MINUTES

Financial Accounting Standards Board

To:	Board Members
From:	Burnap (x283)
Subject:	January 23, 2009, Board Meeting Minutes: Disclosures for Certain Financial Assets
Date:	February 23, 2009
cc:	Leisenring, Golden, Bielstein, Stoklosa, Trench, Laungani, Lott, Proestakes, Allen, Wilkins, C. Smith, Brickman, Malcolm, Homant, Pfeiffer, Maroney, Mussatt, Chookaszian, Posta, Gabriele, Finden, Sutay, FASB Intranet, Klimek

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, Interpretation, or FASB Staff Position.

Topic:	Proposed FSP FAS 107-a, *Disclosures about Certain Financial Assets*
Basis for Discussion:	Board Memorandum No. 9
Length of Discussion:	9 a.m. to 10:15 a.m.

Attendance:

Board members present:	Herz, Linsmeier, Seidman, Siegel, and Smith
Staff in charge of topic:	Trench and Laungani
Other staff at Board table:	Golden, Stoklosa, C. Smith, Glotzer, and Burnap

Summary of Decisions Reached:

The Board discussed the issues raised by respondents in comment letters received on proposed FSP FAS 107-a, *Disclosures about Certain Financial Assets: An Amendment of FASB Statement No. 107,* and decided not to finalize the proposed FSP.

The Board decided to issue a new proposed FSP that would amend FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, to require interim and annual disclosures of fair value measurements for all financial instruments within the scope of that Statement. The Board also decided that the proposed FSP would reiterate qualitative disclosure requirements in Statement 107 and FASB Statement No. 157, *Fair Value Measurements.*

The Board decided that entities should provide the disclosures in Statement 107 for interim and annual periods ending after March 15, 2009. The Board expects to issue a proposed FSP on or around January 30, 2009, with a 30-day comment period. The Board directed the staff to proceed to a draft of a proposed FSP for vote by written ballot.

Objective of Meeting:

The objectives of this meeting were to discuss the comment letters received from constituents on the proposed FASB Staff Position (FSP) FAS 107-a, *Disclosures about Certain Financial Assets: An Amendment of FASB Statement No. 107*, and to decide whether to proceed drafting a final FSP. The objectives of this meeting were met.

Matters Discussed and Decisions Reached:

Constituent Comments

1. Mr. Trench noted that as of January 22, 2009, 67 comment letters were received from constituents on the proposed FSP and that a comment letter summary is posted on the project activities page of the FASB website.

2. Mr. Trench provided an overview of the issues raised in comment letters received. He stated that the majority of respondents did not favor the proposed FSP as

written. Generally, respondents commented that the proposed FSP was not operational by the proposed effective date and represented a piecemeal approach to recognition and measurement of financial instruments. Respondents recommended that the Board focus on the comprehensive financial instruments joint project with the IASB. Some respondents also commented that the proposed FSP introduced a new measurement model and that there was limited due process for this project because of the shortened comment period.

3. Mr. Trench also provided some detailed comments received on the proposed FSP. Some respondents suggested that the scope of the proposed FSP be narrower and only applicable to financial assets that are other-than-temporarily impaired. Some respondents stated that aggregating various measurement attributes in one table does not necessarily increase comparability of the various measurement models in U.S. generally accepted accounting principles. Many respondents requested additional clarification on the description of the incurred loss amount and how it is calculated. Respondents also expressed concerns about the proposed pro-forma income disclosures stating that they could be misleading to users of financial statements.

4. Mr. Trench noted that the comments received by the FASB were consistent with those received by the IASB on their Exposure Draft, *Investments in Debt Instruments: Proposed amendments to IFRS 7*. The IASB decided not to continue with its project on additional disclosures for investments in debt instruments.

5. Ms. C. Smith provided the Board with insights gained from discussions with users regarding the proposed disclosures. She stated that the staff reached out to the users that commented on the proposed FSP. Users stated that fair value disclosures of loans are the most important incremental information in the proposed disclosure in tabular format. However, they would prefer to have a single table in the notes to the financial statements showing all financial instruments at fair value. They believe that aggregating fair value information of all financial instruments in one place would enable preparers to better explain the different assumptions used in

developing valuation estimates and allow analysts to have a more comprehensive picture of changes in values. Some users considered the proposed incurred loss information to be interesting from the perspective of information on minimum losses, but other users believe that such information can be confusing and misleading because the incurred loss amount is calculated differently for different financial instrument types. In addition, the users believed that too much emphasis might be placed on the pro forma income disclosures calculated on an incurred loss basis. Some users suggested that an expected loss measurement, which accounts for management's expectation of all future losses, might be more relevant. The users that supported pro forma income disclosures suggested that the Board require pro forma net income based on fair value. These users stated that while the balance sheet disclosures about fair value could be used to approximate the effect on an entity's earnings, pro forma net income disclosures would include necessary adjustments and provide a more accurate number. Users encouraged progress on the comprehensive financial instruments project, but stressed the need for more fair value information in the short term.

Board Comments

6. Ms. Seidman noted that the users' comments are focused on their preference for more fair value information on an interim basis. Ms. Seidman pointed out two issues for the Board's consideration:

   a. Due to the abbreviated comment period for the proposed FSP, respondents (preparers) focused on their major concerns including the effective date and the calculation of the incurred loss amount, but they did not comment on providing more frequent (quarterly) fair value information for loans and other securities.

   b. One comment letter (CL#38, Crowe Horwath) points out that the example in paragraph 31 in FASB Statement No. 107, *Disclosures about Fair Value Financial Instruments,* indicates two different approaches to fair value measurement (related to disclosures) for loans; one that is consistent with the exit price notion in FASB Statement No. 157, *Fair Value Measurements,* and one that is based on the present value of cash flows discounted at a rate an entity would currently lend at (which would not include a liquidity premium).

7. Ms. Seidman stated that the inconsistency between the standards may cause entities to value their loan portfolios differently for the disclosure requirements under Statement 107 than what was intended by Statement 157, and those valuations may not include certain factors such as current liquidity premiums. Ms. Seidman noted that the Board made other amendments of the examples in Statement 107, but left the example on loans (and long-term debt) intact. She further stated that this inconsistency must be addressed before requiring more frequent fair value disclosures for loans.

8. Ms. Seidman stated that the proposed FSP, as written, should not be finalized. She further stated that the issues identified with this project and other financial instrument issues can be further discussed at the Valuation Resource Group meeting on February 5, 2009, and as part of the loan disclosures project so that the Board can provide a more coordinated response. .

9. Mr. Golden added that the staff also is conducting research on a potential project to improve disclosure requirements within Statement 157. The IASB exposed a document about such disclosures and the staff plans to discuss this potential project with the Valuation Resource Group.

10. Mr. Herz thanked all constituents that commented on the proposed FSP during the short comment period. Mr. Herz stated that he was surprised that preparers and auditors who commented on the proposed FSP stated that they were confused by the incurred loss calculations in the proposed FSP and also cited many operational issues. He observed that this contradicted assertions made by preparers and auditors at the November 25, 2008, roundtable (about financial issues highlighted by the global financial crisis) that impairments for debt securities should be recognized in the income statement for the 2008 calendar year-end based on incurred loss amounts.

11. Mr. Smith also stated his concern about the inconsistency between Statement 157 and the illustration in paragraph 31 of Statement 107, and that the inconsistency should be addressed. Ms. Seidman pointed out that at the time Statement 157 was

being deliberated, the inconsistency would not have been perceived (because the present value of cash flows discounted at the rate an entity would lend at could have been viewed as a proxy for fair value under normal market conditions) but that now, under current market conditions, there is the potential for a significant difference. Ms. Seidman also pointed out a similar inconsistency related to long-term debt in paragraph 31 of Statement 107, and that the Board had recently issued proposed FSP FAS 157-c, *Measuring Liabilities under FASB Statement No. 157* , which would permit an entry price approach. Mr. Golden noted that if the Board were to address this issue, it would require exposure for public comment.

12. Mr. Smith noted that due to the timing of the comment period for the proposed FSP, it did not receive the greatest due process. He concurred with Mr. Herz's and Ms. Seidman's views regarding the comment letters received.

13. Mr. Siegel also echoed Mr. Herz's comments on the shift in views regarding the operationality of the proposed disclosures. Mr. Siegel highlighted that the objective of the proposed disclosures was to provide additional information to facilitate conversations between preparers and users of financial statements. He believes that the proposed disclosures would provide the tangible data needed for preparers and users to discuss the inputs and assumptions used to form estimates. He pointed out that one company included similar disclosures in its earnings release, which led to a more meaningful discussion between management and analysts.

14. Mr. Linsmeier agreed with Mr. Siegel's observations.

Direction of the Project

15. Mr. Trench requested that the Board provide its views on how the staff should proceed with the project. He suggested that the project could be combined with the comprehensive joint project on financial instruments or that the Board could continue with a short-term project on disclosures (but not necessarily the proposed disclosures).

16. Mr. Smith suggested that there needs to be more discussion about how to improve disclosures, which would lead to a new Exposure Draft. He specifically pointed out that the illustration in paragraph 31 of Statement 107 should be reviewed to align with existing guidance. He pointed out that this project could be included in the loan loss disclosures project or the comprehensive joint financial instruments project. He stated that any new disclosure requirements should not be effective for 2008 calendar year financial statements due to operational issues.

17. Mr. Seigel stated that he does not support including discussions about disclosures in another project. However, he is supportive of obtaining the Valuation Resource Group's views regarding fair value of loans.

18. Mr. Linsmeier pointed out that in the current market environment there is considerable uncertainty about the value of financial assets and those values fluctuate significantly. He stated that the Board should proceed with the proposed FSP, amended to require only quarterly fair value information. Mr. Linsmeier believes that providing timely quarterly information about asset values, even with the inconsistency in loan valuation, would help markets and would facilitate discussions between prepares and users of financial statements. He highlighted that valuation methods and assumptions are required to be disclosed in the financial statements and is hopeful that preparers would choose to value loans based on the exit price notion in Statement 157 (or at least provide sufficient information to users to understand how the loans are being valued to facilitate a discussion with analysts). Mr. Linsmeier stated that if this project is combined with another project,

the disclosures may not be effective until 2009 calendar year end. He emphasized the importance of providing fair value information in a timely manner due to current market conditions.

19. Mr. Herz stated that the Board should address users' request for timely fair value information. He further stated that the staff should draft a new Exposure Draft requiring quarterly fair value disclosures for all financial instruments within the scope of Statement 107, effective the first quarter 2009. In addition, he noted that the inconsistency between Statement 157 and Statement 107 regarding the fair value of loans should be addressed in a separate project (and that any new proposed disclosures of fair value on a quarterly basis should be consistent with the methodology used under the current disclosure requirements under Statement 107). Mr. Herz believes loans should be discussed in more detail because a measurement attribute other than fair value may be more suitable for loans. Additionally, Mr. Herz proposed that pro forma income disclosures be required as well as an explanation of the differences between the carrying values and fair values disclosed.

20. Ms. Seidman observed that the Board should wait until after the Valuation Resource Group meeting to make a decision about this project. She stated that the Board should combine projects to minimize revisions and duplication. She noted that many constituents are uncertain about how to estimate fair value in the current market, especially Level 3 financial instruments. She questioned whether the practicability exception in Statement 107 (which is based on excessive cost) would be invoked if entities are required to provide more frequent fair value disclosures for illiquid assets.

21. Mr. Siegel and Mr. Linsmeier supported requiring quarterly fair value information for financial instruments consistent with year-end measurement methodologies if entities include a description of the methods and assumptions used. Mr. Linsmeier stated that he believes that the measurement method for loans should be disclosed regardless of the measurement used (which is already required under Statement 107). He also stated that the reporting under the disclosure requirements should be

consistent with the previous reporting so there is no opportunity for an entity, which was previously disclosing fair value for loans, to now disclose an entry value.

22. Mr. Smith stated that smaller entities may not have the resources to implement all FASB guidance recently issued in addition to the proposed quarterly fair value disclosures. He further stated that the new disclosures should be effective in the second quarter of 2009. He noted that the comment letters received did not focus on the operationality of more frequent fair value disclosures.

23. Mr. Golden recommended that the Board re-expose the proposed FSP because the scope has significantly increased from certain financial assets in the original proposed FSP to all financial instruments within the scope of Statement 107 for the new proposed FSP.

24. Ms. Seidman noted that many respondents were concerned with the pro forma income disclosures and suggested that they should not be required for the Board to issue guidance in a timely manner. Ms. Seidman also was concerned that it may be very time consuming for certain entities (such as private equities) to estimate fair values of their financial instruments on a quarterly basis. She suggested that the Notice for Recipients of the new proposed FSP should include a question requesting comments on the use of the practicability exception in Statement 107.

25. Mr. Herz stated that he would like to limit this guidance to institutions with large financial instrument portfolios, but was unsure how to draft the scope of the new proposed FSP to include only such entities.

26. Mr. Glotzer stated that private companies issue interim financial statements and they may have operational concerns with the new proposed FSP.

Board Vote

27. The Board directed the staff to draft a new document for exposure that amends Statement 107 to require interim as well as annual disclosures about fair value of all financial instruments within the scope of Statement 107. The Notice for Recipients included with the Exposure Draft should request respondents to comment on the following:

    a. Should scope exceptions be made for certain entities and financial instruments?

    b. Can entities comply with the proposed disclosure requirements by the proposed effective date and on an ongoing basis?

28. The Board decided that the Exposure Draft should reiterate the qualitative disclosure requirements within Statements 107 and 157.

29. The Board decided that the proposed guidance should be effective for interim and annual periods ending after March 15, 2009.

30. The Board decided that the comment period should be 30 days.

<u>Follow Up Items:</u>

None.

<u>General Announcements:</u>

None.