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The Life Insurance Association of Japan

CL 26

Comments on ED 7 Financial Instruments: Disclosures

Questions	Comments
Question 1 – Disclosures relating to the significance of financial instruments to financial position and performance The draft IFRS incorporates disclosures at present contained in IAS 32 *Financial Instruments: Disclosure and Presentation* so that all disclosures about financial instruments are located in one Standard. It also proposes to add the following disclosure requirements: (a) financial assets and financial liabilities by classification (see paragraphs 10 and BC13). (b) information about any allowance account (see paragraphs 17 and BC14). (c) income statement amounts by classification (see paragraphs 21(a), BC15 and BC16). (d) fee income and expense (see paragraphs 21(d) and BC17). Are these proposals appropriate? If not, why not? What alternative disclosures would you propose?	No comment
Question 2 – Disclosure of the fair value of collateral and other credit enhancements For an entity's exposure to credit risk, the draft IFRS proposes to require disclosure of the fair value of collateral pledged as security and other credit enhancements unless impracticable (see paragraphs 39, 40, BC27 and BC28). Is this proposal appropriate? If not, why not? What, if any, alternative disclosures would you propose to meet the stated objective?	We are opposed to the proposed requirement for disclosure of the fair value of collateral and other credit enhancements. The proposed draft IFRS requires disclosure of the fair value of collateral when it is practicable, while, not requiring it when it is impracticable. However, assuming that judgment of a financial statements preparer varies depending on the situation, it might not be treated uniformly all the time. Furthermore, it is not always considered effective from the standpoints of cost-benefit approach, because it might cause extra administrative work for an entity.

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Question 3 – Disclosure of a sensitivity analysis For an entity that has an exposure to market risk arising from financial instruments, the draft IFRS proposes to require disclosure of a sensitivity analysis (see paragraphs 43, 44 and BC36-BC39). Is the proposed disclosure of a sensitivity analysis practicable for all entities? If not, why not and what, if any, alternative disclosures of market risk would you propose to meet the stated objective of enabling users to evaluate the nature and extent of market risk?	We are opposed to the proposed disclosure of a sensitivity analysis. It is important that the objective and comparable basic data, which is necessary for analyzing the risk arising from financial instruments, is fully disclosed to financial statements users. The proposed disclosure of a sensitivity analysis by draft IFRS is not considered exactly effective for users to conduct comparative analysis from an objective perspective, since it is up to a financial statement preparer to determine the calculation method and variable zone of risk variable. For example, disclosing type of value at risk model (eg. whether the model relies on Monte-Carlo Simulations or not), and major assumptions (e.g. the holding period and confidence level) proposed in IG 35 lack comparability and might provide misleading information. From the standpoints of cost-benefit, it might not be always effective since it causes the burden of extra administrative work for an entity. As for interest rate risk, disclosure of outstanding amounts on maturity or repricing date (disclosing outstanding amounts for a specific period) as proposed in IAS32 might better perform for objective and comparable information. The disclosure of comparable data for users, such as outstanding amounts in a specific type of business, and outstanding amounts in specific currency, should be required for stock price risk, currency risk as well.
Question 4 – Capital disclosures The draft IFRS proposes disclosure of information that enables users of an entity's financial statements to evaluate the nature and extent of its capital. This includes a proposed requirement to disclose qualitative information about the entity's objectives, policies and processes for managing capital; quantitative data about what the entity regards as capital; whether during the period it complied with any capital targets set by management and any externally imposed capital requirements; and if it has not complied, the consequences of such non-compliance (see paragraphs 46-48 and BC45-BC54). Is this proposal appropriate? If not, why not? Should it be limited to only externally imposed capital requirements? What, if any, alternative disclosures would you propose?	The proposal is not applicable to a financial institution under supervision by regulatory authorities. The proposed capital disclosures as part of financial statements rely on the judgment of regulatory authorities whose primary mission is to inspect capital adequacy and financial soundness, which should be handled in a discreet manner when imposed on an entity. Especially, the disclosure of capital requirement externally imposed (especially, by regulatory authorities) should be carried out in light of supervisory regulation of each country. Hence, IFRS should not require the disclosure of such information, including nature of capital, whether an entity compiling with any capital targets or not (if it is not, the consequences of such non-compliance). In addition, IFRS should not require any capital targets set by management to be disclosed for the following reasons. - The capital target set by management is, in many cases, closely related to the one set by supervisory authorities in content. In other words, it contradicts the IFRS

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	(Financial Instrument: Disclosure) which exempt the disclosure of the target imposed by a supervisory authorities from an entity. • Insurers usually set the capital target, by attempting a variety of assumption and premises. Without unified standards of assumption and premises, disclosing capital target and entity's accomplishment lacks comparability among entities, and might mislead the users of financial statements and policyholders. • Capital target is also closely related to valuation of insurance liabilities, comprehensive development of valuation method is scheduled to be considered in Phase.. Therefore, the capital target set at this point might be subject to a significant amendment later, which would cause misunderstanding and confusion for users of financial statements and policyholders.
Question 5 – Effective date and transition The proposed effective date is for periods beginning on or after 1 January 2007 with earlier adoption encouraged (see paragraphs 49 and BC62-BC67). Entities adopting IFRSs and the draft IFRS for the first time before 1 January 2006 would be exempt from providing comparative disclosures for the draft IFRS in the first year of adoption (see Appendix B, paragraph B9). Are the proposed effective date and transition requirements appropriate? If not, why not? What alternative would you propose?	No comment

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Question 6 – Location of disclosures of risks arising from financial instruments The disclosure of risks arising from financial instruments proposed by the draft IFRS would be part of the financial statements prepared in accordance with International Financial Reporting Standards (see paragraph BC41). Some believe that disclosures about risks should not be part of financial statements prepared in accordance with IFRSs; rather they should be part of the information provided by management outside the financial statements. Do you agree that the disclosures proposed by the draft IFRS should be part of the financial statements? If not, why not?	We are opposed to disclosing risks arising from financial instrument as a part of financial statements. IFRS provides that internal information submitted to management shall be used as risk information. However, this type of information reflects only management policy, and risk management policy of each entity. In addition, the standards of objectivity and continuity required differ from the ones for financial statements, therefore, it should be handled apart from financial statements. Disclosure of risks arising from financial instrument is not always the useful information for users, and highly likely to impose a burdensome load of work on a financial statement preparer. Furthermore, since most of risk information is beyond the capacity of financial statements, in some cases, it does not properly fit into the scope of an accounting audit. Therefore, we consider that each entity should assume its responsibility through explanation by dialogue with stakeholders. Especially, for financial institutions, most of the risks arising from financial instrument coincide with operational risk whose definition and measurement are in its infancy as quoted in paragraph BC40. Hence, the disclosure of risk arising from financial instrument should be discussed along with the disclosure of operational risk in other research projects, not in ED 7 project.
Question 7 – Consequential amendments to IFRS 4 (paragraph B10 of Appendix B) Paragraph B10 of Appendix B proposes amendments to the risk disclosures in IFRS 4 *Insurance Contracts* to make them consistent with the requirements proposed in the draft IFRS. The requirements in IFRS 4 were based on disclosure requirements in IAS 32 that would be amended by the draft IFRS. The Board's reasons for proposing these amendments are set out in paragraphs BC57-BC61. Do you agree that the risk disclosures in IFRS 4 should be amended to make them consistent with the requirements proposed in the draft IFRS? If not, why not and what amendments would you make pending the outcome of phase II of the Board's Insurance project?	We are opposed to amending risk disclosure requirements in IFRS 4. The standards for judgment on insurance contract, which substantially affect the disclosure requirement, are not finalized yet, and expected to reach a conclusion in Phase .of the Insurance Project. Therefore, we could make only the minimum essential change to IFRS 4 (such as amending cross-references to IAS 32) at this point. It is appropriate that it, if necessary, should be reviewed in Phase . of the Insurance Project.

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Question 8 – Implementation Guidance The draft Implementation Guidance accompanying the draft IFRS suggests possible ways to apply the risk disclosure requirements in paragraphs 32-45 (see paragraphs BC19, BC20 and BC42-BC44). Is the Implementation Guidance sufficient? If not, what additional guidance would you propose?	It is a concern that the part of the examples illustrated in the Implementation Guidance might cause misunderstanding for users, if disclosed, therefore it is not appropriate to do so. Concerning the disclosure of quantitative data about concentration of risk as quoted in IG9 (b), the existing exposure which concentrate at a financial institution of specific credibility is said to be the cause for a problem. However, if the risk is adequately diversified over the credibility at the same level, there should be no concentration of risk issues. If absolute credibility is low under the same circumstance, it is not considered rather a matter of credit risk, than concentration of risk, therefore, the examples shown in the Implementation Guidance should be deleted. As for the disclosure of additional information illustrated in IG44 (c), entity's large holding of financial assets, exceeding 15 % of company stocks, is, in most cases, for a company strategy. It is highly improbable that the entity sells them all at once, unless it faces liquidity crisis. Therefore, the examples should be exclusively applied to trading account or completely deleted.
Question 9 – Differences from the Exposure Draft of Proposed Statement of Financial Accounting Standards *Fair Value Measurements* published by the US Financial Accounting Standards Board (FASB). The FASB's Proposed Statement of Financial Accounting Standards *Fair Value Measurements*, which is open for public comment at the same time as this Exposure Draft, proposes guidance on how to measure fair value that would apply broadly to financial and non-financial assets and liabilities that are measured at fair value in accordance with other FASB pronouncements. That Exposure Draft proposes disclosure of information about the use of fair value in measuring assets and liabilities as follows: (a) For assets and liabilities that are remeasured at fair value on a recurring (or ongoing) basis during the period (for example, trading securities) (i) the fair value amounts at the end of the period, in total and as a percentage of total assets and liabilities, (ii) how those fair value amounts were determined (whether based on quoted prices in active markets or on the results of other valuation techniques, indicating the extent to which market inputs were used), and (iii) the effect of the remeasurements on earnings for the period	No comment

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(unrealised gains or losses) relating to those assets and liabilities still held at the reporting date. (b) For assets and liabilities that are remeasured at fair value on a non-recurring (or periodic) basis during the period (for example, impaired assets), a description of (i) the reason for remeasurements, (ii) the fair value amounts, (iii) how those fair value amounts were determined (whether based on quoted prices in active markets or on the results of other valuation techniques, indicating the extent to which market inputs were used), and (iv) the effect of the remeasurements on earnings for the period relating to those assets and liabilities still held at the reporting date. Disclosures similar to (a)(ii) above are proposed in paragraph 31 of the draft IFRS (and are currently required by paragraph 92 of IAS 32) and disclosures similar to (a)(iii) are proposed in paragraph 21(a). Do you agree that the requirements in the draft IFRS provide adequate disclosure of fair value compared with those proposed in the FASB's Exposure Draft? If not, why not, and what changes to the draft IFRS would you propose?	
Question 10 – Other comments Do you have any other comments on the draft IFRS, Implementation Guidance and Illustrative Examples?	No comment