

October 21, 2004

Letter of Comment No: 34 File Reference: EITF03-1A

Mr. Robert Herz, Chairman Financial Accounting Standards Board 401 Merritt 7 Norwalk, CT 06956-5116

Mr. Lawrence W. Smith Chairman of the Emerging Issues Task Force Financial Accounting Standards Board 401 Merritt 7 Norwalk, CT 06956-5116

Dear Sirs:

I am writing on behalf of Fidelity Bancorp, Inc. and its subsidiary, Fidelity Bank, a publicly held community bank with approximately \$625 million in assets serving the greater Pittsburgh area for over 75 years. The purpose of this letter is to express our concern with the proposed interpretation and application of EITF 03-1 "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments".

The Bank holds a fixed income investment portfolio of approximately \$250 million, 100% of which is investment grade quality. It utilizes this investment portfolio as a source of liquidity, as a means to help manage its interest rate risk position and to supplement lending activities. The Bank does not trade securities but classifies them as available-for-sale or held-to-maturity. The guidance contained in EITF 03-1, as proposed, would fundamentally change the way our portfolio is managed.

Currently, approximately 62% of the fixed income securities held are classified as available-for-sale. We may sell some of those securities from time to time, some at below cost and some at gains, to meet unanticipated liquidity needs or to react to a necessitated change in our asset/liability strategy resulting from a change in our interest rate risk position. The selection of securities to sell at such times encompasses a variety of factors including, among other things, current spreads, maturity date of the security and, in some cases, credit rating. A decision to sell a security is made based on the best information available at the time and has no bearing on the other securities remaining in the portfolio. We have had many securities classified as available-for-sale, which we have held until maturity and we intend to continue to do so.



Should a strict "other-than-temporary impairment" standard be finalized, I would anticipate that our investing activity in fixed income securities would have to be reevaluated and could be changed in at least the following ways.

- 1. It is possible that we would classify a greater percentage of securities purchased as held-to-maturity to avoid the impairment problem. From a financial statement users standpoint, this would seem to provide less transparent reporting since the unrealized gain/loss on those securities would now no longer be reported as a component of equity.
- 2. We could change the type of securities that are classified as available-for-sale. Securities with shorter maturity dates and less price volatility would be classified as available-for-sale, while those with more price volatility and longer terms would be classified as held-to-maturity. From an overall portfolio standpoint, this could be done without changing the desired average life or duration benchmarks, while again minimizing our need to deal with the impairment issue.
- 3. We could buy shorter-term bonds to minimize price volatility. Our desired interest rate risk position could be managed by retaining longer-term loans in the portfolio, thereby achieving the same result at a give up of some liquidity.

We believe that, as a practical matter, declines in value resulting from non-credit related factors such as the recent rise in interest rates, are adequately addressed in the current accounting literature. Analysts and users understand where to find the needed information in the balance sheet and the footnotes. I am not aware of any problems that have resulted from the application of current standards to fixed income investments that would necessitate any change in the standards.

Additionally, interest rates are unpredictable and, as you know, go in cycles. It is unreasonable to expect that no bond would ever be valued at below cost for an extended period of time. At the same time, it is equally unreasonable to expect that at some point its value will not be recovered, absent a change in credit rating. Thus, for non-amortizing bonds, the ability to recover the full investment is present. Even for amortizing securities where a change in interest rates can lead to a change in prepayment speeds, yields are adjusted prospectively to reflect the new expected life of the bonds.

In addition to the above points, there is a serious practical matter of implementation that concerns us. The effort required to document what is or is not impaired, the reasonableness of trying to ascertain a forecasted recovery date, and the ongoing work required to change yields on impaired securities going forward seems to outweigh any perceived benefits. Also, in the absence of a "bright line" test (which at minimum should be at least 10% to avoid having to deal with very normal fluctuations), it would appear that comparability among companies would suffer, since the determination of what is or is not other than temporarily impaired would be left up to the judgment of individual companies, their auditors and perhaps the sophistication of their systems.



As a relatively small company of approximately 155 employees, we are faced with the same increasingly complex array of accounting standards as companies many times our size, yet without their resources to address issues such as proposed here. The additional costs necessary to develop and maintain the systems necessary to account for what is proposed and the additional costs that will be incurred to pay independent accountants to audit the results would be an unnecessary burden to a company our size. We believe EITF 03-1 as proposed is ill conceived and would recommend it be withdrawn.

Respectfully,

Richard G. Spencer

President and Chief Executive Officer