March 12, 2012

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

Re: Revised Exposure Draft – Revenue from Contracts with Customers

Dear Sirs,

Mitsui O.S.K. Lines, Ltd (“MOL”), a shipping company in Japan submits this letter for your consideration, the contents of which are our independent answers to the IASB question 1 of the Revised Exposure Draft (“ED”), the timing of revenue recognition of transportation contracts in particular. Besides this comment letter, the Japanese Shipowners Association (“JSA”) also submits its comment letter to the Board concerning four areas of the captioned subject, the contents of which, MOL, as a member of JSA, agrees with and supports in most parts. MOL would appreciate it if the Board could consider this letter in conjunction with JSA’s separate comment letter which summarizes the collective views of the major Japanese shipping companies.

1. MOL’s Views on Question 1 in relation to Transportation Service Contracts

IASB proposes an approach of categorizing performance obligations into two types of performance obligations, either “performance obligations satisfied over time” or “performance obligations satisfied at a point in time”.

JSA and MOL agree with the proposed concept. But JSA’s comment letter does not evidently make clear its thought on a conceptual question whether ocean transportation services should be accounted for as “the performance obligation satisfied over time”, or “the performance obligation satisfied at a point in time”, based on the concept of ED. JSA points out that “we believe whether a specific performance obligation is accounted for as “performance obligations satisfied over time” or as “performance obligations satisfied at a point in time” should be appropriately determined in the context of the entity’s business model (e.g., means of transportation, patterns of voyage)”.
Therefore, MOL writes this letter to explain its own views independently from JSA's letter as follows:

It is commonly understood that a transportation contract in general is a service contract that a carrier promises a customer (i) to carry his/her cargo to his/her designated place from a place of receipt, (ii) to deliver it on a designated date or within an (explicit or implied) transportation period, and (iii) to receive the freight in exchange for the service provided as promised in the contract.

The example of a freight logistics company in BC97 seems to suggest that IASB interprets transportation services should be accounted for as "the performance obligation satisfied over time", not as "the performance obligations satisfied at a point in time" with the reason that "a customer must have benefited from the entity’s performance completed to date (i.e. received goods or services) if another entity could simply fulfill the remaining obligation to the customer without substantially re-performing the work completed to date". MOL disagrees with IASB's reasoning. MOL as a carrier believes that IASB’s logic is not in line with the customer’s expectation on the benefit of the transportation service and is far from the common sense of the general public on the carrier’s performance obligation of the transportation contracts. May it be a realistic solution to allow present revenue recognition practices recognizing revenue over time to continue, it is nonetheless a logical deviation from the basic concept underlying the proposed Revenue from Contract with Customers not to look at the transportation service contract as "the performance obligations satisfied at a point in time".

Unless the cargo is physically delivered to the customer, he/she gains no benefit from the transportation service as he/she cannot use his/her cargo nor gain any control of it. It is against the common sense of the general public to assume that the control of the service is gradually transferred to the customer disregarding the fact that his/her cargo is out of his/her control. MOL is confident that our customers will not agree with IASB’s assumption that they gradually receive a certain amount of the benefit from the incomplete cargo transportation service during their cargoes are physically located somewhere on route to the destinations.

With this being said, MOL admits that there are many transactions in the marine transportation business, for which accounting as "performance obligations satisfied over
time” could better depict the economic substance of the transactions more appropriately rather than accounting for as “performance obligations satisfied at a point in time” from the carrier’s managerial point of view.

2. Our suggestion
As mentioned above, MOL agrees with the proposal about the timing of revenue recognition in principle. However, MOL disagree with such a policy to allow only one revenue recognition method and to disallow the existing several accounting practices for revenue recognition having been generally accepted in a various transportation service sectors, which are structured in consideration to the features of each transportation means (vessel, rail, aircraft, truck, etc.) and each of which is historically accepted because of its own economic reasonability, are denied merely due to the inconformity with the general concept of transferring a performance obligation proposed by the Board.

There are a couple of revenue recognition methods having been accepted in the shipping industry under the Japanese GAAP. They are all designed in order to match associated cost with revenue. Each shipping company or each business segment of it chooses one particular method which it thinks better serves for the management needs.

The liner vessel (container vessel) deals with a large variety of cargoes in containers, various customers and many calling ports. Thus, the freight revenue is usually recognized over estimated transportation period of cargo per a bill of lading (“B/L”, a contract with customer ) since it reflects better the economic feature of the multimodal container transportation. The profit and loss of tramerper vessels is commonly measured on a percentage of or at the completion of a voyage (or a certain cycle similar to a voyage) basis, not on a B/L basis as most voyage expenses accrue until a completion of promised services according to a vessel’s physical movement.

Following steps provided by the revised ED, performance obligation should be identified on a B/L basis as B/L is a unit of contract with each customer. However, there are many cases where it is practically difficult to allocate voyage cost to freight revenue per B/L. In addition, MOL do not see there will be much difference between the amount of revenue based on ED and that based on existing accounting practices in a fiscal year because the duration of one voyage is almost always within three months or less. Below are some of our concerns on the issue of revenue recognition per B/L:

(1) If shipping companies are forced to allocate cost to each B/L, it requires them
significant changes in accounting practice and material modifications in accounting systems. With the current account system in place, MOL cannot allocate voyage cost to each B/L properly. It is physically difficult and impractical for shipping companies to reasonably allocate various expenses such as bunker expense, charter expense and crew expense, which accrue even when a vessel is in a ballasting leg of a voyage to a B/L (performance obligation). Even in the liner business (container vessel) where freight revenue is recognized per B/L currently, voyage cost is not allocated to each B/L.

(2) The management measures the profit and loss of the liner business of container vessel by the percentage of completion basis and that of the tramper business by the percentage of a voyage basis or by the completion of a voyage basis, not by individual B/L. MOL thinks that users of financial statements will not appreciate such financial information, as it is prepared on a basis different from the management point of view.

We would be grateful if we could be given an opportunity to further discuss this matter with the Board and if you have any questions about our comment, please do not hesitate to contact us at ifrsp@molgroup.com.

Sincerely yours,

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