



International Accounting Standards Board

30 Cannon Street

London EC4M 6XH

United Kingdom

Transmitted by email to: commentletters@iasb.org

Paris, 28 April 2011

BPCE's response to the Exposure Draft "Offsetting of financial assets and financial liabilities"

BPCE welcomes the IASB invitation for comments on the Exposure Draft "Offsetting of financial assets and financial liabilities ". Groupe BPCE is the second largest banking group in France in terms of retail banking.

BPCE supports the Boards' decision to retain the existing approach in IAS 32- Financial instruments: Presentation, which did not raise concern during the recent financial crisis.

We agree with the proposal to require offsetting only when the entity has an unconditional right and intends to settle net a financial asset and a financial liability. This would provide clear and transparent information on the face of the financial statement of position to users. We agree that offsetting cannot result from a conditional event, i.e. from a default that might or might not happen in the future and that the balance sheet should not represent only counterparty risks.

However, we have a number of concerns about some of the ED's proposals:

- **Cash collateral:** we believe that, under certain circumstances, cash collateral and the associated financial instrument would meet the offsetting conditions. The IASB should clarify this point.
- **Disclosure:** we believe that some of the ED proposals might significantly increase the disclosures requirements for financial instruments without any relevant benefit on financial statements understanding. In particular, we disagree with presenting credit valuation adjustments made at a portfolio level separately from the gross amount of financial instrument since this is more a measurement related issue than an offsetting related issue. Therefore, we recommend that the Board rationalizes the new proposed disclosures in the light of the current requirements of IFRS 7 on credit risk exposures in order to avoid disclosing redundant information.

BPCE



If you wish to discuss our comments further, you may contact Nicolas Patrigot (+ 33 1 58 40 75 93).

Yours sincerely,

A handwritten signature in black ink, appearing to be "E. Filliat".

Eric Filliat
BPCE



Appendix I Detailed comments

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 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?

We agree with the Boards' decision to develop common offsetting criteria for financial assets and liabilities based on the current requirements of IAS 32. These existing requirements are currently globally satisfactory and did not raise concern during the recent financial crisis.

We agree that the right to offset a financial asset and a liability is required only when the entity has both an unconditional and legally enforceable right to set off and intends to do so. This enables the financial statement of position to represent properly the rights and obligations stemming from the entity's financial transactions. It will also reflect the entity's expected cash inflows and outflows.

We therefore agree with the Boards that the proposed approach will provide information that is useful for assessing the entity's ability to generate cash in the future, the nature and amounts of the entity's economic resources and claims against the entity.

We acknowledge that an alternative approach based on conditional rights of offset would better represent the economic credit risk of the entity but share the view that the objective of financial statement of position is not to provide only information on credit risk or an exposure contingent to a future event (i.e. default). The economic credit risk exposure is well suited in disclosures.

However, BPCE still have a concern regarding the treatment of cash collateral. The ED prohibits cash collateral, including margin accounts to be offset with the associated financial assets or liabilities (ED §9 and C14). However, many quoted derivatives with clearing houses give rise to daily margin call which is viewed as a net settlement of the financial position with the Central Counterparty (CCP), i.e. the position is reset at zero everyday. We also note that, under the existing IAS 32 requirements, the main accounting practice is to legally net the daily margin call against the fair value of derivatives. Thus, it is necessary to make a distinction between collateral given or received as a separate guarantee (e.g. guarantee deposit) and some margin call in cash which are not separate guarantees but means of net settlements in substance cash flows of a derivative financial instrument.

Therefore, the IASB should confirm that this prohibition does not prevent from netting a financial instrument with some cash collateral when the offsetting conditions are perfectly met.

Moreover, regarding the intent condition to realise the financial asset and settle the financial liability simultaneously, we do not see the difference between "simultaneously" and "at the same time". We also consider that transactions with clearing house currently meet the simultaneous condition. We would like the Board to explain if it has a different view.



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?

Consistently with our answer to question 1, we consider that the financial assets and liabilities presented on the statement of financial position should not be based on the potential occurrence of a future event (such as counterparty default).

Therefore, we agree with the Boards that a conditional right of set-off (such as a master netting agreement) is not sufficient to require a presentation on a net basis.

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 offsetting 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 by principle with the proposal to keep the scope of the IAS 32 offsetting guidance unchanged and to require offsetting for both bilateral and multilateral arrangements that meet the offsetting criteria.

Question 4—Disclosures

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

We agree that disclosures about rights of set-off and related arrangement should be strengthened since IAS 32 current requirements are very limited. We also agree with the objective of this new disclosure requirements, i.e. to “enable users to understand the effect of those rights and arrangements on the entity’s financial position” (ED §11). Indeed, we consider that the proposed disclosure would help user to understand the economic credit risk exposures by taking into account mitigating agreement such as conditional netting agreement.

However, we have the following concerns regarding the paragraph 12 of the ED :

- The proposed disclosure in §12 requires to show separately the gross amount of financial assets or liabilities and the portfolio-level before adjustment for credit risk of the counterparties. While we do not see any objection to present the gross amounts separately in the financial statements, we have some concerns with the fact to disclose credit-risk information. Portfolio-level adjustments made to incorporate the credit



risk of the counterparties are typical in derivative valuation processes and have not historically been disclosed separately, as they have been considered a component of valuation as opposed to an offsetting adjustment. Therefore, we do not see the rationale for requiring to disclose separately a valuation component next to credit risk mitigation operations (such as physical collateral arrangement for instance). Consequently, we consider that portfolio-level credit risk adjustments are not relevant in a disclosure about rights of set-off and related arrangements.

- IFRS 7 §36 already requires entities to disclose credit risk exposure without taking into account any collateral or other credit enhancement and a description of collateral and other credit enhancements and their financial effect. The new disclosures proposed by the ED would also convey information on collateral. We recommend the Board to avoid the disclosure of redundant information and therefore to revise the current requirements of IFRS 7 in the light of this new proposed disclosure. We would suggest to add a unique note dealing with this issue under IFRS 7 in order to achieve consistent disclosure requirement under IFRS.

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.

(a) We would not support a retrospective application for comparative financial statements. We consider that “the replacement of IAS 39 would potentially imply a significant scale of changes for financial institutions and in our view, specific transitional relief should be provided for accordingly (e.g. : similarly to the first time adoption of IAS 39 in 2005, restatement of comparatives should not be made mandatory for IFRS 9)”. The offsetting of financial instruments is related to IFRS 9 and should follow the same transition requirements, including the specific relief mentioned above.

(b) We consider that the offsetting of financial assets and financial liabilities is related to IFRS 9. Therefore, we consider that the future standard on offsetting should be applicable at the same time than IFRS 9. BPCE considers that such standards should be implemented at a single date with the effective date being no earlier than annual periods beginning on or after 1st January 2015 to allow preparers to carry out the necessary decisions and system changes in the most optimal way, in view of the significant changes the proposed standards are likely to bring to current practice but also to address users’ needs in terms of comparability.