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International Accounting Standards Board
30 Cannon Street, 1st Floor
London EC4M 6XH
United Kingdom

Comments on Exposure Draft of Proposed Amendments to
IAS32 and IAS39

Dear Sirs;

We, the Japanese Institute of Certified Public Accountants, are pleased to provide comments on Exposure Draft of Proposed Amendments to IAS 32 *Financial Instruments: Disclosure and Presentation*, and IAS 39 *Financial Instruments: Recognition and Measurement*. Among other things, we disagree with the proposed continuing involvement approach for derecognition of financial asset provision stated in the Exposure Draft of Revised IAS 39.

We do have some specific concerns and recommendations with respect to the proposed amendments, which are discussed below.

IAS 32 ***Financial Instruments: Disclosure and Presentation***

(1) The Exposure Draft provides guidance on the classification of derivatives that relate to an entity's own shares (Question 3 of the Invitation to Comment).

Exposure Draft Paragraph 29F proposes that the equity instrument be reclassified as a financial liability at the share redemption amount when an entity has a written put option on the entity's own shares that requires settlement by the delivery of cash or other financial assets in exchange for receiving the entity's own equity instrument.

This treatment requires not only the premium receipt on a put option to be accounted for as a liability, but also the obligation to purchase the entity's own shares to be initially recognized as a liability at the share redemption amount. However, the exercise of the option is dependent upon the future stock price since the written put option is a conditional obligation to repurchase the entity's own shares. As stated in provisions concerning initial measurement of derivatives in the present IAS 39, a liability for acquisition of the entity's own shares which was reclassified from the shareholders' equity account at the time of initiating such a derivative contract does not meet the definition of a liability. Therefore, we propose that initially, the premium on a written put option be accounted for as a component of shareholders' equity and that acquisition of the treasury stock or redemption of the shares be recognized at the amount of the exercise price at the time of exercise of the option.

Consequently, the table in paragraph B27 should be read as follows:

Accounting treatment of a written put:
Gross physical settlement → E
Issuer choice (past practice of gross physical settlement) → E
Counter party choice → D

(2) Paragraph 29B states that an entity should make disclosures in accordance with IAS 24, *Related Party Disclosures*, if the entity reacquires its own shares from related parties. Since such transaction should be disclosed if IAS 24 is applied, it is unnecessary to provide its disclosure requirement in this paragraph.

IAS 39 *Financial Instruments: Recognition and Measurement*

(1) In the present IAS 39, the concepts of economic risk and reward and control are mixed together for derecognition of financial assets. This makes the application of derecognition criteria for financial instruments difficult. As

pointed out by Paragraph C37 of the Exposure Draft, difficulties exist in applying the control model itself, however, we support this model, which requires the derecognition of financial assets based on the transfer of control over those assets.

On the other hand, the proposed continuing involvement approach prohibits the transferor from derecognizing a financial asset or a portion thereof as long as the transferor continues to be involved with all or a portion of the asset transferred. This is not consistent with the present approach, which is based on concepts that financial assets can be divided into its components and that derecognition is made when there is a surrender of control over financial assets.

We support the control model, separating the economic risk and reward concept from the present approach. Moreover, under the continuing involvement approach, many off-balance-sheet transactions including financial asset securitization, in which there may still be continuing involvement in the form of conditional obligation to return the transferred assets, may be unacceptable and therefore the effect on operations can be significant.

For the above reasons, since the financial component approach adopted by Japan and the United States is consistent with the transfer of control concept, the amendment should follow this basis instead of the continuing involvement approach.

(2) We believe that a financial asset transferred under a pass-through arrangement where cash flows are passed through from one party to another (such as from a special purpose entity to an investor) does not meet the conditions of derecognition of a financial asset.

Derecognition of a financial asset should be discussed only when a transfer of legal title occurs. If not legally transferred, derecognition should be dealt as an offset of assets against liabilities when an entity has a legally enforceable right to set them off.

(3) As per the provision of Exposure Draft Paragraph 10, if any financial instrument can be designated as held for trading when it is initially recognized, it would be classified as a financial instrument held for trading regardless of the entity's

intention, which may be inconsistent with the definition of trading purpose. This allows an entity to designate a financial instrument as held for trading despite the fact that the entity acquired the financial asset with an intention to hold to maturity or as available for sale. The consequence may be inconsistent with the present IAS 39 which requires different accounting treatments for each financial instrument based on the entity's intent to hold.

For instance, even if an entity acquires the same kind of financial assets on different dates with or without the intent to resell in the near future, it could classify them as either held for trading or available for sale. This treatment violates the principle that like transactions and events should be accounted for and reported in a like way as IFRS requires.

In this connection, the provision should continue to allow an entity to either include the change in fair value of financial assets available for sale in shareholders' equity or profit and loss account, after they are stated at fair value.

(4) Exposure Draft Paragraph 160 states that any gains or losses on hedge of a forecast transaction should be reclassified from the shareholders' equity account into profit or loss in the same period during which the hedged asset or liability affected the profit and loss account.

We do not agree with this proposal. The proposed treatment may cause complicated processing the transactions and its effect on the profit or loss is the same as the basis adjustment approach, thus, there is no clear reason to amend the present IAS 39.

(5) Regarding the previously derecognized transactions, Exposure Draft Paragraph 171B requires that a financial asset derecognized under the previous derecognition requirements under IAS 39 be recognized as a financial asset on transition to the revised Standard if the asset would not have been derecognized under the revised derecognition requirements (i.e., that prior derecognition transactions not be grandfathered).

We, however, support the alternative proposal as described in Question 10 in the Invitation to Comment, which states that prior derecognized transactions should be grandfathered and only balance disclosures are required, because re-recognition of financial assets previously derecognized may have excessive burden on the entity's record keeping.

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We would be pleased to discuss any aspect of this letter with the IASB or its staff at your convenience.

Michiyoshi Sakamoto
Chairman
Technical Committee for IASB