



Financial Accounting Standards Board

MINUTES



Financial Accounting Standards Board

To: Board Members
From: Hurst (ext. 262)
Subject: Minutes of the July 16, 2003 Board Meeting **Date:** July 17, 2003
cc: Bielstein, Smith, Petrone, FVM Team, Bossio, Tovey, Swift, Polley, Gabriele, Thompson, Mahoney (e-mail), Leisenring (IASB), Sutay, FASB Intranet

Topic: Scope Issues

Basis for Discussion: Memorandum dated July 2, 2003 and July 15, 2003; audience handout (attachment)

Length of Discussion: 9:00 a.m. to 10:10 a.m.

Attendance:

Board members present: Crooch, Herz, Schieneman, Schipper (by phone), Seidman, Trott
Board members absent: None
Staff in charge of topic: MacDonald
Other staff at Board table: Bielstein, Bossio, Hurst, McKenna, Munro
Outside participants: None

Summary for ACTION ALERT

The Board discussed the scope of the initial phase of the project. The Board generally agreed:

- To address at some level the remaining measurement issues identified but not yet addressed in the Replacement of FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, project, prioritizing issues relating to unit of account and reference market, and including issues relating to the measurement of restricted stock.

- Not to address issues relating to EITF Issue No. 02-03, “Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities,” (Issue 2) in this project.

The Board asked the staff to consider the need to address other measurement issues in determining amendments to either eliminate or carry forward (codify) fair value measurement guidance in existing accounting pronouncements. The Board also requested that the staff develop a plan prioritizing all remaining issues for purposes of assessing the timing of the project, in particular, whether it will be possible to issue an exposure draft in this project concurrently with an exposure draft in the business combinations project.

Matters Discussed and Decisions Reached

Ms. MacDonald asked Board members what, if any, additional measurement issues should be addressed in the initial phase of the project, referring to the issues identified on the audience handout (attached).

1. General Measurement Guidance

The Board generally agreed with the proposed clarifications indicated on the audience handout. In addition:

- Mr. Herz suggested that the staff clarify that the estimate of fair value is based on the (hypothetical) price for an item if that item were exchanged in a transaction between willing parties when neither party is acting under compulsion, even if the item currently could not be exchanged in an actual transaction.
- Mr. Trott emphasized the need to refer to a going-concern or in-use valuation premise as a *valuation premise*, separate from a *measurement attribute*, clarifying the purpose of the valuation premise as identifying the relevant market inputs.

2. Measurement Guidance Relating to Financial Instruments

The Board generally agreed to address the remaining measurement issues identified but not yet addressed in the Replacement of FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, project, prioritizing issues relating to unit of account and reference market.

Mr. Trott referred to the interaction between issues relating to the unit of account and reference market and other measurement issues (including issues previously addressed by the Board). He said that resolving those issues should help to resolve measurement issues not previously addressed as well as test the Board's decisions on measurement issues it has previously addressed (for example, issues relating to blockage factors). Other Board members agreed.

Mr. Trott further emphasized the need to consider in this project issues relating to the measurement of restricted stock, referring to related efforts in the Board's project on stock-based compensation.

Mr. Herz also emphasized the importance of considering the practices and principles recommended by the Group of Thirty (G30).

The Board decided not to address issues relating to EITF Issue No. 02-03, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," (Issue 2) in this project because they involve recognition issues that are beyond the scope of this project.

Follow-up Items:

The Board asked the staff to consider the need to address other measurement issues in determining amendments to either eliminate or carry forward (codify) fair value measurement guidance in existing accounting pronouncements. The Board also requested that the staff develop a plan prioritizing all remaining issues for purposes of assessing the timing of the project, in particular, whether it will be possible to issue an exposure draft in this project concurrently with an exposure draft in the business combinations project.

General Announcements:

None.



**Board Meeting Handout
FAIR VALUE MEASUREMENT PROJECT**

At its July 16, 2003 meeting, the Board will discuss what, if any, additional guidance beyond that previously discussed by the Board (including the need to address issues relating to the guidance for using present value techniques to estimate fair value in CON 7) should be included in the scope of the Fair Value Statement developed in the initial phase of this project.

1. General Measurement Guidance

The Board previously decided to include in the scope of the Fair Value Statement the general measurement guidance developed in the business combinations project, subject to certain clarifications. Proposed clarifications are discussed below.

- a. The Board decided to revise the fair value definition to refer to “the amount at which an asset or liability could be exchanged in a current transaction between knowledgeable, unrelated willing parties when neither party is acting under compulsion.”
 - (i) Some Board members indicated that the emphasis on a current exchange transaction could be interpreted as excluding situations in which a liability is settled. *Should the fair value definition be further revised to refer to an asset or liability that could be exchanged or settled or, alternatively, should additional guidance clarify that an exchange transaction includes the settlement of a liability?*
 - (ii) Some Board members also indicated that the reference to willing parties that are not acting under compulsion could be interpreted as excluding certain transactions occurring in the normal course of business, such as regulator-imposed asset sales. *Should additional guidance refer to an exchange between willing parties in a transaction motivated by normal business considerations, that is, other than in a forced liquidation transaction or distress sale?*
- b. The Board decided to specify that a “going-concern or in-use” valuation premise, referred to as *fair value in use*, be used to measure the fair value of assets held and used indicating, however, the need to distinguish between *in-use* as a valuation premise and *value in use* as a measurement attribute. *Should additional clarifying guidance be developed based on the discussion of value in use in CON 7 (paragraph 24), which distinguishes between fair value and value in use by reference to market-based and entity-specific inputs, respectively?*

The staff prepares Board meeting handouts to facilitate the audience's understanding of the issues to be addressed at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect the views of the FASB or its staff. Official positions of the FASB are determined only after extensive due process and deliberations.

2. Measurement Guidance Relating to Financial Instruments

The Board previously decided to include in the scope of the Fair Value Statement measurement guidance relating to financial instruments, including the guidance developed in the FAS 107 project. *Does the Board wish to address (or reconsider) any of the measurement issues previously identified (or discussed) in the FAS 107 project?*

- a. Measurement issues not necessarily specific to financial instruments previously identified but not addressed in the FAS 107 project include:
 - (i) How to define an active market.
 - (ii) How to define transaction costs (not considered in fair value estimates).
 - (iii) How to define the unit of account for an item and, for purposes of identifying the appropriate reference market (and unit of account) in situations in which an entity has access to multiple markets with different prices, how to determine when an entity has “reasonable access” to a market, how to define related “market access” costs, and whether market access costs should be considered in fair value estimates.
 - (iv) How to determine when a transaction price used to estimate fair value becomes “stale.”
- b. Measurement issues specific to financial instruments previously discussed in the FAS 107 project but that the Board might want to reconsider include:
 - (i) Whether to retain its decision to apply the revised fair value definition (and its exchange notion) to financial instruments.
 - (ii) Whether to retain its decision to require that unrestricted equity securities be measured at PxQ, prohibiting adjustment for blockage factors (discounts).
 - (iii) Whether to retain its decision to require that restricted equity securities be measured at PxQ, adjusted for the nature and duration of the restriction and the risk-free interest rate.
 - (iv) Whether to retain its decision to require that fair value estimates be based on the mid-point of a bid-ask spread if the bid-ask spread is created by firm offers to buy and sell in an active market.
- c. Measurement issues specific to financial instruments previously identified but not addressed in the FAS 107 project include issues relating to EITF Issue 02-03 (Issue 2) and measurements involving guarantees.