Straight away

IFRS bulletin from PwC

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IASB clarifies offsetting requirements and requires new converged disclosures

What is the issue?

The IASB has issued an amendment to the application guidance in IAS 32, 'Financial instruments: Presentation', to clarify some of the requirements for offsetting financial assets and financial liabilities on the statement of financial position.

However, the clarified offsetting requirements for amounts presented in the statement of financial position continue to be different from US GAAP. As a result, the IASB has also published an amendment to IFRS 7, 'Financial instruments: Disclosures', reflecting the joint requirements with the FASB to enhance current offsetting disclosures. These new disclosures are intended to facilitate comparison between those entities that prepare IFRS financial statements to those that prepare financial statements in accordance with US GAAP.

Key provisions

The amendments do not change the current offsetting model in IAS 32, which requires an entity to offset a financial asset and financial liability in the statement of financial position only when the entity currently has a legally enforceable right of set-off and intends either to settle the asset and liability on a net basis or to realise the asset and settle the liability simultaneously.

The amendments clarify that the right of set-off must be available today – that is, it is not contingent on a future event. It also must be legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy.

The amendments also clarify that gross settlement mechanisms (such as through a clearing house) with features that both (i) eliminate credit and liquidity risk and (ii) process receivables and payables in a single settlement process, are effectively equivalent to net settlement; they would therefore satisfy the IAS 32 criterion in these instances.

Master netting agreements where the legal right of offset is only enforceable on the occurrence of some future event, such as default of the counterparty, continue not to meet the offsetting requirements.

Disclosures

The amended disclosures will require more extensive disclosures than are currently required under IFRS and US GAAP. The disclosures focus on

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quantitative information about recognised financial instruments that are offset in the statement of financial position, as well as those recognised financial instruments that are subject to master netting or similar arrangements irrespective of whether they are offset.

Transition and effective date

The converged offsetting disclosures in IFRS 7 are to be retrospectively applied, with an effective date of annual periods beginning on or after 1 January 2013.

However, the clarifications to the application guidance in IAS 32 are to be retrospectively applied, with an effective date of annual periods beginning on or after 1 January 2014.

Am I affected?

These amendments primarily affect financial institutions, as they will be required to provide additional disclosures described above. However, other entities that hold financial instruments that may be subject to offsetting rules will also be affected.

What do I need to do?

Management should begin gathering the information necessary to prepare the new disclosure requirements. Management will also need to investigate whether the clarifications of the offsetting principle in IAS 32 result in any changes to what they offset in the statement of financial position today. Management may need to work with the clearing houses they use to determine whether their settlement processes comply with the new requirements.