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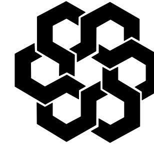
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These notes are based on the staff papers prepared for the IASB and FASB. Paragraph numbers correspond to paragraph numbers used in the joint IASB-FASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

IASB/FASB Meeting: **21 April 2008, London**

Subject: **Completing the February 2006 Memorandum of Understanding: Developing a progress report and timetable for convergence between IFRSs and US GAAP (Agenda paper 3)**

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1. Earlier this year, Bob Herz and David Tweedie agreed that the Boards should provide a progress report and develop a work plan for the completion of the February 2006 Memorandum of Understanding (MOU). When issued, the MOU set out joint project priorities and milestones only through 2008. Both Chairs agreed that constituents would want to know how the Boards intend to proceed beyond 2008 towards completion.

2. To develop the progress report, the Chairs agreed on the need to lay out the updated MOU through at least 2011 and called upon a small team (the Group) to set forth proposals, which are outlined in this paper. In developing proposals, the Chairs asked the Group to identify the relative priority of needed financial reporting improvements, the time frames for completing them, and the major milestones along the way. The two Chairs also agreed that the Boards should consider whether process changes can or should be implemented to reduce the time required to develop standards.

3. While the long-term objective of the MOU to develop improved and converged standards for IFRSs and US GAAP remains relevant, the Group recognized that a previous objective already has been achieved: progress toward improving standards so that the SEC would feel comfortable removing the reconciliation requirement for non-US companies that use IFRSs and are registered in the United States.[1] With the removal of the reconciliation, the Group decided that a logical starting point for any MOU progress report and completion plan (referred to as the MOU completion plan throughout) is to update the Boards' medium-term objective. The Group recommends the following objective:

   > To outline the improvements to existing IFRS that are needed to facilitate mandatory adoption of IFRS in all major capital markets.

4. The Group was tasked with developing recommendations consistent with the following two assumptions:
   a. For capital markets not yet adopting IFRSs, the target date of mandatory adoption is no later than 2013.
   b. A "quiet period" of at least a year before that date is provided.

5. Those assumptions mean that the MOU completion plan should describe progress to be made between now and around mid-2011, a period of about 3 years (36 months). Three years sounds like a long time until you do some math:
   a. Issuing a due process document usually takes about 12 months away from deliberations/analysis—on average, it takes 3 months to prepare and ballot a due process document, 6 months for exposure, and another 3 months to read and summarize comments.
   b. If major projects (except those of exceptionally urgent nature) require two due process documents to complete it (a discussion paper and exposure draft), that leaves about 12 months for Board deliberations, ignoring preparation and

[1] In April 2005, SEC Chief Accountant Don Nicholaison gave a speech that outlined a "roadmap" for removal of the 20-F reconciliation. That roadmap said that removal of the reconciliation would depend on, among other things, measurable progress in addressing priority issues on the IASB-FASB convergence work programme. The Boards developed the MOU to describe for the SEC and others the progress the Boards planned to achieve by 2008.

balloting of the final standard (36 months total less 24 months of due process). The Boards have yet to deliberate any phase of a joint project in less than 12 months (not even short- term convergence projects). It took 18 months to take business combinations from ED to final, and we didn't even converge on all points.

   c. Fortunately, discussion papers already have been issued (liabilities and equity) or will be issued by mid-2008 on several major projects (revenue recognition and financial statement presentation). The Boards should have at least 24 months to deliberate issues in those projects. However, the Boards have been deliberating issues in many of those projects for at least five years. The issues are many and controversial, and completing them in two years represents a significant challenge.

6. So, regardless of the type of project, a mid-2011 completion date goal requires that the Boards work more efficiently than they ever have. Discussions around improving efficiency of projects often revolve around issues of project administration—meeting frequency, staffing, or other work methods issues. Those are all worthy of discussion, and we will discuss them during the administrative portion of the joint meeting. However, there is another fundamental reason why projects take as long as they do: The Boards (and members within each Board) sometimes don't agree on what they are trying to fix and how to fix it.

   a. There are often differences in views over issues of agenda size and project scope—progress is slowed by discussions about whether a project is worthwhile, or whether the issues within a project are worthwhile resolving, or often, expansion of project scope. Short-term convergence projects are good examples of this. Financial statement presentation might be another example of scope "creep" (the scope of the project expanded to include revisions to segment disclosures based on the view that existing segment disclosures were deficient).

   b. A second source of difference is over the approach to be taken, usually, differences in views about the need to develop a conceptual model as the basis for the revised standard. Revenue recognition is an example. Some see the problem as a lack of a robust conceptual model on which to base a principles-based standard, while others seem to see the problem as the lack of standards-

level guidance in specific areas such as multiple-element transactions for which a more focused patch-up effort is appropriate (or, in the US, an effort to codify and rationalize existing practices into three or four models).

c. A third is what we call "cross-cutting" issues—differences in views about whether and how similar issues in active projects should be resolved consistently. If internal consistency is the goal, no project can move any faster than any other to which it is related (for example, under this view, the IASB's replacement business combination standard couldn't be issued until the IASB completed fair value measurement).

7. Each of those differences essentially relates to the project objective—the deficiency the Boards are trying to fix and the way of fixing it. A significant amount of Board time is consumed re-debating those same issues.

8. The Group thus decided that if the Boards are going to be successful completing some set of projects by mid-2011, agreeing on project objectives in April is critical. Board members and staff on the losing end of those debates need to be willing to work hard to achieve an objective with which they don't fully agree. We simply do not have time for "do-overs." For that reason, the Group focused first on identifying and articulating project objectives—the improvements it believes can be accomplished by the mid-2011 goal date. The Group notes, however, that more will be required than defining project objectives. Meeting those improvement goals will require improving our meeting and work processes on some projects too.

9. As we analyzed projects, we found that our priorities, and we suspect the views of Board members, may be driven by two potentially conflicting views:

    a. The IASB agenda priorities should limit the possibility that a company adopting IFRS in 2013 would undergo two changes in a relatively short period (the first change being the adoption of IFRS and the second change being a major revision of an IFRS standard). Thus, work completed by 2011 should be designed to remain in place for three or more years after completion; any other changes to IFRS during the 3-year period after 2011 should be modest. Under this view:

        i. Significant, fundamental weaknesses in existing IFRS need to be prioritized for completion by mid-2011.

    ii. Worthwhile improvements to IFRS can be deferred beyond 2011 if the existing IFRS and US standards are similar (leasing would be an example of this).

b. The IASB always should seek to improve financial reporting, regardless of the timing of IFRS adoption, whether by the US or any other major capital market. This suggests that the IASB should emphasize projects in which major improvements are needed. Under this view:

    i. Significant, fundamental weaknesses in existing IFRS need to be prioritized for completion by mid-2011.

    ii. Worthwhile improvements should not be delayed. For example, if leasing is broken, it should be fixed.

10. The Group concluded that achieving a mid-2011 completion goal will require revisions to scopes and objectives of at least some projects. Thus, the Group's recommendations also considered a pervasive constraint. That is, the Group considered whether the changes that the Boards could reasonably expect to achieve by 2011 are a sufficient improvement in financial reporting to justify the cost those changes might impose on users and preparers of financial statements.

11. In analyzing the individual projects, the Group found it useful to divide them into three categories, listed below in what we see are their relative order of priority:

    a. Projects that address areas where fundamental improvement in IFRS and possibly US GAAP are needed. This category includes revenue recognition and fair value measurement guidance. Given the current situation surrounding the credit crisis, we also include in this category consolidations (with special attention to special-purpose entities) and derecognition.

    b. Projects that address areas for which there is a significant need for improvement in both IFRS and FASB standards. This group generally includes the balance of the MOU.

    c. Projects that address areas in which IFRS currently does not provide guidance. This group includes insurance accounting and accounting for extractive industries. We have not included a separate discussion of this category in this memorandum. We question whether the insurance project can be completed by 2011, given the significant political opposition and demands for additional

field testing. A project on extractive industries is certainly beyond our ability to complete by 2011. At best, the IASB might agree to publish a discussion document on extractive industries prepared by the existing working group of national standards setters, so long as doing so does not consume any Board or staff resource.

The Group notes that it is not exactly true that IFRS does not provide guidance in these areas. IFRS 4 and IFRS 6 contain guidance that enables companies to continue reporting under their existing accounting policies, a status quo situation that new adopting countries presumably would accept. Moreover, provisions within those standards preclude voluntary accounting changes in accounting policies other than those that produce more relevant and no less reliable information. Those provisions should be an adequate safeguard against the adoption of IFRS resulting in a step backward in information content or quality.

12. Group members have different views whether some or all of the Framework should be included in the MOU completion plan.

    a. Some think that the MOU completion plan should focus on standards-level projects. The obstacles faced by companies in switching to IFRS in the near future will be at the standards level. Notwithstanding the hierarchy and IAS 8, work on the Framework, while important, has little effect on a company implementing IFRS.

    b. Others think that some of the Framework, in particular measurement and a disclosure Framework, should be included in the MOU completion plan. The Framework will be the basis for developing standards in the future, and it is important that those major gaps be filled before mandatory adoption of IFRS is required.

13. Another question is whether the MOU completion plan should include other projects on which the Boards have committed to work jointly but were not included in the MOU. We also have not addressed these projects in this memorandum, including those like emission rights on which the Boards hope to work together. The importance of the 2011 date is such that all of those projects must take a subsidiary role to the ones addressed in this memorandum. For their part the IASB and FASB directors intend to make the projects in this memorandum their primary staffing priority. If necessary, they will remove staff

from other projects to serve the projects addressed in this memorandum and will not staff other projects unless and until staff become available.

14. Some Group members think the Boards should actively consider and make decisions about those other joint projects. The purpose of the MOU completion plan is to focus the agenda. If there is insufficient staff or Board time to focus on other joint projects, the Boards should consider removing them from the agenda or formally suspending them. Retaining projects on the agenda that the Boards do not plan to actively work on creates uncertainty for our constituents and can be demoralizing to the staff assigned to them.

15. One other note bears mention before we turn to the detailed analysis of projects. For some projects, the end game is clear and there appears to be significant Board support for achieving that objective. Defining the scope for these projects that can be achieved by 2011 is straightforward. For other projects a solution that would constitute a sufficient improvement in financial reporting is not clear. Those projects are more problematic and, in some cases, we have suggested that some specific decisions may need to be deferred to the October joint meeting.

16. In summary, the Group recommends that the Boards reach a decision on the scope of the MOU completion plan—whether it should include the Boards' joint agenda in full and describe priorities, milestones, and completion dates for each project, or whether it should include only a priority subset of the joint agenda (as was the case with the MOU).

Projects that address fundamental deficiencies in IFRS that require completion as a high priority

17. **Revenue recognition.** We view completing the project to be critical to U.S. adoption of IFRS—revenue is fundamental to financial statement analysis, and the existing guidance in IAS 18 is incomplete, insufficient, and internally inconsistent. We need to recognize that IAS 18 often is applied with US GAAP as a backstop. Preparers who do not find a ready answer in IAS 18 often resort to the detailed guidance provided in US GAAP, so long as that guidance is not inconsistent with IAS 18.

18. In our view, the broad project objective is to develop a single model of revenue recognition that can be applied to a variety of transactions and can resolve current revenue recognition issues consistently.

Recommendation

19. A majority of Board members appear to support (or at least would not object to) the so-called customer consideration approach to measuring performance obligations. We, therefore, recommend that the Boards proceed on that basis. Building on that recommendation, the Boards should move expeditiously to address the following areas:

    a. The definition of a performance obligation

    b. When/how performance obligations are satisfied/extinguished

    c. When, if ever, the initial amount assigned to a performance obligation should change for reasons other than performance (for example, the accounting for arrangements with variable consideration such as volume or milestone-based pricing)

    d. The accounting for conditional obligations such as rights of return

    e. Disclosure

    f. Testing the conclusions reached against existing practice problems. A new revenue recognition model that does not resolve the practice problems recently raised for EITF or IFRIC consideration would not, in our view, represent an improvement in practice. The FASB staff, with its greater experience in topics considered by the EITF, is probably better positioned to perform this part of the work.

20. In our view, the items above (especially items a and b) must be resolved before the Boards issue a discussion document.

21. Given the number of significant issues outstanding, completing a revised revenue recognition standard by mid-2011 represents a major challenge. Focused effort is required to achieve it.

Alternatives considered

22. We also considered an option that focuses on improving disclosures. At the December 2007 FASB-AAA conference, many users identified inadequate disclosures as a glaring weakness of both US GAAP and IFRS. They said improving disclosures should be a

priority. An option for the Boards is to focus on improving disclosures about revenue by 2011, to be followed at a later date by improved standards of recognition and measurement. A primary disadvantage of this approach is that (a) disclosure is a poor substitute for recognition and measurement and (b) disclosure projects tend to reduce the interest in solving the more difficult standards issues.

23. We also observed that users' comments about the need for disclosure tend to focus on the revenue recognition for a particular type of transaction. Crafting a disclosure package that would provide sufficient information about an entity that has perhaps 100 or more different revenue transactions would be daunting. It is not clear the result would satisfy the needs of users.

24. We considered a narrower scope, aimed at making targeted improvements to IAS 18. While a narrow scope might seem appealing, we rejected it. The Boards have not devoted any significant attention to identifying the targeted improvements to IAS 18 that might prove useful. Doing so would constitute a major change in course and would set aside much of the work that already has been done. Nor do we see the possibility that targeted changes might constitute a sufficient improvement in IAS 18 to overcome concerns expressed by the SEC and others.

25. **Fair value measurement.** The Group thinks this project is critical to the adoption of IFRS. Like US GAAP before the issuance of Statement 157, IFRS lacks a consistent/robust definition of fair value. Moreover, members of the FASB Investors Technical Advisory Committee have said the lack of "Statement 157 disclosures" in IFRS is a significant issue for investors.

Recommendations

26. The Group thinks this project should be completed by mid-2011 by limiting its objective to the following:

    a. Amending existing IFRS to replace the various measurement terms used with either entry price or exit price based on the intent of the existing standard

    b. Defining exit price identically to Statement 157

c. Defining a comparable entry price, and providing disclosures about entry and exit price measurements.

27. In our view, this project cannot be completed by 2011 if the IASB seeks to reconsider fundamental features of the FASB standard. Those include, for example, the idea of a market participant view, highest and best use, and principal market.

28. Board discussions of fair value easily and often migrate into conceptual discussions of matters such as

    a. Which measurement attribute *should* be used, rather than what existing standards require

    b. Whether gains on initial recognition are ever appropriate

    c. Is an entity-specific measure an attribute—what does an entity-specific measurement mean?

29. Completing a fair value measurement standard by 2011 requires that the Boards leave those conceptual discussions for the Conceptual Framework or other standards-level projects.

30. **Consolidation Policy.** The FASB has added a project to address identified weaknesses in FIN 46R and Statement 140. (However, that project is limited to narrow improvements and does not address the more basic needs.) The SEC and others expect those improvements to be completed within a year.

31. The IASB continues to discuss improvements to IAS 27. The critical issues are improved guidance relating to effective control and special-purpose entities. Most IASB members seem to agree that analysis of SPEs requires a risk and rewards as an indicator of control; however, some seem to be unsure about whether the principles developed to date would produce appropriate financial reporting results in all circumstances.

Recommendations

32. The goal by 2011 should be a consolidation policy standard that embraces the idea of effective control. A small group of IASB Board members and staff have held preliminary

discussions and outlined an approach. The team should bring that approach to the Board for consideration at the earliest possible time.

33. One possible way of accelerating progress on SPE's might be to retain those who were intimately involved in developing FIN 46R to develop and articulate a set of principles that underpins FIN 46R that would retain the approach but reduce the standard's complexity and perhaps make it suitable for international application. This analysis also should consider deficiencies identified by the FASB in its recent efforts to improve FIN 46R

34. **Derecognition.** The Boards decided in 2006 that both of our derecognition standards needed improvement. Statement 140 was then deemed to be irretrievably broken, and still is despite ongoing repair and maintenance work. IAS 39 was then, and still is, viewed by many as internally inconsistent and anecdotal evidence indicates that it is inconsistently applied in practice. For those reasons, the Boards decided that jointly developing a replacement for both standards was the best path forward.

35. The perceived need for replacement standards has not changed since 2006; however, the current economic situation has changed the relative priority of that project. The US securitization market is several multiples the size of the market in other parts of the world, even recognizing the current credit crunch. Adoption of IAS 39 and SIC 12 by the US marketplace would likely trigger an avalanche of application inquiries and put a spotlight on inconsistent practices.

36. Significant progress toward a replacement standard has been made in the form of a staff research paper developed in consultation with a team of Board advisors. More work is needed, however, primarily to address securitization issues. In particular, the focus now is on who collects the cash, which causes issues in principal-agent relationships. Staff turnover has resulted in a loss of momentum, and progress will be slowed as new staff get up to speed.

Recommendations

37. The Financial Stability Forum has indentified addressing off-balance sheet exposures as an urgent priority, in light of the ongoing credit crisis, and urged standard setters to make improvements on an accelerated basis. This may require making an exposure draft the first document provided for public commentary.

38. We recommend the Boards do so by undertaking the following actions steps in the very near term:

    a. Complete the staff research paper. This will require assigning more experienced staff to address the principal-agent issues. We cannot afford the luxury of waiting for the newly assigned staff to get up to speed on these issues.

    b. Consider comment letters on the FASB proposed revisions to Statement 140 for further insights.

    c. Based on steps a. and b., determine next steps at the October joint board meeting for accelerating development of a new standard.

    d. Consider establishing a small, focused working group of experienced investors, preparers, and auditors that can advise the staff, starting its work during the comment period.

Projects that address areas for which there is a significant need for improvement in IFRS

39. **Financial statement presentation.** The stated purpose of this project is to develop standards for presentation of financial information within the primary financial statements. Many Board members seem to agree that this project is important because of the potential it holds to increase the understandability of financial information produced by the use of fair values within the mixed-attribute measurement system.

40. The most challenging/contentious issue is whether to retain "net income/profit and loss" or some other intermediate measure of performance and the related recycling issue. The Boards need to decide when and where they want to tackle this issue.

a. Some seem to think that the issue is beyond the scope of a presentation project. They believe changes to "net income/profit and loss" are recognition matters to be dealt with in other projects.

b. Others seem to think that "net income/profit and loss" is a presentation issue. It is a matter of disaggregating comprehensive income into components or categories—net income/profit loss is no different than requiring an operating, financing, or discontinued operations category.

Recommendations

41. The project should not seek to determine whether a net income/profit and loss subtotal should be reported and, if so, the nature of the items that should be excluded from it. Financial statement presentation would not result in established principles that other projects would use in determining whether any recognized amounts should be reported outside of earnings (e.g., projects such as postretirement benefits and financial instruments.) We recognize the implication of this recommendation, that being the continued acceptance of an ad hoc approach to items reported outside of net income and differences in our approach to recycling. (See discussion of pensions below.)

42. The project scope should be returned to its original focus on presentation on the face of the financial statements and a limited number of disclosures directly related to presentation issues. Other issues such as improved segment/liquidity disclosures should be addressed in separate projects based on an evaluation of the relative need for improvement in those or other areas.

43. **Postretirement benefits.** The IASB recently has issued a discussion paper on phase 1 of its project focused on measuring cash balance plans, elimination of so-called smoothing devices, and income statement presentation of changes in plan assets and benefit obligations. The measurement issues for cash balance plans are challenging. The Group thinks resolution of those issues should be deferred, if necessary, to issue a final standard on other issues by 2011.

Recommendations

44. The IASB should continue its work on phase 1 of the project. If the issues surrounding cash balance plans prove to be as daunting following the discussion period as they were in the lead up to the discussion paper, then the IASB should consider dropping cash balance plans from the current project. Alternatively, the IASB may consider a definition that while less conceptually pure, leaves promises like those in career average plans untouched.

45. Phase 2 of this project should be suspended and staff resources allocated to MOU projects. The IASB should consider whether to restart work after phase 1 of its project is complete. The research work currently under way by the UK ASB and other national standard setters might be used to jump start progress on phase 2 once it commences.

46. The FASB continues to evaluate how changes in plan assets and benefit obligations would be presented under the proposed presentation principles developed in the financial statement presentation project. That work should continue and can assist the IASB in resolving the open questions of presentation in its discussion document.

47. **Leasing.** The serious deficiencies in existing standards make the leasing project a priority for many. Significant lessee obligations are excluded from corporate balance sheets, distorting financial ratios and complicating financial analysis for investors. Lessor accounting raises many derecognition and revenue recognition issues, but appears to be a relative lower priority for investors and some Board members.

48. There seems to be little dispute that the “right to use” is an asset of the lessee, but the Boards have yet to resolve the difficult issues of the accounting for options (rights to terminate or renew), contingent rent, and other conditional obligations. Nor have the Boards made decisions on the fundamental issue in lessor accounting—whether the lessor should derecognize a portion of the asset subject to lease or recognize a long-term performance obligation.

Recommendations

49. The Boards should improve lessee accounting by the mid-2011 goal. Lessor accounting is an application of revenue recognition and should be dealt with in a manner that reflects the decisions reached in that project. That likely means that improved standards for lessor

accounting would be completed after 2011. We accept as a consequence of this recommendation that there may be a lack of symmetry and a different unit of account between lessee and lessor accounting for some time. We weighed that consequence against the improvement in financial reporting that would come from recognizing lease obligations in lessee's financial statements.

50. In regards to lessee accounting, the Boards should pursue an approach that results in on-balance-sheet presentation of leases. In our view, an approach that views the substantive lease term as the unit of account offers significant promise. In effect, our recommendation would leave the classification of finance leases in IAS 17 unchanged. What were previously operating leases would then be reflected as the acquisition of an intangible asset—the right of use inherent in the lease.

51. We recommend that the Boards proceed without debating changes to amortization and depreciation accounting. We note that many in the leasing business are far more concerned with the pattern of recognized expense (straight line) than with the balance sheet presentation. This should come as no surprise to the IASB following the debate on service concession agreements or to the FASB following its recent meeting with the Equipment Leasing Finance Association.

52. The Boards should avoid reconsidering areas for which current lease accounting provides answers, even though those answers are imperfect. In particular we recommend that the Boards proceed using current definitions of what constitutes a lease and the treatment of contingent rentals.

53. The Group considered whether the Boards should publish the two G4+1 documents on lease accounting as the first stage of due process. We had serious reservations about whether a lease accounting project as currently described can be completed by 2011 if we must draft a new discussion document from scratch. However, we concluded that those documents will not provide a reasonable basis for comment if the Boards accept the idea that the substantive lease term is the unit of account. In our view, a limited project along the lines described above could be captured in a short discussion document without significantly imperilling our ability to make the 2011 deadline.

54. **Financial instruments.** The IASB has issued its discussion paper on complexity in the reporting of financial instruments. The FASB also has issued its comparable Invitation to

Comment. The multiple ways of measuring similar instruments is a source of complexity for many investors. Much of the existing complexity from a preparer perspective arises from existing hedge accounting requirements. The FASB has an active short-term project to address aspects of that complexity. While the discussion paper is open for comment, the IASB should hold education sessions on the FASB's proposed approach.

55. In any event, the changes that the Boards might make to financial instrument accounting could be limited to simplifying hedge accounting and perhaps implementing some of the simplifications in measurement classification described in the discussion paper (a.k.a. the Ron Lott approach). We recommend that the Boards consider carefully whether those steps would meet the sufficient improvement constraint discussed at the beginning of this memorandum. In our view, any changes in financial instrument accounting made between now and 2011 could well be embedded in the literature for 10 years or more. Given that, it might be better to do nothing rather than to continue with a suboptimal solution, albeit one that is perhaps simpler than the solutions we have today.

56. We considered whether the Boards should press ahead with full fair value for all financial instruments. In our view, there are no significant technical obstacles to doing so. The obstacles that exist lie in the area of presentation and the Boards' willingness to deal with the political outcry that would no doubt accompany such a move. We did not make this recommendation because we concluded that there is insufficient Board support for moving to a full fair value solution at this time.

57. In view of that conclusion, we have not identified any major changes to financial instrument accounting that would satisfy our constraint of significant improvements in financial reporting. There may be some changes that can be made, perhaps in hedge accounting or in measurement classification. Until we have received comments on the discussion document and seen the progress of the FASB's work on simplifying hedge accounting, we do not have a basis for making a recommendation in this area. As with derecognition, we recommend that the Boards defer a decision on this topic to the October joint Board meeting when this additional information is available.

58. **Liabilities and equity.** This project is a priority for some in the US because US GAAP is complex, difficult to apply, and needs almost constant maintenance. It may be less of an issue internationally.

Recommendations

59. This is a high-priority project; however, our ability to make progress will depend on whether we can come to an early decision from among the three models included in the discussion paper. We recommend that the IASB focus its efforts during the comment period on developing a view with regard to the following:

    a. Does the IASB support the narrow view of equity adopted by the FASB? While the IASB has had an education session on the topic, it is not deliberated the point.

    b. Can the inconsistency that some perceived between the narrow view of equity and the Framework definition of a liability be resolved? Jim Leisenring has a suggested revision to the liabilities definition that might overcome the inconsistency.

    c. Would a standard based on the narrow view of equity preserve the solution to puttable shares recently published by the IASB? Tom Linsmeier and Sue Bielstein indicate that the FASB's model espousing the narrow view of equity is not incompatible with the IASB conclusions. In addition, that model should be able to be tweaked to make this a non-issue.

60. Consistent with our view that we must come to a common conclusion from among the models, we recommend that the project team identify "lightning rod" instruments that are likely to prove difficult. The comment letters will make the population of those instruments obvious, and we should be able to begin Board discussions shortly before the analysis of comment letters is complete.

SHORT-TERM CONVERGENCE PROJECTS

61. **Earnings per share.** Like it or not, many investors think earnings per share is an important metric, and they would be better served if US GAAP and IFRS at least produced the same denominator in most cases (the goal of the short-term project). Moreover, the Boards' proposed changes would simplify the EPS computation in some cases. That said, some respondents to past FASB exposure drafts think the proposals do not go far enough in simplifying the existing standards and recommend that the Boards reconsider EPS more fundamentally. Such a project would be a natural fit with the

Boards' project on liabilities and equity. If that approach were taken, the Boards should consider whether narrow changes to converge EPS in the interim meet the sufficient improvement constraint described at the beginning of this paper.

62. We are of two views on this project. Some group members maintain that the work done to date would improve financial reporting. Other group members maintain that the computation of earnings per share necessarily will change as a result of the projects on liabilities and equity and financial statement presentation. Those members prefer deferring the work on earnings per share and including it in an exposure draft on liabilities and equity.

63. **Joint ventures.** The IASB should be able to complete this project if it stays true to the original objective of eliminating the option of using proportionate consolidation for joint ventures. The IASB should refrain from tinkering or reconsidering the equity method—that issue should be addressed either through the consolidations project or a financial instruments project.

64. **Taxes.** The Group supports continuing work on the income tax convergence project. The IASB made a commitment to its constituents to develop a principles-based replacement to the existing standard. The FASB may propose adopting the proposed IFRS as a demonstration of the move to a common, global, principles-based standard. Tom Linsmeier and Sue Bielstein observe that the issue of uncertain tax positions is of critical importance in the US context. The IASB always has been willing to address issues that are particularly important in certain jurisdictions, as was the case with puttable shares. While the IASB's upcoming exposure draft does not take the same approach on uncertain tax positions as did the FASB, it is nonetheless important to US adoption that IFRS address this issue.

65. **Other short-term convergence.** The MOU includes possible projects on impairment, a second stage of the fair value option, and research and development. The milestone required by the MOU was a decision about whether differences in those areas should be eliminated through one or more short-term standard-setting efforts. For two reasons, we recommend that the Boards not undertake those standard-setting efforts. First, we believe the Boards' resources would be better spent on the other improvement priorities identified earlier in this memo. Second, the plan assumes that the remaining major capital markets,

including the US, will be adopting IFRSs in the next five years or so. Adoption of IFRS seems to eliminate the need to converge narrow differences in specific standards.

A note on cross-cutting issues

66. Earlier in this paper we acknowledge the importance of cross-cutting issues and the way failure to resolve those issues can slow progress. We acknowledge that IASB members have expressed a desire to separately address a number of cross-cutting issues. This almost certainly reflects frustration over the lack of significant progress in the Conceptual Framework. However, we are reluctant to recommend that any significant resources be devoted to this exercise. We observe that no Board of which we are aware has been able to approach cross-cutting issues outside of the context of individual projects and develop answers that "stick."

67. In our view, achieving progress by 2011 means making some trade-offs, and one of those is the internal consistency of the resulting standard with other IFRS and the current and developing Framework. Internal inconsistencies are not new—they result from taking an incremental approach to improving standards in the absence of a robust Conceptual Framework. We realize our recommendations continue that practice. We are comfortable with that because we believe the results will be meaningful, although imperfect, improvements to financial reporting

68. The recommended approaches in this memorandum do require that the Boards resolve some questions that certainly qualify as cross-cutting issues. For example, we cannot resolve revenue recognition without a definition of a performance obligation (and thus a better definition of a liability). However, on balance, our recommendations minimize the impact of cross-cutting issues.

69. As we consider the staffing implications of our recommendations, it seems clear to us that directors and senior project managers are critical to our ability to complete our work by 2011. The IASB's current plan was to divert one or two senior project managers to work on cross-cutting issues. That no longer seems to us the best use of resources. While it may be possible to single out one or two cross-cutting issues, we ask that the IASB reconsider its earlier decision to devote significant resources to cross-cutting issues.