluntary changes in accounting principle in the final document on accounting changes and error corrections, which is due out shortly. He recommended that for this change, retrospective application not be applied given the difficulty in determining management's intention with classes of servicing rights that were not used as a way to group servicing rights in prior periods. Additionally, he recommended Alternative B due to practical concerns related to the retrospective application of an option that will be available at initial adoption and the beginning of every subsequent year.

11. Mr. Trott stated that the expected Statement on accounting changes will provide the Board with the ability to modify transition provisions in individual statements issued. He further stated that even if the final Statement on accounting changes was followed in this instance, it would be impracticable to apply the change retrospectively given that it may not be possible to independently substantiate management's intent during prior periods.
12. Mr. Leisenring expressed concern with respect to Alternative B because the final Statement on accounting changes will require that voluntary accounting changes be applied retrospectively whereas the guidance on servicing rights will not permit retrospective application for this specific voluntary accounting change. He stated that it is unreasonable to issue a Statement on voluntary accounting changes if the Board is going to require different transition provisions in subsequent Statements that have voluntary treatment alternatives.
13. Five Board members agreed with the staff recommendation (Alternative B). Mr. Herz had provided Mr. Trott with an affirmative proxy on this issue. Ms. Schipper supported Alternative C.
14. Mr. Lott questioned the application of the election at the beginning of the fiscal year after the election is made. He stated that this implies that there has to be some documentation about when the election was made. For

example, he questioned how auditors would determine that the election was made in the fourth quarter of the previous year and not the first quarter of the current year. Mr. Laurenzano stated that he will draft the Exposure Draft so that it states the subsequent election for a class of servicing rights must be applied as of the beginning of a fiscal year. Six Board members agreed. Mr. Herz was not present and did not provide Mr. Trott with his proxy on this issue.

15. Mr. Laurenzano recommended that entities be permitted to transfer all securities that used to economically hedge their servicing rights from the available-for-sale category to the trading category without calling into question an entity's treatment of such securities under Statement 115. He further recommended that this option only be available upon initial adoption of the final Statement. He noted that this restriction is suggested as it anticipates that entities employing this strategy would apply the fair value option to servicing rights as soon as possible. Additionally, he stated that he believes that not limiting the timing of the ability to transfer would weaken the usefulness of Statement 115.
16. Mr. Trott questioned whether this option could be limited to transfers of instruments related to servicing rights. Ms. Schipper stated that, as currently drafted, it would apply to any available-for-sale security, and she questioned whether any entity would be permitted to make this election. Mr. Wilkins stated that this option would be available at the initial adoption of the Statement, and, therefore, if an entity did not have servicing rights, they would not be able to take advantage of this option. He further stated that this option would permit entities with servicing rights to make this election even if they do not decide to measure their servicing rights at fair value upon initial adoption of this Statement.
17. Mr. Trott suggested that this option not be included in the Exposure Draft but that the Board ask constituents (1) whether they would be in favor of this option, (2) if they could provide any suggestions on how to limit the option,

and (3) whether they believe this transfer would be included as a part of the cumulative effect adjustment. Six Board members agreed to including these questions in the notice for recipients. Mr. Herz was not present and did not provide Mr. Trott with his proxy on this issue.

18. Six Board members agreed to the staff drafting the Exposure Draft. Five Board members stated that they would not be presenting an alternative view in this Exposure Draft. Ms. Schipper stated that she will make that decision after further discussion with the staff. Mr. Herz was not present and did not provide Mr. Trott with his proxy on this issue.

Follow-up Items:

None.

General Announcements:

None.