Off-Balance Sheet Financing

On an ongoing basis, our Nordstrom VISA receivables are sold to a master note trust, which has issued $200 million in term notes backed by those VISA receivables. We recognize gains or losses on the sale of the VISA receivables to the trust based on the difference between the face value of the receivables sold and the fair value of the assets created during the securitization process. The fair value of the assets is calculated as the present value of their expected cash flows. The discount rates used to calculate present value represent the volatility and risk of the assets. Significant assumptions and judgments are made to estimate the present value of expected cash flows and to determine the fair value of our retained interest. We have no other off-balance sheet transactions. For additional information see Note 9: Off-balance sheet financing.

Valuation of Long-Lived Assets

We review our intangibles and other long-lived assets annually for impairment or when events or changes in circumstances indicate the carrying value of these assets may not be recoverable. We estimate the fair value of an asset based on the future cash flows the asset is expected to generate. An impairment loss is recognized when the carrying value of the asset exceeds its fair value. Factors used in the valuation of long-lived assets include, but are not limited to, management's plans for future operations, recent operating results and projected cash flows.

Realization of Deferred Tax Assets

In January 2002, we sold our Denver Credit facility generating a capital gain for tax purposes of $15.5 million, which was used to offset a portion of our existing capital loss carryforwards. Capital loss carryforwards of $16.1 million remain available to offset capital gain income in the next two years. No valuation allowance reserve has been provided because we believe it is probable that the full benefit of these carryforwards will be realized.

Our 2002 purchase of the outstanding shares of Nordstrom.com, Inc. series C preferred stock resulted in an expense of $40.4 million which we believe will not be deductible for tax purposes. As a result, we have established a valuation allowance reserve of $15.8 million to offset the deferred tax asset related to this purchase.

Recent Accounting Pronouncements

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." SFAS No. 149 amends SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" for certain decisions made by the FASB as part of the Derivatives Implementation Group process. SFAS No. 149 also amends SFAS No. 133 to incorporate clarifications of the definition of a derivative. SFAS No. 149 is effective for contracts entered into or modified after June 30, 2003, and should be applied prospectively. The adoption of this statement did not have a material impact on our financial statements.

In January 2003, the FASB issued Interpretation No. 46 (Revised 2003) or FIN 46, "Consolidation of Variable Interest Entities," which requires the consolidation of variable interest entities (VIEs). An entity is considered to be a VIE when its equity investors lack controlling financial interest or the entity has insufficient capital to finance its activities without additional subordinated financial support. Consolidation of a VIE by an investor is required when it is determined that the majority of the entity's expected losses or residual returns will be absorbed by that investor. FIN 46 is effective for variable interest entities created or acquired after January 31, 2003. For variable interest entities created before February 1, 2003, FIN 46 must be applied for the first interim or annual period ending after December 15, 2003. The adoption of FIN 46 did not have an impact on our financial statements.

During November 2003, the EITF reached a consensus on Issue 03-10, "Application of Issue No. 02-16 by Resellers to Sales Incentives Offered to Consumers by Manufacturers." EITF 03-10 addresses the accounting and disclosure treatment for a retailer's reimbursement receipt from a vendor for coupons offered directly to consumers by the vendor. EITF 03-10 is effective for coupons distributed to consumers for fiscal years beginning after December 15, 2003. We do not believe the adoption of EITF 03-10 will have an impact on our financial statements.