



April 28, 2011

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

Dear Board Members:

Consejo Mexicano para la Investigación y Desarrollo de Normas de Información Financiera (CINIF), the accounting standard setting body in Mexico, welcomes the opportunity to submit its comments on the Exposure Draft on *Offsetting Financial Assets and Financial Liabilities* (the ED), issued for exposure in January 2011. Set forth below you will find our comments on the topics included in the ED, as well as our responses to the questions included therein.

We have divided our letter in two sections. In the first section you will find our general comments on the ED. The second section includes our responses to the specific questions raised in the ED.

### **General comments on the ED**

In general, we support the combined efforts of the IASB and the FASB to converge on the various issues regarding the offsetting of financial assets and liabilities. The offsetting guidance resulting from this standard will be very helpful in properly applying IFRS 9. In this regard, we believe that it should be incorporated in IFRS 9, not as a self-contained IFRS as indicated at the beginning of page 7 of the ED. We recommend that the presentation guidance currently included in IAS 32, *Financial Instruments: Presentation*, and to be revised by this project should be relocated to a separate “presentation” chapter of IFRS 9. With this, both IAS 39, *Financial Instruments: Recognition and Measurement*, and IAS 32 would be superseded.

Our concerns are explained in the response to the specific questions raised in the ED.

### **Our responses to the specific questions raised in the ED**

<p><b>Question 1—Offsetting criteria: unconditional right and intention to settle net or simultaneously</b></p>
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<p>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:</p>
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- (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 proposed requirement. However, we have some concerns about the concept of simultaneous realization and liquidation. We believe such a transaction should be made through a clearing house or an exchange to be equal to a net cash flow in order that the realization and liquidation take place simultaneously. A financial asset and a financial liability that will be realized and liquidated through an exchange of checks should not be considered simultaneous since the checks (1) may not be cashed at the same time and may be drawn on different banks and (2) may not be cashed until the next day. We believe that related guidance should be included in the standard.

**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?

Yes, we agree that the unconditional right to set off must be enforceable in all circumstances, to ensure that the future cash flow will be a net cash flow.

We are unclear about the guidance included in the last sentence of paragraph C15, which states the following: “Similarly, if the right to set off a recognised financial asset and financial liability is exercisable only before a specific date, that right of set-off does not qualify as an unconditional right of set-off.” Consider a scenario where a contract is signed on March 1, 2012 that grants an unconditional right of set-off for a period of one year, i.e. through February 28, 2013. Based on the guidance cited above, the deadline for exercising the right of set-off converts the right from unconditional to conditional. This means that in the statement of financial position as of December 31, 2012 the related financial assets and financial liabilities could not be offset, despite the fact that at that date there is an unconditional right of set-off and the entity may have the intention of exercising the right and settling net. It would seem to us that the most useful information for investors would be a net presentation in the statement of financial position.

Paragraph 10(d) of the ED defines a conditional right of set-off as a right of set-off that can be exercised only on the occurrence of a future event. It is not clear to us why the deadline for exercising the right represents a “future event”.

**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 the offsetting criteria should be applied to both bilateral and multilateral set-off arrangements. In the case of multilateral set-off arrangements, the unconditional rights should go in both directions from the entity that will recognize the offsetting.

We are unaware of any real life examples of situations where a multilateral right of set-off may be present. We have an example where the unconditional right of set-off was not present and created a problem. As a consequence of the 1982 financial crisis in Mexico and the fact that the Mexican Government decided to establish exchange controls, many entities that had dollar-denominated debt could not freely obtain dollars to pay the debt. The Mexican Central Bank (MCB) created a mechanism by which it lent pesos to the entities, who in turn deposited such pesos in dollar-denominated accounts at the MCB, to guarantee their debt to foreign banks and suppliers.

Such deposit was not accepted as a possible set-off by the foreign banks and suppliers for various legal reasons. The question in Mexico was if it was possible to offset the dollar asset at the MCB with the dollar liability with the foreign bank or supplier. The conclusion was these could not be offset, but that the dollar deposit in the MCB could be offset with the corresponding peso liability, since to draw the dollars on the due dates to pay the foreign bank, the related part of the peso liability had to be paid. This ended up being a bilateral set-off arrangement rather than a multilateral set-off arrangement as the MCB had intended. When the exchange controls were lifted, most entities cancelled the transaction with the MCB, since it was very burdensome in their renegotiation process with foreign banks.

#### **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 believe that certain of the disclosure requirements are excessive. The disclosures requested in paragraph 12 are particularly excessive, since they require presentation in a tabular format of amounts that were offset and those that cannot be offset to determine a net amount. We question what such a net amount represents and why it would be useful. We agree that an entity should disclose the unconditional rights it does not intend to exercise and the conditional rights that only represent credit risk protection. Also, the disclosure required by paragraph 13 regarding a description of each type of conditional rights appears to be excessive, since, as previously indicated, these are risk management measures to protect against credit risk.

Paragraph C20 indicates that “...the entity must strike a balance...”. We do not see how a balance can be achieved with so many disclosures. Disclosures should inform (1) what was offset and why and (2) what was not offset and why.

#### **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.

We believe that the effective date should be the same as the remainder of IFRS 9. A retrospective application should be required in order to have comparative figures,

unless it is impractical. However, Mexican banks indicated that for practical purposes they would prefer a prospective application,

Regarding how long an entity would reasonably require to implement the proposed requirements, for entities other than banks, we believe implementation of the requirements should not require much time. As we believe banks are those that may be most affected, this issue will be in addition to the determination of expected losses. Mexican Banks believe that a minimum of one year will be required to adequately implement this new standard since the change in systems will be significant. Additionally, as their financial ratios will change, they will need enough time to renegotiate covenants and agree with the local regulator on the new ratios of assets to equity.

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Should you require additional information on our comments listed above, please contact Juan M. Gras at (52) 55 5596 5633 ext. 105, William Biese at ext. 113 or me at ext. 103 or by e-mail at [jgras@cinif.org.mx](mailto:jgras@cinif.org.mx), [wbiese@cinif.org.mx](mailto:wbiese@cinif.org.mx), or [fperezcervantes@cinif.org.mx](mailto:fperezcervantes@cinif.org.mx), respectively.

Sincerely,

C.P.C. Felipe Perez Cervantes  
President of the Mexican Financial Reporting Standards Board  
Consejo Mexicano para la Investigación y Desarrollo  
de Normas de Información Financiera (CINIF)