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15 October 2010

Exposure Draft 'Proposed Accounting Standards Update-Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities'
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Dear Sir or Madam:

The Korea Accounting Institute(KAI) has finalized its comments on exposure draft 'Proposed Accounting Standards Update-Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities'. I would appreciate your including our comments in your summary of analysis.

The enclosed comments represent opinions of the KAI. They have been determined after extensive due process and deliberation.

Please do not hesitate to contact us if you have any inquiries regarding our comments. You may direct your inquiries either to me (cwsuh@kasb.or.kr) or to Mr. Won-hee Han (hanster@kasb.or.kr), senior researcher of KAI.

Yours sincerely,



Dr. Chungwoo Suh
Chairman, Korea Accounting Standards Board

Cc: Sungsoo Kwon, Director of Research Department

We are pleased to comment on exposure draft 'Proposed Accounting Standards Update-Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities'. Our comments include views from local constituents. We finalized the comment letter through the due process established in KAI.

(1) Scope

Overall comment

- We believe it is more appropriate to not exclude the loan commitment related to a revolving line of credit issued under a credit card arrangement from the application scope. The loan commitment related to the credit card is composed of many small amounts so that excluding from the application scope due to difficulty in practical accounting treatment of fair value assessment or measurement lacks fairness when compared to other contractual relationships. Moreover, since many small amount loan commitments can exist other than credit card related, allowing the exception of a particular industry's particular type of loan commitment is not appropriate.
- However, some agreed that the circumstances where it is composed of various bonds of small amounts and continuously revolving loan commitment should be excluded from the ED's application scope. The reason was the above circumstances are possible to happen in bank's individual credit or other loan commitments. Thus, the only exclusion on credit card commitment is not appropriate.
- There needs to be a review on the difference between the loan commitment and debt underwriting commitment. Both commitments are to provide credit per GAAP and they are both forward/option transactions which financial assets (cash and debt) are the objects. Therefore, according to the results of whether the objects are the regular way transaction and whether there is the possibility of encashment, it would to be reviewed whether the definition of derivative instruments is satisfied or not. The loan commitment is the main

transactions of financial institutions so that its nature may be considered as separate discussion topic. However there needs to be clarifications on difference between the loan commitment and other derivative instruments.

Question 3: The proposed guidance would require deposit-type and investment contracts of insurance and other entities to be measured at fair value. Do you agree that deposit-type and investment contracts should be included in the scope? If not, why?

We agree

Question 4: The proposed guidance would require an entity to not only determine if they have significant influence over the investee as described currently in Topic 323 on accounting for equity method investments and joint ventures but also to determine if the operations of the investee are related to the entity's consolidated business to qualify for the equity method of accounting. Do you agree with this proposed change to the criteria for equity method of accounting? If not, why?

We agree. We believe it is appropriate to determine if the operations are related when deciding the qualification of the equity method. We believe that explaining which circumstances cannot be 'related' in addition to the current examples of 'related' which is suggested will help the operational application.

Question 5: The proposed guidance would require financial liabilities of investment companies to be measured at fair value with changes in fair value recognized as a net increase (decrease) in net assets. Do you believe that the effect on net asset value will provide decision-useful information? If yes, how will the information provided influence your analysis of the entity? If not, why?

It provides useful information.

Question 7: The proposed guidance would require brokers and dealers in securities to apply the proposed guidance for measuring financial liabilities, which could mean that qualifying changes in fair value would be recognized in other comprehensive

income. Do you believe that this will provide decision-useful information? If yes, how will the information provided influence your analysis of the entity? If not, why?

- We believe it is proper to regulate the subsequent measurement accounting of brokers or dealer's financial assets and liabilities in consistent manner.**

- When fair value of broker and dealer's financial liabilities are recognized in other comprehensive income, there is mismatch in accounting. As a result, it is difficult to say that it provides useful information to the financial statements' users.**

(2) Initial Measurement

Overall comment

- We disagree with the classification of FV-NI and FV-OCI

- We understand that the FASB suggests the classification of FV-OCI as a result of accepting the criticism for full fair value model (i.e. all changes in fair value is recognised in profit or loss), although the ultimate objective is to adopt full fair value model as a single measurement attribute. We also recognise that measuring the items at fair value under the FV-OCI classification will provide timely information that would not be provided under amortised cost measurement. However, this classification method has following problems of not reducing the complexity of accounting treatment which the interested parties raised through the financial crisis.
 - FV-OCI classification increases complexity in classifications. (e.g. some financial liabilities under FV-OCI classification are allowed to be measured at amortised cost when certain criteria are met.)
 - It brings more complexity on the income statement since among the change in profit and loss of FV-OCI items some portions (e.g. interest income, impairment loss) are recognized in profit and loss and the rest is recognized in the OCI.
 - It increases unnecessary volatility in OCI for held-to-maturity financial instruments

- As a result, unless the FASB adopts full-fair value measurement system, we believe it is more appropriate to consider consistency as more important. For example, if IASB's IFRS 9 model is to be followed, for the financial instruments for which the changes in fair value are recognised in OCI, all changes in gains or losses (except for dividends) are recognized in OCI. Thus, In this model, there would be no split of

recognising some changes in fair value in profit or loss and other changes in OCI.

- We do not believe that it is appropriate to require different measurements attributes of fair value and transaction price depending on classification because it lacks of theoretical grounds and would increase complexity in practice.**
- We thus believe for initial measurement it is appropriate to measure all financial instruments at fair value regardless of classification.**
- If the FASB retains the dual initial measurement models, we suggest that the accounting treatment for the difference of transaction price and fair value should be consistent both for FV-OCI and FV-NI.**
- Also, the detail guidances are necessary for determining whether the difference between transaction price and fair value is significant and whether there is reliable evidence.**
- On the other hand, One external party agreed with the FASB's initial measurement principle.**
- It reasons that single initial measurement attribute would be inconsistent with different subsequent measurement attributes depending on FV-NI and FV-OCI classifications.**
- For example, if FV-OCI is initially measured at fair value as required for FV-NI, then the difference between transaction price and fair value would be recognised in profit or loss, but not in OCI. Thus it is inconsistent with FV-OCI classification principle that requires all changes in fair value to be recognised in OCI.**

(3) Subsequent Measurement

Overall comment

- We disagree with the classification of FI-OCI as mentioned in our comment for initial measurement
- We believe it is more proper to classify financial instruments as FV-NI and amortized cost.
- Therefore, it would be more proper to measure all financial liabilities at fair value only when an entity designates the financial liabilities as held-for trading or FV-NI rather than to require qualifying financial liabilities to be measured at amortised cost. Instead it would be necessary to require an entity to disclose fair value information for amortised cost financial items.
- We disagree with measuring core deposits at remeasurement amount for the following reasons.
 - Although we acknowledge that core deposit is one the key business drivers of financial institutions and the users may thus want the financial statements which show the core deposit at remeasurement amount, the introduction of new measurement attribute only for core deposit liability is inappropriate.
 - Core deposit being intangible asset related to deposit, recognising core deposit at remeasurement amount is similar to recognise good will without business combination. The information of remeasurement amount may be useful to an entity's risk management purpose and the investors. Thus such information can be required as disclosure. However, we do not believe such information should be recognised on the face of the financial statements and moreover the recognised amount would not meet the definition of liability.

● **A great deal of subjective information required for calculation of core deposit liability would undermine the reliability of financial statements.**

- We disagree with the exception of measuring certain investments at redemption value. Since the redemption value is the approximation of fair value as mentioned in BC148, it would suffice to require the certain investments to be measured at fair value, mentioning in guidance that redemption value for those certain investments can approximate fair value.**
- Considering the convergence of IFRS and US GAAP, it seems inappropriate to mention specialized industry. This is because the definition of investment company, broker or dealer may differ by individual countries. Furthermore, to improve comparability between companies, it would not be appropriate to make exceptions to certain industry.**
- The exception for the short-term receivables or investments that can be redeemed only for a specified amount are not appropriate. Such exception would increase complexity in terms of measurement attribute and subjective judgement is necessary to determine the scope of application. Furthermore, measuring these receivables or investments at fair value would result in the similar amount to amortised cost or redemption value.**
- In the case that the proposed amendment is finalised as it is, it would be necessary to add requirement on how to recognise gains or losses arising from the changes of measuring qualified financial liabilities, demand deposit, or the investments that can be redeemed only for a specified amount. For example, the exposure draft does not state whether the changes from measuring core deposit at remeasurement amount should be recognised in profit or loss, OCI or other category.**

It would be difficult to determine whether the criteria in paragraph 28.b are met and, especially, '50% rule' would be hard to apply. There need to be further study to

assess the benefits and difficulties in practice. Although we agree that financial liabilities that meet the criteria in paragraph 28.b should be measured at amortised cost, it is questionable why financial liabilities that meet the criteria in paragraph 28.a but does not meet 28.b should be prohibited to be measured at amortised cost.

Question 13: The Board believes that both fair value information and amortized cost information should be provided for financial instruments an entity intends to hold for collection or payment(s) of contractual cash flows. Most Board members believe that this information should be provided in the totals on the face of the financial statements with changes in fair value recognized in reported stockholders' equity as a net increase (decrease) in net assets. Some Board members believe fair value should be presented parenthetically in the statement of financial position. The basis for conclusions and the alternative views describe the reasons for those views. Do you believe the default measurement attribute for financial instruments should be fair value? If not, why? Do you believe that certain financial instruments should be measured using a different measurement attribute? If so, why?

In principle, we disagree to measure all financial instruments at fair value. Since usefulness of fair value information of financial instruments depends heavily on the reliability of market data, reliable fair value information can only be produced in developed markets where markets are active and quoted price information can be easily obtained. Furthermore bond market is relatively inactive compared to stock market in terms of size or transaction volume.

Therefore, it would be desirable to measure only the financial instruments for which objective quoted price is obtainable whereas the other financial instruments need to be measured at amortised cost until infrastructures of the markets are fully developed.

Question 16: The proposed guidance would require an entity to decide whether to measure a financial instrument at fair value with all changes in fair value recognized in net income, at fair value with qualifying changes in fair value recognized in other comprehensive income, or at amortized cost (for certain financial liabilities) at initial recognition. The proposed

guidance would prohibit an entity from subsequently changing that decision. Do you agree that reclassifications should be prohibited? If not, in which circumstances do you believe that reclassifications should be permitted or required? Why?

We believe that reclassification should be required when business model for managing financial instruments is changed as required in IFRS 9.

Question 17: The proposed guidance would require an entity to measure its core deposit liabilities at the present value of the average core deposit amount discounted at the difference between the alternative funds rate and the all-in-cost-to-service rate over the implied maturity of the deposits. Do you believe that this remeasurement approach is appropriate? If not, why? Do you believe that the remeasurement amount should be disclosed in the notes to the financial statements rather than presented on the face of the financial statements? Why or why not?

We disagree with introducing the remeasurement method on the core deposit liabilities. We believe it is proper to measure core deposit liabilities at in amortized cost. Remeasurement method is an introduction of another measurement attribute other than fair value and amortised cost and is thus inconsistent with the objective of simplifying measurements of financial instruments. Furthermore, The fact that judgement differs from company to company on whether the liability is core deposit liability and what the alternative funding sources are may undermine consistency of accounting treatments. The effects of interest rate on core deposit liability can be effectively conveyed by disclosure information.

Question 19: Do you believe that the correct financial instruments are captured by the criteria in the proposed guidance to qualify for measurement at the redemption amount for certain investments that can be redeemed only for a specified amount (such as an investment in the stock of the Federal Home Loan Bank or an investment in the Federal Reserve Bank)? If not, are there any financial instruments that should qualify but do not meet the criteria? Why?

- We believe that certain investments that can be redeemed only for a specified amount should be required to be measured at fair value and measurement at redemption value should be permitted only when obtaining fair value is difficult.**

Question 20: Do you agree that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to a debt instrument measured at fair value with qualifying changes in fair value recognized in other comprehensive income in combination with other deferred tax assets of the entity (rather than segregated and analyzed separately)? If not, why?

- We agree.**

Question 21: The Proposed Implementation Guidance section of this proposed Update provides an example to illustrate the application of the subsequent measurement guidance to convertible debt (Example 10). The Board currently has a project on its technical agenda on financial instruments with characteristics of equity. That project will determine the classification for convertible debt from the issuer's perspective and whether convertible debt should continue to be classified as a liability in its entirety or whether the Board should require bifurcation into a liability component and an equity component. However, based on existing U.S. GAAP, the Board believes that convertible debt would not meet the criterion for a debt instrument under paragraph 21(a)(1) to qualify for changes in fair value to be recognized in other comprehensive income because the principal will not be returned to the creditor (investor) at maturity or other settlement. Do you agree with the Board's application of the proposed subsequent measurement guidance to convertible debt? If not, why?

- We disagree with the proposed subsequent measurement guidance to convertible debt. According to the tentative decision by the IASB and the FASB on the project of financial instrument with characteristics of equity, there could be a change that convertible debt is separated into liability component and equity component. In that case, the proposed amendment that requires convertible debt to be measured at fair value in entirety would be inconsistent with that change. Thus, it would be proper to**

amend the subsequent measurement as to convertible debt after finalisation of the project on financial instrument with characteristics of equity.

Question 24: The proposed guidance would provide amortized cost and fair value information on the face of the financial statements. The Board believes that this would increase the likelihood that both measures are available to users of public entity financial statements on a timely basis and that both measures are given equal attention by preparers and auditors. Do you believe that this approach will provide decision-useful information? If yes, how will the information provided be used in the analysis of an entity? If not, would you recommend another approach (for example, supplemental fair value financial statements in the notes to the financial statements or dual financial statements)?

We do not believe that provision of amortised cost and fair value information on the face of the financial statements is not an appropriate proposal for the following reasons.

First, requiring only debt financial instrument to be presented with the information of two measurement attributes lacks consistency with other assets which are presented with a single attribute. Second, providing excessive information may cause confusion to the users of financial statements in decision-making.

Moreover, providing excessive information will result confusion to the accounting information users in their decision makings.

Question 25: For hybrid financial instruments that currently would require bifurcation and separate accounting under Subtopic 815-15, do you agree that recognizing the entire change in fair value in net income results in more decision-useful information than requiring the embedded derivative to be bifurcated and accounted for separately from the host contract? If yes, how will the information provided be used in the analysis of an entity? If not, for which types of hybrid financial instruments do you believe that it is more decision useful to account for the embedded derivative separately from the host contract? Why?

We agree.

Question 26: IFRS 9 requires hybrid financial assets to be classified in their entirety on the basis of the overall classification approach for financial assets with specific guidance for applying the classification approach to investments in contractually linked instruments that create concentrations of credit risk. Also, for hybrid financial liabilities, the IASB, in order to address the effects of changes in the credit risk of a liability, tentatively has decided to retain existing guidance that requires embedded derivatives to be bifurcated and accounted for separately from a host liability contract if particular conditions are met. Do you believe that the proposed guidance for hybrid financial instruments or the IASB's model for accounting for financial hybrid contracts will provide more decision-useful information? Why?

We agree.

Question 27: Do you believe that measuring certain short-term receivables and payables at amortized cost (plus or minus any fair value hedging adjustments) will provide decision-useful information? If yes, how will the information provided be used in your analysis of an entity? If not, why?

We agree.

(4) Presentation

Overall comment

- In order to improve global comparability, IFRS and US-GAAP need to be matched on the scope of financial liability whose credit risk change should be separately presented, presentation on change attributable to the credit risk, the measurement on the change attributable to the credit risk and whether to recycle the accumulated amount due to change of credit risk from OCI to profit or loss.
- In principle, KAI believes, for financial liabilities that apply the fair value option, the change in fair value due to the change in credit risk is not appropriate to be applied in profit or loss. The reasons are to be followed:
 - Even though the credit risk increased due to the companies' aggravated financial status, recognition in profit is contradicting with the intuition. Thus, this can mislead the financial statements' users.
 - For financial liabilities (not held for trading purpose), there is low possibility on occurrence of this kind of profit or loss. Therefore, the recognition of change in fair value of financial liability due to the change in credit risk does not necessarily provide useful information to the financial statements' users.
- However, if for the financial assets, the fair value option is selected and all changes of fair value are recognized in profit or loss and if in order to prevent mismatch in profit or loss, financial liabilities is designated under fair value option, then, the effects of changes in the credit risk of liabilities should also be recognized in profit of loss as well.
- However, few views that the loaner's change in self credit rating is irrelevant to the market conditions like the interest rate, thus it is difficult to say it has direct

relationship with the accounting mismatch.

- In order to require separately presenting the effects of changes in credit risk of liabilities measured in fair value, the change in fair value due to the change in credit risk should be able to be measured with reliability and the comparability between companies should be improved.**

- When the root purpose of the liabilities' change in fair value due to change in credit risk are recognized in OCI is considered and if practicality of change in fair value due to the change in credit risk is low, the reasons of need to classify whether the price of credit can be realized or whether there are actual profit in classifying the price of credit should be provided. On statement of comprehensive income, requiring the company to separately present the effects of changes in its own credit level makes the statement of comprehensive income difficult. We believe that presenting it on the footnote is good enough as an investment information. In addition, the classification method of the company's change effect on own credit level, except for the change in price of credit, may be arbitrary. Thus if above information is needed, we believe it is proper to be noted in footnote with its method.**

- IASB does not require recycling the accumulated OCI due to the effects of changes in credit risk in profit or loss. On the other hand, FASB requires all of the OCI to be recycled in the profit or loss. KAI is concerned of expanding the items which are to be recognized in the OCI because there is no definition of the characteristics of OCI and there are no comprehensive reviews on what kind of items are to be recognized in OCI and what the meaning of recycling is.**

- Therefore, after a review on this matter is performed, there has to be an agreement whether to recycle the accumulated OCI due to the effects of changes in credit risk in profit or loss.**

Question 35: For financial instruments measured at fair value with qualifying changes in fair value recognized in other comprehensive income, do you believe that the presentation of amortized cost, the allowance for credit losses (for financial assets), the amount needed to

reconcile amortized cost less the allowance for credit losses to fair value, and fair value on the face of the statement of financial position will provide decision-useful information? If yes, how will the information provided be used in your analysis of an entity? If not, why?

Please refer to our comment on the question 24.

(5) Credit Impairment of Financial Assets

Overall comment

We agree with FASB's proposed impairment model in principle.

● The existing impairment model requires the trigger event (or threshold) as impairment loss recognition requirements. However, due to this, delayed recognition on impairment loss and problem on management's arbitrary impairment loss were caused. We believe that the FASB's proposed impairment model eliminates the trigger event on the recognition requirements of impairment loss so that will ameliorate above problems.

● We believe the FASB's impairment model, which only applies the past or present usable information when forecasting future cash flow, provides clearer standard than IASB's expected loss model in regard to forecasting the future cash flows.

● FASB's impairment model, which recognizes impairment loss in a separate profit or loss item compared to the interest income, will appropriately apply the financial institutions' operational method* and will increase understandability of financial statements' users.

* Generally, financial institutions don't manage credit risks in relation to revenue recognition.

● We agree with the FASB's impairment model which immediately recognizes the impairment loss in profit or loss. IASB's expected loss model recognizes the projected expected credit loss at initial recognition through allocation over the continuing term and the subsequent change in expected credit loss is recognized in profit and loss; thus, it is inconsistent on recognition impairment loss. Moreover,

from accrual basis perspective, it is appropriate to recognize the credit impairment (impairment loss) at the time of occurrence. In addition, applying the IASB's expected loss model will burden companies' operations since additional cost of investment system will be caused due to recognizing the impairment loss in connection with the interest income.

However, we wish to note on the following:

- For the purchased financial assets (purchase with deduction of discounted price related to credit loss), if forecasted collectable cash amount in future exceeds the estimated amount at the time of purchase, requiring progressive recalculation of effective interest rate will greatly burden the companies' operations who possess many purchased financial assets.

Among the external review opinions, the followings are the opinions which support the IASB's impairment model.

- According to the FASB's proposed impairment model, the effective interest rate of newly acquired financial instruments or non-impaired purchased financial assets are the reconciling interest rate of the contractual cash flow with the initial recognized amount. Thus, according to the above statement, right after the recognition (day 2), the projected impairment losses on kinds of financial instruments are immediately recognized. This notes the IASB's expected loss model is applied in expected loss of initial effective interest rate. This is contrasting between the ISAB's expected loss model which requires applying the expected loss on the initial effective interest rate, so that the impairment is only recognized when the expected cash flow is changed after the initial recognition. However, there is no clarity on FASB's impairment model on details regarding the recognition of impairment loss after the initial recognition. Thus, FASB needs to clarify on this.

- **There is no theoretical consistency between measuring the effective interest rate with contractual cash flow basis for the originated financial instruments and measuring the effective interest rate with the forecasted cash flow basis for impaired purchased financial assets. Consequently, the effective interest rate should be calculated with the projected cash flow basis.**

- **Moreover, the loss related to credit rating of purchased financial assets are to be classified, however on purchase of a particular financial instrument, the basis whether to include the loss related to credit rating may be unclear.**

Question 37: Do you believe that the objective of the credit impairment model in this proposed Update is clear? If not, what objective would you propose and why?

We believe it is clear.

Question 38: The proposed guidance would require an entity to recognize a credit impairment immediately in net income when the entity does not expect to collect all contractual amounts due for originated financial asset(s) and all amounts originally expected to be collected for purchased financial asset(s).

The IASB Exposure Draft, Financial Instruments: Amortised Cost and Impairment (Exposure Draft on impairment), would require an entity to forecast credit losses upon acquisition and allocate a portion of the initially expected credit losses to each reporting period as a reduction in interest income by using the effective interest rate method. Thus, initially expected credit losses would be recorded over the life of the financial asset as a reduction in interest income. If an entity revises its estimate of cash flows, the entity would adjust the carrying amount (amortized cost) of the financial asset and immediately recognize the amount of the adjustment in net income as an impairment gain or loss.

Do you believe that an entity should immediately recognize a credit impairment in net income when an entity does not expect to collect all contractual amounts due for originated financial asset(s) and all amounts originally expected to be collected for purchased financial

asset(s) as proposed in this Update, or do you believe that an entity should recognize initially expected credit losses over the life of the financial instrument as a reduction in interest income, as proposed in the IASB Exposure Draft on impairment?

We agree. Please refer to the overall comment.

Question 39: Do you agree that a credit impairment should not result from a decline in cash flows expected to be collected due to changes in foreign exchange rates, changes in expected prepayments, or changes in a variable interest rate? If not, why?

We agree. Changes in foreign exchange rates, changes in expected prepayments, or changes in a variable interest rate do not relate to credit impairment. Thus, when assessing the credit impairment, the above should not be considered.

Question 40: For a financial asset evaluated in a pool, the proposed guidance does not specify a particular methodology to be applied by individual entities for determining historical loss rates. Should a specific method be prescribed for determining historical loss rates? If yes, what specific method would you recommend and why?

We believe the particular methodologies for historical loss rates are not necessary since the calculation method can defer due to various industries' operational environment. However, providing special examples in order to increase the understandability of companies which should use the rates can be considered.

Question 41: Do you agree that if an entity subsequently expects to collect more cash flows than originally expected to be collected for a purchased financial asset, the entity should recognize no immediate gain in net income but should adjust the effective interest rate so that the additional cash flows are recognized as an increase in interest income over the remaining life of the financial asset? If not, why?

We disagree. Please refer to the overall comments for the reasons.

- Among the part of accepted review comments by KASB, there were opinions to support the adjustment of the effective interest rate.**

Question 42: If a financial asset that is evaluated for impairment on an individual basis has no indicators of being individually impaired, the proposed guidance would require an entity to determine whether assessing the financial asset together with other financial assets that have similar characteristics indicates that a credit impairment exists. The amount of the credit impairment, if any, would be measured by applying the historical loss rate (adjusted for existing economic factors and conditions) applicable to the group of similar financial assets to the individual financial asset. Do you agree with this requirement? If not, why?

- We agree. We believe above requirements are necessary in order to prevent intentionally delaying the recognition of impairment loss.**

Question 43: The credit impairment model in this proposed Update would remove the probable threshold. Thus, an entity would no longer wait until a credit loss is probable to recognize a credit impairment. An entity would be required to recognize a credit impairment immediately in net income when an entity does not expect to collect all of the contractual cash flows (or, for purchased financial assets, the amount originally expected). This will result in credit impairments being recognized earlier than they are under existing U.S. GAAP. Do you believe that removing the probable threshold so that credit impairments are recognized earlier provides more decision-useful information?

- We agree.**

Question 44: The proposed guidance would require that in determining whether a credit impairment exists, an entity consider all available information relating to past events and existing conditions and their implications for the collectibility of the cash flows attributable to the financial asset(s) at the date of the financial statements. An entity would assume that the economic conditions existing at the end of the reporting period would remain unchanged for the remaining life of the financial asset(s) and would not forecast future events or economic conditions that did not exist at the reporting date. In contrast, the IASB Exposure

Draft on impairment proposes an expected loss approach and would require an entity to estimate credit losses on the basis of probability-weighted possible outcomes.

Do you agree that an entity should assume that economic conditions existing at the reporting date would remain unchanged in determining whether a credit impairment exists, or do you believe that an expected loss approach that would include forecasting future events or economic conditions that did not exist at the end of the reporting period would provide more decision-useful information?

According to the domestic external review opinions accepted by KAI, some asserted that it is necessary to consider the reasonably forecasted future events or economic volatility when deciding whether to recognize the impairment loss. The reasons are followed below.

- **According to the FASB's proposed model, it is difficult to apply as detailed standard since it is not easy to eliminate the forecasted future events when deciding whether to recognize the impairment loss.**
- **The FASB's proposed model replaced is not consistent with the policy of the standard on assessing the impairment loss, thus, it is difficult to achieve ED's object of recognizing the impairment loss early than the current policy.**
- **Removing the standard of assessing the impairment loss is the concept of expected loss model which requires to recognize the credit loss irrelevant to the loss event . On the other hand, the requirement of not considering the forecasted future events when recognizing the loss is the concept of accrual basis model.**

Question 45: The proposed guidance would require that an appropriate historical loss rate (adjusted for existing economic factors and conditions) be determined for each individual pool of similar financial assets. Historical loss rates would reflect cash flows that the entity does not expect to collect over the life of the financial assets in the pool. Do you agree with that approach?

We agree.

(6) Measuring Interest Income on Debt Instruments Held

Overall comment

- We overall agree with FASB's proposal on policies of measuring interest income. However we disagree on adjusting effective interest rate, the rationales for our opinion is explained on overall comment(p.28) of 'credit impairment of financial assets.'

- FASB's impairment model defines the effective interest rate as the interest rate that equals contractual cash flows with the initial cash payment. According to above statement, the floating rate instruments have inconvenience of managing all of past interest payments as the ED's paragraph 67 had mentioned as well. We believe the alternative to minimize this kind of operational burden should be established.

Question 49: Do you agree that the difference in the amount of interest contractually due that exceeds interest accrued on the basis of an entity's current estimate of cash flows expected to be collected for financial assets should be recognized as an increase to the allowance for credit losses? If not, why?

- We agree with recognizing the interest income considering whether to recognize or to reverse the impairment loss. We believe that recognize the interest income and allowance for credit losses based on the collectable amount will give useful information to the financial statements' users.

- We disagree with treating the different amount of interest contractually due that exceeds interest accrued to be recognized as an increase to the allowance for credit losses. The allowance for credit losses present the expected amount which will not be collected among the cash flows of contractual financial assets. However, the exceeding amount of contractual collected cash is the result of decreased amount in amortized cost caused during calculation process of amortized cost. Thus, it should be treated as decrease in carrying amount not decrease in allowance for credit losses.

The supervising authorities disagree with FASB's suggestion on considering the impairment loss when calculating the interest income. They proposed review opinion that it is appropriate not to consider the impairment loss when calculating the interest income. The reason is explained below.

The ED's method only has presentational differences between current method, which is to apply the loss rate at end of the term of amortized cost and set the allowance for credit losses, and the influence on carrying amount and interest income of financial asset are equal. On the other hand, according to the ED's proposal, there will be big operational burden because the accounting system that recognizes interest income and the management system of allowances for credit loss should be united.

Question 50: The proposed guidance would permit, but would not require, separate presentation of interest income on the statement of comprehensive income for financial assets measured at fair value with all changes in fair value recognized in net income. If an entity chooses to present separately interest income for those financial assets, the proposed guidance does not specify a particular method for determining the amount of interest income to be recognized on the face of the statement of comprehensive income. Do you believe that the interest income recognition guidance should be the same for all financial assets?

We agree.

Question 51: Do you believe that the implementation guidance and illustrative examples included in this proposed Update are sufficient to understand the proposed credit impairment and interest income models? If not, what additional guidance or examples are needed?

We believe that the FASB's proposed implementation guidance and illustrative examples increase the understandability of proposed credit impairment and interest income models.

Question 52: Do you believe that the method for recognizing interest income on financial assets measured at fair value with qualifying changes in fair value recognized in other comprehensive income will provide decision-useful information? If yes, how will the information provided be used in your analysis of an entity? If not, why?

The information provided is useful.

Question 53: The method of recognizing interest income will result in the allowance for credit impairments presented in the statement of financial position not equaling cumulative credit impairments recognized in net income because a portion of the allowance will reflect the excess of the amount of interest contractually due over interest income recognized. Do you believe that this is understandable and will provide decision-useful information? If yes, how will the information provided be used? If not, why?

There will be decrease in understandability

Question 54: The proposed guidance would require interest income to be calculated for financial assets measured at fair value with qualifying changes in fair value recognized in other comprehensive income by applying the effective interest rate to the amortized cost balance net of any allowance for credit losses. Thus, the recognition of a credit loss would result in a decrease in interest income recognized. Similarly, a reversal of a previously recognized credit loss would increase the amount of interest income recognized. The IASB Exposure Draft on Impairment proposes that an entity calculate interest by multiplying the effective rate established at initial recognition by the amortized cost basis. The IASB's definition of amortized cost basis is the present value of expected future cash flows discounted by the effective interest rate established at initial recognition and, therefore, includes credit losses recognized to date. Thus, as initially expected credit losses are allocated over the life of the instrument, the amount of interest income decreases.

Both the FASB's and the IASB's models for interest income recognition are similar in that the recognition of an impairment reduces the amount of interest income recognized. However,

as noted in the questions above, the timing of credit impairments and the determination of the effective interest rate differ in the two proposed models. Thus, the amount of interest income recognized under the two proposed models will differ. Do you believe that the FASB's model or the IASB's model provides more decision-useful information? Why?

The FASB's model provides more decision-useful information.

Question 55: Do you agree that an entity should cease accruing interest on a financial asset measured at fair value with qualifying changes in fair value recognized in other comprehensive income if the entity's expectations about cash flows expected to be collected indicate that the overall yield on the financial asset will be negative? If not, why?

We agree.

(7) Derivative Instruments and Hedging Activities

Overall comment

- We agree with FASB's basic direction which is to easily apply the hedge accounting through simplified application requirements of hedge accounting.
- We believe that FASB's proposal is appropriate since it require the quantitative hedge effect when hedge effectiveness is not effectively reasonable to be compared to the current requirements which apply the hedge accounting only on the circumstances when the hedge effectiveness is continuously high from progressively and retroactively testing the hedge effectiveness on quantitative perspective
- However, it is ambiguous to judge how reasonable the effects are. As a result, the reasonable effectiveness must be defined precisely since the companies can intervene subjectivity on the degree of reasonable effectiveness. In other words, there is possibility of applying the current effectiveness standards if clear operational method of determining basis on 'reasonably effective' and sufficiency of qualitative tests are not provided. Furthermore, the current policy states reassessing cannot be done unless there is alteration in situations, thus, there needs to be a detailed policy on what can be considered as the alteration in situations. Generally, there needs to be concrete guidelines on modified standards in order to apply in realistic operations.
- We disagree with the proposal that companies cannot voluntarily withdraw from the designation of hedge relationship. The companies' hedge strategy may change; even though the current hedge method is reasonable and effective, there can be more reasonable yet effective hedge method in accordance with the change in market condition. In addition the method may be reasonable and effective from accounting's point of view however it may not be reasonable and effective from the companies' point of view. As a result, we believe that instead of obligated policy, the selective

policy which is for companies to decide the withdrawal from designation of hedge relationship is more suitable. To reverse the hedge accounting, it's not proper to do opposite derivative instruments' transaction which causes unnecessary cost for the companies. We believes it is also inappropriate to not permit the application of general accounting treatment on hedged items and hedging instruments. Moreover, the statement that derivative instruments as hedging instruments can be viewed as effectively terminated through the opposite transaction is to be misunderstood as able to eliminate the corresponding derivative instrument. Subsequently, there needs to be clarification on above statement with regard to the terminating requirements of hedge accounting.

- There is distinction with IFRS on the content which allows the use of hypothetical derivative instruments with time value when applying the hedge accounting using options. Thus, there needs to be reconciliation between the two.**

Question 58: Do you believe that requiring an effectiveness evaluation after inception only if circumstances suggest that the hedging relationship may no longer be reasonably effective would result in a reduction in the number of times hedging relationships would be discontinued? Why or why not?

- Assessment of hedge effectiveness can be an instrument to judge durability of hedge accounting. And, the result does directly influence the profit or loss, so that the number of assessment on hedge effectiveness is possible to decrease. However we think non-assessment does not reduce the number of hedge accounting being discontinued.**

Question 59: Do you believe that a hedge accounting model that recognizes in net income changes in the fair value and changes in the cash flows of the risk being hedged along with changes in fair value of the hedging instrument provides decision-useful information? If yes, how would that information be used? If not, why?

- KAI has believed that the IASB's tentative decision which is to unite the mechanism of fair value hedge accounting with the cash flow hedge accounting should be reviewed. It is true that the hedge accounting has weaknesses due to application complexity. However, the cash flow hedge accounting lacks in conceptual accounting basis than fair value hedge accounting and may cause problem on volatility of asset. As a result, we disagree with uniting into mechanism on cash flow hedge accounting in order to improve the complexity.**

- For example, if a company applies the cash flow hedge accounting through forward contract on the long-term firm commitment, when there is a rapid change on exchange rate, the rapid increase in liability ratio and impaired capital may happen.**

- KAI agrees with continuously maintaining the fair value hedge accounting model. Also, we suggest to progress profound discussion on appropriately presenting the hedge activities on statement of financial position.**

Question 63: Do you foresee any significant operational concerns or constraints arising from the inability to discontinue fair value hedge accounting or cash flow hedge accounting by simply dedesignating the hedging relationship? If yes, what constraints do you foresee and how would you alleviate them?

- Please refer to our overall comment.**

(8) Disclosures

Question 65: Do you agree with the proposed disclosure requirements? If not, which disclosure requirement do you believe should not be required and why?

We agree.

Question 66: For purchased financial assets, do you believe that the requirement to disclose the principal balance, the purchaser's assessment of the discount related to credit losses inherent in the financial instrument at acquisition, any additional difference between the amortized cost and the principal balance, and the amortized cost in each period will provide decision-useful information? If yes, how will the information provided influence your analysis of an entity? If not, why?

Information provided is useful.

(9) Effective date and transition

Question 68: Do you agree with the transition provision in this proposed Update? If not, why?

We agree.