



C H U B B

## THE CHUBB CORPORATION

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Letter of Comment No: 158  
File Reference: EITF03-1A

Mr. Lawrence Smith  
Director, Technical Application and  
Implementation Activities  
Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, CT 06856-5116

RE: PROPOSED FASB STAFF POSITION NO. EITF  
ISSUE 03-1-a, IMPLEMENTATION GUIDANCE  
FOR THE APPLICATION OF PARAGRAPH 16  
OF EITF ISSUE NO. 03-1, "THE MEANING OF  
OTHER-THAN-TEMPORARY IMPAIRMENT AND  
ITS APPLICATION TO CERTAIN INVESTMENTS"

Dear Mr. Smith:

The Chubb Corporation (Chubb) is a holding company with subsidiaries principally engaged in the property and casualty insurance business. Chubb owned invested assets with a market value of \$30 billion as of September 30, 2004. Chubb's investment portfolio is primarily comprised of high quality debt securities, principally tax-exempt, U.S. Treasury and government agency bonds, mortgage-backed securities and corporate issues as well as foreign bonds. Approximately 98% of Chubb's debt securities are classified as available-for-sale.

We appreciate the opportunity to respond to Proposed FASB Staff Position (FSP) No. EITF Issue 03-1-a, which would provide guidance for the application of EITF Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments.

### Overview

We support the Board's efforts to clarify the meaning of other-than-temporary impairment. However, we have significant concerns about the impact of the guidance included in EITF Issue No. 03-1 and the Proposed FSP on the accounting for available-for-sale debt securities.

In particular, we strongly disagree with the guidance in paragraph 16 of EITF Issue No. 03-1 that would require that, for debt securities, an impairment should be deemed other-than-temporary if the investor does not have the ability and intent to hold the investment until a forecasted recovery of fair value up to the cost of the investment. We believe that this guidance is inconsistent with the Board's decisions related to the accounting for available-for-sale debt securities set forth in Statement of Financial Accounting Standards (SFAS) No. 115, Accounting for Certain Investments in Debt and Equity Securities. Further, we believe that implementation of this guidance would diminish the relevance of the income statement for analysts and other users of financial statements.

#### Definition of Other-Than-Temporary Impairment

We believe that the Board's intent when it issued SFAS No. 115 was that the accounting treatment for unrealized gains and unrealized losses on available-for-sale securities should be consistent. Paragraph 13 of SFAS No. 115 states that unrealized gains and losses for available-for-sale securities shall be excluded from earnings and reported in other comprehensive income until realized. As noted in paragraph 94 of SFAS No. 115, the Board recognized that reporting unrealized gains and losses on available-for-sale debt and equity securities outside earnings would alleviate the potential for volatility in reported earnings. Paragraph 94 goes on to state that the Board recognizes that volatility in earnings can still result from the sale of securities.

Further, the tone of SFAS No. 115 suggests to us a higher threshold for other-than-temporary impairment than that in paragraph 16 of EITF Issue No. 03-1. In paragraph 16 of SFAS No. 115, the Board uses phrases such as "an enterprise shall determine whether a decline in fair value below the amortized cost basis is other than temporary" and "if the decline in fair value is judged to be other than temporary..." Both of these phrases contemplate an evaluative process that relies on fact gathering and the exercise of sound judgment.

The Board decided not to provide comprehensive guidance on other-than-temporary impairment in SFAS No. 115 but did state in paragraph 114 that it believes that other-than-temporary impairment exists if it is probable that the investor will be unable to collect all amounts due according to the contractual terms of the security.

Subsequently, in EITF Topic No. D-44, Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value, the FASB staff indicated that when an entity has decided to sell a specifically identified available-for-sale security whose fair value is less than its cost basis, a writedown for other-than-temporary impairment should be recognized when the decision to sell is made. We believe this is the appropriate threshold for the recognition of an other-than-temporary impairment for an available-for-sale debt security whose fair value is less than its cost basis due to an increase in market interest rates. We recognize that EITF Topic No. D-44 noted that there were other circumstances that needed to be considered in determining when an other-than-temporary impairment exists, but they were not absolute indicators of other-than-temporary impairment.

EITF Issue No. 03-1 would add a second indicator that other-than-temporary impairment for debt securities exists -- the investor does not have the ability and intent to hold the security until a forecasted recovery of fair value up to the cost of the investment, which in certain cases may mean until maturity. The implication is that unrealized losses on available-for-sale debt securities should be excluded from earnings only if the investor represents that the security will not be sold. EITF Issue No. 03-1 would thus create a new investment category: available-for-sale securities that cannot be sold. This is illogical. By definition, an available-for-sale security is available for sale. Further, we do not believe the Board intended its decisions in SFAS No. 115 to be interpreted to mean that for available-for-sale debt securities an other-than-temporary impairment should be deemed to have occurred if the investor does not have the unconditional intent to hold the security until a forecasted recovery of fair value. We believe that the guidance in EITF Topic No. D-44 supports this view.

Therefore, we encourage the Board to eliminate the guidance in paragraph 16 of EITF Issue 03-1 that impairment of a debt security should be deemed other-than-temporary if the investor does not have the intent to hold the security until a forecasted recovery of fair value up to the cost of the investment.

If the Board does not eliminate this indicator of other-than-temporary impairment, we do not believe that the notion that "minor impairments" can be considered temporary would provide any substantive relief from the adverse consequences of applying EITF Issue No. 03-1 during periods of rising interest rates.

First, financial statement preparers and their auditors would have significant difficulties in determining whether or not an impairment is minor. Would unrealized depreciation of 4.9% be considered minor but not 5.1%? Would unrealized depreciation of 4.9% be considered minor for a debt security that matures in two years as well as for one that matures in twenty years?

Even if we were able to get past the issue of what is minor impairment, the guidance in the Proposed FSP would only defer the problem created by EITF Issue No. 03-1. While interest rates move upward and downward, they do not do so in any predictable pattern. Rates may move upward for several years, resulting eventually in the fair value of available-for-sale debt securities being less than their cost by an amount that would not be considered "minor."

#### Impact of EITF Issue No. 03-1 on Relevance of Financial Statements

We do not believe that the implementation of EITF Issue No. 03-1 would improve the relevance of the financial statements. In fact, we believe relevance would be diminished. Since available-for-sale securities are already carried at market value, there would be no change to comprehensive income or shareholders' equity. However, unless an entity represented that it would eliminate virtually all sales of available-for-sale securities at a loss, implementation of EITF Issue No. 03-1 would result in impairment charges in periods when interest rates rise offset by future enhanced investment income on a yield to maturity basis.

The performance of Chubb and most other insurance companies is evaluated based upon a non-GAAP financial measure referred to as "operating income," which is generally defined as net income excluding after-tax realized investment gains and losses. "Operating income" is a critical measure of performance in that it presents results of operations in a manner that allows for a better understanding of the underlying trends in an insurer's business. Operating income is the measure, among others, that investment analysts and investors use to estimate an insurer's earnings and to measure its performance.

The implementation of EITF Issue No. 03-1 would have the effect of increasing Chubb's operating income as any impairment charges would be included in realized investment losses while the future enhanced investment income would be included in operating income. Despite this "benefit", we believe that such accounting treatment would reduce the transparency of the income statement and therefore make it more difficult for analysts and other users of our financial statements to interpret our results. For example, if interest rates were to rise, we could report record operating income in a period based on the strong performance of our business but report a net loss due to a large impairment charge. Less sophisticated users of financial statements, in particular, would be confused by this result.

#### Recordkeeping Burden

The implementation of EITF Issue No. 03-1 would place a significant recordkeeping burden on Chubb. Like other insurance companies, Chubb is required to maintain books and records on a regulatory or statutory basis as well as on a GAAP basis. The cost of available-for-sale debt securities has generally been the same for statutory and for GAAP purposes.

The guidance in EITF Issue No. 03-1 would require that we adjust the cost value for available-for-sale debt securities for GAAP basis reporting when interest rates rise while maintaining the historic cost value for statutory basis reporting. Our investment accounting system is not structured to accommodate such a need. Therefore, the duplicate processing of all investment transactions would be required.

We have several thousand positions in the available-for-sale debt security portfolios of our insurance subsidiaries for which the cost value for GAAP basis reporting would be subject to change in periods of rising interest rates, perhaps in several consecutive quarters. This would be a daunting and time consuming obligation, the cost of which far exceeds any benefit derived from the implementation of EITF Issue No. 03-1.

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In conclusion, we believe that the guidance in EITF Issue No. 03-1 is inconsistent with the Board's decisions in SFAS No. 115 related to the accounting for available-for-sale debt securities and that implementation of this guidance would diminish the value of the income statement to analysts and other users of our financial statements.

We believe that for an available-for-sale debt security whose fair value is less than its cost basis due to an increase in market interest rates, impairment should not be considered other-than-temporary unless the investor has the positive intent to sell the security. Therefore, we strongly encourage the Board to eliminate the guidance in paragraph 16 of EITF Issue No. 03-1 that impairment of a debt security should be deemed other-than-temporary if the investor does not have the intent to hold the security until a forecasted recovery of fair value up to the cost of the investment.

We would be pleased to discuss our comments and recommendations with members of the Board or its staff.

Very truly yours,

Henry B. Schram  
Senior Vice President and  
Chief Accounting Officer