International Financial Reporting Standards

Exposure Draft - *Offsetting Financial Assets and Financial Liabilities*

ARG meeting, London, 23 February 2011

The views expressed in this presentation are those of the presenter,
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What is offsetting?

Offsetting (netting) is the presentation of one or more financial assets and financial liabilities as a single net amount (the difference between them) in the statement of financial position (balance sheet)

Why an offsetting project?

Currently there are different offsetting requirements for IFRSs and US GAAP preparers

	IFRSs	US GAAP
Number of counterparties	Two or more	Only two
Ability to set-off?	Unconditional	Conditional (as well as unconditional)
Intent to set-off?	Required • Settle net, or • Settle simultaneously	Not required for the following: • Some derivatives & cash collateral • Some repos and reverse repos
Offsetting required or permitted if criteria are met?	Required	Permitted
Focus	Cash flows	Credit risk

Main difference arises around master netting agreements

Why an offsetting project? continued

- Different presentation and disclosures requirements result in reduced comparability
- A company's balance sheet can look very different depending on the offsetting requirements
- Investors do not have sufficient information to make decisions
- Constituents have requested a common solution

Analysis of offsetting today

FY2009 (in 000's of millions)	US GAAP Preparers			IFRS Preparers		
	Bank A1	Bank A2	Bank A3	Bank B1	Bank B2	Bank B3
"Gross" derivative assets (1)	**$1,566**	**$1,495**	**$704**	**$318**	**not available (2)**	**not available (2)**
Less: netting adjustments (3)	(1,485)	(1,414)	(645)	(67)	not available (2)	not available (2)
Derivative assets on statement of financial position	$80	$81	$59	$251	£417	€596
Netted amounts as % of "gross" derivative assets	**95%**	**95%**	**92%**	**21%**	**not available (2)**	**not available (2)**

Total "gross" assets (1)	**$3,517**	**$3,637**	**$2,556**	**$2,431**	**not available (2)**	**not available (2)**
Less: netting adjustments(3)	(1,485)	(1,414)	(699) (5)	(67)	not available (2)	not available (2)
Total assets on statement of financial position (4)	$2,032	$2,223	$1,857	$2,364	£1,379	€1,501
Netted amounts as % of total "gross" assets	**42%**	**38%**	**27%**	**3%**	**not available (2)**	**not available (2)**

Analysis of offsetting today continued

Footnotes to table:

[1] “Gross” derivative assets and total “gross” assets include the offsetting, or netting, adjustments from the published financial statements. This amount may not include all gross amounts as some preparers have not disclosed all adjustments related to repo netting, or netting of trade assets and liabilities.

[2] There are no specific requirements under IFRS 7, *Financial Instruments: Disclosures*, to disclose the amounts that are offset in accordance with IAS 32, *Financial Instruments: Presentation*. As a result, the netting adjustments, as well as total “gross” derivatives and total “gross” assets cannot be determined from the published financial statements as these entities did not disclose the netting adjustments that they made, if any.

[3] These netting adjustments are disclosed in the related notes to the published financial statements.

[4] Per the published statements of financial position or notes to the financial statements.

[5] These adjustments include amounts netted for repurchase agreements and other assets that were not net against the derivative assets.

What is proposed?

Offsetting criteria

Offset a recognised financial asset and a recognised financial liability would be **required** when the entity:

- has an **unconditional** and **legally enforceable right to set off** the financial asset and financial liability; and
- **intends** either:
  - to settle the financial asset and liability on a **net basis**, or
  - to realise the financial asset and settle the financial liability **simultaneously**.

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What is proposed? continued

Definition of terms

- **Right of set-off**

  A debtor's legal right, by contract or otherwise, to settle an amount due to a creditor by applying against that amount all or a portion due from the creditor or a third party

- **Unconditional right of set-off**

  A right of set-off the exercisability of which is not contingent on a future event

- **Legally enforceable right of set-off**

  A right of set-off that is enforceable in all circumstances

- **Simultaneous settlement**

  When realisation of a financial asset and settlement of a financial liability occur at the same moment

What is proposed? continued

Disclosures

- **Enhanced disclosures for financial assets and liabilities, including:**
  - underlying exposures subject to offset
  - effect of set-off and related arrangements on the entity's financial position
- **Disclose separately for financial assets and financial liabilities:**

a.	b.	c.	d.	e.	f.	g.	h.	i.
Gross carrying amounts (before offsetting)	Gross amounts offset	Portfolio-level adjustments	**Net amount presented in financial position** (after taking into effect a, b and c)	Amounts subject to conditional rights of set-off	Amounts subject to unconditional and legally enforceable rights of set-off (but which the entity does not intend settle net or simultaneously)	**Net amounts** (after taking into effect d, e and f)	Cash or other financial instruments held or pledged as collateral	**Net exposure** (after taking into effect g and h)
X	(X)	(X)/X	**X**	(X)	(X)	**X**	(X)	**X**

How might the proposals change accounting in the US?

One study estimates that "companies in the S&P 500 could bring up to **$6.9 trillion** and **$6.8 trillion** of off-balance-sheet derivative assets and liabilities on balance sheet, **increasing assets by 26%** and **liabilities by 33%"***

Exhibit 1: Off-Balance-Sheet Derivative Assets and Liabilities by Sector, S&P 500[1], As of Q3 2010
US$ in millions

Sector	A Gross Derivative Assets[2]	B Net Derivative Assets[2]	A - B Off Balance Sheet Derivative Assets	C Gross Derivative Liabilities[2]	D Net Derivative Liabilities[2]	C - D Off Balance Sheet Derivative Liabilities
Consumer Discretionary	$ 4,948	$ 4,742	$ 206	$ 3,116	$ 2,910	$ 206
Consumer Staples	6,953	6,934	20	5,975	5,902	73
Energy	31,308	14,766	16,542	28,572	11,928	16,644
Financials	7,376,075	486,339	6,889,736	7,131,059	397,351	6,733,708
Health Care	6,214	6,210	4	5,703	5,699	4
Industrials	18,062	12,767	5,295	10,739	5,360	5,379
Information Technology	4,892	4,526	366	4,344	3,978	366
Materials	1,561	1,404	157	2,245	2,084	161
Telecommunication	1,502	1,502	-	1,487	1,487	-
Utilities	51,676	17,009	34,667	54,526	19,223	35,303
Total	**$ 7,503,191**	**$ 556,199**	**$ 6,946,993**	**$ 7,247,766**	**$ 455,922**	**$ 6,791,844**

[1]S&P 500 companies as of September 30, 2010.
[2]Gross derivative fair values and effects of netting per FAS 161 and/or FAS 157 disclosures. Source: Company data, Credit Suisse estimates

* Information and table obtained from Credit Suisse Accounting & Tax Research: "*Grossing Up the Balance Sheet, Nearly $7 Trillion of Derivative Assets and Liabilities Could Land on Balance Sheet*" 01/28/11. Highlighting added

Transition and effective date

- **Retrospective application for all periods presented in financial statements**
- **Effective date to be determined based on feedback**

What's next?

Exposure Draft 28 January 2011

Comment period ends 28 April 2011

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Outreach meetings

Roundtables

- **North America**
- **Europe**
- **Asia**

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IFRS planned Q2 2011

Questions for ARG

Financial Statement Presentation

1. When you look at financial assets and financial liability positions (in particular derivatives), do you need gross amounts, net amounts, or both when analysing financial statements?

Gross	_______
Net	_______
Both	_______

2. With the proposed criteria in mind (see slides 7 and 8) , assuming you need both gross and net information, which amounts would you prefer to see on the face of the statement of financial position (balance sheet) and which should be disclosed in the notes to the financial statements?

	Gross amounts	Net amounts
Statement of financial position	______	______
Notes	______	______
Indifferent	______	______

3. If the proposed criteria for allowing offsetting on the statement of financial position changes, would your answer to Question #2 change? If so, how would it change and why?

Yes	_______
No	_______
Why	_______

Questions for ARG continued

Notes to the Accounts

4. An example of the proposed disclosure table for financial assets and financial liabilities is on Slide 9.

Do you find the proposed disclosures useful?

Yes ______

No ______

Indifferent ______

Please explain your response, including any additional information you would like to see disclosed in the notes to the accounts or any components of the proposed disclosures you find useful if you are not supportive of the entire table.

Questions or comments?

Expressions of individual views by members of the IASB and its staff are encouraged. The views expressed in this presentation are those of the presenter. Official positions of the IASB on accounting matters are determined only after extensive due process and deliberation.