

19th May 2011

International Accounting Standards Board
1st Floor 30 Cannon Street
London EC4M 6XH
United Kingdom

(By email: director@iasb.org)

Dear Sirs,

RESPONSE TO EXPOSURE DRAFT – OFFSETTING FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The Institute of Certified Public Accountants of Singapore (ICPAS) appreciates the opportunity to comment on the above exposure draft (ED) issued by the International Accounting Standards Board (IASB) in January 2011. ICPAS supports the IASB and US Financial Accounting Standards Board (FASB) in their joint proposal to establish a common approach to offsetting and improve comparability among the companies.

Our comments on the specific questions in the ED are as follows:

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?

The proposals in the ED are largely consistent with the current IAS 32. We are of the view that the principles do adequately scope the application of offsetting for groups of financial assets and liabilities, with the exception of some concerns as explained below.

Simultaneous Settlement

We are of the view that the definition of “simultaneous” in Appendix C11 for the realisation of a financial asset and settlement of a financial liability is overly prescriptive. Apart from determining that settlements take place at the same moment, paragraph C11 of the ED adds that if settlements take place over a period (even though during this period there is no potential for any change in value of the financial asset and financial liability, and the period between the settlements of the instrument is brief), it is not a simultaneous settlement. The concern for settlements is the exposure to credit or liquidity risk, where settlements risk changes in values as they occur over a brief period of time. Principally, where there is no potential change in value, the ED should not be overly concern on the timing of the settlement.

Currently, financial intermediaries and clearing houses may have certain arrangements, where actual offsetting is processed in batches once or twice a day, rather than on a continuous basis. We are concerned that the offsetting of financial assets and financial liabilities is not allowed under the proposed rules in Appendix C11, even though there may not be exposure to credit or liquid risk. Thus, we would like the Board to consider conducting additional research into the operational issues surrounding the process for offsetting in practice, in order to allow for offsetting in the above circumstances.

Margin Accounts as a Form of Collateral

Paragraph C14 of the ED proposes that margin accounts are treated as a form of collateral and that an entity shall not offset recognised financial assets and financial liabilities with assets pledged as collateral. In practice, the delivering and receiving of the margin account as collateral are under enforceable arrangements and specifically undertaken for the purpose of managing credit and liquidity risks. Where margin accounts do meet the requirements of an unconditional and legally enforceable right to set off the financial asset and financial liability and intends to settle it on a net basis, it is hard to argue conceptually that the presentation for margin accounts cannot be presented net on the face of the statement of financial position to reflect the nature and amounts of the entity’s economic resources and claims against the entity.

Due to the proposed changes in paragraph C14 of the ED, we note that financial institutions may need to gross up their margin accounts (assets) on the statement of financial position and net financial assets/liabilities from the positions taken on behalf of their customers. The banks may have to re-assess their business models and balance sheet limits due to a change in accounting principles, where there has been no fundamental change in the strategy of the business and operational matters. Based on the considerations above, we disagree that margin accounts are not allowed to be offset.

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?

Insolvency or Bankruptcy Situations

Paragraph 10(e) of the ED proposes that the right of set-off has to be enforceable in all circumstances, including insolvency or bankruptcy of a counterparty situation. We are concerned that this may not be a practical application. In Singapore, where a company receives a winding up order from the Court due to insolvency, the Courts have the power to void any execution of the company's property and the Courts may appoint a liquidator to carry out duties to wind up the company. The Court may also decide that any transactions that were undervalued or any transactions where the company has given an unfair preference to a creditor or an associate would be void or voidable. This would mean that even if a company has contractual rights to offset particular financial assets and financial liabilities, the Courts may decide to void the transaction if unfair preference was deemed present. If the proposal in the ED was applied, Companies may only be able to recognise the right of set-off after the legal period, which may not be practical and operationally challenging to track.

In our view, the meaning of legally enforceable could result in differing interpretations when applied in practice. We are of the view that the right of set-off is an important element but the ED should provide further clarification that although contractual rights may be challenged in Courts, the right to challenge should not preclude an entity from offsetting the financial assets and financial liabilities.

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 offsetting criteria should apply to both bilateral and multilateral set-off arrangements.

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?

In light of the limited circumstances under which offsetting are allowed, we are of the view that the disclosure requirements seem to be overly burdensome for preparers. In general, IFRS 7 require adequate disclosures of risks relating to all financial instruments and any additional disclosure requirements should be dealt with in the context of IFRS 7. We are of the view that some of the proposed disclosure requirements would require extensive data mining and some tabular disclosure requirements by class may be of limited value as offsetting is done across classes.

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) We agree with the proposed transition requirements and that the retrospective application would be important for comparability for period-on-period comparison.
- (b) The period an entity would take to implement the proposed requirements would depend on the nature of the business. We would expect financial institutions to take more time in implementing due to the volume of transactions with the same counterparty.

Should you require any further clarification, please feel free to contact Ms Grace Chua, Technical Manager, from ICPAS via email at grace.chua@icpas.org.sg.

Yours faithfully,



Janet Tan
Executive Director