

Accounting Standards Board of Japan (ASBJ)

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5 April 2013

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

Dear Sir or Madame,

Comments on the Exposure Draft “Novation of Derivatives and Continuation of Hedge Accounting (Proposed amendments to IAS39 and IFRS9) “

We appreciate the efforts made by the International Accounting Standards Board (IASB) in the Financial Instruments Accounting Project and welcome the opportunity to express our comments on the Exposure Draft on Novation of Derivatives and Continuation of Hedge Accounting (hereinafter referred to as “the ED”). The following views are those of the Financial Instruments Technical Committee within the Accounting Standards Board of Japan.

1. General Comment

1. We believe from the viewpoint of economic substance that accounting for the novation of a derivative to a CCP as a continuation of the hedge relationship, would provide more useful information to users of financial statements. Therefore we basically agree with the IASB’s proposal to provide relief from the discontinuation of hedge accounting in this type of novation, only when certain conditions are met. However, we would like to express our views on the appropriateness of those conditions in our comments to Question 1 and 2.

2. Comments on specific questions

Our comments on the questions set out in the ED are as follows:

Question 1

The IASB proposes to amend IAS 39 so that the novation of a hedging instrument does not cause an entity to discontinue hedge accounting if, and only if, the following conditions are met:

- (i) the novation is required by laws or regulations;

- (ii) the novation results in a central counterparty (sometimes called ‘clearing organisation’ or ‘clearing agency’) becoming the new counterparty to each of the parties to the novated derivative; and
- (iii) the changes to the terms of the novated derivative arising from the novation of the contract to a central counterparty are limited to those that are necessary to effect the terms of the novated derivative. Such changes would be limited to those that are consistent with the terms that would have been expected if the contract had originally been entered into with the central counterparty. These changes include changes in the collateral requirements of the novated derivative as a result of the novation; rights to offset receivables and payables balances with the central counterparty; and charges levied by the central counterparty.

Do you agree with this proposal? If not, why? What criteria would you propose instead, and why?

2. We understand that this initiative will provide accounting relief in response to the change in the regulatory system, which was aimed at achieving the political goal of reducing counterparty risks. We also understand that strict conditions will be imposed to prevent the relief from being abused.
3. It is our understanding that some¹ of the laws or regulations that have been implemented or are in the process of being implemented in each country, state that the novation to a CCP is not required for derivatives entered into prior to the introduction of the regulations or laws (existing derivatives)
4. We have outreached to Japanese constituents on this point, and were informed that some of them who are engaged in derivative transactions would prefer using a CCP for non-mandated existing derivatives as well (i.e. they would like to voluntarily novate existing derivatives to a CCP, where they have received consent from the counterparty to do so) in order to reduce the counterparty risks.
5. In this situation, if the condition (i) “the novation is required by laws or regulations” were imposed as the necessary condition, the relief would not be provided for non-mandatory existing derivatives, although they would be novated to a CCP. Taking note of this situation, Japanese constituents expressed their concern that the accounting relief would become ineffective in practice. We also understand their concern to a certain extent.

¹ For example, this can be said of Japan and USA.

Question2

The IASB proposes to address those novations arising from current changes in legislation or regulation requiring the greater use of central counterparties. To do this it has limited the scope of the proposed amendments to a novation that is *required* by such laws or regulations. Do you agree that the scope of the proposed amendment will provide relief for all novations arising from such legislation or regulations? If not, why not and how would you propose to define the scope?

6. Please refer to our comments to Question 1.

Question3

The IASB also proposes that equivalent amendments to those proposed for IAS 39 be made to the forthcoming chapter on hedge accounting which will be incorporated in IFRS 9 Financial Instruments. The proposed requirements to be included in IFRS 9 are based on the draft requirements of the chapter on hedge accounting, which is published on the IASB's website. Do you agree? Why or why not?

7. This issue would arise in the forthcoming chapter on hedge accounting which will be incorporated in IFRS 9 Financial Instruments, in addition to the existing IAS39. Therefore we agree with the proposal that equivalent amendments to those proposed for IAS 39, be made to the forthcoming chapter on hedge accounting which will be incorporated in IFRS 9 Financial Instruments.

Question4

The IASB considered requiring disclosures when an entity does not discontinue hedge accounting as a result of a novation that meets the criteria of these proposed amendments to IAS 39. However, the IASB decided not to do so in this circumstance for the reason set out in paragraph BC13 of this proposal.

Do you agree? Why or why not?

8. We agree with the proposal for the reason stated in paragraph BC13.

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

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Atsushi Kogasaka', written in a cursive style.

Atsushi Kogasaka

Chairman of the Financial Instruments Technical Committee

Vice Chairman of the Accounting Standards Board of Japan