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30 July, 2004

Sir David Tweedie, Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM
Fax number: + 44 20 7246 6411

Via E-mail, Fax and Postal Mail

Re: Proposed Amendments to IFRS 3

Dear Sir David:

On behalf of the members of the National Cooperative Business Association, I am writing to comment on the International Accounting Standards Board's Exposure Draft - Amendments to IFRS 3 Business Combinations – *"Combinations by Contract Alone or Involving Mutual Entities."* I am pleased to comment on the proposed Amendments.

NCBA is the national membership association of all types of cooperative businesses in the United States. More than 40,000 cooperatives operate in every industry and serve some 120 million members across the country. Many cooperatives are direct members of NCBA and we represent many thousands of other cooperatives through our members that are national and state-level associations of cooperatives. NCBA is a member organization of the International Co-operative Alliance.

Cooperative businesses are owned and democratically controlled by their members – the people who use the cooperative's services or buy its goods – not by investors. They return surplus revenues to members proportionate to their use of the cooperative, not proportionate to their ownership share. Loan agreements, bylaws, and other documents generally require cooperatives to prepare audited financial statements in accordance with generally accepted accounting principles (GAAP).

NCBA emphatically disagrees with the proposed Amendments and we believe they will cause undue harm to cooperatives if they are applied. We ask that IASB maintain the application of IFRS 3 as it was approved in March of 2004 and to continue to allow cooperatives to use the pooling of interest method of accounting for business combinations. The proposed Amendments, insofar as they require cooperatives to use the purchase method of accounting for business combinations, do not appropriately recognize how cooperatives are different from other business entities and would cause cooperatives to incur far more costs than would give any benefits if they are applied.

NCBA has been working with the Financial Accounting Standards Board (FASB) in the U.S. to explain the impact that changes in accounting standards will have on cooperatives. When FASB proposed the application of their standard FAS 150 (Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity) to cooperatives last year, NCBA mounted an educational effort to show FASB the effect that FAS 150 would have had on cooperatives. Since then, FASB has formed a Small Business Advisory Committee and invited NCBA to nominate a representative to help them understand the impact that their standards would have on cooperatives. Just as FAS 150 failed to acknowledge how cooperatives are different from other business entities, the proposed Amendments also fail to account for these differences.

While shareholders of investor-owned businesses seek to maximize returns on their investment, members of a cooperative join it in order to receive services, not return on investment. Because of this, cooperatives do not typically combine as the result of a sale of shares. Cooperatives combine in order to provide their members with better service. In most cases, cooperative combinations are mergers of equals. In fact, many of these mergers that do benefit the members of the cooperatives would not occur if one cooperative had to be treated as the purchaser and the other as the purchasee.

The typical combination of investor-owned businesses is a purchase of the majority of common stock in the purchasee business. This cannot happen with cooperatives, because the principle of "one-person-one-vote" prohibits one member from taking control of the majority of the voting rights. Member shares are typically not transferable to non-members. Moreover, member shares are issued and redeemed on a nominal basis, and therefore do not have a market value which an acquirer would be willing to pay. Shares issued to members of the combined entity do not reflect any kind of purchase price or cost of the combination. Any kind of purchase method depending on measuring the cost of the combination leads to serious practical problems if applied to cooperatives. Applying the purchase method would add substantial costs to the merger and would continue to add ongoing substantial costs for the new entity into the future.

Please do not hesitate to contact me at (202) 383-5442 or by e-mail at phazen@ncba.coop, if you have any questions.

Sincerely,

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Annex

Comments of National Cooperative Business Association 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 typically difficult, if not impossible, to determine which entity is the purchaser and which is the purchasee in the cases of mergers of cooperatives. The most important issue in mergers of cooperatives, however, is that requiring one entity to be treated as a purchaser fundamentally fails to recognize the difference between cooperatives and investor-owned businesses.

The shares of cooperative members are typically non-transferable and of nominal value and all members enjoying equal voting rights.

In the proposed method for measuring the cost of the combination, different from the one to apply to all other enterprises, there would be no good will. This interim proposal should not be applied and an appropriate method of accounting for mergers of cooperatives should be further studied.

While we have not yet seen an appropriate accounting methodology for the mergers of cooperatives, there has been mention of a "fresh start accounting" method, which we believe would be superior to the purchase method. The IASB should look at all alternatives to find an appropriate long-term solution that respects the legal nature of cooperatives and reflects their economic reality.

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 means the retroactive application of the standard. Hasty regulatory changes just four months after the approval in March of the IFRS 3, that might be possibly approved by the IASB at the end of 2004, provides neither time for adaptation (costly and time consuming) nor a stable regulatory environment that may deliver the benefits of trust and reliability.

The interim proposal may require changing laws in many countries in the world and statutory changes for cooperatives. This is neither appropriate nor efficient. It also pre-empts the outcome of an adequate and stable solution for the long term.

We therefore ask that IFRS 3 not be applied to cooperatives until proper guidelines and adequate accounting solutions and time frame are set. Until the appropriate solutions are found, we ask that cooperatives be allowed to continue using the pooling of interests method when accounting for mergers.