**FASB** 

Technical Director- Ref. 2011- 100

Regarding: Balance Sheet Offsetting April 28, 2011

Sent To: Director@Fasb.org

By: Dr. Joseph S. Maresca CPA, CISA

\_\_\_\_\_

Colleagues,

Thank you for the opportunity to critique Balance Sheet - Offsetting items.

Details follow:

## BACKGROUND:

\_\_\_\_\_

The FASB seeks input from members of the Accounting Profession on various questions presented for review.

Question 1: The right of offset of recognizable eligible assets or liabilities where the entity has an unconditional and legally enforceable right of setoff and to settle the assets and liabilities on a net basis or to realize assets or settle the liabilities simultaneously . A right of setoff must be legally enforceable in all circumstances. Eligible assets or liabilities presented in the financial statements are done so in a manner which helps to assess:

- o the ability to generate cash flows in the future
- o the nature and amount of entity resources and claims
- o the entity liquidity and solvency

Question 2: The exercise is not contingent upon a future event.

Question 3: Requires offsetting for bilateral and multilateral setoff arrangements meeting the offset criteria. Set-off cannot be contingent upon an event happening.

210-20-45-E

An entity undertakes multiple transactions with a single counterparty. Such an agreement may provide for a single net settlement of all financial instruments and derivatives covered by the agreement in the event of default in or termination of any one contract.

## **CRITIQUE**

Question 1: The right of offset of recognizable eligible assets or liabilities where the entity has an unconditional and legally enforceable right of setoff and to settle the assets and liabilities on a net basis or to realize assets or settle the liabilities simultaneously. A right of setoff must be legally enforceable in all circumstances. Eligible assets or liabilities presented in the financial statements are done so in a manner which helps to assets:

- o the ability to generate cash flows in the future
- o the nature and amount of entity resources and claims
- o the entity liquidity and solvency

Member Response to Question 1

I agree. When the entity has the ability to generate cash flows in the future **AND** can reasonably settle the nature and amount of entity resources and claims and

counterclaims (reasonably anticipated in the circumstances) **AND** the entity is solvent and reasonably liquid **THEN** there is a high likelihood of business continuity which gives significant confidence and comfort to the readers of the financial statements who rely on the representations made therein.

The boards are proposing that offsetting should apply only when the right of set-off is enforceable at all times, including in default and bankruptcy, and the ability to exercise this right is unconditional, that is, it does not depend on a future event. The entities involved must intend to settle the amounts due with a single payment or simultaneously. Provided all of these requirements are met, offsetting would be required. The proposals would amend IFRSs and US GAAP and eliminate several industry-specific netting practices.

Member Response to Question 2

I agree. The exercise is not contingent upon a future event.

Member Response to Question 3

Requires offsetting for bilateral and multilateral setoff arrangements meeting the offset criteria. Set-off cannot be contingent upon an event happening.

**I agree** provided that the Agreements which specify the above should be constructed tightly by the financial experts and involved legal counsels of the parties and counterparties. Otherwise, the Courts may construe these agreements in ways unintended by the parties. In addition, there may be more difficult legal issues for agreements emanating from overseas jurisdictions and subject to overseas laws and conventions. Such setoffs between the parent and subsidiaries could have additional complexities when attempting a consolidation.

Credit analysts might prefer to see both the net (on balance sheet) and gross (in footnote disclosure) exposure for derivatives. Equity analysts might like having the gross exposures on the face of the balance sheet.

In addition, fair disclosure for offsetting of bilateral and multilateral setoff arrangements may have varying levels of complexity not comprehended fully by readers of the financial statements.

210-20-45-E

An entity undertakes multiple transactions with a single counterparty. Such an agreement may provide for a single net settlement of all financial instruments and derivatives covered by the agreement in the event of default in or termination of any one contract.

Reference:

1)

http://www.ifrs.org/News/Press+Releases/Offsetting+ED+January+2011.htm