

August 31, 2009

Technical Director  
International Accounting Standards Board  
30 Cannon Street, 1<sup>st</sup> Floor  
London, EC4M 6XH  
United Kingdom

Dear Technical Director:

**Re: Discussion Paper – Credit Risk in Liability Measurement**

The Committee on Corporate Reporting (CCR) of the Financial Executive International Canada (FEI Canada) is writing to provide its response to the International Accounting Standards Board (IASB) Discussion Paper “Credit Risk in Liability Measurement”.

FEI Canada is the all-industry professional membership association for senior financial executives. With eleven chapters across Canada and more than 2,000 members, FEI Canada provides professional development, thought leadership and advocacy services to its members. The association membership, which consists of Chief Financial Officers, Audit Committee Directors and senior executives in the Finance, Controller, Treasury and Taxation functions, represents a significant number of Canada’s leading and most influential corporations.

The Committee on Corporate Reporting (CCR) is one of two national advocacy committees of FEI Canada. CCR comprises more than 20 senior financial executives representing a broad cross section of the FEI Canada membership and of the Canadian economy who have volunteered their time, experience and knowledge to consider and recommend action on a range of issues related to accounting, corporate reporting and disclosure. In addition to advocacy, CCR is devoted to improving the awareness and educational implications of the issues it addresses, and is focused on continually improving the standards and regulations impacting corporate reporting.

**We believe this discussion paper raises some fundamental questions about how a liability should be measured and believe the IASB should look to develop a formal approach to measure liabilities.** In particular there are different models in IAS 17, 37 and the new financial instrument proposals. Guidance on the measurement of liabilities would provide some necessary guidance to assist users in narrowing down the ranges of alternatives to be considered when they are reviewing specific issues such as the ones raised in this discussion paper.

In response to the specific questions in the Discussion Paper we have the following comments:

**Question 1 – When a liability is first recognised, should its measurement (a) always, (b) sometimes or (c) never incorporate the price of credit risk inherent in the liability? Why?**

When a liability arises through a third party transaction, typically the issuance of debt for cash, own credit risk will be reflected in terms associated with the debt including the interest rate, security and related covenants. The liability itself should be measured at the exchange amount.

To record a cash transaction at anything other than the exchange amount at initial recognition would be counter intuitive and not useful to users of the financial statements.

When a liability does not arise from a separate third party transaction, such as asset retirement obligations and warranties, own credit risk should not be incorporated in the measurement of the liability. This would provide for a consistent measurement basis of these types of liabilities from one entity to another.

Including own credit in the initial measurement of non-financial liabilities favors weak companies as they will show lower liabilities than strong companies and including own credit risk in the initial measurement of a non-financial liability is inconsistent with the going concern assumption since it assumes some likelihood of default (not going concern).

**Question 2 Should current measurements following initial recognition (a) always, (b) sometimes or (c) never incorporate the price of credit risk inherent in the liability? Why? If the answer is ‘sometimes’, in what cases should subsequent current measurements exclude the price of the credit risk inherent in the liability?**

Current measurements following initial recognition should not include changes in credit risk for most liabilities. Assuming loans are to be held to maturity, recording a change in the recorded value would be inconsistent with Guidance provided in International Accounting Standard 39. For the majority of loans, it can be assumed that the loan will be held to maturity and therefore amortized cost is the most appropriate method to use. Recording a gain to income from a decline in creditworthiness would not provide relevant information and in fact would provide misleading information.

Liabilities that could be traded, (such as derivatives) are the exception and should be always incorporate the price of credit risk inherent in the liability.

**Question 3 How should the amount of a change in market interest rates attributable to the price of the credit risk inherent in the liability be determined?**

Given our response to Question 1, this would not be applicable when a liability arises through a third party transaction.

In addition, we believe this discussion paper raises some fundamental questions about how a liability should be measured and believe the IASB should look to develop a formal approach to measure liabilities.

We believe that measurement of credit risk requires further research as there are no well-established frameworks to do so. In particular, parsing risk between economic, industry and company specific factors can only result in estimates devoid of a common process. This would result in inconsistencies in the preparation of financial statements from one entity to another.

**Question 4 The paper describes three categories of approaches to liability measurement and credit standing. Which of the approaches do you prefer, and why? Are there other alternatives that have not been identified?**



We agree with the approach described in paragraph 62 (c) of the staff paper with the following exceptions which have been inserted and underlined in paragraph below:

“Measure borrowings and other liabilities that result from an exchange for cash at the amount of the cash proceeds. Measure liabilities that do not have a cash exchange at the present value of expected future cash flows, discounted at the risk-free rate of interest. Subsequent current measurements of liabilities that have an exchange of cash and are not held for trading should NOT incorporate changes in credit risk or interest rate and instead should be measured at amortized cost. Subsequent current measurements of liabilities that have an exchange of cash and are held for trading should incorporate changes in market interest rates, including changes arising from the entity’s credit quality. Subsequent current measurements that do not have a cash exchange should incorporate changes in market risk-free interest rates. This would have the effect for liabilities other than for trading of fixing the credit spread at the original amount and incorporating all changes in the risk-free rate, and for liabilities to held for trading of reflecting the entity’s current cost of credit.”

The Committee would like to thank the Board for the opportunity to provide a response to the Discussion Paper.

Yours very truly,

A handwritten signature in black ink, appearing to read "Victor Wells".

Victor Wells  
Chair  
Committee on Corporate Reporting  
FEI Canada

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