## Comments on Amendments to IAS 32 and 39

CL 13A

**The Life Insurance Association of Japan**

**IAS 32**

| Questions in "Invitation to Comment" | Reply and Opinion |
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| **Question 1 - Probabilities of different manners of settlement (paragraphs 19, 22, and 22A)**<br>Do you agree that the classification of a financial instrument as a liability or as equity in accordance with the substance of the contractual arrangements should be made without regard to probabilities of different manners of settlement? The proposed amendments eliminate the notion in paragraph 22 that an instrument that the issuer is economically compelled to redeem because of a contractually accelerating dividend should be classified as a financial liability. In addition, the proposed amendments require a financial instrument that the issuer could be required to settle by delivering cash or other financial assets, depending on the occurrence or non-occurrence of uncertain future events or on the outcome of uncertain circumstances that are beyond the control of both the issuer and the holder of the instrument, to be classified as a financial liability, irrespective of the probability of those events or circumstances occurring (paragraph 22A). | .In the case of executing accounting with regard to probabilities, we can agree with the direction of clarifying the definition of a financial liability without regard to probabilities, because it is possible that arbitrariness will come into play depending on how probability is considered. |
| **Question 2 -- Separation of liability and equity elements (paragraphs 28 and 29)**<br>Do you agree that the options in IAS 32 for an issuer to measure the liability element of a compound financial instrument initially either as a residual amount after separating the equity element or based on a relative-fair-value method should be eliminated and, instead, any asset and liability elements should be separated and measured first and then the residual assigned to the equity element? | .We agree with first separating the asset and liability elements and then assigning the residual to the equity element if the basis is the IASB Framework. However, there are unclear aspects of the framework itself. |
| **Question 4 -- Consolidation of the text in IAS 32 and IAS 39 into one comprehensive Standard**<br>Do you believe it would be useful to integrate the text in IAS 32 and IAS 39 into one comprehensive Standard on the accounting for financial instruments? | .We have no particular reason for opposing coordinated integration into one Standard. However, if additional revisions cannot be avoided in order to integrate the standards, we are opposed to hasty integration and would like to have opportunities established to examine the matter anew and submit |

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| (Although the Board is not proposing such a change in this Exposure Draft, it may consider this possibility in finalising the revised Standards.) | comments. |

**IAS 39**

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| **Question 2 -- Derecognition: continuing involvement approach (paragraphs 35-57)**<br>Do you agree that the proposed continuing involvement approach should be established as the principle for derecognition of financial assets under IAS 39? If not, what approach would you propose? | . We basically support the financial-components approach applied by leading countries at present.<br>. Adoption of a new approach would be a fundamental change in the Standard. Therefore, we feel that it is necessary to examine the matter carefully and thoroughly based on the standpoints of the convenience of financial information users and convergence, while taking into consideration comparisons with the financial-components approach. In addition, it would be essential to institute minute guidance if the new approach were to be adopted. |
| **Question 3 -- Derecognition: pass-through arrangements (paragraph 41)**<br>Do you agree that assets transferred under pass-through arrangements where the cash flows are passed through from one entity to another (such as from a special purpose entity to an investor) should qualify for derecognition based on the conditions set out in paragraph 41 of the Exposure Draft? | . Since this item is preconditioned upon the continuing involvement approach, which is the principal thinking of the derecognition proposed elsewhere, it is related to whether this approach is accepted to begin with. |
| **Question 4 -- Measurement: fair value designation (paragraph 10)**<br>Do you agree that an entity should be permitted to designate any financial instrument irrevocably at initial recognition as an instrument that is measured at fair value with changes in fair value recognised in profit or loss? | . The Exposure Draft states that an entity, by designating the held for trading, measures any financial instrument at initial recognition at fair value with changes in fair value recognised in profit or loss. Therefore, because profits and losses would fluctuate greatly every year, we believe that it would not be possible to "properly indicate business results for a single business year," which is the fundamental purpose of the profit and loss statement.<br>. In addition, if this amendment is accepted, it will ultimately be possible to practice the same accounting as put forth in the JWG Draft. This appears to have the intent of ultimately introducing the JWG Draft into the framework without solving any of the problems, in spite of the many views |

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| | around the world opposing the JWG Draft.<br>.This amendment enables the designation of a financial liability as held for trading and results in the appraisal of the fair value of a financial liability that is designated as belonging to the applicable classification. However, it is believed that if financial liabilities are to be assessed at fair value, they will reflect one's own credit risk in the same way that the JWG Draft proposal does. Because Paragraph 100D of the proposed amendments includes the stipulation "provided there is no change in the credit risk of the debtor after the origination of the debt instrument…," it can be interpreted to mean that the precondition is having the debtor's credit risk reflected in the assessment of liabilities, and this causes concern. |
| **Question 5 -- Fair value measurement considerations paragraphs 95-100D)**<br>Do you agree with the requirements about how to determine fair values that have been included in paragraphs 95---100D of the Exposure Draft? Additional guidance is included in paragraphs A32---A42 of Appendix A. Do you have any suggestions for additional requirements or guidance? | .There is little meaning in making financial instruments with no active market for circulation (or no developed market) a target of fair value appraisal. Since it is believed to be appropriate not to include such instruments for fair value appraisal as held-to-maturity instruments, we do not agree with 100 and 100D of the IASB proposals.<br>.It is believed that the Exposure Draft is based on the perception that it is possible to appraise the fair value of all financial instruments. The LIAJ feels that using valuation techniques for estimates of fair value in cases where there is no active market and including these estimated values in financial statements as fair values will impair the comparability of financial statements. |
| **Question 6 -- Collective evaluation of impairment (paragraphs 112 and 113A--113D)**<br>Do you agree that a loan asset or other financial asset measured at amortised cost that has been individually assessed for impairment and found not to be individually impaired should be included in a group of assets with similar credit risk characteristics that are collectively evaluated for impairment? Do you agree with the methodology for measuring such impairment in paragraphs 113A-113D? | .We can agree with the evaluation of impairment as a group.<br>This is because it is similar to the accounting of general reserves in Japan and the concept can be understood. Also, excluding the claims concerned of individual reserves, we consider it as being virtually the same as the Japanese practice of calculating general reserves and its scope of calculation.<br>However, we do not agree with the methodology for measuring such impairment.<br>This is because the methodology is too complicated and would incur to great a practical burden. It is too complicated to estimate the contingent liabilities category using the procedure of estimating future cash flow on a group-basis |

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| **Question 8 -- Hedges of firm commitments (paragraphs 137 and 140)**<br>Do you agree that a hedge of an unrecognised firm commitment (a fair value exposure) should be accounted for as a fair value hedge instead of a cash flow hedge as it is at present? | .The proposed amendment has a firm commitment accounted for as a fair value hedge. However, when there has been no transfer of spots, which are hedge targets, at the end of the term, spots will not be included in financial statements. However, the portion of a spot whose market price fluctuates is recognised as an asset or liability and the market value portion of a hedge method is recognised as profit or loss. Prior to the amendments, because spots were not included in financial statements, the market values of spots were handled using cash flow hedges in order to prevent them from being reflected in financial statements. Therefore, we do not believe that there is a particular need to change this to a fair value hedge.<br>.Prior to the amendments, both forecasted transactions and firm commitments were cash flow hedges. However, the proposed amendments make firm commitments fair value hedges. Insufficient reason has been presented for carrying out differing accounting in spite of the transactions being of virtually the same type.<br>.We have been told that the amendments are to promote convergence and conform to US accounting standards by taking into consideration the burden on US entities when standards differ. We believe that the thinking concerning hedge accounting should be established first and that preferential consideration should not be given only to conforming to US standards. |
| **Question 9 -- 'Basis adjustments' (paragraph 160)**<br>Do you agree that when a hedged forecast transaction results in an asset or liability, the cumulative gain or loss that had previously been recognised directly in equity should remain in equity and be released from equity | . We believe that when considering the intent of a hedged forecast transaction, which fixes acquisition price, it is unnecessary to change the existing method of including hedge profit or loss in acquisition price. |

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| consistently with the reporting of gains or losses on the hedged asset or liability? | |
| **Question 10 -- Prior derecognition transactions (paragraph 171B)**<br>Do you agree that a financial asset that was derecognised under the previous derecognition requirements in IAS 39 should be recognised as a financial asset on transition to the revised Standard if the asset would not have been derecognised under the revised derecognition requirements (ie that prior derecognition transactions should not be grandfathered)? Alternatively, should prior derecognition transactions be grandfathered and disclosure be required of the balances that would have been recognised had the new requirements been applied? | .It is extremely difficult go back in the past and determine the existence of continuing involvement. Therefore, following the revision it should be unnecessary to recognise as financial assets any past derecognised financial assets.<br>.It should be noted that frequent changes in the basic thinking concerning accounting are not desirable from a practical standpoint. Therefore, we request that there be careful discussion of the issue and active disclosure and explanation of the process and bases of the discussion, not questions based on suppositions. |