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Berlin, 20 April 2011

Dear Françoise,

Exposure Draft ED/2011/1 Offsetting Financial Assets and Financial Liabilities

On behalf of the German Accounting Standards Board (GASB), I am writing to comment on EFRAG's draft comment letter on the IASB's Exposure Draft ED/2011/1 'Offsetting Financial Assets and Financial Liabilities'. We appreciate the opportunity to comment on EFRAG's draft comment letter.

For our arguments, please see the appendix (comment letter to the IASB) attached to this letter.

If you would like to discuss any aspect of this comment letter in more detail, please do not hesitate to contact me.

Yours sincerely,

Liesel Knorr
President



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Sir David Tweedie
Chairman of the
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Berlin, 20 April 2011

Dear David,

Exposure Draft ED/2011/1 Offsetting Financial Assets and Financial Liabilities

On behalf of the German Accounting Standards Board (GASB) I am writing to comment on the IASB Exposure Draft ED/2011/1 'Offsetting Financial Assets and Financial Liabilities' (herein referred to as 'ED'). We appreciate the opportunity to comment on the ED.

The GASB welcomes the efforts of the IASB and the FASB to achieve a converged approach for offsetting financial assets and financial liabilities which eliminates significant differences in IFRS and US GAAP statements of financial position.

We agree with the proposal to establish a clear principle for offsetting financial assets and financial liabilities. We believe that the proposed offsetting criteria – which broadly agree with the current IFRS requirements – are generally appropriate and that offsetting should be required when these criteria are met for both bilateral and multilateral set-off arrangements.

However, we have concerns with regard to the following issues. The narrow definition of 'simultaneously' as further described in paragraph C11 of the ED may prevent offsetting in cases where settlement with a central clearing house occurs in batches due to the volume of transactions and processing constraints although all offsetting criteria are met. Furthermore, it is unclear from paragraph C14 of the ED whether a general exception from offsetting for margin accounts (collateral obtained or pledged in



respect of financial instruments) is intended even in instances where all offsetting criteria are met.

The GASB does not agree with the proposed requirements to disclose gross positions of the netted financial assets and financial liabilities when a net presentation in the statement of financial position is required because all of the offsetting criteria are met. In addition, we believe that the proposed disclosures in respect of collateral obtained or pledged are redundant because IFRS 7 already requires such disclosures.

Please find our detailed comments on the questions raised in the ED in the appendix to this letter. If you would like to discuss our comments further, please do not hesitate to contact me.

Yours sincerely,

Liesel Knorr
President



Appendix

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?

The GASB agrees with the proposed offsetting criteria and the requirement to offset when these criteria are met. We support to establish a clear principle for offsetting financial assets and financial liabilities that justifies an exception from the general gross presentation requirement in IAS 1. In our opinion, paragraphs 4 and 5 of the ED set out an appropriate principle in this respect and this principle is in general adequately converted into applicable criteria.

However, we have identified the following issues in the proposed application guidance in appendix C of the ED which raises our concerns. Paragraph C11 appears to prevent offsetting in cases where settlement with a central clearing house occurs in batches due to the volume of transactions and processing constraints, although in these circumstances there is no exposure to credit or liquidity risk and the cash flows are in effect equivalent to a single net amount. We believe that the criterion 'simultaneously' is appropriate but the IASB should consider this issue when re-deliberating the meaning of the criterion and clarify that the criterion is met in such situations.

Another point of concern is the guidance in paragraph C14. This could be read as a general exception from applying the offsetting criteria to collateral obtained or pledged in respect of financial assets and financial liabilities. We do not believe that such an exception would be appropriate. Thus, it should be clarified that the offsetting criteria also apply to margin accounts and that margin accounts should be netted with other positions if the general criteria are met. For example, in certain instances



with central clearing houses the margin accounts are included in the net settlement cash flows due and therefore should be offset accordingly.

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 enforceable 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?

The GASB agrees with the proposal that the unconditional right of set-off must be enforceable in all circumstances.

We understand that the proposed offsetting requirements are stricter than those in the Basel Framework for prudential regulation and that some have asked for an alignment between accounting standards and regulatory requirements. However, we believe that the objectives of the Basel Framework and IFRS are different and therefore do not allow such an alignment. In this respect, we agree with the IASB's position set out in BC64 and BC65 of the ED.



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?

We agree with the proposal to require offsetting of financial assets and financial liabilities when the offsetting criteria are met, irrespective of whether the set-off arrangements are bilateral or multilateral.

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?

The GASB does not agree with the proposed requirement to disclose the gross amounts of financial assets and liabilities for which net presentation in the statement of financial position is required because all of the offsetting criteria are met. The proposed offsetting criteria are sufficiently strict to ensure that offsetting is only applicable when the entity has, in substance, a single net financial asset or financial liability which reflects the entity's expected cash flows. We believe that in such a situation information about gross positions is not appropriate.

We agree that the proposed disclosure requirements in cases where not all of the offsetting criteria are met as well as about related arrangements (including information about collateral and master netting agreements) are helpful to inform users of financial statements about the link between the corresponding financial assets and financial liabilities. Nevertheless, we would like to point out that IFRS 7 already requires disclosures relating to collateral pledged or held (paragraphs 14 and 15) and to credit risk mitigation (paragraphs 36-38). We believe that those disclosure re-



requirements are adequate and do not see a need for additionally providing this information for a subset of transactions, i.e. for offsetting and related arrangements.

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.

The GASB agrees with the proposal to apply the netting requirements retrospectively to all comparative periods presented. As the proposed requirements compare broadly with the current offsetting requirements in IAS 32, we do not expect significant difficulties regarding presentation.

In contrast, the proposed disclosure requirements are more extensive compared to what is currently required under IFRS 7, so that some entities are likely to require a certain lead-time to accumulate the necessary information, especially for comparative periods. We therefore favour either a late effective date for or a prospective application of the disclosure requirements.