

Rome, 30 July 2004

Email: CommentLetters@iasb.org

Sir David Tweedie
Chairman
International Accounting Standard Board
30, Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir Tweedie,

We welcome the opportunity given to us by the IAS Board to comment on its Exposure Draft – Amendments to IFRS 3 Business Combinations: “**Combinations by Contract Alone or Involving Mutual Entities**”.

Confcooperative is a national umbrella organisation representing over 18,000 member co-operatives with 3 million individual members involved in all economic sectors (agrofood, housing, banking, fisheries, consumers, social and health care, workers and production, tourism, mutuals, etc), a relevant part of which would be negatively affected by the proposed amendments since the model of the co-operative consortia is widely used in Italy.

This is why we strongly disagree with the amendments proposed to IFRS 3 and with any standard which could arise from the Exposure Draft, until which time a new accounting method for business combinations appropriate to the specific nature of co-operatives and mutuals is proposed.

In relation to the specific questions raised in the Exposure Draft, our comments are set out below :

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?

Establishing who is the acquirer and acquiree in the event of mergers between cooperatives and/or mutuals is not easy and likewise difficult in the case of contractual groups of cooperatives and/ or mutuals. This is however not the key issue here but rather the fact that due to the legal personality of mutual entities, such legal figure of acquirer is not applicable.

The application of the purchase method would eventually entail a transfer of shares and notification to a notary. The co-operative's property would be dissolved and the decision-making powers inversed with a top down approach.

In cases where Members' possess shares in co-operatives and mutuals, these are nominal and non-transferable, with all members enjoying equal voting rights. In many instances mutuals have no shares. This is also sometimes the case for co-operatives. Instead, property is collectively owned.

The fact of coming together (co-operating among mutual entities), a frequent occurrence amongst mutuals, should not therefore be qualified as "business combination" - even if it might at first sight appear similar to what the IAS defines as "Dual listed corporations" - firstly because they are not listed and secondly because they have no shares to exchange.

In general it is not possible to legally acquire a cooperative or mutual or to directly transfer members' shares (in the case of cooperatives). This only becomes possible once the entity is de-mutualised and converted into a conventional enterprise. Only then can it be legally acquired. This situation falls outside the scope of "business combination" of mutual entities and is therefore outside 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, no transaction takes place. It is rather a contractual agreement between two parties to share control of certain assets and/or activities, based on democratic and voluntary decision-making. The outcome of a business combination of mutual entities linked together through a contractual group is not the control of one entity over another. It is rather two entities with equal control over certain assets and joint activities common. The use of the term “control” should not here be equated to the IASB’s use of the concept as it is currently being re-defined.

Contractual groups cannot be assimilated to hierarchical control and the concentration of capital. The motivating factor is rather co-operation for specific socio-economic functions and to ensure long-term sustainability. New co-operatives can democratically decide to join the group in the same manner that the founding members democratically decided to set up the cooperative. Participation is driven by a socio-economic function that the group performs. As such, it can in no way be assimilated to a purchase, nor is the use of the purchase method to any intents or purposes justifiable.

Given the principle, “one person one vote”, it is impossible to control a co-operative entity by purchasing the majority of its members’ share capital (such shares are not transferable). Members’ voting powers are limited, even if one member possesses more shares than another.

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?

We believe that some of the proposals set out in the Exposure Draft do not favour legal certainty and a stable regulatory environment, both of which are fundamental to the development of businesses.

The retroactive application of the standard proposed in the Exposure Draft is not legally acceptable and could result in serious uncertainty.

Furthermore, the introduction of new standards or amendments shortly after the approval in March of the IFRS 3 does not allow time for adaptation and is detrimental to the stability of the regulatory framework.

The solution proposed is a temporary one, but may entail changes to the laws of many countries as well as statutory changes for cooperatives and changes to existing contracts amongst mutual entities. We do not consider this to be appropriate nor will it help foster an adequate long-term solution.

The Interim solution proposed uses key terms which are currently being re-defined. This adds a further element of confusion. We therefore express our reservations about the application of the solution proposed in the Exposure Draft and believe that it would be more appropriate to set out guidelines based on clear and accepted concepts.

While waiting appropriate arrangements, we would advocate continuing with the pooling of interests and the net book value methods for mergers and contractual combinations among mutual entities (cooperatives and mutuals).

Confcooperative and its members are deeply concerned about the amendments proposed in the Exposure Draft and do hope the IASB will pay due attention to the specificity of co-operative and mutuals in dealing with this matter.

We are at your full disposal in case you would need additional clarifications on our comments or on co-operatives and mutuals specific nature.

Yours Sincerely

Luigi Marino
President