Dear Sir,

**IASB EXPOSURE DRAFT – OFFSETTING FINANCIAL ASSETS AND FINANCIAL LIABILITIES**

The Institute of Chartered Accountants of Pakistan welcomes the opportunity to provide comments on the IASB Exposure Draft – Offsetting Financial Assets and Financial Liabilities.

We appreciate the IASB and FASB's collaborative efforts to develop this joint proposal on offsetting financial assets and financial liabilities in the statement of financial position.

Our detailed responses are enclosed in the Appendix of this letter.

Yours truly,

Muhammad Owais Mukati
Senior Manager Technical Services

Enc.: As above
Appendix

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

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

Comment: Yes, we agree with the proposed requirement to offset when there is an unconditional right and intention to settle net or simultaneously.

Question 2 Unconditional right to set off must be enforceable in all circumstances

Comment: We have some reservations on the proposed requirement. The condition to ensure existence of an unconditional right to offset in all circumstances will have practical difficulties for the preparers of financial statements in anticipation of future situation which may include default and bankruptcy. Specially, in case of bankruptcy there could be a situation where local laws applicable on bankruptcy may conflict with the contractual rights.

Question 3 Multilateral set-off arrangements

Comment: Agreed that offsetting criteria should be applied to both bilateral and multilateral setoff arrangements. Traditionally the offsetting is allowed for arrangements between two parties.

Question 4 Disclosures

Comment: We agree with the proposed enhanced disclosure requirements for financial assets and financial liabilities that have be subject to offsetting as the information will be valuable to the users of financial statements.

Question 5 Effective date and transition

Comment: Agreed except that the retrospective application of the requirements may be cumbersome outweighing the benefits.

Other Matters

Some clarification is required for cases where cash margin / mark to market losses exposure account operates as cash deposit / advance payment to / or from counterparty and that are used in the normal course of events to settle payments or receipt under the transaction. Usually there is right of offsetting the payables with the cash margin and parties also usually intend to settle net. Should the cash margins / mark to market losses exposure be allowed to be offset against the related payable? Or under the ED they are covered within the definition of Collateral and are required to be presented separately without being offset?
Secondly, in current IAS 32 it has been stated that if an entity intends to realize the assets and settle the liability simultaneously an entity shall offset the respective assets and liabilities. The same principle has been carried forward in ED; however simultaneous has been defined as the same moment. The Board has debated the appropriateness of offsetting in statement of financial position and what financial position should portray. It has been stated in BC 8 that "It is a general principle of financial reporting that (a) assets and liabilities are presented separately from each other consistently with their characteristics as resources or obligations of the entity and (b) offsetting recognized assets and recognized liabilities detracts from the ability of users both to understand the transactions, other events and conditions that have occurred and to assess the entity's future cash flows."

Further BC 15 state that "Generally, presenting assets and liabilities net limits the ability of users of financial statements to assess the future economic benefits available to, and obligations of, the entity and hence their ability to assess the entity's financial strengths and weaknesses. Offsetting obscures the existence of some assets and liabilities and thereby reduces users' ability either to assess the entity's liquidity and solvency and its needs for additional financing or to predict how future cash flows will be distributed among those with a claim against the entity."

The addition of simultaneous settlement is odd at what the Board has been stating throughout ED "offsetting a financial asset and a financial liability in the statement of financial position is consistent with the objective of financial reporting only if, on the basis of the rights and obligations associated with a financial asset and a financial liability, the entity has, in effect, a right to or obligation for only the net amount (ie the entity has, in effect, a single net financial asset or financial liability)." Though IASB stated that in simultaneous settlement i.e. where gross amount of cheque issued and gross amount of cheque received, the entity, in effect, has an exposure to net amount. However, it has not been consistent with paragraph 5 (c) of the ED where it has been stated that financial assets and financial liabilities should be presented in statement of financial positions in a manner that provides information that is useful in assessing entity's liquidity and solvency. Though the effect of simultaneous settlement is entity having in effect exposure to net amount however, still an entity has to pay gross and receive gross on respective liabilities and assets so gross presentation better reflect entity's liquidity and solvency position rather netting the two.