



Communauté Européenne des Coopératives de Consommateurs

European Community of Consumer Cooperatives

Sir David Tweedie - Chairman
International Accounting Standards Board
30 Cannon Street
UK - London EC4M 6XH

30 July 2004

Re: Comments on International Accounting Standards Board Exposure Draft - Amendments to IFRS 3 Business Combinations – “Combinations by Contract Alone or Involving Mutual Entities”.

Dear Sir David

EURO COOP – the European Community of Consumer Co-operatives – is the representative body for european consumer co-operatives. Founded in 1957, our primary objectives include representing the interests of consumer co-operatives and their consumer-members. Our membership base comprises national organisations of consumer co-operatives from 18 european countries, with in excess of 30, 000 sales outlets, 300, 000 employees and 22 million consumer-members.

EURO COOP is pleased to be able to comment on the proposed amendments to IFRS3 as follows.

Grosso modo, EURO COOP disagrees with the proposed amendments.

While we can understand some of the concerns that have led to the IFRS3 standard on Business Combinations that discards the pooling of interests method and which is linked to non-mutual entities, EURO COOP however considers that the proposed amendments to IFRS 3 are not appropriate to mutual entities – including consumer co-operatives - and reflect neither their legal nature nor economic reality. Eliminating the pooling of interest method and replacing it with one that is less appropriate to our sector does not represent an improvement to existing accounting standards. Rather, application of the proposed purchase or acquisition method to mutual entities would give rise to many new questions.

We therefore request the IAS Board to maintain the IFRS 3 as passed in March 2004, and to apply the accounting method of pooling of interest to mutual entities until proper guidelines are issued.

Finally, we should also like to take this opportunity to stress the specificity of mutual entities compared to other forms of enterprise, and in particular the accounting treatment of their framework for co-operating in various ways (e.g., via legal merger, contractual arrangement, co-operative of co-operatives, etc.). While in other forms of enterprise shareholders look for “value creation”, namely maximum shareholder value, in the co-operative and mutual sectors, the objective is to optimise services provided to members-owners, and in the case of consumer co-operatives, consumer-members.

We trust you will take account of these comments and those contained in the attached Annex during the ongoing deliberations on this matter. Please do not hesitate to contact us if you have any questions.

Yours sincerely

Dónal WALSHE
Secretary General.

Annex

EURO COOP Comments on Proposed Amendments to IFRS 3 Business Combinations

Question 1

The Exposure Draft proposes:

(a) to remove from IFRS 3 the scope exclusions for business combinations involving two or more mutual entities and business combinations in which separate entities are brought together to form a reporting entity by contract alone without the obtaining of an ownership interests

(b) to require the acquirer to measure the cost of a business combination as:

i. the aggregate of the following amounts when the combination is one in which the acquirer and acquiree are both mutual entities:

☐ *the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities; and*

☐ *the fair value, at the date of exchange, of any assets given, liabilities incurred or assumed, or equity instruments issued by the acquirer in exchange for control of the acquiree*

Therefore, goodwill would be recognised in the accounting for such transactions only to the extent of any consideration given by the acquirer in exchange for the control of the acquiree.

ii. The net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities when the combination is one in which separate entities or businesses are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest. Therefore no goodwill would arise in the accounting for such transactions. Is this an appropriate interim solution to the accounting for such transactions until the Board develops guidance on applying the purchase method to such transactions as part of a subsequent phase of its Business Combinations project? If not, what other approaches would you recommend as an interim solution to the accounting for such transactions, and why?

Responses to question 1

It is indeed difficult to determine who is the acquirer and acquiree in the cases of mergers of co-operatives and/or mutuals, as well as in the cases of contractual groups of co-operatives and/or mutuals.

However, the main issue is not the difficulty of identifying who should be the acquirer and acquiree, but the fact that due to the legal nature of mutual entities, the legal figure of acquirer is not applicable.

The application of the purchase method would entail, sooner or later, a true transfer of shares and legal notification to a notary, dissolution of the property of a co-operative and inversion of the decision-making powers by concentrating them at the apex level.

Members' shares in co-operatives and mutuals, when these do exist, are non-transferable and nominal, with all members enjoying equal voting rights.

In many mutuals and in some co-operatives, there are no shares at all, and property is collective. The cases of getting together (co-operating among mutual entities), very frequent among mutuals, should not be qualified as "business combination" even though it may look like as the IAS defined term of "Dual listed corporations", firstly because they are not listed, and secondly because they do not have shares to exchange.

It is not possible, in general, to legally acquire a co-operative or mutual or to directly transfer the members' shares (in the case of co-operatives), at least not before the entity is de-mutualised and turned into another form of enterprise. Only then can it be acquired legally, a case that falls out of the scope of "business combination" of mutual entities, and therefore out of the scope of the proposed Amendment.

There is thus no exchange of consideration in mergers except for the financial compensation among the members' shares.

In the case of contractual groups, there is no transaction taking place, but a contractual agreement between two parties to share control of certain assets and/or activities, based on democratic and voluntary decision-

making. (The use of the term "control" should not be equalled to the IASB content of the concept as it is being worked out at the moment). The result of a Business Combination of mutual entities linked together through a contractual group is not the control of an entity by another, but rather two entities which control, under conditions of equal power, certain assets and activities in common.

Contractual groups do not lead to hierarchical control and concentration of capital. Their logic is of co-operation for specific socio-economic functions, and to ensure the long-term sustainability of the latter. When new co-operatives enter the group, they democratically decide to join, in the same way as their founding members previously decided democratically to constitute the co-operative. Such actions are motivated by a socio-economic function that the group performs. This can in no way be assimilated to a purchase, nor can it justify the utilisation of the purchase method.

Moreover, it is not possible to control a co-operative entity by purchasing the majority of its' members' share capital (such shares are not transferable) and there are limits to members' voting power (principle of "one person one vote"), even if one member has more shares than another member.

In the special method for measuring the cost of the combination, different from the one to apply to all other enterprises, it has been proposed that there will be no good will. This interim proposal should not be applied, and a proper method for accounting co-operation and mergers of equals should be studied and elaborated.

And last but not least, the proposed amendment would contradict existing national legislation, some of which only recently passed into law. In France for example, after a year of discussions between specialists in accountancy and co-operative law, the French CNC – National Accounting Council – recently stated it would be impossible to consolidate the accounts of co-operatives and instead created the "combination of accounts" method. This was due to the fact that a) individual members have no right to co-operative reserves, and b) the principle of "one person one vote" that prevents control in the capitalistic sense.

Question 2

The Exposure Draft proposes that no amendments be made to the transitional and effective date requirements in IFRS 3. This would have the effects set out in paragraph 6(a) – 6(c) above on the accounting for business combinations in which the acquirer and acquiree are both mutual entities or in which separate entities or businesses are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest.

Is this appropriate? If not, what transitional and effective date arrangements would you recommend for such business combinations and why?

Responses to question 2

The date proposed in the Exposure Draft implies the retroactive application of the standard, something that is not legally acceptable.

Furthermore, such relatively hasty regulatory changes - coming only four months after the approval in March this year of IFRS 3 - and with a view to being approved by the IASB at end-2004 provides neither time for adaptation (costly and time-consuming) nor the requisite stable regulatory environment.

The arrangement proposed is Interim (temporary) even though it may require changing laws in many European countries in addition to statutory changes for thousands of consumer co-operatives across Europe. It would also require changes to existing contracts among mutual entities. This is neither appropriate nor efficient; it also pre-empts the outcome of an adequate and stable solution for the long term.

We therefore request the non-application of the IFRS 3 to mutual entities – including consumer co-operatives - until proper guidelines and adequate accounting solutions and time frame are set. Until the appropriate solutions are found, we recommend to continue with the pooling of interests and the net book value methods for mergers and contractual combinations among mutual entities (co-operatives and mutuals).