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

Comments on Exposure Draft of Proposed Amendments to IAS 33
"Simplifying Earnings per Share"

Dear Sirs/Madams,

We appreciate the IASB's efforts on the Earnings per Share (EPS) project and welcome the opportunity to provide comments on Exposure Draft of Proposed Amendments to International Accounting Standard (IAS) 33 (the ED), "Simplifying Earnings per Share". The comments are those of the Technical Committee for Earnings per Share of the Accounting Standards Board of Japan.

General Comments

1. We support the underlying idea of the project that converge the difference between existing IAS 33 and Statement of Financial Accounting Standard (SFAS) 128 that could be solved shortly.
2. However, given the liability and equity project that will be completed by 2011, it would be better to consider the EPS project along with the liability and equity project since the outcome of the liability and equity project could substantially affect EPS computation.

Question 1—Mandatorily convertible instruments and instruments issuable for little or no cash or other consideration

Paragraphs 18 and 19 of the exposure draft propose that the weighted average number of ordinary shares should include only instruments that give (or are deemed to give) their holder the right to share currently in profit or loss of the period. If ordinary shares issuable for little or no cash or other consideration or mandatorily convertible instruments do not meet this condition, they will no longer affect basic EPS. (a) Do you agree that the weighted average number of ordinary shares for basic EPS should include only instruments that give (or are deemed to give) their holder the right to share currently in profit or loss of the period? Why or why not?

(b) Does the exposure draft apply this principle correctly to mandatorily convertible instruments and ordinary shares issuable for little or no cash or other consideration? Why or why not?

3. The objective of basic EPS information is to provide a measure of the interests of each ordinary share of a parent entity in the performance of the entity over the reporting period (paragraph 11 of IAS33). Thus, the instruments that are currently not issuable as those shares nor convertible into those shares should not be included in basic EPS computation even if the future issuance or conversion is certain. We agree with the proposal that the weighted average number of ordinary shares for basic EPS should include instruments that give their holder the right to share currently in profit or loss of the period. However, when instruments are deemed to give their holder the right to share currently in profit or loss, the number of shares for basic EPS should be limited to the ordinary shares that are not only currently issuable for little or no cash or other consideration but will also be issued with certainty.
4. Japanese GAAP requires that, for certain convertible shares, the number of shares calculated in accordance with if-converted method should be added to the weighted average number of ordinary shares for basic EPS. This includes shares that have no senior rights to dividend and that have different participation amount from that of another class of ordinary shares which is not predetermined. Since the treatment of these kinds of shares is unclear in existing IAS 33 and the exposure draft, the Board should clarify how to deal with them.

Question 2—Gross physically settled contracts to repurchase an entity's own shares and mandatorily redeemable ordinary shares

Paragraphs A31 and A32 of this exposure draft propose clarifying that an entity treats ordinary shares that are subject to a gross physically settled contract to repurchase its own shares as if the entity had already repurchased the shares.

Therefore, the entity excludes those shares from the denominator of the EPS calculation. To calculate EPS, an entity allocates dividends to the financial liability relating to the present value of the redemption amount of the contract.

Therefore, the liability is a participating instrument and the guidance in paragraphs A23–A28 applies to this instrument. However, such contracts sometimes require the holder to remit back to the entity any dividends paid on the shares to be repurchased. If that is the case, the liability is not a participating instrument.

The Board proposes that the principles for contracts to repurchase an entity's own shares for cash or other financial assets should also apply to mandatorily redeemable ordinary shares.

Do you agree with the proposed treatment of gross physically settled contracts to repurchase an entity's own shares and mandatorily redeemable shares? Why or why not?

5. According to IAS 32, gross physically settled contracts to repurchase an entity's own shares

give rise to a financial liability for the present value of the redemption amount. We are aware that the ordinary shares subject to the contracts are subtracted from the weighted average number of ordinary shares for basic EPS computation in consistent with the above mentioned accounting treatment of IAS 32. We are also aware that the two-class method applies to the instruments since the definition of a participating security is met when dividend is allocated to the instruments.

6. In addition, we agree with applying the similar principle of EPS computation to mandatory redeemable ordinary shares because the accounting treatment of such shares is the same as that of gross physically settled contracts to repurchase an entity's own shares.

Question 3—Instruments that are measured at fair value through profit or loss

For an instrument (or the derivative component of a compound instrument) that is measured at fair value through profit or loss, paragraphs 26 and A28 propose that an entity should not:

(a) adjust the diluted EPS calculation for the assumed exercise or conversion of that instrument; or

(b) apply the guidance for participating instruments and two-class ordinary shares in paragraphs A23–A28.

Do you agree that the fair value changes sufficiently reflect the effect on ordinary equity holders of instruments measured at fair value through profit or loss and that recognising those changes in profit or loss eliminates the need for further adjustments to the calculation of EPS? Why or why not?

7. Though simplifying EPS computation, the proposed method in the ED will lead to inconsistent adjustments for diluted EPS, depending on whether instruments are measured at fair value through profit or loss. Therefore, it would be better that calculation of diluted EPS for the instruments that are measured at fair value through profit or loss is made consistently with those are not.

Question 4—Options, warrants and their equivalents

For the calculation of diluted EPS, an entity assumes the exercise of dilutive options, warrants and their equivalents that are not measured at fair value through profit or loss. Similarly, paragraph 6 of this exposure draft proposes clarifying that to calculate diluted EPS an entity assumes the settlement of forward contracts to sell its own shares, unless the contract is measured at fair value through profit or loss. In addition, the boards propose that the ordinary shares arising from the assumed exercise or settlement of those potential ordinary shares should be regarded as issued at the end-of-period market price, rather than at their average market price during the period.

(a) Do you agree that to calculate diluted EPS an entity should assume the settlement of forward sale contracts on its own shares in the same way as options, warrants and their equivalents? Why or why not?

(b) Do you agree that ordinary shares arising from the assumed exercise or settlement of options, warrants and their equivalents should be regarded as issued at the end-of-period market price? Why or why not?

8. With regard to Question 4(a), we agree to apply the same principles to diluted EPS calculation as those of options, warrants and their equivalents by clarifying the treatment for the settlement of forward sale contracts on its own shares.

9. With regard to Question 4(b), we agree that the ordinary shares arising from the assumed exercise or settlement of those potential ordinary shares should be regarded as issued at the end-of-period market price, rather than at their average market price during the period. Reasons are as follows:
   - As stated in paragraph BC23 of the ED, it would simplify the calculation of diluted EPS;
   - As stated in Exposure Draft of Proposed Amendments to SFAS128, it would allow for consistency by including the end-of-period carrying value of a liability, if applicable, as an assumed proceed; and
   - Users can assess the dilutive effect of potential ordinary shares by the latest market price in the reporting period.

10. We note paragraph BC23 of the ED states that "[t]he use of end-of-period market prices also resolves an inconsistency in IAS33." This reasoning is inappropriate and should be eliminated from the basis for conclusion. This is because the use of average market price is more consistent with the objective of diluted EPS, which is to provide a measure of the interest of each ordinary share in the performance of an entity. Rather, the reasons described in paragraph 9 above should be emphasized in this amendment.

Question 5—Participating instruments and two-class ordinary shares

Paragraph A23 proposes to extend the scope of the application guidance for participating instruments to include participating instruments that are classified as liabilities. In addition, the Board proposes to amend the application guidance for participating instruments and two-class ordinary shares. The proposed application guidance would introduce a test to determine whether a convertible financial instrument would have a more dilutive effect if the application guidance in paragraph A26 and A27 for participating instruments and two-class ordinary shares is applied or if conversion is assumed. The entity would assume the more dilutive treatment for diluted EPS. Also, the amended application guidance would require that, if the test causes an entity to assume conversion of dilutive convertible instruments, diluted EPS should reflect actual dividends for the period. In contrast, diluted EPS would not include dividends that might have been payable had conversion occurred at the beginning of the period.

Do you agree with the proposed amendments to the application guidance for participating instruments and two-class ordinary shares? Why or why not?

11. If the instruments give their holder the right to participate in dividends with ordinary shares according to a predetermined formula, the entity should treat them consistently regardless of whether those instruments are classified as liability or as equity. Therefore, we agree to extend the scope of the application guidance to include participating instruments that are classified as liability.
12. To calculate more dilutive effect for dilutive EPS, we also agree to clarify the treatment of participating instruments.

Question 6—Disclosure requirements

The Board does not propose additional disclosures beyond those disclosures already required in IAS 33.

Are additional disclosures needed? If so, what additional disclosures should be provided and why?

13. We are concerned that proposed treatment of instruments that are measured at fair value through profit or loss does not necessarily reflect the dilutive effect (See paragraph 7 of this comment letter) because fair value could be changed by other factors than dilution. Therefore, if the Board did not reconsider the proposed treatment and decided not to require further adjustments for those instruments in calculating diluted EPS, it would be better to disclose the additional numbers of shares that would have been included in the number of diluted share had the instruments not been reported at fair value through profit or loss and the amount of profit or loss that should be adjusted in the numerator.

We hope that our comments will contribute to the IASB's future deliberation in this project.

Sincerely yours,

Take Arai

Takehiro Arai
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