19 May

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Director
Canadian Accounting Standards Board
277 Wellington Street West
Toronto
Ontario M5V 3H2
Canada
Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
LONDON EC4M 6XH
UNITED KINGDOM

Dear Sir David,

Discussion Paper: Measurement Bases for Financial Accounting – Measurement on Initial Recognition
IFRIC Draft Interpretations D12 to D14 - Service Concession Arrangements
IFRIC Draft Interpretation D15 Reassessment of Embedded Derivatives

The Malaysian Accounting Standards Board (MASB) appreciates the opportunity to offer its views on the Discussion Paper: Measurement Bases for Financial Accounting – Measurement on Initial Recognition (DP).

We commend the efforts of the staff of the Canadian Accounting Standards Board in developing the DPto .

Support the IASB taking on the project into the agenda following 4 IFRIC Draft Interpretations:

(i)D12 Service Concession Arrangements - Determining the Accounting Model;

(ii)D13 Service Concession Arrangements - The Financial Asset Model;

(iii)D14 Service Concession Arrangements - The Intangible Asset Model; and

(iv)D15 Reassessment of Embedded Derivatives.

We support appreciate the efforts of IFRIC to provide guidance on the accounting by operators for public infrastructure service concessions and the . We also support IFRIC's move to clarify whether reassessment of an embedded derivative is required throughout the life of a contract.

Having reviewed the draft Interpretations and comments feedback received from the Malaysian constituents, we Generally we have no objection to the proposals in the DP. We support the measurement hierarchy in the DP which allows the use of other measurement bases as substitute for fair value, such as the use of current cost and valuation techniques that use entity-specific inputs only.

However, we wish to point out that the

A the responses would be provided to IASB for them to take into account in its projects, it would be helpful if the proposals in the DP should have ttaken into consideration the deliberations on the related convergence projects undertaken by IASB and FASB, such as the Conceptual Framework or Fair Value Measurement, to ensure consistency of application of the concepts used.

For example, t
The DP defines fair value as:

> "*the amount for which an asset or liability could be exchanged between knowledgeable, willing parties in an arm's length transaction*".

However, IASB plans to issue an Exposure Draft on Fair Value Measurements, based on the FASB's final Fair Value Measurements standard, by April 2006 which which defines fair value as

> "*the price that would be received for an asset or paid to transfer a liability in a current transaction between marketplace participants in the reference market for the asset or liability*".

We suggest that there must be consistencyt in the definition of fair value if the responses would to be used for the IASB's purposes and for the DP would to fit into the current agenda of the IASB.

In addition, we noted the DP explains that the conclusions reached therein are tentative and will be re-assessed when their potential implications for re-measurement are considered in subsequent papers. The IASB acknowledges that the DP would be helpful in considering initial and subsequent measurement, ie phase C of its project on Conceptual Framework. In this regard, it would be helpful if the proposals in the DP on initial measurement to be finalised coterminous with the proposals on subsequent measurement since there is no clean division between initial measurement and re-measurement.

are in support of the proposed management commentary disclosure framework for to

also proposal to add this item on the agenda although the will recognise that there are other pressing accounting issues that should take priority over this document. In the meantime, securities regulators, being interested parties to this document, should be consulted for views and to determine the extent to which the information as laid out in the commentary will be useful. After all, many securities regulators have put into place some form of theirs.

If the general view was for the have y,the more plausible route will be by way of a standard However, we hold the view that management commentary should not be an integral part of the financial reports. While such sustainable reporting, etc., are important smanagement commentary is but The difficulty of making is real, especially from an auditing standpointwe believe that ambit of the In this regard, tIASB may wish toconsider ing similar provides for voluntary requirementsIn many jurisdictions, alternatively requirements

We are pleased to submit our responses to the questions you raised in the DP overleaf.

Should you require further information, please contact Dr. Nordin Mohd Zain, the Executive Director of MASB, via e-mail at nordin@masb.org.my.

Yours sincerely,

Dato' Zainal Abidin Putih
Chairman

With this proper framework in place, there will be greater comparability of management commentary information across jurisdictions that have use IFRS as their accounting standards.

However, we believe that management commentary should not be an integral part of the financial reports.

> He went on to explain that preparers would have no problem as to where MC should be placed in the Financial Reports. However, it might be a problem for auditors if MC was placed within the Financial Statements. He stated that if auditors could give assurance to information in an IPO, why not MC. Auditors could always express an opinion with the available information.

Issue of other stakeholders –

Issue of audit

Have in place some form of guidance although not comprehensivehave no objections to the proposal laid out in D15.

However, there are areas in D12, D13 and D14 whichwe merit considerable attention.

Generally, we are of the view that a project of such pervasive nature as a service concession should have been dealt with by the Board, viade a separate standard, rather than having to address it through interpretations. Clearly, the three Interpretations could have been amalgamated for more efficient guidance for stakeholders, and at the same time could avoid users having to refer to many other related standards.

An approach that can be taken is for the IASB to consider determining an appropriate accounting model that reflects more comprehensively government-private sector collaboration based on service concession practices across jurisdictions, including those in Malaysia. to account for the service concession arrangement based on practices across jurisdictions, including those in Malaysia. Such an accounting model is required to reflect more comprehensively government-private sector collaboration. There could beare established models for such. We believe that the model within a separate financial reporting standard can address the shortcomings of the principles proposed in the draft interpretations which seemed to have conflicting accounting treatments even under circumstances where the arrangements for which the associated cash flows and risks are essentially the same. An example is where the grantor makes the payments or where the grantor guarantees the operator's returns. The degree of risk faced by the operator in both instances would be low under both situations and yet, they are accounted differently under the draft Interpretations.

In the process of determining a model, it will be appropriate to then consider treating service concession arrangement and the underlying asset as a separate class of assets and accounted for as such. This approach is similar to the approach taken by the IASC in considering investment property within a separate standard and in classifying investment property as a separate class of assets.

disagree with the proposals in draft Interpretations D12 to D14. However, we have no objections to the proposal laid out in D15.

We suggest that the IASB to develop a separate accounting standard on accounting for service concession arrangements, rather than an interpretation of the existing IFRSs. The draft Interpretations iseem incomplete in respect of the election of application of the accounting model. F, for example it has not clarified whether the determination of the accounting model is a one-off election made at inception of the concession arrangement or a matter of reassessment. The

Interpretations are also Another example is that the draft Interpretations is silent on the timing of recognition of intangible asset under the intangible asset model.

The drafts Interpretations haves also drawn an inappropriate line between the financial asset model and intangible asset model, such that similar transaction will have to be accounted differently even though they are essentially the same. For example, the treatment for maintenance and repairs obligations provided in D13 is different from the one in D14 even though in substance the contractual obligation in both models is of the same nature.

In essence, while the proposed Interpretations are meant to ensure consistency in practice, there are areas to improve in the drafting to maintain clarity and avoid unnecessary inconsistency in application. The macro view is that a separate standard issued by the Board is recommended to address that will enable identification of a large number of concessionaires that may fall outside the scope of the Interpretation and addressing more comprehensively the treatment of government-private sector collaborations.

We suggest that the IASB to consider determining an appropriate accounting model to account for this service concession arrangement as a separate class of asset, similar to what the IASC had done for investment property which is classified as a separate class of asset. An appropriate accounting model is required because the draft Interpretations calls for different accounting treatment even though in circumstance where the arrangements for which the cash flows and risks attached thereto are essential the same. For example, where the grantor makes the payments or where the grantor guaranteeing the operator's return, the degree of risk faced by the operator in both instances would be similarly low and yet, they are accounted differently under the draft Interpretations.

<u>Discussion Paper</u>
<u>Management Commentary</u>

Requirements for management commentary (MC)

The project team concluded that an entity's financial report should be viewed as a package comprising the primary financial statements, accompanying notes and MC (section 1). They also concluded that the quality of MC was likely to be enhanced if the IASB issued requirements relating to MC (section 6).

Question 1: Do you agree that MC should be considered as an integral part of financial reports? If not, why not?

Requirements for MC

The project team concluded that an entity's financial report should be viewed as a package comprising the primary financial statements, accompanying notes and MC (section 1). They also concluded that the quality of MC was likely to be enhanced if the IASB issued requirements relating to MC (section 6).

Question 1: Do you agree that MC should be considered as an integral part of financial reports? If not, why not?

We regard management commentary (MC) information as an integral part of financial reports.

The financial statements as currently covered by the IFRS should be seen as a kind of stand-alone package for accounting purposes. An additional MC should complement and supplement the financial statements as part of the financial reporting package of companies. In our opinion figure 1.1 of the discussion paper (see page 12) adequately illustrates the relationship of the different financial reporting instruments. We do not think that the boundaries of the financial statements should be extended in order to include MC information.

Almost all companies that apply IFRS provide some additional statements to meet the information needs of investors and often an even wider group of stakeholders. Since the information proposed to be included in MC is derived from or linked to financial statements—for example, information about research and development of a pharmaceutical company—it should form part of the financial reporting package together with the financial statements.

Indeed, the MC is so important, and the links between it and the financial statements so great, that we believe the IASB's Framework document should be extended to cover the MC. We note in this context that the Framework is currently under examination for improvement. Since this project is still at a fairly early stage it appears to be a great opportunity to discuss a possible extension of the scope of the Framework to other financial reporting, and thereby bringing it more into line with the wording of the IASCF Constitution and the IFRS Preface. This issue could be part of phase E of the project, presentation and disclosure, including financial reporting boundaries. Such material would help ensure that a consistent approach is adopted to the subject and that conflicts between otherwise separate projects are avoided.

We think that the material that we comment on under 'Question 5' below would be a good starting point for the Framework discussion of the MC.

Question 2: Should the development of requirements for MC be a priority for the IASB? If not, why not? If yes, what form should any requirements take?

We are fully supportive of the project on MC, because we see MC as a key element of business reporting. We would support the IASB taking it onto its active agenda. We believe the IASB should adopt a principle-based high-level approach to the subject, because we think such an approach has the potential to be of great benefit internationally.

Question 3: Should entities be required to include MC in their financial report in order to assert compliance with IFRSs? Please explain why or why not.

Assuming that the IASB decides to issue MC requirements, we support developing a standard. It seems that voluntary guidance already exists in many forms all over the world, thus a standard is more likely to enhance and harmonise MC information.

Purpose of MC

The project team concluded that, rather than having one dominant objective, MC has three principal objectives (section 2). The project team also concluded that the primary focus of MC is to meet the information requirements of investors.

<u>Question 4:</u> Do you agree with the objectives suggested by the project team or, if not, how should they be changed? Is the focus on investors appropriate?

We agree with the three principal objectives of MC, which the paper describes as being to:

supplement and complement the financial statements;
provide an analysis of the entity through the eyes of the management; and
have an orientation to the future.

We think that the focus on investors is appropriate. We note in this context that the IASB has tentatively decided to revise what its Framework says about the primary users of financial statements; at the moment the Framework states that investors are the primary users, but the IASB has tentatively decided to extend this to include creditors. As we see the MC as a document prepared primarily for the capital markets, our view is that, even if the IASB implements its tentative decision, the focus of MC should remain on investors. It might be useful to include in the definition of MC a reference to this focus on investor information needs.

We also agree that the scope of MC should not be extended to meeting special needs of a wider set of stakeholders. As mentioned in paragraph 30 of the discussion paper, MC should not be a replacement of sustainability and corporate social responsibility reports prepared by many companies nowadays. Nevertheless, this kind of environmental issues, social responsibility issues as well as issues of sustainability should be included in management commentary if such issues have had or is expected to have a significant influence on the financial development or position of an entity. Even investors concerned principally with financial returns will be interested in a company's environmental and social policies to the extent that they might have an impact on risks and future financial returns. Such impacts can cause, for example reduced revenues, if customers react to a company's environmental policy, or significantly increase costs because of accidents due to poor safety standards.

Principles, qualitative characteristics and content of MC

The project team concluded that it is not appropriate to specify the precise information that must be disclosed within MC, or how it is presented. Rather, they believe that any requirements for MC should set out the principles and qualitative characteristics, as well as the essential areas of MC, necessary to make the information useful to investors. It is up to management to determine what information is required to meet these requirements, and to determine how the information is presented. The project team has also suggested that it is appropriate consider ways to limit the amount of information management is allowed to disclose, as a way of ensuring that it is the most important information which is presented to investors. (See sections 3 and 4)

<u>Question 5: </u>Do you agree with the principles and qualitative characteristics that the project team believes are essential in the preparation of MC? If not, what additional principles or characteristics are required, or which ones suggested by the project team would you change? to avoid iobscuring. of financial statements

<u>Having qualitative characteristics for management commentary is essential for improving the quality of such financial reports. We agree with the characteristics as set out in the discussion paper.</u>

<u>We regard the three proposed principles of MC (set out in paragraph 39) as appropriate. We recognise that, if the information is given through the eyes of management, comparability between entities is difficult to achieve, but agree that the qualitative characteristics of MC should focus on achieving comparability over time. Another important issue is the supportability of the information contained in MC as proposed and explained in paragraph 75.</u>

<u>Question 6: The DP outlines the essential content areas that MC should cover. Do you agree with these? If not, what additional areas would you recommend or which ones suggested by the project team would you change?</u>

We agree with the principles-based high-level approach adopted to the content of MC. We are also broadly supportive of the specific things the paper says on content, although we have the following observations:

We do not consider paragraph 100 to be a comprehensive list and would suggest that this is made clear in the text.

We think there ought to be strong linkage between the information provided about the objectives and strategies of a company (paragraph 100b) and the information provided on its results and prospects (paragraph 100d). This linkage is very important for the comparability of management commentary information over time.

Although the paper refers to segmental information, we think it should emphasise that MC information should generally be provided on a segment basis. We recognise that not all information contained in MC can be or should be segmented, e.g. information about the cash flow management. We think best practice is to segment the key MC content information unless impracticable to do so and to use the same segmentation in MC as that used in the financial statements (A13 of the proposed standard).

We think the “key resources, risks and relationships” (paragraph 100c) should include more information about the risk management of the company. Reporting about the entity specific risk management system and its processes of identifying the risks as well as the ongoing improvement effort of the management system respectively are very important information for investors.

Question 7: Do you think it is appropriate to provide guidance or requirements to limit the amount of information disclosed within MC, or at least ensure that the most important information is highlighted? If not, why not? If yes, how would you suggest this is best achieved?

We agree with the approach of the discussion paper—it is important that the MC does not get cluttered up and its message obscured. For that reason we suggest that any standard should emphasise that:

MC should focus on issues relevant to investors and should be presented in a way that highlights those issues of greatest importance to investors.

the information included in the MC should be balanced and the presentation of the information should also be balanced. For example, negative information that is important to investors should be given the same prominence as positive information that is as important to investors.

Question 8: Does your jurisdiction already have requirements for some entities to provide MC? If yes, are your local requirements consistent with the model the project team has set out? If they are not consistent, what would the major areas of conflict or difference be?

The Fourth and Seventh EU Company Law Directives already require the preparation and presentation of an annual report which is very similar to the management commentary as proposed by the working group. Additionally, the annual report will become a mandatory and essential part of the annual and half-yearly financial reports of security issuers listed on regulated markets in the EU from 2007 onwards. Further details of the EU legislation are set out in Appendix B12-B15 of the discussion paper. So far we are not aware of any major areas of conflict or differences.

Placement principles

The project team concluded that it would be helpful to establish principles to guide the IASB in determining whether information it requires entities to disclose within financial reports should be placed in MC, on the face of the primary financial statements or in the notes to the financial statements. The project team has suggested some principles (section 5).

Question 9: Are the placement principles suggested by the project team helpful and, if applied, are they likely to lead to more consistent and appropriate placement of information within financial reports? If not, what is a more appropriate model?

The DP's discussion of placement and placement criteria in paragraphs 153-185 is a good discussion that is worth studying carefully. We are supportive of the suggestion that criteria are needed to determine whether a piece of information should be provided in the management commentary rather than the financial statements and vice versa. However, we suggest reconsidering and specifying the placement principles. In particular, although the criteria described in paragraph 169 b) for including information in the notes to the primary financial statements is derived from the current IASB Framework, the term "…essential to an *understanding* of the primary financial statements and its elements…" might not be suitable to define the boundary between the information within the financial statements on the one side and MC information on the other side. MC information might also be necessary for an understanding of the results and outcomes of the financial statements by providing contextual and strategic information, e.g. a report on the developments of the financial year under report.

Should you require further information, please contact Dr. Nordin Mohd Zain, the technical Executive Ddirector of MASB, via e-mail at nordin@masb.org.my.

Yours sincerely,

Dato' Zainal Abidin Putih
Chairman