



ED/2011/1

Offsetting Financial Assets and Financial Liabilities

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1. Background

- Different offsetting requirements are responsible for the largest quantitative difference in IFRS und US GAAP balance sheets.
- Constituents have requested a common solution.
- *ED/2011/1 Offsetting Financial Assets and Financial Liabilities*
 - Published for public comment on 28 January 2011
 - Comments due on 28 April 2011



2. Objective

- Establish a principle for offsetting financial assets and financial liabilities:

An entity shall offset a recognised financial asset and recognised financial liability only when

- a) on the basis of the rights and obligations associated with the financial asset and financial liability, the entity has a right to or obligation for only the net amount (ie the entity has, in effect, a single net financial asset or financial liability) and
- b) the amount, resulting from offsetting the financial asset and financial liability, reflects an entity's expected cash flows from settling two or more separate financial instruments.



3. Offsetting criteria (1)

- An entity shall offset a recognised financial asset and a recognised financial liability and shall present the net amount in the statement of financial position when the entity:
 - a) has an unconditional and legally enforceable right to set off the financial asset and financial liability; and
 - b) intends either:
 - i. to settle the financial asset and financial liability on a net basis, or
 - ii. to realise the financial asset and settle the financial liability simultaneously.
- In all other circumstances, financial assets and financial liabilities are presented separately from each other according to their nature as assets or liabilities.



3. Offsetting criteria (2)

- For the purpose of this [draft] IFRS:
 - a) **Offsetting** is the presentation of one or more financial assets and financial liabilities as a single net amount in the statement of financial position.
 - b) A **right of set-off** is a debtor's legal right, by contract or otherwise, to settle or otherwise eliminate all or a portion of an amount due to a creditor by applying against that amount all or a portion of an amount due from the creditor or a third party.
 - c) An **unconditional** right of set-off is a right of set-off the exercisability of which is not contingent on the occurrence of a future event.



3. Offsetting criteria (3)

- d) A **conditional** right of set-off is a right of set-off that can be exercised only on occurrence of a future event.
- e) A **legally enforceable** right of set-off is a right of set-off that is enforceable in all circumstances (ie enforceable both in the normal course of business and on the default, insolvency or bankruptcy of one of the counterparties).
- f) Realisation of a financial asset and settlement of a financial liability are treated as **simultaneous** only when the settlements are executed at the same moment.



3. Offsetting criteria (4)

- The proposals are broadly comparable to the requirements contained in IAS 32 today.
- They clarify that a right of set-off must be enforceable at all times and not only currently.
- Under US GAAP, the proposals represent a remarkable change.



3. Offsetting criteria (5)

Question 1 – Offsetting criteria: unconditional right and intention to settle net or simultaneously

The proposals would require an entity to offset a recognised financial asset and a recognised financial liability when the entity has an unconditional and legally enforceable right to set off the financial asset and the financial liability and intends either:

- (a) to settle the financial asset and financial liability on a net basis or
- (b) to realise the financial asset and settle the financial liability simultaneously.

Do you agree with this proposed requirement? If not, why? What criteria would you propose instead, and why?



3. Offsetting criteria (6)

Question 2 – Unconditional right of set-off must be enforceable in all circumstances

It is proposed that financial assets and financial liabilities must be offset if, and only if, they are subject to an unconditional and legally enforceable right of set-off. The proposals specify that an unconditional and legally enforce-able right of set-off is enforceable in all circumstances (ie it is enforceable in the normal course of business and on the default, insolvency or bankruptcy of a counterparty) and its exercisability is not contingent on a future event. Do you agree with this proposed requirement? If not, why? What would you propose instead, and why?

Question 3 – Multilateral set-off arrangements

The proposals would require offsetting for both bilateral and multilateral set-off arrangements that meet the offsetting criteria. Do you agree that the off-setting criteria should be applied to both bilateral and multilateral set-off arrangements? If not, why? What would you propose instead, and why? What are some of the common situations in which a multilateral right of set-off may be present?



4. Disclosure (1)

- An entity shall disclose information about rights of set-off and related arrangements (such as collateral agreements) associated with the entity's financial assets and financial liabilities to enable users of its financial statements to understand the effect of those rights and arrangements on the entity's financial position.
- Paragraph 12 of the ED contains the minimum requirements to be disclosed. This information shall be presented in a tabular format, unless another format is more appropriate. The ED contains illustrative examples that represent a possible way to meet these quantitative disclosure requirements.



4. Disclosure (2)

- As a minimum the following information shall be disclosed separately for financial assets and financial liabilities recognised at the end of the reporting period by class of financial instruments:
 - a) the gross carrying amounts (before offsetting)
 - b) gross amounts offset and resulting net amount presented in the statement of financial position
 - c) gross amounts subject to unconditional and legally enforceable rights to set-off but which the entity does not intent to settle net or simultaneously
 - d) gross amounts subject to conditional rights of set-off



4. Disclosure (3)

- e) the net amount of financial assets and financial liabilities after taking into account the effects of items in a) – d)
- f) the amount of cash or the fair value of other financial instruments held or pledged as collateral (excluding the amount of cash or portion of fair value in excess of the resulting net amount presented in the statement of financial position under b))
- g) net exposure = the net amount of financial assets and financial liabilities (ie the difference) after taking into account the effect of the items in e) and f)



4. Disclosure (4)

Financial assets subject to offsetting and related arrangements

CU million

As at 31 December 20XX	(i)	(ii)	(iii)=(i)-(ii)	(iv)	(v)	(vi)=(iii)-(iv)-(v)	(vii) Collateral held		(viii)
	Gross amount of assets	Gross amount of liabilities offset against assets in the statement of financial position	Net amount of assets in the statement of financial position	Gross amount of liabilities subject to conditional rights of set-off	Gross amount of liabilities subject to an unconditional and legally enforceable right of set-off but the entity does not intend to settle net or simultaneously	Net amount of assets before deducting collateral	Cash	Fair value of other financial instruments received as collateral	Net exposure
Description									
Exchange traded financial instruments									
OTC derivatives, repurchase and stock lending agreements and similar financial instruments									
Other financial instruments									
Financial assets at fair value through profit or loss									
Total									
Financial assets at amortised cost									
Total									



4. Disclosure (5)

Financial liabilities subject to offsetting and related arrangements

CU million

As at 31 December 20XX

	(i)	(ii)	(iii)=(i)-(ii)	(iv)	(v)	(vi)=(iii)-(iv)-(v)	(vi)		(vii)
							Collateral pledged		
	Gross amount of liabilities	Gross amount of assets offset against liabilities in the statement of financial position	Net amount of liabilities in the statement of financial position	Gross amount of assets subject to conditional rights of set-off	Gross amount of assets subject to an unconditional and legally enforceable right of set-off but the entity does not intend to settle net or simultaneously	Net amount of liabilities before deducting collateral	Cash	Fair value of other financial instruments pledged as collateral	Net exposure

Description

Exchange traded financial instruments

OTC derivatives, repurchase and stock borrowing agreements and similar financial instruments

Other financial instruments

Financial liabilities at fair value through profit or loss

Total

Financial liabilities at amortised cost

Total



4. Disclosure (6)

Question 4 – Disclosures

Do you agree with the proposed disclosure requirements in paragraphs 11-15? If not, why? How would you amend those requirements, and why?



5. Effective date and transition

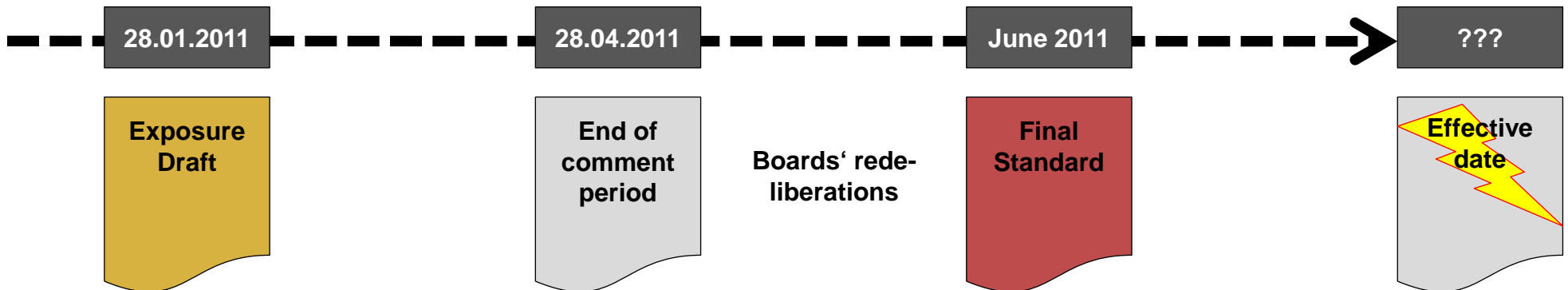
- The effective date has not yet been determined.
- The proposed requirements shall be applied retrospectively for all comparative periods presented.

Question 5 – Effective date and transition

- (a) Do you agree with the proposed transition requirements in Appendix A? If not, why? How would you propose to amend those requirements, and why?
- (b) Please provide an estimate of how long an entity would reasonably require to implement the proposed requirements.



6. Next steps



Thank you very much for your attention!

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