



**CITIZENS NATIONAL BANK**

201 West Main St.  
Henderson, Texas 75652

VIA E-MAIL

October 29, 2004

Letter of Comment No: 172  
File Reference: EITF03-1A

Mr. Robert Herz  
Chairman  
Financial Accounting Standards Board  
401 Merritt 7  
Norwalk, Connecticut 06856-5166

Mr. Lawrence Smith  
Chairman  
Emerging Issues Task Force  
Financial Accounting Standards Board  
401 Merritt 7  
Norwalk, Connecticut 06856-5166

RE: FSP EITF Issue 03-1-a, Implementation Guidance for the  
Application of Paragraph 16 of EITF Issue No. 03-1

I am writing to comment on your recently issued EITF Issue 03-1 "The Meaning of Other Than Temporary Impairment and its Application to Certain Investments" ("EITF 03-1"). I am the Vice President and Portfolio Manager of Citizens National Bank, NA in Henderson, Texas. We are a \$575 million community bank with 17 branches in north east Texas.

We are very apprehensive about the potential negative ramifications of EITF 03-01. Implementation as currently interpreted will certainly cause increased income and capital volatility, reduce or severely discourage sound long-term asset management and will impact financial institutions disproportionately based on individual investment asset concentrations. For example:

- Reported financial statements that do not accurately reflect the results of our business activities (earnings volatility, asset carrying values, capital levels, risk profile, etc.);
- As a result of the above, very real Sarbanes-Oxley related concerns associated with required signatures by senior Bank officers on financial statements that might be "technically correct" from an accounting perspective, yet materially misleading as to the true financial performance and risk profile of our Bank;

- The impact on a Bank with a loan to deposit (LTD) ratio of 40%, like our Bank, would be very different than on a Bank with a 90% LTD ratio. By accounting standards, the low LTD Bank would be considerably more “risky” than the higher LTD Bank.
- Ability to prudently manage risks, such as liquidity and interest rate sensitivity, at the enterprise level. Implementation will completely change how banks manage their investment portfolios, depriving them of the ability to use this component of their balance sheet to manage their asset/liability and liquidity positions. It would force Banks to make investment decisions based on accounting treatment, but not necessarily in the best interest of the Bank as a going concern;
- Intent to hold is not the proper approach for determining when to book an interest rate related impairment (an intent to sell is the established practice under FAS 115).
- Available for sale securities should be exactly that, “available” at the investor’s option to be sold;
- A systemic lowering of banking industry earnings;
- Inappropriately reduced regulatory capital levels that constrains the banking industry’s ability to support economic growth (especially for community Banks); and
- Decreased availability and/or higher cost of raising capital.

#### Recommendations:

Our recommendation is to clarify FAS115 by excluding other than temporary impairment accounting from situations where there have been market value declines due solely to interest rate related changes; unless an entity’s actions speak clearly to exception treatment. For example, in situations where there is a definitive plan for sale (voluntary or otherwise), Banks should record a charge at the time of determination of the plan and not wait for the transaction to occur. Similarly, if there was an “egregious” pattern of selling that would seem to indicate that a portion or all of a portfolio was misclassified as available for sale rather than trading.

If FASB moves forward with EITF 03-1, then at the very least it should address clearly with pertinent examples the following issues:

- Enable sales to be conducted for documented strategies related to prudent risk management such as interest rate sensitivity and liquidity management.
- Provide a “bright-line” test for minor impairment (at least 5%, and preferably more) whereby impairment would be assumed to be temporary without requiring further analysis and documentation. Requiring formal analysis and documentation for every security with an unrealized loss would be an extreme burden.
- For pre-payable/callable premium securities with book prices above the “bright-line” test, provide concrete examples of typical securities and how they would be accounted for under the “new rule”. For example, premium mortgage-backed securities (MBS) and collateralized mortgage obligations (CMO), callable bonds priced at premiums and amortized to call date, long-term municipal bonds, premium commercial MBS and other types of premium bonds with yield maintenance agreements and/or prepayment penalties.

- Allow rate related impairments to be recovered up to amortized cost as is done for mortgage servicing rights. Why create a new “permanent” cost basis that implies a low probability of recovery for a financial instrument whose value changes daily and is expected to increase with business cycles (when rates decline) and/or as time passes (the security moves closer to maturity)?
- Provide tangible guidance on what constitutes a pattern of selling (e.g. relative level of sales either in # of transactions or \$ volume; time period over which activity is analyzed, etc.) Interpretations from the accounting profession have varied greatly.
- We believe interest rate related market price changes should be excluded from the recognition aspect of 03-1 because this would be a total departure from current industry practice with respect to SFAS 115. If interest rate related price changes are not excluded from the recognition aspect of 03-1, we believe the current wording of 03-1, without additional guidance and a specific “bright line” loss threshold, will result in a significant burden to depository institutions, uneven application of the rule and will cause accounting firms to overly focus on “normal” interest rate related losses.
- By adopting the changes proposed above, we believe the broad goal of 03-1 can be achieved while limiting the application burden and providing a more even and consistent application.

Thank you for considering our comments regarding the very critical issues associated with EITF 03-1 and the related ramifications for our Bank and for the banking industry as a whole.

Sincerely,

Marjorie J. Wagner, CPA  
Vice President and Portfolio Manager  
Citizens National Bank, NA  
201 W. Main St.  
Henderson, TX 75654

Phone: 903-657-8521  
Fax: 903-657-9224  
Email: [mwagner@cnbtxas.com](mailto:mwagner@cnbtxas.com)