



6 July 2009

To: **Members of the Hong Kong Institute of CPAs**  
**All other interested parties**

**INVITATION TO COMMENT ON IASB DISCUSSION PAPER ON CREDIT RISK  
IN LIABILITY MEASUREMENT**

***Comments to be received by 10 August 2009***

The Hong Kong Institute of Certified Public Accountants' (Institute) Financial Reporting Standards Committee (FRSC) is seeking comments on the IASB Discussion Paper which has been posted on the Institute's website at:

[www.hkicpa.org.hk/professionaltechnical/accounting/exposedraft/content.php](http://www.hkicpa.org.hk/professionaltechnical/accounting/exposedraft/content.php)

Credit risk in liability measurement is often referred to as 'own credit risk'. Credit risk is one component of fair value and, as a result, changes in 'own credit risk' are recognised when an entity's debt is fair valued. Some see the outcome as counter-intuitive and recent developments in the financial markets have led to increased concerns about the gains that result from reductions in the fair value of an entity's liabilities.

The IASB has issued a discussion paper and an accompanying IASB staff paper that describes the most common arguments for and against including credit risk in measuring liabilities. The objective of the invitation to comment is to generate a focused discussion that will enhance the debate on this topic. The issue of "own credit risk" has relevance to a range of IASB projects, in particular in the accounting for financial instruments, insurance, fair value measurement and provisions, contingent liabilities and contingent assets.

--- The discussion paper also examines alternative approaches to liability measurement other than fair value. A summary of the approaches described in the Discussion Paper is set out in the Appendix.

In accordance with the Institute's Convergence Due Process, comments are invited from any interested party.

Comments should be supported by specific reasoning and should be submitted in written form.

To allow your comments on the IASB Discussion Paper to be considered, they are requested to be received by the Institute on or before **10 August 2009**.

Comments may be sent by mail, fax or e-mail to:

Steve Ong  
Director, Standard Setting  
Hong Kong Institute of Certified Public Accountants  
37<sup>th</sup> Floor, Wu Chung House  
213 Queen's Road East  
Wanchai, Hong Kong

Fax number (+852) 2865 6776  
E-mail: [commentletters@hkicpa.org.hk](mailto:commentletters@hkicpa.org.hk)

Comments may be made available for public review unless otherwise requested by the contributor.



**Summary of alternative approaches to liability measurement in the Discussion Paper**

**(1) Alternative 1**

Measure all liabilities using the risk-free rate of interest and expected future cash flows, excluding any expectations about default. Any difference between the resulting amount and cash proceeds (if any) should be charged to income immediately.

**(2) Alternative 2**

Measure all liabilities using the risk-free rate of interest and expected future cash flows, excluding any expectations about default. Any difference between the resulting amount and cash proceeds (if any) should be charged to equity and amortised over the life of the liability.

**(3) Alternative 3**

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 market rates that exclude the effect of credit risk. Subsequent current measurements should incorporate changes in market interest rates. Changes arising from the entity's credit quality or the price of its credit should be excluded from the market interest rates. This would have the effects of fixing the credit spread at the original amount and incorporating all changes in the risk-free rate.

The appendix to the IASB staff paper includes simplified examples of the above alternatives, along with an example of including credit risk in the liability measurement.