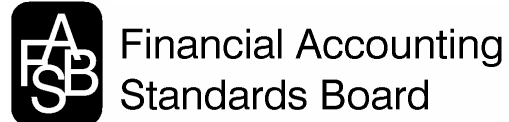


MINUTES



To: Board Members

From: Auction Rate Securities Team
(Duke, ext. 297 and Trench, ext. 455)

Subject: Minutes of the October 5, 2005 Board Meeting--ARS **Date:** October 14, 2005

cc: L. Smith, Bielstein, Petrone, Golden, Belcher, Jacobs, Gabriele, Leisenring, Getz, Carney, Swift, Polley, Mahoney, Project Team, 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: Agenda Decision: Definitions of Cash and Cash Equivalents under FASB Statement No. 95, *Statement of Cash Flows*

Basis for Discussion: Memorandums dated September 22 and October 3, 2005

Length of Discussion: 9:55 a.m. to 10:15 a.m.

Attendance:

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

Board members absent: None

Staff in charge of topic: Trench

Other staff at Board table: L. Smith, Golden, Belcher, and Duke

Outside participants: Leisenring

Summary of Decisions Reached:

The Board considered but decided not to add a project to its technical agenda, at this time, to address the financial statement classification of auction rate securities (ARS) pursuant to the definition of cash equivalents under FASB Statement No. 95, *Statement of Cash Flows*. A majority of Board members were in favor of the staff bringing this agenda topic back to the Board once staff resources become available.

Objective of Meeting:

The objective of the meeting was for the Board to decide whether to add a project to its agenda to address the financial statement classification of ARS pursuant to the definition stated in Statement 95. The objective was met; however, as noted in the Summary of Decisions Reached, a majority of Board members were in favor of the staff bringing this agenda topic back to the Board once staff resources become available.

Matters Discussed and Decisions Reached:

1. Mr. Trench stated that the staff would ask Board members to consider whether to add a project to its agenda to address the financial statement classification of ARS pursuant to the definition stated in Statement 95. He stated that, in practice, ARS were historically classified as cash equivalents due to the periodic interest rate reset and the liquidity provided by a dutch auction. However, the stated maturity of these securities often ranges between 20 to 30 years. Failed auctions, while rare, could occur if investors were selling more securities than the market demanded and no clearing bid was received. While underwriting brokers and dealers running the auction can enter a clearing bid, they are under no legal obligation to do so.
2. Mr. Trench stated that in late 2004 and early 2005, the auditing community questioned the historical classification of these securities as cash equivalents due to the long-term maturity and the fact that liquidity is provided by third-party market participants (which is generally associated with long-term investments). This resulted in entities that classified these investments as

cash equivalents to reclassify them out of cash equivalents and in some cases led to restatements. The preparer community believes that the highly-liquid nature of these securities along with the “par-in, par-out” nature of these securities would allow ARS to be considered as cash equivalents.

3. Mr. Trench stated that the staff has developed two alternative approaches to address the issue:
 - a. Approach A—Not add a project to address this issue.
 - b. Approach B—Add a project to the Board’s agenda that revisits the definition of cash equivalents in Statement 95 from the perspective that the characteristics of ARS may not have been contemplated when Statement 95 was issued.

4. Mr. Trench stated that the staff recommended that the Board not add a project to its agenda to revisit the definition of cash equivalents (Approach A). While the staff is sympathetic with the argument that there are similarities between cash equivalents and ARS from the perspective of liquidity, the staff believes that undertaking a project of this nature may, in all likelihood, result in considerable expansion of what is considered a cash equivalent, and will divert staff resources from existing agenda projects. He then turned the matter over to the Board for deliberation.

5. Mr. Batavick stated that while he was sympathetic to the issue, the Board currently has ten major projects, seven technical application and implementation projects, around twenty FASB Staff Positions (FSPs), and a handful of research projects on its technical agenda for the next six months. Additionally, agenda decisions concerning the accounting for pensions and leases are coming soon. Mr. Batavick stated that he was not in favor of adding a project because he did not believe there were any Board or staff resources to allocate to this project at this time. He stated that he supported revisiting the topic if there is a significant reduction in the FSP docket.

6. Mr. Young stated that the Board should add a project to its agenda to address the accounting for ARS. With a 200 billion dollar market, this is a significant issue. The quantitative data (in relation to default statistics) suggests that the performance of these securities is higher than some securities that are considered to be cash equivalents today. To be representationally faithful, ARS also should be classified as cash equivalents. When the Board is faced with issues like this, then everything should be done to correct them. He stated that ARS are effectively cash equivalents and that if Statement 95 was principles-based instead of rules-based, that ARS would be classified as cash equivalents. Because Statement 95 is rules-based, it has not stood the test of time because securities such as ARS were not contemplated at the time it was written. He stated that the preparer and users are not being served by the inability to classify ARS as cash equivalents.
7. Mr. Crooch asked what the current status of these securities are in practice and whether the issue has been resolved.
8. Mr. Smith stated that as a result of the guidance issued by the major accounting firms, a large number of companies have reclassified these securities on their balance sheets so that ARS are no longer considered cash equivalents.
9. Mr. Young asked about Variable Rate Demand Obligations (VRDOs). He asked if accounting firms issued guidance on VRDOs that is similar to the guidance issued for ARS, and if the Board would consider that issue.
10. Mr. Smith stated that the issue concerning VRDOs has not been brought to light by the major accounting firms at this time.
11. Mr. Young stated that he did not want to see a market shut down by an obsolete accounting rule, but that is effectively what happened to the ARS market. Ms. Seidman stated that there has been a 50 percent decrease in the issuance of ARS since the issuance of the new firm guidance.

12. Mr. Crooch stated that he would not add a project to the agenda. As an aside, he stated that this is a good example of why the word “generally” should not be used in a standard.
13. Ms. Schipper agreed with the staff recommendation. The fact that ARS rely on the behavior of third parties, and not the issuer, for their liquidity seemed to her to be almost dispositive as to whether ARS would meet the intent of the Board that crafted Statement 95.
14. Ms. Seidman stated that she agreed with Mr. Batavick. She stated that the issue was not of sufficient priority to displace other issues on the Board's agenda. She stated that she would consider adding the project to the agenda in the future if the list of FSP issues currently being addressed clears and this issue persists. She stated that she would envision a project that would revisit the definition of a cash equivalent. She also stated that the basis for conclusions to Statement 95 contains a great principle about classifying extremely liquid securities as cash but that the additional rule hinders the principle.
15. Mr. Herz stated that he agreed with Mr. Young. He stated that the accounting for ARS is an important issue and that he does not agree with the conservative interpretation that has been put into practice. He stated that money market funds are an example of a cash equivalent that does not have a maturity date that meets the rule, as the accounts do not have a legal maturity date. He stated that ARS meet the principle in Statement 95 through the credit characteristics which provide an insignificant risk to cash flows. The market is disserved by treating similar securities differently. When the key attributes are similar, then the accounting treatment should be similar. By focusing on the bright-line, the principle is not well served. He stated that he is chagrined by the Board not taking this project on over projects that are a result of the accounting firms asking for more of a bright-line. By not taking on this project, the FASB fails in its mission to look at emerging issues and address them.

16. Mr. Trott stated that he would not add the project to the Board's agenda. He stated that the issue would come into play with the financial performance reporting by business enterprises project in Segment B, when the Board considers the definition of a financing cost and whether and how the cost is netted. He stated that he disagreed with Mr. Herz on replacing other issues on the Board's agenda with this one. He stated that he does not believe that ARS meet the Statement 95 requirements for classification as cash equivalents.

17. Mr. Smith stated that he understood that five Board members (GJB, GMC, KAS, LFS, and EWT) did not support adding the project to the agenda; however, two of those Board members (GJB and LFS) favored revisiting the issue if staff resources become available. Two Board members (RHH and DMY) voted to add the project to the Board's agenda. Because two Board members' decisions were based upon the availability of staff resources, Mr. Smith posed the question to the Board that if staff resources become available would the Board want the staff to begin working on the project or return to the Board for approval to proceed. Mr. Trott indicated that he would prefer that the staff bring the issue back to the Board before commencing work on the project and the other Board members agreed.

18. Mr. Batavick reiterated that he would be interested in revisiting the issue if space opens up on the Board's agenda. Ms. Seidman concluded by stating that she wanted to learn if the meeting raised any concerns with the non-Big 4 constituency about a broader need to address the issue.

Follow-up Items:

None.

General Announcements:

None.