MINUTES

To:	Board Members
From:	Beneficial Interests Team (Bergstrom, ext. 296)
Subject:	Minutes of the April 13, 2005 Board Meeting (Beneficial Interests)
Date:	April 20, 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, effective date, transition, and disclosure issues related to the Beneficial Interests Project.

Basis for Discussion: Beneficial Interests Memorandum 13

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: E. Smith

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

Outside participants: Leisenring

<u>Summary of Decisions Reached</u>:

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 establish 60-day comment periods for the Exposure Drafts.
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 Statements are issued.

Separately, the Board decided for the beneficial interests project—

3. To require no incremental disclosures in regard to the Board's decision to allow a fair value option election for hybrid financial instruments with embedded derivatives that otherwise would require bifurcation
4. To apply the decisions reached in the beneficial interests project prospectively to only new transactions.

Objectives of the Board Meeting

The objectives of the meeting were for the Board (1) 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 and (2) to discuss potential refinements to the definition of a participating interest.

Matters Discussed and Decisions Reached:

The following paragraphs summarize the Board's views on the major issues discussed at the meeting. The views and matters presented in these minutes may not be in the specific order in which they were discussed at the meeting.

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 the 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. E. Smith presented the issue of transition of the proposed guidance in the beneficial interests project. He stated that issues regarding transition concerned two populations: (a) existing investments and (b) prospective investments. Further, existing investments can be broken into two subsets:

   (1) Beneficial interests that have used the Statement 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets," exemption and have not been evaluated for bifurcation under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*.

   (2) Hybrid Financial Instruments (instruments that have a combination of a host and a derivative that are already bifurcated and measured at fair value.

5. Mr. E. Smith then described two transition alternatives for these types of beneficial interests.

   a. Apply the fair value election prospectively to only new transactions. Under this alternative, the fair value election would be available only for transactions entered into after the effective date of the Statement and would not be available to hybrid financial instruments existing at the effective date that would have been bifurcated under existing requirements of Statement 133.

   b. Apply the bifurcation requirements initially to all existing instruments and prospectively to new transactions.

6. Ms. Seidman introduced a third alternative which would apply prospectively to all new transactions and allow an entity to mark to market, on an all or nothing basis, the entity's existing hybrid financial instruments that have been bifurcated at the effective date of the new guidance. Ms. Seidman believed that such a provision would simplify the application of Statement 133.

7. Mr. E. Smith noted the staff's concern that it would be burdensome at transition to require a full evaluation of interests that fell under the temporary

exemption from the bifurcation requirements of Statement 133 provided by Implementation Issue D1. Also, Mr. E. Smith noted that he believed that if the fair value election were to be allowed for bifurcated items, it would be necessary to allow the election to be applied on an instrument-by-instrument basis, which would allow an entity to “cherry pick” the instruments that it wanted to mark to fair value to achieve a desired accounting result.

8. Mr. Trott noted that one of the reasons for the bifurcation requirement was to allow the bifurcated derivative to act as a qualified hedging instrument. Mr. Trott stated his support for the staff’s recommendation, Alternative A, because existing bifurcated derivatives have already been separated and consequently the derivative is already being marked to fair value and the accounting for the host has already been established. The other five Board members in attendance agreed with Alternative A.

9. Ms. Seidman noted that under the proposed guidance in the fair value option project, a bifurcated hybrid instrument for which the derivative is being used as a hedging instrument would allow the host object being hedged to be marked to fair value, which would achieve accounting simplification for derivatives, but noted her support for Alternative A at this time. However, Ms. Schipper expressed her concern that the expansiveness of the fair value option project has yet to be determined and did not feel comfortable relying on what might happen in the fair value option project in determining transition of the of the fair value election guidance in the beneficial interests project.

10. Mr. E. Smith then introduced possible disclosure requirements related to the Board’s decision to allow a fair value option election for hybrid financial instruments with embedded derivatives that otherwise would require bifurcation. The election results in two possible outcomes: (A) a hybrid instrument subject to bifurcation will be identified, and the hybrid will be bifurcated into a host contract and a derivative instrument or (B) a hybrid instrument subject to bifurcation will be identified, but the fair value option will be elected resulting in the hybrid being accounted for as a single instrument

at fair value with changes in fair value recognized in earnings. Mr. E. Smith noted that the staff analyzed whether additional disclosure would be necessary in instances in which an entity elected to account for the hybrid instrument as a single instrument at fair value (outcome B) and provided four possible alternative disclosure requirements:

a. Do not require any incremental disclosures.

b. Require incremental qualitative disclosures.

c. Require incremental qualitative and quantitative disclosures.

d. Require disclosure consistent with the International Accounting Standards Board's Exposure Draft 7, *Financial Instruments: Disclosures.*

11. Mr. E. Smith noted that the staff believed that no incremental disclosure was necessary and, consequently, recommended Alterative A. However, Ms. Seidman did make note that she expects the fair value option project to develop a set of disclosures that would apply to situations in which an entity elected to account for a hybrid instrument as a single financial instrument at fair value and suggested that the Board consider expanding this area of derivatives disclosures because there are currently no disclosure requirements, even on a qualitative basis, concerning why an entity is holding an embedded derivative or how they fit into the overall risk profile of the entity. Mr. Young expressed a timing concern about the other projects (specifically the fair value measurement project and the derivatives disclosure project) that would incorporate related disclosure requirements for hybrid instruments not being implemented before the proposed guidance in the beneficial interests project becomes GAAP. The Board generally agreed with Mr. Young's concern but unanimously agreed to move forward with no incremental disclosure requirements being included in the beneficial interests project under the assumption that if the timing of the other related projects did not occur as anticipated, the Board would address the disclosure issue again in redliberations. Mr. Trott mentioned that Mr. Herz was in support of the staff's recommendation as well.

12. The Board unanimously approved the staff's request to begin drafting the beneficial interests Exposure Draft and confirmed that no Board member intends on including an alternative view in the Exposure Draft.

Follow-up Items:
None

General Announcements:
None