



LETTER OF COMMENT NO. 89

To: Joe Vernuccio

Subject: Fwd: Proposed FSP FAS 115-a, FAS 124-a & EITF 99-20-b

I do not know why my responses to items 4 and 5 were cut off on the e-mail you sent back to me. See the complete response below. Please call at 570-724-8533 if there is still information missing. Thanks!

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>>> Mark Hughes 3/27/2009 1:01 PM >>>

March 27, 2009

Re: FSP FAS 115-a, FAS 124-a, and EITF 99-20-b

Dear Chairman Herz:

I am the Chief Financial Officer for Citizens & Northern Corporation, a relatively small banking corporation. The views expressed below are mine and not necessarily those of my employer.

My thoughts on the specific questions raised by the Board are as follows:

1. Separate presentation of credit-related losses (as a component of earnings) from the unrealized, noncredit component of impairment provides useful information. Recognition of credit-related losses as a charge against earnings is consistent with accountants' and investors' long-standing, traditional view of the elements to be included in determining earnings. On the other hand, I am opposed to inclusion in the calculation of earnings of market price adjustments, driven by changes in interest rates, changes in market spreads based on liquidity premiums and other noncredit-related factors. I believe inclusion of these types of noncredit-related adjustments in determining earnings adds inappropriate volatility to measurement of earnings, and detracts from the usefulness of financial statements.
2. The guidance related to measuring the credit component of other-than-temporary impairment (OTTI) of a debt security is clear and operational. I believe separate presentation of credit-related losses (as a component of earnings) from the unrealized,

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noncredit component of impairment is a good idea. I agree with the approach suggested in this FSP that the noncredit-related component of impairment should be realized in earnings only when the entity has either: (a) the intent to sell the security, or (b) based on facts and circumstances, it is more likely than not the entity will have to sell the security before recovery.

3. The modifications to existing guidance regarding management's assertions necessary to avoid OTTI treatment may be slightly more operational than existing guidelines, but not much. I believe clarification is necessary regarding equity securities, and I cannot determine whether the modifications will result in a significant change to the assessment of whether an equity security is OTTI. The FSP sends mixed messages as it relates to evaluating equity securities for OTTI. The requirement in paragraph 12 that, in order for an equity security to be considered OTTI, the entity must intend to sell it at a loss or it must be more likely than not that a loss will be realized, is consistent with my view of the OTTI issue – that equity markets are cyclical, and the determination of whether it is "more likely than not" a loss will be realized should be evaluated taking into consideration the investing entity's circumstances, as well as the circumstances of the issuer of the security. Paragraph 12 could be interpreted to indicate that, depending on an investing entity's liquidity, capital position and other factors, as well as the issuer's financial condition, it may be appropriate to hold a security in an unrealized loss position for an extended period of time, perhaps as long as several years, without recording an OTTI loss. Paragraph 7, on the other hand, states, "...entities will still need to consider the severity and duration of the impairment and the financial condition and near-term prospects of the issuer." In today's market, many stock values have fallen 50% or more from their cost bases established in purchases made in 2007 or earlier years. In evaluating for OTTI, I agree that it makes sense to consider the financial condition of the issuer, to evaluate whether it appears the issuer is a going concern with a likely opportunity to continue to operate for the foreseeable future. However, some auditors (perhaps in response to written and verbal comments from SEC staff) interpret the "severity and duration" conditions more arbitrarily – for example, if the market price has fallen below cost by 30% or more, and has been in an unrealized loss position for a year or more, they believe OTTI exists unless management can "prove" the stock price will increase to a level eliminating the unrealized loss. It is, of course, impossible to prove the future direction or amount of a stock price.
4. I do not agree with the requirement for amortizing impairment of held-to-maturity securities through other comprehensive income. In fact, I do not agree that, upon recognition of OTTI, it makes sense to adjust the carrying value of held-to-maturity securities to fair value. I think it makes more sense, in the case of held-to-maturity securities, to record OTTI through earnings, based on the same principles used for available-for-sale securities, with ongoing disclosures thereafter of fair value and (the revised) cost basis.
5. The proposed effective date is operational.

Thank you for your consideration.

Mark A. Hughes

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