MINUTES

Financial Accounting Standards Board

To: Board Members

From: Fair Value Option Team
(Cowan ext. 233)

Subject: Minutes of the October 18, 2006 Board Meeting: Fair Value Option

Date: October 27, 2006

cc: Bielstein, Smith, MacDonald, Leisenring, Fair Value Option Team, Fair Value Measurements Team, Gabriele, Polley, Swift, 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: Fair Value Option Phase 1 Redeliberations

Basis for Discussion: Board Memorandums No. 23, dated September 27, 2006; Nos. 24 and 25, dated October 3, 2006; No. 26, dated October 12, 2006

Length of Discussion: 11:15 a.m. to 12:15 p.m. and 1:00 p.m. to 2:15 p.m.

Attendance:

Board members present: Batavick, Crooch (via telephone), Herz, Linsmeier, Seidman, Trott, and Young

Board member absent: None

Staff in charge of topic: Wilkins

Other staff at Board table: L. Smith, Lott, Barker, MacDonald, Mechanick, Stoklosa, and Cowan

Outside participants: None

Summary of Decisions Reached:

The Board redeliberated certain issues related to the following:

1. Election of the Fair Value Option (FVO)
2. Recognition, Measurement, and Presentation
3. Proposed New Disclosures
4. Transition and Effective Date
5. Scope of the Statement

The Board decided:

Election of the FVO

1. To indicate in the FVO Statement that if financial assets that have been reported at fair value (with changes included in earnings) because of the nature of the subsidiary that has been holding those assets are transferred to another entity within the consolidated reporting entity for which such fair value accounting is not required, the FVO may be elected on the date of the transfer.

2. To have the staff perform further work on the contract-by-contract election and to provide the Board with examples of its application to certain financial instruments, including insurance.

Recognition, Measurement, and Presentation

3. To refer to existing guidance on operating measures/performance indicators in FASB Statement No. 117, *Financial Statements of Not-for-Profit Organizations,* AICPA Statement of Position 02-2, *Accounting for Derivative Instruments and Hedging Activities by Not-for-Profit Health Care Organizations, and Clarification of the Performance Indicator,* and the AICPA Audit and Accounting Guide, *Health Care Organizations*, rather than imposing a one-size-fits-all requirement. Consequently, not-for-profit health care providers would include the changes in fair value within the performance indicator, whereas other not-for-profit organizations would include such changes either within or outside their operating measure/performance indicator, consistent with how they define that measure.

4. To modify the disclosure requirements in paragraphs 12(b) and 12(c) of the proposed Statement to ensure sufficient transparency of the impact of the FVO on the reporting by not-for-profit organizations of changes in net assets, operating measures/performance indicators (if presented), and the line item components therein.

5. To expand the disclosure requirements in paragraphs 12(b) and 12(c) of the proposed Statement with regard to not-for-profit organizations to encompass the impact of the FVO not only on an operating measure/performance indicator but also on the overall changes in the three classes of net assets (unrestricted, temporarily restricted, and permanently restricted).

6. To require the costs and fees related to financial assets or financial liabilities for which the FVO is elected upon initial recognition to be recognized in earnings as incurred and not deferred. Similarly, the FVO Statement will indicate that the unamortized deferred costs, fees, premiums, and discounts related to existing financial assets and financial liabilities for which the FVO has been elected at the initial application of the FVO Statement should be written off as part of the cumulative-effect adjustment to the opening balance of retained earnings.

Proposed New Disclosures

7. To require an entity to (a) disclose management's basis for its decision to elect the FVO for a contract or group of similar contracts and (b) if the fair value election is not chosen for all contracts within a group of similar contracts, disclose the reasons for only partial election as of each date for which a statement of financial position is presented. The disclosure of the reasons for electing the FVO for only certain contracts within a group of similar contracts should provide sufficient information for users to understand how those groups of similar contracts reconcile to the line items presented in the statement of financial position.

8. To require an entity to disclose the difference between an asset's fair value carrying amount and the aggregate principal amount to be received for those assets for which the FVO has been elected as of each date for which a statement of financial position is presented.

9. For loans and receivables for which the FVO has been elected, not to require disclosure of the maximum amount of credit risk of the loan or receivable at the reporting date, but to require separate

disclosure of (a) the creditor's estimate of the fair value changes attributable to changes in expected cash flows relative to borrower-specific credit risk and (b) all other changes in fair value that are included in current-period earnings for each period for which an income statement is presented. The Board also decided not to provide detailed computational guidance on how to determine the approximation of the amount of the loan's or receivable's fair value change attributable to changes in borrower-specific credit risk.

10. If an entity classifies a loan as held for investment and elects the FVO for that loan, to require the entity to disclose the fair value carrying amount of loans ninety days or more past due. In addition, if an entity's policy for such loans is to continue to recognize interest income on an amortized cost basis separately from other changes in fair value, the entity will be required to disclose the aggregate fair value carrying amount of loans that are in nonaccrual status. Those disclosure requirements are required as of each date for which a statement of financial position is presented.

11. Not to require any special disclosures in the year of initial application of the FVO Statement if an existing financial asset or financial liability for which the FVO has been elected at the beginning of that fiscal year is sold or settled (extinguished) later in that year prior to its maturity.

12. Not to require that all fair value disclosures for assets and liabilities reported at fair value pursuant to the FVO be provided in a single note to the financial statements.

13. To require entities to disclose, as of each date for which a statement of financial position is presented, the following for investments that would otherwise be accounted for under the equity method (because of having significant influence over the operating and financial policies of the investee) but that are reported at fair value pursuant to the FVO:

    a. The name of each investee and the percentage of ownership of common stock, as well as the accounting policies of the investor with respect to investments in common stock. (The disclosure should include the names of any significant investee corporations in which the investor holds 20 percent or more of the voting stock but the investor is not deemed to have significant influence over the operating and financial policies of the investee, together with the reasons why the investor is not deemed to have significant influence. The disclosure should also include the names of any significant investee corporations in which the investor holds less than 20 percent of the voting stock and the investor is deemed to have significant influence over the operating and financial policies of the investee, together with the reasons why the investor is deemed to have significant influence.)

b. Summarized information about the assets, liabilities, and results of operations of the investees to be presented in the notes or in separate statements, either individually or in groups, as appropriate when investments in common stock of corporate joint ventures or other equity method investments are, in the aggregate, material in relation to the financial position or results of operations of an investor.

14. To require quantitative and qualitative disclosures of the effect on earnings of initially measuring at fair value under the FVO election if an entity elects the FVO either upon the occurrence of a new-basis event or at the time the entity obtains significant influence for an investment that would otherwise be accounted for under the equity method. Those disclosures should indicate where in the income statement the effect on earnings is reflected.

15. To require that the disclosure requirements in the FVO Statement also apply to investments in securities that are classified in the trading category under FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* and the hybrid financial instruments that are reported at fair value through earnings under the fair value election permitted by FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments,* and its amendment of paragraph 16 of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities.*

16. To require that the fair value disclosures in the notes be presented together with those related individual carrying amounts for those line items, if the carrying amounts of individual line items reported in the statement of financial position are a combination of fair value and non-fair-value amounts.

Transition and Effective Date

17. To require that the effective date of the FVO Statement be the same as the effective date of Statement 157; thus, the FVO

Statement should be effective for financial statements issued for fiscal years beginning after November 15, 2007.

18. To permit an entity to early adopt the FVO Statement provided that the entity also adopts all of the requirements (measurement and disclosure) of Statement 157 concurrent with or prior to the early adoption of the FVO Statement.

19. To permit early adoption of the FVO Statement within 120 days of the beginning of the reporting entity's fiscal year, thereby making the FVO election retroactive to the beginning of that fiscal year (or the date of initial recognition, if later).

20. Not to modify the requirements that the effect of initial adoption be accounted for as a cumulative-effect adjustment through retained earnings or the prohibition against retrospective application.

21. To require a one-time reconciliation that presents the current historical/amortized cost amount with the corresponding fair value measures as of the date of adoption for those items reported pursuant to the FVO. That reconciliation should be presented by category of assets and liabilities as presented in the statement of financial position.

Scope of the Statement

22. To permit the FVO election for a host financial instrument that is being accounted for separately due to the bifurcation of an embedded derivative nonfinancial instrument from a hybrid nonfinancial instrument pursuant to paragraph 12 of Statement 133, provided that the scope exceptions in the FVO Statement are not applicable to the host financial instrument.

23. To add a scope exception to the FVO Statement for (a) contracts issued or held by the reporting entity that are both (1) indexed to its own stock and (2) classified in stockholders' equity in its statement of financial position and (b) contracts issued or held by the reporting entity that contain embedded derivatives that both (1) are indexed to its own stock and (2) would, on a standalone basis, be classified in stockholders' equity in its statement of financial position.

24. To amend Statement 115 to exclude from its scope all investments that, absent a FVO election under the FVO Statement, would be required to be accounted for under the equity method of accounting under APB Opinion No. 18, *The Equity Method of*

Accounting for Investments in Common Stock (rather than excluding "investments in equity securities accounted for under the equity method").

Objectives of Meeting:

The objective of the meeting was for the Board to redeliberate certain issues related to Phase 1 of the FVO project. The objective of the meeting was met.

Matters Discussed and Decisions Reached:

ELECTION OF THE FVO

Election of the FVO for Items Previously Reported at Fair Value under Investment Company Accounting

1. Mr. Wilkins noted that proposed AICPA Statement of Position (SOP), *Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies,* provides guidance for when a company is prohibited from applying investment company accounting and also for when a company must apply investment company accounting (and, therefore, must use fair value). Because the SOP, when finalized, will change the current practice regarding which entities can be accounted for as investment companies, certain financial and nonfinancial assets will need to be transferred out of investment company subsidiaries into other entities within the consolidated reporting entity prior to the effective date of that SOP. The issue is whether the FVO may be elected for the transferred financial assets at the date of their transfer.

2. Mr. Wilkins stated that the staff recommends that the FVO Statement indicate that if financial assets that have been reported at fair value (with changes included in earnings) because of the nature of the subsidiary that has been holding those assets are transferred to

another entity within the consolidated reporting entity for which such fair value accounting is not required, the FVO may be elected on the date of the transfer. The recommendation is not limited to the financial assets of investment companies.

3. Mr. Young expressed concern that allowing a FVO election in this situation could lead to abuse when the entities transferred would otherwise be consolidated. Mr. Smith clarified that the financial assets transferred would still need to meet the scope requirements of the FVO Statement before the FVO could be elected. He stated that investments in entities that would otherwise be consolidated are not within the scope of the FVO and would therefore not be eligible for the FVO election at the time they were transferred.

4. The Board agreed unanimously with the staff's recommendation.

Required Contract-by-Contract Election

5. Mr. Wilkins explained that, based on the discussion at the Board meeting on September 6, 2006, the staff recommends that the FVO Statement merely indicate that the determination of fair value must be consistent with the guidance in FASB Statement No. 157, *Fair Value Measurements*, and that the focus of the contract-by-contract election is on the individual agreement that the reporting entity has entered into and the minimum denomination that is explicitly transferable in its current form.

6. Mr. Linsmeier stated that at the Education session, the Board and staff discussed specific language to use regarding the minimum level at which the FVO should be elected as it relates to applying the contract-by-contract requirement of the FVO Statement. He explained that it may be preferable to eliminate the words "explicitly transferable"

since some items may be eligible for the FVO election, but may not be transferable, thus causing confusion. Additionally, Mr. Linsmeier expressed concern that even if the term “explicitly transferable” was removed, the contract-by-contract requirement still may not be applied consistently and may result in conclusions that are inconsistent with the Board’s intentions. That is, the contract-by-contract requirement may be applied to certain items in a way that would result in the FVO election for something other than a contract, as envisioned by the Board.

7. Mr. Linsmeier stated that he was concerned that the current articulation of the contract-by-contract election would result in constituents requesting that the Board define a contract for several different financial instruments, as practice problems arise in applying the FVO Statement. That is, preparers may find the definition of contract-by-contract election to be inoperable.

8. Mr. Linsmeier explained that he believes the issue could not be resolved by stating that the contract-by-contract election should be consistent with Statement 115, since the FVO scope applied to a much broader set of financial instruments. Furthermore, Mr. Linsmeier stated that Statement 115 deals with securities that would likely be the simplest financial instruments to which the contract-by-contract election could be applied, providing little help on more complex financial instruments that are within the scope of the FVO Statement.

9. Mr. Trott stated that he agreed with Mr. Linsmeier, but that he preferred that the staff proceed to drafting the final standard while working out the wording and examples of application of the contract-by-contract election for later approval by the Board. He stated that the

staff's examples should address credit card receivables, loans, and other areas for which potential issues had been identified. Mr. Trott stated that he was concerned that if the staff did not do further work on the contract-by-contract election, the Board's intent would not be clearly communicated and applied.

10. Ms. Seidman noted that the staff's approach was consistent with the approach used in distinguishing between attached derivatives and embedded derivatives under Statement 133. She also agreed that the staff should provide examples of the application of the contract-by-contract election, especially for loans and insurance.

11. Mr. Herz asked the staff to do further work on articulating the contract-by-contract election, as well as developing application examples, as requested by other Board members.

12. Mr. Smith stated that the staff would provide the Board with application examples of the contract-by-contract election for certain financial instruments and come back to the Board for a final decision on the contract-by-contract election. He explained further that the staff would begin drafting the final FVO Statement and update that draft with the Board's future decision on the contract-by-contract election.

SELECTED RECOGNITION, MEASUREMENT, AND PRESENTATION ISSUES

Requiring Not-for-Profit Organizations to Include the Changes in Fair Value in the Performance Measure

13. Mr. Mechanick stated that the staff recommends that, as it did in FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, the Board refer to existing guidance on operating measures/performance indicators in FASB

Statement No. 117, *Financial Statements of Not-for-Profit Organizations,* AICPA Statement of Position 02-2, *Accounting for Derivative Instruments and Hedging Activities by Not-for-Profit Health Care Organizations, and Clarification of the Performance Indicator*, and the AICPA Audit and Accounting Guide, *Health Care Organizations*, (the Health Care Guide), rather than imposing a one-size-fits-all requirement. Not-for-profit health care providers would include the changes in fair value within the performance indicator. Other not-for-profit organizations would include such changes either within or outside their operating measure/performance indicator, consistent with how they define such that measure. Mr. Mechanick indicated that the recommended approach would not only acknowledge the diversity of not-for-profit operating measures, but it would also help promote—or at least not deter—the use of the FVO for some key not-for-profit financial assets and liabilities, such as multi-year contributions receivable and liabilities under split-interest agreements without embedded derivatives, because it would not thrust unwarranted operating measure volatility on such organizations in return.

14. Mr. Mechanick stated that even with the staff's recommendation, many not-for-profit health care providers may still have to accept increased volatility in their performance indicator if they were to elect the FVO, for example, for multi-year contributions and split-interest agreements, which are primarily reported outside of the indicator pursuant to paragraph 10.21 of the Health Care Guide. However, Mr. Mechanick explained that any attempt to resolve that dilemma would require a comprehensive review of the health care sector's performance indicator model. He stated that the staff believed such

review, while perhaps desirable, was outside the scope of the FVO project.

15. The Board unanimously agreed with the staff's recommendation.

16. Mr. Mechanick further stated that the staff also recommends that the disclosure requirements in paragraphs 12(b) and 12(c) of the ED be modified for not-for-profit organizations to ensure sufficient transparency of the impact of the FVO on the changes in net assets. Mr. Mechanick noted that many of the primary users of not-for-profit financial statements are concerned more with an organization's financial ability to provide services in the future, and how and why that may have changed during the current year, than they are about projecting future cash flows. Their focus in making such assessments is on the changes in each of the net asset classes (unrestricted, temporarily restricted, and permanently restricted). Mr. Mechanick stated that, consistent with Statement 157, the staff thus recommends expanding the disclosure requirements in paragraphs 12(b) and 12(c) of the proposed Statement with regard to not-for-profit organizations to encompass the impact of the FVO not only on an operating measure/performance indicator (if presented) but also on the overall changes in the three classes of net assets.

17. The Board unanimously agreed with the staff's recommendation.

Effect of the FVO Election on Deferred Costs and Fees

18. Mr. Wilkins stated that the staff recommends that the FVO Statement indicate that the costs and fees related to financial assets or financial liabilities for which the FVO is elected be recognized in earnings as incurred and not deferred. Similarly, he stated that the FVO Statement should indicate that the unamortized deferred costs, fees,

premiums, and discounts related to existing financial assets and financial liabilities for which the FVO has been elected at the initial application of the FVO Statement should be written off as part of the cumulative-effect adjustment to the opening balance of retained earnings.

19. Ms. Seidman asked whether this applied to more than loans, to which Mr. Wilkins replied yes. He stated that the deferred origination costs of loans and the deferred acquisition costs of insurance contracts were two examples to which the staff's recommendation would apply. Ms. Seidman stated that the wording in the standard section of the final Statement should make this clear.

20. The Board unanimously agreed with the staff's recommendation.

ADDITIONAL DISCLOSURES

Reasons for Electing or Partially Electing the FVO

21. Ms. Barker stated that the staff recommends that the FVO document require an entity to (a) disclose management's basis for its decision to elect the FVO for a contract or group of similar contracts and (b) if the fair value election is not chosen for all contracts within a group of similar contracts, disclose the reasons for only partial election. She explained that the staff believes the Board should not stipulate guidance regarding how to determine groups of similar contracts. However, she further explained that the disclosure of the reasons for electing the FVO for only certain contracts within a group of similar contracts should provide sufficient information for users to understand how those groups of similar contracts reconcile to the line items presented in the statement of financial position. Additionally, Ms. Barker stated that the staff recommends the additional disclosure

requirement be required as of each date for which a statement of financial position is presented.

22. The Board unanimously agreed with the staff's recommendations.

The Difference between an Asset's Fair Value Carrying Amount and the Aggregate Principal Amount to Be Received

23. Ms. Barker stated that the staff recommends the Board require an entity to disclose the difference between an asset's fair value carrying amount and the aggregate principal amount to be received for those assets for which the FVO has been elected. She also stated that the staff recommends that this additional disclosure requirement be required as of each date for which a statement of financial position is presented.

24. The Board unanimously agreed with the staff's recommendations.

Information Regarding Significant Changes in the Fair Value of Assets

25. Ms. Barker explained that the staff believes that no specific requirement to disclose quantitative or qualitative information regarding significant changes in the fair values of assets reported pursuant to the FVO should be required. Mr. Young did not agree with the staff's recommendation. He noted that the Board had already heard complaints from users of the financial statements regarding a similar disclosure requirement in Statement 156. Mr. Trott suggested that these complaints may be a compliance issue rather than a standard setting issue.

26. The Board voted six to one (DMY opposing) in favor of the staff's recommendation.

Information about Loans and Receivables Reported at Fair Value Pursuant to the FVO

27. Ms. Barker stated that the staff recommends that the Board not require disclosure of the maximum amount of credit risk of the loan or receivable at the reporting date. She stated that the staff also recommends that, for loans and receivables for which the FVO has been elected, the Board require separate disclosure of (a) the creditor's estimate of the fair value changes attributable to changes in expected cash flows relative to borrower-specific credit risk and (b) all other changes in fair value that is included in current-period earnings. Additionally, Ms. Barker stated that the staff recommends that the Board not provide detailed computational guidance on how to determine the approximation of the amount of the loan's or receivable's fair value change attributable to changes in borrower-specific credit risk. The staff recommends that the additional disclosure requirement proposed above be required for each period for which an income statement is presented.

28. Ms. Barker further explained that the staff recommends that, if an entity classifies a loan as held for investment and elects the FVO for that loan, the entity be required to disclose the fair value carrying amount of loans ninety days or more past due. In addition, if the entity's policy for such loans is to continue to recognize interest income on an amortized cost basis separately from other changes in fair value, the entity should be required to disclose the aggregate fair value carrying amount of loans that are in nonaccrual status. Ms. Barker stated that the staff recommends that the additional disclosure requirements proposed above be required as of each date for which a statement of financial position is presented.

29. Ms. Seidman asked whether these disclosures were in response to the requests received from regulators in their comment letters. Ms. Barker explained that the staff believes that these disclosures adequately addressed the points made by regulators in their comment letters. Mr. Trott stated that he believes fair value captures more information than the current accounting for loans, but that he does not want to take away useful information provided by current GAAP (for example, charge offs and recaptures). He noted that such information is useful to users of the financial statements in understanding the risks of the assets and liabilities.

30. Mr. Linsmeier stated that it is critical for the Board to help users in the transition to fair value reporting from other measurement bases. He noted that comments arose at the User Advisory Council meeting that were similar to the point raised by Mr. Trott. That is, users of the financial statements generally support fair value measurement for all financial instruments, but that they do not want to lose the useful information already provided by existing GAAP. Mr. Linsmeier explained that he looks at all disclosures together as a package to help users of the financial statements understand the transition from one measurement basis to another. Because of this view, Mr Linsmeier stated that it is utterly important for the Board to understand whether or not all disclosures regarding the use of fair value, from Statement 107 through the FVO Statement, communicate the necessary information well. Mr. Linsmeier reemphasized that the Board needs to seriously look at the full package of fair value disclosures.

31. The Board unanimously agreed with the staff's recommendations regarding loans and receivables reported at fair value pursuant to the FVO Statement, as discussed above.

Disclosures in Year of Adoption about FVO Election of Assets Later Sold and Liabilities Settled Prematurely

32. Mr. Wilkins stated that the staff recommends that the FVO Statement not require any special disclosures if, in initially adopting the FVO Statement, the FVO has been elected at the beginning of a fiscal year for an existing financial asset or financial liability that is sold or settled (extinguished) later in that fiscal year prior to its maturity. Mr. Young stated that he is concerned about users' questions regarding adoption and whether they would have enough information to understand the effects of the FVO on existing items for which the FVO was elected. Mr. Wilkins noted that the staff is recommending a transition provision for a special one-time disclosure regarding the effects of the FVO on existing items that should address Mr. Young's concern.

33. The Board unanimously agreed with the staff's recommendation.

Aggregate FVO Disclosures in One Note

34. Ms. Barker stated that the staff recommends that all fair value disclosures for assets and liabilities reported at fair value pursuant to the FVO be provided in a single note to the financial statements. She also explained that the staff recommends that the use of tabular formats be required, when applicable.

35. Mr. Trott stated that although he does not object to grouping unique disclosures required by the FVO Statement together, he does not want to duplicate disclosures in several places. Because of this preference, he stated that he does not want to require that all FVO

disclosures be contained in one note. Mr. Trott explained that it would be better to have fair value information in the notes together rather than having FVO items together. He stated that he does not want to impair entities' ability to communicate in the most effective manner. Mr. Trott stated that he would not require consolidation of all the FVO disclosures into one note; rather, he would leave it to the preparer to decide where to put disclosures in order to communicate the best information.

36. Mr. Linsmeier stated that he is also concerned about how to communicate all of the disclosures. He explained that he wants to distinguish between book value and fair value to help users understand the book and fair values of items not required to be measured at fair value. He also would require the same information for items that are not required to be accounted for at fair value but are electively accounted for at fair value. He stated that he does not believe pulling FVO disclosures into one note versus including them with the disclosures related to the items for which the FVO is elected would be more useful. Mr. Linsmeier noted that he does not want to require that companies keep two sets of books. He explained that it is important for the Board to think strategically about disclosures and to consider what information users would need available to facilitate a transition to fair value measurements. Mr. Linsmeier stated that the disclosures should help users see the volatility in items for which the FVO was not elected.

37. Ms. Seidman stated that some of the disclosure information must be presented comprehensively, especially the qualitative information. She explained that for quantitative disclosures, an approach similar to Statement 107 could be used. That is, the numbers could be included

in one note with cross references to notes containing more detailed information regarding those numbers. Mr. Batavick stated that it is hard not to duplicate some of the disclosures because the duplicative information will be used in different areas to communicate different things. He stated that he agrees with Mr. Trott in that the preparer should have discretion in where the required disclosures of the FVO Statement are provided. Mr. Crooch stated that he agrees with Mr. Batavick.

38. Mr. Herz stated that he could agree to Mr. Trott's proposal, but that he also wants to have information displayed as explained by Mr. Linsmeier. That is, Mr. Herz indicated that he wants to start with a Statement 107 type disclosure comparing fair values and carrying values, then a discussion of why the FVO was or was not elected, and then a reference to a fair value measurements table. Mr. Herz explained that he prefers to start with the broadest disclosures and work to more detailed information. He noted that he would not object to such information being provided in a practice aid. Mr. Trott explained that he envisions one fair value note with subsections for Statement 107, the FVO, Statement 157, etc.

39. Mr. Young stated that the staff needs to provide examples to a group of users to ensure that they can gather the information they need and that the disclosures are sufficiently clear. That is, the examples should be tested with users to make sure they meet the objectives of the FVO Statement.

40. Mr. Smith stated that a majority of the Board does not agree with the staff's recommendation. He also noted that he is concerned with FVO disclosures being all over the financial statements and therefore difficult to find and use effectively. He proposed that flexibility be

provided to preparers in choosing where to incorporate FVO disclosures, but that preparers should be required to explain where fair value measurements are located in the notes to the financial statements. Mr. Smith also stated that the staff would work on providing an example of how this could be accomplished.

41. Ms. Seidman noted that many financial institutions are eager to early adopt the FVO Statement to get rid of accounting measurement attribute mismatches so that their securities could be more accurately priced. Because of the importance of the information that the FVO will provide, she suggested that the staff solicit input from financial institutions planning to early adopt the FVO Statement.

42. The Board members rejected the staff's recommendation and were unanimous in their view that companies should have flexibility in communicating the information and that the staff should provide an example of how this could be done.

Investments That Would Otherwise Be Accounted for under the Equity Method—Additional Disclosure Requirements

43. Ms. Barker stated that since the Board agrees with the staff's previous recommendation to require disclosure of the reasons an entity elects the FVO, that disclosure requirement need not be repeated for investments that would otherwise be accounted for under the equity method.

44. The Board unanimously agreed.

45. Ms. Barker explained that, due to other disclosures required by Statement 157 and the FVO document, the staff recommends that no disclosure of qualitative information about significant changes in the

fair values of investments that would otherwise be accounted for under the equity method be required.

46. The Board unanimously agreed.

47. Ms. Barker further stated that the staff recommends an entity be required to disclose, as of each date for which a statement of financial position is presented, the following for investments that would otherwise be accounted for under the equity method (because of having significant influence over the operating and financial policies of the investee) but that are reported at fair value pursuant to the FVO:

    a. The name of each investee and the percentage of ownership of common stock, as well as the accounting policies of the investor with respect to investments in common stock. (The disclosure should include the names of any significant investee corporations in which the investor holds 20 percent or more of the voting stock but the investor is not deemed to have significant influence over the operating and financial policies of the investee, together with the reasons why the investor is not deemed to have significant influence. The disclosure should also include the names of any significant investee corporations in which the investor holds less than 20 percent of the voting stock and the investor is deemed to have significant influence over the operating and financial policies of the investee, together with the reasons why the investor is deemed to have significant influence.)

    b. Summarized information about the assets, liabilities, and results of operations of the investees to be presented in the notes or in separate statements, either individually or in groups, as appropriate when investments in common stock of corporate joint ventures or other equity method investments are, in the aggregate, material in relation to the financial position or results of operations of an investor.

48. The Board unanimously agreed with the staff's recommendation in item (a) above; however, Mr. Linsmeier disagreed with item (b) since he believed that fair value provided more relevant information. The other six Board members agreed with the staff's recommendation.

49. Additionally, Ms. Barker explained that if an entity elects the FVO either upon the occurrence of a new-basis event or at the time the entity obtains significant influence for an investment that would otherwise be accounted for under the equity method, the staff recommends that the Board require quantitative and qualitative disclosures of the effect on earnings of initially measuring at fair value under the FVO election, including where in the income statement the effects on earnings were included.

50. The Board unanimously agreed with the staff's recommendation.

Consolidation of Disclosure Requirements

51. Ms. Barker stated that the staff believed that the consolidation of existing disclosure requirements for financial instruments is outside of the scope of the FVO project.

52. The Board noted that it had already discussed this in the issue above regarding consolidation of FVO disclosures.

Application of the FVO Disclosure Requirements to Statements 115 and 155

53. Mr. Wilkins stated that the staff recommended that the FVO Statement require that the disclosure requirements in that Statement also apply

to investments in securities that are classified in the trading category under FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* and the hybrid financial instruments that are reported at fair value through earnings under the fair value election permitted by FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*, and its amendment of paragraph 16 of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*.

54. The Board unanimously agreed with the staff's recommendation.

Incorporation of a Statement 107 Disclosure Requirement

55. Mr. Wilkins stated that the staff recommends that the FVO Statement require that, if the carrying amounts of individual line items reported in the statement of financial position are a combination of fair value and non-fair-value amounts, the fair value disclosures in the notes shall be presented together with those related individual carrying amounts for those line items.

56. The Board unanimously agreed with the staff's recommendation.

TRANSITION AND EFFECTIVE DATE

57. Ms. Barker explained that the staff majority recommends that the effective date of the FVO document be the same as the effective date of Statement 157 and, thus, the FVO Statement should be effective for financial statements issued for fiscal years beginning after November 15, 2007. Mr. Wilkins indicated that a staff minority recommends that the FVO Statement should be effective for financial statements issued for fiscal years beginning after November 15, 2008, in order to provide companies with additional time to identify the existing financial assets and financial liabilities for which they would

like to elect the FVO. Ms. Barker explained that the staff recommends that an entity be permitted to early-adopt the FVO document but believes that an entity must also concurrently adopt all of the requirements (measurement and disclosure) of Statement 157 for any item for which an entity has elected the FVO (without having to adopt Statement 157 on an entity-wide basis).

58. Additionally, Ms. Barker explained that the staff recommends no modification to the requirement that an entity that early-adopts the FVO document must do so as of the beginning of an entity's fiscal year that begins after issuance of the final FVO Statement. (The staff notes that the early-adoption provisions of Statement 155 and FASB Statement No. 156, *Accounting for Servicing of Financial Assets*, permit adoption as of the beginning of an entity's fiscal year, provided that the entity has not yet issued financial statements, including any interim financial statements, for that fiscal year.)

59. The Board unanimously agreed with the majority staff's recommendation to have the effective date be the same as the effective date of Statement 157. That is, the FVO Statement will be effective for financial statements issued for fiscal years beginning after November 15, 2007. The Board also unanimously agreed that an entity is not permitted to early-adopt the FVO Statement prior to the adoption of Statement 157 on an entity-wide basis. Board members were uniform in their desire to reduce the complexity of the effective dates and transition provisions for users and preparers.

60. The Board disagreed with the staff's recommendation to permit early adoption of the FVO Statement for only fiscal years that begin after issuance of the final FVO Statement. The Board voted six to one (DMY opposing) to permit a reporting entity to elect early adoption of

the FVO Statement within 120 days of the beginning of the entity's earlier fiscal year for which it has not yet issued financial statements for any interim period of that fiscal year, in which case the FVO election for then existing financial assets and financial liabilities would be retroactive to the beginning of that fiscal year (or the date of initial recognition, if later). Mr. Young generally disagreed with permitting early adoption of the FVO Statement until the Board had considered the systems changes necessary on the part of users in order to use and analyze the new information that will be provided pursuant to the FVO Statement.

61. Ms. Barker stated that the staff recommends no modification to the requirement that the effect of initial adoption be accounted for as a cumulative effect adjustment through retained earnings. She also stated that the staff recommends no modification to the prohibition against retrospective application to previously reported periods.

62. The Board unanimously agreed with both of those staff recommendations.

63. Additionally, Ms. Barker explained that the staff recommends that the FVO document require a one-time reconciliation disclosing the current historical/amortized cost amount with the corresponding fair value measures as of the date of adoption for those items reported pursuant to the FVO. She also stated that the staff recommends that the reconciliation be presented by major category of assets and liabilities, as presented in the statement of financial position.

64. The Board unanimously agreed with both of those staff recommendations.

MISCELLANEOUS SCOPE ISSUES

Hybrid Nonfinancial Instruments

65. Mr. Wilkins stated that the staff recommends that the Board specifically permit the FVO election for a host financial instrument that is being accounted for separately due to the bifurcation of an embedded derivative nonfinancial instrument from a hybrid nonfinancial instrument pursuant to paragraph 12 of Statement 133, provided that the scope exceptions in the FVO Statement are not applicable to the host financial instrument.

66. The Board unanimously agreed with the staff's recommendation.

Convertible Debt

67. Mr. Wilkins explained that the staff recommends that a scope exception be added to the FVO Statement to prohibit only the issuer of convertible debt with beneficial conversion features (whether contingent or non-contingent) from electing the FVO for that contract.

68. Mr. Wilkins noted that the proposed scope exception would not impair the ability of the issuer to elect, at the date of initial recognition, the FVO for convertible debt without beneficial conversion features. (Because convertible debt is a debt security under Statement 115, the investor already has the ability to choose to account for its investment in convertible debt at fair value with the changes in fair value reflected in earnings as they occur.)

69. Ms. Seidman suggested that the scope exception be for all contracts issued or held by the reporting entity that are both (a) indexed to its own stock and (b) classified in stockholders' equity in its statement of financial position. Additionally, to cover convertible debt securities,

the scope exception would also apply to contracts issued or held by the reporting entity that contain embedded derivatives that both (1) are indexed to its own stock and (2) would, on a standalone basis, be classified in stockholders' equity in its statement of financial position.

70. The Board unanimously agreed with Ms. Seidman's recommendation.

Distinguishing the Scopes of Statement 115 and the FVO Statement

71. Mr. Wilkins stated that the staff recommends that Statement 115 be amended to exclude from its scope all investments that, absent a FVO election under the FVO Statement, would be required to be accounted for under the equity method of accounting under Opinion 18 (rather than excluding "investments in equity securities accounted for under the equity method").

72. The Board unanimously agreed with the staff's recommendation.

Follow-up Items:

73. Mr. Herz asked the staff to provide the Board with examples of the application of the contract-by-contract election to various financial instruments.

General Announcements:

74. None