The LIAJ's Comments on the Exposure Draft Mandatory Effective Date of IFRS 9

21th October 2011

The Life Insurance Association of Japan (LIAJ)

Contents

1. General opinions on the exposure draft

1. With our greatest respect to the continuing efforts of the International Accounting Standards Board (IASB) for financial instrument project, the Life Insurance Association of Japan (LIAJ) would like to extend our gratitude to the Board for providing us with the opportunity to submit our comments on the exposure draft, *Mandatory Effective Date of IFRS 9* (hereinafter referred to as 'the exposure draft'), published in August 2011.

2. The LIAJ is a trade association comprised of all 45 life insurance companies operating in Japan. Its aim is to promote the sound development of the life insurance industry and maintain its reliability in Japan. We would like to respectfully request that the Board carefully consider the comments submitted from the sole representative body of the life insurance industry in Japan, which holds the second largest life insurance market in the world.

1.1 Proposals to ensure appropriate representation of life insurance business

3. Amendments to accounting standards for financial instruments that account for a large part of life insurers' assets and developments of the project for insurance contracts that account for a large part of life insurers' liabilities, would have a great impact on life insurers. Therefore, we believe that all the phases of IFRS 9 including this exposure draft and the insurance contracts project need to be considered in a consistent manner.

4. The nature of life insurance business is to underwrite risks over a long period and requires insurers to firmly fulfil obligations to policyholders, instead of gaining profits through changes in the fair value of financial assets and liabilities they hold. We think financial statements of life insurers should enable users to understand the reality of such business, and we are concerned that recognising in profit or loss 'unrealised gains and losses' such as changes in the fair value of equity instruments held for a long-term would cause misunderstanding among the users. Therefore, even if the financial assets and insurance liabilities are presented at current value in the statement of financial position, we believe that changes in the current value should not be recognised in profit or loss until they are realised, which ensures the consistency between the accounting for financial instruments and insurance contracts.

(Proposals for improvement of IFRS 9)

5. While the FASB currently works on a project to review the accounting for financial instruments, the proposed directions of the IASB and FASB are not necessarily the same. In light of comments the IASB will receive during public consultation on FASB's decisions , we hope that the IASB will redeliberate IFRS 9 *Classification and Measurement.*

6. An accounting standard for classification and measurement of financial assets that account for a large part of life insurers' assets was issued as IFRS 9 *Financial Instruments*. While it is proposed, in this exposure draft, to delay the mandatory effective date of IFRS 9, we believe that a fundamental review is required for IFRS 9, which includes the review of not only the mandatory effective date of IFRS 9 but also the substance of IFRS 9.

7. In particular we'd like to note that, under IFRS 9, although an entity is allowed to make an irrevocable election to present in other comprehensive income (OCI) subsequent changes in the fair value of equity instruments that are not held for trading (i.e. OCI option), such amounts presented in OCI shall not be subsequently recognised in profit or loss. We are concerned that

such treatment under IFRS 9 will alter the fundamental nature of profit or loss. In this context, we believe that the IASB should redeliberate IFRS 9 in line with the following principles so that it can represent the nature of life insurance business in an appropriate manner.

- Under the OCI option, the OCI amounts should be recognised in profit or loss upon realisation.
- The OCI option should be allowed not only for equity instruments, but also for other financial instruments that are not held for trading purposes, and the OCI amounts should be recognised in profit or loss upon realisation.

2. Responses to the questions

2.1 Question 1

The Board proposes to amend IFRS 9 (2009) and IFRS 9 (2010) so that entities would be required to apply them for annual periods beginning on or after 1 January 2015. Do you agree? Why or why not? If not, what alternative do you propose?

<Delaying the mandatory effective date of IFRS 9 from 2013>

[We agree with this part.]

8. In terms of the mandatory effective date of IFRS 9, we believe that it is necessary to avoid an insurer having to face several rounds of major changes in a short period. Therefore, we agree with the proposal to delay the effective date of IFRS 9 from annual periods beginning on or after 1 January 2013.

<Deferring the mandatory effective date of IFRS 9 to 2015>

[We do not agree with this part.]

9. In this exposure draft, it is proposed to defer the mandatory effective date of IFRS 9 to annual periods beginning on or after 1 January 2015. However, the impairment and hedge accounting phases of IFRS 9 and the accounting for insurance contracts still remain under deliberation, and it would be difficult to judge whether the proposed time line is appropriate or not. Therefore, we do not agree with the proposal to defer the mandatory effective date to 2015.

<Maintaining the substance of IFRS 9>

[We do not agree with this part.]

10. In this exposure draft, it is proposed to delay the mandatory effective date of IFRS 9. It does not, however, refer to a possibility of a fundamental review of the substance of IFRS 9. We believe that there are following problems with IFRS 9, and therefore we do not agree with the idea of maintaining the substance of it.

    - It does not appropriately represent the nature of businesses (such as life insurance) which do not aim at gaining profits through changes in the fair value of assets and liabilities they hold.

    - There is a concern that the current IFRS 9 is inconsistent with what has been proposed for the insurance contract project since the exposure draft.

11. We believe that the IASB should redeliberate IFRS 9 to make amendments in line with the following principles, in addition to the proposed delay in the mandatory effective date of IFRS 9.

    - Under the OCI option, the OCI amounts should be recognised in profit or loss upon realisation.
    - The OCI option should be allowed not only for equity instruments, but also for other

financial instruments that are not held for trading purposes, and the OCI amounts should be recognised in profit or loss upon realisation.

2.2 Question 2

The Board proposes not to change the requirement in IFRS 9 for comparatives to be presented for entities that initially apply IFRS 9 for reporting periods beginning on or after 1 January 2012. Do you agree? Why or why not? If not, what alternative do you propose?

[No comment.]