

March 28, 2011

241280

Website: www.iasb.org

Sir David Tweedie International Accounting Standards Board First Floor, 30 Cannon Street London, EC4M 6XH United Kingdom

Dear Sir David Tweedie:

RE: IASB Supplementary Exposure Draft "Financial Instruments: Impairment"

Thank you for the opportunity to comment on the IASB supplementary exposure draft "Financial Instruments: Impairment." The views expressed in this letter reflect the views of the Province of British Columbia (the Province). These views are based on a commitment to preparing financial statements that are understandable and meet the information and decision-making needs of the public and the Legislature acting on their behalf.

The Summary Financial Statements of the Province are prepared in accordance with Canadian Public Sector Accounting Board (PSAB) standards. The Province will be impacted by the proposed revisions contained in the exposure draft because several of our entities adopted IFRS in 2011; these entities are accounted for by the Province on the modified equity basis. In addition, IPSASB and PSAB guidance may be impacted by IASB guidance in the future.

The Province does not believe the expected loss approach for the recognition of financial impairment is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment of a financial asset recognized at amortized cost. The use of the expected loss approach would result in:

- Impairment losses being recognized based on an expected future event, which is
 inconsistent with the IFRS conceptual framework, (the conceptual framework states that
 the assets of any entity result from past transactions or other past events);
- Artificial volatility being introduced to an entity's bottom line with the volatility only being eliminated with the sale or other disposal of the financial asset; and
- Recognition of impairment losses before they have actually been incurred.

Financial assets recognized at amortized cost are held with the objective to hold the assets in order to collect contractual cash flows. The use of the expected loss approach for the recognition

of impairment losses would impose fair value measurement on financial assets that are otherwise measured at amortised cost, thus effectively eliminating the amortized cost category of financial assets. The Province believes stakeholders would be better informed of the change in credit value through the notes to the financial statements unless there has been an incurred credit loss, which should be recognized immediately.

The expected loss approach would introduce a great deal of subjectivity into the assessment of the impairment of financial assets. The expected loss would be influenced by an entity's current position in an economic cycle. In an economic downturn, the expected losses related to financial assets recognized at amortized cost would increase. Once the economic cycle turns to a more optimistic position, the expected losses related to a financial asset would decrease. Over the period of the economic cycle, the expected losses would change either positively or negatively but the underlying characteristics of the financial assets have not changed at all. The entity is still holding the asset in order to collect the contractual cash flows and these do not change until a loss has been incurred. It is, therefore, counter intuitive to recognize expected losses before a loss has actually been incurred.

Responses to specific questions posed in the exposure draft are attached. Should you have any comments or questions, please contact me at 250 387-6692 or by e-mail: Stuart.Newton@gov.bc.ca, or Carl Fischer, Executive Director, Financial Reporting and Advisory Services Branch, at 250 356-9272 or by e-mail: Carl.Fischer@gov.bc.ca.

On behalf of the Province of British Columbia

Sincerely,

Stuart Newton, CA, CIA Acting Comptroller General

Enclosure

cc:

Peter Milburn Deputy Minister Ministry of Finance

Sabine Feulgen A/Deputy Secretary to the Treasury Board Ministry of Finance

Carl Fischer
Executive Director
Financial Reporting and Advisory Services

Peter Martin, Director Accounting Standards Board, Canada E-mail: ed.accounting@cica.ca

General

An important weakness that has been identified with respect to the current impairment models under IFRSs and US GAAP is delayed recognition of credit losses associated with financial assets. This supplementary document proposes a revised approach for an impairment model for financial assets in open portfolios that would recognise credit losses from initial recognition of a financial asset. The timing of recognition would vary according to the differentiation of financial assets into two groups as described in paragraphs 2, 3 and B2–B4 of the supplementary document.

Ouestion 1

Do you believe the approach for recognition of impairment described in this supplementary document deals with this weakness (ie delayed recognition of expected credit losses)? If not, how do you believe the proposed model should be revised and why?

The Province does not believe the expected loss approach for the recognition of financial impairment, is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment of a financial asset recognized at amortized cost. The use of the expected loss approach would result in:

- Impairment losses being recognized based on an expected future event, which is inconsistent with the IFRS conceptual framework (the conceptual framework states that the assets of any entity result from past transactions or other past events);
- Artificial volatility being introduced to an entity's bottom line with the volatility only being eliminated with the sale or other disposal of the financial asset; and
- Recognition of impairment losses before they have actually been incurred.

Financial assets recognized at amortized cost are held with the objective to hold the assets in order to collect contractual cash flows. The use of the expected loss approach for the recognition of impairment losses would impose fair value measurement on financial assets that are otherwise measured at amortised cost, thus effectively eliminating the amortized cost category of financial assets. The Province believes stakeholders would be better informed of the change in credit value through the notes to the financial statements unless there has been an incurred credit loss, which should be recognized immediately.

The expected loss approach would introduce a great deal of subjectivity into the impairment assessment. The expected loss would be influenced by an entity's current position in an economic cycle. In an economic downturn, the expected losses related to financial assets recognized at amortized cost would increase. Once the economic cycle turns to a more optimistic position, the expected losses related to a financial asset would decrease. Over the period of the economic cycle, the expected losses would change either positively or negatively but the underlying characteristics of the financial assets would not have changed at all. The entity is still holding the asset in order to collect the contractual cash flows and these do not change until a loss has been incurred. It is therefore counter intuitive to recognize expected losses before a loss has actually been incurred.

Scope - Open Portfolios

The scope of this document is limited to financial assets managed in an open portfolio. However, the boards expect to use the comments received on this supplementary document, and the original proposals published by the IASB and the FASB, to determine whether a single impairment model should be applied to all financial assets or whether there are differences that justify multiple impairment models. Therefore, the boards are asking for views on whether the proposals outlined in this document could be applied to closed portfolios, single instruments and any other types of instruments.

Question 2

Is the impairment model proposed in the supplementary document at least as operational for closed portfolios and other instruments as it is for open portfolios? Why or why not?

Although the supplementary document seeks views on whether the proposed approach is suitable for open portfolios, the boards welcome any comments on its suitability for single assets and closed portfolios and also comments on how important it is to have a single impairment approach for all relevant financial assets.

The Province does not believe the expected loss approach for the recognition of financial impairment is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment of a financial asset recognized at amortized cost.

Differentiation of credit loss recognition (paragraphs 2, 3 and B2-B4)

This document proposes that financial assets managed on an open portfolio basis should be placed into two groups, based on their credit characteristics, for the purpose of determining the impairment allowance. For one group, the entire amount of expected credit losses would be recognized in the impairment allowance (this group is often referred to as the 'bad book'). For the other group (often referred to as the 'good book'), expected credit losses would be recognized on a portfolio basis over a time period at the higher of the time-proportional expected credit losses (depending on the age of the portfolio) and the credit losses expected to occur within the foreseeable future period (being a minimum of twelve months).

Question 3

Do you agree that for financial assets in the 'good book' it is appropriate to recognise the impairment allowance using the approach described above? Why or why not?

This question is not applicable to the province.

Question 4

Would the proposed approach to determining the impairment allowance on a time-proportional basis be operational? Why or why not?

The Province does not believe the expected loss approach for the recognition of financial impairment, is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment of a financial asset recognized at amortized cost.

Question 5

Would the proposed approach provide information that is useful for decision-making? If not, how would you modify the proposal?

The Province does not believe that the proposed approach would provide decision-useful information because the use of the expected loss approach would result in:

- Impairment losses being recognized based on an expected future event, which is inconsistent with the IFRS conceptual framework, (the conceptual framework states that the assets of any entity result from past transactions or other past events);
- Artificial volatility being introduced to an entity's bottom line with the volatility only being eliminated with the sale or other disposal of the financial asset; and
- · Recognition of impairment losses before they have actually been incurred.

Financial assets recognized at amortized cost are held with the objective to hold the assets in order to collect contractual cash flows. The use of the expected loss approach for the recognition of impairment losses would impose fair value measurement on financial assets that are otherwise measured at amortized cost, thus effectively eliminating the amortized cost category of financial assets. The Province believes stakeholders would be better informed of the change in credit value through the notes to the financial statements unless there has been an incurred credit loss, which should be recognized immediately.

The expected loss approach would introduce a great deal of subjectivity into the impairment assessment. The expected loss would be influenced by an entity's current position in an economic cycle. In an economic downturn, the expected losses related to financial assets recognized at amortized cost would increase. Once the economic cycle turns to a more optimistic position, the expected losses related to a financial asset would decrease. Over the period of the economic cycle, the expected losses would change either positively or negatively, but the underlying characteristics of the financial assets have not changed at all. The entity is still holding the asset in order to collect the contractual cash flows and these do not change until a loss has been incurred. It is, therefore, counter intuitive to recognize expected losses before a loss has actually been incurred.

The principle for how to determine whether a financial asset should be in the group for which the entire amount of expected credit losses would be recognized (i.e. the 'bad book') is described in paragraph 3 as follows:

"It is no longer appropriate to recognize expected credit losses over a time period if the collectability of a financial asset, or group of financial assets, becomes so uncertain that the entity's credit risk management objective changes for that asset or group, thereof from receiving the regular payments from the debtor to recovery of all or a portion of the financial asset."

Therefore, financial assets would be included in and transferred between the two groups (i.e., the 'good book' and the 'bad book') in accordance with an entity's internal risk management.

Question 6

Is the requirement to differentiate between the two groups (i.e. 'good book' and 'bad book') for the purpose of determining the impairment allowance clearly described? If not, how could it be described more clearly?

The question is not applicable to the Province.

Question 7

Is the requirement to differentiate between the two groups (i.e. 'good book' and 'bad book') for the purpose of determining the impairment allowance operational and/or auditable? If not, how could it be made more operational and/or auditable?

The question is not applicable to the Province.

Question 8

Do you agree with the proposed requirement to differentiate between the two groups (ie 'good book' and 'bad book') for the purpose of determining the impairment allowance? If not, what requirement would you propose and why?

The question is not applicable to the Province.

Minimum impairment allowance amount (paragraph 2(a)(ii))

This document proposes to differentiate the recognition of credit losses depending on the classification of a financial asset into two groups (often referred to as the 'good book' and the 'bad book'). For the 'bad book', the allowance amount would always be equal to the lifetime expected credit losses for the financial assets in that group. Paragraph 2(a)(ii) would require the time-proportional impairment allowance (i.e., in relation to the 'good book') never to be less than a minimum allowance amount ('floor'). This would ensure that this allowance amount would at least cover the expected credit losses over the near term. The floor is proposed to be the amount of credit losses expected to occur within the foreseeable future (required to be no less than twelve months after an entity's reporting date). The model that was being developed by the FASB is consistent with this 'floor' approach, but the FASB did not propose the minimum of 'no less than twelve months'.

Question 9

The boards are seeking comment with respect to the minimum allowance amount (floor) that would be required under this model. Specifically, on the following issues:

(a) Do you agree with the proposal to require a floor for the impairment allowance related to the 'good book'? Why or why not?

The question is not applicable to the Province.

(b) Alternatively, do you believe that an entity should be required to invoke a floor for the impairment allowance related to the 'good book' only in circumstances in which there is evidence of an early loss pattern?

The question is not applicable to the Province.

(c) If you agree with a proposed minimum allowance amount, do you further agree that it should be determined on the basis of losses expected to occur within the foreseeable future (and no less than twelve months)? Why or why not? If you disagree, how would you prefer the minimum allowance to be determined and why?

The question is not applicable to the Province.

(d) For the foreseeable future, would the period considered in developing the expected loss estimate change on the basis of changes in economic conditions?

The Province does not believe the expected loss approach for the recognition of impairment is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment for a financial asset recognized at amortized cost.

(e) Do you believe that the foreseeable future period (for purposes of a credit impairment model) is typically a period greater than twelve months? Why or why not? Please provide data to support your response, including details of particular portfolios for which you believe this will be the case.

The Province does not believe the expected loss approach for the recognition of financial impairment is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment of a financial asset recognized at amortized cost.

(f) If you agree that the foreseeable future is typically a period greater than twelve months, in order to facilitate comparability, do you believe that a 'ceiling' should be established for determining the amount of credit impairment to be recognised under the 'floor' requirement (for example, no more than three years after an entity's reporting date)? If so, please provide data and/or reasons to support your response.

The Province does not believe the expected loss approach for the recognition of financial impairment is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment of a financial asset recognized at amortized cost.

Question 10

Do you believe that the floor will typically be equal to or higher than the amount calculated in accordance with paragraph 2(a)(i)? Please provide data and/or reasons to support your response, including details of particular portfolios for which you believe this will be the case.

The question is not applicable to the Province.

Flexibility related to using discounted amounts (paragraphs B8(a) and B10)

Paragraph B8(a) permits an entity to use a discounted or undiscounted estimate when calculating the time-proportional allowance amount in accordance with that paragraph.

When using a discounted expected loss amount, paragraph B10 permits an entity to use as the discount rate any reasonable rate between (and including) the risk-free rate and the effective interest rate (as used for the effective interest method in IAS 39). This flexibility is intended to make discounting operationally feasible. Requiring the use of the effective interest rate would give rise to operational complexity similar to that identified in the comments received by the IASB in relation to an integrated effective interest rate approach. (Note: The FASB did not deliberate this issue. This was a decision reached by the IASB only; however, comment is requested in this joint document because this is an integral component of the time-proportional approach.)

Question 11

The boards are seeking comment with respect to the flexibility related to using discounted amounts. Specifically, on the following issues:

(a) Do you agree with the flexibility permitted to use either a discounted or undiscounted estimate when applying the approach described in paragraph B8(a)? Why or why not?

The question is not applicable to the Province.

(b) Do you agree with permitting flexibility in the selection of a discount rate when using a discounted expected loss amount? Why or why not?

The question is not applicable to the Province.

Approaches developed by the IASB and FASB separately

As mentioned in the Introduction and in the Basis for Conclusions, the model described in this document is being proposed by the IASB and FASB because both boards are committed to reaching a common solution to impairment accounting. However, the IASB and the FASB had been developing models that would address their differing primary objectives. Components of these models are reflected in the common proposal. In summary, the approaches are:

Model	Recognition of credit losses (when appropriate to recognise over life - ie 'good book')	Recognition of credit losses (when NOT appropriate to recognise over life - ie 'bad book')
Common proposal	Higher of: (a) time-proportional amount of remaining lifetime expected credit losses; and (b) all expected credit losses for the foreseeable future (being a minimum of twelve months)	Full amount of remaining lifetime expected credit losses
IASB approach	Time-proportional amount of remaining lifetime expected credit losses	Full amount of remaining lifetime expected credit losses
FASB approach	Recognise expected credit losses for the foreseeable future (no minimum period specified)	

The approach that was being developed by the IASB for open portfolios of financial assets measured at amortized cost took into account comments received in comment letters, the advice from the Expert Advisory Panel (EAP) and other outreach activities. For financial assets for which it is appropriate to consider credit losses over their life (commonly called the 'good book'), the credit losses expected to occur for the remaining life of the financial

assets would be recognized using a time-proportional approach. For all other financial assets, credit losses expected to occur for the remaining life would be immediately recognized. In other words, the model being developed by the IASB was the model described in this document without consideration of a 'floor' amount.

Question 12

Would you prefer the IASB approach for open portfolios of financial assets measured at amortised cost to the common proposal in this document? Why or why not? If you would not prefer this specific IASB approach, do you prefer the general concept of the IASB approach (ie to recognise expected credit losses over the life of the assets)? Why or why not?

The Province does not agree with either IASB or the FASB approach. The Province does not believe the expected loss approach for the recognition of financial impairment is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment of a financial asset recognized at amortized cost.

The approach that was being developed by the FASB addressed the comments on its original exposure draft and other outreach activities. That model being developed would have required an entity to recognize immediately all credit losses expected to occur in the foreseeable future (not explicitly set at a minimum of twelve months). As described in paragraphs B11 and B12, the foreseeable future time period is the period for which reasonable and supportable information exists to support specific projections of events and conditions. In other words, the approach being developed by the FASB applied a similar concept to the 'floor' included in this document to recognize credit losses expected to occur within the foreseeable future at or after the first reporting date after initial recognition for all financial assets within the scope of this document.

Question 13

Would you prefer the FASB approach for assets in the scope of this document to the common proposal in this document? Why or why not? If you would not prefer this specific FASB approach, do you prefer the general concept of this FASB approach (ie to recognise currently credit losses expected to occur in the foreseeable future)? Why or why not?

The Province does not agree with either IASB or the FASB approach. The Province does not believe the expected loss approach for the recognition of financial impairment is the appropriate approach to recognize impairments of financial assets recognized at amortized cost. The Province believes the IASB should retain the incurred loss approach for the recognition of impairment of a financial asset recognized at amortized cost.