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n°70

Paris 14th April 2011

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

Re : Exposure draft 2011/1 : Offsetting of financial assets and financial liabilities

Dear Sir David,

I am writing on behalf of the Autorité des Normes Comptables (ANC) to express our views on the above-mentioned exposure draft.

The ANC welcomes the IASB's and the FASB's consideration of stakeholders' concern that the current difference between the IFRS and US GAAP approaches to the netting of financial assets and liabilities can result in significant differences in the total assets of financial institutions and thus have significant consequences on financial ratios. Providing a common solution consistently applied both under IFRS and US GAAP is the most important target to reach.

Regarding the proposed offsetting criteria, we support the Boards' decision to retain the existing approach in IAS 32, which did not raise concerns 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, which will provide clear and transparent information on the face of the statement of financial position. We agree that offsetting cannot result from a conditional event, i.e. from a default that might or might not happen in the future. We also agree that the balance sheet should not represent only counterparty risks.

However, we disagree with some of the ED's proposals on:

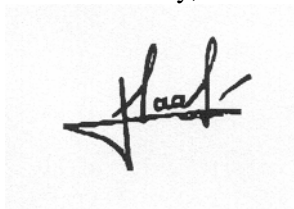
- Cash collateral: we believe that, under certain circumstances, margin calls with clearing houses and the associated financial instrument would meet the offsetting conditions. The IASB should reconsider this point.
- Disclosure:
 - We disagree with presenting credit valuation adjustments made at a portfolio level separately from the gross amount of the financial instruments since and is not relevant in terms of offsetting of financial assets and liabilities.

- We recommend that the Board rationalises 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.

Our detailed comments on the ED are set out in the Appendix I to this letter.

If you have any questions concerning our comments, we would be pleased to discuss them.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Haas', with a stylized flourish extending to the left.

Jérôme Haas

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 concerns during the recent financial crisis.

We agree to require an entity to offset a financial asset and a liability only when the entity has both an unconditional and legally enforceable right to offset and intends to do so. This enables the statement of financial 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 the statement of financial 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.

Having said that, we 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 a daily margin call which is viewed as a net settlement of the financial position with such central counterparties, 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 net the daily margin call against the fair value of derivatives. Thus, it is necessary to distinguish between collateral given or received as a separate guarantee (e.g. guarantee deposit) that is enforced in case of default and margin calls in cash which are not conditional on default and are considered as a means of settlement of the underlying financial instruments.

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

Moreover, regarding the condition to realise the financial asset and settle the financial liability simultaneously, we do not see any difference between "simultaneously" and "at the same time". We also consider that transactions with clearing houses currently meet the simultaneous condition. We would like the Board to provide explanations 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 Q1, 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 offset (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 that, by principle, a multilateral arrangement should not be excluded from the net presentation requirements if the offsetting criteria are met.

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 to offset and related arrangements should be strengthened since the current requirements in IAS 32 are very limited. We also agree with the objective of these 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 disclosures would help readers understand the economic credit risk exposures by taking into account mitigating agreements such as conditional netting agreements.

However, we disagree with the following in paragraph 12 of the ED:

- the proposed disclosure in par. 12 requires that the gross amount of financial assets or liabilities and the portfolio-level before adjustment for credit risk of the counterparties be shown separately. Portfolio-level adjustments related to the credit risk of the counterparties, similarly to expected loss depreciation on financial assets at amortised cost, does not constitute a right to offset and is not related to the netting issue addressed by the ED. Therefore, we do not see the rationale for requiring that such information be disclosed separately next to rights to offset and related arrangements (such as physical collateral arrangement for instance). We consider that portfolio-level credit risk adjustments are not relevant in a disclosure about offsetting of financial assets and liabilities. Moreover, since such adjustments are measured on a net portfolio basis, it would be practically difficult to allocate by class of gross assets or liabilities.

- IFRS 7 par. 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 that the Board avoids requiring disclosure of redundant information and therefore that the current requirements of IFRS 7 be revised in the light of this new proposed disclosure. One way to achieve consistent disclosure requirements would be to rationalise under the same standard (i.e. IFRS 7) a unique note dealing with this issue.

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) As explained in our comment letter to the *Rfv Effective Dates and Transition Methods*, 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 revision of IAS 39. Therefore, we consider that the future standard on offsetting should be applicable at the same time as IFRS 9. Consistently with our answer to the *Rfv Effective Dates and Transition Methods*, “under the assumption that the proposed standards are actually issued by 30th June 2011, and coming from a jurisdiction where IFRS have been applied since 2005, the ANC 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** (in other words allowing three to four years for implementation) 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.”.