

<b>Q&amp;A CNC 19/016</b>	<b><u>QUESTIONS / ANSWERS :</u></b>  <b>ACCOUNTING SET-OFF OF ORDERS IN PROGRESS AND PAYMENTS RECEIVED ON ACCOUNT OF ORDERS</b>
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**Question:**

Can an undertaking presenting its annual accounts in accordance with LUX GAAP or LUX GAAP – FV offset the asset item “orders in progress” against the liability item “payments received on account of orders”?

**Answer:**

**1. General principle of non-offsetting and exceptions**

Article 33 LRCS<sup>1</sup> establishes the general principle of non-offsetting between assets and liabilities or between expenses and income.

However, there are exceptions to this accounting principle that may result from the right to offset under the law<sup>2</sup>.

**2. Exception applicable to the presentation of orders in progress and of payments received on account of orders**

In accordance with the accounting principle of non-offsetting, work and orders in progress by the undertaking are generally presented under the heading ‘D.I. Stocks / Inventories’ within assets, while payments received on account of orders are generally presented under the heading ‘C. Creditors’ under capital, reserves and liabilities.

In accordance with European accounting law, Luxembourg accounting law has provided for an exception on this point. The balance sheet layout in Article 34 LRCS explicitly provides for an item entitled “C.3. Payments received on account of orders in so far as they are not shown separately as deduction from stocks”<sup>3</sup>, the wording of which is identical to that provided for in Directive 2013/34/EU<sup>4</sup> and the former 4<sup>th</sup> Directive 78/660/EEC<sup>5</sup>.

This explicit wording leads to the conclusion that it is possible for undertakings (optional) to offset the stock / inventory item corresponding to orders in progress against the liability item corresponding to payments received on account of those orders.

This analysis is confirmed by the preparatory parliamentary works which led to the adoption of the Law of 4 May 1984 (Section XIII LSC)<sup>6</sup>, which has now been repealed and replaced by Title II LRCS, but whose substance remains unchanged on this point.

<sup>1</sup> Art. 33 LRCS

*“Any set-off between asset and liability items or between income and expenditures items shall be prohibited without prejudice to the cases where there is a right of set-off pursuant to the law. In cases where a set-off has been performed between asset and liability items or between income and expenditures items, the amounts set-off shall be specified as gross amounts in the notes to the accounts”.*

<sup>2</sup> See: Parliamentary document 2657-0 (1982-1983), commentary on the articles, Art. 211.: “(...) Under this principle, offsetting debts payable against claims receivable is prohibited. This accounting rule obviously does not apply to legal offsetting, which is a rule of civil law. (...) A few exceptions remain; the directive itself provides for a limited number of cases where offsetting is permitted, provided that it is clearly indicated”.

<sup>3</sup> See: Annex I of the Grand Ducal Regulation of 18 December 2015 determining the form and content of the layouts of balance sheets and profit and loss accounts and implementing Articles 34, 35, 46 and 47 of the amended Law of 19 December 2002 on the Trade and companies register, as well as on the bookkeeping and annual accounts of undertakings.

<sup>4</sup> See: Annex III ‘Horizontal balance sheet format provided for in Article 10’ and Annex IV ‘Vertical balance sheet format provided for in Article 10’ of Directive 2013/34/EU.

<sup>5</sup> See: Articles 9 and 10 of the 4<sup>th</sup> Directive 78/660/EEC.

<sup>6</sup> See: Parliamentary Document 2657-0 (1982-1983), commentary on the articles:

- Art. 211 : “(...) There are a few exceptions; the directive itself provides for a limited number of cases where offsetting is permitted, provided that it is clearly indicated. Thus, payments received on account of orders normally appearing as liabilities may be deducted from stock / inventories on the assets side, if the deduction is made separately”.

- Art. 213 : « (...) C. Creditors. “(...) As indicated by its wording, the item ‘Payments received on account of orders’ could also be deducted in a visible manner from the assets under the item ‘Stocks / Inventories’.”

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**3. Application rules in the event of an accounting offsetting**

Offsetting as referred to in point 2 has several implications for undertakings choosing to use this presentation method. In particular, undertakings opting for offsetting must:

- carry out a separate assessment of each contract<sup>7</sup>;
- make provisions, where applicable, for risks related to the continued execution of orders in progress, to the extent that these risks are not covered by value adjustments recognised in accordance with section 61 LRCS;
- present the debit balance under the heading 'D.I. Stocks / Inventories' when the amount of work and orders in progress exceeds the amount of advance payments received for a given contract;
- present the credit balance under the heading 'C. Creditors' when the amount of payments received on account of orders exceeds the amount of work and orders in progress for a given contract;
- disclose in the notes to the accounts, the accounting methods and measurement / valuation bases adopted for orders in progress and payments received on account of orders<sup>8</sup>;
- provide in the notes a breakdown of the gross amounts (un-offset)<sup>9</sup>.

It should be noted that if offsetting can be carried out in the balance sheet, these items (orders in progress and payments received on account of orders) must nevertheless be presented separately in the trial balance prepared in accordance with the Standard chart of accounts (PCN) to be filed with the Trade and companies register (RCS). The undertaking should therefore use, for example, accounts 312 'Contracts in progress – Goods' and 431 'Down payment received within one year' within the PCN, even if, in the balance sheet, the amounts entered in these two PCN accounts are grouped together under the same item "C.3. Payments received on account of orders in so far as they are not shown separately as deduction from stocks (inventories)"<sup>10</sup>.

**4. Impact on external users of the accounts**

Without calling into question the above, it should be noted that the use of the option to offset orders in progress against payments received on account is not neutral for external users of the accounts, as it results in a change in the presentation of the undertaking's financial position.

In this context, it is important that the use of the offsetting option be respectful of the rights of shareholders and third parties to accounting information that gives a true and fair view of the undertaking's assets and liabilities, financial position and net profit or loss. The members of the administrative or management bodies of the undertakings concerned must ensure, in particular, that the principle of consistency of accounting policies is complied with and they can be held liable in the event of misuse.

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<sup>7</sup> Pursuant to Article 51(1)(e) LRCS, "the components of asset and liability items must be valued separately".

<sup>8</sup> Article 65 (1) 1° LRCS provides that the notes must include information on "accounting policies and measurement bases".

<sup>9</sup> Article 33, 2<sup>nd</sup> sentence LRCS provides that "[i]n cases where a set-off has been performed between asset and liability items or between income and expenditures items, the amounts set-off shall be specified as gross amounts in the notes to the accounts".

<sup>10</sup> In the event that the amount of payments received on account of orders exceeds the amount of work and orders in progress.

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