

October 29, 2004

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

Re: September 2004 Proposed FASB Staff Position (FSP), *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:

One of the objectives that the Council of the American Institute of Certified Public Accountants (AICPA) established for the PCPS Executive Committee is to act as an advocate for all local and regional firms and represent those firms' interests on professional issues, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective. These comments, however, do not necessarily reflect the positions of the AICPA.

TIC has reviewed the Proposed FSP and is providing the following comments for your consideration.

FASB FSP 03-1-a, Issue 1—Minor Impairments

Issue 1: The Board considered defining minor impairment as an impairment of 5 percent or less. Some Board members believe that minor impairments can be considered temporary without further analysis because normal interest rate and/or sector spread volatility is expected to eliminate a minor impairment. Some Board members disagree with defining minor impairment as an impairment of 5 percent or less because that definition embodies assumptions about the volatility of the applicable interest rate.

Others prefer that the guidance not provide a "bright-line" test. For these reasons, the Board generally supported the notion that minor impairments can be considered temporary and did not support including either additional guidance or a numerical threshold to be used in determining whether an impairment is minor. Do you believe that financial statement preparers and auditors will be able to apply the notion of "minor impairment" without any additional guidance from the FASB? If not, do you believe that the Board should specify a numerical rule or threshold and, if so, what would that rule or threshold be?

TIC does not support a 5% "bright line" test for evaluating minor impairments, consistent with the views of certain FASB members. Instead, TIC believes the evaluation of minor impairments should be a subjective determination left to practitioner/preparer judgment without further guidance from the FASB. The establishment of a bright line based on a 5% impairment threshold would produce arbitrary write-downs above the threshold and

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no write-downs below the threshold. Artificial thresholds eliminate the necessary consideration of the nature of the investment, industry variables, the market conditions as of a given time, and other possible pertinent factors. TIC is concerned that such hard-and-fast rules would lead to inappropriate conclusions in some cases. TIC also believes that the disclosure requirements in EITF Issue 03-1, paragraph 21, will clarify the investor's rationale and assist the financial statement user in understanding why certain significant unrealized losses were not considered to be other-than-temporary impairments.

TIC also believes impairment should be evaluated on a security-by-security basis; TIC's client base usually does not "pool" such investments.

FASB FSP 03-1-a, Issue 2—Limiting the Notion of Minor Impairments to Debt Securities Evaluated for Impairment Pursuant to Paragraph 16 of Issue 03-1

Issue 2: The Board generally believes that it is appropriate to limit the notion of "minor impairments" that would not create the need for an ability and intent assertion to debt securities analyzed for impairment under paragraph 16 that are impaired because of interest rate and/or sector spread increases, since, absent a sale prior to recovery or maturity, such impairments will be recovered. Because the same cannot be said for debt securities that can be contractually prepaid or otherwise settled in such a way that the investor would not recover substantially all of its cost and equity securities, the Board generally does not support extending the exclusion to investments analyzed for impairment under paragraphs 10–15 of Issue 03-1. However, some Board members support expanding the notion of "minor impairments" to all investments analyzed under Issue 03-1 because they acknowledge that normal price volatility may eliminate an impairment. Do you support the Board's conclusion to limit the notion of "minor impairments" to debt securities analyzed for impairment under paragraph 16 that are impaired because of interest rate and/or sector spread increases? If not, why?

TIC concurs with the minority Board view that would support expanding the notion of "minor impairments" to all investments analyzed under EITF Issue 03-1. TIC believes most minor impairments in equity securities covered by EITF Issue 03-1 may be attributed to the typical reasons for the normal fluctuations that occur in the fair value of any investment over time. Although the notion of minor impairment is always subjective, it should include a cost/benefit element—i.e., the point at which the impairment is too small to justify the effort involved in estimating and disclosing the projected outcome of future events. The cost of accounting for minor impairments becomes more onerous when an entity has a mixed pool of numerous investments (especially since EITF Issue 03-1 requires the other-than-temporary disclosure for all investments in an unrealized loss position for which other-than-temporary impairments have not been recognized, including marketable equity securities [per example on pages 1506K-1506L of FASB *EITF Abstracts*]).

TIC appreciates the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

October 29, 2004
Mr. Lawrence Smith, CPA

Sincerely,

Stephen M. McEachern, Chair
PCPS Technical Issues Committee

cc: PCPS Executive and Technical Issues Committees