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LETTER OF COMMENT NO.

334

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

**File Reference: Proposed FSP's FAS 157-e and FAS 115-a, FAS 124-a,  
and EITF 99-20-b**

Dear Mr. Golden:

BDO Seidman, LLP is pleased to offer comments on the proposed FASB Staff Position Nos. FAS 115-a, FAS 124-a, and EITF 99-20-b, "Recognition and Presentation of Other-Than-Temporary Impairments" ("FSP FAS 115-a") and FAS 157-e, "Determining Whether a Market is Not Active and a Transaction is Not Distressed" ("FSP FAS 157-e", collectively, the "proposed FSPs"). We believe that the Board should not issue proposed FSP FAS 157-e and should issue FSP FAS 115-a with changes. Before delving into the technical issues in the proposed FSPs, we would like to note some procedural and regulatory concerns.

An independent standard setting mechanism with robust due process is essential to the public's confidence in the reliability of financial reporting. We are concerned that the abbreviated comment period and accelerated timetable for issuing the final FSPs might give the impression of diluting the due process that should be applied to issuance of such important pronouncements. In addition, to the extent concerns about losses recorded as a result of fair value measurements and other-than-temporary impairments (OTTI) reflect concerns about the adequacy of regulatory capital for banks or insurance companies, those concerns are more appropriately addressed directly by the



regulators through changes to the calculation of how such amounts are determined, not by changing GAAP.

#### FAS 157-e

Under the proposal, a reporting entity presumes that a quoted price in an inactive market is associated with a distressed transaction unless the reporting entity has evidence that: (a) there was sufficient time before the measurement date to allow for usual and customary marketing activities for the asset, and (b) there were multiple bidders for the asset.

Reporting entities rarely will have any information about the marketing activities or number of buyers for observed transactions and, in those cases, they are likely to presume that substantially all transactions in inactive markets are distressed transactions. We believe the presumption is unlikely to reflect the economic substance most of the time. Furthermore, with this presumption, entities will have little incentive to seek information that may be publicly available with a little investigating. We also note that some securities have always traded in inactive markets and likely will continue to do so, even after the credit crisis is resolved. The Board's proposal effectively would result in a presumption that every transaction for these kinds of securities is a distressed transaction. As a result, we do not think the Board should issue this document as proposed.

We believe that the factors that indicate an inactive market and the two conditions that define a distressed transaction are useful additions to the accounting literature. In addition, to the extent that the Board believes that FSP FAS 157-3 has been applied inappropriately and requires clarification, we would support clarifying language. We think these objectives could be achieved without issuing a new FSP. If the Board decides to proceed with a new FSP, we would support the inclusion of the guidance about inactive markets and distressed transactions, but not the aforementioned presumption in the proposal.

*The Board raises the following five questions for constituents:*



1. *Is the proposed effective date operational?* We think it is not. We think relatively few reporting entities are capable of implementing the sort of valuation models that the FSP requires for first quarter reporting.
2. *Will this proposed FSP meet the objective of improving financial reporting?* No, for the reason cited above.
3. *Is the two-step model understandable and operational?* Yes, it is understandable and operational, but it does not reflect economic substance most of the time. The alternative is to clarify and provide application guidance for the factors that identify an inactive market and a distressed transaction, and allow reporting entities to weigh all of the evidence in deciding whether a transaction in an inactive market is distressed, rather than creating a presumption.
4. *Are the factors in paragraph 11 indicating an inactive market appropriate?* Yes.
5. *What costs would auditors expect to incur if the FSP is issued in its current form?* We believe our costs of conducting an audit would generally increase, because the inputs to the valuation models would be entirely subjective when the observed transactions are presumed to be distressed sales. This, in turn, would require engagement teams to spend additional time determining the reasonableness of management's assumptions where those assumptions are not based on observable data and may require expanded use of valuation experts.

FAS 115-a, 124-a, and EITF 99-20-b

1. *New triggers.* Whenever the fair value of a security is less than its cost basis at the measurement date, an entity assesses the impaired security to determine if the impairment is other than temporary. Currently, an impairment is considered temporary if, among other things, the reporting entity has the intent and ability to hold the security for a period of time that is sufficient for an anticipated recovery in fair value. The proposed FSP would change those triggers. Under the proposed FSP, an impairment would be considered temporary if, among other things, the reporting entity does not intend to sell the security and it is more likely than not that it will not sell the security before a recovery in fair value.



The proposed new triggers for an other-than-temporary impairment are less operational than the current requirement. Under the current requirement, if an entity, contrary to its representation as to ability and intent to hold a security until recovery in fair value, subsequently sells the security, it should be able to point to an objective change in facts. In contrast, under the proposal, it may be easier for management to make the initial assertion that the entity does not intend to sell and it is not more likely than not that it will sell, but there is no framework for determining whether a subsequent decision to sell is based on an objective change in facts or whether the original assertion was incorrect. We believe these new triggers would make it easier for an entity to avoid an OTTI charge. Therefore, we believe the Board should not change the triggers.

2. *New presentation.* Under the proposed FSP, if an entity holds a depreciated debt security (1) that it does not intend to sell, (2) for which it is not more likely than not that the entity will sell before recovery in fair value, and (3) for which it is probable that the entity won't collect all contractual cash flows, then an OTTI exists. However, in contrast to current requirements, only the portion of the impairment related to credit losses would be recognized in earnings, while the remaining portion would be recognized in other comprehensive income.

We support this change in presentation for debt securities classified as available for sale. However, we do not support the proposal for debt securities classified as held to maturity. For held-to-maturity securities, we believe that only the incurred credit loss should be recorded. In that regard, the held-to-maturity security should not be written down to fair value, because the entity doesn't expect to ever realize that portion of the impairment. A key part of the rationale for classification as held to maturity is that, because the holder does not intend (or need) to sell the security before maturity, the effects of changes in cash flows are relevant but changes in fair value are not. Our proposal would significantly narrow the differences in accounting for held-to-maturity debt securities and loans held for investment, which is one of the declared objectives of this project. In addition, our proposal would



eliminate the complex and, in our view, meaningless, amortization of the impairment loss carried in accumulated OCI.

In addition, we suggest clarifying that incurred credit losses should be computed in accordance with the guidance in FASB Statements No. 5 and 114. The proposal allows a variety of approaches to computing the credit loss portion of an OTTI. The flexibility inherent in the proposal will not significantly narrow the difference between the treatments of debt securities versus loans held for investment.

We suggest that the Board include in the final FSP all applicable impairment guidance, including Staff Accounting Bulletin No. 59, so that preparers and auditors will have access to all relevant impairment guidance in a single pronouncement.

We also believe that the Board needs to provide transition guidance for securities that were deemed to have an OTTI in 2008 or prior. For example, guidance should be provided regarding the accounting for those securities where further OTTI is experienced after the effective date of the new FSP.

The Board raises the following five questions for constituents:

1. *Does the separate presentation of credit losses and other market value changes provide decision-useful information?* Yes, for available-for sale securities, if the Board adopts the change we suggest to measure credit losses using the incurred loss model, because it would provide greater comparability between loans and debt securities. No, for held-to-maturity securities, for the reasons stated above.
2. *Is the guidance on credit losses clear and operational?* Not as proposed. We think the proposal is unclear about how to measure the credit loss component. If issued in this way in final form, it will lead to more diversity in practice, not less. As noted above, we believe the Board needs to specify that credit losses represent incurred losses measured using Statements 5 and 114.



3. *Are the new triggers to avoid considering an impairment other than temporary more operational than the current triggers?* We think the proposed triggers are less operational for the reasons cited above.
4. *Do you agree with the requirement to amortize the OCI portion of an impairment on held-to-maturity securities?* No. For the reason cited above, we believe that the OCI component should not be recorded for held-to-maturity securities.
5. *Is the proposed effective date operational?* Yes, we believe it is.

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We would be pleased to discuss our comments with the FASB staff. Please direct questions to Ben Neuhausen at 312-616-4661.

Very truly yours,  
BDO Seidman, LLP