Accounting Standards Board of Japan (ASBJ)
Fukoku Seimei Building 20F, 2-2, Uchisaiwaicho 2-chome, Chiyoda-ku, Tokyo 100-0011, Japan
Phone +81-3-5510-2737 Facsimile +81-3-5510-2717 URL http://www.asb.or.jp/

July 15, 2010

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir or Madame,

Comments on the Exposure Draft "Fair Value Option for Financial Liabilities"

We appreciate the efforts of the International Accounting Standards Board (IASB) on the financial instruments project and welcome the opportunity to comment on the Exposure Draft "Fair Value Option for Financial Liabilities" (hereinafter referred to as the "ED"). The views described below are those of the Financial Instruments Technical Committee within the Accounting Standards Board of Japan.

General Comments

1. We generally support the IASB's proposal which would retain existing requirements, except for certain requirements of fair value option (FVO), on classification and measurement of financial liabilities, and which would also present the portion of fair value change that is attributable to changes in the own credit risk of the liability in other comprehensive income (OCI). However, we have some different views on proposed FVO treatment, which are mentioned as follows.

2. Our comments below on FVO assume existing requirements in IAS39 as a starting point of discussion, and also assume existing treatment on hedge accounting etc. We think those issues as to whether there should be FVO and whether its criteria are appropriate should be considered in the context of hedge accounting. IFRS 9 "Financial Instruments" also indicated possible consideration of FVO in the separate phase (see IFRS 9, BC 63).

3. Although it is not mentioned in the questions in the ED, with regard to bifurcation of hybrid financial instruments, we think that the approach that would mitigate

the problems raised by the criterion of "closely related", recognized in IFRS 9, should be explored.

4. Although it is not mentioned in the ED, with regard to cost exception which is considered to be eliminated, we are of the view that fair value with regard to contracts settled by the delivery of an unquoted equity instruments whose fair value cannot reliably be measured does not provide decision useful information, which we had commented on the IASB's exposure draft "Financial Instruments: Classification and Measurement".

<u>Comments on Questions</u>

Our comments on the questions set out in the ED are provided below.

<u>Comment on Question 1</u>

5. On condition that recycling into profit or loss is retained, we agree with the proposal that for all liabilities designated under the FVO their fair value changes attributable to the own credit risk should not affect profit or loss (see also the comment on Question 7). We are of the view that recognizing fair value changes attributable to the own credit risk in profit or loss would not provide useful information except that liabilities are held for trading. However, when an entity applies the FVO to financial instruments that are managed and whose performance is evaluated on a fair value basis, we think that it is appropriate to present the fair value changes including the portion attributable to changes in the own credit risk in profit or loss in order to reflect the substance of entity's management in the financial statements.

<u>Comment on Question 2</u>

6. With regard to the FVO whose condition is to eliminate or significantly reduce a measurement or recognition inconsistency in IAS 39, we have come up with two cases when the accounting mismatch which is attributable to the own credit risk would be offset. One is when a financial liability and a corresponding financial asset have the same credit risk and their credit price itself changes. The other case is when an entity has a financial asset whose price links to the entity's own credit risk. Although we are aware that there are cases in which the value of the financial assets and financial liabilities are linked, most of them seem not

attributable to the own credit risk. Thus, we are of the view that it is very rare that the alternative approach asked in Question 2 is effective, and we do not support this alternative also from the viewpoint of reducing complexity.

Comment on Question 3

7. On condition that recycling to profit or loss is retained, we agree with the proposal that the portion of the fair value changes that is attributable to changes in the own credit risk of liabilities designated under FVO should be presented in OCI. However, we understand the concern in paragraph BC 33 of the ED that the use of OCI should not be expanded until the IASB addresses that issue comprehensively. Even if we agree with the proposal at this moment, we think that the efforts for clarifying the feature of OCI would be necessary in future.

Comment on Question 4 and Question 5

8. We think that the two-step approach provides more disclosure information than one-step approach, while preparation costs are almost the same. This is a cross-cutting issue of financial statement presentation, so we think full deliberation would be necessary.

Comment on Question 6

9. We are of the view that changes in the own credit risk of liabilities are not considered to be transactions with shareholders. We think that such changes should be presented through comprehensive income and should not be included directly in equity.

Comment on Question 7

10. We disagree with the proposal that prohibits recycling from OCI to profit or loss. Profit or loss represents entity's total performance and, when accompanied by comprehensive income, it would provide useful information, so we are of the view that, with respect to financial instruments with changes in fair value through OCI recycling to profit or loss should be retained.
11. Paragraph BC37 of the ED states that one reason for prohibiting recycling is that it is consistent with the Board's view that gains or losses on the liabilities elected for fair value option should be recognised once in the comprehensive income statement. However, we expect the IASB to have a conceptual discussion on the definition of income (profit or loss and comprehensive income) in the future, and, through this

discussion, to make efforts toward gaining consensus among constituents on which items presented as other comprehensive income should be recycled to profit or loss.

Comment on Question 8

12. We agree with the proposal that the guidance in IFRS 7 “Financial Instruments: Disclosures” should be used for determining the amount of the change in fair value that is attributable to changes in liability’s credit risk, on condition that it provides faithful presentation of the amount.

Comment on Question 9

13. We agree with the proposals related to early adoption.

Comment on Question 10

14. We agree with the proposal that is consistent with IFRS 9, which requires retrospective application.

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We expect that our comments will contribute to the forthcoming deliberations in the project.

Yours sincerely,

Atsushi Kato
Chairman of the Financial Instruments Technical Committee
Vice Chairman of the Accounting Standards Board of Japan