

Letter of Comment No: 177
File Reference: EITF03-1A

October 29, 2004

Mr. Lawrence W. Smith
Director-Technical Application & Implementation Activities-FSP
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-516

Re: Comments on Proposed FASB Staff Position EITF Issue 03-1

I am writing to the Board to express Peoples Bank's concern with Emerging Issues Task Force Issue 03-1, The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments. We are concerned about the potential negative impact EITF 03-1 will have on financial statements, bank earnings, asset/liability management and risk management strategies.

We are particularly concerned with the interpretation of impairment due to interest rate increases and the subsequent potential "tainting" of investments that can occur when selling securities at a loss that are categorized as Available-For-Sale (AFS).

People's Bank generally categorizes all of its debt securities as AFS, as defined by SFAS 115, Accounting for Investments in Certain Debt and Equity Securities. AFS securities provide a source of liquidity and interest income, and may be used to adjust the bank's interest rate risk position. This portfolio is typically used as part of People's asset/liability management strategy and may be sold in response to, or in anticipation of, factors such as changes in market conditions and interest rates, changes in security prepayment rates, liquidity considerations and regulatory capital requirements. Indeed, the ability to restructure the AFS portfolio at any time in the interest rate cycle is one of the primary tools used in bank asset/liability and risk management.

Under EITF 03-1, as interest rates increase above those existing at the time of purchase, the fair value will decline, thereby creating impairment. For any securities affected by increases in interest rates, the bank can still expect to receive the contractual cash flows and full return of principal and interest over the remaining life of the security, assuming no change in credit.

Based on our asset/liability and risk management business practices, the bank may decide to adjust its risk profile by selling AFS securities, some of which may be impaired due to increases in interest rates. Under such a scenario, it could be interpreted that the bank's intent is not to hold similar securities until recovery, thereby tainting the entire AFS portfolio. This tainting would then require the permanent write down of the securities through earnings. This interpretation is in direct conflict with SFAS 115 and would effectively change the accounting for the AFS portfolio to a "lower of cost or market" standard. We feel that EITF 03-1 improperly impedes the bank's ability to prudently manage its asset/liability and interest rate risk strategies.

Our recommendation is to exclude impairment due to interest rate changes. The recognition of impairment due to changes in interest rates will also result in inaccurate and misleading financial statements. To the extent that impairments are not credit-related and relate to assets that are not sold, any impairment losses recorded in one period will be reversed in subsequent periods as investment income. The effective yield of the impaired securities would have to be increased in order to accrete the carrying value of the securities to par by maturity. This unnecessary recycling of income reduces the integrity of any subsequent financial statements.

In addition, any interpretation guidance provided by the Board must be clear and concise for consistent application by financial institutions and public accounting firms.

Thank you for your time and consideration with respect to this matter. Please feel free to contact me at (203) 338-4114 or vince.calabrese@peoples.com with questions or if you need additional information.

Sincerely,

Vincent J. Calabrese
Senior Vice President and Controller
People's Bank