January 21, 2022

International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Board Members:

Consejo Mexicano de Normas de Información Financiera (CINIF), the accounting standard setting body in Mexico, welcomes the opportunity to submit its comments on the Request for Information regarding the Post-implementation Review of IFRS 9, *Financial Instruments*, Classification and Measurement (the RFI). Set forth below you will find our comments on the RFI.

Overall comments

We conducted outreach with selected groups that could provide us with appropriate feedback on the RFI. The overall conclusion from such outreach is that the application of the new requirements prescribed by IFRS 9 has not generated significant issues or problems. Nevertheless, we received some specific comments that are described below.

Answers to specific questions

Set forth below are our answers to the specific questions included in the RFI.

Question 1—Classification and measurement
Do the classification and measurement requirements in IFRS 9: (a) enable an entity to align the measurement of financial assets with the cash flow characteristics of the assets and how the entity expects to manage them? Why or why not? (b) result in an entity providing useful information to the users of the financial statements about the amount, timing and uncertainty of future cash flows? Why or why not? Please provide information about the effects of the classification and measurement changes introduced by IFRS 9, including the ongoing costs and benefits in preparing, auditing, enforcing or using information about financial instruments. This question aims to help the Board understand respondents' overall views and experiences relating to the IFRS 9 classification and measurement requirements. Sections 2–8 seek more detailed information on the specific requirements.

Our outreach showed that the classification requirements in IFRS 9 enable an entity to align the measurement of financial assets with the cash flow characteristics of the assets and result in an entity providing useful information to the users of the financial statements about the amount, timing and uncertainty of future cash flows. There were no adverse comments regarding the classification and measurement requirements.

Question 2—Business model for managing financial assets
(a) Is the business model assessment working as the Board intended? Why or why not? Please explain whether requiring entities to classify and measure financial assets based on the business model assessment achieves the Board's objective of entities providing users of financial statements with useful information about how an entity manages its financial assets to generate cash flows. (b) Can the business model assessment be applied consistently? Why or why not? Please explain whether the distinction between the different business models in IFRS 9 is clear and whether the application guidance on the evidence an entity considers in determining the business model is sufficient. (c) Are there any unexpected effects arising from the business model assessment? How significant are these effects? Please explain the costs and benefits of the business model assessment, considering any financial reporting or operational effects for preparers of financial statements, users of financial statements, auditors or regulators. In responding to (a)–(c), please include information about reclassification of financial assets (see Spotlight 2).

Overall, our outreach indicated that the business model assessment is working as the Board intended. One observation was that IFRS 9 states that a change in business model is "significant to the entity's operations" and is expected to be "very infrequent". However, our outreach pointed out that there is no definition of "very infrequent" in the standard, which would assist in determining if there was a change in the business model that justifies the reclassification of financial assets. Also, there is no guidance on what is considered to be "significant to the entity's operations". As a result, the guidance on these issues found in other IFRS standards is applied by analogy. This may create different interpretations and diversity in practice. No specific examples of diversity in practice were provided.

Question 3—Contractual cash flow characteristics
(a) Is the cash flow characteristics assessment working as the Board intended? Why or why not? Please explain whether requiring entities to classify and measure a financial asset considering the asset's cash flow characteristics achieves the Board's objective of entities providing users of financial statements with useful information about the amount, timing and uncertainty of future cash flows. If, in your view, useful information could be provided about a financial asset with cash flows that are not SPPI applying IFRS 9 (that is, an asset that is required to be measured at fair value through profit or loss applying IFRS 9) by applying a different measurement approach (that is, using amortised cost or fair value through OCI) please explain:

(i) why the asset is required to be measured at fair value through profit or loss (that is, why, applying IFRS 9, the entity concludes that the asset has cash flows that are not SPPI).

(ii) which measurement approach you think could provide useful information about the asset and why, including an explanation of how that approach would apply. For example, please explain how you would apply the amortised cost measurement requirements to the asset (in particular, if cash flows are subject to variability other than credit risk). (See Section 7 for more questions about applying the effective interest method.)

(b) Can the cash flow characteristics assessment be applied consistently? Why or why not?

Please explain whether the requirements are clear and comprehensive enough to enable the assessment to be applied in a consistent manner to all financial assets within the scope of IFRS 9 (including financial assets with new product features such as sustainability-linked features).

If diversity in practice exists, please explain how pervasive the diversity is and its effect on entities' financial statements.

(c) Are there any unexpected effects arising from the cash flow characteristics assessment? How significant are these effects?

Please explain the costs and benefits of the contractual cash flow assessment, considering any financial reporting effects or operational effects for preparers of financial statements, users of financial statements, auditors or regulators.

In responding to (a)–(c), please include information about financial instruments with sustainability-linked features (see Spotlight 3.1) and contractually linked instruments (see Spotlight 3.2).

Our outreach indicated that, in the case of embedded derivatives, it is not always clear when these are clearly and closely related to the economic characteristics and risks of the host contract to avoid separate recognition. This is critical for entities that have liabilities with an embedded derivative, and there is a question as to whether or not to separate the embedded derivative. It is difficult to measure the embedded derivative due to the lack of observable data or because it is difficult to measure it directly. Regarding instruments linked to ESG indicators, what has been observed is that, if the entity is complying with them, there could be a reduction of the interest rate or the interest rate will not be increased, while the cash flows continue to be considered SPPI. There are not many such instruments outstanding presently, but their number is expected to increase in the future, resulting in complex conditions with which to comply. Some interested parties indicated that guidance thereon would be appreciated.

Question 4—Equity instruments and other comprehensive income

(a) Is the option to present fair value changes on investments in equity instruments in OCI working as the Board intended? Why or why not?

Please explain whether the information about investments in equity instruments prepared applying IFRS 9 is useful to users of financial statements (considering both (i) equity instruments measured at fair value through profit and loss; and (ii) equity instruments to which the OCI presentation option has been applied).

For equity instruments to which the OCI presentation option has been applied, please explain whether information about those investments is useful considering the types of investments for which the Board intended the option to apply, the prohibition from recycling gains and losses on disposal and the disclosures required by IFRS 7.

(b) For what equity instruments do entities elect to present fair value changes in OCI?

Please explain the characteristics of these equity instruments, an entity's reason for choosing to use the option for those instruments, and what proportion of the entity's equity investment portfolio comprises those instruments.

(c) Are there any unexpected effects arising from the option to present fair value changes on investments in equity instruments in OCI? How significant are these effects?

Please explain whether the requirements introduced by IFRS 9 had any effects on entities' investment decisions. If yes, why, how and to what extent? Please provide any available evidence supporting your response which will enable the Board to understand the context and significance of the effects.

In responding to (a)–(c), please include information about recycling of gains and losses (see Spotlight 4).

Our outreach indicated that investments in this kind of instruments are not common. It may be an exceptional investment. This encompasses both industrial and commercial entities as well as entities in the financial sector such as banks. Therefore, there is no basis to identify a trend for this kind of investments.

Question 5—Financial liabilities and own credit

(a) Are the requirements for presenting the effects of own credit in OCI working as the Board intended? Why or why not?

Please explain whether the requirements, including the related disclosure requirements, achieved the Board's objective, in particular, whether the requirements capture the appropriate population of financial liabilities.

(b) Are there any other matters relating to financial liabilities that you think the Board should consider as part of this post-implementation review (apart from modifications, which are discussed in Section 6)?

Please explain the matter and why it relates to the assessments the Board makes in a post-implementation review.

Our outreach confirmed that the Mexican regulator does not allow banks to designate financial liabilities to be measured at fair value. We noticed the case of certain trusts that invest in financial instruments that are measured at fair value, and therefore the associated financial liabilities are also measured at fair value with the effects of own credit risk for these liabilities being recognized in OCI, unless this increases the accounting mismatch. These instruments are not common. There were comments that it would be sound to recognize liabilities of investment funds at fair value in order to have symmetry with assets valued at fair value.

Question 6—Modifications to contractual cash flows

(a) Are the requirements for modifications to contractual cash flows working as the Board intended? Why or why not?

Please explain what changes you consider to be modifications of a financial asset for the purpose of applying paragraph 5.4.3 of IFRS 9 and as a modification of a financial liability for the purpose of applying paragraph 3.3.2 of IFRS 9. Does the application of those paragraphs, and the disclosure requirements related to modifications, result in useful information for users of financial statements?

(b) Can the requirements for modifications to contractual cash flows be applied consistently? Why or why not?

Please explain whether the requirements enable entities to assess in a consistent manner whether a financial asset or a financial liability is modified and whether a modification results in derecognition. Have the requirements been applied differently to financial assets and financial liabilities?

If diversity in practice exists, please explain how pervasive the diversity is and its effects on entities' financial statements.

There was a consensus that it is a professional judgment issue whether to consider a financial asset or a financial liability to be extinguished for accounting purposes and a new one generated, thereby requiring all deferred expenses incurred when issuing the original asset or liability to be derecognized and applied to profit and loss. In some cases, the 10% or more cash flow variation rule prescribed for financial liabilities is used for financial assets. This generates diversity in practice. One of the problems with liabilities is whether or not to consider new expenses in the 10% test. In the case of banks that are subsidiaries of foreign banks, the policies are prescribed by the parent.

When large banks restructure a large number of loans (mainly automobile, credit card or mortgage loans), they consider the loan to be extinguished for accounting purposes and a new one generated. This is a practical measure that helps them to manage the portfolios. Only in the case of large loans are the new cash flows discounted to evaluate whether there has been an extinguishment for accounting purposes. In many cases the loans have been restructured to reduce the interest rates in accordance with the market trend, and such cases the loans are not considered to be extinguished.

In connection with the deferral of payments that occurred due to the Covid pandemic, the effect of the deferral was computed and recognized in profit and loss.

Question 7—Amortized cost and the effective interest method

(a) Is the effective interest method working as the Board intended? Why or why not?

Please explain whether applying the requirements results in useful information for users of financial statements about the amount, timing and uncertainty of future cash flows of the financial instruments that are measured applying the effective interest method.

(b) Can the effective interest method be applied consistently? Why or why not?

Please explain the types of changes in contractual cash flows for which entities apply paragraph B5.4.5 of IFRS 9 or paragraph B5.4.6 of IFRS 9 (the 'catch-up adjustment') and whether there is diversity in practice in determining when those paragraphs apply.

Please also explain the line item in profit or loss in which the catch-up adjustments are presented and how significant these adjustments typically are.

If diversity in practice exists, please explain how pervasive the diversity is and its effect on entities' financial statements.

In responding to questions (a)–(b), please include information about interest rates subject to conditions and estimating future cash flows (see Spotlight 7)

Some of the old and large banks have indicated that they would need to make significative changes to their systems to incorporate the effective interest rate method, which would be a complicated and prolonged process. The changes would be to incorporate the effect of the upfront commission collected and the transaction costs incurred when granting the loan, which usually offset each other. As a result, the net amount of commission and transaction costs amortized on a straight-line basis plus interest determined with the contractual rate does not differ significantly from the amount that would have been recognized using the effective interest rate method. This issue must be evaluated every reporting period to determine whether the difference using the two rates continues to be immaterial. A few new banks, which are still small in size, have set up, from the beginning, systems to apply the effective interest rate method.

Question 8—Transition
(a) Did the transition requirements work as the Board intended? Why or why not? Please explain whether the combination of the relief from restating comparative information and the requirement for transition disclosures achieved an appropriate balance between reducing costs for preparers of financial statements and providing useful information to users of financial statements. Please also explain whether, and for what requirements, the Board could have provided additional transition reliefs without significantly reducing the usefulness of information for users of financial statements. (b) Were there any unexpected effects of, or challenges with, applying the transition requirements? Why or why not? Please explain any unexpected effects or challenges preparers of financial statements faced applying the classification and measurement requirements retrospectively. How were those challenges overcome?

To date there have been no problems with the transition to IFRS 9. The Mexican regulator has deferred adoption by the financial service sector to 2022. However, banks that are subsidiaries of foreign banks implemented IFRS 9 in 2018 without major problems, and other banks that are preparing for transition have not observed any significant problems. There were no significant problems observed by non-financial sector entities that began application in 2018.

Question 9—Other matters
(a) Are there any further matters that you think the Board should examine as part of the post-implementation review of the classification and measurement requirements in IFRS 9? If yes, what are those matters and why should they be examined? Please explain why those matters should be considered in the context of the purpose of the post-implementation review, and the pervasiveness of any matter raised. Please provide examples and supporting evidence when relevant. (b) Considering the Board's approach to developing IFRS 9 in general, do you have any views on lessons learned that could provide helpful input to the Board's future standard-setting projects?

There were no other matters we believe the Board should examine as part of the post-implementation review of the classification and measurement requirements in IFRS 9.

Should you require additional information on our comments listed above, please contact Juan M. Gras at (52) 55 2886 6560 or me at (52) 55 5403 8309 or by e-mail at jgras@cinif.org.mx or egarcia@cinif.org.mx, respectively.

Sincerely,

C.P.C. Elsa Beatriz García Bojorges
President of the Mexican Financial Reporting Standards Board
Consejo Mexicano de Normas de Información Financiera (CINIF)

Cc: Mr. Tadeu Cendon