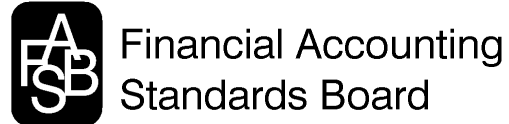


MINUTES



To: Board Members

From: Prince (ext. 229)

Subject: Minutes of the February 20, 2008 Board Meeting: Objective and Qualitative Characteristics Phase **Date:** February 29, 2008

cc: Leisenring, Bielstein, Golden, MacDonald, Lott, J. Johnson, Bossio, T. Johnson, Bement, Chesney, Posta, Gabriele, Chookaszian, Allen, Kilmek, Sutay, FASB Intranet, Lian, Crook, Hague, Villmann, Rees, Willis, Hickey, Teixeira, Wilson

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: Objective and Qualitative Characteristics Phase

Basis for Discussion: Board Handout

Length of Discussion: 3:00 p.m. to 4:15 p.m.

Attendance:

Board members present:	FASB: Herz, Batavick, Crooch, Linsmeier, Smith, and Young
Board members absent:	Seidman
Staff in charge of topic:	Bossio and Lian (IASB)
Other staff at Board table:	T. Johnson, Chesney, and Prince
Other staff by phone:	Crook

Summary of Decisions Reached:

The Board discussed three issues that arose during the review of drafts of the forthcoming Exposure Draft on the objectives of financial reporting and qualitative characteristics of financial information and Preliminary Views on the reporting entity. Those issues were as follows:

1. How to address constituents' concerns about the potential implications of selecting the entity perspective in developing the objective of financial reporting for the forthcoming Exposure Draft and for the related Preliminary Views. The Board affirmed its decision that general purpose financial reporting is directed at the reporting by an entity to its capital providers rather than reporting from the perspective of a particular class of capital providers. The Board directed the staff to prepare an analysis of the implications of selecting the entity perspective for consideration in drafting of those documents. The Board expressed its willingness to engage in additional outreach but also expressed that the staff analysis be timely so as not to cause undue delay in the release of the forthcoming Exposure Draft and Preliminary Views.
2. Whether to use the term *accuracy* or *free from error* to describe a component of faithful representation. The Board expressed a preference for the term *accuracy*. This is because the term *free from error* also could be deemed absolute. However, the Board also directed the staff to consider drafting the discussion of the qualitative characteristic of faithful representation without using either term or the need for any specific components of faithful representation.
3. How to strengthen the discussion of comparability in the conceptual framework. The Board provided suggestions for improving the discussion of comparability in the forthcoming Exposure Draft.

Objective of Meeting:

The objective of the meeting was for the Board to discuss three issues that arose during the review of the pre-ballot draft of the forthcoming Exposure Draft on the objectives of financial reporting and qualitative characteristics of financial information and to provide feedback on plans for addressing those issues. The objective was met.

Matters Discussed and Decisions Reached:

Issue 1: The Potential Implications of Adopting the Entity Perspective

1. Mr. Bossio stated that the staff seeks Board feedback on how to address constituents' concerns about the potential implications of having selected the entity perspective in developing the objective of financial reporting. Mr. Bossio noted that constituents may perceive implications not specifically identified by the staff, and that constituents feel they have not been given ample opportunity to debate the merits of the so-called proprietary perspective. Mr. Bossio also noted that the IASB addressed the same issue at its Board Meeting on February 19, 2008, and that no firm conclusion was reached. The IASB did, however, direct the staff to proceed with a draft of a separate document that will articulate the potential implications of having chosen the entity perspective.

Issue 1 Board Comments

2. Mr. Batavick asked the staff what the current timeline is for releasing the Phase A Exposure Draft and the Phase D Preliminary Views document. Mr. Bossio noted that the next step for the ED is proceeding to a ballot draft version. Mr. Bossio also noted, however, that before doing so, the IASB Board has asked the staff to proceed with the drafting of a separate document that might be issued as an Invitation to Comment to invite comments on potential implications of both the ED and PV. Mr. Bossio noted that Mr. J. Johnson had indicated the initial draft of that document was a week away before being submitted for staff review by Mr. Bossio and Mr. T. Johnson. Ms. Crook stated that the PV still has one outstanding issue and, pending the resolution of that issue, the PV will then proceed directly to ballot draft. Mr. Batavick expressed concern that he does not want to delay the issuance of the two documents with the drafting of a new, separate document. Mr. Bossio commented that the document containing the potential implications of the perspective decision would most likely be ready for the joint meeting in April.

3. Mr. Herz stated that he does not think that adopting the entity perspective has implications for the earlier phases of the project, but it may have implications for the reporting entity phase. Mr. Herz expressed concern that this issue might cause further

delay for the project. Mr. Herz asked the staff whether it has a good understanding of the constituents' concerns. Mr. Linsmeier stated that constituents' primary concerns revolve around two issues: first, whether the perspective decision has implications for the *parent company approach* and, second, whether the perspective decision has implications for the definitions of liability and equity. He added that he doesn't think it has implications for the definitions.

4. Mr. Linsmeier stated that having the staff prepare a separate document may be a useful exercise, as he has noticed that even among Board members, there is a misunderstanding of the implications of adopting the entity perspective. The drafting of the separate document would help Board members to have a common understanding of the issue even if the Boards decide that publishing a separate third document is unnecessary. Mr. Bossio added that he could not be sure about the extent of the implications the constituents may perceive from the entity perspective decision. He added, however, that the IASB discussed both of the concerns noted by Mr. Linsmeier.

5. Mr. Crooch questioned whether the real issue revolved around producing parent-only versus consolidated financial statements. Ms. Crook stated that she believes the concern of constituents is not only about parent-only financial statements but also the parent-company approach of consolidated financial statements. She noted that constituents may want to discuss the ramifications of the economic entity perspective and how it differs from the parent-company approach. She also noted that she believes constituents want to have the decision to adopt the entity perspective explicitly mentioned in the conceptual framework

6. Mr. Young asked Ms. Crook whether she viewed the parent company approach as part of the proprietary perspective or as a third, separate perspective. Ms. Crook responded that she sees it as a mixture of both the entity perspective and the proprietary perspective. Mr. Bossio stated that the use of different labels for similar ideas may have led to some of the confusion. Mr. Linsmeier stated that, regardless of whether the term entity perspective was removed from the Exposure Draft, constituents would still raise concerns. He also stated he was concerned that the Board has not made known to constituents what it intends by its decision to adopt the entity perspective.

7. Mr. Herz asked the staff what the timeline for the document discussing the potential implications of the perspective decision would be. Mr. Bossio noted that after reviewing the initial draft next week and discussing with Mr. J. Johnson upon his return from London, the staff would be in a position to provide the Board with the projected timeline. Mr. Herz stated that he doesn't want the document to slow down the issuance of the Exposure Draft. Mr. Linsmeier also stated he did not want the development of the document to delay the issuance of the Exposure Draft or the Preliminary Views document. Board members indicated that they did not want to commit to publishing a document discussing what the implications might be of adopting the entity perspective. Mr. Herz asked the staff to develop a timeline for the release of the Exposure Draft and the Preliminary Views document.

Issue 2: Accuracy vs. Free from Error

8. Ms. Lian stated that some Board members and one external reviewer were concerned with using the term *accuracy* to describe a component of faithful representation. Accuracy not only presents translation issues but also can be interpreted as precision. However, the staff is concerned that using the term *free from error* would imply a degree of absoluteness not intended by the underlying concept. Ms. Lian noted that the IASB considered this debate at their meeting held on February 19, 2008 and expressed their preference for the term *free from material error* because it does not indicate absolute precision and because the term is not new to IASB literature. Mr. T. Johnson noted that the IASB would prefer avoiding introducing a new term, which may create misunderstanding for their constituents. Ms. Lian then asked the Board which term the Board would prefer.

Issue 2 Board Comments

9. Mr. Linsmeier noted that by using the term *free from material error*, some constituents may infer that it is OK to ignore an immaterial error, which is not the Board's intent. Mr. Linsmeier also noted that he was uncomfortable with using the term *error* to capture the underlying notion of uncertainty. He stated that *error* means a mistake has been made, not that uncertainty exists. He also stated he does not endorse either *error* or the insertion of *material* into the term *free from error*.

10. Mr. T. Johnson noted that the IASB *Framework* contains the term *free from material error* when describing the concept of reliability, and that the term is used elsewhere in the IASB literature. As a result, IASB constituents understand what *free from material error* means. He further noted that in the IASB *Framework*, *free from material error* is not a subheading. Mr. Linsmeier stated that he had noticed that, within the Exposure Draft, *relevance* does not contain separate subheadings for each of its components whereas *faithful representation* does.

11. Mr. Bossio stated that the debate regarding which term to use is simply a debate over labels as opposed to the definitions that the labels represent. Mr. T. Johnson noted that the Preliminary Views document did not contain subheadings for the components of faithful representation; rather, the document stated the interplay of the components in one paragraph. Mr. Linsmeier suggested that the staff change the Exposure Draft's discussion of faithful representation back to how it was originally discussed in the Preliminary Views document. Mr. Herz expressed support for Mr. Linsmeier's suggestion. Mr. T. Johnson also stated that it is much easier to describe faithful representation rather than trying to place labels on the components of faithful representation.

12. Mr. Smith stated he has no preference for which term is used. Mr. Batavick stated he would accept the term *free from material error* to facilitate the forward progress of the project; however, his first preference would be to rewrite the discussion of faithful representation, as suggested by Mr. Linsmeier, so that it aligns with the Exposure Draft's discussion of relevance that does not rely on subheadings or emphasize components. Mr. Crooch stated that he could not determine which term he preferred although he hesitated using a term with a reference to materiality.

13. Mr. Young stated he does not agree that *accuracy* is the same as *free from material error*. Mr. Young stated he prefers to stay with *accuracy* or to expand the term *free from material error*. Mr. Herz expressed that he did not favor *free from material error*. He also expressed that the arguments raised by Mr. Linsmeier are important. Mr. Herz stated that he would be in favor of rewriting the part of the Exposure Draft discussing faithful representation. Mr. Crooch noted that by using *free from material error*, constituents

would be measuring how far off they could faithfully represent something rather than trying to most accurately depict an economic phenomenon.

14. Mr. Batavick asked the staff whether it would be possible to redraft the description of faithful representation and present it to all 21 members of the Board prior to the next Board meeting. Mr. Herz expressed support for Mr. Batavick's idea.

Issue 3: Comparability as an Enhancing Qualitative Characteristic

15. Ms. Lian stated that some Board members have raised concerns about the discussion of comparability in the Exposure Draft. Specifically, these Board members are concerned that comparability, as an enhancing qualitative characteristic, will be viewed as an optional, rather than a necessary, qualitative characteristic. Ms. Lian noted that the staff will attempt to address these concerns through redrafting efforts.

Issue 3 Board Comments

16. Mr. Herz stated that there is something troublesome with the use of the label *enhancing*. He is concerned that *enhancing* may be interpreted as desirable but not necessary. Mr. Young questioned whether removing the label of *enhancing* was a possibility. Mr. Bossio mentioned that the use of *enhancing*, to a degree, stems from the notion of fundamental characteristics as used in Concepts Statement No. 2, which notes that both *relevance* and *reliability* (as used at that time) are essential characteristics. (That is, as noted in paragraph 42 of CON 2 "it may be possible to trade relevance for reliability or vice versa, though not to the point of dispensing with one of them altogether.") Mr. Smith expressed that he was not in favor of having one qualitative characteristic carry greater weight than another qualitative characteristic.

17. Mr. T. Johnson noted that the Preliminary Views document stated that all of the qualitative characteristics are complementary concepts in achieving decision usefulness. Their application, in concert, should maximize the decision usefulness of financial reporting. Some Board members expressed that they favored the language in the Preliminary Views document.

18. Mr. Linsmeier expressed that there may be some difference between enhancing qualitative characteristics. Verifiability, timeliness, and understandability may not be achievable and, therefore, could be considered enhancing. He questioned where comparability would fit in and expressed his opinion that he thinks it fits better with the fundamental qualitative characteristics. He stated that comparability is most likely characterized as an enhancing characteristic because it may not be achieved when standard-setting bodies change accounting standards, thus leading to incomparable information for a period of time.

19. Mr. Young questioned why there has to be an order when considering the qualitative characteristics. Mr. T. Johnson stated that it is a matter of efficiency in assisting the Board in making decisions. Mr. Young expressed his preference for the language in the Preliminary Views document. Mr. Bossio stated that he thought the goal is to strive to maximize all of the qualitative characteristics. Mr. Herz noted that there are unavoidable trade-offs, for example, between understandability and faithful representation. He further noted that all the qualitative characteristics cannot be maximized all the time. Mr. Batavick noted that it would be helpful to have language in the Exposure Draft discussing the goal of maximizing the qualitative characteristics.

20. Ms. Lian also stated that one Board member wanted to ensure that standard setters do not permit multiple accounting methods for similar economic phenomena. Mr. T. Johnson mentioned that the Board member wanted to avoid allowing for *implicit* options that users of financial reports might not be aware of, in contrast to *explicit* options (for example, FIFO or LIFO) that they would be aware of.

21. Mr. Young asked the staff whether activity-based accounting would be supported by the conceptual framework. Mr. Linsmeier stated that it could be argued that different activities represent different economic phenomena. Mr. Smith stated that the real concern may be trying to avoid *explicit* options rather than *implicit* options. Mr. T. Johnson stated that the concern is that users cannot discern *implicit* options whereas *explicit* options are identifiable. Mr. Bossio stated that there is concern that some standards are written so ambiguously that the standards are interpreted in different ways

and that users of financial reports are not aware of the different interpretations being used. Mr. Herz stated that both *implicit* and *explicit* options are important to consider.

Follow-Up Items:

The staff will set a timeline for the release of the Exposure Draft and the Preliminary Views document. The staff will circulate to all Board members a redrafted portion of the Exposure Draft that discusses faithful representation without the use of components.

General Announcements:

None.