STAFF PAPER

19 November–23 November 2012

IASB Board Meeting

Project	Offsetting Disclosures—Amendments to IFRS 7		
Paper topic	Update		

CONTACT(S)	Barbara Davidson Katherine Cancro	bdavidson@ifrs.org kcancro@ifrs.org	+44 (0)20 7246 6907 +44 (0)20 7246 6928

This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IASB and does not represent the views of the IASB or any individual member of the IASB. Comments on the application of IFRSs do not purport to set out acceptable or unacceptable application of IFRSs. Technical decisions are made in public and reported in IASB *Update*.

Background

1. The different offsetting models in IFRS and US GAAP result in significant differences between amounts presented in statements of financial position prepared in accordance with IFRSs and those prepared in accordance with US GAAP, particularly for entities that have large amounts of derivative activities.

2. In January 2011, in response to requests from users of financial statements and recommendations from the Financial Stability Board to achieve convergence of the boards' requirements for offsetting financial assets and financial liabilities, the IASB and the FASB (the boards) published the Exposure Draft *Offsetting Financial Assets and Financial Liabilities*. The proposals in the Exposure Draft would have replaced the requirements for offsetting financial assets and financial liabilities and would have established a common approach with the FASB. However, after considering the responses to the Exposure Draft, the boards decided to maintain their respective offsetting models.

3. Instead the boards agreed on converged disclosures. The stated objective of the disclosures is to allow users of financial statements to evaluate the effect or potential effect of netting arrangements, including rights of set-off associated with an entity's recognised financial assets and recognised financial liabilities, on the

The IASB is the independent standard-setting body of the IFRS Foundation, a not-for-profit corporation promoting the adoption of IFRSs. For more information visit www.ifrs.org

entity's financial position[1]. In addition, a benefit of having converged requirements is that the disclosures would also allow users of financial statements to compare the financial statements of IFRS and US GAAP preparers.

4. The new disclosures apply to:

   (a) financial assets and financial liabilities that are actually set off in the statement of financial position; and

   (b) financial assets and financial liabilities that are subject to enforceable master netting arrangements or similar agreements, even if they are not set off in the statement of financial position.

5. The joint offsetting disclosure requirements *Disclosures-Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7)*[2] were published in December 2011. They are effective from 1 January 2013.

Purpose of this paper

6. On 31 October 2012, as a result of feedback received from stakeholders, the FASB tentatively decided to amend the scope of its related disclosure requirements (Update 2011-11) from the previously converged scope (as described in paragraph 4 above). The purpose of this paper is to update the IASB on the FASB's recent decisions. We are not asking the IASB to make any decisions.

---

[1] Paragraph 13B of IFRS 7 *Financial Instruments: Disclosures*: *An entity shall disclose information to enable users of its financial statements to evaluate the effect or potential effect of netting arrangements on the entity's financial position. This includes the effect or potential effect of rights of set-off associated with the entity's recognised financial assets and recognised financial liabilities that are within the scope of paragraph 13A.*

[2] The equivalent document by the FASB is called Accounting Standards Update No. 2011-11, *Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities* (Update 2011-11).

FASB discussions

7. In October 2012 the FASB staff reported that preparers of US GAAP financial statements had identified implementation issues, and inconsistency in planned practice, on whether the following are within the scope of Update 2011-11:

   (a) trade receivables and trade payables; and

   (b) unsettled regular-way trades[3].

8. The FASB staff reported that constituents asked that the FASB consider the above items in the context of objectives of the disclosures, operationality, and analysis of costs versus benefits[4]. Consequently, the FASB decided to add a project to its agenda to clarify and amend what instruments should be within the scope of Update 2011-11.

Trade receivables and trade payables

9. The FASB staff reported that their constituents were concerned because, based on their initial review of a selection of contracts, many trade payable and trade receivable transactions were entered into under master netting or similar agreements and would therefore be included within the scope of the required disclosures. For example, the US constituents indicated that many standard commercial contracts between customers and suppliers are subject to provisions that provide for a legal right of set-off in event of default and, therefore, they believed that these contracts would be considered to be within the scope.

---

[3] Regular way trades (or regular way purchases/sales, as they are referred to in IFRS) in US GAAP include both of the following:

> *a. All transactions in exchange-traded financial instruments that are expected to settle within the standard settlement cycle of that exchange (for example, three days for U.S. exchanges).*
>
> *b. All transactions in cash-market-traded financial instruments that are expected to settle within the time frame prevalent or traditional for each specific instrument (for example, for U.S. government securities, one or two days).*
>
> (ASC 940-20-45-3)

A regular way purchase or sale in IFRS is a *purchase or sale of a financial asset under a contract whose terms require delivery of the asset within the time frame established generally by regulation or convention in the marketplace concerned.* (IFRS 9 *Financial Instruments* Appendix A)

[4] Per the FASB's 31 October 2012 Board Meeting Handout *Balance Sheet Offsetting: Scope Clarification of 2011-11* (the FASB's Board Meeting Handout), available at www.fasb.org.

Unsettled regular-way trades

10. In US GAAP these transactions must be recorded on trade date.[5] [6] However, US GAAP also has a broker-dealer industry based exception that permits set-off of trade date receivables/payables for unsettled regular-way trades[7]. In contrast, IFRS allows entities to choose between trade date and settlement date accounting for such transactions[8] [9], but would only permit (and at that point require) offsetting if the offsetting requirements in IAS 32 *Financial Instruments: Presentation* are met.

11. The FASB staff reported that during the initial drafting of the scope requirements constituents indicated that such transactions would not fall into the scope of the proposed disclosures. However, upon further review of their agreements, US stakeholders now believe that they have entered into such transactions under an enforceable master netting arrangement and that those transactions are therefore within the scope of the disclosures.

Objective of the disclosures

12. The FASB staff state that the objective of the disclosures is *to provide information for users of financial statements to facilitate the comparison between those entities that prepare their financial statements on the basis of U.S. GAAP with those that present their financial statements on the basis of IFRS. As it relates to trade payables and trade receivables they would have similar presentation under both IFRS and US GAAP*[10].

13. The FASB staff further reported that including unsettled regular-way trades would not improve comparability between US GAAP and IFRS financial statements,

---

[5] For example, under ASC 940-320-25-1

[6] Trade date is the date that an entity commits itself to purchase or sell an asset, while settlement date is the date that an asset is delivered to or by an entity.

[7] Payables and receivables arising from unsettled regular-way trades may be recorded net in an account titled net receivable (or payable) for unsettled regular-way trades. (ASC 940-320-45-3)

[8] IFRS 9 Paragraph B3.1.3

[9] Trade date accounting/settlement date accounting essentially determines the date on which the related asset is recognised on acquisition or derecognised on sale/disposal.

[10] Per the FASB's Board Meeting Handout

because the requirements for such trades are different in IFRS and their understanding is that IFRS preparers mainly apply settlement date accounting.[11]

Operationality of the disclosures

14. Loans and customer deposits at the same financial institution are excluded from the disclosure requirements (**unless** they are already set off in the statement of financial position)[12]. The Basis for Conclusions on IFRS 7 cites reasons for the exclusion, including: operational burden, that such rights are often a result of statute, and that such rights are primarily a credit enhancement rather than a way of mitigating credit risk. Some US constituents have suggested that the FASB refer to these requirements when considering whether trade payables and receivables and unsettled regular-way trades be included in the disclosures.

15. Some US constituents are also concerned that the amount of time required to implement the disclosures would be significant and therefore the disclosures would not be possible for these items given the effective date. Inclusion of trade payables and receivables in the scope would require a *comprehensive review of all contracts to determine if the provisions of each contract would be considered a master netting arrangement or similar agreement, which would not be operational given the current effective date.*[13] Similarly, US constituents state concerns about the inclusion of unsettled regular-way trades because this would *require a system by system analysis of the related activity as this information is not currently tracked.*[14] Consequently, they do not have the ability to generate such gross information for disclosure purposes on a timely basis, if at all.

Costs versus benefits of the disclosures

16. US constituents noted that the costs of including such items in the disclosures would be significant while the benefits would be minimal. For example, they

---

[11] Since the FASB Board meeting the IASB staff has reached out to various IFRS preparers and gathered preliminary information that many IFRS preparers do apply trade date accounting for their regular way purchases /sales.

[12] IFRS 7 Paragraphs BC24H and BC24I

[13] Per the FASB's Board Meeting Handout

[14] Ibid.

stated that *users do not request information related to these instruments when discussing the offsetting disclosure requirements because they are not significant reconciling items between U.S. GAAP and IFRS and, therefore, there is no related benefit*[15]. In addition, they noted that *the Exposure Draft and discussions leading up to the final was primarily focused on presentation of derivatives, repurchase agreements, and securities lending*.[16]

FASB tentative decisions

17. As a result of the feedback received and the timing of the effective date of the disclosures, **the FASB tentatively decided to amend the scope of its offsetting disclosure requirements by limiting their scope to derivatives, sale and repurchase agreements and reverse sale and repurchase agreements, and securities borrowing and lending arrangements**.

18. The IASB staff note that transactions that result in the greatest differences in IFRS and US GAAP statements of financial position (ie derivatives) **would** still be within the scope of the disclosures. As a result, comparability would still be improved for users of financial statements.

19. However, if the FASB's tentative decisions are finalised, the offsetting disclosures in IFRS and US GAAP would cover different items. This would mean that the information provided about offsetting arrangements would be more comprehensive for IFRS preparers. In particular, even if items are set off in the financial statements, if they are not of the type listed, the offsetting disclosures would not be provided by US GAAP preparers. For example, if a trade receivable and trade payable were actually set off in the statement of financial position, an IFRS preparer would be required to provide information about the underlying gross balances whereas a US GAAP preparer would not.

20. The FASB's proposed amendments would be effective from 1 January 2013. An Exposure Draft of the proposed amendments is expected to be issued in November for a 25-day comment period.

---

[15] Per the FASB's Board Meeting Handout

[16] Ibid.

IASB staff analysis

21. Before the FASB discussed this issue, we had **not** been aware of similar concerns from IFRS preparers regarding the offsetting disclosures. However, since the FASB has made its tentative decisions we have received questions about whether we will provide similar relief. This is particularly the case because the scope was converged and this was a joint project.

22. The IASB staff do not recommend that the IASB consider changing the scope of the disclosures. As stated above, we have not been made aware of scope issues such as those raised by the FASB. The current application guidance (for example, in paragraph B41[17]) is already clear regarding the types of arrangements that are within the scope. The scope also includes any transactions that are currently being set off in the statement of financial position.

23. Consistent with the wording in the disclosure requirements, the IASB staff are of the view that one of the key objectives of the disclosures is to provide more information about offsetting and credit risk mitigation. This would include the effect of netting arrangements on the entity's financial position. The current scope is consistent with that objective.

24. The IASB staff are not sure that the scope exclusion related to conditional rights to set off loans and customer deposits can **automatically** be applied to trade receivables/payables and unsettled regular way trades. Such rights are often a result of statute. The lender will typically look to the underlying property as collateral for the receivable and the main source of credit mitigation. More importantly, **the scope of the disclosures does not exclude these transactions if they are set off in the statement of financial position**.

25. In addition, the boards have already limited the scope from that proposed in the Exposure Draft. Further reducing the scope of the disclosures by excluding items

---

[17] IFRS 7 Paragraph B41: *The similar agreements referred to in paragraphs 13A and B40 include derivative clearing agreements, global master repurchase agreements, global master securities lending agreements, and any related rights to financial collateral. The similar financial instruments and transactions referred to in paragraph B40 include derivatives, sale and repurchase agreements, reverse sale and repurchase agreements, securities borrowing, and securities lending agreements. Examples of financial instruments that are not within the scope of paragraph 13A are loans and customer deposits at the same institution (unless they are set off in the statement of financial position), and financial instruments that are subject only to a collateral agreement.*

for which the netting requirements are the same under IFRS and US GAAP, and that are already set off in the statement of financial position, would not, in the view of the IASB staff, meet the stated objective of the disclosures, which is to provide information to users of financial statements about the amounts that are currently being offset under the related requirements.

26. As previously noted, a benefit of having converged requirements is that the disclosures would also allow users of financial statements to compare the financial statements of IFRS and US GAAP preparers. However, this is not the sole or stated objective of the disclosures. While discussions during the Exposure Draft may have focused on the instruments that result in the main differences between IFRS and US GAAP, they did not exclude other types of arrangements that would also meet the requirements. We undertook extensive outreach with users of financial statements as part of the offsetting project. During that outreach users expressed an interest in better understanding offsetting (and the effect of netting arrangements). Automatically excluding information subject to different accounting treatment, for example, regular-way trades, may inappropriately reduce the information that users need to compare IFRS and US GAAP financial statements.

27. Entities may also enter into similar arrangements that meet the objectives of the disclosures but that are not referred to as derivatives/repurchase agreements, etc. If the scope is limited, such arrangements could be inappropriately excluded from the scope of the disclosure requirements.

28. Finally, because of the need to comply with the required due process steps, we could not provide relief before the mandatory effective date of 1 January 2013. Because the change would reduce information that would otherwise be available to users of financial statements, the staff are of the view that at a comment period of at least 90 days would be required.