September 30, 2010

Technical Director Financial Accounting Standards Board 401 Merritt 7 PO Box 5116 Norwalk CT 06856-5116

File Reference No. 1810-100

Dear Sirs or Madams,

Comments on the Proposed Accounting Standards Update "Accounting for Financial Instruments and Revisions to the Accounting for Derivative <u>Instruments and Hedging Activities"</u>

We are a group of Japanese companies that prepare consolidated financial statements under the accounting principles generally accepted in the United States. We appreciate the FASB's efforts for the project of revising the accounting for Financial Instruments. Our comments on the Proposed Accounting Standards Update, Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities (the "proposed Update") are noted below.

## [Executive Summary]

We support the mixed measurement attribute model which reflects the entity's business activities. Under this method, the attribute of measurement would be decided according to the investment objective of financial instruments and how the entity manages the financial instruments, which we think is essential to make financial reporting useful.

We are concerned that if the only treatment available for equity investment would be FVTNI, without any exceptions, this would possibly not accurately reflect the reality of the investment. We respectfully request that the FASB to dissolve the difference from IFRS 9 and the proposals in the IASB's exposure draft, "Financial Instruments: Amortized Cost and Impairment" and strongly request that FVTOCI of equity investment be made available as an alternative and recycling from OCI to net income be permitted upon sale.

<sup>&</sup>lt;sup>1</sup> The names of companies represented are noted at the bottom of this letter.

[Answer to each question]

**Question 1:** Do you agree with the scope of financial instruments included in this proposed Update? If not, which other financial instruments do you believe should be excluded or which financial instruments should be included that are proposed to be excluded? Why?

We support this proposed Update.

**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 do not support this proposed Update.

We believe that the application of equity method should be based on the management business strategy and decision-making in relation to the investments. The new criterion provided by the proposed Update which focuses solely on the relationship between the investee and the investor may create disparity from actual business strategy. Therefore, our view is that the current determination guidance is more preferable in comparison to the proposed Update.

**Question 8:** Do you agree with the initial measurement principles for financial instruments? If not, why?

We support the initial measurement which is determined in accordance with the subsequent measurement classification. Please refer to Question15 for our comments on the subsequent measurement.

We request, however, an exceptional treatment for cross-holding shares. Same as the classification under IFRS9 and the current "available for sale" category, the classification to FVTOCI should be added and then the recycle to net income should be allowed at the time of sale. We also request an exceptional treatment for unlisted equity securities to be held for business relationship purposes. It is difficult to obtain sufficient transparency regarding the fair value of such equity securities, and therefore, the acquisition cost should be accepted as an alternative subsequent measurement method.

Question 9: For financial instruments for which qualifying changes in fair value

are recognized in other comprehensive income, do you agree that a significant difference between the transaction price and the fair value on the transaction date should be recognized in net income if the significant difference relates to something other than fees or costs or because the market in which the transaction occurs is different from the market in which the reporting entity would transact? If not, why?

We support this proposed Update.

**Question 10:** Do you believe that there should be a single initial measurement principle regardless of whether changes in fair value of a financial instrument are recognized in net income or other comprehensive income? If yes, should that principle require initial measurement at the transaction price or fair value? Why?

No, it should be changed according to the subsequent measurement.

**Question 11:** Do you agree that transaction fees and costs should be (1) expensed immediately for financial instruments measured at fair value with all changes in fair value recognized in net income and (2) deferred and amortized as an adjustment of the yield for financial instruments measured at fair value with qualifying changes in fair value recognized in other comprehensive income? If not, why?

We support this proposed Update.

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?

We do not support this proposed Update.

If an entity's business strategy is not to sell the financial assets but to collect the contractual cash flows, the amortized cost method would better represent the business strategy. Where the amortized cost method is appropriate, it is sufficient that the amortized cost would be presented in the statements of financial position and the fair value information would be presented separately in notes to the financial statements, rather than presenting fair value in the statements of financial position and recognize changes in fair value in other comprehensive income. We are concerned that the users of financial statements would be confused if both the fair value and amortized cost information would be provided on the face of the financial statements.

**Question 14:** The proposed guidance would require that interest income or expense, credit impairments and reversals (for financial assets), and realized gains and losses be recognized in net income for financial instruments that meet the criteria for qualifying changes in fair value to be recognized in other comprehensive income. Do you believe that any other fair value changes should be recognized in net income for these financial instruments? If yes, which changes in fair value should be separately recognized in net income? Why?

We do not believe that other changes in fair value should be recognized in net income.

**Question 15:** Do you believe that the subsequent measurement principles should be the same for financial assets and financial liabilities? If not, why?

We do not believe that the subsequent measurement principles should be the same for financial assets and financial liabilities.

Transfer of financial liabilities is quite rare. We do not believe that an entity should implement the subsequent measurement when such entity holds financial liabilities primarily for making the contractually required cash payments and such contractual cash flow is fixed. We believe that only financial liabilities and derivatives liabilities held for trading purposes would be measured at fair value.

Regarding the hybrid instruments and in consideration to the presentation of entity's own credit risk, we believe that it is reasonable to continue the current practice of bifurcation of embedded derivatives similar to the IASB proposal.

**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 the reclassification should not be prohibited.

The classification decision should reflect an entity's business strategy and the reclassification should be required when an entity's business strategy changes.

**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-incost-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 do not believe that this remeasurement approach is appropriate.

We do not believe that the benefits would outweigh the implementation costs of remeasurement approach. Rather, we are concerned that this would hinder the readability of financial statements by introducing complexity of a measurement attribute that is different from the fair value or the amortized cost. Therefore, the readability of financial statements would be hindered.

**Question 18:** Do you agree that a financial liability should be permitted to be measured at amortized cost if it meets the criteria for recognizing qualifying changes in fair value in other comprehensive income and if measuring the liability at fair value would create or exacerbate a measurement attribute mismatch? If not, why?

We do not agree with this proposed Update.

We anticipate there would be some mismatch of measurement attributes where the liabilities are not linked to certain assets depending on the business strategies. The judgment to elect fair value or amortized cost should be left with the management according to the entity's business strategy.

**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 do not agree with this proposed Update.

It would not be appropriate to value a deferred tax asset associated with the debt instrument that is going to be held to maturity and the collectability of such asset is certain if held to the maturity in the same way as the other deferred tax assets.

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 do not agree with this proposed Update.

It would create a mismatch if no hedge would be placed on the financial instruments indexed to the issuer's own equity.

**Question 28:** Do you believe that the proposed criteria for recognizing qualifying changes in fair value in other comprehensive income are operational? If not, why?

We do not believe that this proposed Update is operational.

Cross-holding shares are not held by an entity's management for short term profits, and therefore it should not be subject to net income. If these types of income would be included in net income, it would become difficult to substantiate the reasons for such cross-holdings to the investors.

**Question 30:** Do you believe that the proposed criteria are operational to qualify for measuring a financial liability at amortized cost? If not, why?

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We do not believe that this proposed Update is operational.

The requirements for adopting the amortized cost method for financial liabilities are not realistic. The decision to choose between the fair value and the amortized cost should be left with management.

Question 31: 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-incost-to-service rate over the implied maturity of the deposits. Do you believe that this remeasurement approach is operational? Do you believe that the remeasurement approach is clearly defined? If not, what, if any, additional guidance is needed?

Refer to the Question 17.

Question 32: For financial liabilities measured at fair value with all changes in fair value recognized in net income, do you agree that separate presentation of changes in an entity's credit standing (excluding changes in the price of credit) is appropriate, or do you believe that it is more appropriate to recognize the changes in an entity's credit standing (with or without changes in the price of credit) in other comprehensive income, which would be consistent with the IASB's tentative decisions on financial liabilities measured at fair value under the fair value option? Why?

For non-trading financial liabilities, we believe that it is appropriate to recognize changes in fair value attributable to entity's own credit risk in other comprehensive income on the basis that the recycling to net income be allowed. For trading financial liabilities, it is operationally difficult to separately disclose changes in fair value attributable to the entity's own credit risk, and we do not believe it is useful information for investment decision-making.

**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 that this proposed update is clear.

**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 support this proposed Update.

**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 do not agree with this proposed Update.

We do not believe that it is operational.

**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 do not agree with this proposed Update.

We are concerned that this proposal would increase operational burdens by requiring an implementation of impairment test on the group basis after an impairment determination is made on the individual basis. Further, this proposal requires a determination of historical loss rate on the group basis, while providing no guidance as to how to determine an appropriate historical loss rate. Therefore, we do not believe that the benefits outweigh the cost of preparation.

**Question 46:** 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 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 be more appropriate? Are both methods operational? If not, why?

We support this proposed Update.

We do not believe that it is appropriate to include future uncertainties such as future economic condition into estimation. We support FASB proposal over IASB.

**Question 48:** 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. Do you believe that the recognition of interest income should be affected by the recognition or reversal of credit impairments? If not, why?

We do not support this proposed Update.

We do not think it is practical.

**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 support this proposed Update.

**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?

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Regarding financial assets measured at fair value with all changes in fair value recognized in net income, the same presentation together with other attributes is not always appropriate. Several options which take practicability and clarity into consideration should be accepted.

**Question 56:** Do you believe that modifying the effectiveness threshold from *highly effective* to *reasonably effective* is appropriate? Why or why not?

We believe that it is appropriate.

We expect that this mitigation of effectiveness criteria would avoid negative implications such as not being able to apply the hedge accounting over the entire period.

**Question 61:** Do you foresee any significant operational concerns or constraints in calculating ineffectiveness for cash flow hedging relationships? If yes, what constraints do you foresee and how would you alleviate them?

We do not foresee any significant operational concerns or constraints.

**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 do not support this proposed Update.

Especially, the disclosure requirements of the allowance for doubtful accounts and FVTOCI are detailed and therefore, we expect situations that require extensive system developments. Therefore, the cost of preparation does not meet the benefits of investors.

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

We do not support this proposed Update.

This proposed Update requires the disclosure of previous year's financial position which we consider detailed and excessive. Sufficient transition period would be required if the proposed Update requires retroactive note disclosures to the previous year's financial position.

**Question 70:** How much time do you believe is needed to implement the proposed guidance?

We recommend the FASB to provide sufficient transition period after the final version of the

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proposed Update is distributed. This proposed Update requires a wide variety of changes and modification on the measurement of financial instruments. We believe that it would realistically take five years for the transition period, and take at least three to four years after the submission of final version of the proposed Update if we consider the effects of transition from the current standard, development of the fair value measurement methodology, establishment of the internal control pursuant to Sarbens-Oxley Act of 2002, system development and the testing period.

**Question 71:** Do you believe the proposed transition provision is operational? If not, why?

We expect some operational difficulty relating to the retroactive application. Short-cut method which deems the acquisition to be made at the book value as of the transition date should be made as an option.

We hope that our comments contribute to your forthcoming deliberations in this project.

Sincerely yours,

## A Group of Japanese Companies:

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CANON INC.

**KYOCERA** Corporation

**KUBOTA** Corporation

SANYO Electric Co., Ltd.

Sony Corporation

**TDK** Corporation

**Toshiba Corporation** 

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