

19 May 2006

To Mr Paul Martin
Director of Accounting Standards
Canadian Accounting Standards Board
277 Wellington Street West,
Toronto, Ontario
M5V 3H2 Canada
(ed.accounting@cica.org)

Tower 42
25 Old Broad Street
London EC2N 1HQ
United Kingdom
t + 44 (0) 20 7382 1770
f + 44 (0) 20 7382 1771
www.c-ebs.org

Dear Mr. Martin,

**Discussion Paper Measurement Bases for Financial Accounting –
Measurement on Initial recognition**

The Committee of European Banking Supervisors (CEBS), comprised of high level representatives from banking supervisory authorities and central banks of the European Union, welcomes the opportunity to comment on the discussion paper issued by the CASB Staff on behalf of the IASB regarding Measurement Bases for Financial Accounting – Measurement on Initial Recognition.

Banking supervisory authorities and central banks have a strong interest in promoting sound and high quality accounting and disclosure standards for the banking and financial industry, as well as transparent and comparable financial statements that strengthen market discipline. The measurement of financial and non-financial instruments in financial statements at initial recognition represents a matter of particular interest from a prudential perspective.

In that respect, measurement bases represent a key aspect for users of financial statements, in their analysis of a credit institution's financial situation. Moreover they are an important aspect for banking supervisors to consider in the assessment of a bank's solvency and its ability to comply with capital requirements.

Our comments are presented in the attached appendix. CEBS found it more useful to provide general comments summarizing its views on the conceptual issues raised in the discussion paper, rather than answering each individual item of the questionnaire provided by CASB Staff.

The enclosed comments have been prepared by one of CEBS' expert groups, the Expert Group on Financial Information (EGFI), chaired by Mr. Arnoud Vossen, in charge of monitoring any developments in that area and of preparing positions to be taken by CEBS. The development of our comments on this Discussion Paper was coordinated by a Subgroup of EGFI under the direction of Mr. Patrick Amis.

If you have any questions regarding our comments, please feel free to contact Mr. Arnoud Vossen (+31.20.524.3903) or Mr. Patrick Amis (+33.1.4292.6032).

Yours sincerely,

A handwritten signature in black ink, consisting of a large loop followed by a series of smaller, fluid strokes.

Danièle Nouy

Chair, Committee of European Banking Supervisors

Appendix - Comments on the main issues raised in the discussion paper

Status and position of the discussion paper

CEBS has three main comments on the overall status of the paper.

Firstly, the discussion paper uses the objectives and qualitative characteristics of the current framework as criteria for evaluating the possible bases of measurement on initial recognition. As these objectives and qualitative characteristics will be redefined within the scope of the Conceptual Framework project, CEBS thinks that it would be preferable to wait for the ending of the part of the project dealing with the objectives and qualitative characteristics (Phase A) before treating measurement issues (Phase C) where these characteristics are used as criteria.

Secondly, in our view the interaction between some of the issues arising from this discussion paper, and issues related to subsequent measurement, revenue recognition and performance reporting, is not made sufficiently clear. The discussion paper states in several places that its conclusions are tentative and subject to further analysis regarding re-measurement. We would agree that a discussion on initial recognition measurement is difficult to handle as long as there is no precise view on subsequent measurement and revenue recognition.

In this respect, we noted that some of the conclusions of the discussion paper could have wider implications for subsequent measurement and revenue recognition. In particular, we are concerned that such conclusions could lead to greater use of fair values for the measurement of instruments for which there is no liquid market and whose fair value might be difficult to assess reliably. Such a change should only take place after full consideration of the advantages and disadvantages for financial reporting. Thus, we recommend that a decision on initial recognition measurement should be taken only in conjunction with further research and analysis on the bases for subsequent measurement.

Thirdly, we also have some difficulty in assessing the links between this discussion paper and the exposure draft on fair value measurements published by the FASB. We understood that the IASB is planning to issue this latter document - once it has been finalized - as an exposure draft to its own constituency; however we see no visible link with the CASB paper. More generally, we recommend clarifying how the CASB discussion paper fits into the current IASB and FASB project for revising their respective conceptual frameworks.

Moreover, CEBS thinks that a more general debate on fair value as a measurement basis should take place and further research should be carried out on this subject before deciding that fair value is always more relevant than other measurement bases on initial recognition.

Modification of the fair value definition and hierarchy

The discussion paper proposes to amend the current definition of fair value, notably when it states that liabilities should be measured at initial

recognition for their exchange price rather than for their settlement amount.

The implementation of this amended definition could significantly change the content, and possibly the presentation, of financial statements, in particular for the banking industry. We are in particular concerned that there could be an impact on financial statements in relation to day one profits or losses that would be recognised on initial recognition at exchange price for instruments for which there is no liquid market or whose fair value cannot be measured reliably. CEBS therefore would like to recommend having further discussions on this issue – and linking it to subsequent measurement - before making such an important amendment.

The discussion paper states that further research should be carried out regarding the existence of multiple markets for the same instrument and the implications for measurement. We fully share this view and believe that such research should be extended to the situations where there is a discrepancy between market data and transaction price on initial recognition.

More generally, the discussion paper does not sufficiently consider that one characteristic of the finance and banking industry is, to a certain extent, to provide prices for markets. This issue could be explored further.

We noted also that the proposed definition, and the fair value hierarchy, is different from the one developed in the FASB exposure draft on fair value measurements. We recommend addressing any inconsistency between the two definitions before going further with the discussion paper.

Trade-off between reliability and relevance

The discussion paper notes that most conceptual frameworks indicate that a trade-off must be made between relevance and reliability. CEBS believes that the relationship between the relevance and the reliability criteria is more complex than just a simple trade-off. We would like to reiterate the importance we accord to the reliability criterion, and would welcome more explanation regarding how the discussion paper came to the conclusion that relevance should be favoured over reliability. In addition, we recommend that this discussion takes place in the broader context of the revision of the conceptual framework of the IASB and the FASB.