



INTERNATIONAL  
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ALLIANCE

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LETTER OF COMMENT NO. (

Robert H. Herz  
Chairman  
Financial Accounting Standards  
Board  
401 Merritt 7, P.O. Box 5116  
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USA

Geneva, 8 January 2007

Dear Mr. Herz,

On behalf of the international co-operative community of 800 million members, I am writing about the equity and liabilities convergence project. The International Co-operative Alliance (ICA), established in 1895, is an association of 230 national co-operatives in 92 countries. Our members are concerned about the direction of the convergence effort and its potentially detrimental impact on the co-operative model of business.

### **Co-operatives – A Significant Part of the Global Economy**

The co-operative sector represents a significant contribution to our global economy. According to a recent survey by ICA, the top 300 co-operatives around the world had nearly \$1 trillion in revenues in 2004. That is only slightly less than the economy of the world's ninth largest economy, Canada. Co-ops create over 100 million jobs, more than all of the multinational corporations combined. Co-operative enterprises contribute to every sector of the economy and are among the largest businesses in the world.

### **A Different Business Model**

Our members have worked hard in the United States, at the European Union and around the world to educate accounting standard setters about the co-operative model. Once policymakers understand the model, they can act to ensure that standards are developed to meet the needs of users, preparers, analysts and others interested in the financial statements of co-ops. But we have often found in the past that standard setting organizations reached simplifying assumptions that would treat the co-operative business model as synonymous with the investor-owned business model.

The act of a co-operative offering goods or services to its membership at reasonable cost is not functionally equivalent to an investor-owned entity earning a profit for its shareholders. Such an assumption may disproportionately impact the financial statements of co-operatives simply because of their chosen form of organization. We do not believe that it is the role of accounting standards to create unequal competition conditions for one form of business model over other forms.

According to the co-operative standards established by the ICA General Assembly under the "Statement on the Co-operative Identity" in 1995 and fully incorporated into ILO Co-operatives

stable accounting environment on a long-term horizon, due to the possible impact on prudential capital.

The Milestone Draft represents some accommodation for U.S. co-operatives and I appreciate all the work of FASB and staff to incorporate the changes. However, that approach does not accommodate the needs of the international cooperative community and jeopardizes the "acquis" obtained by the Co-operative sector under IAS and IFRIC 2.

The international co-operative community rallied and made significant compromises to develop its response to International Accounting Standard (IAS) 32 which the IASB recognized in the form of International Reporting Financial Interpretation Committee (IFRIC) Interpretation 2. For many co-operatives, this was a compromise that forced some changes in the bylaws and structure of their organization.

I believe that IFRIC 2 is a reasonable approach that accommodates the co-operative business model and we urge you to consider adoption of such a standard worldwide for co-operatives and other mutual entities. Therefore, the substance of the content of IAS 32 and IFRIC 2 should constitute a strict minimum threshold for the classification of co-operative shares. I believe that no share type, which is considered as equity today under IAS 32 and IFRIC 2, should be declassified into liability as the result of any future amendment of the Equity-Liability Distinction.

A requirement for instruments to represent proportional claims to shares of the net assets of the entity (that is, there is no ceiling) either before or at liquidation as a defining condition for the financial instrument to be considered as equity could not be fulfilled by many co-operatives, due to statutory provisions and national co-operative legislation.

The FASB and the IASB should consider alternative approaches to the ones explored so far. Any such approach would have to be compatible with the cooperative business model, company form and legal framework.

Regardless of which approach you take, I and my Board strongly believe that any proposed standard on liabilities and equity should result in the following:

- The financial contribution of members in the form of co-op shares or other ownership instruments is viewed as equity;
- Past redemption practices should not define the relationship between the member's financial contribution and the co-op where the governing entity, the Board, retains control over the financial contribution and its ultimate redemption.

**Our position is further detailed in the attached resolution.** We look forward to working with FASB and IASB to ensure that accounting standards address the needs of the international cooperative community.

Yours sincerely,



Ivano Barberini  
President

## ICA RESOLUTION ON IAS 32

Whereas Co-operatives are directly concerned by the application of IFRS, due to the fact that many of them issue debt securities listed on a regulated market;  
Whereas IAS 32 pursues a settlement approach that would have led to the classification of co-operative shares as liabilities in case of unconditional redemption;

Whereas IFRIC 2, as adopted by the IASB in 2005, provides a clarification of conditions under which redemption is not unconditional and cooperative shares could consequently continue to be classified as equity;

Whereas the FASB and the IASB have decided to review their respective financial reporting standards in the context of the Convergence project aiming at mutual recognition of US-GAAP and IFRS;

Whereas the distinction of equity and liabilities on the balance sheet forms part of this convergence effort;

Whereas the Ownership-Settlement Approach proposed by the FASB in its First Milestone Draft would jeopardise the "acquis" obtained by the Co-operative sector under IAS 32 and IFRIC 2;

### **The International Co-operative Alliance considers that:**

- The substance of IAS 32 and IFRIC 2 should constitute the strict minimum threshold for the classification of co-operative shares. No share type, which is considered as equity today should be declassified into liability as the result of any future amendment of the Equity-Liability Distinction.
- Co-operative Banks in particular need a stable accounting environment on a long-term horizon on the issue of the classification of their shares as equity:
  - ☞ Due to the ongoing prudential debate on the own funds definition, the accounting definition of equity could increasingly influence the supervisors' perception of regulatory capital. Consequently, a declassification of cooperative shares from equity into liability could have considerable consequences on their lending capacity, on their rating and hence on their economic subsistence.
- Any modification of the Equity-Liability Distinction would probably result in fundamental consequences, requiring a wide-ranging overhaul of cooperatives' institutional framework, including their concept of co-operative shares, their corporate governance, etc.