



**Australian Government**  
**Australian Accounting  
Standards Board**

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Comment Letter No. 74

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28 April 2011

Sir David Tweedie  
Chairman  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
UNITED KINGDOM

Dear David

**AASB comments on IASB Exposure Draft ED/2011/1**  
***Offsetting Financial Assets and Financial Liabilities***

The Australian Accounting Standards Board (AASB) welcomes the opportunity to provide comments on the Exposure Draft ED/2011/1 *Offsetting Financial Assets and Financial Liabilities* (ED/2011/1). In formulating its comments, the AASB sought and considered the views of Australian constituents through comment letters and other consultation. The comment letters received are published on the AASB's website.

The AASB understands that the differences in offsetting requirements between IAS 32 *Financial Instruments: Presentation* and US GAAP have resulted in a significant presentation gap between financial statements prepared in accordance with IFRSs and US GAAP. Accordingly, the AASB appreciates the IASB-FASB joint efforts to improve the comparability of financial statements prepared under IFRSs and US GAAP.

Overall, the AASB supports the IASB and the FASB's proposals to retain the existing IAS 32 criteria for offsetting financial assets and financial liabilities on the face of the balance sheet. In addition, the AASB agrees with the IASB and the FASB's rationale that there is no basis for excluding multi-lateral set off arrangements from the scope of offsetting if all the criteria proposed in ED/2011/1 are met.

The AASB understands that ED/2011/1 prohibits assets pledged as collateral or the obligation to return collateral obtained to be offset against the associated financial assets and financial liabilities and supports this proposal.

The AASB is concerned about some of the proposed additional guidance, particularly guidance that clarifies the notion of 'unconditional right' and its application in the context of

other IFRSs. The AASB also considers that, for clarity, some of the application guidance in ED/2011/1 relating to the unconditional right criterion should be included in the text of the Standard.

Whilst the AASB is supportive of more robust disclosures about financial assets and financial liabilities that offset on the face of the balance sheet, the AASB considers the cost burden and relative usefulness of some of the ED/2011/1 disclosures need to be considered in conjunction with proposed disclosures in other financial instruments exposure drafts and existing disclosure requirements in IFRS 7 *Financial Instruments: Disclosures* as a whole. The AASB considers there is an opportunity to have a more cohesive and cost-effective set of disclosure requirements.

The AASB views, as summarised above, are explained in more detail in the attached Appendix.

If you have any queries regarding any matters in this submission, please contact me or Christina Ng ([cng@asb.gov.au](mailto:cng@asb.gov.au)) and Angus Thomson ([athomson@asb.gov.au](mailto:athomson@asb.gov.au)).

Yours sincerely



Kevin M. Stevenson

Chairman and CEO



## APPENDIX

### 1 Principles for offsetting criteria (Questions 1 and 2)

- 1.1 The AASB is supportive of the proposal to retain the existing IAS 32 *Financial Instruments: Presentation* requirements for offsetting financial assets and financial liabilities on the face of the balance sheet.

#### *Unconditional and legally enforceable right to offset*

- 1.2 While the proposed offsetting criteria in ED/2011/1 are not expected to significantly change the outcomes under IAS 32, the AASB notes ED/2011/1 clarifies that the right to offset must also be ‘unconditional’. Paragraphs C5 and C6 of ED/2011/1 further clarify that, aside from a contract, a right of set off may also arise as a result of a provision in law (or a regulation).
- 1.3 The AASB notes the application of ‘unconditional’ in ED/2011/1 in comparison to other Standards, for example, paragraph 69(d) of IAS 1 *Presentation of Financial Statements*, which states that “an entity shall classify a liability as current when... it does not have an ‘unconditional’ right to defer settlement of the liability for at least twelve months after the reporting period...”. In particular, the AASB is aware that in practice the ‘unconditional’ criterion in paragraph 69(d) of IAS 1 is applied in the context of conditions as at the reporting date, which for a going concern would not include bankruptcy or insolvency. context. The proposed clarification of the meaning of unconditional in ED/2011/1, which includes assessing conditionality in the context of bankruptcy or insolvency calls into question how that term should be interpreted in other IFRSs. The AASB is of the view that if the ‘unconditional’ requirement were applied in the proposed context under IAS 1, all liabilities would most likely be classified as ‘current’.
- 1.4 The AASB considers that, if the IASB and the FASB proceed with the proposed requirement for a right to set off to be unconditional and legally enforceable in all circumstances, including at times of bankruptcy or insolvency, it is of such significance that it should be incorporated in the principles of the Standard and not in the guidance. Furthermore, the AASB considers the term should be used consistently across the IFRSs. Accordingly, the IASB and the FASB would need to clarify that the meaning ascribed to the term in ED/2011/1 also applies in IAS 1 (which seems unlikely to lead to the presentation of useful information), or find a new term for the purposes of IAS 1 liability classification.
- 1.5 The AASB also considers that the requirement for reassessment of the right of set off when conditions have changed should be incorporated in the principles of the Standard and not in the guidance.



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### *Offsetting collateralised assets and liabilities against their associated financial assets and financial liabilities*

1.6 The AASB understands that ED/2011/1 prohibits assets pledged as collateral (or the right to reclaim the collateral) or the obligation to return collateral obtained to be offset against the associated financial assets and financial liabilities and the AASB supports this proposal. However, the AASB also understands the implication is that offsetting of derivatives and cash collateral, which can be achieved in some circumstances under IAS 32, would no longer be allowed and considers that this needs to be clarified in the Basis for Conclusions.

### **2 Multi-lateral set off arrangements (Question 3)**

2.1 The AASB supports the conclusion that, although multi-lateral offsetting is likely to be unusual, in principle there is no basis for explicitly excluding multi-lateral set off arrangements from the scope of offsetting if all the criteria proposed in paragraph 6 of ED/2011/1 are met.

### **3 Cost burden versus user benefit disclosures (Question 4)**

3.1 The AASB is supportive of the proposal to provide gross to net reconciliations by class of financial instruments [paragraphs 12(a) and 12(b)] as the AASB considers disaggregations of information, especially those that make up the net amounts of rights and obligations, to be useful to some groups of users.

3.2 However, the AASB considers that proposed paragraphs 12(c), 12(d), 12(e) and 13 are unnecessary and would, in general, provide information that would be overwhelming to users, since those paragraphs apply whether or not the offsetting criteria are met. The AASB has been informed that financial institutions in particular generally do not store historical data in a manner that would readily enable the information proposed in paragraphs 12(c), 12(d), 12(e) and 13 to be prepared. As such, entities may face significant challenges and increased costs to establish and maintain the information systems that would be required.

3.3 The AASB agrees with paragraph BC77 of ED/2011/1 regarding the user benefit in disclosing the value of collateral pledged or obtained as such information aids in the understanding of an entity's net exposure. However, the AASB notes that IFRS 7 *Financial Instruments: Disclosures* already requires detailed disclosures of collateral information in paragraphs 14, 15, 36(a), 36(b) and 38, and ED/2011/1 does not propose an amendment or any cross-reference to existing IFRS 7.

3.4 If the ED/2011/1 disclosures were to proceed, the AASB considers the cost burden and relative usefulness of paragraphs 12(c), 12(d), 12(e), 12(f), 12(g) and 13 of ED/2011/1 need to be considered and rationalised in conjunction with proposed disclosures in



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other financial instruments exposure drafts and existing disclosure requirements in IFRS 7 as a whole. The AASB considers there is an opportunity to have a more cohesive and cost-effective set of disclosure requirements.

### **4 Transition (Question 5)**

- 4.1 The AASB supports the proposed retrospective transition requirements in Appendix A of ED/2011/1. However, the AASB believes that, if the IASB and the FASB are going to persist with the proposed guidance on unconditional right and proposed disclosures in paragraphs 12(c) to 13 of ED/2011/1, there should be sufficient lead time for entities to reassess their existing set off arrangements and to accommodate changes to their information systems.

### **5 Other**

- 5.1 The AASB was informed that a common misinterpretation about offsetting under IAS 32 is that gains and losses of the associated financial assets and financial liabilities are permitted to be offset on the face of Statement of Comprehensive Income. The AASB recommends that the IASB and the FASB clearly identify in a final Standard that such netting of gains and losses is not permitted.