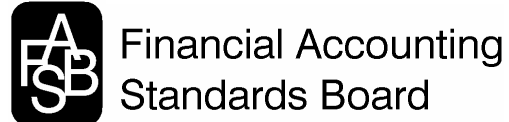


## MINUTES



**To:** Board Members

**From:** Van Beek (ext. 447)

**Subject:** Minutes of the October 11, 2006 Board Meeting—FSP EITF 03-6-a, “Determining Whether Instruments Granted in Share-Based Payment Transactions are Participating Securities” **Date:** October 18, 2006

**cc:** Bielstein, Smith, MacDonald, Leisenring, Polley, Golden, Cassel, Sarno, J. Johnson, Stevens, Bolash, Jolla, Singleton (IASB), Van Beek, Sledge, Vernuccio, Richter, Gabriele, Carney, Allen, 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: Proposed FASB Staff Position EITF 03-6-a, “Determining Whether Instruments Granted in Share-Based Payment Transactions are Participating Securities”

Basis for Discussion: Memorandum No. 1, dated October 5, 2006

Length of Discussion: 9:15 a.m. to 9:25 a.m.

Attendance:

Board members present:	Herz, Batavick, Crooch, Linsmeier, Seidman, Trott, Young, and Leisenring (IASB)
Board members absent:	None
Staff in charge of topic:	Sarno
Other staff at Board table:	L. Smith, Golden, and Van Beek
Outside participants:	None

### **Summary of Decisions Reached**

The Board decided to issue a proposed FASB Staff Position (FSP) to address whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in basic earnings per share (EPS) using the two-class method described in paragraphs 60 and 61 of FASB Statement No. 128, *Earnings per Share*. In approving the proposed FSP for issuance, the Board decided that unvested share-based payment awards that provide a noncontingent transfer of value constitute a participation right and therefore should be included in the computation of basic EPS pursuant to the two-class method.

The Board also decided that:

1. The guidance in the final FSP should be applied as follows:
  - a. The effective date should be the first reporting period beginning after the date the FSP is posted to the FASB website.
  - b. All prior-period EPS data presented should be adjusted retrospectively (including interim financial statements, summaries of earnings, and selected financial data) to conform with the provisions of the FSP.
2. The FSP should be exposed for a 60-day comment period.

The Board directed the staff to proceed to draft a proposed FSP for vote by written ballot.

### **Objective of Meeting**

The objective of this meeting was for the Board to discuss whether to approve for issuance a proposed FSP to address whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in basic EPS using the two-class method described in paragraphs 60 and 61 of Statement 128. The objectives of the meeting were met.

### **Matters Discussed and Decisions Reached**

#### **BACKGROUND AND TA&I COMMITTEE RECOMMENDATIONS**

1. Mr. Sarno opened the meeting by stating that the TA&I Committee (the Committee) considered two possible alternatives for unvested share-based payment awards. The first alternative would not have considered unvested share-based payment awards participating securities and therefore would have excluded them from the earnings allocation in computing basic EPS pursuant to the two-class method. The second alternative, and the Committee's recommendation for the Board, requires that unvested

share-based payment awards that provide a noncontingent transfer of value constitute a participation right and therefore should be included in the computation of basic EPS pursuant to the two-class method. To illustrate the Committee's recommendation, a share-based payment award that contains a nonforfeitable right to receive cash when dividends are paid to common shareholders irrespective of whether that award has vested or remains unvested shall be considered a participating security. Conversely, a share-based payment award that participates in undistributed earnings via a reduction in the exercise price of the award when distributions are made to common shareholders would not be considered a participation right because the transfer of value to the holder of the award is contingent upon the exercise of the award.

2. Mr. Linsmeier inquired whether the Board had considered treating dividends and dividend equivalents as compensation cost, rather than as a component of the earnings per share computation. Mr. Trott stated that the Board decided (in FASB Statement No. 123 (revised 2004), *Share-Based Payment*) that dividends and dividend equivalents that are actually paid to share-based payment award holders that are expected to vest are comparable to regular dividends paid to common shareholders and therefore they should not be treated as compensation cost. He stated that these share-based payment awards are equity instruments and thus the payments made on those equity instruments are considered dividends rather than compensation cost. Ms. Seidman stated that expected dividends are considered when calculating the estimate of the fair value of share-based payment awards. Mr. Leisenring added that treating dividends paid to share-based payment award holders as compensation cost would result in a double counting of the compensation cost.

3. Mr. Trott stated that whether instruments granted in share-based payment transactions are participating securities prior to vesting is an issue because (a) the dividends received on those instruments (expected to vest) are not considered compensation cost and (b) the share-based payment equity instruments have similar rights and receive similar payoffs, but are nonetheless different from common shareholders. Mr. Trott stated that the Committee's recommendation is based on the premise that (a) the unvested equity instruments resulting from share-based payment transactions are a form of equity instruments that have different characteristics than that of common stock and (b) holders of these instruments participate in the distributed and undistributed earnings of an entity.

4. Mr. Herz inquired whether diversity in practice currently existed and how dividends and dividend equivalents were currently being treated. Mr. Golden stated that entities are consistently treating dividends and dividend equivalents (paid on the underlying equity shares resulting from share based payment awards) as regular dividends paid to common shareholders (not compensation cost) with no charge against net income. Further, entities are not including these unvested share-based payment awards in the computation of EPS.

5. All Board members agreed with the Committee recommendation that unvested share-based payment awards that provide a noncontingent transfer of value constitute a participation right and therefore should be included in the computation of basic EPS pursuant to the two-class method and approved the proposed FSP for issuance.

#### **COMMENT PERIOD AND TRANSITION**

6. Mr. Sarno concluded by stating that the staff recommends that the proposed FSP should be exposed for a 60-day comment period. The effective date should be the first reporting period beginning after the date the FSP is posted to the FASB website. All prior-period EPS data presented shall be adjusted retrospectively (including interim financial statements, summaries of earnings, and selected financial data) to conform with the provisions of this FSP. All Board members agreed with the staff recommended comment period and transition requirements.

#### **DRAFTING A PROPOSED FSP**

7. There were no further comments by the Board. The Board directed the staff to proceed to draft a proposed FSP for vote by written ballot.

#### **Follow-up Items:**

8. The staff will draft a proposed FSP for vote by written ballot.

#### **General Announcements:**

9. None