

MINUTES



Financial Accounting
Standards Board

To: Board Members

From: FVM/FSP Team (Arveseth, ext. 384)

Subject: Minutes of the July 26, 2006 Board Meeting: Proposed FSP on the Measurement of Certain Nonfinancial Assets and Nonfinancial Liabilities

Date: August 1, 2006

cc: Bielstein, L. Smith, MacDonald, Fair Value Measurements Team, Business Combinations Team, Derivatives Disclosures Team, McBeth, Polley, Gabriele, Carney, Allen, Sutay, Leisenring (IASB), Nelson (IASB), FASB Intranet

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Topic: Proposed FSP on the Measurement of Certain Nonfinancial Assets and Nonfinancial Liabilities

Basis for Discussion: Memorandum dated July 13, 2006

Length of Discussion: 10:30 a.m. to 11:45 a.m.

Attendance:

Board members present: FASB: Batavick, Crooch, Herz, Seidman, Trott, Young, and Linsmeier
IASB: Leisenring

Board members absent: None

Staff in charge of topic: Stevens

Other staff at Board table: MacDonald, Todorova, Arveseth, Lott, Bielstein, and Smith

Outside participants: None

Summary of Decisions Reached

The Board discussed the diversity in practice that has arisen with respect to the use of an entity's own assumptions, rather than market-participant assumptions, to measure the fair value of nonfinancial assets and nonfinancial liabilities. The Board decided to provide guidance to address that diversity in practice and directed the staff to develop alternative approaches for discussion at a future Board meeting.

Objective of Meeting

The objective of the meeting was for the Board to discuss alternatives to address the diversity in practice that has arisen with respect to the use of an entity's own assumptions to measure the fair value of nonfinancial assets and nonfinancial liabilities. The objective of the meeting was met.

Matters Discussed and Decisions Reached

1. Mr. Stevens opened the discussion by noting that a number of reviewers of the draft of a final Statement on fair value measurement (draft Statement) expressed concern that the application of the market-participant approach to nonfinancial assets and nonfinancial liabilities would change the existing measurement approach under FASB Statements No. 141, *Business Combinations*, No. 142, *Goodwill and Other Intangible Assets*, and No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. Moreover, Mr. Stevens noted that those reviewers expressed significant concerns about the operability of the guidance for the reporting entity to identify market participants and to use their assumptions in fair value measurements. Additionally, some reviewers asserted that measurement of a nonfinancial asset should reflect the manner in which that asset will be deployed in the entity's operations rather than the manner in which that asset would be deployed by a market participant.

2. Mr. Stevens stated that, although these comments were received in connection with the draft Statement, the requirement to use market-participant

assumptions is currently specified in Statements 141, 142, and 144. However, certain language in those Statements may have caused some confusion about the requirement to use market-participant assumptions in fair value measurements and, as a result, different interpretations have been reached in practice. Mr. Stevens noted that the Board added this project to its agenda with the objective of issuing guidance to resolve those practice issues.

3. Mr. Stevens stated that this guidance would not affect the final Statement on fair value measurement; rather, it would amend the guidance in Statements 141, 142, and 144 to permit entities to measure certain nonfinancial assets and nonfinancial liabilities using their own assumptions. Mr. Stevens stated that such proposed guidance would potentially:

- a. Identify circumstances in which an entity may use its own assumptions in fair-value-based measurements of nonfinancial assets or nonfinancial liabilities, regardless of whether market-participant assumptions are available without undue cost and effort.
- b. Explicitly state that the use of an entity's own assumptions in fair-value-based measurements of nonfinancial assets or nonfinancial liabilities is not intended to permit an entity to assume that the asset or liability should be measured at zero.
- c. Clarify that, depending on the nature of the entity's own assumptions versus market-participant assumptions with respect to a particular nonfinancial asset or nonfinancial liability, a fair-value-based measurement using an entity's own assumptions could be less than, equal to, or greater than a fair value measurement of the asset or liability.
- d. Contain examples illustrating the use of an entity's own assumptions in fair-value-based measurements.

4. Mr. Stevens asked the Board if it supported the issuance of a proposed FASB Staff Position (FSP) that, for measurements within its scope, would permit the use of an entity's own assumptions instead of market-participant assumptions to measure nonfinancial assets and nonfinancial liabilities that would otherwise be required to be measured at fair value. The Board agreed to provide guidance that would address the practice issues related to the use of market-participant assumptions under Statements 141, 142, and 144.

However, there were differing views among the Board members regarding the nature and scope of that guidance.

5. Mr. Trott stated that an entity-specific measurement is not equivalent to a fair-value-based measurement. Therefore, Mr. Trott stated that the guidance should not provide a new method for measurement under Statements 141, 142, and 144, but, rather, should explain that an entity must use market-participant assumptions that are available without undue cost or effort in making fair value measurements. Mr. Trott stated that part of the confusion has resulted from the use of fair value measurements by some entities in circumstances where the relevant GAAP does not specify a fair value measurement attribute. For example, paragraph 37(d)(1) of Statement 141 specifies that plant and equipment to be used shall be measured at the current replacement cost for similar capacity unless the expected future use of the assets indicates a lower value to the acquiring entity (that is, it does not require that plant and equipment to be used be measured at fair value). He further noted that Statement 141 does require a fair value measurement for intangible assets and indicated that the Board will be analyzing the appropriateness of that measurement attribute in its current project on business combinations.

6. Ms. Seidman stated that the proposed guidance should address the diversity that exists related to the requirements to use market-participant assumptions under Statements 141, 142, and 144. She noted that the Board will be redeliberating some of those provisions in its project on business combinations (and a possible future convergence project on impairment). In the interim, Ms. Seidman stated that the proposed guidance should permit entities to continue to incorporate assumptions about their intended use of an asset that is required to be measured at fair value in cases where information about fair value is not observable. That type of approach would seem to bridge between the references to budgets, etc., and the fair value measurement objective.

7. Mr. Batavick noted that the fair value measurement criteria in the draft Statement are more developed than the criteria under Statements 141, 142,

and 144. In addition, Mr. Batavick stated that many entities may view a cash-flow analysis based on their intended use of an asset to be consistent with a fair value measurement that is based on the assumptions market participants would use in pricing the asset. Mr. Batavick further stated that the guidance should permit entities to continue with their current practices until these issues are resolved as part of other projects on the Board's agenda.

8. Mr. Linsmeier stated that part of the confusion caused by Statements 141, 142, and 144 relates to the guidance permitting an entity to use its own assumptions if market-participant assumptions are not available without undue cost and effort. Specifically, those standards are not necessarily clear regarding how the potential existence of contrary data may impact the use of an entity's own assumptions in those circumstances.

9. Mr. Herz stated the concept of fair value has been construed on a wider basis than it is used in the draft Statement. Mr. Herz stated that the Board should have two objectives for the issuance of guidance to address the practice issues related to the use of market-participant assumptions under Statements 141, 142, and 144. The first objective is to ensure a consistent use of the term *fair value*. The second objective is to determine an appropriate method of how to address the existing practice issues.

10. Based on the views expressed by the Board members, Mr. Herz summarized those views into two alternatives for the Board to consider related to the issuance of an FSP on the measurement of nonfinancial assets and nonfinancial liabilities. They are:

- a. Permit an alternative to a fair value measurement that would otherwise involve significant unobservable inputs (Level 3). For example, that alternative may permit an entity to measure a nonfinancial asset using the assumptions that would be used by a market participant that would deploy the asset in the same manner as the reporting entity. Another possible alternative would be to permit a *value-in-use measurement* (that is, as that term is used in IAS 36, *Impairment of Assets*).

- b. Clarify that an entity may measure a nonfinancial asset using its own assumptions in circumstances where no contrary data exist indicating market participants would use different assumptions.

Mr. Herz requested that the staff develop an analysis of those alternatives and how those alternatives relate to the Board's construction of Level 3 inputs in the draft Statement. Mr. Herz stated that the issuance of the final Statement on fair value measurement should not be postponed pending the Board's decisions on that analysis.

Follow-up Items:

The Board requested that the staff develop alternative approaches for discussion at a future Board meeting.

General Announcements:

None.