May 4, 2011

Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Via Electronic Mail: director@fasb.org, File Reference No. 2011-100

International Accounting Standards Board
30 Cannon Street
London, EC4M 6XH
United Kingdom

Via upload to www.ifrs.org


Dear Sir/Madam:

Standard & Poor’s Ratings Services appreciates the opportunity to provide the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) (collectively, the Boards), our comments on the Boards’ Proposed Accounting Standards Update, Balance Sheet (Topic 210) Offsetting/Exposure Draft ED/2011/1, Offsetting Financial Assets and Financial Liabilities (the Proposed Standard). The views expressed in this letter represent those of Standard & Poor’s Ratings Services and do not address, nor do we intend them to address, the views of any other subsidiary or division of Standard & Poor's Financial Services LLC or of its parent, The McGraw-Hill Companies. We intend our comments to address the analytical needs and expectations of our credit analysts.¹

General
We continue to support international harmonization of accounting standards and believe a common set of high quality and consistently enforced accounting standards would best facilitate efficient global capital markets. We support the Boards’ objective to harmonize

¹ The opinions stated herein are intended to represent Standard & Poor’s Ratings Services’ views on potential changes in accounting and financial reporting standards. Our current ratings criteria are not affected by our comments on the Proposed Standard.
their respective standards in the area of balance sheet offsetting, and generally the proposed offsetting criteria. However, we believe the Proposed Standard would result in greater gross presentation for certain financial assets and financial liabilities for which we believe a net presentation is more appropriate, and thereby reduce credit exposure and liquidity information that is currently available within the statement of financial position under U.S. GAAP that is more meaningful to our analysis. Therefore, we recommend that the Boards include an exception with respect to offsetting when a netting agreement that is legally enforceable in the event of default or bankruptcy is present (e.g., an agreement drafted pursuant to the International Swaps and Derivatives Association (ISDA) master agreement that mandate a settlement on a net basis in the event of non performance). We believe that this exception should be mandated for financial assets and liabilities that are managed on a net basis and that are of a similar nature. Such net presentation should be complemented by additional disclosures as further discussed below. We do not believe assets and liabilities that are distinct in nature—or assets and liabilities that do not have similar characteristics—should be offset. For example, we would not like to see receivables being netted against loans payable or commodity derivatives offsetting FX derivatives even if they would be settled on a net basis in the event of non performance.

In our view, there are several benefits to maintaining the exceptions available under U.S. GAAP when netting agreements are present with the same counterparty. Notably, the net presentation in that case, for like assets and maturities, will provide more meaningful credit and liquidity risk information in our view. This would be the case, in particular, considering that cash or other collateral may change hands quite often. In the event of a bankruptcy or a default-triggered settlement, we believe that the current U.S. GAAP offsetting rules will provide a more representative portrayal of the ultimate settlement amounts. In our view, net presentation in these circumstances will provide greater insight about credit and liquidity risks and how they are managed.

Whether or not the Boards ultimately decide to provide an exception for legally enforceable agreements that call for netting, we believe that the proposed disclosures about the net exposure of an entity would be useful to our analysis of credit and liquidity risks. However, we suggest adding disclosures about counterparty risk and contingent claims information as we further elaborate below (see Disclosures).

**International Consistency**

We historically have not been able to easily compare global companies, partly because of differences in offsetting rules between the two accounting frameworks. Because we rate companies globally, comparable accounting is important to our peer analysis and comparisons. These reporting differences affect the assessment of the resulting key financial metrics that are relevant to our analysis such as return on assets, leverage, and other credit and liquidity ratios. We acknowledge that the difference in the offsetting standards have a significant impact on reported assets and liabilities, and is one of the single largest differences between U.S. GAAP and IFRS, as noted in the “Introduction and Invitation To Comment” section of the Proposed Standard. We believe convergence between U.S. GAAP and IFRS should be a significant consideration and a priority for the Boards in their respective deliberations of the offsetting standard.
Offsetting of Financial Assets and Financial Liabilities

One of the Boards’ objectives in the Proposed Standard is for the financial statements to present useful information to assess the nature and amounts of companies’ economic resources and claims against them. We believe that during the recent financial crisis, gross presentation of balance sheets under IFRS was not considered as meaningful as net presentation to our analysis. We viewed the net presentations applied under U.S. GAAP as more relevant since it better portrayed a company’s net credit and liquidity exposures and economic risks underlying its assets and liabilities—albeit not a complete view of all potential risks. For example, it was our experience during the recent financial crisis that for those financial institutions that had a master netting agreement in place, the net basis presentation was more indicative of the amounts that were eventually settled. We therefore prefer not to separate transactions on the balance sheet where netting agreements exist for like assets and like liabilities that are managed on a net basis.

In addition, the Boards aim for more meaningful presentation of a company’s liquidity and solvency. From a practical viewpoint, in the event of daily settlements, liquidity risk changes daily, making gross presentation less meaningful because transactions may not and will likely not be settled at the gross amounts. Moreover, it is our understanding that derivative dealers manage derivatives liquidity risk on a net position basis and liquidity flows based on net exposure.

Further, for derivatives, companies might collateralize substantial amounts of their exposure. A company’s funding requirements are affected by collateral held and posted. It is our understanding that companies determine margining requirements on a net basis. Under the Proposed Standard, the statement of financial position, and, therefore, balance sheet derived financial measures, may not reflect the specific aspects that are important to our analysis, including liquidity risk.

Multilateral Setoff Arrangements

We generally support the Proposed Standard that the same principles should be applied to both bilateral and multilateral setoff arrangements that meet offsetting criteria. In our view, the number of parties to a contract is not relevant as long as the offsetting criteria are met. We do not view the parties to a bilateral or multilateral contract differently; although one party in a multilateral contract can be more at risk than the others. This also underscores the importance of comprehensive credit risk disclosures that should complement any balance sheet presentation methodology the Boards ultimately decide to mandate.

Disclosures

We support the Boards’ proposal to include disclosures about the gross values of financial assets and financial liabilities, related collateral, and the net exposure. We believe comprehensive disclosure about the nature of the financial assets and financial liabilities including the reconciliation from gross assets/liabilities to net assets/liabilities will provide helpful information to understand financial risks of the company and the financial asset and financial liability exposures. Further, the proposed disclosures will be
an important facet in allowing financial statement users to better comprehend the application and consequences of the Proposed Standard.

We also provide further recommendations for additional disclosures as follows:

- **Counterparty exposure should be disclosed** – The Proposed Standard requires disclosure of information by class of financial instruments after taking into account the characteristics of those financial instruments and the applicable rights of set-off. However, we believe that in practice companies set off financial assets and financial liabilities at a counterparty level. Accordingly, disclosure of the gross and net amounts of financial assets and financial liabilities by counterparty rather than by portfolio would be more meaningful to our analysis. Counterparty exposure disclosures would allow us to better understand the net exposure of a company in line with the way counterparty risks are managed.

- **Net exposure disclosure should include counterparty claims** – In addition, we would support disclosures that provide additional information about derivative counterparty priority claims on a company’s assets or counterparty security interests in the company’s assets.

Further, we previously have commented that we support the development by the Boards of a more structured approach to disclosure in the form of a disclosure framework. We strongly encourage the Boards to work together on this project and on a comprehensive disclosure framework, giving further consideration to additional relevant disclosures related to balance sheet offsetting. Integrating the above on a broader framework will capture counterparty and liquidity risks more completely and holistically.

**Effective Date and Transition**

Given the significant changes to reported balances in the statement of financial position, we believe the retrospective presentation for all comparative periods presented would be most meaningful for peer and period-to-period analysis.
We thank you for the opportunity to provide our comments on the Proposed Standard. We would be pleased to discuss our views with any member of the Boards or your staff. If you have any questions or require additional information, please contact the undersigned.

Very truly yours,

Neri Bukspan
Executive Managing Director, Chief Quality Officer, and Chief Accountant
Standard & Poor’s
neri_bukspan@standardandpoors.com
(212) 438-1792

Joyce Joseph
Managing Director, Corporate & Government Ratings
Standard & Poor’s
joyce_joseph@standardandpoors.com
(212) 438-1217

Shripad Joshi
Director, Corporate & Government Ratings
Standard & Poor’s
shripad_joshi@standardandpoors.com
(212) 438-4069