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LETTER OF COMMENT NO.

December 23, 2008

Technical Director Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116

## Proposed FSP EITF 99-20a

## Dear Director:

This letter is in response to the proposed FSP, "Amendments to the Impairment and Interest Income Measurement Guidance of EITF Issue No. 99-20." While I have no objection to the revision to EITF 99-20, I believe the proposal fails to deal with the much larger and important issue of how other than temporary impairment (OTTI) is being applied in practice to debt securities, particularly mortgage backed securities. Given that the Board has agreed to issue the guidance on 99-20, I urge you to use the very limited window of opportunity in the next few weeks to deal with OTTI more broadly.

As noted in the proposed FSP dealing with EITF 99-20, the issue of OTTI for debt securities originated in Statement 115 dealing with marketable securities. Given the deferral of recognizing losses in current income when applying either the available-for-sale or held-to-maturity models for certain debt securities, the Board decided that losses should be recognized in current income when it was probable all amounts due wouldn't be collected. That provision was included at least in part as a compromise between those Board members who would have preferred that all marketable securities be marked

to market through income and other Board members who supported the AFS and HTM models. Without such provision, it is quite possible that the Board would not have had enough votes to issue the final Statement.

However, in spite of including the OTTI provision in Statement 115, the Board explicitly decided not to provide guidance on how to apply the OTTI approach in practice. As current Board members well know, this has resulted in major issues in practice since the issuance of Statement 115, and there have been several efforts to provide guidance on how to identify and measure OTTI. The SEC and EITF have each issued documents that provide factors that should be considered but the final determination of whether a security is other than temporarily impaired often remains a judgment call by companies and their auditors.

In today's somewhat dysfunctional markets for debt securities, auditors are naturally cautious about how OTTI should be applied and probably lean toward impairment write downs when there is a close call. I am aware of one situation where a company's projections of future cash flows from mortgage backed securities fell well less than 1% short of full collection of principal and interest based on models that showed questions about full collection of underlying mortgage loans many years in the future. In this case, the accounting firm insisted that OTTI had occurred and required a write down through earnings of over 40% of the carrying amount of the security based on very limited market information. Recognizing what seems to be a major liquidity discount in current income doesn't seem to represent a true measure of the event that triggered the OTTI.

I am aware that bankers, accounting firms, and others have written to the Board previously to bring this issue to your attention and urge clarification of OTTI guidance so that credit losses associated with asset backed securities are recognized in current income but liquidity discounts are not. And, as noted by SEC Chairman Cox in his remarks at the recent AICPA conference about the SEC's study of market value accounting, "The work we have already done suggests that the accounting standard setters could improve upon the existing security impairment models. Investors have also clearly indicated a view that the current concept of mark-to-market accounting increases the transparency of financial information provided to investors — but that in inactive or illiquid markets, additional guidance would be useful to promote reasonable application of the standards."

It isn't clear to me why the Board would elect to deal with the 99-20 issue and not with OTTI more broadly. While the 99-20 issue may be a critical issue for some entities for this year end, the broader OTTI matter is as well. Thus, I believe the Board should quickly expand the scope of this project as others have suggested. If it isn't feasible to issue guidance on the expanded OTTI matter on such a short timetable, the Board should nevertheless take this project on and deal with it expeditiously.

Sincerely,

Dennis R. Beresford Ernst & Young Executive Professor of Accounting