C45

MASB MALAYSIAN ACCOUNTING STANDARDS BOARD
LEMBAGA PIAWAIAN PERAKAUNAN MALAYSIA

1 September 2009

Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London ED 4M 6 XH
United Kingdom

Dear Sir David

IASB DISCUSSION PAPER – CREDIT RISK IN LIABILITY MEASUREMENT

The Malaysian Accounting Standards Board welcomes the opportunity to provide comments on the IASB Discussion Paper – Credit Risk in Liability Measurement (DP).

We appreciate the IASB's initiative to seek views from users of financial statements to generate a focused discussion to enhance the debate of whether or not to include the effect of non-performance risk in the measurement of a liability.

Having considered the arguments set out in the DP, we do not support the arguments for inclusion of credit risk in subsequent measurement of liabilities.

When a liability is first recognised, we believe the price of credit risk should only be incorporated in the liability measurement if and only if the effects of the borrower's credit standing has been factored in determining the exchange value of the debt contract i.e. the liability transacted value, which has incorporated the credit risk of the borrower, is at the date of transaction reflective of the fair value of that transaction. In other words, we believe the amount of liability to be recognised initially would be equal to the amount the entity is required to pay rather than based on a hypothetical amount the market expects the entity to pay.

As for the current measurement of liabilities, changes of the price in relation to credit risk should not be incorporated in the liability measurement. In our view, the subsequent measurement of liabilities incorporating changes in own credit risk is inappropriate. Conceptually, any changes in own credit risk should be in relation to the whole portfolio of net assets held by the reporting entity (including those that are not currently measured and recognised on balance sheet). The inclusion of the effects of changes in own credit risk into liabilities in isolation (without corresponding adjustments to other affected items in the net assets) is thus incomplete and inappropriate. In our view, for this reason, the credit risk portion in the initial fair value measurement at the inception should be 'pegged' or 'frozen' and left unchanged subsequently.

In addition, subsequent reporting of the effects of changes in an entity's credit standing is "counter intuitive". Changes in credit standing will result in confusing and misleading outcomes. When the reporting entity's credit standing improves, its liabilities will increase in value with resulting losses. Whilst correspondingly, if its credit standing deteriorates, the value of its liabilities will drop with resulting gain. As one of the arguments rightly pointed out, reporting a gain from a decline in credit quality can mask a deteriorating situation, especially in current market conditions.

Suite 5.2, Level 5, Wisma UOA Pantai, No. 11, Jalan Pantai Jaya, 59200 Kuala Lumpur
Tel : (603) 2240-9200 Fax : (603) 2240-9300 E-mail : masb@masb.org.my Website : www.masb.org.my

To illustrate the above, at the inception date, if a bond issuer (rated AAA) has committed to pay a coupon rate of 50bp above risk free rate, the 50bp credit spread should remain constant (even though the issuer may have a better or worse rating in the future years) for the subsequent fair value measurement of the liability to be reported in the bond issuer's financial statements. In other words, subsequent changes in the fair value of the liability in the issuer's book should not be affected by the changes in its own credit standing but only due to changes in other related factors e.g. market risks.

If you need further clarification, please contact Ms Tan Bee Leng at +603 2240 9200 or by email at beeleng@masb.org.my.

Thank you.

Yours sincerely,

Mohammad Faiz Azmi
Chairman