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April 28, 2011

International Accounting Standards Board

30 Cannon Street,  
London EC4M 6XH  
United Kingdom

Dear Sirs,

This letter is the response of the Canadian Accounting Standards Board (AcSB) to the Exposure Draft “Offsetting Financial Assets and Financial Liabilities” issued jointly by the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) (together “the Boards”), in January 2011.

The Canadian Accounting Standards Board (AcSB) is the independent body responsible for setting accounting standards for Canadian private sector entities. The AcSB consists of members from a variety of backgrounds, including preparers, advisors, academics and financial statement users. Additional information about the AcSB can be found at [www.acsb.org](http://www.acsb.org).

The staff of the AcSB consulted various Canadian preparers, practitioners and users. The views expressed in this letter take into account comments and perspectives raised by these stakeholders and AcSB members. However, they do not necessarily represent a common view of the AcSB, its Committees or staff. Views of the AcSB are developed only through due process.

Canadian accounting requirements for offsetting financial assets and financial liabilities, in effect since 1996, are identical to the corresponding requirements in IAS 32. Accordingly, Canadian

entities have more experience applying the requirements than most other entities. The AcSB is not aware that the offsetting requirements have caused any difficulties in practice or are being applied inconsistently in Canada.

We commend the Boards in their efforts to develop requirements for offsetting financial assets and financial liabilities that will converge IFRSs and US GAAP. Having the same offsetting requirements in both sets of standards will improve international comparability between entities and benefit financial statement users.

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

The AcSB agrees with the objective that an entity should offset a recognized financial asset and a recognized financial liability only when the entity has an unconditional and legally enforceable right to set-off and intends to either settle the financial asset and financial liability on a net basis or realize them simultaneously. When an entity meets the proposed offsetting criteria, an entity has a right to, or obligation for, only the net amount that is equivalent to a single net financial asset or financial liability. In these circumstances, offsetting is appropriate.

We also agree that offsetting of financial assets and financial liabilities should be allowed in limited circumstances only (i.e., when the criteria for offsetting are met) and that offsetting should be mandatory when these criteria are met, rather than allowing offsetting to be an accounting policy choice. We think that mandatory application of the offsetting proposals is necessary in order to represent an entity's net position faithfully and to achieve comparability between entities.

In particular, we agree that a settlement is simultaneous only “if settlements take place at the same moment (i.e., there is exposure to only the net or reduced amount)” (paragraph C11). We think that explanation in the application guidance is clear.

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

We agree that the right of set-off should be unconditional and enforceable in all circumstances because it reflects an entity's ability to receive its future cash flows from settling separate financial instruments.

### **Question 3—Multilateral set-off arrangements**

We agree that the offsetting criteria should be applied to both bilateral and multilateral set-off arrangements.

### **Question 4—Disclosures**

We disagree with the disclosure proposals because the required information is excessive and may be too costly and, perhaps, even impractical for entities to provide. We are concerned that the proposals will require significantly more information to be disclosed than is currently required in IFRS 7 *Financial Instruments: Disclosures* while also duplicating some IFRS 7 requirements, which is unnecessary.

We disagree that there is a need to disclose information about the gross amounts of offset items. The very strict requirements for offsetting are designed to result in offsetting only when there is no credit risk exposure. Accordingly, information about the gross amounts of offset items does not appear to serve any useful purpose and no reason for providing it is given in the Basis for Conclusions. The original offset items have essentially disappeared and the unit of account has become the net amount. Thus, only the net amount is the economic phenomenon that is relevant to users and information about its expected future cash flows and risk exposures should be provided.

For financial assets and financial liabilities that are not offset, it is unclear why the general principles for disclosures about financial instruments as set out in IFRS 7 do not result in sufficient information about an entity's financial instruments. For example, paragraphs 36(a) and 36(b) in IFRS 7 already contain disclosure requirements about an entity's credit risk, including collateral provided. Though the Basis for Conclusions notes that "faithful representation requires provision of all relevant information that is necessary for a user to understand the phenomenon being depicted", no explanation is provided as to how these additional disclosures will help users make more informed investing and lending decisions. To balance the information needs of users and provide financial statements that are understandable, we think that users need to explain why each of the additional pieces of disclosure is necessary.

From discussions with preparers and advisors, we understand these disclosures may be very costly and, perhaps, even impractical for entities to provide. For example, few preparers track the information today on a contract by contract basis that could be used to prepare the quantitative disclosures. Entities will incur significant costs to track the gross amounts for financial assets and financial liabilities that are offset, as well as information about those arrangements that do not qualify for offsetting. To report that information, entities may need to rebuild their systems to track the gross amounts.

Therefore, we recommend that the IASB review the level and types of disclosures proposed compared to the existing requirements in IFRS 7 to identify how to enhance existing requirements rather than requiring a new set of disclosures about offsetting and other issues. In proposing to expand the existing disclosure requirements, we urge the Boards to take into account the costs and practicality of any additional disclosures as well as the decision-usefulness of each piece of additional disclosure.

#### **Question 5—Effective date and transition**

- (a) We agree that the proposals should be applied retrospectively for all comparative periods presented because retrospective application provides users with more decision-useful information.
- (b) We think that entities will need two years to implement the new proposals because they will need time to track the information and then apply the proposals. Additionally, since the proposals could significantly affect financial statement ratios for some entities, entities will need sufficient time to revise agreements, such as management or employee remunerations arrangements and financing agreements for debt covenants. For example, debt agreements often place limits on the total amount of allowable debt that could be exceeded if an entity no longer meets the criteria for offsetting. Therefore, we recommend that this amendment should be effective no earlier than January 1, 2014. As explained in our response to the IASB's Request for Views on "Effective Dates and Transition Methods", we do not support setting multiple effective dates for the different phases of the Financial Instruments projects. Instead, we urge the IASB to require all phases of IFRS 9 to become effective at the same time. However, earlier application of phases of IFRS 9 should be permitted because some

entities may have adopted the phases already issued.

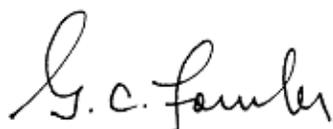
*Cost/benefit considerations*

The Exposure Draft proposals may impose significant additional costs for some entities. Therefore, we think that the Exposure Draft should have asked whether the benefits of the proposals outweigh the costs. Also, to fulfill its due process, the IASB should have documented in the Basis for Conclusions document the cost/benefit analysis it performed when developing the proposals and explained its rationale for the proposals.

We think that the benefits of achieving convergence in the offsetting requirements in IFRSs and US GAAP outweigh the costs, particularly since this difference is the single largest quantitative difference in statements of financial position between IFRSs and US GAAP. However, the benefits of the proposals are mitigated because the extent of additional disclosures that will be required under both IFRSs and US GAAP (see our response to question 4).

We would be pleased to elaborate on our comments in more detail if you require. If so, please contact me, Peter Martin, Director, Accounting Standards at +1 416 204-3276 (email [peter.martin@cica.ca](mailto:peter.martin@cica.ca)) or Grace Lang, Principal, Accounting Standards at +1 416 204-3478 (email [grace.lang@cica.ca](mailto:grace.lang@cica.ca)).

Yours truly,

A handwritten signature in cursive script that reads "G. C. Fowler".

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