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July 30, 2004

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

Subject: Comments on International Accounting Standards Board's Amendments to IFRS 3 Business Combinations Effects on Mutual Insurance Companies

Dear Sir David,

Thank you for the opportunity to comment on the proposed Amendments cited above.

The Canadian Association of Mutual Insurance Companies (CAMIC) is a national trade association for property and casualty mutual insurers in Canada. It provides information, research, advocacy to its members and negotiates supply agreements. The Association promotes a strong, healthy and competitive insurance market and supports regulatory efficiency and legislative changes which are in the interest of all policyholders. The present membership of CAMIC includes 96 mutual insurers from coast to coast. In 2003, our member companies had approximately 4 million policyholders; employed in excess of 10,000 managers, employees and agents and underwrote $4.1 billion in premiums (11.7% of the Canadian market).

Mutual insurance companies are owned by their policyholders and most of them operate under the one member, one vote principle. The policyholders elect the board of directors of their company. Mutual insurers are renowned for their strong balance sheet and their community involvement. Most Canadian mutual insurers are based in small communities.

To be more competitive on the Canadian market many small mutual insurance companies have merged with other mutual insurers in recent years. We expect that trend to continue in the near future.

We recommend the non-application of the proposed amendments to IFRS 3 on mutuals as they would have a negative effect on Canadian mutuals' ability to merge and consolidate. This is the reason behind CAMIC's strong opposition to the proposed amendments.

The Exposure Draft would subject combinations by contract alone involving mutual entities to IFRS 3; which would have the effect applying a specific purchase method. This would impact differently on mutual insurers than on stock insurance companies.

IFRS 3 does not take into account the specific legal and economic reality of mutuals. While stock companies tend to maximize value for their shareholders, mutuals work for the benefit of their members.

A mutual insurer does not have shareholders; it is owned by its members where each member owns a portion of the company, portion based on the number of members. Each member has one vote and owns one part of the company. His part of the company cannot be sold nor transferred. When a member leaves the company, his voting right has no market value and that member losses his share of the company. Should the mutual insurance company merge with another mutual insurance company, each member of the new company would own one part of that new company, based on the new company's number of members.

Based on these significant differences, we request the IAS Board to maintain the IFRS 3 as was passed in March 2004, and to apply the accounting method of pooling of interest to mutual entities until appropriate guidelines can be worked out and issued.

Any modification to the IFRS 3 standard should take into account the uniqueness of the mutual system. To this end we recommend that you form a working group that encompasses mutual representatives.

Mutually yours,

Normand Lafrenière
President
Canadian Association of Mutual Insurance Companies (CAMIC)
fd/NL

Annex

Comments of the
Canadian Association of Mutual Insurance Companies (CAMIC)
on the 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?

Response

It is not possible to legally acquire a mutual company or to directly transfer the members' shares, at least not before the entity is demutualised and turned into a stock company. 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.

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?

Response

The amendments proposed should not be implemented as they would be costly and ineffective at creating a stable and reliable regulatory environment.

Implementing the Exposure Draft "as is" would mean applying the standard retroactively: this is illegal.

We request the non-application of the IFRS 3 pending the establishment of proper guidelines and accounting solutions that respect the uniqueness of mutuals. We therefore recommend continuing with the pooling of interests and the net book value methods for mergers and contractual combinations among mutual entities.