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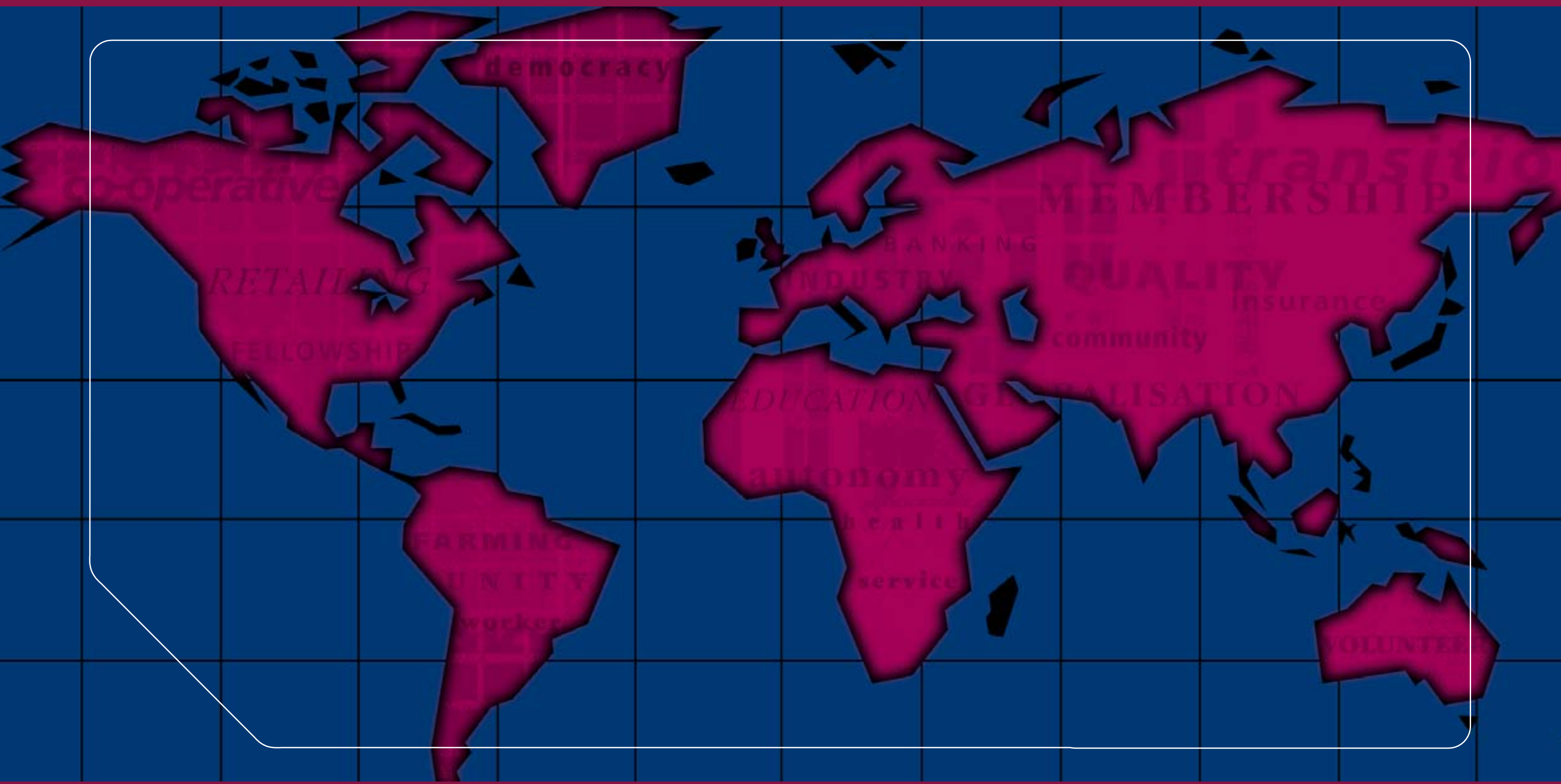

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Editorial

We commence this issue with a wide ranging paper concerned to explore the continuing relevance of the co-operative difference in the context of globalisation. In our Special Guest Paper section *Andrea Bernardi* reviews the contemporary debate on the role of co-operatives in the global economy from an Italian perspective but with insights that have certainly a far wider relevance. His conclusion that the market rather than institutional forces should determine the extent of co-operative activity is certainly in tune with the liberalised economic environment which is offering so few regulatory constraints on the co-operatives private sector competitors. Co-operative need to grow and as they grow they may need to buy and operate subsidiaries and *Andrea Bernardi* insists can do so using the latest management methodologies without any loss of their most important competitive weapon namely, what it is that differentiates them from their private sector competitors.

We are delighted to welcome back *Iiro Jussila*, and *Juha-Matti Sakasa* and, for the first time, their new co-author *Janne Tienari* who have conducted a very important piece of research into the issues of co-operative governance. Their paper suggests a new direction for research on co-operative governance examining the impact of the psychological dimension of peoples' sense of ownership, the significant differences in this sense of ownership at different levels, and its significance for explaining tensions between actors at local and regional/national co-operative structures. The small Finnish population and strongly defined regional identities may limit the general applicability of this research in more urban mass culture societies. Notwithstanding this possibility I recognised very similar past responses by boards and members in the UK local consumer co-operatives resistance to merger as is identified in this interesting Finish research. Of course market realities in the end forced the mergers through, rather too late in the UK case to stop the dramatic loss in market share. Their paper considers critically the wide range of approaches to governance and their comparison and contrasting of the different emphasis in approaches and in the discussion rooted in their consideration of different ownership models provides us with an important refection which I am sure will rightly stimulate further research and hopefully some development of management practices in the areas of membership and governance.

One new approach to governance in the modern context that the authors did not consider was the proposition that *modern management methodologies, particularly TQM, provide in the co-operative context a mechanism for governance.* (See: Davis, P., *Managing the Co-operative Difference,* ILO Co-operative Branch, Geneva, 1999) I suggested that modern management methods are in fact *more effective* in the co-operative business model because they *can act as a governance mechanism.* Total Quality Management (TQM) as applied in the private sector, where stakeholder tensions and conflicts are much more clearly defined and hard to resolve, is much more problematic. In this Finnish study the overlap of stakeholders through both "ownership and customership" supports this contention. TQM in the co-operative context is I suggested particularly suited to mobilising opinion of "passive" members and overcoming diluted or unrepresentative democratic processes in the case of national and large regional co-operatives. My case study to illustrate the point was the UK Co-operative Bank plc as it developed in 1980s and 1990s under the leadership of *Terry Thomas.* Of course such an application requires a CEO like that of *Terry Thomas* who is committed to and has an understanding of co-operative values and purpose. Here the issue is a lack of management development and dedicated recruitment and selection agencies to support co-operatives to employ managers with the right values as well as the right technical expertise. This is sadly lacking in just about all countries. These HRM issues rarely come into the debate on governance. To the extent that governance is about how individuals in positions of trust and leadership behave the omission is particularly unhelpful.

The issue of character formation in determining moral behaviour in general and leadership behaviour in particular is a fascinating subject. In their paper exploring leadership from its moral and ethical dimension *Natale, Libertella, Rothschild and Sora* argues forcibly for a greater engagement with the character formation informing the leaders' moral compass. The authors of this paper recognise character formation goes back to ones earliest socialisation in family and schooling. The literature they draw on however rejects the idea of character formation as something fixed for life from relatively early on in ones development. They quote George (2006) and others to the effect that the characters moral compass is developed over a lifetime. From the co-operative standpoint this topic has a pressing relevance given the often weak governance *content* found in even the most committed participatory systems in co-operatives. As co-operatives grow so member control weakens and managerial control strengthens. Boards need to be able to identify the right character profiles for their management executives to help to ensure the leadership provided by professional management is on mission in terms of co-operative values and purpose. The fate of the Canadian Wheat Pool and the current debacle in the de-mutualised Northern Rock bank (former building society) in the UK are among many examples of demutualisation across the world led from the inside by top management. These cases demonstrate how important the moral compass and value commitment of co-operative management is. *Natal, Libertella, Rothschild and Sora* concludes there are a variety of definitions and development approaches which seek to address the character and ethical development of leaders today. Their paper reviews this literature comprehensively but recognises that so far research is far from conclusive as to what is possible or desirable in a variety of different organisational contexts and they call for further research to be undertaken.

In the paper by *Hanf and Schweikert* we have in their case study of product segmentation strategies in the German wine Co-operative sector another illustration of the important leadership role managers of co-operatives play in practice. In this case to ensure their co-operative not only responds effectively to changing market conditions but also is defended against behaviour by some members that might undermine the economic effectiveness of the co-operative itself. It is surprising to find in Germany laws that require food co-operatives to take any standard of produce. This seems to be contrary to the very high standards of health and quality one has come to expect from German produced food and drink. I know of no co-operative principle that says members can join yet ignore the standards or rules of their co-operative? Open Membership and Voluntary Membership principles yes I have heard of these, but not Anarchic Membership! Indeed it was the late Will. Watkins who, rightly in my view, stated that for a co-operative unity was more important than democracy. (*Co-operative Values Today and Tomorrow,* Holyoake Press, Manchester, 1990, p19) Agricultural Co-operatives are, as the German case study indicates, merging and regrouping in order to retain the necessary leverage on behalf of the small farmer.

Nobody wants to see a European countryside like that of the prairies. Whilst producers co-operatives must respond to the growing power of supermarkets in terms of quality in order not to loose overall market share they also must try to ensure that they defend the rich variety of local wines and other products by developing their relationships and promotional activities with the small specialist wine merchants and by direct marketing through wine clubs etc. of their members low volume but high quality local wines. It is not a question of either or but of getting the balance right in financial terms and in marketing terms, connecting products, price, and place and services to the appropriate customer segment. Education is another important Co-operative principle that can be an important marketing tool today enabling producer co-operatives to reach out to the end consumer and develop their market. Co-operatives particularly those engaged in food and wine production need to be as concerned with consumer education as member education; on the one hand in terms of trade justice, health and sustainability and on the other in terms of encouraging the end consumer to experience the rich variety of good things to eat and drink that nature and labour can produce.

In another Finnish contribution, *Terhi Uski, IIiro Jussila, and Susa Kovanen* present their research into Corporate Social Responsibility (CSR) as practised in the Finnish S co-operative case study. Their research seems to bear out the versatility as well as the strategic importance of the co-operative principle of education. Their qualitative analysis suggests that social responsibility as put into action by Finnish S co-operative fulfilled co-operative values and emphasized regional responsibility demonstrating the importance of customer-owner relations and taking care of the continuity of co-operative business embedded in its regional and / or other community context.

The theme of governance re-emerges in the paper by *Norah Bryrn, Olive McCathy and Michael Ward.* They suggest that there are lessons in the credit union supervisory committee model as a governance tool that could be applied more generally to audit committees throughout the financial services sector and beyond. The paper has some very interesting data

CO-OPERATIVE GROUP TO SELL SHOEFAYRE

The Co-operative Group has today (10 September) announced that it has exchanged contracts with Shoe Zone which is set to buy the Group's retail footwear business, Shoefayre for an undisclosed sum.

Shoefayre, a Leicester-based business, which has annual sales of £65 million, operates 240 high street outlets across the UK, offering a wide range of value footwear.

A spokesman for the Co-operative Group explained: "We have taken this decision after very careful consideration of the options open to us, having supported the business through an extensive change programme over the last 18 months.

"The UK footwear market is highly competitive and further consolidation among retailers is inevitable. It's a specialist area, which is not a core activity for the Group and we would need to make considerable further investment in Shoefayre over a long period of time with uncertain prospects of putting the business back on a sound financial footing.

"In the circumstances, sale of the business to a well-known and profitable footwear retailer is both logical and desirable."

The Group took full control of Shoefayre in 2005, having previously been one of a number of Co-operative shareholders in the business.

It subsequently launched a business turn around programme, which has made considerable progress in reducing costs and improving the customer offer. The sale is expected to be completed in the next few weeks. Shoefayre employs 1900 people, more than 1300 of whom are part-time.

Ends

Notes to Editors:
On 29 July 2007, The Co-operative Group and United Co-operatives merged. The new society is the world's largest consumer co-operative with a turnover of more than £9 billion, 4 million members and 87,500 employees.

The society's major businesses include food, financial services, funerals, pharmacy and travel, together with property, farming, consumer legal services and motor dealerships. In addition, the society operates the on-line electrical and bed retailer, E-stores.

The new organisation operates over 4,500 trading outlets throughout the UK, including food stores, pharmacies, travel branches and funeral homes, which will adopt the uniformed brand - The Co-operative.

on the composition of Irish credit union supervisory committees cross-referenced to their proactive engagement with the main board. I wonder whether this research does not carry the seeds for a further look at composition of boards related to incidents of innovation, social venturing or entrepreneurship within co-operatives?

Al Rashid has given us an interesting business history covering the difficult period leading up to the current situation in Iraq. It deals with issues of incorporation of the co-operative movement by the state and the states ability to use its financial leverage to manipulate co-operatives for its own political agenda. On the question of political interference and the negative impact of top down control of co-operatives by government we have some hard hitting commentary by *Dr Krishna Ramesha*. His focus is on the impact of Co-operative Banking reform in India and its' likely influence on the Indian Co-operative Banks. He draws our attention to the urgent need for more research on the impact of general financial services regulation on co-operative financial services. This is of course is a global problem and we hope to carry more examples and discussion on this from both Co-operative Banking and Credit Union perspectives in future issues.

Under our Executive Opinion features *Roy Allen* presents an interesting paper concerning the application of the risk assessment literature to the co-operative sector. Roy insists that a conscious application of risk management principles to membership based organisations will strengthen their defensive position and enable them to improve their recruitment, development and retention of stakeholders in general. This whole topic of risk management in the co-operative context merits further discussion and debate and we are delighted that Roy has taken time to open this discussion up in our pages. At one level the whole co-operative project may be seen as an exercise in social risk management. If the movement does take on board the principles that it chooses to publicly differentiate itself by (ICA Statement of Co-operative Identity) then the level and complexity of the risks co-operatives need to manage rises accordingly and need to be reflected on and managed.

In the paper by *Edgar Parnell* we have not so much an executive opinion as an executive action with Edgars' establishment of a new Consumer Justice Co-operative. Globalisation has increased the distance between the various stages in the supply chain as well as increased the relative size and complexity of the organisations occupying those various stages. The consumer has very little support in such an unequal contest of individual versus corporation. The market and competitive pressures may help to keep big organisations responsive to their customers and their image according to the economics textbooks and corporate public relations departments. The reality of oligopoly may mean that in many cases customers have little choice in practice and that once a decision to purchase has been made the customer ability to get redress can be limited. Edgars initiative may well be something that the consumer co-operative movement might at first see as a rival or implied criticism of its own effectiveness. But I believe a more considered reflection will show that Edgars' idea is right. An independent non- retailing body is the only one that can be said to deal impartially with genuine consumer concerns. As such genuine retailers and other service providers should welcome and support Edgars Consumer Justice Co-operative as a timely move to counter unethical traders.

I am grateful to *Gus Poston* for his excellent write up of his field research in terms of the methodology as well as the strategic management context. I hope we can carry more reports of field work in development goals and strategy and how such activities are being managed in future issues.

Finally I wish to draw readers attention to the sale of the UK Co-operative Shoe chain *Shoefayre* and call for papers on this and other co-operative sell-offs from academics, senior managers and co-operative directors primarily in the Co-operative Movement in Britain. Overseas commentary on the British movement would also be welcome. I would like the authors of these papers to respond to the following press release, which I reproduce in full opposite as it was sent to me by the Co-operatives Group PR Department following my request for a copy. This is the latest in a long and sad line of sales of major brands by the UK Co-operative Group from the demise of food manufacturing through to the more recent sale of its' opticians business. It is particularly unfortunate for the consumer of shoes in the UK as shoe retailing is such a highly concentrated market and as such the co-operative presence was all the more important to provide real choice. In funeral services the industry is now a virtual duopoly between the Co-op and a US Multinational. A successful consumer co-operative movement in Britain is clearly therefore in the public interest if we believe the economics rhetoric on the importance of real competition.

Am I alone in thinking that this is yet another illustration that the British consumer co-operative movements' management are unable to expand and develop its retail business? Is the rationale that the movement needs to raise capital? If so what is the purpose? Given that we are about to embark on giving capital away in a new member dividend scheme being short of capital cannot be the answer so we fall back on the explanation that our management are not able to run the retail shoe business successfully. Another explanation might be that they are going to invest members' capital in a more beneficial way? If so what are the new business ventures and or services to members that are being delivered with the undisclosed sum? Who brokered this deal? After the scandals of recent years are not members entitled to total transparency concerning a sell off of this nature? Academic papers and executive opinions to the editor please.

Peter Davis
December 2007

Mission of the Journal

- ***To act as a medium for the dissemination of best management practise in the co-operative movement***
- ***To act as a medium for the publication and dissemination of research into the management of co-operatives***
- ***To act as a platform for informed debate within the co-operative sector on issues and problems arising from the management of co-operatives***
- ***To act as a vehicle for promoting the professional development and status of managers in the co-operative sector across the management profession as a whole.***
- ***To act as a medium for the discussion and dissemination of the latest thinking in all areas of management that may have a relevance to the practise of management in the co-operative sector.***

The Co-operative Difference: economic, organizational and policy issues

Andrea Bernardi

Abstract

The paper poses the question what is different about co-operatives and is co-operative action still relevant today? Why should policymakers pursue it in development strategies? In what way are co-operatives different in terms of economic theory and organisation theory? And if there are differences in organisation, human resource management practices, property rights and forms of collective action, what are the governance issues to be addressed so as to allow co-operatives to operate and grow correctly? The article proposes a reflection both on research opportunities and on the management challenges of co-operatives with particular emphasis on co-operative relationships and organizational lifecycle issues.

Key words

Co-operatives, Collective action, Lifecycle

Introduction

This paper was written against the background of animated discussion in Italy on the role of co-operation. A large, traditional insurance company controlled by numerous co-operative firms attempted a stock-market takeover of a major Italian bank with the aim of creating a co-operative banking and insurance corporation. The takeover bid failed because of opposition on the part of Italy's central bank and scandals involving the top management of the insurance company, which is controlled by the co-operative movement connected with the Lega delle Co-operative.

The birth of a co-operative enterprise is characterized by the primacy accorded to collaborative association between people, be they consumers, users or entrepreneurs. The motivation, involvement and participation[1], of workers have become very modern priorities in our post-fordist economy for most leading multinationals as well as smaller enterprises (Noe et al. 2006).

In the present-day West European societies, characterized by mature democracy and the disappearance of ideologies and mass movements, the capacity for association among individuals has become a precious asset to be protected and cultivated, above all in areas that have not ever known intense and constant social mobilisation and have always suffered from a shortage of social capital (Bourdieu 1980, Coleman 1990, Fukuyama 1995, Putnam 1993).[2]

Co-operatives in our economies

Flexible specialization is the most successful organisational model in the new "industrial paradigm" (Sabel 1984) characterized by transition from the standardised mass production of similar goods by means of specific and non-flexible machines to non-standardised production where organisation performs the task of adapting flexible plant to uncertain markets. The winning formula in this new paradigm is no longer the large-scale integrated company but the small firm capable of working with its neighbours to develop technical and human organisational capacity enabling it to adapt to market fluctuations and changes in the tastes and needs of consumers. The model that has emerged is based on growing integration, co-operation and competition between enterprises that belong to the same network.

The traditional industrial paradigm prompting the pursuit of concentration and economies of scale is giving way – or at least according equal importance – to the model of networks, flexibility, the "soft" integration of districts, alliances, consortiums, and flexible forms of shareholding. The form of co-ordination developed within the network has no hierarchical rules and is not based solely on price mechanisms. In other words, we are outside Williamson's market/hierarchy dichotomy (Williamson 1981) and inside a flow of vertical (two-way), horizontal (equal) and lateral (decentralized) relations (Ouchi 1980).

The co-operative firm must find, and indeed has found, its own role in this scenario, one that can be brilliant and crucial in the intricately flexible and competitive relations between enterprises. It should, however, be pointed out immediately that the co-operative form of co-ordination of economic activities, occupying an intermediate position in the hierarchy-market continuum, is intrinsically difficult to achieve (Seravalli, Arrighetti and Wolleb 2001). It is the delicate result of balance that supports bottom-up collective action between people and firms. Such balance is difficult to establish and maintain in a world increasingly dependent and based on information that is witnessing the ever more frequent failure of the other two pure forms of co-ordination, namely hierarchy and the market (consider Stiglitz's works on the consequences of the structural and pervasive lack of information, Stiglitz 1975). Given this awareness, economic theory has moved well beyond the bipolar hierarchy-market model and adopted an intermediate formula of transaction regulation, namely the clan or the collective (Barney and Ouchi 1985, Williamson 1986). This intermediate form, which is actually the oldest (Douglas 1986), remains the most difficult to establish in everyday practice. Thus it is no coincidence that hierarchy and market are the solutions most widely adopted. Though difficult to establish, it is, however, necessary and competitive once put in motion. Some anthropologists who have traced back the ancient roots of co-operation claim that bottom-up collective action is practically bound to disappear in open or large-scale communities (Douglas 1986, Levi-Strauss 1973). Consider the forms of collective or communitarian work that were so widespread not only in all the pre-Columbian communities but also in Asia.

It is by no means irrelevant in this schematic overview to point out that in Europe the pure protagonists of the other bipolar model, i.e. state and market, are also proving more and more frequently incapable of meeting the demands made on them by the communities. Here too, as we shall see, there is an explosion of the bipartite model to make way for an intermediate figure, namely the third sector. In short, authentic co-operation could suddenly find itself modern, necessary, equipped to tackle the challenges of our day, and in some cases a step ahead of the traditional companies, which have always regarded it with suspicion and attitude of superiority.

If this is true, co-operatives have something to offer workers, markets, and the communities on which they focus. This paper will examine how government and local authorities can help to harness these energies and this ancient modernity.

Between state and market

Nearly all the European countries went through a cycle of massive state intervention in the economy and a phase of privatisation and liberalisation between 1945 and 2005. After the most important experience of state control in West Europe in the post-war years, the Italian economy in particular has been involved in an intense process of privatisation and liberalisation since the 1990s (with marked deceleration in the early years of this century). Privatisation has been carried out in Italy with determination, even though the ownership structures deriving from the sale of former state-owned concerns have not always guaranteed correct transition to a market culture. Not always courageous and not always accompanied by adequate action on the part of the authorities responsible for control and regulation, liberalisation has produced no results. In other words, many of the markets involved in privatisation and liberalisation have not become competitive, many former state-owned concerns have not become contestable, many of the economic agents that have taken over from the state in the control of utilities, banks and industrial concerns have shown no desire or ability to operate with an adequate entrepreneurial market culture.

Italian citizens have seen a slow but constant decline in the services provided by the welfare state since the 1990s. The retreat of the state with respect to certain demands expressed by citizens, has given rise of a new private-sector entrepreneurial class with much the same oligopolistic tendencies and no greater concern for the customers and users of regulated markets. The internal political instability caused by the crisis of the "First Republic", and demographic changes have unquestionably been additional major factors of stress for Italian society.

A still more important and often crucial role for social stability and economic plurality (Spear 2000) has been assumed in this context by intermediaries between state and market, individual and society, enterprise and citizen. The phenomenon appears to be common to most of the European continent but particularly intense in Italy, which underwent a radical political crisis in the 1990s that has yet to find resolution in a mature bipolar system. The demographic figures (OECD 2004) show marked aging of the population accompanied by the perception of reduced security and stability. In economic and institutional terms, we can see an industrial crisis due primarily to productive specialisation accompanied by historical inefficiency in the public sector.

Let us consider the rapid growth of associative participation and voluntary service, the new leading role of co-operatives, the debate on the civil economy and the social responsibility of firms, and the growing interest in non-profit concerns and the third sector. This world – both associative and entrepreneurial, both for-profit and non-profit – constitutes not only a buffer between the two other major components of the western societies and economies but also in many cases a necessary contribution to the correct functioning of a plural, efficient, competitive market with respect for the consumer, the user and the citizen. It is, however, no easy matter to explain and defend the importance of these organisational forms in a world that is so uninterested in economic pluralism and practically convinced that we have indeed arrived at the "end of history" (Fukuyama 1992), at least on the economic front. History has not, however, come to an end, at least in the sense that there are different forms of market economy (Albert 1991) and different forms of company and company ownership as well as very different ways of running a firm in a market economy.

Co-operative identity and role

The internal and external debate on co-operative values and identity has in any case regained present-day relevance and intensity. The question arises of whether there are qualitative or quantitative limitations to be placed on the operations of co-operatives to ensure protection of their identity. Co-operatives can hold shares in companies, including those quoted on the stock exchange. Even though there are few who believe that co-operatives should remain small and residual, there is discussion in Italy today about the need for limits to ensure that such shares are held with a view to the best possible pursuit of the co-operative's mutualist objectives.[3] While we believe it important for the plurality (Hansmann 1996) of the Italian economy [4] that co-operatives should be able to operate in all sectors and all markets, it is equally important that this should take place in accordance with the identity of the co-operative movement and its primary values, such as mutualism and democracy (Olsen 2002). The lack of homogeneity in the characteristics of the firms operating in a market increases the capacity to meet the needs expressed in that market .

> *"There is a place in a modern mixed market economy for a model of business that is driven by the needs of the people who use its services rather than those who invest their capital in it. Indeed such forms assist the efficient and sustainable functioning of markets." (Commission of the European Communities, 2001).*

Regardless of the economic and social sector of action, we believe on the whole that co-operation of the first, second and third degree can be seen as a tool or logic of corporate integration. There is a need for integration both at the national level (in a country like Italy, suffering from industrial dwarfism and now discovering to its cost that small is beautiful but not sufficient) and at the European level, where it is becoming essential in an ever-increasing number of industrial sectors to attain the supranational critical mass needed to operate on the global markets.

Co-operatives must make integration at group and sector level their watchword. They must experiment with processes of internationalisation and strengthen their international partnerships: not only a presence on foreign markets but also integration with other co-operative concerns. Interest attaches in this connection to a number of developments in Europe, e.g. the integration achieved between Danish and Swedish co-operatives. There are, however, also more streamlined forms of collaboration. For example, co-operatives from different countries can set up joint enterprises to market their products. Given the territorial nature of the co-operatives participating and the international dimension of the strategy adopted, cases of this type have been described as instances of authentic "glocalism".

We are convinced that co-operatives can demonstrate that it is possible to "square the circle" (Dahrendorf 1996), combining competitiveness and innovation, territorial roots and social and environmental sustainability. Co-operatives should accept this challenge and blaze an exemplary trail for other economic concerns. While co-operatives can certainly make a contribution, the regulating authorities must be fully convinced and aware that co-operation is a delicate plant that grows spontaneously but is not an aggressive weed. The spontaneity of co-operatives stems from the innate human tendency to work together. In the works produced immediately after his famous treatise on competition in the animal world, Darwin himself took pains to point out (not least in order to counter the apocryphal readings that have continued up to our day) that human evolution, unlike its animal counterpart, is based on co-operation, altruism and love rather than competition, selection and struggle (Pievani 2006). Moreover, this collaboration is not only typical of poor or struggling economies and communities. The co-operative lends itself to human collaboration in the satisfaction of both basic and higher needs. The co-operative serves to set up a store in poor, isolated village, to organise free and secure work, and to fight unemployment or exploitation but also to offer work with greater fulfilment and autonomy, to foster the spread of socially and environmentally sustainable foodstuffs, or indeed to buy and run an otherwise inaccessible sailing boat. In short, co-operation is a tool serving to overcome difficulties and the state of necessity or simply to meet higher demands in the pursuit of goods or values that society is not otherwise in a position to supply.

Co-operative action and process

Though spontaneous and innate in human beings, as pointed out above, this form of organisation in also rare, not least because the co-operative formula requires specific ingredients that are not always readily available everywhere. Co-operatives are organised in a different way, for example, given that participation and democracy have organisational consequences (Davis 2004). The participation of co-operative members and workers rests on different motivations from those operating in traditional firms. Some have spoken of "ideological workers" (Ackerman 1986) and some of "ideological organisations" (Mintzberg 1996). The role of the trade union and the functioning of industrial relations are also different. With respect to the tripolar model of market, hierarchy and clan (Barney and Ouchi 1986), it seems possible to suggest that the transactions of co-operatives and their members are potentially subject in some cases to considerations not only of price but also of hierarchy and trust. With reference to Hirschman (1970), it seems possible to state that the weapons of exit, voice and loyalty are sometimes simultaneously available to co-operatives and their members. While having three weapons in one's hand may prove very useful in some cases, however, it can also prevent reaction in others. In any case, co-operative behaviours are the result of equilibrium in situations of heterogeneity as regards aims, conduct, and the agents themselves (Spear 2004).

As shown by Axelrod (1984, 1981), co-operative interaction is rare but possible and potentially stable, above all in a medium-term evolutionary and iterative perspective. The actors can learn to co-operate from the experience of previous interaction, they can be induced to do so through sunk investment, or they can be institutionally directed toward co-operation. In short, bottom-up collective co-operative action is more complex. This complexity must be handled and supported to ensure that it takes shape from strength rather than weakness. Co-operative firms are non-capitalist enterprises in that the ownership rights are not transferable.[5] A co-operative is created in order to provide a service for its members and to do so with a democratic and transparent form of management based on participation. It is created in order to foster entrepreneurship in accordance with the territorial nature of the enterprise and the freedom of entry and exit for members. Co-operatives are enterprises controlled by members (workers, consumers, producers or associated entrepreneurs).

As Zamagni (2001) points out, the primary objective of the co-operative is "not the maximization of profit, as it is for the capitalist enterprise, but maximization of the social dividend defined as the difference between revenues and costs (but not including labour costs) divided by the number of members. This means that while in the capital-based enterprise profit is a residue that ends up in the hands of the owners and wages are a constraint, the exact opposite is true in the co-operative firm, where the remuneration of the holders of the capital is a constraint and the social dividend a residue." Actually every economic explanation of the co-operative difference is not valid for every type of co-operative. This last one, as an example, is valid only for worker co-operative.

Co-operatives and the policy maker

Co-operative firms are, however, enterprises integrated perfectly into the mechanisms and culture of the market economy, and it is precisely in the world's most advanced market economies that they now account for a larger (and often growing) proportion of national income. It is precisely in these economic contexts that co-operatives often help to counter the effects of market failures. Company control is based on individuals and not on capital (per capita voting). These individuals, i.e. the members, forgo the use of their property rights because it is impossible for those leaving the co-operative to obtain the increase in value of economic capital incorporated in their share of the firm. In return for this sacrifice, legislation in many countries offers the benefit of tax exemption on a proportion of the profits; to the extent that members (owners) and customers (users) are the same persons, no profits can be derived in order to be taxed. The tax exemption of profits channelled into an indivisible reserve (as in the fiscal policy of Italy and other countries) can, however, also be seen in actual fact as no more than an incentive to company capitalization (Similar laws encouraging co-operative capitalization also exist in certain countries for non-co-operative firms).

For this reason, there is nothing extraordinary about the present system capable of damaging the functioning of the market. On the one hand, entrepreneurs taking a critical view of the advantages enjoyed by co-operatives can convert their firms into co-operatives whenever they choose. On the other, tax schemes to encourage capitalization have always existed and will continue to do so also for traditional firms. Moreover, all economists, politicians and leaders of entrepreneurial organisations with a knowledge of the demographic statistics for Italian firms[6] should take great interest in the ability of co-operatives to be inter-generational and, in exemplary cases, oriented toward capitalization. The figures for the last 15 years clearly indicate a strong tendency toward growth on the part of Italian co-operatives, unlike the average Italian firm.

Moreover, current Italian legislation requires co-operatives to allocate 3% of their profits for social purposes, which is usually done through the national mutualist funds for training and promotion in the co-operative sphere. This legislative provision constitutes one of the stimuli behind the efforts of co-operatives in the sector of social solidarity and mutual aid (also at the external level), together with their traditional values and ideology. Those who have questioned in recent months the legitimacy of a joint-stock corporation being controlled through the stock market by a company that is a co-operative and hence not contestable cannot ignore the fact that none of Italy's major quoted companies are actually contestable on the market because they are controlled by intricate interlocking systems of shareholders' agreements permitting the iron-clad protection of ownership rights with minimal amounts of capital. The ownership of unquoted firms is also extremely concentrated and almost equally as non-transferable in practise as the co-operative.

Criteria for the evaluation of co-operative authenticity

Non-profit?

The recent demands for co-operatives to remain in the "non-profit" area of the Italian economy make no sense. All in all, it must be stated again that co-operatives are non-capitalistic but oriented toward the market and the pursuit of results ensuring their stability and growth in terms of finances and assets. We can say Co-operatives are "not for profit" in the sense their aim is not to achieve profits for distribution to the owners of capital. Notwithstanding most co-operatives still have to make a return on capital employed sufficient to grow at a competitve rate in their particular marketcontext. Not all co-operatives operate in the third sector. Actually neither "in profits" nor in "not for profits" is where the co-operative difference lies. Co-operatives are bodies resulting from a unique system of ownership and governance endowed with a particular social responsibility to meet the developmental needs of their members, other stakeholders and the wider community.

Size?

A certain nominal institutional form does not mean we will always have a good corporate behaviour. For these reasons it does not make sense, in the light of the above considerations, to call for limits to be somehow imposed on the size of co-operative firms or to restrict the sectors in which they or their subsidiaries can operate. In any case, large and successful co-operatives do not necessarily stop being "good" co-operatives. Growth in terms of scale (social base, balance sheets, organisational complexity, etc.) and age is not always accompanied by a loss of cultural and democratic values. There are no industrial sectors where co-operatives maintain or lose their identity by definition. Functional and organisational development is not incompatible with preservation of the co-operative identity. It should be borne in mind that the same phenomena of false co-operation are already present all over the world from Colombia to Chile, from Finland to Spain, which proves that is not even the degree of social development and prosperity that fosters or deters them (Bernardi 2005).

The growth of co-operatives is necessary in many industrial sectors and the tool of the co-operative group is useful as well. It is also a good idea to experiment with processes of internationalisation and to concentrate the attention of the co-operative movement on the need for organisational development and on the question of generational turnover, which is currently assuming ever-greater importance.

Participation?

The problem of false co-operatives unquestionably exists in Italy, and it is in this area that the problem of unfair competition comes into play. There are co-operatives in name only, where the members have no real right to participate in the decision-making process. Current Italian legislation grants tax benefits only to "predominantly mutualist" co-operatives, where relations with members account for at least 51% of the business (work or sales, depending on the type of co-operative). This indicator is not, however, sufficient. Apart from the quantitative yardstick, it is necessary to identify a new system of parameters in order to attribute mutualist merit. Not all the "predominantly mutualist" co-operatives, in the sense indicated by current legislation, are good co-operatives and mutualistically meritorious, and vice versa. The quantitative provision is certainly insufficient to assess mutualist merit. Why not propose legislation or a system of voluntary certification designed to limit the phenomenon? One possibility would be a national co-operative logo with certification of managerial qualities and democratic governance (based on an ISO or TQM model accompanied by a social report). The local authorities must become more perspicacious in the formulation of calls for tenders to select co-operative firms that are meritorious from all points of view.

Co-operative firms seem to be intrinsically organisations oriented toward a lower degree of consumption of social capital (Spear 2000). This is not because they are "better" more socially responsible by definition – we are indeed well aware that this is not so – but simply because the functioning of co-operatives requires the production and use of social capital (Fukuyama 1999, Hollis 1998) rather than consumption. Suffice it to consider the way they are run through democratic assemblies, their links of mutual aid with other co-operatives, and the extent to which they are rooted in local communities. Suffice it note that the regions with the greatest co-operative tradition and vocation in Italy are those to which Putnam (1993) attributes a higher level of public spirit.

It must be said, however, that with the authoritative exceptions of Walras and Alfred Marshall (1890), who noted the superiority of the work of the co-operative movement, the classical and neoclassical economists have always viewed the co-operative enterprise with suspicion and denied the existence of any specific economic behaviour on the part of co-operatives in terms of economic theory. Some have indeed endeavoured to demonstrate the economic inefficiency and limitations of self-managed enterprises (e.g. Einaudi, Pantaleoni and Ward). The opposite approach is instead taken in both the strictly economic and the philosophical works of Jaroslav Vanek (1970, 1985, 2000), the illustrious economist of Cornell University, who went so far during the last years of his intellectual career as to trace the origins of co-operation in the history of Christianity.

Keynes and Robertson conversed on the macroeconomic effects of the presence of co-operatives, as an example, in terms of stability of the economic cycle. Another theoretical explanation of the economic significance of co-operative firms suggests that their competitive advantage is based on the efforts of consumers to overcome the uncertainties associated with the presence of informational asymmetries in the purchasing of goods and services.

With reference to the question of differentiation and identity, it could be argued that for some years now various Italian co-operatives have stopped insisting on their differentiation or made an effort to become more similar to other firms because of their inability to communicate the positive nature of their difference. They have at least stopped proclaiming their differentiation in terms of an alternative to capitalistic company control (which remains the only true difference for economists). It has for some time now been another difference that is insisted on in image campaigns, in the co-operative corporate identity, and in the conferences of the co-operative organisations. This is based on a democratic approach, social solidarity and responsibility, the ability to foster local development, and attention to the rights of members and consumers. It can also be added that it is intrinsically visible in the tradition of self-managed and co-operative work that development is freedom (Sen 2001), that the well-being and autonomy of workers and entrepreneurial success are not only compatible but also interconnected.

The problem of poor image of the co-operative sector

The co-operative image is in need of improvement. The co-operative enterprise must be conceived and communicated externally as the form ensuring the greatest degree of well-being for workers as well as the most economically advantageous conditions for users and consumers.

A report of the European Commission uses this definition:

> *"A co-operative is an enterprise like any other, but it is also an enterprise that exists to serve the needs of the members who own and control it, rather than solely to provide a return on investment. All enterprises exist to serve the interests of their cardinal stakeholder groups. For traditional companies that means investors, however in a co-operative returns on capital (which are in some cases permitted) must always be subordinated to other interests. In fact a non-co-operative enterprise might be called an association of capital (or investor-driven business) whereas a co-operative is an association of people (or people-driven business)." (Commission of the European Communities, 2001).*

Paradoxically enough, it is precisely this very important public report that offers the most striking example of the identity problems discussed here. It is very strange that the European co-operative movement, which certainly had contributed to the drafting of that report, allowed it to be written that the co-operative is an enterprise like any other. Co-operatives are very particular enterprises indeed and very different from other forms of economic organisation.

The impact of life cycle and change on co-operatives

This change in attitude with respect to the system is a characteristic that Meister (1969) and Zan (1982) noted through an empirical study ot the orgarnizatonal lifecycles[7] of co-operatives and that it appears possible to use metaphorically today in discussing the state of the co-operative movement as a whole. The authors have two different visions of the evolution toward the market, professionalism and efficiency of co-operatives. On the one hand, there is optimism that co-operative values and features can stand up to competition from capitalist firms; on the other, pessimism that growth, reorganisation, and time will irreparably transform the co-operative spirit of the movement.

According to Meister there are generally four lifecycle phases among co-operatives.

In phase I, denominated by the author as the *phase of conquest,* there is hope and enthusiasm of members, low degree of differentiation in the social system, direct democracy and emphasis on assemblies. There is low differentiation of organs and positions and responsibilities are assumed on a voluntary basis. There is an imprecise economic management with low levels of efficiency and results falling far short of expectations.

In phase II, called *phase of consolidation,* we usually find idealism giving way to indifference and greater differentiation of roles. The power of management groups is reinforced with differentiation of organs, delegation, attention to economic questions.

In phase III, named *phase of coexistence,* we usually find subordination to the external environment also in terms of values. There is always greater expansion of delegation and adoption en bloc of methods previously described as capitalist.

In phase IV, called *phase of management power*, the economic, organizational and managerial complexity necessitate the maximum degree of specialisation. Managers and directors (not always coming from an internal career path) hold the real power and no real control is exercised by members or their delegated representatives. The concentration of information in the hands of experts is high.

According to Zan there are generally three phases in the co-operative organization lifecycle.

In phase I, named, *phase of defence* we usually find collective enthusiasm and direct democracy. There is organisational simplicity and mechanical solidarity. The members share an internal closure, the union of weaknesses, the rejection of the market and the culture of struggle. In phase II, *denominated phase of consolidation,* there is an initial political and economic success that brings an increase in size and complexity. This, in turn, brings delegated democracy, crisis of solidarity, opening of social base and acceptance of market although pointing out its contradictions. In phase III, named *Industrial phase,* the economic consolidation suggests an organisational rationalisation with greater formalisation and organic solidarity. At the end the culture of the market facilitated with the arrival of new members and managers coming from the outside will prevail.

The partially diverging theses of Zan and Meister are broadly discussed and analysed in a recent work on the organisation of co-operatives (Battaglia 2005), which compares Italian, European and Latin American case studies in an effort to take stock of the relationship between growth, the continued existence of ideological, cultural and participatory characteristics, and the external influence of what is known as the co-operative organisational field (DiMaggio, Powell 1991, Battaglia 2005). One of the identity problems facing co-operative firms today seems to be the search for a way to preserve their differentiation while complying with most of the rules of the system. It is necessary first to consider the cornerstones of this differentiation and bring them into line with the new requirements of society and the economic system, and second to pursue and defend this differentiation – or new differentiation – through coherent and transparent interaction with the other forms of business and all their stakeholders.

Only when both the national co-operative organisations and the individual firms have thoroughly considered the questions of identity and differentiation will it be possible to address the problem of the growth strategy of the co-operative movement. Only then will it be possible to discuss, for example, the advisability of certain financial or industrial operations, mergers and alliances, or the instrumental use of capitalistic firms. In any case, it already appears obvious that the decision to do without modern entrepreneurial tools serving to compete on an equal footing with capitalist (or traditional) firms would involve too great a risk. While it would be a mistake, in our view, to impose legislative limits on the sectors in which co-operatives can operate, it is undeniably true that the co-operative formula proves particularly competitive in some industrial sectors and not in others. It can be suggested initially that this derives from differences in the combination of the productive factors of capital and labour in the different industries.

It then appears equally obvious that the traditional links between Italian co-operative organisations and political parties (especially the old Communist and Christian Democrat parties) must be reinterpreted in order to meet the new requirements not only of co-operation but also of the political sphere and the national economic system. While the existence of a cultural matrix is a strength and a source of riches, co-operatives and the organisations representing them must maintain their independence with respect to national and local politics (and vice versa). Dialogue with all the social and economic actors, including the political, is instead indispensable and advisable.

The consideration of co-operative identity certainly cannot overlook the importance of the real degree of democracy and participation in the decision-making processes. There can by no co-operation if member participation is not practised, cultivated and fostered by management. Members must be qualitatively and quantitatively involved more frequently in the decision-making processes and in the renewal of managerial structures. It is necessary to strengthen the mechanisms of democratic participation (e.g. by examining the issue of delegation and voting at a distance) so as to avoid any undue increase in the powers of managers (sometimes professionals hired from outside) at the expense of the membership.

This is a currently relevant problem in Italy but also in the rest of the world. And the role of human resources in company competitiveness is far more critical today than in the past all over the world. Motivation, empowerment, delegation and participation are becoming extremely powerful and indispensable tools above all – but not exclusively – in knowledge-intensive firms and services. Co-operatives can derive an advantage from this because they have been accustomed to worker centrality and involvement from the very outset. And then, how can the co-operative tradition not be regarded as modern at a time when so many are calling for greater industrial democracy? Borzaga (2002) points out that social co-operatives,

> *"……..seem to have succeeded in finding ways to govern their strategic factor of production, i.e. labour, that are more efficient than those adopted by the public sector, capitalist firms and most of the other non-profit organisations. While paying their workers less on average than the other organisations operating in the sector of social services, they adopt salary structures that reward seniority and loyalty, and appear capable of attracting young educated and motivated workers through incentives other than salary.*
>
> *It also appears that the social co-operatives have succeeded so far in attracting a well-trained and motivated workforce and adopting wage and organisational strategies perceived as fair by their workers despite the limited scale of their resources."*

There are nevertheless also different economic explanations of the successful presence of co-operatives in our markets outside of the social co-operative area (Ackerman 1986, Hansmann 1996).

The importance of control and governance

We consider it important to return to the question of control over the firm. As Hansmann (1996) points out, there are efficiency-related grounds to establish when it is preferable that the owner of an enterprise should be one of the possible parties operating in our market economies: the entrepreneur, the investor, the state, management, the users, the workers, etc. It is context alone that determines the conditions enabling one of these to perform the function more efficiently. There should be no prejudices with respect to one or more of the potential owners (Olsen 2002).

> *"The freedom of enterprise is a fundamental characteristic of the most advanced modern economies. Capitalism, on the contrary, is contingent; it is simply the particular form of ownership that most often, but certainly not always, proves most efficient with the given technology."*

And it is precisely comparison and competition between different forms of company control that can produce positive effects for the markets. But are the mechanisms through which the members of a co-operative, the owners of this form of enterprise, can supervise and assess its progress adequate today? Since the type of ownership is different, there are also differences in the challenges of co-operative governance (Cornforth 2004). Corporate governance is to be understood as a set of tools (institutions, rules, mechanisms, guarantees) designed to foster a correct decision-making process within the company in the interests of the various categories of stakeholders (Powell 1987). The problem of governance arises with the separation of ownership and management in large-scale corporations. The alleged scandals and industrial crises of the last few years have made this a currently relevant problem, and not only in Italy. Co-operative business systems with highly fragmented ownership (or rights) require particular attention, and this problem is further complicated by the imperfect transferability of ownership rights and the greater number of types[8] of stakeholder in the co-operative. The reform of company law has had a partial effect in this sector.[9]

The typical – and opposite – risks are the inability of the member or groups of members to exercise the correct degree of control and guidance over management and the inability of management to implement adequately competitive strategies enabling the firm to operate on the market. It is obviously impossible to address this question without going into the details of each type of co-operative.[10] For example, the control over company internal bodies, with respect to the management of co-operatives making great use of equity stakes in instrumental companies, appears to be a very sensitive and critical issue because it is more difficult to exercise control, because the risk of deviation with respect to the original and statutory objectives is greater, because the divergence of goals between management and members is potentially greater, and because of the potential growth of non-transparent conduct. At the same time, however, there can also be growth in mutualist effectiveness with respect to members or to the competitiveness of the core activities managed directly by the co-operative. It is important to let members select the system of management and to specify the roles of the elected and of the appointed leadership.

There are, however, some possible reforms that appear suitable for practically all of the co-operative world, including the rotation and limitation of appointments, greater use of proxies in general meetings, independence of management, controls over the indirect distribution of ownership shares, adequacy of organisational structure in relation to size and type of co-operative, certainty of mutualist exchange, adequate information and involvement of the grassroots membership, and the co-ordination of control functions. Reflection also appears necessary because there is no lack of different schools of thought even within the Italian co-operative movement.[11] As regards proxies, for example, those in favour are opposed by other who think that democratic participation must be individual rather than delegated and that therefore only the former is to be fostered and promoted, e.g. through the mechanism of separate assemblies. Many react very negatively to talk of limitations on mandates for company appointments, e.g. by pointing out that no such limitations exist in traditional firms.[12]

The squaring of the circle can only come about, however, through an understanding of co-operative differentiation and identity. We are talking about enterprises that differ from others starting from their system of ownership rights, enterprises of an initially democratic nature that see the fragmentation of their members' rights increase together with their growth. Paradoxically enough, in a context of family entrepreneurship such as obtains in Italy, co-operatives are experiencing the centrality of management and the necessary division of ownership and management before traditional firms (as happened previously with the state-owned companies). It is necessary to consider the risk of the major co-operative firms coming to operate like authentic public companies but without some of the safeguards provided for quoted companies, e.g. mechanisms of association and representation for small shareholders, more stringent procedures of auditing and control, a framework to regulate conflicts of interest, etc. It is in any case be possible to argue theoretically that the major co-operatives, unlike quoted companies with vast numbers of shareholders, would not encounter the typical risk of management oriented toward predominantly short-term objectives (being motivated, for example, by reward systems linked to share prices). The development of participatory mechanisms with multiple voting involves the risk, however, of producing a hybrid in still greater need of innovative mechanisms of governance (Spear 2004).

Conclusions

The leitmotiv of this discussion appears to be differentiation, something often put aside, forgotten or viewed with suspicion by the co-operative members themselves. In our view, the international co-operative movement should regain its pride in its diferentiation and use this as the basis to reconstruct its identity.

It is possible to trace a consensus in the economic and organisational literature on the differentiation rather than the superiority or inferiority of the co-operative entrepreneurial formula. In particular, differentiation combined with the characteristics of markets and technologies becomes a competitive advantage in some industrial sectors and a disadvantage in others. We believe, however, that it must be the market and not legislation that sets limits on the operations of co-operatives. We believe that the residual tax benefits granted to co-operatives in Italy and many other countries are prompted by their differentiation and in no way prejudicial to the correct functioning of market; to the extent that members and customers are the same persons, no profits can be derived in order to be taxed. These advantages are in any case available to anyone opting for the co-operative form of enterprise. Co-operatives do not ask for privileges. The treatment they receive must remain partially different because they are inherently different.

The strategy for the next one hundred years of co-operation in Italy needs to address the question of co-operative differentiation and identity. In any case, an understanding of present-day differentiation is essential, for example, to the use of forms of training capable of guiding co-operative management toward ethical differentiation and an understanding of the organisational and operational peculiarities of enterprises of the co-operative type. Co-operative management must be able to operate in a different type of firm but must also be equipped with the entrepreneurial tools used by non-co-operative companies.(Davis, 1999)

Co-operative firms are different and must remain so. Their ancient modernity is the strength upon which they can draw in addressing the market for human services. It is certainly not a good idea to conceal the need for entrepreneurial and organisational development. Co-operatives must be capable of coping with generational turnover and handling the degree of organisational development that is indispensable for healthy growth. Growth must be managed but is essential in many industrial sectors for firms wishing to be competitive at the national and international level.

Resumen

¿Las cooperativas y la acción cooperativa son experiencias modernas? Por qué debería llevarla a cabo el actor político en las políticas de desarrollo? Qué diferencia cooperativa hay desde el punto de vista de la teoria económica y de la organización? Y, si existen diferencias en cuanto a la organización, en la práctica de la gestión de los recursos humanos, en los derechos de propiedad y en las actitudes de acción colectiva, ¿cuáles son las cuestiones de gobernabilidad que tienen que controlarse para que la cooperativa pueda operar y crecer adecuadamente?

Riassunto

Le cooperative e l’azione cooperativa sono una esperienza moderna? Perché dovrebbero essere sostenute dal policy maker nelle politiche di sviluppo? Quale è la differenza cooperativa dal punto di vista della teoria economica e dell’organizzazione?

E se ci sono differenze nell’organizzazione, nelle pratiche di gestione delle risorse umane, nei diritti di proprietà e negli atteggiamenti di azione collettiva, quali sono le questioni di governance che devono essere tenute sotto controllo affinché la cooperativa possa operare e crescere adeguatamente?

Notes

1. See in this connection the partial results of the Metatrend 2004 study carried out by the CRORA research centre on business organisation of the Bocconi University under the supervision of Anna Grandori, which draws attention to the competitive importance of mechanisms of organisational equity and democracy in firms.
2. Putnam’s notion of social capital is linked to the concept of civic tradition and is a collective asset rather than a resource enjoyed by individuals. Bourdieu’s is less tied to the tradition of a certain community: “Social capital is the set of actual or potential resources connected with the possession of a lasting network of more or less institutionalised relations of reciprocal knowledge and recognition, i.e. with belonging to a group (…). The volume of social capital possessed by a particular agent therefore depends on the scale of the network of connections that he can effectively mobilise and by the volume of capital (economic, cultural and symbolic) held by each of those with whom he is connected.” The view put forward by Fukuyama is oriented toward the idea of trust and the sharing of values. Other views occupy an intermediate position between the ideas of the relational network and a shared tradition of values and trust.
3. Some co-operative managers have, for example, called for legislation taking into account new forms of mutualism, e.g. at the group level.
4. Plurality of forms of enterprise and ownership structure: ownership by shareholders, workers, users, or in some cases (why not?) through public shareholding.
5. The very concept of economic capital loses its meaning because it is impossible to transfer or sell the enterprise.

6. Dwarfism and difficulties in handling family succession are critical issues in the Italian entrepreneurial system.
7. Other studies on organizational life cycle, such as Greiner (1972), Alderfer (1972), Whetten, Kimberly, Cameron (1980), Quinn and Cameron (1983), Baum and Singh (1994), Van de Ven, Poole (1995), Aldrich (1999), were born around capitalist traditional firms and do not always work with the co-operative organizations. For example Greiner cycle from some points of view result inverted in co-operatives.
8. In some cases, for example, there are theoretically clashes between the interests of the member and the worker or the member and the consumer, stakeholders that are often represented, however, by the same individuals. Moreover, the benefits that members wish to derive from their membership of the co-operative are nearly always much more complex than those of the shareholders of public companies, who expect no more than dividends and capital gains. Nor are they always and exclusively of an economic nature.
9. As a result of the reform of company law, the traditional system of a board of directors or single chief executive is now flanked by the "dualistic" and "monistic" systems. Under the dualistic system (of German derivation), responsibility for management and control is assigned to a supervisory board, appointed by the general meeting, and a management board appointed directly by the supervisory board, which also approves the balance sheet. Under the monistic system (of Anglo-Saxon derivation), responsibilities for management and control are instead assigned respectively to the board of directors, appointed by the general meeting, and a committee for management control set up within the same, the members of which must possess particular requisites of independence and professional expertise.
10. Size is also a crucial variable. Structure and mechanisms of control differ greatly from the viewpoint of organisation theory and economic theory depending on whether the co-operative is small, medium or large.
11. There are even differences of opinion as regards the question of increasing the ratio of member workers to non-member workers or the need to accelerate decision-making processes. The debate on governance is also open, however, with respect to non-co-operative firms.
12. The problem of the effective nature of members' rights also exists, however, in associations, trade unions and political parties.

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Leadership: a moral and ethical perspective

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Abstract

The two traditional styles of leadership most often referenced are the transactional and the transformational. In this paper, we approach leadership from a moral and ethical perspective. This paper focuses on the moral compass inside every leader, which enables him or her to engage in meaningful, authentic moral dialogue and discernment with their organization, while remaining anchored in his or her unique moral beliefs (Thompson, 2004). The leader's moral compass enables him or her to guide the organization and his or her followers in an ethical and moral direction. According to Bill George, author of the Authentic Leadership (2005), leaders are those who are committed to a purpose or a mission, so they live by their values and know the true direction of their moral compass. Effective leaders utilize an internal set of morals and principles to navigate the often-treacherous waters of business and set a course for success before making a decision (Covey, 2000). According to various researchers through the practice of these virtues, leaders acquire the inner-directed and habitual strength of mind that will incorporate a strong moral compass and moral principles in their behavior. In today's business climate, which is still reeling from some of most highly publicized cases of corporate fraud, the moral direction provided by leaders is essential for long-term success of an organization (MacRae, 2002). Although the qualities of moral leadership may be defined differently by various researchers, it is thought that the development of one's moral compass begins in childhood, where parents introduce youngsters to the principles of right and wrong actions as well as the concepts of fairness, decency, and compassion (Amen, 2004). Many of the recent corporate ethics scandals have been committed by graduates of some of the most prestigious business schools. This has led schools to place increasing emphasis on ethics education. For some institutions, this has meant the introduction of stand-alone classes in ethics, while other institutions have sought to infuse ethics into various business courses. "Real leadership requires years of development and hard work" (George, 2006). Although this process may well begin in childhood, higher education institutions and leadership development programs can play a vital role in developing ethical and moral leaders.

Key words

Moral and Ethical Leadership, Moral Compass, Ethical Leadership Development

Introduction

Leadership is described as having many manifestations. The two most commonly discussed styles are the transactional and the transformational. The transactional leader focuses on the efficiency of his or her management style and is more tactical in nature with an emphasis on immediate problem solving. On the other hand, the transformational leader has a holistic understanding of his or her position and influence characterized by a strategic outlook as well as a vision that inspires his or her followers. The most recent studies on leadership suggest a third style known as laissez-faire leadership. This leadership style encompasses characteristics that focus on administrative effectiveness and self-directed management with a hands-off approach (Tatum, Eberlin, Kottrava & Bradberry, 2003).

Leadership is a multifaceted field with different issues depending on the perspective from which it is addressed. In this paper, leadership is addressed from its moral and ethical perspective. This paper focuses on the interior of every leader – the moral tenets that the leader uses to guide followers as well as the assumptions he or she makes in formulating decisions. The authors utilize Thompson's (2004) belief, which states that every effective leader is guided by internal moral solidarity, which is referred to as a moral compass. As Thompson (2004) further elaborates, the moral compass is one of the leader's virtues, qualities, roles, and approaches for creating moral solidarity for his or her followers. The moral compass inside every leader enables him or her to engage in meaningful, authentic moral dialogue and discernment with their organization, while remaining anchored in his or her unique moral beliefs (Thompson, 2004).

This paper provides an introduction to several basic concepts that are necessary as a starting point in understanding leadership concepts, principles, and styles. Following these basic concepts, it will also provide an overview of the leader in utilizing their moral compass in the proper guidance of their followers to achieve mutual goals. Lastly, this paper will explore the development of ethical and moral leaders.

Definition of leadership

As Paglis and Greene (2002) explain, there are numerous definitions of leadership. Some view leadership as a course of action in which the leader determines where the organization is at present, where it needs to go in the future, and then devises a strategy to achieve this goal. Leadership is also seen as the process in which an organization's goal is identified, a strategy is developed to attain the goal, and group members or followers are directed and encouraged in efforts toward achieving the goal. Furthermore, leadership is also managing change by establishing influence over followers, encouraging followers to concentrate their efforts on achieving changes in the objectives, and leading followers in facing the challenges to attaining the desired change.

In addition, Kakabadse (2000) points out that some scholars view leadership from a behavioral and personal perspective. Accordingly, leadership is seen as the personal relationship between the leader and the followers toward working for a shared goal. Others view leadership as aspects of behavior, whether positive in nature and under the control of the leader, or reactive as a result of multiple external forces.

Regardless of the various definitions of leadership, they all agree on the leaders preoccupation with strategic and relational goals and with the profound influence leaders have on the organization. The degree of emphasis and the manner of achieving followers acceptance, co-operation and commitment remains problematic in terms of leadership style and organizational resources and purpose.

Leadership styles

Tatum, Everlin, Kottrava, and Bradberry (2003) discuss the three most common styles of leadership. According to Tatum et al., scholars have viewed leadership styles as transformational or transactional, and recent research suggests a third style: laissez-faire. Tatum et al. describe transformational leaders as having a vision of the future, and by relying on their magnetism, they motivate their followers to strive toward reaching their shared goal. Transactional leaders are tactical in their management approach concentrating on short-term goals with a compensatory reward system for their followers. Laissez-faire leaders are seen as slow to react, often distant and characterized by their "passive-avoidant" and "management by exception" style of leadership.

Despite leadership having many definitions and styles, as described above, the authors believe for leaders to be truly successful it is their moral and ethical framework that guides them in properly leading their organizations. Below we point to a growing body of literature that recognizes the importance of underpinning leadership with a strong ethical or moral compass.

Moral compass

The leader's moral compass enables him or her to guide the organization and his or her followers in an ethical and moral direction. According to Bill George, author of Authentic Leadership (2005), leaders are those who are committed to a purpose or a mission, so they live by their values and know the true direction of their moral compass. Moreover, a true and effective leader has a behavior consisting of an influence process that is consistent with ethical and moral values (Mendoca, 2001).

Research has shown that during the decision-making process leaders utilize three types of assumptions: assumptions about themselves, assumptions about others, and assumptions about the world. The accuracy of these assumptions is determined by the leader's moral compass (Wilson, 1996). Acting as the moral compass of an organization, the leader can navigate the intricacies of situations and uncover the information that may not be readily apparent. For every organization, its leader's moral compass will be at the root of the organization's effectiveness, efficiency, cohesion, and acceptability to society. Therefore, leaders determine the direction for their organizations, making themselves the moral compass for the group. They set the course that others follow and this direction must be a combination of strategic thinking and moral sense. A leader employs his or her inner compass to sense when a change of direction is needed or to keep the organization on the path to its shared goals (Wilson, 1996).

Pardoni (2004) cites examples where leaders did not follow their moral compass thereby proving themselves ineffective in guiding their organizations to a proper destination.

A superintendent in Maryland accepts a top honor and a $25,000 cash prize in a national recognition program from a textbook vendor. The award is only offered because the vendor is doing millions of dollars worth of business with the superintendent's school district. Before accepting this reward, the superintendent made assumptions about himself and his personal benefit gained from the award. He obviously did not make the correct assumptions about the feelings of his peers, followers, supervisors, and the

Department of Education because his decision was harshly criticized by the media and by other school districts.

School board members in an Indiana district spent $4,400 of the money earmarked for public relations on an engraved Rolex watch for the district's retiring superintendent. By the superintendent accepting this gift, the entire school district was scrutinized by the media and other school districts.

Martha Stewart's (Pardini, 2004) lying about her personal stock sale is another example of a weak moral compass. Martha Stewart assumed that her personal interest in avoiding jail time would be satisfied by lying to the courts. However, she failed to consider the consequences if she was caught and the public's view of her actions.

These leaders acted without regard for their own moral compass. They made improper assumptions that impacted themselves, their followers, and their organizations in a negative manner.

Moral development and outcomes

Contrary to the above leaders, effective leaders are those who utilize an internal set of morals and principles to navigate the often-treacherous waters of business and set a course for success before making a decision (Covey, 2000). For effective leadership to be defined as leadership exercised for the benefit of the followers, not the enrichment of the leaders (Mackay, 2004) there clearly needs to be a highly developed sense of a morality which values followers as intrinsically (important in their own right) important rather than just instrumentally important for the organization. Leaders are responsible for the organization's moral climate that, in effect, reflects the moral development of the leader and of the followers.

Thompson (2004) views the moral compass as the impermeable boundary between the leader's individual morals and the morals of the culture. This viewpoint acknowledges that leaders have some level of choice in how their culture will morally define them and how strong a role they will assume in reinforcing the morality of their culture. A moral compass enables a leader to engage in meaningful, authentic moral dialogue and discernment while remaining anchored in his or her unique moral traditions The leader's personal moral development results from character formation through the practice of virtue in private as well as in public life. Ethical leadership manifests itself in three dimensions: a) the leader's motives, b) the leader's influence strategies, and c) the leader's character formation. Stated differently, the leader's motives and influence strategies are the foundation of the leader's character. In line with the above-mentioned three dimensions, the U.S. Military Academy, an institution dedicated to developing moral leaders, offers the following principles as a guideline to its students in maintaining a moral compass:

- Understand yourself and strive for self-improvement.
- Develop tactical and technical proficiency.
- Assume responsibility and be responsible for your actions.
- Formulate timely and well-grounded decisions.
- Be a role model.
- Know your employees and monitor their welfare.
- Maintain communications with your employees.
- Be responsible for your employees.
- Ensure employees understand their assignments.
- Train your employees to function as a team.
- Utilize your team to its highest capabilities.
- Establish priorities.
- Take the initiative (Mackay, 2004)

Through the use of morally appropriate influence, as well as strategies and tactics that are motivated and guided by moral intent, leaders can facilitate the growth of their own moral compass. Leaders set the tone for the moral caliber of their followers, and by their moral behavior, leaders can strengthen or corrode the moral fiber of their organizations. "A study of Fortune 500 Industrial and Fortune 500 Service companies indicates that an organization's top managers and their ethical commitment guide how a firm's programs are implemented" (Mendoca, 2001).

For example, the leaders of Enron Corporation. had a well-developed code of ethics. Nevertheless, it was the leaders who guided the organization to fraud and embezzlement, due to their weak moral compasses and failure to make the right assumptions. The company's code of ethics was certainly not enough to guide the leader's moral compasses and that of the organization as a whole.

Contrary to the Enron situation, effective leadership concerns itself with high moral ground such as Gandhi's civil disobedience movement, Martin Luther King's civil rights campaign, and Mandela's fight to end apartheid. These movements and their leaders' determination exhibit a high moral outlook with a determination to achieve their goals and a constant renewal of their commitment to succeed (Safty, 2003).

Virtuous moral leadership

In the process of creating leaders, part of their moral compass consists of three virtues: hope, trust, and civility (Sergiovanni, 2005). The virtues, as they apply to moral compass can be explained as follows:

HOPE – As previously mentioned, one part of a leader's role is making assumptions as a component of the decision making process. Hope plays a large role in the assumptions that are made by the leader. Combined with hope is the concept of faith, which implies the leader's commitment to his or her moral compass as well as the moral culture of his or her organization.

TRUST – Leaders must establish a culture of trust in their organization, so that the followers believe in the path on which their leader is taking them to reach their common goals.

CIVILITY – This virtue builds frameworks within the leaders and their followers that enable a common bond to be developed between their divergent views and interests. Civility draws leaders outward to embrace differences and to look upon society as a whole and see where their specific organization can fit in and assist in the betterment of the world in which they prosper. Civility is at the heart of building communities that bond people together, while creating bridges that connect them to other people and views by using their moral compass to guide the leaders and their organizations to a better future.

According to Sergiovanni (2005), all of the above stated virtues develop a part of the leader's moral compass. Mendoca (2001) on the other hand, presents four different virtues that are necessary in developing the moral compass of the leader:

PRUDENCE – A prudent leader willingly accepts divergent stakeholder views as a source for new information, which may contribute to making better assessments and decisions.

JUSTICE – A leader with a strong sense of justice seeks to give credit to others, which includes supporting others in exercising their rights and fulfilling their duties. The judicious leader considers the rights of all stakeholders and strives to achieve a balanced and fair approach in fulfilling his or her fiduciary responsibility.

FORTITUDE – A leader with fortitude has the courage to face risks and challenging situations; strives to overcome obstacles and act in a noble manner. Perseverance in the face of great challenges is an underlying quality of fortitude.

TEMPERANCE – A leader who exhibits temperance sees the differences between self-indulgence and necessity. Through self-control, the leader avoids self-indulgence, and effectively allocates resources, effort, and time.

According to various researchers through the practice of these virtues, leaders acquire the inner-directed and habitual strength of mind that will incorporate a strong moral compass and moral principles in their behavior and thereby form their character. A different viewpoint shown by a third researcher in this field, Sample (2002), provides seven "timeless" principles of leadership, which inevitably build the moral compass as well:

1. Leaders understand that casualties are unavoidable. The idea that there can always be a "win-win" proposition is simply untrue. Many of the best leaders succeed by establishing a moral line that they will not cross, while using a finely honed moral calculus to evaluate situations and set strategic direction of their organizations.
2. Leaders inspire followers to make a real commitment, often energizing people to take actions that are contrary to their natural inclinations.
3. Leaders need vision, but vision alone is not enough to overcome obstacles. Despite a strong vision, for leaders to be effective they cannot be overwhelmed in the face of challenges.
4. Leaders view issues from new perspectives, form innovative connections, and see solutions that others do not see. Unlike vision, perspective enables leaders to accept sound suggestions from followers that will prove to be beneficial to the overall success of the organization.
5. Leaders need laser-like internal instincts to keep them from stubbornly fostering an agenda not yet accepted by their followers. Nevertheless, this laser-like instinct will also ensure that as a leader they are not misdirected by the whimsical ideas of their followers.
6. Leaders see the many shades of gray in situations. Rather than categorizing life in rigid or absolute terms, effective leaders see the subtleties and take the time to consider all the facts in situations, prior to making a decision.

7. Leaders manage the un-pleasantries of leadership; they do not defer the difficult challenges confronting their organizations. It is through their ability to confront the tough issues that leaders can gain credibility in the eyes of their followers (Sample, 2002).

Development of ethical leaders

Although the qualities that comprise moral leadership may be defined differently by various researchers, it is widely believed that the development of one's moral compass begins in the home during childhood, where parents introduce youngsters to the principles of right and wrong actions as well as the concepts of fairness, decency, and compassion (Amen, 2004). As guidelines for the development of a moral compass in children Amen (2004) recommends: a) build a bond that will encourage your youngster to share your values, b) set an example by living the ethics that you preach, c) encourage discussions when sensitive issues and learning opportunities arise, and d) establish a set of written commandants to live by. Although these guidelines were intended for use by parents in the moral development of children, they would appear also to be sound principles for use by higher education institutions and corporate leadership development programs, as they seek to develop ethical leaders.

> *"While some believe that ethics is better left to or primarily determined by family and religious upbringing, the complexity of business ethics in our society necessitates a continuous learning approach" (McAlister, 2004, p. 55).*

However, one seeks to approach the development of ethics in leaders, there is a clear need to improve the ethical development of leaders. The recent popularity of "boot camp" style leadership development programs, such as Outward Bound and other physically oriented group experiences, can be counter productive to the development of ethical and moral leaders (Center for Creative Leadership, 1999). Physical group activities, which often include military type missions, may teach teamwork but they also appear to foster the belief that leadership is a win-lose situation, where it is "us" against the enemy. A leadership development program of this nature does not engender a sense of respect, compassion, and understanding for one's opponents, and it does little to promote the desire to explore alternative solutions.

In contrast to the "boot camp" style of leadership training, there are programs such as the Center for Creative Leadership's Looking Glass Company Simulation (1999). In this six-hour simulation, leadership training participants take on various roles and face an array of business challenges. The participants are encouraged to listen, understand others' concerns, voice their own concerns, and work with others to reach consensus-based agreements.

Many of the principals in the recent corporate ethics scandals have been graduates of prestigious business schools; this has led higher education institutions to place an increasing emphasis on ethics education. For some institutions, this has meant the introduction of stand-alone classes in ethics, while other business schools have sought to infuse ethics into all aspects of their business courses. Researcher Carroll (2005) conducted a study of undergraduate business school students as part of an effort to determine the best approaches to teaching ethics in the classroom. A survey of students found professor-directed lectures, case studies, and discussions to be the tools most valued by students in helping them to develop ethical leadership skills. It is also interesting to note that students listed their ethics courses as second only to their management courses in importance to them.

Another approach to teaching ethics in higher education was employed by Eller College of Management (BizEd, 2005). A survey at Eller indicated that 63% of the business school students admitted to cheating in the past year. Eller decided that to change the ethics of its students, it would need to revise the ethical culture of its own organization. Their multi-dimensional approach, which they labeled "e-tegrity" includes a student ethics oath, student honor board, e-tegrity Web site, installation of plagiarism-detecting software, and an annual ethics competition. Whatever approaches an institution employs, future business leaders need to gain skills that will help them to identify ethical issues, understand ethical standards in business, and develop the moral courage to make what are often difficult ethical decisions.

Conclusions

In today's business climate, which is still reeling from some of the most highly publicized cases of corporate fraud, the moral direction provided by leaders is essential for the long-term success of an organization (MacRae, 2002). Leaders must follow their inner moral compass and set an example of ethical leadership for their organizations. "Real leadership requires years of development and hard work" (George, 2006). Although this process may well begin in childhood, higher education institutions and leadership development programs can play a vital role in developing the moral compass of future leaders.

Further research into effective methods for developing ethical leaders is clearly merited.

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Dynamics and Tensions in Governance: evidence from Finnish co-operatives*

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Abstract

Questions related to corporate governance have become an integral part of management and organization studies. As the concept entails, the literature on corporate governance centres on the management and control of joint stock companies or corporations while other forms of economic organization have received less scholarly attention. Against this background, co-operatives offer a timely and relevant empirical context for studying governance. In this paper, we propose a framework for analyzing co-operative governance, and illustrate the dynamics and tensions involved with in-depth evidence from Finnish customer owned co-operatives. We outline problematic related to social construction of ownership and governance in organizations with multiple stakeholders and a dispersed pool of member-owners.

Key words

Co-operatives, Governance, Ownership.

Introduction

In recent decades, corporate governance has attracted extensive research in the field of organizations and management. Research on corporate governance has usually focused on the control of executive self-interest and the protection of shareholder interests in settings where ownership and control are separated. The emphasis has been on the efficacy of the various mechanisms available to protect shareholders from the self-interested actions of executives (e.g., Shleifer & Vishny, 1997).

Recently, the conceptualization of corporate governance has evolved in unprecedented ways. Daily, Dalton, & Cannella (2003:371) define corporate governance as "the determination of broad uses to which organizational resources will be deployed", including "the resolution of conflicts among the myriad participants in organizations". This definition goes beyond the popular agency theory (e.g., Fama & Jensen, 1983) and employs, for example, resource dependency theory, stewardship theory, and power theory perspectives on governance.

Forms of economic organization that deviate from the joint stock company have also received scholarly attention. Ownership structure has been identified as an important determinant of corporate governance and business behaviour, and one of the studied alternative forms has been the co-operative organization in which ownership is often dispersed (e.g., Shleifer & Vishny, 1997; Pedersen, & Thomsen, 1997). Crucially, the various forms that governance takes in different legal and cultural contexts have also been specified. Aguilera and Jackson (2003) note that there are institutional factors that shape how actors' interests are socially constructed (e.g., Berger & Luckmann, 1966; Durkheim, 1938/1894). Pedersen and Thomsen (2000), for example, propose that the identity of owners is an important determinant in corporate governance, as it has implications for objectives and uses of power.

While some institutional factors and formal aspects of ownership have been recently considered in research on corporate governance, an institutional perspective on organization and other dimensions of ownership have received less attention. Daily et al's. (2003) definition of organization in corporate governance comes close to this perspective, which is concerned with questions related to internal organizational dynamics determined by the institutional environment or organizational field (cf. Greenwood & Hinings, 1996). In recent decades, management scholars have also considered various dimensions of ownership (Tannenbaum, 1983; Pierce, Kostova, & Dirks, 2001; Rousseau & Shperling, 2003). These contribute to our understanding of organizational behaviour and organizational members' expected rights and responsibilities, which, again, relates to new definitions of corporate governance (Aoki, 2000; Aguilera & Jackson, 2003).

In this paper, we focus on the dynamics of governance in a co-operative context. We highlight the various aspects of ownership to understand how governance in co-operative organizations evolves in time. We offer data from Finnish co-operatives where ownership is highly dispersed at local level but relatively centralized at group level. We follow Daily et al. (2003), Pedersen & Thomsen (1999), Pierce et al. (2001), and Greenwood & Hinings (1996) in identifying particular elements of governance and ownership to sort out our evidence as we seek to understand how actors perceive the elements to have intertwined in time to produce particular organizational outcomes. In this way, we attempt to shed new light on tensions in co-operative governance.

Corporate governance

The foci of interest in corporate governance is the arrangement where diversifying stock owners hire boards of directors, who in turn, hire managers to conduct, or monitor, the day-to-day activities in the firm in which the owner has financial interest (Walsh & Seward, 1990). Agency theory has been the dominant perspective in corporate governance research (e.g., Dalton, Daily, Certo, & Roengpitya, 2003; Shleifer & Vishny, 1997) as it has been found appropriate for conceptualizing the controlling and monitoring role of directors and board members (Daily et al. 2003). The foundational idea in the agency theory perspective on governance is that without control, managers are more likely to deviate from interests of shareholders (Fama & Jensen, 1983). Hence, the term corporate governance refers to the integrated set of internal and external controls that harmonize agency conflicts of interest resulting from the separation of ownership and control (Baysinger & Hoskisson, 1990; Williamson, 1984).

The role of board members in corporate governance has been a widely discussed topic (e.g., Johnson, Daily, & Ellstrand, 1996; Baysinger & Hoskisson, 1990; Williamson, 1984). Agency theorists argue that the board, with its legal authority to hire, fire, and compensate top management, safeguards invested capital and, in consequence, occupy an important role in corporate governance (Williamson, 1984). Astute or opportunistic CEOs may influence the inclinations of the board, and thus set the premises for the board's deliberations and decisions (Baysinger & Hoskisson, 1990). In addition to the control and monitoring role, directors and board members also occupy service and resource dependence roles (see e.g., Zahra and Pearce 1989 for a review of board roles). However, to explain these roles theoretical perspectives beyond agency theory are necessary (Johnson et al., 1996).

Resource dependence theory provides a theoretical foundation for directors' resource role (Daily et al. 2003). This perspective addresses contributions of board members as boundary spanners of the organization and its environment (Johnson et al., 1996; Zahra & Pearce, 1989). The appointment of representatives of interdependent organizations in boards provides access to essential resources and secures those resources through linkages to the external environment (cf. Hillman, Cannella, & Paetzold, 2000; Pfeffer & Salancik, 1978). For example, "outsiders" who are members of other institutions can provide advice in specific topics, either in board meetings or in private communication with firm executives that may otherwise be more costly for the firm to secure. Daily et al. (2003) conclude that the provision of these resources enhances organizational functioning, firm performance, success and survival.

There are also theoretical approaches to governance that have their roots in sociology and psychology. The stewardship theory, which provides a theoretical foundation for understanding the directors' service role, defines situations in which managers are not motivated by individual goals, but rather are "stewards" whose motives are aligned with the objectives of their principals. The foundational idea of this perspective is that stewards will not substitute or trade self-serving behaviours for co-operative behaviours (Daily et al. 2003; Davis, Schoorman, & Donaldson, 1997). However, the stewardship perspective does not adopt a view of executives and directors as altruistic. As Lane, Cannella, and Lubatkin (1998) point out, stewardship theorists simply recognize that there are many situations in which executives conclude that serving principals' interests also serves their own. Davis et al. (1997) maintain that placing higher value on co-operation than defection – and behaving accordingly – can be considered rational. Also, managerial efficiency and reputation are often found interwoven with the performance of the firm (Baysinger & Hoskisson, 1990). Hence, in order to protect their reputation as expert decision makers, executives and directors are inclined to behave in a manner that would maximize financial performance indicators, including shareholder returns (Daily et al. 2003).

Researchers have also applied a power perspective to corporate governance. The power relationship between the CEOs and board of directors has been of particular interest, for example, to Finkelstein & D'Aveni (1994) and Daily et al. (2003). Although the board has formal power over management, in fact, it is the CEO that often dominates the board. This is suggested to be a consequence of the board member selection, over which CEOs may have determining influence (Mizruchi, 1983). The timing of a director's appointment to the board may also have impact on the power relationship between the CEO and board members, because members appointed during the tenure of the current CEO may feel beholden to him and may be less likely to challenge him (Wade, O'Reilly, & Chandratat, 1990).

Governance of co-operatives

Co-operatives are owned by their members. In principle, they are democratically governed economic organizations in the vein of "one-man-one-vote". Membership includes equal share of ownership and voice in governance. In principle, a co-operative is open for all who wish to benefit from its services. This foundational principle is grounded on stakeholder theory, which, according to Freeman, Wicks, & Parmar (2004:364), in its core declares that "economic value is created by people who voluntarily come together and co-operate to improve everyone's circumstance".

What distinguishes co-operative membership from corporate ownership is that the members are non-investors. They seek primarily other types of benefits from the firm than maximum value to their financial investment, which in co-operatives is typically relatively small (e.g., Skurnik & Vihriälä, 1999). It must, however, be born in mind that the significance of the differences between co-operative membership and corporate ownership may differ between societal (or cultural) contexts. Pedersen and Thomsen (1997) note that in European settings shareholders are traditionally considered to be one of a number of stakeholder groups and corporate goals may at times be inconsistent with shareholder wealth maximization. There are also certain features in the governance of co-operatives that may differ from corporations (Hansman, 1999). First, an important determinant of governance of co-operatives is the poor liquidity of ownership. According to Pedersen and Thomsen (1997), members of a co-operative, who cannot resell shares, are likely to oppose investment projects that stretch beyond their ownership period. Second, owners have less sources of information, such as the stock market, in the co-operative context (Hansman, 1999).

Further, some features of governance are accentuated in co-operatives. From a principal-agent perspective, for example, a large number of small owners are likely to face some difficulty in coordinating their efforts to exert control over management (Wade et al. 1990). Small owners may also have little incentive to monitor management behaviour (Daily et al. 2003). However, according to Hansman (1999), even large consumer co-operatives in which ownership is highly dispersed and a strong separation between ownership and control is exhibited are commonly more closely controlled by their members than are investor owned firms. In general, the need for close control can be understood as one of the reasons why co-operatives, unlike corporations, are likely to thrive only where such relationship is possible (Hansman, 1999). However, this may again vary between contexts. For example, members of Finnish co-operatives have been considered as rather passive owners (Tainio, 1999).

Finally, owners of corporations and co-operatives may have inherently different views of other stakeholders. This may have influence on how executives behave in relation to the stakeholders. Whereas capital markets discipline corporate executives who ignore shareholders in order to benefit other stakeholders (Holmstrom & Kaplan, 2001), co-operative owners may look approvingly at executives who are attentive to regional and local stakeholders' interests. This is due to the fact that "seats" on supervisory boards of co-operatives may in practice be reserved for representatives of particular local constituencies (Hansman, 1999; Tainio, 1999). Executives in co-operatives may also interact more with stakeholders such as customers and employees, while corporate top executives' work is more directed towards interaction with investors and their representatives. Through interaction, values, preferences and objectives of particular stakeholders may influence the goals and decisions of organizational actors (cf. Thomsen & Pedersen, 2000; Thomsen, 2004).

Dynamics, tensions and the question of ownership

Building on institutional theory (e.g., DiMaggio & Powell, 1983; Meyer & Rowan, 1977; Selznick, 1957), Greenwood and Hinings (1996) have conceptualized organizations as heterogeneous entities composed of functionally differentiated groups pursuing goals and promoting interests. For example, the way organizations "respond" to evolutionary and revolutionary change is considered a function of their internal dynamics. Evolutionary change is something that occurs gradually and relatively slowly (Pettigrew, 1985), whereas revolutionary change takes place swiftly and affects virtually all parts of the organization simultaneously (Tushman & Romanelli, 1985). As the various groups pursue their potentially conflicting goals and promote their interests they may also relate differently to organizational change.

Institutional theorists (e.g., Meyer et al., 1993; Zucker, 1983; Meyer & Rowan, 1977) argue that regularized organizational behaviours are the product of ideas, values, and beliefs that originate in the institutional context (i.e., intra-organizational dynamics are in interaction with contextual dynamics). To survive organizations must accommodate institutional expectations, even if they are apparently inconsistent with efficiency or efficient task performance expectations. In brief, organizational behaviours are in part products of both competitive and contextual institutional pressures (cf. Greenwood & Hinings, 1996).

In pursuit of understanding dynamics and tensions of ownership and governance in organizations, the concept of ownership needs to be broadened. From the traditional perspective, ownership is about the formal right to control the firm and appropriate the residual earnings. Thus, ownership and related rights are derived from the societal legal system (cf. Rousseau & Shperling, 2003; Grunebaum, 1987). However, there are aspects that go beyond the traditional view. Ownership norms are implicit in the minds, language, and behaviours of individuals. These culturally grounded perceptions of ownership may not totally coincide with explicit legalistic conceptions (Rudmin & Berry, 1987). Also the psychology of ownership (e.g., Heider, 1958) has emerged as a significant area of inquiry in understanding behaviours and attitudes of organizational actors in general (Pierce et al. 2001) and ownership-related decisions by individuals in particular (cf. Beggan & Brown, 1994).

On the individual level, ownership can in a psychological perspective be conceptualized as an association between an object and a person in the mind of a person (Heider, 1958), and organization (i.e., a physical, social, or cultural part of it) becomes a possible object of such association (cf. Jussila & Puumalainen, 2005; Pierce et al. 2001). Psychological ownership, that is, the individual or collective feeling that an object is “mine”, “ours” or “part of self” (e.g., Van Dyne & Pierce, 2004; Pierce & Rodgers, 2004) may under some conditions have effects that create tensions in organizations (cf. Dirks et al., 1996). For example, organizational members may want to retain exclusive control over a target or managers may resist interventions that empower others, because they feel a high degree of ownership toward (the management of) a particular unit (Pierce et al., 2001). Psychological ownership may also have influence on how organizational members orientate to organizational changes. Dirks et al. (1996) suggest that psychological ownership leads to positive or negative orientations toward change, contingent on the type of change involved. In general, the orientation is likely to be positive when the change is self-initiated, evolutionary or additive and the orientation is likely to be negative when the change is imposed, revolutionary, or subtractive.

On the interpersonal level, individual and collective perceptions of ownership and the rights and responsibilities associated with it are shaped and interpreted through social reality in each context (Dittmar, 1992; cf. Berger and Luckmann, 1966). “Organizational” perceptions of ownership may be shaped, for example, by manifestations of psychological ownership (e.g., This is MINE!). This means that subjectively perceived ownership may become part of social reality through language. In the eyes of a third party, also the presence of association between a person and an object may be sufficient enough to influence the perceived strength of ownership, and the perception of who has the right to use the target, benefit of it and to exercise control over it. Beggan and Brown (1994) note that in contexts where people lack a strong justification for decisions, they often use these kinds of cues.

In all, dynamics of governance seem to arise from both competitive and institutional pressures and various socially shared and argued perceptions of ownership. In co-operatives, these are often transferred to organizational decision making through the supervisory board, which occupies several roles in governance.

Context, data and method

A number of Finnish co-operative organizations have - to the apparent surprise of some experts - managed to maintain a relatively successful trajectory of performance throughout recent years (cf. Skurnik, 2005). Our focus is on the S Group (retail sector) and the Finnish OP Bank Group. Both organizations are owned by their customers and staff. At least in principle these co-operatives demonstrate a relatively decentralized mode of governance.

The S Group consists of 22 independent regional co-operative societies as well as a central organization SOK and its subsidiaries, owned by the regional co-ops. The 22 co-operatives, in turn, are owned by their members. In total, the co-operatives in the S Group have about 1,5 million customer owners (the total population of Finland is 5,2 million). Businesses in the S Group include food and groceries, specialty goods, hotels and restaurants, hardware and agriculture, automobiles, service stations, and welfare services. In its most important fields of business, food and groceries and specialty goods, the domestic market share of the group is around 36 percent (recent acquisition of SPAR Finland is not included). The group declares its purpose as to provide services and benefits for committed customer-owners. The central organization, which is owned by the 22 independently run and governed co-operatives, provides advice, support and service activities for regional societies. (www.s-kanava.net: accessed May 12th 2006)

The OP Bank Group consists of 236 independent banks (local and regional) and a statutory Central Co-operative. The co-operative banks are owned and governed by local members. In total, the local and regional co-operatives have about 1,1 million member owners. The business of the co-operative banks includes private, corporate and community banking. The domestic market share of the group is around 31 percent in savings and loans. Due to recent acquisition of Pohjola, OP Bank Group has also become a major player on the field of insurance. The central organization (OPK), which is owned by the local and regional banks, provides advice, technical support and banking services, including Central Bank (OKO) services for its owner banks. OPK also has statutory responsibility to supervise and control the banks. (www.op.fi: accessed May 12th 2006)

The qualitative data for our study includes company documents and archival material as well as in-depth interviews carried out in spring 2004. First, we interviewed a total of three Finnish experts on the concept of "co-operative organization"; definitions, history, present and future. Second, we analyzed an extensive amount of archival material on both the S Group and the OP Bank Group. This includes non-scientific published studies, periodicals for personnel from year 1970 to 2004 and annual reports. Third, we carried out a total of eleven in-depth interviews among elected executives, managers and supervisory board members both in regional co-operatives and at the headquarters in both organizations. In these interviews, we used the "snow-balling" principle (e.g., Greenwood, Suddaby, & Hinings, 2002) where new interviewees were selected based on earlier interviewees' recommendations. In sum, we have relied on triangulation of qualitative data in our study (cf. Alasuutari, 1995).

The data was first studied systematically to gain understanding of the research context and to form a preliminary understanding of corporate governance in co-operatives. Next, the data was organized by themes, and analyzed in detail by the corresponding author and one of the co-authors. Much of the literature we build on in this study is psychology-based and quantitative, and implies correlations among "variables". However, in this paper, our intention is not to look for psychological mechanisms or study psychological reality of individual organizational actors. Rather, we interpret how organizational actors talk about elements of ownership, governance, and institutional factors and provide accounts of how these have intertwined in time to produce particular organizational outcomes. These accounts are triangulated with our extensive archival material to gain in-depth understanding on the topic. In this way, we are also able to provide a rich description of different versions of social reality related to the phenomenon we are focused on.

Evidence from Finnish co-operatives

Co-operative ownership is usually dispersed. This is well illustrated by the fact that Finnish local or regional co-operative societies may have thousands or tens of thousands of owners. Ownership is, however, more centralized at Group level in our case organizations as the central units are owned by 22 co-operatives in the S Group and 236 co-operatives in the OP Bank Group.

In their accounts, the experts interviewed seemed to be consistent with academic reflections on the topic of co-operative ownership (e.g., Tainio, 1999; Skurnik & Vihriälä, 1999), which is perceived to differ from corporate ownership not only in the amount of investment but also by a more intimate relationship to the target of ownership. They also referred to feelings of ownership, when speaking of the differences between co-operative and corporate ownership:

> *"Corporate ownership is purely about investment that is expected to result in an increase of value… co-operative ownership is about a feeling of ownership for the organization along with possibilities to influence. It's also about the role of the co-operative developing your community… it feels more intimate."*

Ownership and customership are interwoven in customer-owned co-operatives (where, for example, an employee may simultaneously be a customer and owner). This means that whereas corporate owners are investors that aim to benefit from increase in the value of their shares, co-operative owners are non-investors that get their benefits by active participation as customers. That is, the return of surplus is bound to the use of services provided by the co-operative. As a retired regional co-operative executive put it:

> *"In co-operatives, the members get the benefits of ownership by being active customers of their co-operatives. I am a master concentrator myself (laughter); I always see to it that my family uses co-operative products and services whenever possible. This way we can get the best possible value of co-operative ownership as a household"*

Although the increase of share value is not considered a significant goal of co-operative activity, some executives of regional S Group co-operatives spoke for increasing the return of surplus to members. Some executives of Co-operative Banks viewed the wealth and welfare of members as the ultimate mission of co-operative banking:

> *"I define ownership and the mission of co-operative banks as to help members gain wealth and succeed… customers must have a feeling that they succeed with the help of the co-operative bank, that is, by using the services it provides."*

While benefits for members, through providing locally consumed services, were presented as the primary goal of co-operatives, also other stakeholders were considered important. Some aims of co-operative activity in business were pointed out to lie on the societal and regional level. For example, co-operatives, as an alternative to international firms with investor owners, were considered to play an important role as defenders of national, regional, and local ownership in general. As the following representations illustrate:

> *"The locally 'own' co-operative bank is more than just a profit maximization organization; it is an institution that holds together the local community"*

> *"In certain areas independence has been highly valued; holding on to 'own' organizations [co-operative banks] has been considered extremely important"*

> *"I believe that in relation to the global world the locality of Co-operative Bank is considered important in nationalistic perspective"*

The nationalistic element in co-operative business is noteworthy (cf. Skurnik, 2005); as co-operative ownership is locally based and controlled. In our data, the regional and local dimensions complicate this notion as co-operatives are also presented to participate in developing the regions and towns they are located in, and providing it economic and financial support.

The term "owner" was not actively used in Finnish co-operatives before the late 1980s. This term was introduced alongside "member" in the co-operatives studied through terms such as "customer owner" (S Group) and "owner member" (OP Bank Group) during the late 1980s and early 1990s. Around the same time, scholars and practitioners of co-operative organization began to debate the development of ownership and governance in Finnish co-operatives. Our interviewees' accounts of co-operative members' activity as owners are in line with academic work, according to which Finnish owners were considered passive (Tainio, 1999). However, ownership and governance were also argued to have revived as an outcome of recent public debate in Finland (cf. Skurnik, 2005).

Whereas in corporations the shareholders may have different voting rights and, thus, voice in governance, in co-operatives each owner has an equal share (and one vote) that cannot be resold. In the accounts of our interviewees, this principally democratic system is valued although it is occasionally criticized:

> *"If there are 30000 members and you are one of them, you have no opportunities whatsoever to control the co-operative."*

Beggan and Brown (1994) imply that when legal ownership is a minor determinant, other dimensions of ownership come to play a major role in decision making. In our interviewees' accounts, the voice of individual owners in governing consumer co-operatives is restricted. The owners' direct interaction and social influence were suggested to be significant in justifying decisions, concerning both operational and strategic issues.

Whereas in corporate context the stock market is considered a significant source of information and mechanism of governance (Pedersen & Thomsen, 1997), co-operative organizations lack such a mechanism (cf. Skurnik, 2005). However, the market is considered to control consumer co-operatives as well. In co-operative context, this refers to owners' behaviour as consumers. Owners are represented in the governance of co-operatives as members of representative bodies and supervisory boards and, at times, on the boards. Such choices are outcomes of democratic process. First, owners elect members to representative bodies, which assemble the supervisory board, which, in turn, selects individual board members. In our interviews, the objective of this system is presented as threefold: 1) it is considered democratic, 2) it is perceived to contribute to the coherence of the co-operative by equal voice, and 3) it is viewed to create stability. Due to the system, hostile takeovers are not possible in co-operatives.

Daily et al. (2003) discuss four different perspectives on board roles in governance: agency, resource dependency, steward and power. In the context of our study, all governing organs of owners may take such roles: the representatives, the supervisory board and the board. In the agency perspective (Williamson, 1984), the role of the board is to safeguard invested capital. In the co-operative context, too, the significance of this role is crucial. In the accounts of our interviewees, some (former) executives of co-operatives were described as opportunistic and astute (cf. Baysinger and Hoskisson, 1990). Some major failures were described, and some explanations were provided. For example, during 1980s some regional Co-operative Bank executives took unbearable risks to seek high profits and to pursue "personal ambitions". The governance system in the bank group was ineffective and lacked necessary control mechanisms. The boards were often doomed to fail due to their incompetence and lack of accurate knowledge of the field during a time when institutional pressures dramatically transformed the business environment.

In Johnson et al. (1996), board roles have been considered from the resource dependency perspective. This addresses board members' contributions as boundary spanners of the organization and its environment. Our interviewees emphasized the role of the supervisory board in this role. Many perceived board members to be a great asset in achieving strategically important knowledge from different businesses and fields. This was presented to be an outcome of the composition of the board as the supervisory board often comprises of virtually all major stakeholders of each region. For example, in S Group co-operatives board members often hold significant positions in the private or public sectors. In the S Group, the interviewees gave a number of examples of situations where individuals involved in local and regional politics attempt to lobby for the co-operative over its competitors. However, in addition to major stakeholders, also laymen may play an active role in co-operative governing organs. This means that local or regional resources are widely employed. A top manager in an S Group co-operative maintained:

> *"The role of all members in all governing organs has been emphasized to make them monitor the environment, to 'act like radar', so to speak. They have also been brought to the strategy work of our organization"*

According to the stewardship theory perspective, there is no agency conflict when managers' and owners' interests are aligned (Daily et al. 2003). This alignment is perceived to be a significant characteristic of many Finnish co-operatives. At least two issues account for this. First, the salary of many CEOs of regional co-operatives is bound to firm performance. Second, in the stakeholders' view, co-operative CEOs have become highly respected due to their track record. The interest of the CEOs is to maintain such a reputation, which leads to behaviours in line with owners interests. Trust and a long term perspective on business may be created in this way. For example, in the S Group, regional CEOs are monitored by owners and other stakeholders. Their managerial efficiency and competence is judged by in-group measures that are considered to be in line with the owners' interests.

In the power perspective, CEOs are often considered to dominate the board although it has formal power over the CEO (Daily et al. 2003). In co-operatives this is reflected in retiring CEOs' traditional major role in appointing their successors and, at times, even board members (cf. Miruchi, 1983). However, CEOs are, in practice, hired and fired by supervisory boards. If the business runs successfully, "that is all they have to do", as one of our interviewees put it. When the performance deteriorates, the CEOs power wavers.

As the discussion above entails, several sources of tensions are built in the governance of co-operatives. Greenwood and Hinings (1996) conceptualize organizations as heterogeneous entities composed of functionally differentiated groups pursuing particular goals and promoting interests. A constant tension between the goals and interests of individual regional co-operatives and the group level is a crucial characteristic of our case organizations:

> *"Because the OP Bank Group consists of several independent business units, that is, the co-operative banks, implementation of group level strategy to all banks has been challenging, to say the least."*

> *"From whose perspective should we look at maximization of firm value - the owners, customers, employees, other stakeholders or some other interest groups? Each interest group aims to maximize value from their perspective…"*

Thus, it seems that tensions in consumer co-operative groups can be derived from the organization structure, which reflects the different interests of stakeholders. Regional and local contextual dynamics seem to create tensions in the group level. For example, some influential individuals or groups may consider their own mission more important than group level goals. Different owner identities have been emphasized (cf. Thomsen, 2004) as basis for group level tensions. In the co-operatives studied, each regional co-operative has its own values and missions that may, in fact, be somewhat inconsistent with other co-operatives in the group. Some of our interviewees discussed gradual restructuring in the organization and the possibility of mergers between regional co-operatives due to competitive and institutional pressures:

"The municipality structure is creaking; consolidations of municipalities occur all the time and co-operation is needed… how quickly do co-operatives follow these changes?"

"Each region has its own values and beliefs and their own dialect. There is no point in merging organizations if regional identities are mixed. As you know, for example, people here are very different from the people in the neighbouring region"

"When you think of a situation in which executives and strategic decision making are located at the headquarters in Helsinki and the business is located approximately 500km away [name of the place removed], there is no way for people at the headquarters to understand the way customers think or what they expect."

These kinds of comments are significant as they pinpoint local and regional identities as a crucial feature in the governance of co-operative organizations. Above, we discussed co-operatives as a significant alternative to international firms with investor owners. The challenge in co-operatives is, however, to coordinate local and regional interests and preferences and to meet them competitively at the national level.

Our interviewees discussed several kinds of institutional pressures related to group level strategies and negotiating organizational structure. In line with Pedersen and Thomsen (1997), the governing organs of local and regional co-operatives were presented to be likely to oppose investments that stretch beyond the perceived time horizon of the members' ownership. In brief, local and regional organizations of the OP Bank Group were thought to be more likely to accommodate contextual institutional expectations than to react to competitive pressures or to be consistent with group level expectations for efficiency. Some interviewees seemed to perceive that, for example, reluctance to merge with other co-operatives could be explained by stakeholders' feelings of shared ownership for their co-operative (cf. Van dyne & Pierce, 2004; Pierce et al. 2001):

"As we did not begin to merge the [S Group] co-operatives early enough, what happened was that members, the owners of the co-operative, began to defend their own, the co-operative, vigorously and to say that they'll manage. They fought for their little co-operative until all the money was gone and a merger was the only option."

"In many locations, the societal change has led to a situation where the local co-operative bank is for the local citizens the only thing that is truly theirs. When the group tries to negotiate mergers, the owners' representatives in the governing body make their ownership explicit by saying: 'This is our co-operative, we make our own decisions and nobody will tell us how to run this bank'."

In Pierce et al.'s (2001) theory of psychological ownership in organizations, feelings of ownership are proposed to lead to resistance to change, when the change is imposed, revolutionary, or subtractive. Dirks et al. (1996) suggest that individuals orientate negatively toward imposed change on the target of their ownership. Accounts by our interviewees seem to be consistent with these claims.

In principle, co-operative managers are expected to conduct or monitor day-to-day activities in the co-operative while owners' representatives (often laymen) are expected to think through strategic guidelines and control the management (cf. Walsh and Seward, 1990). Their roles and relationship are, in practice, ambiguous. In our material, this was pointed out as a significant source of tensions in co-operative governance. For example, according to an S Group regional co-operative executive, the regulations in the group indicate that the CEO is always the chairman of the board, both in regional co-operative societies and SOK, the central unit.

Whereas the supervisory board can be considered a significant resource for the co-operative, the knowledge the board members possess and the connections they have to the organization's business environment are also perceived as important sources of power. Despite the principally democratic governance, the largest stakeholder groups are not always considered effective or powerful as owners, even though they outnumber other stakeholders. Often it is not the number of people you have behind particular objectives that counts; rather, it is crucial who you have on your side:

"In co-operative governance the voice of the owner is small, although the owners' governing organs do have control over many strategic issues. Yet, especially in local settings, the power is often based on socio- economic position…"

At group level, the ownership is highly centralized, especially in the S Group. The 22 regional co-operatives own the central unit, which also means that the regional co-operatives have power over it. According to our interviewees, conflicts of interests between regional co-operatives and central units may result in public debate and subsequent changes in top management. In the end, the voice of regional CEOs and supervisory boards may overrun the voice of the central unit CEO.

In the OP Bank Group, in which ownership of the central unit is less centralized (236 member co-operatives), conflicts between the group level and regional (or local) interests have led to different outcomes. Often the diversified interests have been between particular co-operatives rather than between central and regional units. This is despite the fact that in some accounts the central unit was represented as a "power-seeking organization by nature". In 1997, tensions resulted in the members of 44 (mostly) local co-operative banks opting to break away from the Group. Today, co-operative bank CEOs generally consider the balance between group level unity and local independence as the most important question in the governance of the group.

Discussion

In this paper, we have emphasized different aspects of ownership (cf. Pierce et al., 2001) and the neo-institutional perspective on organization (cf. Greenwood & Hinings, 1996) to understand governance in co-operative context. Grounding our study on in-depth evidence from large Finnish consumer co-operatives, which operate with an organization that consists of local and regional co-operatives and a central unit, we have analyzed dynamics and tensions in co-operative governance involving owners, their elected representatives, as well as, executives and managers. Our evidence is consistent with earlier studies on corporate governance (e.g., Daily et al. 2003; Thomsen, 2004) and governance of co-operatives (e.g., Pedersen & Thomsen, 1997; Tainio, 1999) in suggesting that various board roles and contextual differences are important in understanding governance. However, our study also brings some new insights to research on co-operative governance, as we shed light on the dynamics and tensions of governance arising from different dimensions of ownership. We also consider competitive pressures and institutional dynamics of governance in co-operative context.

First, our study illuminates the broad and complex nature of ownership in the governance of co-operatives. From an economic-institutional perspective, co-operative ownership is highly dispersed and stable. However, from individual and interpersonal perspectives ownership is more dynamic and unstable. Psychological ownership is a multidisciplinary concept developed by Pierce et al. (2001) to understand employees' and managers' behaviours and decisions in organizations. This concept seems particularly suitable to understanding co-operatives in which the dispersed ownership leaves room for social manoeuvring in governance. Such manoeuvring is evident in members' interaction with co-operative management, and it is based on members' psychological ties with the co-operative, often with a regional or local dimension. These considerations are important as they often seem to justify decisions made in co-operative organizations.

Second, nationalistic, regional and local elements in contemporary co-operative business explicate a crucial dimension in governance. From a national perspective, co-operatives, which are owned and governed by regional and local stakeholders, may provide stability and security under the uncertainties that globalization brings to national or regional economies (cf. Skurnik, 2005). In an organization that consists of local and regional co-operatives and a central (national) unit, however, seeds of tension and conflict are simultaneously sown on two levels of governance. On the group level, tensions and conflicts seem to arise from organization structure as the owners of the central unit, that is, the regional and local co-operatives, may have diverging values and objectives - in the same way as individual members and stakeholders within regional and local co-operatives.

In relation to the second point in particular, our results are as yet tentative. More research is needed in the future. We have grounded our study on triangulation of qualitative data. This should be extended by statistical analysis of quantitative data when further exploring dynamics and tensions pinpointed in the present study. This could enhance our understanding of the ways in which managers' and co-operative members' representatives' feelings and perceptions of ownership relate to governance and governance-related attitudes and behaviours in co-operative context and, in turn, how these link with the apparent role of co-operatives as defenders of local ownership in the uncertainties created by quartile capitalism and the mobility of investor owners. Surveys could also provide us with more knowledge of institutional pressures and dynamics influencing governance of co-operatives.

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How to Deal with Member Heterogeneity – management implications

Jon H. Hanf and Erik Scweickert

Abstract

It is clear that in recent years vertically coordinated chain systems have gained in importance in the agri-business. Thus, analyzing strategic questions of any agri-businesses must consider vertically coordinated systems. A co-op's strategy must account for the demands of the network and in particular those of the focal company. Due to the principles of co-ops, a potential conflict arises. In addition to these conflicting goals, the co-op management also must consider that in general their members are very heterogeneous. We consider a management concept that aims to create homogeneous member groups with which certain important highly strategic requirements of the focal company can be fulfilled.

The aim of our paper is twofold: (1) we want to empirically test whether co-operatives actually divide their members into homogeneous subgroups.(2) we want to determine whether this strategy has a positive contribution to the co-operatives' success. We have chosen wine co-operatives for the empirical portion of our study.

Key words

Co-operatives, German Wine Market, Strategic Member group, Success Factor

Introduction

In the literature as well as in practice there is a great deal of discussion on the topic of member heterogeneity. For example, Bijman (2005) has shown that there is a positive correlation between the homogeneity of the members and the success of co-operatives. However, take the example of a German wine co-opeative which produces wine on roughly 400 ha. While the largest member owns about 180 ha and the top 10 members together hold about 300 ha, the remaining 500 members grow wine on approximately 100 ha altogether. Without doubt, one can consider the member of this co-operative to be heterogeneous. However, the management as well as the members consider their co-operative as very successful.

So how is the success achieved? The management of the co-op has divided its members into different groups. Within these groups the members have similar quality orientation and business strategies. Producing different quality categories the co-operative is able to supply their different customers according to their needs. According to this example the aim of our paper is twofold. First we want to empirically test whether co-operatives actually divide their members into homogeneous subgroups. Second, we want to determine whether this strategy has a positive contribution to the co-operatives' success. We have chosen wine co-operatives for the empirical portion of our study for mainly two reasons. First, in accordance with the general trend of Raiffeisen co-operatives, wine co-operatives are undergoing structural change, albeit at a slower pace. Second, wine co-operatives have a large number of members that are very heterogeneous.

Our paper is structured as follows. In section 2 we address problems esteeming of the co-operative principals and take a closer look on member heterogeneity. In the third section we introduce wine co-operatives and outline the relevance of strategic member groups in this sector. Section 4 deals with the empirical aspect and includes our results. In the last section we address the limitations of our work as well as the managerial implications and we give a short summary.

Co-operatives and member heterogeneity

Problems in Co-operatives

The German Raiffeisen co-operative system can be described as rich in tradition and highly developed. The principles of Raiffeisen co-operatives are the identity of users and owners, member orientation, the democratic principle of voting, and the lack of barriers to entry (Anschhoff and Henningsen, 1986; Laurinkari and Brazda, 1990). Other business goals such as correcting market failure, guaranteeing markets, and enhancing margins can be viewed as tools to meet those business goals (van Dijk, 1997; Cook, 1997; Sykuta and Cook, 2001).

Due to their unique institutional form as a member-owned firm, co-operatives face several problems.

Traditionally, an open membership policy has led to co-operatives having rather heterogeneous members. However, in Germany there is a tendency for Raiffeisen co-operatives to merge[1], those merged co-operatives are becoming more diverse in their business operations in addition to their members becoming more heterogeneous.

In general, members can vary according to their geographic dispersion, variance in age and education, farm sizes and type, as well as business objectives and strategies (Iliopoulis and Cook, 1999). Bijman (2005) deduces that membership heterogeneity could cause a number of inefficiency problems, including agency problems, commitment problems, decision-making problems, opportunistic behavior, coordination problems, and problems regarding the strategic focus. Furthermore, Fulton and Giannakas (2001) showed that the cross-subsidization and member heterogeneity in large centralized, multipurpose co-operatives may lead to substantial financial pressures for the co-operative because members do not see a strong connection between the success of the co-operative and their own business. However, Raiffeisen co-operatives can be characterized as being Janus faced, i.e. they are member-owned firms as well as associations of individuals (Anschhoff and Henningsen, 1986). In addition to economic matters, social mechanisms such as trust and loyalty to the co-operative firm are of high importance. However, the more heterogeneous the members, the more these social mechanisms lose their function (Bijman, 2005). Using a property rights approach, Cook (1995) pointed out five general sets of problems: free riding problems, horizon problems, portfolio problems, control problems, and influence cost problems. Furthermore, Karantininis and Zago (2001) showed that instead of selling their commodities to open co-operatives, farmers would rather sell them to investor-owned firms if they had the choice. Fulton (1995) concludes that if markets disappear as a result of increased vertical coordination, co-operatives may also begin to disappear. Hendrikse and Bijman (2002) share this assessment in the event that the investment of the processor or retailer becomes more important for the total chain value than the investments by the farmers. Because of the importance of quality in the agri-business, the findings of Eilers and Hanf (1999) address a major weakness of co-operatives. Using a principal-agent approach and the concepts of opportunistic behavior, conflicts of interest, asymmetric information, and stochastic conditions, they showed that it is not clear who is the principal and who is the agent, i.e. both the co-operatives and the members can be principals and agents. For this reason, neither leadership mechanisms nor selective terms of delivery can be enforced by the co-operatives, i.e. the members can deliver all the commodities that alternative dealers do not accept. Co-operatives that are forced to accept these commodities face the problem of adverse selection. Cook (1994) showed that in comparison to a manager of an investor owned firm the overall challenges of a co-operative manager are not significantly different but more difficult.

Homogeneous member interests

Evaluating the problems of co-operatives, we attached particular importance to the members' heterogeneity. The more heterogeneous the members, the more single interests have to be combined and satisfied. In contrast, we assume a positive correlation between the homogeneity of members or their interests and the efficiency and success of the co-operative. Thus, we think that a co-operative should have a strategy to make their member interests more homogeneous to work successfully. The introduction of "New Generation Co-operatives"[2] in the U.S. shows that aligning the interests of specialized farmers or marketing their products in a special way enhances the co-operative's performance (Cook and Chaddad, 2004; Cook, 1995; Drescher and Ratjen, 1999; Harris et al., 1996). In recent years so-called umbrella co-operatives have been studied in this context. Such "multi-string co-ops" act as a kind of holding structure for different activities which are within themselves focused (Bijman, 2005; Bijman et al., 2004; Fulton and Gibbings, 2000). Examples include Danish Crown in Denmark (Nilsson and Petersen, 2001) and The Greenery in the Netherlands (Bijman and Hendrikse, 2003).

Another approach is the formation of "strategic member groups." Hanf and Schweickert (2003) have defined them as clusters of members of a co-operative which have a similar strategy and/or aim at the same market. Thus, these members have homogeneous interests regarding at least one particular business goal. Thus, the interests within a strategic member group[3] can be described as homogeneous and heterogeneous against those of other strategic member groups. By using the concept of "strategic member groups" the management of a co-operative can segment its members in different groups with homogeneous interests. The management is thereby able to work out different strategies to satisfy the different member groups. In a more general context Iliopolis and Cook (1999) have shown that members of a co-operative can be segmented according to the degree of geographical dispersion of the members, variance in members' age and education level, the percentage of non-farm income, and differences in business objectives and strategy.

Co-operatives in the German wine sector

Having addressed co-ops and the problems of heterogeneous member interests in theoretical and general context, in the following section we apply our thoughts in an empirical study. This study was conducted in the German wine sector. Although this is a particular sector, the co-operative problems are similar to those of general Raiffeisen co-operatives. Thus, the results and insights we gain are not only valuable and applicable within this particular sector, but they are also general in nature.

Wine co-operatives strive to improve their members' economic situation by collaborating in vinification and marketing of the grapes or their processed products. Accordingly, the general function of wine co-operatives can be described processing grapes, producing must, and vinificating (fermenting, fining, clearing, and other oenological practices in the cellar for winemaking), bottling, and marketing wine. German wine co-operatives play an important role in the business; in the fiscal year 2001-02 they produced nearly 35% of the nation's wine. Due to the sectors structure[4], the majority of wine growers are members of co-operatives. More than 60,000 members belong to 246 primary co-operatives[5]. Additionally, two secondary co-operatives (federations) have been established.

The increase in retailers' power as well as the shift in consumer demand has had obvious effects on the wine co-operatives. Facing a situation where nationwide operating retailers are responsible for more than 70% of wine sales, co-operatives have had to rearrange their distribution channels. On the one hand, having traditionally focused on the local or regional markets and quantity and financial restraints, the majority of small and medium-sized primary wine co-operatives continue to direct their marketing efforts toward specialized retailers (special wine stores), local retailers, restaurants, and direct selling. On the other hand large, primary as well as secondary co-ops target the retail market. Thus, they have to deal with the demands of the retailers and their customers.

Meeting the quality demands of the retailers and of the consumers is necessary to prevail in the market. Thus, co-operatives must produce and market huge quantities of easy recognizable good quality wine. Wine co-operatives have traditionally paid the same price for all grapes. The only differentiation is by grading the grapes on a six-level scale determined by a minimum degree °Oechsle. Hence, every member produces those grapes he likes best or that he has always grown, without considering whether the grapes match the consumer quality criteria. Additionally, members of German co-operatives are not obliged to deliver defined amounts and defined quality; instead the co-operative must accept and market any kind of quality and amount. As a result, members select their grapes adversely so that they sell the grapes of better quality to other businesses, mostly privately owned enterprises.

The introduction of the profile wine concept[6] as well as the demands of the retailers gave the co-operatves the unique chance to work out a marketing strategy based on the consumer and retailer demands, instead of member production. By demanding tight quality management, the profile wine concept creates at least two member groups with homogeneous quality understanding and homogeneous business interests so they can be called strategic member groups. Because the profile wine concept is only an additional law, members are not required to comply with it. However, if they choose to get involved, they must abide by its obligations and rules. The obligations and rules of 'Classic' and 'Selection' are explained below.

The profile wine concept demands more quality management efforts than waiting to see what the vintage will bring and making the best with the raw material. Under the new concept of Classic, wine growers need to know in advance which care and attention measures they will use to achieve the optimum grape quality for a special type of profile wine: appropriate vine-cutting, adjusted green cover and fertilization, special vine protection, and de-suckering and thinning out surplus grapes. Wine co-operatives know the quality levels to be expected by the documentation of each vintage; therefore, they can plan the process and rate the grapes before they are pressed. The co-operatives pay more for those grapes that produce a higher-quality wine.

For the Selection profile wine type, the co-operatives must additionally rate the grapes and the vines both. The oenologists of the co-operatives must choose the best vineyards and define the criteria of the 'strategic member group Selection.' The groups' viticulturists must adhere to the selected measures for the vines. Therefore, the vines are rated and documented through the year at different degrees of vine development. Moreover, a rating of the vines, defined labor-measures in the vineyards over the year and special harvesting requests must be conducted and supervised by the co-operative. Furthermore, the vines have to be registered by the Federal Wine Authorities.

In summary, in the face of shifts in consumer demand and the increasing importance of retailers in the wine chain, wine co-operatives must find strategies to overcome quality and quantity problems resulting from the co-operative principles in general and the wine industry in particular. The introduction of the profile wine concept has helped to build strategic member groups so that co-operatives can offer an attractive product portfolio to retail customers as well as end consumers. This theoretical framework will be empirically tested in the following study. Additionally, it will analyze whether co-operatives using this approach work successfully.

Empirical analyses

We analyzed the 147 wine co-operatives with own vinification (“wet“ wine co-operatives) by questionnaire; more than 40% of them responded. The composition of the analyzed “wet“ wine co-operatives is representative so that all German wine-growing regions are fully represented. Only the four small wine-growing regions with only 1 or 2 small “wet“ wine co-operatives are underrepresented. The majority (78.3 %) of the analyzed co-operatives are between 51 and 100 years old. One-third of the “wet“ wine co-operativess have vineyards of 100 to 200 ha and the number of members differs ranges from 100 to 300. Fifteen percent of those sampled produce their wine on fewer than 50 ha and 10% have more than 500 ha.

The quality of a wine is determined by a variety of influences; however the type and taste of the wine are mainly dominated by the grapes and the work done on the vines (Troost, 1988). Therefore, we examine the measures used to create this competitive advantage.

In our survey 71.7 % of the “wet“ wine co-operatives pay the viticulturist according to their “yield per hectare.” Through this payment-measure they encourage the wine-growers not to exaggerate the potential of the vines, resulting in better wine quality. As shown in Table 2 they rated the measure 2.22 on a scale from 1 to 5.

Because the value of the measure “Average Oechsle” with 1.82 is lower than the one for “yield per hectare,” “wet“ wine co-operatives (80%) apply the measure “Average Oechsle” more often. One reason is because this procedure has a self-financing character. The viticulturists are not paid until the vintage is over. Afterwards they analyze the average degree Oechsle for every variety. Based on these results, they pay a surcharge for those viticulturists who delivered grapes above the average degree (depending how much the grapes are above the average). Respectively, viticulturists who deliver below-average grapes are paid less. The payment depends on the sugar content. The least used procedure was the system of rating the grapes before they are pressed. Forty-five percent of the “wet“ wine co-operatives did not apply this procedure of negative-selection in which grapes that do not match the minimum quality level are picked out. We suppose that one reason why the “wet“ wine co-operatives hesitate to implement this procedure is the missing positive incentive and the resulting negative mood if the grapes are not accepted after one year of hard work.

Table 1: Empirical results of the “wet“ wine co-operativs’ measures to create competitive advantages

		Yield per Hectare	Average Oechsle	Grape Rating	Open Strategic Member Group	Closed Strategic Member Group
N	Valid	60	60	60	60	60
	Missing	0	0	0	0	0
Mean		2.22	1.82	3.00	2.08	1.97
Modus		1	1	5	1	1
Std.-Deviation		1.606	1.408	1.657	1.565	1.507
Range[a]		4	4	4	4	4
Minimum		1	1	1	1	1
Maximum		5	5	5	5	5

a) No "wet“ wine co-operative chooses the value 3 = indifferent; they all took a position.

Table 2: Connection Between Success and Open Strategic Member Group

Number of "Wet" Wine Co-operatives per Success-Category that Build an Open Strategic Member Group					
Success-Category	**Extent of an Open Strategic Member Group**				
	We do this measure fully	Yes we do	Indifferent	we do not really do	No we don't
Very Successful	5	0	0	0	2
Successful	28	6	0	5	3
Don't Know	2	0	0	1	1
Not Successful	5	0	0	0	0
Very Unsuccessful	0	1	0	0	0
No Statement	1	0	0	0	0

The concept of an open strategic member group is opposite to the negative selection concept. We consider the open strategic member group a weaker form of the above-described concept of building a strategic member group. 73.3 % of the analyzed co-operatives offer their viticulturists the option to rate the grapes for the production of higher quality profile-wine. The viticulturists receive more money if their grapes match the criteria. Corresponding to the demand for this type of wine, every member has the chance to join this open strategic member group. The value 2.08 (2 = yes we do) on the scale shows the agreement of the "wet" wine co-operatives with this system. One step further is the system of the closed strategic member group, implemented by 78.3 % of the "wet" wine co-operatives. The value 1.97 on the scale confirms the important role of this strategic member group.

Strategic member groups are not only implemented because of the production of the Classic and Selection profile wines. In addition to 48.3 % of the "wet" wine co-operatives already producing Classic wines, 25% of the co-operatives produce according to the matching standards but they market these wines differently. Therefore, 73.3% of the "wet" wine co-operatives have open strategic member groups producing at a high standard. The same is true for Selection: 78.3 % have closed strategic member groups but only 38.3 % produce Selection or the corresponding '1.Gewächs' (grand cru). This indicates the importance of strategic member groups as a competitive advantage. Indeed,

Table 3: Connection Between Success and Closed Strategic Member Group

Number of "Wet" Wine Co-operatives per Success-Category that Build a Closed Strategic Member Group					
Success-Category	**Extent of a Closed Strategic Member Group**				
	We do this measure fully	Yes we do	Indifferent	we do not really do	No we don't
Very Successful	5	2	0	0	0
Successful	24	7	0	4	7
Don't Know	2	1	0	0	1
Not Successful	4	0	0	0	1
Very Unsuccessful	1	0	0	0	0
No Statement	1	0	0	0	0

introducing the profile wine concept led to strategic member groups

The study also analyzes the connection between the success of the analyzed co-operatives and the implementation of strategic member groups. Looking at the building of an open strategic member group in Table 3 we see that in particular the successful (28 times) and very successful (5 times) “wet“ wine co-operativess built an open strategic member group.

We see a even more precise picture in Fig. 3. Every very successful “wet“ wine co-operative either implemented a closed strategic member group (5 times) or somehow introduced a closed strategic member group. In part of the “only” successful co-operatives we find 24 really introducing and 7 somehow introducing a closed strategic member group. Thus, 63.4% of the “wet“ wine co-operatives that built a closed strategic member group are successful or very successful. Only 6.7 % of them are not successful, and no more than 1.7 % are very unsuccessful.

The results of our survey show that German wine co-operatives are looking for ways to enhance their quality by overcoming some traditional restraints of co-operatives. The results show that co-operatives try to work out management approaches and incentive schemes that make heterogeneous member interests more homogeneous.

Conclusion

Limitations

Our study, as any study, suffers from some limitations. It is based on a single sector with its own particular characteristics. Thus, one can argue whether it is possible to generalize the results across sectors. However, because the derivation is based on arguments found in general co-operative theories and related managerial approaches, we assume that this restraint is softened.

Questioning the management of co-operatives can be a subject of dispute. Instead, we could have surveyed members. However, we understand the formation of strategic member groups as a strategic management assignment. By particularly considering the developments in the downstream side, we think that a sole member orientation is not adequate today. In other words, a successful strategy has to consider the upstream as well as the downstream side.

The method of self-typing also can be questioned. However, opposite to investor-owned firms, where success can easily be measured solely by short- and/or long-term oriented financial performance, co-operative success must be measured in a broader sense. Because co-operative success includes hard and soft facts alike, we decided to use the self-typing approach. Co-op managers in the German wine business work closely together with the supervisory board; therefore, we believe that the managers can accurately judge the overall performance of the co-op.

Managerial implications and future research

In several interviews managers and members of the supervisory boards told us that they see a need to deal with the heterogeneous member interests on one side and to build a bridge between the demands of the members and the demands of the retailers and the end consumers on the other side. In this context we see the main managerial implications of our article.

Using the approach of strategic member groups, the co-op management can either segment their members according to the members’ own interests or, if the management is facing external pressure, according to such external interests. Thus, we believe that by forming strategic member groups and working out appropriate marketing strategies for them, the management of co-operatives is able to satisfy the needs and demands of their members as well as those of retailers and consumers.

We see two main areas for future research. Because the topic of building homogeneous member interests is not only important to wine co-operatives, we consider this topic to be of high general interest and we want to encourage studies in other sectors. We also consider the question of who should be surveyed. We outlined above why we have considered the management, in our context, as the most appropriate. However, because co-ops are member driven organizations, we encourage studies which analyze the values the members attach to efforts making their interests more homogeneous.

Summary

Like every other enterprise co-operatives are embedded in an environment of fierce competition. Especially the demand of the retail business is high. The retailers demand high quality on the one hand, decreasing prices on the other. These demands of the upstream side put co-operative managers in a dilemma: on the upstream side their members are not accustomed to strict quality requirements and delivery obligations. This traditional approach to quality management, together with great variation of member sizes, leads to heterogeneous quality policies at the members firms. Thus, the management of the co-operatives must provide a solution. By grouping the members according to their quality policies the co-ops can create groups of members with homogeneous business interests and they are simultaneously able to create different product ranges so that they can satisfy the downstream demands.

We conducted our empirical survey at vinificating wine co-operatives in Germany because the new profile wine concept has given wine co-operatives the ability to apply stricter quality management as well as delivery obligations. The results show that wine co-operatives use profile wine concept as one method to group their members. We also observed an increase in the quality for these groups. Moreover, we found that this increase of quality, which was due to belonging to a strategic member group, correlated with better performance.

Notes

1 See fig 4 in the appendix

2 The "New Generation Co-operative" can be understand as Sapiro III organizations in which asset appreciation mechanism, base equity plans, as well as increased share liquidity by delivery rights clearing houses have been developed (Cook 1995). The major advantage can be seen in the improvement of members` incentives to contribute to risk capital to the co-operative (Chaddad and Cook, 2004).

3 This definition shows that the idea of "strategic member groups" is derived from the idea of "strategic groups" which are used to detect the main rivals of a firm. The concept of strategic groups has to be seen in the context of the value chain and the generic strategies of cost leadership, market-wide differentiation, and in niche markets as well as the model of the five forces (Cloutier and Saives, 2002; Dranove et al., 1998; Leask and Pranell, 2005; Gloy, 1996; Homburg and Sütterlin, 1992; McLeay et al. 1996; Porter 1980).

4 The structure of grape growers is dominated by small wine-growers. Overall, there are more than 34,375 wine businesses.

5 Wine co-ops can be divided into 147 "wet" wine co-ops, which possess their own vinification facilities, and 99 "dry" wine co-ops that do not conduct their own vinification.

6 The profile wine concept is based on a law to enforce the production of classic-styled wines with an easily recognizable origin type (Schweickert, 2002). In addition to the traditional wine labeling system, the profile wine concept introduced the category-terms 'Classic' and 'Selection' (Schweickert, 2005).

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Appendix

Table 4: Development of Raiffeisen Co-operatives 1950-2003* (Raiffeisen, 2004)

	1950	1970	1990	2001	2002	2003
Total No. of Raiffeisen cooperatives	**23.753**	**13.764**	**5.199**	**3.632**	**3.423**	**3.286**
Credit with commodity business	11.216	4.920	1.474	354	301	274
Supply and marketing	2.710	1.740	645	473	458	430
Dairies	5.726	3.705	846	378	354	347
Livestock and meat	329	263	205	112	117	106
Wine-growers	508	500	310	256	238	236
Fruit, vegetable, gardening	205	201	114	125	121	117
Centers	83	90	53	32	29	27
Agricultural cooperatives				795	769	751
Other Raiffeisen cooperatives	2.976	2.345	1.552	1.107	1.036	998
Total proceeds turnover (Mio. Euro)	**3.463**	**17.461**	**39.030**	**39.431**	**37.596***	**37.500***
Total No. membership (in thousands)	**3.278**	**3.870**	**4.487**	**2.653**	**2.495***	**2.385***

*preliminary figures

Social Responsibility in S Group co-operatives: a qualitative analysis of archival data

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Abstract

In recent years, the concept of corporate social responsibility (CSR) has been of interest to many scholars in the field of management. Dimensions of CSR, such as social and environmental values have been typically supported by co-operatives, which often operate in social economy. The aim of this article is to understand how CSR is constructed and how it is connected to stakeholder relations in Finnish S Group co-operatives. Based on our qualitative analysis, we suggest that the social responsibility of the case organization can be interpreted as fulfilling co-operative values, emphasizing regional responsibility, understanding the importance of customer-owner relations and taking care of the continuity of co-operative business.

Key words

Co-operation, Corporate Social Responsibility, Stakeholders

Introduction

Research on corporate social responsibility (CSR) (e.g., Knox & Maklan, 2004; Carroll, 1998; 1981) has received a lot of scholarly attention in recent decades. The key approaches may be divided into three approaches: 1) ethical responsibility, 2) economic responsibility, and 3) corporate citizenship (Windsor, 2006). More specifically, CSR related questions have been studied in various theoretical frameworks (McWilliams, Siegel, Wright, 2006), such as agency theory (e.g., Friedman, 1970), stewardship theory (e.g., Donaldson & Davis, 1991), resource-based view of the firm (e.g., Hart, 1995), institutional theory (e.g., Jennings & Zandbergen, 1995), theory of the firm (e.g., McWilliams & Siegel, 2001) and stakeholder theory (e.g., Smith, 2003). The stakeholder perspective has been widely employed in research on CSR (e.g., Agle, Mitchell, Sonnenfelt, 1999; Berman, Wicks, Kotha & Jones, 1999).

Despite of the extensive attention to CSR in research on mainstream organizations, the framework has been rarely employed to analyze CSR in a co-operative context. This may be seen as ironic given that social responsibility has traditionally been an essential part of the co-operative philosophy (e.g., MacPherson, 1995; Münkner, 1981). This is illustrated by co-operative values and principles which include, for example, "concern for the community" (See International Co-operative Alliance, Geneva, Statement of Co-operative Identity 1995, MacPherson, 1995, p21, Nilsson, 1996, p637). The co-operative philosophy seems to be consistent also with Carroll's (1979) definitions of corporate social responsibility, according to which a responsible business enterprise notifies not only economical and legal demands, but also the ethical demands which the society directs to the business operation. That is, co-operatives are - in their operations and businesses - sensitive to the interests of their stakeholders. In a broad definition, stakeholders are usually characterized as *"any group or individual who can affect or is affected by the achievement of the organization's objectives"* (Freeman, 1984, p46). According to this definition, it seems that any social actor functioning within the community context of a co-operative can be considered as a stakeholder of the co-operative organization. This may be particularly significant in the context of consumer co-operatives.

In this study we will focus on stakeholder theory perspective on CSR (e.g., Donaldson & Preston, 1995). The aim of our study is to describe and understand how social responsibility is constructed and how it is linked to stakeholder relations in Finnish S Group co-operatives. We employ qualitative methods (e.g., Denzin & Lincoln, 2003) to solve the mystery of CSR in the given context. Our data consists of various written articles and archival materials published in S Group's magazines during the years 2000-2005.

Corporate social responsibility

Regardless of the wide recognition of CSR in various fields of research (Van Marrewijk, 2003), academics have not come to an agreement on the key question - What is the importance of CSR to the enterprise? For example, some economists (e.g., Friedman, 1962) have argued that the only social responsibility of an enterprise is its efficient use of resources in order to increase its profits. Some of the recent strategy scholars (e.g., Grant, 2005) seem to agree with the Friedman economistic and market based approach in their accounts of the topic, emphasizing profit maximization as the only objective of a firm's operations.

However, there exist many strong arguments that speak for the benefits of social responsibility to the enterprise (Davis, 1973). First of all, the enterprise must produce those goods and services for which there exists demand at a given time. In other words, the better the enterprise follows the expectations and the needs of a society, the better it will position itself in a society. Secondly, by following and reacting to the expectations of the society, the enterprise may achieve a more favorable image on the markets (see also Knox & Maklan, 2004). Thirdly, social responsibility may operate as a competitive advantage of an enterprise or at the minimum it can be considered as a precondition for successful business operation.

Davis (1973) defined that social responsibility takes into account also other demands than solely the legal demands which the enterprise faces. This is because society grants authority (legitimacy and power) to business leaders and, "in the long run, those who do not use power in a manner which society considers responsible will tend to lose it" (Davis, 1973 p.314). A more elaborated framework of CSR was developed by Carroll (1979), who added an ethical perspective to corporate social responsibility to the previously employed economic and legal views. By employing CSR an enterprise takes into account the needs and interests of the wider society in its operations and decisions (George, 2003). According to stakeholder-theory, CSR refers to a condition where an enterprise aims at making decisions which have positive impacts on all of its stakeholders (Epstein, 1987: 104). Finally, Windsor (2006) has added an environmental dimension to our understanding of how CSR is acted out by arguing for the inclusion of values supporting environmental sustainability as being at core of the responsible enterprise's value base today.

Stakeholder perspective

One of the fundamental questions of CSR is *"Why the enterprise should consider social responsibility in its actions?"* One of the rationales of CSR is that if an enterprise itself shows that it follows the principles and ethics of CSR, the legislators - a group of stakeholders (Freeman & Reed, 1983) - do not have to impose legislations in order to direct the enterprise to a more *"responsible direction"* (Davis, 1973, p314). In a broader sense, organizations may engage in CSR to gain legitimacy from their stakeholders in order to survive (e.g., Meyer & Rowan, 1977; Mizruchi & Fein, 1999). *Stakeholders* (Smith, 2003; Mitchell, Agle, Wood, 1997; Murray & Vogel, 1997; Freemand & Reed, 1983) are usually characterized as social actors (individuals or organizations) which effect the operations of an enterprise or to whom the enterprise has an effect on - such as the owners, investors, employees or customers of the enterprise. In other words, the relationships that exist between the stakeholder and the enterprise are usually based on ownership, contract, and customer-relationship or on legal demands (Talvio & Välimaa, 2004, p49). Donaldson and Preston (1995, p87) point out that research on stakeholder-theory usually focuses on analyzing corporate stakeholders from normative, descriptive (empirical) or instrumental views. The normative view on stakeholders (Carroll, 1989) gives guidance on how an enterprise should treat its stakeholders and why it should acknowledge the expectations of various stakeholders and act on them. George (2003) argues that employees are one of the most important stakeholder-groups for an enterprise and as such employers' should pay attention to them. Employees who are motivated to serve the customers of the enterprise and to develop the business operation, provide the company with a competitive advantage due to the development of competences which are difficult to reproduce by competitors. The descriptive view on stakeholders (e.g., Brenner & Cochran, 1991) describes how the enterprise manages its stakeholders or interacts with them and whether it takes into account the expectations of the stakeholders. The instrumental view on stakeholders (e.g., Aupperle, Carroll & Hatfield, 1985) focuses on analyzing how and to what extent the stakeholders can effect the operation of the enterprise.

Corporate social responsibility and stakeholder perspective on co-operatives

According to the literature on co-operatives (e.g., Skurnik, 2005; Nilsson, 1996; Münkner, 1981), it is typical for co-operative organizations to aim at both economic and social goals in their operations. Laurinkari (2004, p 25), for one, writes that;

> *"co-operation is about economic or social collaboration and is exercised in the form ofco-operative business enterprise in order to satisfy the various needs of co-operative's members".*

That is, the purpose of co-operative enterprises is not profit maximization. (Nilsson, 1996 and Munkner, 1981) Instead, co-operatives typically aim at delivery of valued services to their members which add value, both economic and social, to their members as well as the surrounding society. There is a collective dimension as well as an individual dimension to the value added process in a co-operative but it is not profit as such as it remains undistributed during the co-operatives life time lifetime and in a wind up context even them in some examples (see the Industrial Common Ownership Model in the UK) monies left after creditors ext has to be reinvested in another co-operative or co-operative investment fund. In other words, various dimensions of CSR may be considered important for co-operatives relative to their various stakeholders and their actions in this respect are supported by the ICA Statement of Co-operative Identity – incorporated in the eight co-operative principles (cf. MacPherson, 1995).

It could be argued that co-operatives gain legitimacy through their local and regional stakeholders more easily than some of their competitors whose roots may be seen to be either international or outside the region. That is, co-operatives may be looked at more favorably because co-operatives have a genuine interest in developing the community in which they are embedded in (e.g., Tuominen, Jussila, & Saksa, 2006). While it has been stated that co-operatives should operate as any other business enterprise to succeed economically well in order to compete and operate in the markets (e.g., Laidlaw, 1981), a communal approach to business can be considered rational because the survival and success of a co-operative is strongly linked to the survival and success of its operating area. This is highlighted in customer-owned businesses, which may be considered by ownership as "captives of their regions" (Davis, 2001). This is among the reasons why co-operatives work together with other (interdependent) local and regional actors (e.g., the stakeholders that share their destiny) to create a well-functioning institutional environment (e.g., Kotonen, Tuominen, & Jussila, 2007). In sum, it could be argued that co-operation, corporate social responsibility and stakeholder management are closely interconnected at the level of the locality of co-operative practise and membership.

Methodology for the S. Group co-operatives study

Our study was conducted in Finnish S Group, which consists of 22 independent regional co-operatives, 19 local co-operatives and central organization SOK. S Group co-operatives represent *"customer-owned co-operative entrepreneurship"* while SOK operates as a provider of common support services and as knowledge and development centre for regional and local co-operatives. S Group co-operatives have been important actors in Finnish society and economy for over 100 years. In addition, they have been characterized as containers of local and regional identity reproduced in their operations. (e.g., Neilimo, 2006, p5; S Group, 2006)

The purpose of S Group is to provide services and benefits to its committed customer-owners. It has been argued that they are tightly market controlled by their customer-owners (i.e., their businesses are efficiently focused to satisfy the economic needs of their members). S Group aims at increasing the commitment of their customer-owners and at acquiring committed, well concentrated members. (e.g., Neilimo, 2006 p5; S Group, 2006)

In this study we aimed to reaching our objectives by qualitative methods (e.g., Denzin & Lincoln, 2003, p257). The research material consists of fifty-six articles and texts - published in S Group during years 2000-2005 - in which the topic of our investigation is discussed. Our iteratively enhanced understanding of the topic was based on gradual analysis. That is, first we collected empirical material through the annual reports of SOK and its social responsibility reports. By analyzing this material, we drew conclusions on how the S Group declares its definition of policy in terms of responsibility. According to our analysis, regional co-operatives are independent (i.e., inside S Group) in terms of CSR. Second, we collected and analyzed annual reports and social responsibility reports of various regional co-operatives based on the interpretations made in the first phase. Finally, while our aim was to analyze accounts on CSR aimed at employees and customer-owners, we collected the topic related articles published in S Group's employee magazine "Ässä" and customer-owner magazine "Yhteishyvä".

Discourses of CSR in Finnish media

In Finnish society and business environment, many discourses (i.e., well established ways of speaking and writing about something) are constructed and employed to discuss CSR. Among these, Vehkaperä (2003) found four dominant discourses of CSR in Talouselämä, one of the leading business magazines in Finland. These discourses focus on 1) Benefit of the entire society, 2) Benefit of all of the company's stakeholders, 3) Benefit of the enterprise, and 4) Benefit of the owner. According to Vehkaperä's (2003: 97) analysis, these discourses differ from one another in that they emphasize either responsibility or consequence and either broad or narrow definition of CSR.

	Emphasis on responsibility ethics	Emphasis on consequence ethics
Broad definition of CSR	1. Benefit of the entire society	2. Benefit of all of the stakeholders
Narrow definition of CSR	4. Benefit of the enterprise	3. Benefit of the owner

Fig. 1. The Discourses of CSR in Finnish media (Vehkaperä, 2003: 97)

The discourses presented in Fig. 1 seem to be consistent with the distinct definitions made in previous research on CSR. For example, the "Benefit of the entire society" - discourse seems to maintain the idea that that by employing CSR, an enterprise takes into account of the needs and interests of the wider society in its operations and decisions (cf. Carroll, 1979). On the other hand, the "Benefit of the owner" - discourse is consistent with the accounts put forward by certain capitalist economists (e.g., Friedman, 1962). This particular discourse may be employed to reproduce the idea that an enterprise should concentrate in efficient use of its resources to benefit solely the owners and not, for example, to use of its resources to certain communal purposes.

The history of CSR in S Group

Consistent with the previous research on co-operatives (e.g., Laurinkari, 2004; Hansmann, 1999; Nilsson, 1996), accounts put forward in our data maintain that S Group co-operatives were originally established to carry out both economic and social objectives. According to Neilimo (2006, p31) CSR has been identified as peculiar to S Group right from the beginning:

> *"Sustainable operations are built on strong value base. The S Group's values and operations as a regional, democratically managed group of companies suit the values of Finnish society and of Finns as individuals. This is why the S Group's core values - excellence, responsibility, renewal and partnership - have carried us for 100 years."*

According to our data, co-operatives have carried an important mission in Finnish society, which has been emphasized during national crises, for example, before and the World War II. As put forward in our data, SOK and the regional co-operatives have operated as exemplary responsibility-carriers in Finnish society especially in 1930s, after the wars and during the time of reconstruction. SOK and regional co-operatives have strongly operated as promoters and supporters of Finnish education, culture and environmental issues (e.g., libraries, study circles, movies and paper recycling). That is, in addition to other dimensions of CSR, environmental values and responsibility have also been highly important in S Group (cf. Windsor, 2006). However, according to our data, S Group officially accepted the established principles and values of environmental policy (in 2002) only after the managers of co-operatives had interpreted that there were strong institutional pressures (e.g., from media) to do so. As a result of adaptation S Group finally published its first responsibility report in 2005.

Accounts of co-operative history in Finland speak about development in which co-operative organizations have in various situations adapted their operations according to the demands imposed by the society and, thus, been able posit themselves in a way that secures their survival. This notion is consistent with Davis's (1973) arguments in that the better the enterprise follows the expectations and the needs of a society, the better it will position itself in a it. On the other hand, S Group has found itself in its most severe crisis under circumstances in which it has not been able to adapt its businesses fast enough to societal changes and market pressures in 1960's and 70's.. During the given period, S Group did not pay enough attention to the economic dimension of CSR spoken for by Friedman (1962). Today, S Group attempts to satisfy both the economic-rational and social psychological (e.g., emotional) needs of their members. That is, the operations and businesses of S Group are designed and implemented in a way that appeals to customer-owners' and other stakeholders' rational and social psychological motives (e.g., Neilimo, 2006).

Definitions of CSR in S Group

In management research, the definitions of CSR have included various dimensions, such as economical, legal and ethical views of responsibility (e.g., Carroll, 1979; Davis, 1973). Consistently with these, also the definitions and features of corporate social responsibility in S Group include various dimensions. As stated in our data:

> *"The purpose of S Group is to provide services and benefits to committed customer-owners responsibly following the principles of sustainable development. By responsibility we mean locally, economically, ecologically and socially responsible long-term business operations."*

According to our analysis, the discourses in S Group's publications emphasize economical, social and environmental dimensions of corporate responsibility. S Group's CSR seems to be consistent with the notions (e.g., Davis, 1973) according to which as enterprise has to be economically strong in order to operate and succeed in a market and society. It is consistent with, for example, Laidlaw's (1981) ideas; the economical responsibility is often a precondition for socially responsible operation of co-operatives.

In the context of our study, economic responsibility may be considered to consist of benefits for customer-owners and the region in which the co-operative organization is embedded as well as the entire society. As put forward in our data, major share of the profits co-operatives show are directed to the development of their operating areas:

> *"We return one third of our annual surplus to our members. Last year this amount was 135 million euros. One third of the surplus is used for development of operations and one third goes to taxation. Responsible action is present in each part."*

Being economically responsible is considered to be appealing to stakeholders' economic-rational motives, whereas being socially and environmentally responsible is assumed to appeal to stakeholders social motives. Finally, according to our data, all the responsible behavior is considered to appeal to co-operative stakeholders' psychological motives.

The commitment of customer-owners is assumed to be stronger when their own co-operative contributes extensively to the welfare of the society. In other words, the responsible operation of the co-operative produces additional value to its customer-owners. As put forward in our data:

> *"Social responsibility is seen as a natural part of the value basis of S Group and the principles are well employed in different operational programs in various units. The goal is to produce additional value to the committed customer-owners through the management of economical, social and environmental information."*

Appealing to stakeholders' emotions by means of discourse in publications may not be entirely altruistic. That is, it may simply be part of a strategy which aims at constructing a more "positive" image of the group and, thus, create competitive advantage to the co-operative (cf. Knox & Maklan, 2004). However, when it is made to increase member commitment, the focused communication may also be considered as a practice consistent with co-operative philosophy (cf. MacPherson, 1995).

The role of stakeholders in S Group's operations

Accounts of stakeholders in S Group's publications seem to be consistent with the definitions given in literature on social responsibility and stakeholder management (e.g., Freeman & Reed, 1983). As put forward in our data:

> *"Stakeholders are defined as all of those parties which have something to do with S Group or to whom the S Group effects or which have impact on the operations of S Group. Collaboration [with the stakeholders] may be based on economical, ideological or some other interests. Stakeholders may therefore have a direct relationship with the group - as employees or customer-owners. Stakeholders have always some kind of expectations of the operations of the enterprise."*

The normative view on stakeholders (e.g., Donaldson & Preston; Carroll, 1989) focuses to on the question of: "Why should an enterprise pay attention to its stakeholders?" According to our data, the co-operational form of business sets its own demands in regard to the prioritization of stakeholders. In our S Group co-operatives, various stakeholder-groups are considered highly important, for example, because of high interdependence. Many regional stakeholders share co-operative's destiny. Co-operatives are tentative especially to their customer-owners, who are the basis of their existence. Also employees are also highly important stakeholders to S Group (George, 2003). S Group co-operatives have succeeded well in national employee satisfaction competitions. According to our data the tentative approach to employees is a great asset of co-operatives. It is considered to help co-operatives to become better places to work, but to operate more efficiently and produce better quality services.

The instrumental view on stakeholders (e.g., Donaldson & Preston, 1995; Aupperle et al., 1985) focuses on the question of *"How much stakeholders effect the operation of the enterprise?"* As the customers are also owners of the enterprise, they are able to have voice in the co-operative in many ways (e.g., via customer feedback, personal relations, governance etc.) and therefore produce outcomes on the operations of their co-operative. According to our data, the operations of the S Group are also effected, for example, by local and national authorities and decision-makers, EU-authorities, consumer and environmental organizations, international organizations and national as well as international competitors.

The relationship between the stakeholders and perspectives of responsibility

S Group has strengthened its stakeholder-relationships during the last ten years, when the corporate social responsibility has emerged to a highly important role in Finnish media. By reporting its long-term responsibility, S Group can achieve a more favorable image among its stakeholders. The stakeholder-relationships have become particularly strong when examined locally and regionally. According to our analysis, this may an outcome of the significant role of locality and regionality in various responsibility-discourses in S Group's publications. Regionality has been presented along three other perspectives (economical, social, and environmental) of responsibility. The concept of "regional responsibility" is efficiently put into practice in the operations of regional co-operatives:

> *"The strength of responsibility in S Group is its regional structure. Regional co-operatives understand the features of their regions, preferences of their customer-owners and they enhance the stable development of their regions through their operations. Regional co-operatives are strong influencers in their regions as their decision-making is local and they are governed by their own customer-owners."*

The accounts put forward in our data seem to be consistent with, for example, George's (2003) ideas on the high importance of recognizing the surrounding society as a group of stakeholders. In various communal settings of our study, local citizens are interpreted to be interested about the new jobs and tax revenues which the enterprises bring to the region. According to our data, CSR of the regional co-operatives have many welcomed "effects" on their regions. The ethical and responsible operations of co-operatives are considered to increase trust between co-operatives and its business partners as well as other stakeholders and to bring conformity and predictability to their operations (Vehkaperä, 2003). That is, the CSR of S Group was considered as a "trust building mechanism". As put forward in our data:

> *"All our operation and collaboration with different stakeholders are based on trust. Our operation is open, honest and trustful. We carry responsibility of our employees´ welfare, the safety of our operation and the welfare of the citizens and the environment in our region."*

The precondition for the generation of trust between regional citizens and S Group is the open dialogue between the co-operatives and their stakeholders. Stakeholder-communication may be employed as a means of increasing both customer-owners' and employees' commitment to the co-operative.

Conclusion

The aim of our study was to understand how the concept of corporate social responsibility is constructed and how it is interconnected with stakeholders in various archival materials of our case organization (S Group). By employing qualitative analysis on our data, we found four discourses which emerged in the publications of S Group.

Fig. 2 presents these discourses which are employed to construct S Group's CSR and its stakeholder-management:

"Co-operative's involvement in peoples' everyday life" - discourse describes co-operatives as a long-lasting and stable actors, which are prepared to change their operations according to the changes of the society and operational environment. In this discourse, the co-operative is presented as a trustful partner who doesn't abandon its principles even when facing difficult times. The publications of S Group appeal also to people's emotions. For example, they emphasize

CO-OPERATIVE'S INVOLVEMENT IN PEOPLES' EVERYDAY LIFE	CO-OPERATIVE AS A REGIONAL ACTOR
• Long history of responsibility • Responsibility in changes of society • Continuity • Appealing to emotions	• Regionality • "Human faced" business • Domestic values • Trust
CO-OPERATIVE AS A SERVANT OF CUSTOMER-OWNERS • Customer-owners and employees are the most important stakeholders. • Responsibility as a producer of additional value to customer-owners • Responsible action together with the stakeholders of S Group.	CO-OPERATIVE AS A PROFIT-MAKING ACTOR • Responsibility as part of "normal operation" • Principles of economical responsibilities • Profitability of the operation

Fig. 2: The discourses of responsibility and stakeholder –management in S Group

that the S Group has been with and for Finnish people under the time of war and reconstruction in Finland. *"Co-operative as a regional actor"* -discourse emphasizes the importance of regionality in S Group. For example, regional co-operatives understand well the needs and preferences of customer-owners and other stakeholders of their region and are actively involved in many local activities.

"Co-operative as a servant of customer-owners" -discourse focuses on S Group's collaboration with co-operatives' most important group of stakeholders - their customer-owners. In this discourse, the expectations and needs of customer-owners are considered as vital for the successful operation and business of S Group. In addition, actions and goals of S Group are justified - in the archival materials - by emphasizing that they produce additional value to customer-owners. What is typical to "*Co-operative as a profit-making actor*" -discourse is that the economic responsibility finds its rationale and justification in other goals and responsibilities that co-operatives carry along economic responsibilities.

Consistently with previous research on CSR (e.g., Windsor, 2006; Carroll, 1979; Davis, 1973), we found that the CSR of S Group includes economic, social and environmental dimensions. However, we also found that in S Group another dimension could be added, which unifies the above mentioned dimensions. According to our data, the so called "regional responsibility" is in the core of S Group's CSR. On the regional level, this notion is consistent with Nilsson's (1994) statements in that co-operatives emphasize the welfare of the entire society in their actions and decisions.

Finnish discourses of CSR are typically divided into four different levels which emphasize either the benefit of an enterprise, owner, all stakeholders or the benefit of the entire society (Vehkaperä, 2003). In our study we found that in S Group the benefit of the entire society was also emphasized. In this discourse, the enterprise questions profit maximization as the primary mission of the enterprise - it considers its mission is to increase the welfare of the society and not only its owners.

This paper is a preliminary attempt to integrate the perspectives in research on corporate social responsibility, co-operation and stakeholder management and our evidence is based on limited data. Our findings do suggest that further investigations would be worthwhile. For future research it should be interesting to follow, for example, how the CSR of S Group co-operatives is understood by various stakeholders in different geographical regions. In addition, it would we interesting to use comparative analysis and compare the actions of responsibility in S Group and in a competitor's company. There is also the need to reflect on the implications of some aspects of our reseach for the context of globalization and the growing evidence from research in other countries of the special competencies the co-operative social dimension provides for their competitive strategy as a business and as an association.

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An alternative approach to oversight: the case of the supervisory committee in Irish credit unions

Noreen Byrne, Olive McCarthy and Michael Ward

Abstract

The credit union supervisory committee, as a distinct model of organisational oversight, is very much invisible within corporate governance research. The focus is almost entirely on its corporate counterpart, the audit committee. This means that best practice is based almost entirely on audit committee experience, even though the audit committee model has not always prevented large-scale corporate losses. Audit committee and corporate and co-operative governance literature may benefit from the perspective of alternative models, such as that of the credit union supervisory committee.

This paper explores the role of the supervisory committee in credit union governance and the structure of supervision, oversight and regulation within the Irish credit union movement. It reports the findings of a survey of credit union supervisory committees and qualitative interviews with key players in credit union supervision and development in Ireland, including the regulators of the credit union movement. A profile of the composition, activities and skills levels of supervisory committees is examined. The findings show that it is the high level of activity of the supervisory committee and its clear-cut independence that set it apart from other organisational oversight models.

Key words

Audit Committees, Credit Unions, Governance, Regulating Financial Services, Supervisory Committees.

Introduction

The credit union supervisory committee, as a model of organisational oversight, is very much invisible within corporate governance research, where the focus is almost entirely on its corporate counterpart, the audit committee. Thus, best practice is based almost entirely on audit committee experience. This is despite the existence of over 40,000 successful credit unions worldwide, safeguarding US$600 billion in member savings under the supervision of credit union supervisory committees.

Given the changing nature of regulation of credit unions in Ireland, the role and value of the supervisory committee is coming under increased scrutiny, particularly as a result of its increased importance under the 1997 Credit Union Act. In the Republic of Ireland (RoI) alone, there are over 400 credit unions with ?7 billion in member savings, and all credit unions are required by legislation to elect from their membership a supervisory committee charged with *'the general duty of overseeing the performance by the directors of their functions'* (Credit Union Act 1997, S.58 (1)). The Irish Financial Services Regulatory Authority (IFSRA)1 has expressed the view that credit union supervisory committees should develop along the lines of the audit committee model. With the abundance of research and best practice guidelines on audit committees, compared with little or no research on supervisory committees, this is hardly surprising. Therefore, the authors are of the view that it is important to examine the value of the supervisory committee model before any drastic changes are made to its structure and practices.

This paper explores the role of the supervisory committee in credit union governance and presents a comparison with the audit committee model. It reports the findings of a survey of credit union supervisory committees and qualitative interviews with key players in credit union supervision in Ireland. In order to compare the audit committee and supervisory committee models, the authors draw on past audit committee research. It is hoped that this paper will be a useful starting point for further research into the Supervisory Committee model of organisational oversight while also presenting an alternative model to that of the audit committee in corporate governance literature.

The corporate audit committee

The corporate audit committee is an internal control or monitoring body in an organisation. According to Collier (1997:74), they have 'responsibility for reviewing the financial statements and the accounting principles and practices underlying them, liaising with the external and internal auditors, and reviewing the effectiveness of internal controls'. The audit committee is now recognised has having a central role to play in good corporate governance. This has led many of the corporate governance guidelines and codes such as those produced by Cadbury (1992), Higgs (2003) and Smith (2003) to focus on strengthening the role of the audit committee.

The Irish Companies (Auditing and Accounting) Bill (2003) requires all public companies (whether listed or not) and all large private companies to have an audit committee (Devlin, 2003:25). Much of the corporate governance literature also focuses on audit committees. The following quotes give a flavour of some of the views in the literature:

> *'One of the many lessons from the still unfolding Enron scandal is the critical role of audits and the trouble that can befall an organisation when its audit committee is not doing its job'. Reed (2002, p40)*

> *'Recent events in the U.S. economy have organisations scrambling to ensure they have all the right pieces in place to avert financial disaster. Many are discovering that one of the most important is a strong audit committee'. Verschoor (2002, p26)*

The audit committee model, however, has not prevented recent corporate losses (such as those in Barings, Enron, AIB/First Maryland). Some observers (Sweeney 2002; Spira 1999; Collier 1997) refer in particular to its lack of independence as a key factor in the weaknesses of this committee. Most literature and corporate governance reports grapple with the notion of independence and rarely make clear recommendations in this regard. On one hand, independence is seen as essential to effective oversight (Verschoor 2002; Spollen 1997), while on the other, it is viewed as potentially damaging, where separation between the board and audit committee might result in difficult tensions within the organisation (Smith 2003).

The 1992 Cadbury Committee, in reporting on corporate governance, defined audit committee independence as being 'freedom from company connection or relationship which might interfere with the exercise of independent judgement' (Spira 1999:263). In corporate companies, the audit committee operates as a sub-committee of the board and is comprised of non-executive directors. In this respect, the board can exercise some control over the audit committee and can decide who its members are. The members of the audit committee, as non-executive directors, can also participate in corporate decision-making. It is this 'blurred distinction' (Smith 2002:25) between roles that often causes confusion and lack of trust among shareholders and undermines responsibilities.

Another weakness raised is the level of relative inactivity of many audit committees, where they only meet four times per annum, which as Healy and Palepu (2002) suggest, translates into only a few hours in the year. Our findings later show that credit union supervisory committees meet regularly, with many meeting on a weekly basis.

Healy and Palepu (2002) also criticise audit committee members for their often modest background in finance and accounting. DeZoort (1997), in a review of relevant literature, states that:

> *'Findings in this area indicate that, while expertise and experience in oversight areas are perceived as critical components of overall committee effectiveness, they are lacking for many audit committee members.' DeZoort (1997, p213)*

Sweeney (2002,) confirms the earlier findings by DeZoort (1997).

> *'Audit committee ineptitude, in particular, is generally acknowledged to be among the principal reasons why shareholders suffered billions of dollars in losses over the last year or so'. (Sweeney,2002, p16)*

Smith (2003) states that at least one member of the audit committee must have

> *'significant, recent and relevant financial experience…It is highly desirable for this member to have a professional qualification from one of the professional accountancy bodies'. (Smith, 2003, p9)*

Smith goes on to state that there should be an induction programme for new committee members and that training should be provided to all audit committee members on an on-going and timely basis. These sentiments are echoed in the Higgs Report (2003). So while active, experienced and trained audit committees are now seen as an essential element of good governance in corporate companies, the jury is largely still out with regard to the operational definition of independence.

The credit union supervisory committee

The supervisory committee in a credit union has a similar function to that of an audit committee. In Irish credit unions, it is a statutory committee, established by the Credit Union Act (Republic of Ireland) 1997. It is elected from among the members of the credit union, by the members of the credit union, and is responsible to the credit union membership. The committee consists of three or five members, all of whom work in a voluntary capacity and represent the interests of the general membership. The primary function of the committee is to oversee the performance of the credit union directors. The Supervisory Committee normally attends all board meetings but does not participate in decision-making. Thus, its independence from the board is secured.

Supervisory committees came into being at an early stage in credit union development, as early as the Raiffeisen movement of the late 1800s[i]. Possibly one of the reasons Irish credit unions adopted the idea of a supervisory committee was because the agricultural credit societies and village banks failed in the early 1900s partly as a result of 'inadequate control procedures' (Quinn, 1999:13). It seems credit unions were intent not to repeat the same mistakes.

The supervisory committee, as an independent entity, seems to be the most popular model of organisational oversight used in credit union movements[ii]. As indicated earlier, the credit union supervisory committee model does not appear to have played any role in the development of corporate governance theory or practice. Even within credit union circles, there is little focus on supervisory committees. However, within the corporate sector, audit committees are now seen as a key ingredient in a good corporate governance structure.

Credit union governance structure

Individual credit union

The governance structure in a credit union is comprised of four main elements: the membership at the AGM, the board of directors, the supervisory committee and the salaried management. As Figure 1 below depicts, the supervisory committee performs the pure oversight role in the credit union.

The key issue in governance is that in most organisations, including credit unions, there is a degree of separation between those who own the organisation and those who manage the organisation[iii]. Thus, there must be an oversight function of some sort in organisations to ensure that management always acts in the interests of the owners. In corporate companies, this role is performed by the non-executive directors and the audit committee. In credit unions, the board of directors perform an executive, and to a lesser extent, an oversight function. The supervisory committee in the credit union performs a pure oversight role.

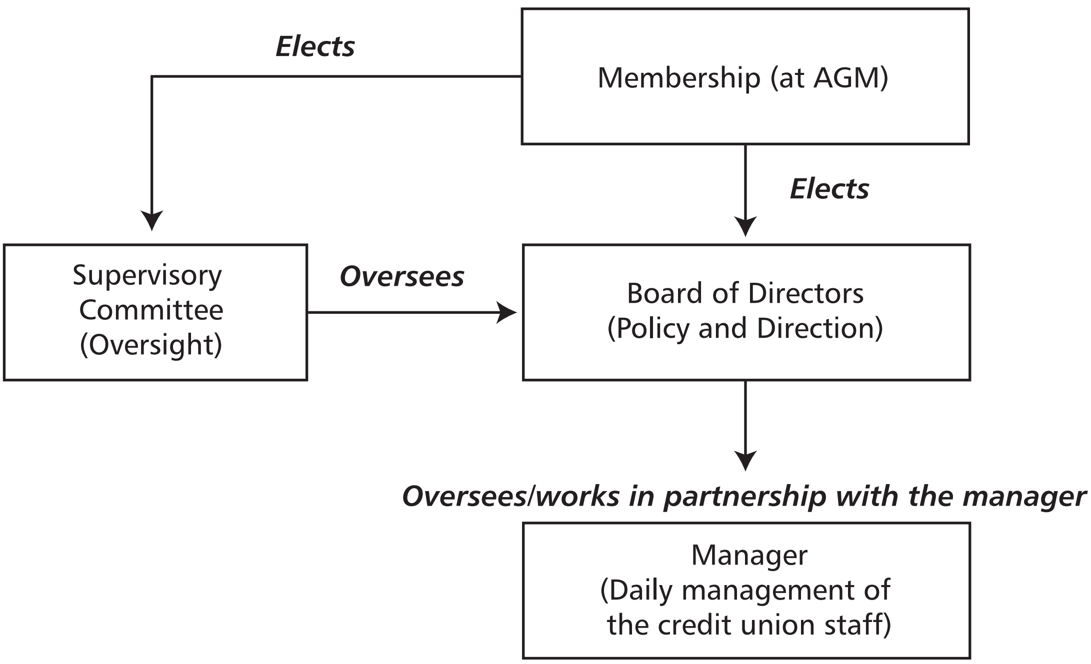
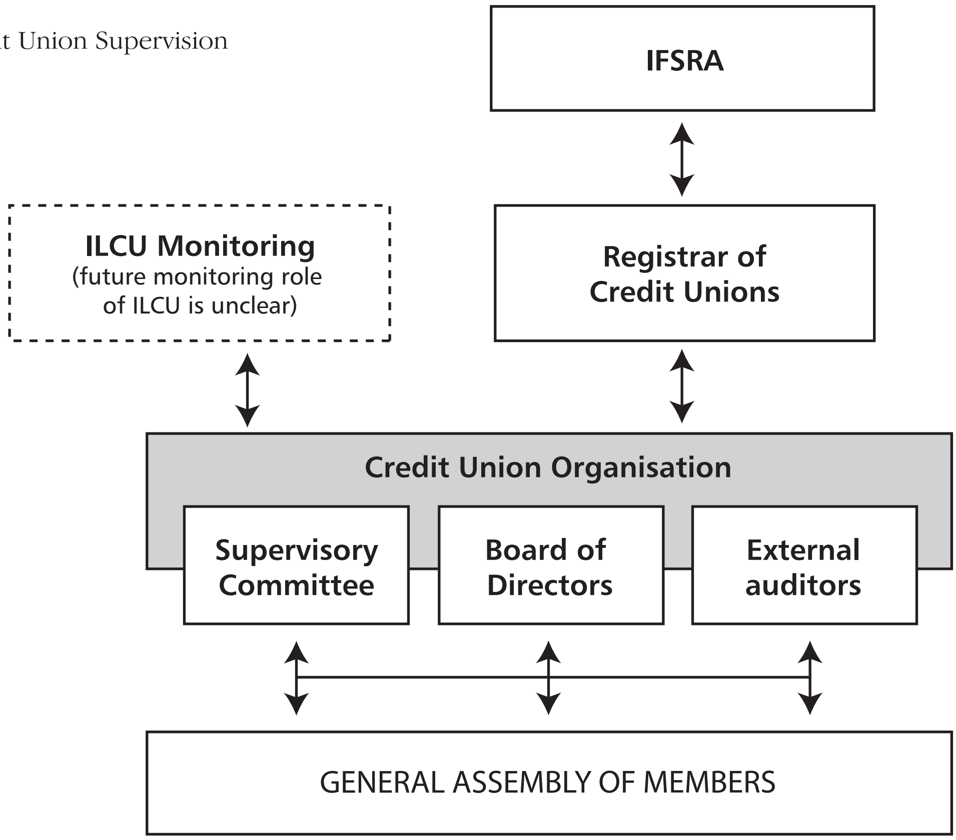


Figure 1 Corporate Governance Structure in Credit Unions. Adapted from Branch & Baker, 2001

Figure 2 Credit Union Supervision



The role of the supervisory committee within the overall regulation of credit unions is as an internal regulator.

Credit union movement

There is a number of layers of supervision and oversight in the credit union movement. The ultimate supervisory authority is IFSRA, which, as a result of intense lobbying by the Irish League of Credit Unions (ILCU)[iv], has a dedicated Registrar of Credit Unions to regulate credit unions. The ILCU also acts as a monitoring body. It employs a number of field officers who visit credit unions and monitor their books and operations. (The precise monitoring role the ILCU will play into the future is unclear at the present time, as it may be taken over by IFSRA.)

The regulatory structure is presented diagrammatically in Figure 2.

The research

The research conducted consisted of both a quantitative and qualitative research methodology. The quantitative element comprised of a survey with 125 supervisory committee members from 39 Irish credit unions. These surveys were administered face to face and focused on the composition of the committee. The authors draw a comparison with the audit committee model in terms of compositional factors. The qualitative element of the study involved interviews with a number of key witnesses who are involved in credit union supervision, development and regulation. These interviews focus on the key issues of the role of the supervisory committee, skills required by supervisors and on whether the committee should remain fully independent or develop along the lines of the audit committee model.

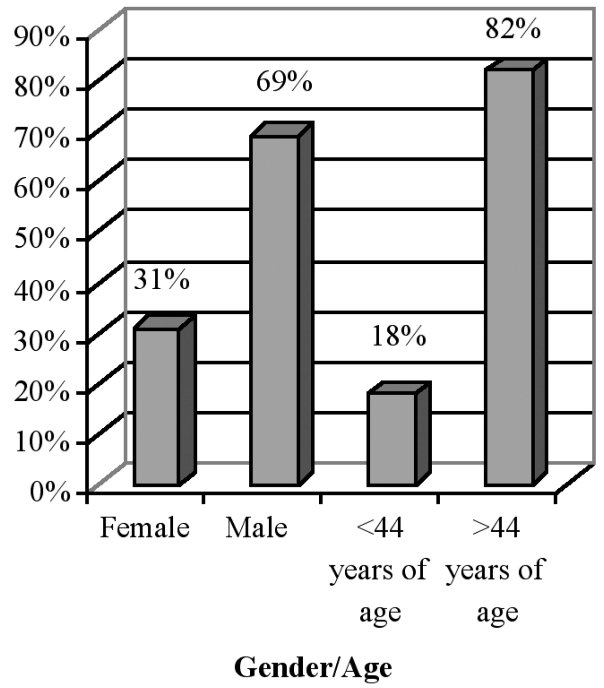
Findings – Survey

A profile of the individual supervisor in terms of age and gender is first presented. This is then followed by aggregated data on the committee as whole, in terms of composition.

General profile of the individual supervisor

The research presents an overall profile of the individual who volunteers their time to the credit union as a supervisor. The most striking characteristic is that supervisors tend to be male and over 44 years of age (See Figure 3). The numerical dominance of males on supervisory committees was also found by McKillop et al (2002).

Figure 3 Profile of individual supervisor



Thus, it could be suggested that for regeneration and for representational purposes, supervisory committees should attempt to have greater balance in their membership.

Committee composition

In order to determine the committee composition, we aggregated the data and examined each supervisory committee. The results are present in Table 1. While the Table only focus on the supervisory committee, we compare the results with audit committee research and suggested best practice. Table 1 indicates that credit union supervisory committees are numerically dominated by male members. As the authors are not aware of any gender research on corporate audit committees, it was not possible to make a comparison between the supervisory committee and the audit committee on this factor.

In terms of length of service on the committee, 82% of committees have one or more members in at least their second term of service. This suggests a strong level of experience on these committees. 18% of committees are in their first term. It could be suggested that these committees are inexperienced and have the disadvantage that they lack the guidance of more experienced members. PricewaterhouseCoopers (2000) point out that committees must consider both continuity and the desirability of fresh perspectives for their development. They state that 'rapid turnover can be detrimental to the committee's effectiveness' since members need time to gain experience and the benefit of a historical perspective.

Eighty percent of the surveyed supervisory committees consist of members with previous credit union experience in some other capacity, as board member, sub-committee member, or staff member. This is a positive finding given that a good understanding of the business is essential to the effective operation of a supervisory committee. It is also interesting to note that 90% of committees have at least one member with relevant supervisory committee training. It is interesting to compare this with training provided for audit committees.

The American Society of Corporate Secretaries (ASCS), in its 1998 survey on audit committee effectiveness, found that only 6% of 550 public companies provide formal training to their audit committee members. The ILCU runs specific courses for supervisory committee members. 64% of supervisory committees surveyed have at least one member with accounting experience and/or qualifications. Smith (2003) recommends that there should be at least one member who is financially literate on the corporate audit committee. The aforementioned audit committee survey carried out by the ASCS found that 74% of respondents had at least one audit committee member who had a finance or accounting background (PriceWaterhouseCoopers, 2000). The credit union supervisory committee, at 64%, compares less favourably.

The research found that all the supervisory committee members work on a voluntary basis. This differs significantly from the corporate audit committee which is remunerated for its time. Supervisory committee members must be members of the credit union and must not hold a directorship or be an employee of the credit union. This helps to ensure independence and objective judgement. This differs from the audit committee where directors (independent and not) can be members of the audit committee. All the supervisory committees studied were elected by the membership of the credit union and are an independent entity from the board of directors. This differs from the audit committee selection methods. The Public Company Governance Survey (1999-2000) carried out by the National Association of Corporate Directors found that in 41% of companies the audit committee members are chosen by the full board and in 35% are chosen by the CEO and/or the board chair (PriceWaterhouseCoopers, 2000).

Supervisory Committee Composition	
Gender • All/majority male • All/majority female	78% 22%
Length of Service • All members in their 1st term (3 years and less) • At least one or more members in their second term or more	18% 82%
Previous CU experience • No previous credit union experience on the committee • At least one or more members with previous credit union experience	20% 80%
Participation in relevant supervisory committee training • No supervisory committee training received by the committee • At least one or more members who have participated in supervisory committee training	10% 90%
Formal accounting experience and/or qualifications • No formal accounting experience and/or qualifications • At least one or more members on the committee with accounting experience and/or qualifications	36% 64%
Remuneration • All supervisory committee members work on a voluntary basis	100%
Independence of the committee • All members of the supervisory committee are elected by the membership (shareholders) of the credit union. • There are no credit union directors, employees or other credit union committee members on the supervisory committee	100% 100%

Table 1, Compositional Profile of Supervisory Committees

Activity level of the committee

Supervisory committees meet approximately 40 times or more in the year to carry out on-going spot checks on the general operations of the credit union. In addition to these meetings, supervisory committees are required to meet four times a year with the board, in the absence of salaried management, to report on the performance of the board. In contrast, the corporate audit committees normally meet on a quarterly basis. They also attend all monthly board meetings. It might be argued that twelve board meetings, versus four audit committee meetings, might well leave non-executive directors with a greater sense of their duties on the board rather than their responsibilities as audit committee members.

Unlike corporate audit committees, supervisory committees are observers at an operational as well as a strategic level in credit unions. This ensures that they are close to the everyday, operational activities of the credit union, are familiar with the staff members and can build positive relationships with management. They also attend all board meetings as observers and can easily be familiar with decisions made and the rationale behind them, while retaining the committee's independence. The on-going interaction at both of these levels of the organisation may enable supervisory committees to recognise and deal with a potential difficulty or issue early and before they can develop into more serious problems.

In reporting to the board, the supervisory committee can make recommendations to the board for improving performance. While these are not binding, they are also a useful measure of committee activity. Figure 4 shows the level of activity of supervisory committees in terms of recommendation-making.

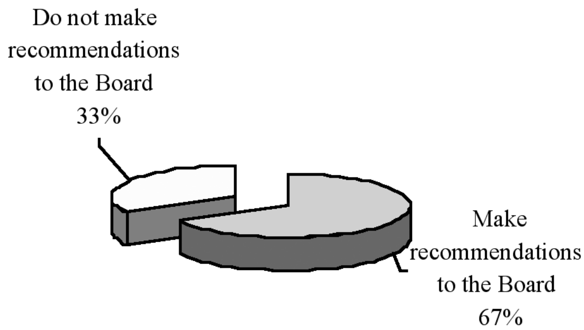


Figure 4, Supervisory committee recommendation-making to the board

The majority (67%) of the studied supervisory committees make recommendations to the board. However, a significant 33% claim not to make recommendations. Why do some committees make recommendations and others do not? To attempt to answer this, we cross-tabulated supervisory committee composition with the tendency to make recommendations to the board. The results of these cross-tabulations are presented in Table 2.

While none of the above results are significant at the $p < 0.05$ level, there would appear to be a slightly greater tendency for those committees which are male dominated, those with longer serving members and those with previous credit union experience to be more active in making recommendations to the board.

Supervisory Committee Composition	Committees which make recommend ations to the board of directors	Chi Square Result P< 0.05
Gender • All/majority male • All/majority female	21 (72%) 4 (44%)	.122
Length of service on committee • All members in their first term (3 yrs or less) • At least one or more members in their second term or more	3 (43%) 23 (72%)	.140
Participation in supervisory committee training • None of the members have participated in supervisory committee training • At least one or more members have participated in supervisory committee training	2 (50%) 24 (69%)	.455
Previous credit union experience • No previous credit union experience on the committee • At least one or more members with previous credit union experience	4 (50%) 22 (71%)	.262
Formal accounting experience and/or qualifications • No accounting experience and/or qualifications • At least one or more members with accounting experience and/or qualifications	9 (64%) 17 (68%)	.813

Table 2, Cross-tabulations of supervisory committee composition and recommendation-making to the board

It is important to remember that the sample size was small, being only 39 credit unions. An extension of the sample size in future research may alter the statistical significance of the findings.

The findings of the survey indicate that the credit union supervisory committee composition and structure compares favourably with the best practice guideline set out for audit committees. In some cases the supervisory committee outperforms the audit committee, particular in terms of its level of activity, independence and participation in specific training. However, it compares less favourably in terms of financial expertise. The next section of this paper will examine the views of a number of key witnesses from the credit union movement, including the financial regulatory body (IFSRA).

Findings – Key witness interviews

Ten key witnesses were interviewed from the following organisations: ILCU, Credit Union Development Association (CUDA), IFSRA, former Registrar of Friendly Societies, Credit Union Supervisors' Forum as well as other individuals who are deeply involved in the work of supervisory committees.

The interviews covered a number of areas, including the role and perceived skills of supervisory committees and the independence of the supervisory committee.

Role of the supervisory committee

Many of the key witnesses felt that there was often confusion in the minds of both the supervisory committee and the board of directors about their respective roles. The general agreement was that the supervisory committee must confine its role to oversight only. A quote from one of the key witnesses summarises this point:

> *"Supervisory committees do not have any role in the running of the credit union, they cannot influence board decision making, cannot voice an opinion, but can make a point of order/or a point of information…supervisory committees must know how far they can go and must not go beyond this point."*

One other key witness stated that

> *"on occasions, supervisors become involved in policy making and that this causes tension and problems in the credit union".*

Another key witness indicated that the supervisory committee and the board often only become aware of supervisors' roles when there is a difficulty in the credit union –"from this comes more understanding and possibly respect from the board about the role of the supervisory committee". If this is the case, it is unfortunate that the credit union has to experience some turbulence before the role of the supervisory committee is fully recognised.

Skills required

The key witnesses were in general agreement about the important skills required on a supervisory committee. These are listed as follows in the general order of importance:

1. Common Sense
2. Human resources or people skills
3. Financial skills
4. Independence, sound judgement and the ability to ask constructive questions

5. A clear understanding of roles
6. The ability to view the overall picture and not simply focus on the routine aspect of their work

Almost all key witnesses felt that supervisors need common sense primarily, and then specialised knowledge. A quote from one key witness summarises that view:

> *"A supervisory committee can have all the financial skills and qualifications but if it does not have common sense and people skills then this committee will not be effective."*

However, in saying that, many of the key witnesses highlighted that a major shortcoming in many supervisory committees is a lack of financial knowledge. It was also suggested by some of the key witnesses that supervisory committees may have a tendency to over-focus on certain elements of their work while ignoring other areas. Spollen (1997) alludes to this tendency when he says that sometimes the internal control function in a company tends to over focus on the areas known best and on simpler routine tasks while ignoring the more complex areas of the organisation. One key witness summarises this point as follows:

> *"Some supervisors will put all their effort into balancing the bank reconciliation down to the last cent. When the organisation has assets of several million, supervisors must be able keep their work in context and see the overall picture."*

Supervisory committee as an independent entity

Some of the key witnesses feel that the supervisory committee, as an independent entity, can create tension in credit unions. These key witnesses feel that the committee should become a sub-committee of the board similar to the audit committee in corporate companies.

In Ireland, the statutory independence of the supervisory committee has, in fact, increased. In the Credit Union Act 1966, one director could sit on the committee. The 1997 Credit Union Act changed this to ensure that no director could be a member of the committee. It was felt by the drafters of the 1997 Act that a supervisory committee which contains directors 'defies logic' in that it does not make sense for a board director to be responsible for reviewing board performance.

While the Irish legislation is strengthening the role of the supervisory committee, other credit union legislation from around the world would appear to have weakened the role of the supervisory committee. Of 104 summary credit union legislations from around the world, only 10 mention the supervisory committee. While this may be so, the World Council of Credit Unions (WOCCU) has kept the concept of the independent supervisory committee to the fore in its model law for credit unions.

Should the supervisory committee remain an independent entity or should it be a sub-committee of the board? The view from the majority of the key witnesses was that the supervisory committee should remain independent of the board. Many felt that this independence was the key to its effectiveness. It was felt that this independence would only result in tensions between the board and the supervisory committee if both parties were unclear of their roles and responsibilities. Perhaps the real issue underlying that of independence is clarity of role.

In the corporate governance codes and literature, there appears to be a pre-occupation with the importance of independence, although precise definitions are not always forthcoming. Spira (1999) indicates that substantial emphasis is placed on independence in Cadbury (1992), which she says implies that "independence is a prerequisite for ethical behaviour in the context of corporate governance". In fact, Higgs (2003), Smith (2003) and also Cadbury (1992) recommend that at least half of the board should be made up of non-executive directors. However, the non-executive directors also sit on the board and are involved in decision-making. This has led a number of commentators (Spira 1999, p263, Collier 1997, p80) to highlight the conflict for the non-executive director in trying to carry out a decision-making role and a monitoring role at the same time. Spira (1999, p263) has indicated that the corporate governance codes have not sufficiently dealt with this dilemma. O'Higgins (2003, p32) highlights that this may result in a 'latent threat' to the unitary nature of the board.

Under the Stock Exchange's Combined Code, non-executive directors on an audit committee should be 'independent of management and free from any business or other relationship would could materially interfere with the exercise of their independent judgement'. However, because the audit committee is a sub-committee of the board and its members therefore also sit on the board, independence can be difficult. Vicknair, Hickman and Carnes (cited in Collier 1997) have raised doubts about the impartiality of 'grey' area directors, who are 'not wholly independent of management' and who may undermine the position of audit committees as 'truly independent corporate governance entities'.

Thus, if independence and impacts on the unitary board are issues in corporate companies, perhaps it is better to have a group separate to the board who, if carrying out their role in an effective and clearly understood way, are truly independent and do not affect the unitary function of the board.

Conclusions

The supervisory committee model may well be a useful alternative model to the corporate audit committee model for organisational oversight. Its clear and unequivocal independence from the board overcomes one of the main, widely recognised shortcomings of the corporate model. The high level of activity of the Supervisory Committees surveyed challenges the so-called cavalier approach of many audit committees. This can be explained, at least in part, by the prior experience and regular training of committee members, factors which are deemed to be important in the literature, as well as the clear understanding of their role. It might also be accounted for by the fact that committee members receive no remuneration to fulfil their duties, which may indicate a commitment to the organisation and its members that goes beyond any pecuniary interest.

The supervisory committees surveyed are not without their faults. Their numerical dominance by males must be addressed. Their weakness relative to audit committees in terms of financially qualified members must also be tackled through revised recruitment and professional training strategies. As already indicated, this research was restricted by the lack of literature on credit union supervisory committees and credit union regulation. It is also limited in that it does not delve into the many complex issues which impact on supervisory committees, such as the psychological dynamics between the committee and the board/management, the issue of volunteer commitment to credit unions, and the levels of trust between members and their supervisory committee.

However, it is also disappointing to see that the audit committee research does not appear to cover these types of issues to any great extent either. It is the hope of the authors that this research will be the foundation of more in-depth research in the future. Such research is important as it helps those outside the credit union and co-operative world to better understand these unique and important organisations.

Notes

i The original legal framework for credit unions, the Cooperative law (1868,1871) paragraph 38 (I) stated 'It is the task of the Supervisory Board (Verwaltungsrat, Aufsichtsrat) to supervise the Executive Board (Vorstand) in their management in all branches of the administration…' (cited in Raiffeisen, 1970:55)

ii The English-Canadian credit union movement has adopted the corporate model of the audit committee which operates as a sub-committee of the board rather than as an independent entity.

iii In the case of the credit unions, the members own the organisation but they elect a board to run the organisation on their behalf.

iv The largest umbrella body for Irish credit unions.

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The Credit Problem in Rural Iraq: the Baathist state-owned agricultural banks financing of land reform co-operatives

Al Rashid

Abstract

The institutional rural credit problem in Iraq is complex and multi-dimensional, involving politics, society and culture. This article presents insight into the failure of successive military regimes and the Baathist state (represented by the state-owned Agricultural Bank) to provide adequate and viable loans to land reform co-operatives from 1958 to 1975.

The credit problem in Iraq, as in many developing countries, centers on the continuous indebtedness of the farmers and the relatively high cost of obtaining credit. During the last three decades, successive Iraqi regimes have attempted, however unsuccessfully, to tackle the deficiency in Iraq's rural credit system. The objective of the 1958 coup was to strengthen institutionalized credit in order to create a more competitive credit system.

The Co-operative Bank and the Agricultural Bank were to help attain this goal. Six years after the Land Reform Law of 1958 was enacted, little had been achieved. A new credit policy was adopted after the Baath coup d'etat of 1963 which advocated the elimination of non-institutional sources of credit. It was felt that increasing the loans advanced by the Agricultural Bank to the co-operatives could do this. This policy was retained by the Baath regime with the added provision that the co-operatives were to replace non-institutional sources of credit and that institutionalized credit was to be considered an important means to increase agricultural productivity. While there was a significant increase in both the number and size of loans allocated by the Agricultural Bank to the co-operatives. The government sought to control the co-operatives to achieve political objectives and discouraged any financial viability that might challenge its authority. The article concludes with some policy suggestions to improve the future institutional credit market in rural Iraq.

Key words

Agricultural Banking, Agricultural Credit, Agricultural Co-operatives, Iraq, Land Reform, Rural Development, State.

The nature of the rural credit problem in developing countries

During the last four decades, several valuable studies and articles covering the literature on rural credit problems in developing countries were published. Specialized studies sponsored by international organizations such as the F.A.O. and I.M.F. have contributed significantly to understanding the dimensions of the rural credit problem in developing countries. In a developing economy the difficulties of obtaining capital of any sort are great, due to low-income and considerable inequalities in income distribution. There are usually three main sources of finance; current income, past savings and loans. Due to the subsistence nature of the agricultural economy and the time lag between incurring the costs of production and the eventual returns on investment, credit is fundamental to the continued process of production. According to Balkenhol,

> *"Without finance there can be no income generation or poverty alleviation. Without finance enterprises cannot be created or sustained. All businesses … whether they are large or small, engaged in manufacturing or trade, located in the countryside or in the city, owner-managed companies or public corporations… need access to regular and adequate financing for production, sales and distribution. Even informal income- generating activities need financial resources for working capital and investment purposes, as well as the know-how required to manage such resources" (Balkenhol, 1991, pp645-655).*

From the point of view of the cost of credit, agriculture in a developing economy suffers from certain disadvantages as compared with other sectors such as industry and trade. These include the small, fragmented nature of peasant operations, the risks and uncertainties involved in farming, capital scarcity and the high degree of competition between borrowers for capital, the slow rate of turnover of capital due to the long gestation period of agricultural production, and the monopoly position of many money-lenders and traders; all these impose conditions which make the cost of credit to agriculture higher than in many other types of economic activity (U.N.F.A.O., 1957, p12). Due to high risk and uncertainty, a money-lender would add a two to 200 percent premium to the normal rate of interest, depending on his anticipated rate of default. Since the proportion of defaults is high in the less-developed countries, rates of interest would obviously be adjusted upward in order to make good the loss caused by defaults (Wai, 58, pp107-113).

Moreover, the cost of management of loans is higher in agriculture compared to other sectors. The number of loans advanced by the money-lenders in rural areas may be relatively small and the size of individual loans are generally small. (Bottomley, 63, p29) As a result of these factors, and also due to the inclusion of the monopolistic position of the money-lender, the latter charges a higher rate of interest (Bottomley, 63, p29). Other studies highlighted that the majority of state-owned agricultural banks had not been effective in their primary goal of improving access to credit in rural. (Al Hilali, 69, p235)

> *"A reduction in the cost of borrowing has been achieved only for large borrowers, while small producers have been saddled with high transactions costs", (Vega,A. and Graham, 95, p20).*

This demonstrates a tremendous discrepancy between the stated objectives of these institutional lending organizations to assist small farmers to obtain reasonably priced loans and the actual results. A number of studies over the past twenty years have confirmed these characteristics of rural financial markets. For example, Stiglitz concluded that adverse selection and moral hazard could prevent interest rates from achieving equilibrium between the supply and demand of credit (Stiglitz, 93, pp19-62). The role of politics in granting rural loans has been closely studied. For example, Cole stated the following about the public rural lending practice in India.

> *"Over the 1985-1999 period, agricultural lending by public banks in India grew 5 to 10 percentage points faster in election years than in years after an election, that election year loans were more likely to be made to districts with more heavily contested elections, that these loans were less likely to be repaid, and that they did not measurably affect agricultural out put." (Conning and Udry, 05, p13).*

The neo-liberal development literature emphasized micro credit programs as a promising method to counter the defects of the rural financial markets in developing countries. However, a comprehensive study of 13 micro-credit programs in Asia, Africa and South America indicated that the benefits of the micro credit programs under study were not scale neutral as the upper and middle income poor tended to benefit more than poorest of the poor (Hulme and Mosley, 96).

In general, the literature on rural credit distinguishes between "the traditional approach to rural finance" and a newer approach. The former is premised on extensive intervention in the rural markets to encourage farmers to adopt new technology, obtain favorable interest rate or to correct the bias towards urban dwellers. The latter aims to achieve the same objectives by promoting efficient rural financial markets through favorable policy environment, improving the legal and regulatory procedures that support rural finance markets, and addressing specific market failures in cost-effective ways through well designed, self-sustaining interventions (Yaron et al, 98, pp147-170).

It is important to emphasize that despite its importance to the rural economy rural finance by itself is not a panacea for achieving advanced agriculture. The task of transforming traditional agriculture requires well-integrated economic and social plans.

From 1958–2003, a strong interventionist –redistributive policy, guided Iraq's policy makers. Some key aspects of this policy reflect central planning, encouraging an import-substitution and industrialization orientation, the introduction of land reforms and food subsidies. The dramatic increase in oil revenues during the period from 1958-1980 had significant political and social implications. These revenues were used by the state to create an authoritarian regime where citizens traded their political rights in exchange for economic benefits and the relative security of state jobs.

Indebtedness and the rural credit problem in Iraq

Although no comprehensive information is available concerning the extent of indebtedness in rural Iraq, there are indications that the average Iraqi farmer has a very meager amount of capital at his disposal. During the last four decades the increasing problem of indebtedness, its causes and implications, has presented a grave challenge to successive regimes in Iraq. To the Iraqi farmer, borrowing is necessary not only to meet the costs of production but also to maintain his family. When, after the 1958 coup, the government began to favor the formation of co-operatives, it was found that a considerable number of farmers were unable to meet the minimum share-holding costs of 1.250 Iraqi Dinar (I.D.) per annum.

A study undertaken by the Institute of Co-operation and Agricultural Extension found that 8 to 12 percent of member farmers in co-operatives had debts exceeding 100 I.D. outstanding for over two years. Approximately 11 percent of the farmers were selling their cereal crops to merchants prior to harvest ("selling green"). About 50 percent of the farmers were indebted to merchants for the supply of credit on consumer goods, while 7 percent of the farmers were tied to the merchants by the provision of agricultural inputs, basically seeds and cultivation tools on credit. About 17 to 20 percent of the farmers were indebted to friends and relatives through the provision of loan funds to meet social and emergency expenditure (Russel, Sriram and Al-Abdulla, 71, p28).

Under such conditions indebtedness tends to be identified with poverty and is not associated with increased productive investment leading to enhanced productivity and income earning capacity. Although the maximum rate of interest permissible under Iraqi civil law is restricted to 7 percent per annum, this has no effective force in rural Iraq and is vastly exceeded in practice. The cost of credit obtained from money-lenders in rural Iraq has certain distinctive peculiarities as it tends to be disguised and charged indirectly. Direct methods of charging interest are not very common in rural areas in deference to the emphatic pronouncements of Islam against usury.

The Koran prohibits the creation of money, by money but allows money to be used for trading tangible assets that can generate a profit. Thus money- lenders adopted ingenious disguised usurious practices. One such common method is the advancement of money against an anticipated crop (called "selling green") so that the deal appears to be a commercial rather than a purely monetary transaction. It is difficult to give a typical figure for interest rates levied in various parts of rural Iraq, since rates vary greatly from lender to lender and from region to region. The rates average 30% for one season, and can vary from 60 to 100% from one season to another (Al-Khyat, 70, p115). Another study by Al-Hilali indicated that the average interest rates in rural Iraq could fluctuate between 10 to 30 percent per annum (Al-Hilali, 69, p235).

The high cost of credit in most cases, is due to the lack of effective competition between the sources of credit. Apart from the semi-monopolistic position of the money-lenders that enabled them to exact more onerous credit terms, a considerable degree of risk is involved because of the conditions under which Iraqi agriculture is practiced. For example, more than one-third of the total area under cultivation depends entirely on rainfall, which is highly erratic and seasonal. Moreover, the losses on crop yields caused by insects and pests may reach substantial proportions in some seasons, and according to one-study losses caused by pests to wheat and barley were valued at an average of 10,000,000 I.D. annually. Similarly, animal husbandry is characterized by inadequate forage and poorly developed veterinary services; these resulted in low levels of livestock production.

The agricultural credit policy and the supply of credit after 1958

One of the main objects of the Land Reform programme implemented after 1958 was to strengthen institutionalized credit as a step towards creating a more competitive credit system in rural Iraq. Theoretically it was to constitute an integral part of the land reform programme, which sought to facilitate the emergence and establishment of independent and productive family farms. Among the institutional agencies co-operatives were viewed as an important instrument for tackling the credit problem, as they tend to undermine the quasi-monopolistic position hitherto enjoyed by the private money-lender. Furthermore, co-operatives have certain advantages over other agricultural credit institutions once a certain level of efficiency has been achieved. Operating on a local basis the board is familiar with the character and ability of its members and is, therefore, qualified to extend credit on the basis of a sound appraisal of each cultivator's personal merits. Moreover, co-operatives can be organized so as to reach small farmers scattered throughout remote areas (Surridge, 62).

Solving the problem of rural credit in Iraq necessitated the strengthening of the institutional agencies and improving their operational efficiency. The co-operative credit system required considerable assistance in order to develop a sufficiently competent autonomous organizational and financial structure to withstand and challenge the strong competition from private vested interests, and to meet the growing needs of agricultural development.

The supply of credit and the role of the Co-operative Bank in financing Land Reform Co-operatives

The sources of credit in rural Iraq may be classified into two broad categories; institutional credit agencies represented mainly by the Agricultural Bank and the Co-operative Bank and non-institutional sources such as merchants, relatives, friends and money-lenders, such as village shop-keepers and other local traders. In 1956, the Ministry of Social Affairs made a recommendation emphasizing the co-operatives' urgent need for financial and technical assistance. In 1959, following the introduction of the first agrarian reform, the Co-operative Bank was reorganized to encourage the co-operative movement and participate in any action designed to promote co-operative societies and accelerate their development and progress. In order to achieve this the Ministry of Agriculture and Agrarian Reform authorized the Co-operative Bank to undertake the following measures:

1. Provision of co-operative societies with various types of credit;
2. The purchase and import of any articles of equipment, or commodities that might be required by co-operatives;
3. To act as an agency for co-operatives in exporting their products;
4. To accept deposits from co-operatives and their members, as well as from non-co-operative organizations and individuals;
5. To assist co-operatives in foreign exchange matters;
6. To serve co-operative societies and their members through the provision of various banking facilities;
7. To provide co-operatives with storage facilities;
8. To participate in co-operative projects sponsored by co-operative societies and research the possibilities of expanding such projects.
9. To provide co-operatives with economic, technical, statistical and administrative assistance and advice (Al-Hilali, 1969).

Co-operative Bank capital and loans

In 1956, the nominal capital of the Co-operative Bank was 250,000 I.D., which was increased to 3 million I.D. in 1959, with 51 percent of this capital to be advanced by the Ministry of Finance, and the rest to be contributed by the co-operative societies, which benefited from the credit services of the bank. The capital position of the bank indicated that both the Ministry of Finance's subsidy and the co-operatives' statutory subscription were insufficient to significantly boost the expansion of the embryonic co-operative movement. By the end of 1964/1965, the paid-up capital of the Co-operative Bank, represented only 22.15 percent of the bank's nominal capital, amounted to 664,439 I.D. of which 600,000 I.D. originated from the Ministry of Finance and the remainder from subscription by co-operatives.

The Co-operative Bank law lacked detailed provisions specifying the nature, amount and duration of loans to be granted to the co-operatives. Most of the loans subsequently granted by the bank were short and medium-term, ranging from six months to four or five years. These two types of loan were usually required by, and extended to, agricultural and consumer co-operative societies, whereas long-term loans, with periods from six to twelve years, were allocated in particular to building co-operatives. The actual rates of interest charged by the bank varied according to the type of co-operative negotiating the loan. Three to four percent was charged on loans granted to co-operatives and four-and-a-half percent on loans extended to non-agricultural co-operative societies.

Although this policy favored co-operatives in principle, by levying subsidized rates of interest (compared to the previously mentioned private sector rates believed to range between 30 percent and 100 percent per annum), the volume of credit released to agricultural co-operatives was minimal compared to that absorbed by non-agricultural co-operatives. For example, only six percent of the total credit outflow was destined for agricultural co-operatives, compared with 92 percent for building co-operatives during the period of 1959 to 1964 (Iraq, 74).

It is difficult to measure the extent to which the credit needs of co-operative members were met by the Co-operative Bank due to the absence of reliable information about their credit requirements. Nevertheless, a study submitted by the Supreme Agricultural Committee indicated the minimal impact of institutionalized credit by revealing that, whereas in 1972 non-institutional sources provided the farmers in Baghdad province alone with an estimated 2 million I.D., the total institutional credit supplied annually in the whole of Iraq amounted to only 3,889,000 I.D. (Iraq, 1972, p81). This situation prevailed at a time when the beneficiaries from the land reform were in urgent need of credit, as former landlords ceased to supply loans and money-lenders were reluctant to advance funds in the uncertain political situation that followed the coup of 1958.

The Agricultural Co-operative Bank and its role in financing land reform co-operatives

In 1945/46, an Agricultural Bank aiming to serve the agricultural sector was established with state funds and with nominal capital of 500,000 I.D. An analysis of the growth of bank capital and its credit operation is important in assessing the performance of the agricultural banks in relation to their stated aim of tackling the credit problem in rural Iraq.

Despite a steady growth in the bank's assets, a continuous discrepancy existed between nominal and paid-up capital. This, coupled with increased demand by the farmers for credit following the first Agrarian Reform, seriously affected the bank's lending position. Successive regimes between 1952 and 1974 repeatedly stressed the importance of adequately financing the Agricultural banks to promote higher productivity in practice non-agricultural banks received a greater allocation of funds from the government. For example, over the period 1952 to 1973 the average paid-up capital of the Agricultural Bank was approximately 5.3 million I.D. compared with 12.8 million I.D. of the Bank for Building and Construction. Even after the accession of the new regime in 1958 when the capital assets of the banks were publicly stated to have been raised to 10 million I.D., only 6, 243,897 I.D. were reported to have been allocated by 1965 (Iraq, 76).

The Agricultural Bank and credit operations

The Agricultural Bank's credit operations were severely criticized in the period immediately prior to 1958 coup on the grounds that large landowners having adequate securities at their disposal constituted its most important clients. Since the Agricultural Bank required collateral such as assets or personal property as prior conditions for a loan this consequently disqualified the majority of landless farmers from availing themselves of its credit services. Despite a progressive increase in the number and size of loans advanced annually by the Agricultural Bank, they represented a total of only 25,374,276 I.D. for the period 1938 to 1972 or an annual average of 746,302 I.D. This compared very unfavorably with non-institutionalized forms of credit, which provided an estimated annual 17 million I.D. in Iraq before 1958 (Iraq, 1976).

Although successful implementation of land reform necessitates careful advanced planning and coordination between the various institutionalized agencies operating within the agricultural sector, no detailed instructions were issued to the Land Reform co-operatives in order to familiarize members with the size, type and duration of the loans available. The year 1964 was crucial in the evolution of the government's credit policy as it represented a more committed orientation towards the co-operative movement. For the first time a consistent set of regulations was introduced governing credit facilities accorded to Land Reform Co-operatives. The following are some of these important aspects:

1. A direct contact was established for the first time between the Agricultural Bank and the Directorate General of Agricultural Co-operatives, which aimed at achieving an annual credit plan.
2. Agricultural co-operatives were freed from the immovable property qualifications as a surety measure, the latter being replaced by an official guarantee from the Supreme Agricultural Committee, which is the highest authority in the agricultural sector responsible for planning the development of the agricultural sector.
3. A preferential interest rate of three percent was established on loans to agricultural co-operatives, this being significantly lower than the rates charged by non-institutional sources of credit.
4. Branch managers of the Agricultural Bank were authorized to grant loans with prior consultation with the Directorate General of Agricultural Co-operatives Headquarters in Baghdad to hasten the loan procedure.
5. Individual co-operatives were permitted to borrow in excess of 3,000 I.D. (Tabra, 76).

As a result of the Agricultural Bank's new policy of giving priority to agricultural co-operatives, the latter's share of the total volume of loans issued increased from twenty four percent in 1964/65 to fifty nine percent in 1975 (Iraq, 75). No official explanation was provided for why 41 percent secured no loans especially since, at that time, all co-operatives members were experiencing an acute need.

Distribution of credit within the co-operative sector

Although the total credits allocated to the co-operatives increased significantly over the period from 1964 to 1974, it is noteworthy that certain co-operatives continued to benefit from the Agricultural Bank loans whereas others continued to be excluded despite their meager internal resources. This uneven channeling of loans to some co-operatives to the exclusion of others may be explained by bureaucratic shortcomings of the Directorate General of Agriculture Co-operatives. For example, whereas the Agricultural Bank allocated 7,346,790 I.D. to the Directorate General in 1972 for redistribution to the co-operatives, only 2,202,359 I.D., or 36 percent of the sum allocated, was actually withdrawn and redistributed. By 1973-74, the proportion had risen to 42 percent (Iraq, 1976).

Reliance on external rather than internal resources may have bene essential during the early stages in the establishment of co-operatives in developing countries, but for the emergence of a truly independent and self-sustaining co-operative movement this initial relationship must be accompanied by a reversal of this pattern, which, in the long-term, must be inimical to the application of the basic co-operative principles of self-help and local autonomy. A major factor, which aggravates the problem of utilizing co-operative resources, is the restrictive centralization in decision-making. Some Land Reform Co-operatives accumulated relatively large reserve funds but they were not allowed to utilize them productively. This passive attitude toward developing the internal finances of the co-operatives was the result of a the government policy that sought to control the co-operative movement and discourage any financial viability that might challenge its authority.

The government agricultural credit policy after the 1968 Baathist coup

The official publications concerning the objectives of the credit policy lacked coherence. After a careful reading of these publications, however, the following points emerged as significant aspects of Government policy:

1. The necessity of combating the long-lasting problem of overdue loans by farmers in rural Iraq, which was considered a partial cause of their low productivity (as it limits their capability to invest);
2. The elimination of non-institutional sources of credit and their replacement by institutional credit to ensure more equitable interest rates;
3. Enhancing farmers' productive ability through the important means of institutional credit (Iraq, 76.)

During the mid 1970s, the government attempted to make institutional credit more available. The Agricultural Bank reaffirmed the favorable interest rate of three percent on loans to Land Reform co-operatives. Baker questioned the rationale of such a policy:

> *"Why (couldn't) peasants borrowing at exorbitant interest rates in the informal market (from money lenders) borrow at the equivalent rate from credit institutions? Low rates of interest give an impression to the borrowers that the future is amply provided for, and thus, encourage consumption. On the other hand, a high rate of interest increases the reward for saving." (Baker, 73.)*

In Iraq, the reduced interest rate of three percent was applicable to Land Reform Co-operative loans only, and was justified on the assumption that these subsidized loans were to be utilized for productive purposes by the farmers. In 1974, the Agricultural Bank advanced to the co-operatives loans totaling I.D. 3,851,230, the largest amount ever disbursed to co-operatives by the Bank. However the share received by each co-operative averaged only I.D.2, 805. This amount could hardly serve to neither increase co-operative members' productivity nor contribute significantly to improving farmers' incomes. According to the 1971 Census, the informal credit market (i.e., private lenders) provided I.D.7.8 million to farmers, while the Agricultural Bank provided only I.D. 3.1 million (Iraq, 1975).

Reasons for the high default rates on the Agricultural Bank loans

Following the governments' policy in 1964 of extending credit availability. There was a significant increase in both the number and size of Agricultural Bank loans allocated to the Land Reform co-operatives. There was also a considerable increase in defaults, from 1 percent in 1966 to 53 percent in 1975 (Iraq, 1976). Some direct and indirect causes for these default rates during the 1970's follow. The following are some of the problems that might have directly or indirectly caused a considerable increase in co-operative default rates during the 1970's.

Land reform regulations

The stated objective of the Ministry of Agriculture was to facilitate the emergence of an efficient credit system in rural Iraq. In practice, the land reform regulations severely restricted the right to sell or mortgage the redistributed land. The Supreme Agricultural Committee acted as the grantor of loans advanced to co-operatives.

This may have encouraged borrowers to believe that expropriation of their land, as penalty for default, was only a remote possibility. One moral hazard factor in aggravating default rates was the lack of security or collateral received from the debtor in exchange for the co-operative loan. Another factor was the fact that the Directorate General of Agricultural Co-operation did not formulate a credit policy to encourage co-operatives to build their own internal savings to serve as sources of loans to members. This led to a weaker commitment to repay loans since the co-operatives lost nothing in the case of default. So persistent was this situation that loans were regularly written off.

The Agricultural Bank and its co-operative loans practices

A critical function of any lending institution is monitoring the status of the enterprise, which has been funded. In this instance, the Agricultural Bank depended on the co-operative supervisors to report and follow up on information related to the Bank's investments. In fact, co-operative supervisors coped with heavy workloads (some of them managing more than one co-operative), which relegated such reporting to a low priority. More critically, these supervisors reported up to a different authority, the Directorate General of Agricultural Co-operation within the Ministry of Agriculture, which reduced their incentive to follow through as requested.

The Agricultural Bank was also to some extent culpable because of its loan recovery process. Loans were not collected as efficiently as possible due to a lack of experienced and qualified personnel. The Bank suffered from the absence of an extensive branch network to adequately monitor and supervise the loans to the co-operatives. In 1975 the Agricultural Bank operated 35 branches primarily concentrated in the main provinces, whereas the co-operatives were distributed among Iraq's 318 administrative regions. High default rates by co-operatives drained the scarce resources of the Agricultural Bank and increased the social opportunity cost of institutional loans. The defaults affected the mutual trust between the co-operatives and the Agricultural Bank, undermining a key fundamental principal for a sound system of agricultural credit.

Poverty and the default rate

Rural poverty in Iraq contributed to the issue of loan repayment and defaults. Farmers who subsisted on meager incomes naturally devoted a large percentage of whatever additional sources came their way to funding basic needs. They did not have access to commercial bank loans (which were not available in rural areas for rural credit) nor could they afford the costly credit offered by traditional money lenders. The introduction of institutional loans offered by the government state-owned Bank, which did not require guarantees or collateral, created an environment in which farmers made basic and understandable decisions in support of their most immediate needs. (See Appendix 1)

The Fallow System and Default Rates

The fallow system is widespread in Iraqi agriculture. This practice involves cultivation of half of the land while the remainder is left fallow until the next year.

This practice is partially responsible for lowering crop production and, consequently, affecting rural income. The fallow system is widely accepted by farmers in rural areas, who believe it has these three advantages: the land's fertility returns in a period of fallowness; it relieves demand on water supply, especially in the summer; and, it reduces the amount of salinity in the cultivated land. (Majid, 67, p41) Contrary to what the farmers believe, however, the fallow system is destructive and wasteful. Wild grass takes hold and then becomes part of the harvest, reducing the yield and its quality. Nor is there strong evidence to suggest a correlation between the fallow system and lower salinity. The continuation of this system is one of the factors, which decreases productivity, negatively affecting farmers' incomes and, ultimately, their capability to repay loans.

Socio-cultural factors affecting repayment of loans

Farmers in rural Iraq do not make their economic decision in a social or cultural vacuum. They are profoundly influenced by the customs, norms, and modes of the society in which they live. There are few sociological and anthropological studies of Iraqi farmers' investments habits. Of these, one study indicated that farmers prefer to allocate a relatively high percentage of their scarce resources to fulfill religious and social activities rather than to productive investments that can enhance their immediate income or future accumulation of capital. (Rashid & Ajam, 74) Such behaviour might further explain the high default rate on agricultural loans. More socio-economic research is required to analyze the impact of values and norms and their impact on capital accumulation and economic growth.

The Oil Boom of the Seventies and the Default Rate

Another factor that could have encouraged laxity in collecting overdue loans from the co-operatives in addition to the political objectives was the dramatic increase in oil revenues during the seventies. The oil revenues provided a surplus of 35 to 40 billion of foreign reserves. (Alnasrawi, 94) The availability of this surplus may have relaxed the financial discipline of the Agricultural Bank, lessoning enforcement of collection procedures, which in turn impacted the co-operative default rate.

The Baathist control of rural organizations

Despite the fact that the rate of default on co-operative loans dramatically increased during the seventies, neither the Agricultural Bank nor the Directorate General of Agricultural Co-operation attempted to analyze the reasons. One reason might be attributed to the effective Baathist control of all rural organizations (including co-operatives) during the seventies. The goal was to increase the Baath party base and achieve more integration with its urbanized base. Although no figures exist for the number of co-operative members who were enrolled, Baath party membership increased significantly between 1968 and 1976 from between 100-200 in 1968 to 500,000 members in 1976. (Potter & Sick, 2004, p140) It is possible that members of the co-operatives who enrolled did not feel obligated to repay the co-operative loans on the assumption that they were entitled to compensation for following the Baath party political line. In addition, this understanding was enhanced when co-operative members were asked to provide political information on the opposition and, when during the eighties, they were asked to report on soldiers who deserted during the Iraq-Iran war (Tareek Al-shaab, 2006).

Conclusion

It has been noticed that the main beneficiaries of the Agricultural Bank loans during the last four decades were not the small farmers but, rather, rich farmers who were able to provide the collateral required for their loans. Thus, the institutional credit system failed in its basic objective of providing the co-operative small farmers with adequate credit to enhance their productivity. Thus though some of the literature on the one hand suggests poverty and need are key factors in the high levels of default on loan repayments this evidence suggests, given the high proportion of loans going to rich farmers, that corruption or political patronage may be a more significant factor.

In Appendix 1 I reflect on the reality of poverty in Iraq and in Appendix 2 I suggest some of the actions that are clearly essential to ensure the mistakes of the past documented in this paper are not repeated. Whilst the state has much to answer for in terms of the failures it is also apparent that civil society or the lack of it must also be recognize as having been a significant factor in the weakness and failures of co-operatives in Iraq. Money without the human and social capital to make use of it will not resolve the fundamental challenges that co-operatives can help to address. Governments need to give more attention to investment in the human capital which must surely be a prerequisite to any offer of purely financial aid. It is also clear that real auditable accountability for the money provided in terms of bills of sale in the context of field based inspections and real sanctions for the misappropriation of money must be put in place .

A clear line needs to be drawn between money which is aid for managing and relieving the immediate needs of the rural or urban poor and money provided for the short to medium term development of the local economy. Co-operatives may use some of their surpluses for social and welfare purposes but they must never be permitted to utilize economic loans for such purposes and their leadership and management must be clear that they have a responsibility to all the members and the wider community to ensure that members use the funds for agricultural development for the purposes intended. It may well in the context of Iraq be appropriate for the Mosque to manage welfare funds for the poor but it can never be right for any religious institution in any context to siphon off funds intended for economic development.

If local co-operatives are to manage development they must themselves be managed by professional people utilizing transparent management information systems in the interests of the whole membership in their community context. Governments need to give the development of such management their leadership capacity their priority rather than simply taking the easy route of giving money that provides politically expedient immediate amelioration but that fails to address the deep seated social and structural issues.

In countries like Iraq unless the cultural issues are addressed as a part of the human and social capital development co-operatives will merely reflect the problems and cannot be realistically expected to transform them. Individuals with vision, values and skills can build communities. Government can help provide the infrastructure to enable such individual change agents to emerge but government cannot use a civil service or other institutional framework as a substitute for local leadership.

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Appendix 1. A brief review of the sketchy literature on rural poverty in Iraq.

The International Bank's report published in 1959, uses a hypothetical example of a peasant in the irrigated zone, where barley is the principal crop, to serve as a rough indicator of a framer's income. This farmer, who usually cultivates about 25 Donums (a donum is one-quarter of a hectare), was provided with a share of the harvest calculated at three tons (from a gross output of 7.5 tons), which he could then take to market to sell at 10 I.D. a ton (1952 prices). If this share of the summer crop at 10 I.D.was added to the 30 I.D. incomes of his winter and summer crops, his annual income totaled 40 I.D. (International Bank, 59, pp132-133).

From this meagre income, the farmer was often compelled to contribute sums for religious purposes as well as for guards and servants for the Sheik "landlord". The few studies addressing farmers' incomes after the Agrarian Reform law of 1958 provided differing conclusions. According to Al-Jasim, the land reform of 1958 did not improve peasants' income, which totaled between 10 I.D and 20 I.D. from 1958-1964 (Al-Jasim, 69). Al-Talibani's study estimated that peasants' per-capita income prior to the agrarian reform of 1958 was 20 I.D. from winter crops and 12 I.D. from summer products, totaling 32 I.D. per annum.

After the agrarian reform, it was estimated that the income of peasants who owned 40 Donums of rich soil farmed by the traditional rotation system amounted to I.D. 80 from winter and 48 I.D. from summer products for 128 I.D. annual per-capita income (Al-Talibani, 69, pp72-73). Al-Talibani's study, however, is not representative of results on all types of soil in Iraq, differing as they do in fertility, and divided broadly into three different categories (Al-Janabi, 67). A critical distinction should be noted between the standard of living of farmers as a whole and those who benefited from the agrarian reform law. The number of rural agrarian families who benefited from the law was estimated at 57,117 out of a total of 714,017 agrarian families by the end of 1958. Official statistics suggest an increase in the average share of rural family incomes from I.D. 134.3 in 1953 to I.D. 261 in 1969 (Hashim, 70, p69). These estimates are not accurate, however, because of the weakness of an arithmetic average as a representative statistical measure. The official statistics also did not provide a clear distinction between people working in the agricultural sector and those merely depending upon agriculture. More recent studies indicate that overall absolute poverty in urban areas increased from 25 percent in 1988 to 72 percent in 1993, while in rural areas, it increased from 33.8 percent to 72 percent between 1988 and 1993 (Shaar, 04). The F.A.O. indicated that in 2003, 55 percent of the population was poor and 44 percent were currently food insecure (F.A.O., 03).

The widespread poverty that plagued Iraq during the last twenty-five years was the result of misguided government policies and priorities that did not recognize the importance of encouraging efficient allocation of resources to the productive sectors of the economy. Instead these resources were directed to the military, an unproductive sector. Finally, the country faced three devastating wars as well as sanctions that devastated its economy and ripped its social fabric.

Appendix 2. Potential Policies to Improve Future Rural Credit in Iraq

While acknowledging the importance of market forces to stimulate economic growth, there is a great need in today's Iraq to ensure a balanced mix of public and private participation to achieve economic growth. An agricultural development policy should increase farmers' access to subsidized credit, infrastructure, extension services, improved inputs and technologies designed to assist small farmers to achieve high productivity and higher levels of income.

The following are some suggestions to improve and remedy some of the failures of the credit market that plagued rural credit in Iraq during the last four decades.

1. The Ministry of Agriculture and the Agricultural Bank should consider setting clear rural credit policies for short, medium and long-range loans. Medium and long-range loans can be effective in encouraging crop diversification. Beyond that, special attention should focus on building infrastructure. No amount of accessible credit can induce a subsistence farmer to grow cash crops, for example, if there is no place to store the crops nor roads or transportation facilities to reach the market.
2. The Ministry of Agriculture should propose that the co-operative model be reinstated to help create cohesion out of disarray. Rural co-operatives are established in man developing countries for the purpose of achieving increased agricultural production, higher farm incomes and enhanced market competitiveness. However, in this new incarnation, the government should insure that the basic principals of co-operation are applied to create a reasonable environment for co-operatives to succeed. Co-operatives should not be reinstated simply for the sake of establishing co-operatives. Rural co-operatives are established in many developing countries for the purpose of achieving increased agricultural productivity, higher farm incomes and enhancing the competitiveness of the agricultural markets. The co-operative model can serve as a useful medium in which to supply subsidized credit to the small farmers in rural areas. Reliance on formal subsidized credit is essential at this stage. However, to maintain a truly independent co-operative in the long run, the co-operatives should develop their own internal resources to insure autonomy and financial viability.

3. Democratically elected management in can contribute to the future success of newly formed co-operatives. They can identify and broker joint collateral packages to reduce default possibilities and ensure timely payment of loans. Co-operatives have a role to play in the development of civil society; they enforce democracy and contribute to the development of competitive markets.
4. The Agricultural Bank should be independent of the Ministry of Agriculture to avoid political manipulation.
5. Sufficient funds should be allocated to the Agricultural Bank since it is the primary source of institutional rural credit. Moreover, the Agricultural Bank should develop quantified objectives and practical processes to estimate the need for and nature of the credit to be disbursed across rural Iraq.
6. The Agricultural Bank should address the timely collection of its loans. It would need to implement efficient, ongoing loan supervision at the village level. In addition, this supervision should ensure full geographic scope covering all rural villages receiving loans.
7. The Agricultural Bank would need to work more closely with both extension services and the co-operatives' management to educate farmers in the new realities, particularly that loans are not gifts from the government. The extension services should educate farmers that there is no link exists between securing a loan and supporting the politics of the government. The co-operative's management should inform members that defaulting on loans jeopardizes their chances of receiving future loans.
8. The decision on loans granted to individual farmers should be made at the local village level, assisted by the local Board of Directors of the co-operatives, who are democratically elected.
9. The Agricultural Bank should consider formulating a package of incentives aimed at encouraging their loan administrators to stay in rural areas. Additionally, the Agricultural Bank could provide incentive plan for the timely repayment of loans. These could include interest rebates and access to larger loans.
10. The Agricultural Bank should implement management information systems that enhance the efficiency of controlling and supervising the loans.
11. The Agricultural Bank should consider adopting international best practices for regulatory, accounting and disclosure procedures.
12. The new co-operatives should not be used as government agencies and the Directorate of Agricultural Co-operation should encourage these co-operatives to function autonomously. Historical experience shows that co-operatives contribute best to their members and to their rural society when they are true to their principles.

Prudential Norms and Performance: research issues in co-operative banking in India

K Ramesha

Abstract

The co-operative banking sector in India following a history of government sponsorship and direction which characterizes the whole of the Indian co-operative movement post independence has found itself vulnerable and lacking managerial capacity to respond to the new regulatory and competitive environment effecting financial services following Indian government adjustment to the globalization of this sector. The problems have been mounting since the programme of liberalization commenced in 1991 and has become particularly apparent since the phased introduction commencing in 1996 of the new prudential norms covering capital adequacy, income recognition, asset classification and provisioning norms. There is an urgent need to research and map the relationship between the imposition of general financial sector regulation on the co-operative financial services sector and the particular difficulties the movement currently faces.

Key words

Co-operative Banking, Prudential Norms, Performance, Research, Regulation

Indian co-operative banking – a historical introduction

The Indian co-operative movement, like its counterparts in other countries of the world has been essentially a child of distress. The state's patronage to the movement continued even after 1947, the year in which India attained independence. The independent India accepted the concept of a centrally-planned economy and co-operative organizations were assigned an important role. The policy of the Government towards the co-operative movement was guided by the recommendations of the Saraiya Committee, which stated that "the co-operative society had an important role to play as the most suitable medium for the democratization of economic planning". Since 1950s, co-operatives in India have made remarkable progress in various segments of the Indian economy.

During the last century, the co-operative movement has entered several sectors such as credit and banking, production, processing, distribution/marketing, housing, warehousing, irrigation, transport, textiles and even industries. Though the quantitative expansion has been commendable, in order to get a clearer view, it would be useful to consider the following.

- Historically, Governments and policy makers paid more attention to agricultural co-operatives and thus, the growth and development of the Indian co-operative movement is rather heavily tilted in favour of the agricultural co-operatives in general and, credit co-operatives in rural areas, in particular. In some areas such as dairy, urban banking and sugar, co-operatives did achieve success to an extent but there are larger areas where they have not been that successful.
- The co-operative credit movement in modern India, seems to be a state initiated movement. The state partnership is, perhaps, the unique feature of the Indian co-operative movement. Today, the Government's contribution to the share capital of primary agricultural co-operatives accounts for almost 7.5 percent of the total.
- The state partnership which was conceived as a measure for strengthening the co-operative institutions had paved the way for ever-increasing state control over co-operatives, their increasing bureaucracy and politicization culminating in virtually depriving the co-operatives of their vitality as well as their democratic and autonomous character. This has been acknowledged as a critical co-operative problem since the 80's or even earlier and one of the ICA conferences of that period was devoted to that issue alone. Unfortunately one may reference many countries/sectors where this problem is currently present.
- Dormant membership, lack of active participation of members in the management, lack of professionalism (and absence of corporate governance), undue political and bureaucratic intervention, have made the majority of co-operatives at the primary level almost moribund. Inevitably, this has resulted in weakening the co-operative edifice. The upward transmission of the weaknesses of the primary societies has affected the capabilities of the higher level co-operative

federations in so far as their usefulness to the former is concerned.

- With regard to the agricultural credit co-operative structure, although the quantitative expansion has been quite satisfactory, the movement continues to suffer from structural defects and operational deficiencies. The acknowledged operational deficiencies of the co-operative credit structure have been (I) weak recycling of credit, (ii) poor resource mobilization, (iii) ineffective lending and (iv) poor recovery.
- The agricultural credit co-operative system in general has become rather over dependent on external support in terms of participation in share capital by Government and refinance from the Government owned Financial Institutions.

Co-operative banking in India today

Credit co-operatives are the oldest and most numerous of all the types of co-operatives in India. These institutions may be broadly classified into urban credit co-operatives and rural credit co-operatives. There are about 2090 urban credit co-operatives, popularly known as Urban Co-operative Banks, which constitute the 10 percent of the aggregate banking business and therefore can be regarded as an important segment of the banking system. Rural credit co-operatives may be further divided into short-term credit co-operatives and long-term credit co-operatives. With regard to short-term credit co-operatives, at the grass-root level there are some 92,000 Primary Agricultural Credit Societies (PACS) dealing directly with the individual borrowers. At the central level (district level) District Central Co-operative Banks (DCCB) function as a link between primary societies and State Co-operative Apex Banks (SCB). It should be mentioned that DCCB and SCB are the federal co-operatives and thus the objective is to serve the member co-operatives.

As against the three-tier structure of the short-term credit co-operatives, the structure of the long-term credit co-operatives has two tiers in many states with Primary Co-operative Agriculture and Rural Development Banks (PCARDB) at the primary level and State Co-operative Agriculture and Rural Development Bank at the state level. However, in some states there is a unitary structure with state level co-operative operating through their own branches and in other states an integrated federal level structure prevails.

Credit co-operatives in the post-reform period

The process of economic and financial sector reforms was initiated in 1991, as a step towards a broader process of international economic integration and globalization of financial markets. The first phase of the current reform of the financial sector was initiated in 1992 based on the recommendations of the Committee on Financial System (RBI, 1991). The progress achieved in a substantial, yet non-disruptive, manner gave the confidence to launch what was described as the second generation or second phase of reforms, which focused especially on the banking sector. The report of the Committee on Banking Sector Reforms (RBI, 1998) provided a framework for the second phase of reforms in the banking system. The broad features of the on going banking reforms were; gradual deregulation of interest rates, tightening of prudential standards, increased competition and transparency, improvement of the quality of supervision, partial removal of selective credit controls, assistance to banks in debt recovery and reforms in money and foreign exchange markets. The general objective of the banking sector reforms was to improve the sectors efficiency by introducing an element of competition.

The extension of the reforms, and particularly of those that were connected to the application of prudential standards to co-operative banking institutions, which were an important component of the banking system, was argues to be essential as any weaknesses in the co-operative segment could pose a systemic risk to the whole. Although co-operative banks operate at the district and state level, the urgency for and importance of extending the reforms toward them, need hardly be emphasized if one kept in view their reach and scale of operations. Therefore, the banking sector reforms could be treated as complete only if encompassing the co-operative segment, enabling it to function on sound lines at par with the other banking institutions. Accordingly, prudential standards covering capital adequacy, income recognition, and asset classification and provisioning norms were applied to co-operative banks in a phased manner commencing from 1996.

Co-operative banks in figures

On March 31, 2003, the situation of the Indian co-operative banking sector was the following: 5 out of 30 State Co-operative Banks, (SCB) 102 out of 367 District Central Co-operative Banks, (DCCB) incurred losses which amounted. The gross NPAs of SCBs and DCCBs as a percentage of loans outstanding, on March 2002, were 13.4 and 19.7 (RBI, Report on Trend and Progress 2003 / 2002. A quick inspection of 10 SCBs and 88 DCCBs by NABARD during 2003-04 revealed that some of the weaknesses that continued to affect the functioning of these banks were improper application/implementation of income recognition and asset classification norms, inadequate risk management strategies, deficient internal checks and controls and poor credit monitoring. Further, if one looked at rural co-operatives from a non-financial angle, then also this picture appears to be rather bleak. For instance, on March 2000, the elected management of 41 percent of the State Co-operative Banks, 37 percent of the State Co-operative Agricultural and Rural Development Banks, 21 percent of the District Central Co-operative Banks and 8 percent of the Primary Co-operative Agricultural and Rural Development Banks stood suspended.

The Urban Co-operative Banking (UCBs) segment, which was considered as one of the robust and fast expanding segments of the banking system in early nineties, became one of the weakest with intermittent cases of failures/irregularities. A host of factors could be responsible for this, among which one might include increased competition, tightened prudential, supervision and regulatory standards, multiple control, etc. Although the Committee on the Financial System (1991) had indeed lauded the performance and progress of urban banking segment in the early nineties, today there are apprehensions as to whether these entities will be able to survive in an increasingly competitive environment. According to data of March 31, 2003, the number of UCBs classified as "weak" stood at 944 and 142 of these could not comply with the stipulated minimum capital requirements. The scheduled UCBS as a segment recorded negative net profit during the last three years. During 2003-04 alone, liquidation proceedings have been initiated in 23 UCBs, apart from re-scheduling two scheduled UCBs. Deposits grew by 3.3 percent (as against 10.6 percent for the previous year) during the first half of 2003-2004. Credit, in tandem, declined by 6.1 per cent in sharp contrast to an increase of 2.8 per cent of the previous year. The relatively low deposit growth also speaks of the falling confidence of the general public in co-operative banks, particularly in the UCBs due to the recent untoward incidents. However, nearly 45 per cent of the UCBs, which account for 55 per cent of the deposit base of the sector, are considered to be financially sound (RBI, Mid-term Review of Annual Policy, 2004).

The above analysis, despite its limitations, shows that the credit co-operative movement has become weaker during the post-reform period. It is also true at least to some extent that the co-operative banks have failed to take the cue from the initiatives of RBI in regard to prudential norms. Although co-operative banking organizations have survived, recent trends suggest that they are unable to deliver the expected results. In the present competitive environment, it is imperative that co-operative banks should be encouraged to initiate the process of operational restructuring to ensure their financial soundness in order to be able to withstand the competition, survive and grow. It is important to note that co-operative banks (and the movement) will be able to serve their larger responsibilities that are connected with societal dimensions only when they are financially strong.

Emerging research issues in co-operative banking

Against this backdrop, it is argued that the following three aspects of critical importance need to be considered on a priority basis by the policy makers, regulator/s and co-operators to ensure the survival of co-operative banking in India. Needless to mention, these aspects of critical importance are highly inter-related and call for concerted efforts by all those concerned. The reform measures that were applied to the UCB sector may be classified into three broad categories. First, while recognizing the differences between commercial and urban co-operative banks, the majority of the prudential norms introduced for commercial banks are being extended to UCBs, albeit in a phased manner. Second, certain policy initiatives have been introduced (through Monetary & Credit Policies) to contain the systemic risk emanating from the co-operative sector, in particular from the UCB sector. Finally, the duality/multiplicity of control has been recognized as an irritant to their effective regulation and supervision.

Although, the focal point of the reforms has been prudential norms, steps were also initiated to professionalize the management and the UCBs human resources in general. The author identified several broad areas for further research under three categories, i.e., prudential standards, professional management & governance and supervision & regulation.

Prudential Standards

In 1993, RBI introduced Income Recognition and Asset Classification Norms to UCBs. In 1995, the prudential exposure norms toward single/group borrowers applied also to them. Subsequently, in a phased time frame, the capital adequacy norms (capital to risk weighted asset ratio) was the third element that was added. While the promotion of prudent financial practices has become a sine qua non in the highly competitive globalized environment (in order to safeguard the financial health of the system, in particular of the UCB sector), it should not be forgotten that such standards were contrived essentially for commercial banks.

Although, the notion of a code of good practices is intuitively appealing, the temptation to prescribe universally valid model codes which, however, do not allow for differences in the institutional development, the legislative framework and more broadly, the different stages of development to be considered, should be avoided. In other words, while there is no dispute that UCBs should be subjected to prudential standards (capital adequacy, asset classification, income recognition and provisioning norms), it is not yet clear, whether the prudential standards prescribed for commercial banks would work without distorting the co-operative character of UCBs.

For instance, capital is widely regarded as an index of the risk taking ability of a financial intermediary and therefore, a minimum capital requirement for an urban co-operative bank (to conduct banking business) may seem to be justified in order to ensure stability in the financial system. If one looks at a co-operative credit society/bank, with a typical co-operative created on the basis of self help and mutual help, then possibly its members (usually with limited means) may not be able to raise the required capital. If the capital base is to be strengthened, these banks will have to start dealing with non-members (or nominal members) on a large scale and perhaps may have to shift from "surplus" to "profit". It is worth mentioning that in India, urban co-operative banks though on par with commercial banks with regard to prudential standards, are not permitted to boost their capital base through sub-ordinate debts. Further, there are ceilings on the value of the individual share holdings which have not been revised for quite a long period.

Secondly, in order to ensure the credit co-operative societies'/ banks' adherence to the prudential standards, the regulator's frequency (and scope) of intervention should increase and, thereby, inevitably affect their co-operative character. In this regard, in India, the regulator's intervention has indirectly infringed upon the functional autonomy covering areas like share-linkage, credit, investment, deposit etc.

Thirdly, in the name of protecting the interests of the depositors (the majority of whom are not members of co-operative banks), the prudential standards were not only extended but even the professional content in the management committee of the urban co-operative credit societies/banks was also stipulated. While one cannot remain ignorant of the role of the Government in the promotion and development of co-operation in India, prescribing the number and qualification of the nominee directors may impair the co-operative character of the bank.

Fourthly, the strict entry norms in terms of minimum capital and membership requirements as it prevails in India, prevent the birth of new credit co-operatives and constrain the existing societies in so far as their expansion is concerned. Fifthly, the introduction of the same prudential standards blurred the difference between urban credit co-operatives/banks and commercial banks and possibly, the former may have to progressively imbibe the character of the latter, and possibly cause an identity crisis. There could be several such dimensions as discussed above. Therefore, it appears that the benefits of the prudential standards to urban credit co-operatives/banks came at a cost. The cost, needless to mention, is the dilution of the co-operative character (in terms of adherence to the principles). Hence, following the above discussion, four major issues (or broad areas for investigation by researchers/scholars interested in co-operative banking) are listed below.

a. How relevant are the prudential standards (i.e. norms of Basle Committee – accepted and implemented by most countries) to co-operative credit societies/banks?

b. In countries where prudential standards have been extended to urban credit societies/banks, has the desired results been obtained? Can urban credit societies/banks adhere fully to prudential practices as defined?

c. What are the implications of extended prudential standards to urban credit societies/banks co-operative character?

d. Is it possible to derive a set of prudential norms especially for urban credit co-operative societies/banks from the Basle Standards?

Professional Management and Governance

Good corporate governance is critical to the efficient functioning of any entity and even more of a banking entity. Thus, the need for professional management and healthy governance practices in urban credit co-operative societies/banks in the present competitive environment is self evident. Hence, the management of a financial intermediary, co-operative or commercial bank, irrespectively of its size, requires highly competent human resources either paid staff or elected management. The framework for good governance and professional management in the co-operative sector should essentially emanate from the guiding principles and the given legal framework in different countries/states.

However, in India, co-operative banks' directors/managers are frequently suspended and Government officials are posted or nominated onto the board. Unfortunately this trend has increased in the post reform period. Quite often the reason quoted is the lack of qualified and competent directors and the protection of depositors' interests (the majority of whom are not members). While this is true, to some extent, the solution to this problem is certainly not the Government's intervention as it seriously impairs the co-operative character. More than 200 urban co-operative banks were identified as weak/sick banks by the regulator at the end of March 2003.

According to the co-operative philosophy/principles any individual member can get himself/herself elected to the management committee of a co-operative bank. It is this management committee which is entrusted with responsibilities such as risk management - policy/strategy, credit and NPA management, investment management, marketing plan/strategy, asset-liability management etc. It should also be noted that the very concept of banking (financial intermediation) is undergoing critical changes in the contemporary competitive environment and the conventional management framework with which co-operative banks are comfortable may not be sufficient. Given this, it is doubtful whether the elected management (as per the existing provisions of co-operative legislation and stated principles) by individuals without sufficient knowledge/experience in financial markets or management can be at the helm of affairs of a co-operative bank?

There is an urgent need to ensure that in co-operative organizations, the system of governance including the size and composition of the board of directors (or elected management) is driven by the purpose and objectives of the business. In this regard, the following issues/areas may be of some interest to co-operative researchers.

Is it possible to develop a framework of good governance for urban credit co-operatives/banks within the guiding principles of co-operation?

How can we ensure that the system of governance including the size and composition of the board of directors are in consonance with the purpose and objectives of a co-operative bank? What level of awareness and competencies are required for the board of directors for the effective management of a co-operative bank and how to ensure that within the framework of co-operative principles?

Supervision and Regulation

Currently in India, urban credit co-operatives/banks are subjected to a dual control, which means that the administration related aspects are supervised and regulated by the State Government and the banking operations are supervised and regulated by the central bank of the country. This has, inevitably, resulted in overlapping jurisdiction of the state Government and the central bank of the country. Moreover, a clear-cut demarcation line of the financial and administrative areas for regulation is almost impossible to be drawn. Even if it were possible it would definitely act as an impediment to an effective supervision.

While the central bank of the country has, under the Banking Regulation Act, the wherewithal to deal with crucial aspects of commercial banks functions, in the case of co-operative banks it requires the intervention of the Registrar of Co-operative Societies. Given the number of urban credit co-operatives/banks, the central bank of the country is not in a position to effectively supervise them. Thus, the duality of control not only affects the quality of supervision and regulations, but also the effective functioning of the urban co-operative banking sector.

Needless to mention, under this regime of dual control, that urban co-operative banks may turn out to be neither co-operative nor commercial banks. Below are some areas of concern need to be researched.

a. Which type and level of supervision and regulation is required for urban credit co-operatives? Is it possible to draw an outline of the supervisory framework?

b. Is the existing supervisor/regulator (central bank of the country) appropriate for regulating and supervising the activities of urban credit co-operatives/banks?

c. Can we think of a separate agency (or even regulator) for urban credit co-operatives?

Conclusion

While the progress of the co-operative movement in India in general, and co-operative banking in particular, has been significant, the movement is clearly having difficulties in adjusting to the post reforms period. It seems the extension of reforms particularly in prudential standards to urban co-operative banking has provided substantial scope for external intervention which, in the process, has affected its co-operative character in terms of its adherence to the co-operative principles. More importantly, there are indications suggesting that the Indian credit co-operatives as a segment have become weak during the post-reforms period. It is also true, at least to some extent, that co-operative banks have failed to take the cue from the initiatives of the regulator in regard to prudential norms. Although co-operative banking organizations have survived, recent trends suggest that they are unable to deliver the expected results without substantial change in organizational culture and operating standards.

In the present competitive environment, it is imperative for co-operative banks to be encouraged to initiate the process of operational restructuring in order to ensure their financial soundness so that they will be able not only to withstand the competition but also to survive and grow. With regard to the extension of reforms to the co-operative banking segment, it is not clear, yet, whether the same would ensure its soundness and stability. Although the promotion of prudent financial practices in urban co-operative banks has become a sine qua non in the modern competitive environment, one can not afford to ignore that such practices were contrived essentially for commercial banks. The particular role and purposes of co-operative banking particularly in their capacity to mobilize micro-finance and provide an ownership base for the poorest strata of society at the heart of the economy should not be underestimated and indeed it is imperative that policy makers take full account of these issues. Further co-operative bank research is a priority. The most important araes are prudential standards, management & governance and supervision & regulation.

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Time for a new addition to the consumer co-operative movement

Edgar Parnell

Consumer co-operation

When the early co-operators of Rochdale set up their first co-operative shop in 1844, they were primarily motivated by a desire to get unadulterated food and to free themselves from exploitation by unscrupulous traders. Their solution was to provide their own retail service where quality and fairness could be assured. In the 21st Century in many parts of the world the consumer co-operative retail based business model has suffered setback and in some countries has ceased to exist at all. Whilst private sector retailing has grown to global operational levels few national consumer co-operatives have been able to go beyond the confines of their country of origin. Unscrupulous traders remain ready to exploit consumers, and these are not necessarily small businesses but very often large-scale national and multi-national concerns.

In a more positive vein there is a rising tide of consumer awareness concerning ethical consumption concerned with health, environmental and justice based issues in which the British Co-operative Bank has played a leading role in promoting. The British Food Retailing arm of our consumer co-operative movement has established benchmarks for consumer standards in both health and labelling. The Japanese consumer co-operative at Kobi sets the global standard in fresh food, quality assurance, health merchandising, supply chain management, energy conservation and consumer education in a cultural as well as specifically informational content.

However, it is easy by a process of monopolistic practices, confusion marketing and advertising budgets that consumer co-operatives just cannot match for co-operative established benchmarks to be missed by the average consumer. Governance processes and other institutional issues are also making it hard for the best retail co-operatives to translate their local /regional competencies onto the global marketplace. In addition to these barriers facing traditional retail based co-operatives, consumers consume goods and services in most countries which in any case are just not provided for by their retail based consumer co-operatives.

A new initiative

There is a clear need that is not being properly addressed for greater consumer justice concerning the quality of the products and services they receive across the full range of consumption. Such a co-operative focus would both raise consumer awareness of the standards that are available as well as help individuals seek redress for the failures and misleading presentation of goods and services. This is why the Consumer Justice Co-operative needs to be launched. It would not be an alternative to retail based co-operation nor a diversion to the Fair Trade and environmentalists lobby but rather an added framework to reinforce the overall struggle for justice in a variety of forms that unites the whole co-operative movement.

In today's world, only when people co-operate in large numbers, sufficient to counterbalance the power of big business can consumers expect to make any real difference to the way that many businesses treat their customers. Many people feel an overwhelming sense of powerlessness when in dispute with faceless companies, often global in scale, with their headquarters based in a different country. It is totally frustrating to be fobbed-off by junior personnel or unable to speak to a 'real person'. Increasingly, companies are making use of automated response systems designed to deter complaints and recent systems screen-out calls from persistent complainants. Many companies are getting away with making the lives of their customers (victims) a misery, with impunity, and it is about time that the tables were turned on these offending businesses.

Legislation appears to have almost reached the limits of its capacity to protect the consumer when dealing with the bad practices of many companies. Legal action is rarely an option for the individual due to the high costs and the inordinate length of time it takes. Even where there are established statutory or industry sponsored 'watchdogs', these often seem incapable of securing the necessary fundamental change to the offending companies. The government's consumer service, while providing useful information, is inherently timid and toothless when addressing specific complaints. Our politicians seem to be either more interested in protecting big business or are 'running scared' when it comes to confronting major companies that are investing in facilities and providing jobs. All too often frustrated consumers with legitimate complaints about poor quality goods and services, simply 'give-up' in the face of a lack of response or avoidance tactics, so any complaint soon becomes a lost cause.

Individual complainants can sometimes win minor victories, although, significant change in the behaviour of substandard businesses only happens when the combined power of dissatisfied consumers is brought to bear. Some groups of consumers have sought to address specific consumer issues, such as: bank and credit card charges, telephone scams (aided and abetted by telecom companies) and so on. However, such groups act in isolation and often have great difficulty in pressing their case. There are also several individuals and organisations that started out as genuine consumer action champions, but the difficulties facing small-scale campaign groups have resulted in 'burn-out' or acceptance of commercial financial support, which compromises their independence.

The Consumer Justice Co-operative

The purpose of the Consumer Justice Co-operative (CJC) is to combine the power of those people who are: a) recipients of poor quality goods and services and/or b) victims of unacceptable practices of companies. CJC will highlight the causes of complaints and act as an advocate on behalf of its members; it will support and provide networking for existing consumer action groups and, where necessary, organise new groups to help them pursue their complaints against offending companies. CJC will be a completely independent organisation and will only seek recourse to the law when other efforts to secure necessary changes in company behaviour have been exhausted. CJC will provide the following services to its members:

1. Direct help for individual complainants to get redress for their grievances against businesses.
2. Support action groups where the same problems are affecting members and not being resolved, in bringing the necessary pressure to bear on the offending business so they respond positively. (Naming, shaming plus more radical measures when needed.)
3. Offer group legal costs insurance policy covering consumer disputes.
4. Provide vital information to members which aids their purchase decision-making and help prevent them becoming victims of scams etc.
5. Address wider issues of consumers' rights, affecting members, on their behalf.
6. CJC will publish a web-based newsletter highlighting the complaints of members.

It is anticipated that clusters of members with similar complaints will be organised into groups or networks and assisted by research and support from the CJC office. The outcomes from the various campaigns shall be reported back to members via the newsletter. Members will be recruited, both as individuals and as groups, from existing groups of dissatisfied consumers and from members of organisations with an interest in supporting the aims of CJC, for example: trade unions, women's organisations and similar special interest groups.

Organisation of CJC

CJC will be financed by annual subscriptions from members. Initially, voluntary group leaders will undertake much of the work, so at this stage the operating costs of CJC could be relatively small, but as the membership grows full-time professional staff will be required. Member share capital is also needed to finance the essential fixed assets, in particular IT systems and hardware. Donations and grants will be accepted, always provided these come without 'strings attached' that could jeopardise the independence of CJC. Supplying additional services, such as: in-depth research commissioned by specific groups pursuing specific actions against offending companies, may also raise income. It is anticipated that CJC will act as a trustee for an associated, but separate, educational charity that will provide training to consumers so as to improve their capacity to obtain value for money and secure justice from the suppliers of goods and services.

A business plan is being developed and a prospectus will soon be made available to potential members. An intensive recruitment campaign is also planned, which will be launched via the World Wide Web and through the media. As soon as a number of high profile causes are championed by CJC it is anticipated that even more significant numbers of members will be recruited. Very soon a steering group will be selected to carry forward the initial development of CJC and the registration of this new co-operative. Anyone interested in getting more information about the CJC and or becoming involved can make contact via the website: www.consumerjustice.org.uk

Risk and Reward: assessing stakeholder risk in a member based organization

Roy Allen

Introduction

The purpose of this paper is to commence a discussion on the merits of assessing and calculating the various elements of risk associated with traditional member based organizations and their total compliment of stakeholders: members, employees, suppliers, customers, investors or providers of capital and their geographic community.

There are many forms of risk both economic and value-driven. Though this paper will introduce and discuss these and more, its primary goal is to begin a dialogue on whether and how generally accepted quantitative research principles, such as those practiced by actuaries in determining life insurance and annuity premiums or risk assessment strategies developed by energy based companies to deal with environmental concerns, can be laterally employed in member based organizations to first qualify and then quantify individual and co-operative risk among associated stakeholders. I will argue below that by understanding and employing such customized tools, a member based organization may become better prepared to structure and or restructure their entire stakeholder recruitment, development and retention programs and achieve a stronger defensive position against risk.

Key words

Risk Assessment , Risk Management

Forms of risk

Value-driven risks vary among stakeholders, indeed they may vary greatly among members of society as a whole. Societal risks and on a much more micro basis a specific community's risk, may in fact be very different than an individual risks (Harden 1968). Speaking of grazing rights, Harden determined that while a pasture may be a common resource, it is not a common good. In fact, if every individual votes and /or exploits his or her personal rights and /or interests in or to the common resource (the pastureland), the affects on the community at large would be disastrous. The community must first qualify the primary baseline criteria important to them. This may include but is not limited to the following factors. The pasture land (resources) available; the desires (needs) of the individual farmers; and qualitative (values) issues such as environmental stewardship, fair trade and sustainable succession or development issues; the community can then best exploit the deliverables (opportunity) defined via scientific quantification (risk/reward).

Seeing the economic and social as a whole rather than opposites

Assessing value-driven risk, whether in terms of social or economic value added and their respective methodologies required to sustain the organization or community itself, can never be successful by unilaterally surrendering to either the economic or social master. Value-driven risk is about a shared purpose that defines and expands both the economic and social dimensions. This is and must remain the essential differentiation in the co-operative context. Once the values are defined, documented and agreed to, the quantification methods should be clear and assessing risk becomes academic, (Sullivan 1982) using the following steps.

1. Find the data - mathematical, behavioral, historical and natural
2. Catalog and correlate the data
3. Evaluate and communicate the information

There is simply no way a member based organization or any other can present a responsible case for measuring best practices or lost opportunities without following the same three steps.

Purpose is prior to process for determining leading values

What is the primary or collective purpose of the organization? Who does this purpose matter to? Who should it matter to? Who is or will be effected by its success? In what proportion will the various stakeholders be at risk in the event of such success or failure - socially and economically? What is the expectation of the stakeholders as to the longevity of the organization? For example, in a typical real estate investment club, the term of relationship among the member owners (social or economic) may be specifically set at 5-20 years. Co-operatives cannot correctly evaluate risk without clear statements of purpose (mission) related to their various stakeholders.

Ownership is an important issue

With a worker owned enterprise, the mission may be to provide sustainable employment for several generations. Using the same investment strategy or risk assessment model for different forms of ownership with contrasting missions would be unwise, chaotic and prove unsuccessful in one and possibly both cases. Beginning with the collection of data, a researcher would need to profile a specific subset of member based organizations for there are many - social, religious, educational, etc. And, once the profiling begins, it must continue in its collection of data for as long as the duration of the organization. The world does not stand still. It changes daily and the affects of those changes define the future information required to sustain the organization.

Perhaps, for preliminary demonstration purposes, targeting both a consumer based membership and an employee owned enterprise would be helpful in defining common and also their contrasting goals and the requisite procedures for customization. A consumer co-operative aggregates the purchasing power of individuals and families to provide cheaper prices for goods and services and/or to obtain goods and services that would otherwise be unavailable. However, that is where the commonalities stop. Each consumer co-operative often adds their own personal touches through their value agenda - whether it be environmental, economic justice (fair trade), educational, or price.

Their unique characteristics must define their risk assessment formulas. Organizationally, consumer co-operatives can either operate as a community enterprise or a buying group among particular individuals (Co-operative Development Services, 2006). However, their purpose is neither singular nor exact. The community dimension may add local competencies that represent competitive advantage and hence also represent areas of risk.

But whatever the economic or social priorities its processes need to reflect social impacts thus it operates in a socially responsible manner focused on such matters as employee benefits or environmental advocacy as its primary purpose. What therefore, should its' risk assessment and stakeholder investment strategies be? They must be qualified by the defined mission of its membership. Each organization is unique. Risk assessment criteria is no different. In a retail co-operative, the purpose may be for all buyers of groceries in a specific area to combine their purchasing power and buy their desired items (organic, locally grown, wheat-free, vegetarian, etc.) in bulk with opportunities for quality and savings. At the end of the year, after all expenses are paid the customers who become member owners get to participate in any surplus revenue that is leftover in the form of distributions.

Another form of consumer co-operative, with different goals, is the credit union which was originally developed in the nineteenth century. These associations have two primary purposes. Firstly, the mobilisation of small savings and secondly, the provision of access to small loans and capital sums to individual members for their greater benefit and welfare and that of their community. Sometimes competition evolves between factionalized credit unions demographics so that they forget that they are really consumer co-operatives (what's best for the membership) and that institutional interests should not drive policy. Within the co-operative credit union their can also appear to be tensions between the depositor-member-owner, or the creditor-member-owner (I refer to their relative balance of interests, as in fact creditor-members have to be savers in credit unions). Here there is an economic risk that is absolutely quantifiable. But the success of low default rates that characterise the best managed credit unions may well be due to the individual creditors perceived social risks in their cultural or social context. Though both retail, and other procurement co-operatives and credit unions are based on the consumer co-operative model, their missions may incorporate a variety goals depending on the socio technical and cultural circumstances. When the mission itself is directed into more than one purpose, the methodologies practiced to define, develop and sustain that missions risks must follow suit.

Finally, we consider the worker-owned co-operative or employee owned enterprise. A worker co-operative is defined as follows:

> *"The main purpose of a worker co-operative is to provide employment for its members. Each member pays a membership fee or purchases a membership share, and has one vote regardless of how much money they have invested in the co-op. The co-ops' assets are collectively owned and surplus earnings are allocated to the workers according to policies established by the co-op,*

often in proportion to hours worked by members and with limited return on shares" (Ontario Worker Co-operative Federation, 2006).

Such a definition of purpose has clarity and simplicity for the purpose of risk assessment but other forms of employee ownership may present a more complex picture. A different form of worker owned organization is the ESOP or Employee Stock Ownership Plan that is used primarily in the United States. According to the National Centre for Employee Ownership (NCEO), the purpose is quite different. An employee stock ownership plan (ESOP) is a type of tax-qualified employee benefit plan in which most or all of the assets are invested in stock of the employer. Like profit sharing, which is governed by many of the same laws, an ESOP generally must include at least all full-time employees meeting certain age and service requirements. Employees do not actually buy shares in an ESOP. Instead, the company contributes its own shares to the plan, contributes cash to buy its own stock (often from an existing owner), or, most commonly, has the plan borrow money to buy stock, with the company repaying the loan (National Centre for Employee Ownership, 2002).

The result of the above purpose is that the employees, since they do not actually pay for the shares are not accountable for the investment. It is the corporation that actually borrows the money and holds responsibility for the risk. If there are other financial shareholders, their economic investment too is at risk - but, the risk may be different determined by the purpose of the investment - social or economic. However, the employees also have a risk, that being one of lost opportunity in the event that their rewarded shares for time spent on the job do not rise in value. It is easy to conclude that each organization needs an assessment tool that not only quantifies the risk, but qualifies it.

A general definition of risk

According to a George Washington University report on Dam Safety,

Risk = probability x consequence or in a more elaborate expression we define risk as follows: Risk = threat 3 x vulnerability x {direct (short-term) consequences + indirect (broad) consequences}. (George Washington University, 2006)

Their assessment is a simple one. What are the benefits? What is the threat of failure? What is acceptable risk? What is not? What are the short term and long term opportunities, consequences and the vulnerability of the plan compared to other public policy. Then, they incorporate the science of risk assessment into the framework of stated public aspirations in an attempt to balance and/or improve stakeholder options. It is sometimes like the pastureland conversation discussed earlier in this paper. Does the public good created by conserving or exploiting the common resource outweigh the individual sacrifice? What are the needs of the community, the available resources to service the needs, the probability of certain events, the risks associated with both action and inaction, and the opportunity for stakeholder success? Often, the winner in a public works project is focused on economic gain, not the potential social cost.

The medical field looks at things a little differently. According to an article published by the American Academy of Ophthalmology (Karmel, 2003) and quoting Paul L. Kaufman, MD.

"The computer may spit out a risk analysis, a percentage risk, but you still have to make a decision with the patient.........There's always the art of medicine,where you have to individualize and say, 'I know what the formula says, and this patient is outside the box.' You still have the art, but you want the art to be overlaid on a solid scientific basis....... This is the way medicine should be practiced."

Perhaps his endorsement of scientific quantitative risk analysis, as well as its qualitative application can be adopted by member based organizations as well. Real or perceived risk cannot be managed without a defined purpose and assessment cannot be accomplished without proven scientific methods - data collection, statistical proofing and the utility of mathematical modelling. However, once the data is collected, the ultimate decision making process must fully take into account the stated organizational purpose. So too must the various stakeholder positions regarding equal, or the much more hotly contested issue to quantify - equitable distribution. An interesting case for further study might include an agricultural co-operative. A typical stated purpose looks like this: "We will seek to maximize net returns at the farm by preserving and enhancing milk markets and milk-marketing relationships, and by providing services and programs that create real economic value (aaowebsite, Dairylea 2006). However, ask three different farm members what their measurement of success is and you will likely get three different answers. Can the co-operative strategy fail to take account of specific risks faced by individual members?

How are market preservation goals affected by existing strategies for economic gain? If a regional economy, by measurement of its gross domestic product, determines that a billion dollars can be made or lost over a ten year period if the market remains at status quo, what is the present investment required to keep the co-operative vital? The how is not as important as is the what and the why? For example, it is generally accepted business knowledge that if you are a $100,000 firm and want to become a $1,000,000 firm, you cannot use the expense calculations of the former, but must adopt those of the latter. If the industry requires a three percent expenditure for marketing, the managers of the firm cannot budget $3,000 (3% of 100,000), but must discover a way to deliver $30,000 (3% of 1,000,000) to the budget prior to the revenue ramping up - or, they will never reach their objective. The same budgeting adjustments will apply to training and production technologies. How might this be achieved without risking the existing business?

Sharing risks

One way would be to contact suppliers who may benefit from the growth and negotiate a revenue sharing agreement on all income growth over the present level of $100,000. This will not cut into the suppliers present profitability, but may secure future business revenues. Another strategy may be to prepare a tangible and intangible asset analysis to determine whether the firm might have a tradable resource (time or proprietary process) that can help them fund a larger marketing campaign. They know why they need a bigger budget - they want to grow. They know what they need - 3% of the targeted revenue. Now, they simply have to discover how to gather the resources and assess the associated risks - real or implied. Why + What + How - Risk = Opportunity.

Complex missions responding to a complex marketplace

Subsequent break-even and profitability analysis will ultimately be determined by the margins of the individual participants. However, in our world of value-added market opportunities (organic milk, premium ice cream, fair trade coffee, range fed chickens, green technologies, life time employment, etc.), the why is front and centre - consumers respond to more than price. Service, quality, experience, and community also can contribute to a better life - for the company and the consumer. Therefore, leaders must be prepared to deliver sustainable multiple outcomes or surrender the playing field to others who can.

In traditional business accounting, the balance sheet and/or profit and loss statement are used to provide managers with a clear assessment of return on invested resources - (time, money, labour, equipment, etc.). However, the balance sheet will not reflect non-financial risks such as climatic, political or social activities. Yet, these calamities or opportunities, depending on the event and twist of fate, can often effect a project more dramatically than good or bad fiscal strategy. How does the gas and oil business prepare for these non business events? To begin with, it must assess as best as possible, the prevalent risks that can affect its survival which may typically be thought of as “beyond control”. Then, it must educate managers, shareholders, investment analysts and workers how to better understand these risks and challenge them to develop assessment and strategic solutions for dealing with them. Hybrid insurance products reduce the risk of sudden changes in climate - such as typhoons, earthquakes and flooding. Social calamities can be planned for by investing in education so that all affected stakeholders understand the complexities of demand, process and expected outcomes of a particular project.

Finally, events caused by anomalies such as political ideologies can be planned for using diversification strategies and/or funding research on alternative energy (back-up plan technologies). What might happen to energy industry stocks if the general public simply woke up one day and decided to “vote with their wallets” to force a peace initiative in the Middle East? Might this happen? Probably not, but the environmental risk, those being caused by man or nature, must be acknowledged and assessed when developing a comprehensive sustainability model (Walker 2005).The best accepted environmental risk assessment tool in the oil and gas industry may be precaution (McLaren 2000). That too, however, may not necessarily be as useful in developing a sustainable nation state at the macro-level or local community member based organizations at the micro-level.

Conclusion

Only by funding, defining and acting upon their own qualitative research, can value-based organizations develop quantitative risk assessment tools which integrate commercial and sustainable social success (Business Social Responsibility, 2005). Calculus and probability theory are key components of assessing risks and assessing risk is the foundation of actuary science. However, risk can be both present and pending. What is relevant now is not necessarily more so than that which might occur tomorrow. It is a matter of researching the known, calculating cause and effect of deliberate action or inaction, engaging critical thinking, discussion of probable future events and drawing knowledge based conclusions to determine the mathematical possibility of any or all of them occurring during the same business cycle. Member based organizations deal with the same complexities as any other participant in a global economy - fiscal, environmental, stakeholder rights, regulation and sustainability. They must therefore become as diligent and vigilant in exploiting the professional sciences adopted by their competitors. Ensuring a clear understanding of the risks associated with the whole socio-economic mission of co-operative enterprise as a business risk is to recognise not a duality confusing and distracting management, but a potential quality and brand advantage of enormous significance for the shape of the market economy and civil society. Co-operative risk assessment by the same token needs to recognise that risks to open markets, the erosion of civil society and break down of community represent serious risks to the continuation of the co-operative business model.

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The Credit Co-operative Movement in Myanmar: an application of the "thrift and credit co-operative evaluation methodology".

Gus Poston

Abstract

There are approx 400,000 members of thrift and credit co-operatives in Myanmar. Most members are public servants, but the movement is becoming increasingly strong among traders and entrepreneurs. This case study describes the movement and indicates priorities for development.

There is likely to be rapid growth in the financial services sector in Myanmar once macro-economic conditions become more favourable. The thrift and credit co-operative movement is the only provider of financial services for many people and is well placed to lead this growth, so long as it develops its capabilities now. The priorities are to (i) develop the national and regional support structures so they are more responsive to societies' needs, (ii) change the culture of the leadership of the societies, focusing on independent growth and member needs, and (iii) expand societies' products and membership so they achieve scale.

Key words

Credit Co-operatives, Culture Change, Development, Evaluation Methodology, Institutional Support, Leadership, Membership, Myanmar, Strategy.

Approach

This study of the credit co-operative movement of Myanmar followes the 'Thrift and Credit Co-operative Evaluation Methodology'. This methodology, described in outline in Fig 1, can be found at www.NewThinking.org.uk/toolkit.htm, along with templates and evaluation forms. The methodology creates a baseline description of a co-operative movement, identifies strategic priorities and compares the performance of a co-operative movement with peers. The rest of this case study follows the framework of the methodology.

During the investigation the author visited a number of co-operatives, as well as Central Co-operative Services (CCS) and the Department of Co-operatives. The author thanks CCS for assistance in these visits. *The Methodology described in Fig 1 below at section A provides a framework for the descriptive sections of the Thrift and Credit Co-operative Movement and of its various segments.*

Base description of the co-operative movement in Myanmar

Co-operative societies have a long history in Myanmar. The first co-operative societies were founded in 1904 to provide savings and credit services, similar to the model applied in other South Asian British colonies. Under the Co-operative Law of 1970, co-operatives were closely controlled and monitored by the national government, along socialist principles. With the change to an open-market economic system, a new law was passed in 1992 – one of the most liberal co-operative laws. Since then, the government has been reducing its influence in the day to day operations of co-operatives.

There is a national support structure, led by the Ministry of Co-operatives.

The co-operative movement has four levels. Each level conducts commercial activities, which may include trading, service provision inter-lending, etc. Each level primarily offers services to its owners, but may also work with other parts of the movement (e.g. the Tertiary Credit Union serves the Secondary level Syndicates, but also Primary Societies).

There are 17,092 primary societies based in villages, towns, factories and government institutions. Their membership ranges form 15 to 3000 in agricultural co-operatives, industrial co-operatives, general trading co-operatives, education employee co-operatives, and credit co-operatives.

The co-operative movement has founded a commercial bank – the Co-operative Bank, founded under the commercial banking legislation. It is the result of the merger between the previous Co-operative Bank, Co-operative Promoter's Bank and Co-operative Farmer's Bank. It currently has 15 branches (5 in Yangon Division, 5 in Mandalay Division, 3 in Pego

Division, one in Shan State). The Co-operative Bank is owned by the co-operative societies and private shareholders. It offers normal commercial saving and loan products, lending with collateral, both to the co-operative movement and other customers. It is said to focus on larger, commercial operations.

The Central Co-operative Society (CCS) is the Apex level body of the co-operative movement. CCS is based in Yangon and recently moved to offices separate to the Ministry of Co-operatives, although it still works in partnership with the Department of Co-operatives and with the approval of the Ministry of

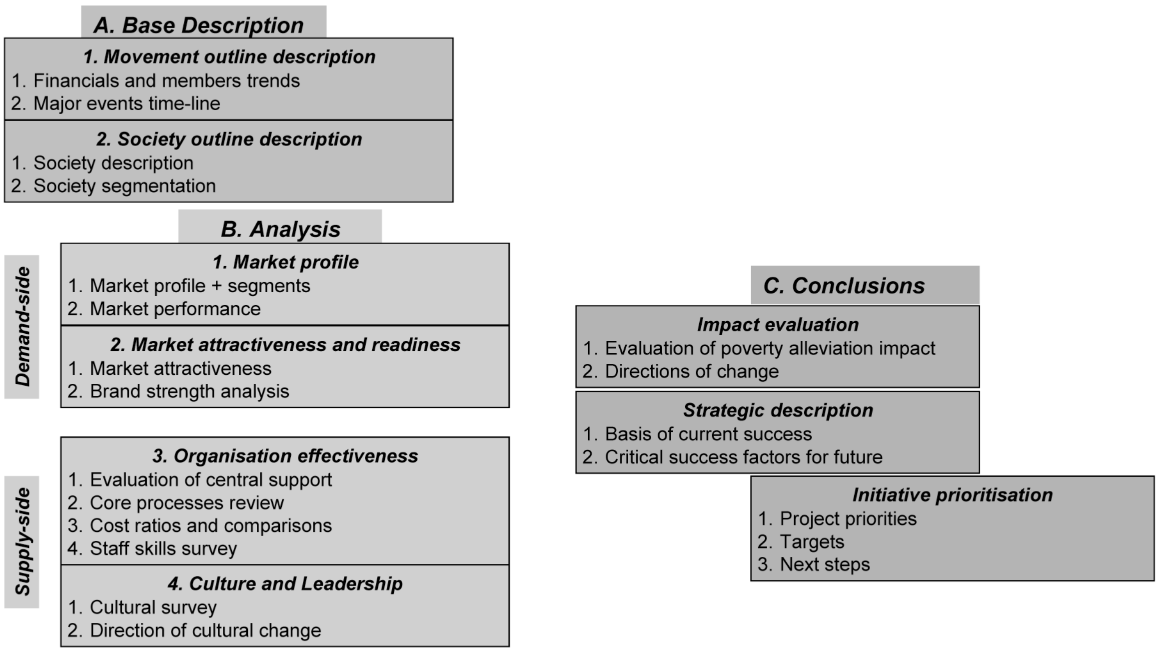

Fig 1: 'Thrift and credit co-operative evaluation methodology'

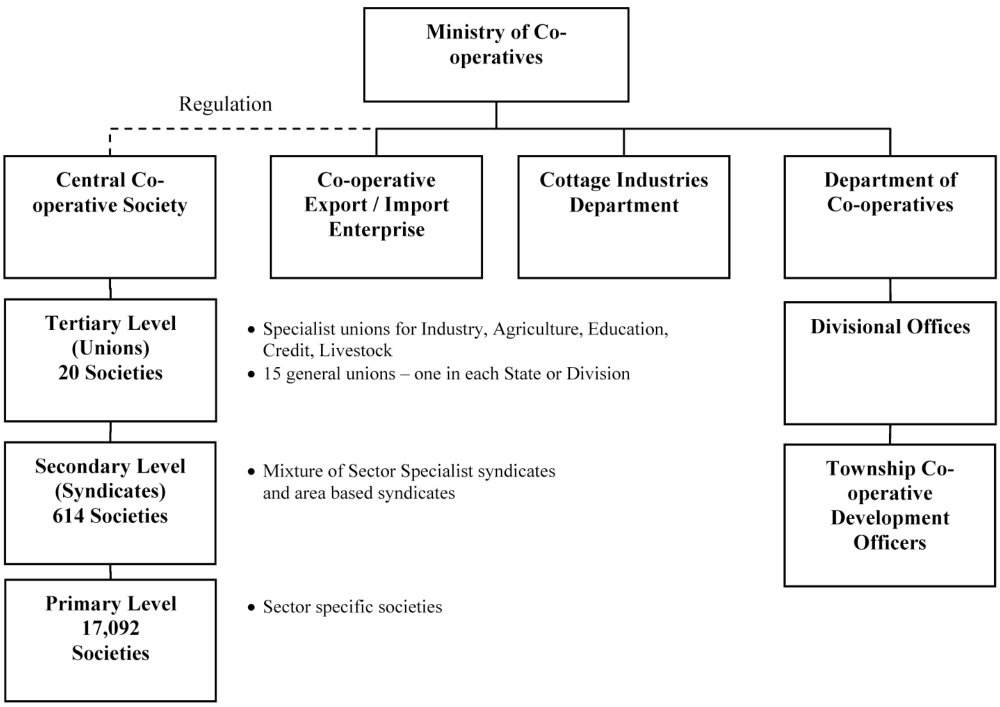

Fig 2: Structure of co-operative movement in Myanmar

Co-operatives. It is responsible for mobilising and supporting the whole co-operative movement and is currently expanding its activities.

CCS has had a new organisation structure since mid 2006, with departments responsible for Research and Planning (research into activities of co-operatives and planning CCS's future activities), Business Development (export promotion), Education and Training (initially focusing on CCS staff), International Relations (relationship with ICA Asia Pacific Office and ASEAN associations), Budget and Admin. Additionally, the CCS plans to develop a micro-finance capability – potentially in a separate department.

The Department of Co-operatives is responsible for regulation, training, organisation, supervision, planning, inspection and liquidation of co-operatives. The head-offices of the department are in Naypyidaw, the new capital of Myanmar. There are Divisional Offices in the major towns and Township Co-operative Development Officers in each township who work with individual co-operatives.

The Co-operative Export and Import Enterprise, reporting to the Ministry of Co-operatives, provides market information and expertise in exporting, and helps co-operatives form joint ventures with foreign companies. The Enterprise acts as a trader – earning revenue from exports and importing inputs required by co-operatives that are then sold to co-operatives. The Cottage Industries Department promotes handicraft manufacture in rural areas with training, marketing and micro-credit. There are a number of co-operative training institutions: the Co-operative Degree College, the Co-operative College, four Co-operative Regional Colleges, four State/Division Co-operative Training Schools and three Commercial Training Schools.

Base description of savings and credit co-operatives

In March 2007, there were 1839 primary credit co-operatives, with approximately 374,000 members and 7,820 million Kyat total outstanding savings and shares. The number of co-operatives and members is falling, by 3.1% and 3.5% over the past year respectively, as defunct co-operatives are closed down. Over the same period shares increased by 15%, savings by 20% and loans by 30% (compared to inflation of approximately 30%). There are two* main types of savings and credit co-operative: department credit co-operatives and bazaar credit co-operatives.

Departmental credit co-operatives

There are 1604 'department credit co-operatives' (87% of the total), with 340,000 members (91% of the total). Societies typically range in size from 50 to 500 members, although there are some department co-operatives with 3000 members. The average number of members is 215. They were typically set up in the 1970s for government employees. Department co-operatives are typically in urban areas, based in a government department, factory, school, etc, although there are also societies in more remote areas which typically serve a number of different offices. Members are normally made up of the 'middle officials' of the institution, such as teachers, nurses or workers employed in government owned companies.

On average, the shares and savings of members in the department co-operatives is low, only 15,500 Kyat per person. The societies often lend out more than their total paid-up shares plus savings, the difference being made up in un-disbursed profits. The average lending per person is 26,100 Kyat. As a result, department co-operatives only represent 67% of the total shares + savings and 44% of the loans of the overall movement.

Membership in the department co-operatives is falling. The number of societies fell 4.3% during 2006 and membership fell 6%. This is due to a combination of the number of public servants reducing and inactive co-operatives closing. However, the activity of the remaining members increased considerably. Shares plus savings per member increased 31% and loans per member increased 71% over the same period, albeit from a low base.

Overall, department co-operatives still have many members, but their activity is low. Most operate as simple rotating credit clubs. Few societies have 'professionalised'. Systems, products and processes are very simple. Although savings and loan volumes are increasing, there is clearly considerable potential for growth.

Example 1: No. 3 State High-School Co-operative Society – a Departmental Credit Co-operative

Society background

Members are teachers and other staff at 5 high schools, 1 middle School and 12 primary Schools – total 420 members. The society started in 1974 so has more than 30 years' experience.

Shares and savings

Members buy shares of 6,000 kyat each, so there is a total 2.5m Kyat in shares. The society has total savings of 14.55m Kyat, i.e. 34.5k Kyat per person average. Savings are paid 1% per month (12.7% pa). The society keeps excess savings in the State Bank – but only 300k Kyat (2% of assets).

Loans

Members can get loans of 20 months – paid back monthly. Loans are limited to 140k Kyat for High School teachers, 120k Kyat for middle school teachers and 100k Kyat for Primary School. Loans pay 1% per month interest – i.e. there is no net interest income.

Operations

Savings and loan re-payments are made during general meetings and registered in the manual ledger – which is kept at one of the high-schools. Meetings are always held in one of the high-school class-rooms.

Leadership and support

There are 5 members on the board, all voluntary. The president is one of the high-school head-masters, the rest are teachers. All members meet once per month to decide who get the loans – members alone decide, there is no external influence. The Department of Co-operatives Local Co-operative Township Officer checks accounts once per quarter and audits annually – but provides no other support.

Membership characteristics

All teachers at these schools are members: membership used to be obligatory but is not any more. Members would not use other banks, as they do not understand them. They say 'we are teachers, not economists'.

Bazaar credit unions

There are 180 bazaar credit co-operatives with 17,600 members. Most started about 10 years ago. In addition, there are 56 'other' co-operatives with 17,200 members which have similar operations – most of these 'other' co-operatives serve traders not working in formal 'bazaars' and the two categories have been taken together in this analysis. In total, this represents only 13% of societies and 9% of members. On average bazaar co-operatives have 140 members, but some have 500 members.

Membership is normally restricted to traders in a particular bazaar (a market – typically a building with a large number of market stalls), but some societies have started to offer services to other local businesses outside the bazaar and some allow non-members to have accounts. Members are more actively engaged in bazaar co-operatives than in department co-operatives. the average loans per member is 398,000 Kyat, so bazaar co-operatives represent 56% of the loans of the movement. Religious institutions are said to often leave

2006-2007	Bazaar Co-ops	Other Co-ops	Department Co-ops	Total
Societies	180	56	1603	1839
Members	17,674	17,291	339,794	374,759
Shares (Kyat M)	304	322	547	1173
Savings (Kyat M)	1101	824	4722	6647
Loans (Kyat M)	9565	1755	8891	20211
Average member per soc	98	309	212	204
Average savings per member	79,495	66,277	15,506	20,867
Average loan per member	541,190	101,498	26,166	53,931

Table 1: Basic financial performance of thrift and credit co-operatives in Myanmar

large deposits with the societies. Lending is normally provided for business expansion, although some offer consumer loans, education loans, etc. Some bazaar societies already have products specially designed for poor traders – providing 50,000 Kyat 'micro-loans'. The number of bazaar co-operative members and societies is increasing slowly, by 3.4% and 4.7% respectively.

Although bazaar co-operatives are smaller than department co-operatives, they have attracted higher savings and loans per customer. However, customer activity is not growing fast, the average shares plus saving per person only increased 12% last year and loans only increased 4.7%, a real decline given high rates of inflation. This may be because few bazaar co-operatives innovate their product range or market to new members. Most bazaar co-operatives also operate as simple rotating credit clubs. They do not make an active credit decision, but simply lend money to each member in turn. They do not try to attract members from outside the bazaar. Many do not offer deposit accounts, but simply lend out member's shares and the accumulated compulsory savings. Many do, however, have high costs, since they typically have staff and relatively complex operations. As a result, they are sub-scale, i.e. with high cost income ratios driven by high cost asset ratios.

Some bazaar co-operatives have, however, transformed themselves into full credit unions – attracting members from outside of the formal bazaar, offering a range of products, taking on savings and offering larger loans to members. These societies have much stronger financial performance, since they are larger and therefore operating at scale. There is a major opportunity to increase the range of services in the less dynamic bazaar co-operatives, many of which already have staff and more professional operations. This wider product range would create a rate of growth that would allow them to reach scale and so reduce their cost income ratios.

Example 2: Shiplaw Bazaar Credit Co-operative

Society background

Members are mostly traders at the Shiplaw township bazaar. There are 370 members, 56 of whom are 'micro-finance' customers, some of whom are not located in the bazaar building. The society started 10 years ago.

Shares and savings

Each normal member pays 48,000 in shares, although the 'micro-finance' customers do not pay this amount. There were 240m Kyat in shares and 258 m Kyat in savings at the end of 2006 – a total of 489 m Kyat. At the end of 2005 the total was 280m Kyat – a growth of 77% in one year.

Loans

There are several different types of loans – ranging from 48,000 Kyat to 270,000 Kyat. Most loans are for 3 months, with a total interest of 6% (e.g. 1% interest rate per month plus 3% 'operational cost' set up charge). Members need to have 2% of their loan in a savings account. Loans are typically given for business development, to existing traders. Loan repayments are made daily. These repayments exceed demand for loans as loans are given to members in rotation. There have not been any cases of bad-debt.

Operations

The society has a staff of 7 and an office in the Bazaar. All operations are manual. The society plans to expand its lending operations with new products. If it had additional funds it could lend more, but it does not know where these funds can be sourced. The society plans to increase its micro-finance activities, which started two years ago.

**Financial Societies*

A third type of credit co-operative – financial societies – flourished in the late 1990s and early 2000s. These societies often had only a few members and offered financial services to a large number of non-members. Since they were regulated by the Co-operative Law (rather than the Central Bank Law) they were free to set interest rates, which were typically considerably higher than commercial bank rates. As a result of the high interest rates they grew fast, but were judged a danger to the financial system by the Central Bank, which wanted to enforce a lower interest rate. These societies had their regulatory approval removed in the mid 2000s.

Future Opportunities for Growth

All types of thrift and credit co-operative society have a board of Directors with 5 full-time members: Chairman, Vice Chairman, Secretary, Vice Secretary and Director. The Board of Directors has a 4 year tenure. Full member meetings typically occur once a year – but may be more often.

Members are also able to borrow up on 3 times their savings and shares. Given that the average member has approx 20,000 Kyat as savings and shares, this implies an average loan of 60,000 Kyat – however, since societies cover a wide range of different income groups there is a significant variation in this amount. Emergency loans are given for 1 month, typical loans are for 4-5 months and

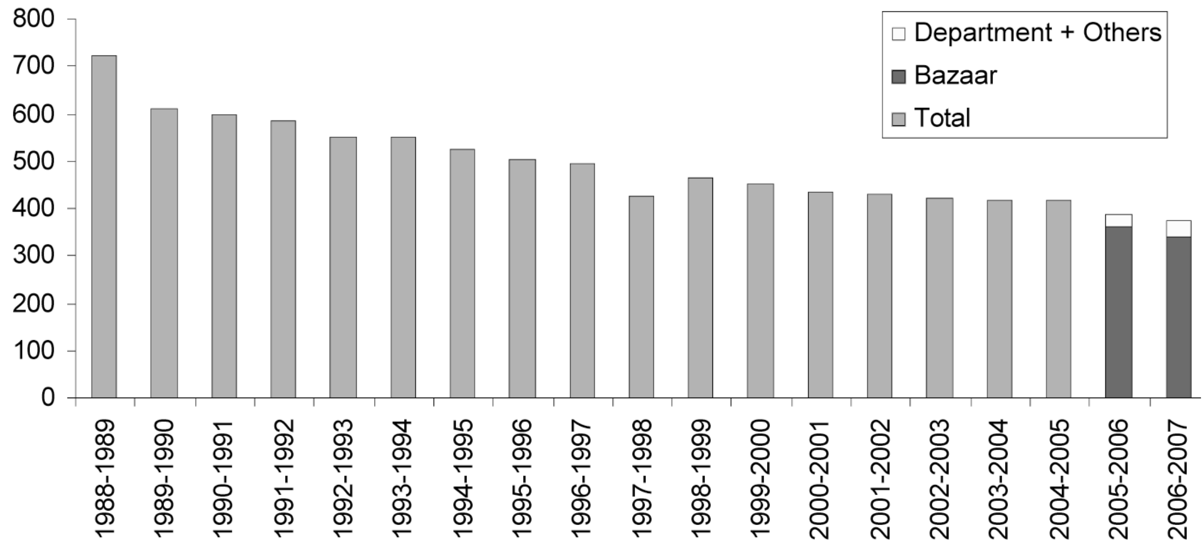

Fig 3: Membership Development

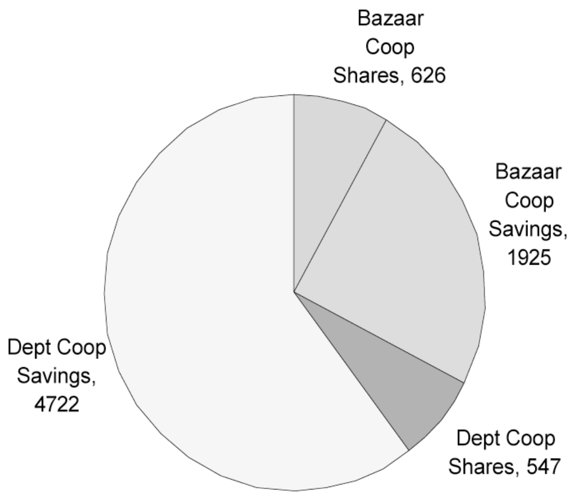

Fig 4: Breakdown of savings and shares in Thrift and Credit Co-operatives

sometimes loans of up to one year are available. Typically, interest rates are now 1% per month for deposits (12.7% pa) and 1.5% for loans (19.6% pa), although higher interest rates are offered for higher risk loans.

Primary Societies normally lend almost all of their deposits and shares – so are not in need of an external organisation to take their excess liquidity. Given the negative real interest rates there is a great demand for loans. However, Secondary and Tertiary level Credit Unions borrow from the societies and the Co-operative Bank and on-lend to Primary Societies to support their liquidity. Some of these loans require collateral.

Large societies have staff, of up to 7 people. In smaller societies, especially in Department Co-operatives, operations are completed by the Board of Directors who may or may not receive a daily re-imbursement. Agricultural Co-operative Societies provide loans for seasonal farming to whole communities. Loans of 20,000 Kyat per hectare are provided, which are re-paid in a lump sum at the end of the growing season.

Analysis of thrift and credit co-operatives in Myanmar

The Methodology described in Fig 1 at section B provides a framework for the analysis of the Thrift and Credit Co-operatives.

Market Profile

The banking sector in Myanmar is poorly developed. There are relatively few banks and few people have bank accounts. The government has established some commercial banks, which have branches in urban areas. There are also some private banks that cater to richer people and agricultural credit co-operatives provide some seasonal credit for farmers. But it appears that the majority of the middle-class population and lower income non-farming groups do not have access to formal financial services - Myanmar is one of the last 'un-developed banking markets'. In emergencies, the two options for the majority of the population are to turn to informal money lenders who charge from 10% per month (213% per year) to 30% per month (2,300% per year), or to use a credit co-operative.

Market Attractiveness of Thrift and Credit Co-operative Societies

Market attractiveness is determined by the level of competition in the market, the macro-economic environment, the legislative environment and public opinion of co-operatives. These elements are taken in turn.

There is very little competition in the market. The few existing financial services institutions: agricultural co-operatives and formal banks do not cater to the target market of the thrift and credit co-operative societies.

Thrift and credit co-operative societies face a major barrier to growth from the macro-economic environment, especially interest rates which are set well below inflation. Inflation is estimated to be approximately 30% per year, while the Central Bank of Myanmar requests credit co-operatives to maintain interest rates at close to 12% per year. This creates a negative real interest rate and co-operatives cannot easily sell savings products.

Thus the thrift and credit co-operative movement in Myanmar is in a strong position in the marketplace. This is the right time to build up the capabilities of the organisations so that they can grow fast once there is increase in demand. The entrance of multinational financial service providers could change this favourable context very rapidly.

Organisation effectiveness

Most of the credit co-operatives in Myanmar operate as simple rotating credit clubs. Members pay for membership which entitles them to a periodic payment of 3 to 10 times their membership 'fee', so long as they also provide a proportion of the payment as a compulsory saving. No credit decision is made, but people wait their turn for the payment. There is little member growth, perhaps because there is little benefit to members if the society grows.

Given the simplicity of the operations, many of the societies have developed surprisingly complex systems, with staff, daily collections, daily settlements processes and audited accounts. In other countries, such a simple product is often delivered by a simple voluntary organisation with no staff or formal accounting. As a result, the co-operatives have high cost to asset ratios and hence low profitability.

Some societies have developed beyond the simple product set to become full credit unions: they provide a wide range of products, make active loan decisions, have more customers. These operations need staff and more complex systems. These societies have much larger volumes of business and are more profitable.

The challenge facing the movement is to convert more of the simple 'rotating credit clubs' into 'Credit Unions'. Much of the work has already been done, since societies have the staff and most of the accounting processes required. They now need to develop their product range and attract more customers and volume of business. This will require external support.

There is currently very little central support provided to co-operatives. None of the co-operatives interviewed during this study had received any regular support from Central Co-operative Services, syndicates or unions. All had regular contacts with the Department of Co-operatives, for quarterly audits and to provide basic introductory training, but did not receive any support on process or product development. There is little inter-lending at the moment, partially because societies lend out all of their assets. There are many opportunities to increase central support, which will require a significant change in approach from the syndicates, unions and the Central Co-operative Services.

The first step is to ensure that national institutions are responsive to the issues facing member societies. Given that the priority is to transform small 'Credit Clubs' into 'Credit Unions', it is likely that the co-operatives will then need assistance to design new products, attract new members and market their services to non-members. This assistance could be given as a 'bundled package of assistance', delivered through a motivation and change program.

Currently, few standard operational processes are being employed by the co-operatives. This is can be seen, for example, by the differences in the preparation of annual accounts between different societies. There are no standard processes for credit evaluation or customer acquisition. This lack of standardisation carries few risks at the moment, since most societies have a simple product set, but as societies develop they will need more standards to reduce operational risk and ensure the managers do not spend time 're-investing the wheel'. Elsewhere, national federations have created a standard 'model branch' which details operational approaches, sales processes, marketing messages, audit, IT systems, etc.

Culture and leadership

To investigate the current culture, a set of check-box evaluation tools were used to evaluate the movement on 'member orientation', 'organization flexibility', 'movement effectiveness', 'staff development 'and 'direction of cultural change'. Overall the movement scored low in all measures and cultural change is a major priority (see www.newthinking.org/toolkit.htm for more details of the evaluation framework).

The low score on member orientation reflects the current lack of focus on member issues. Member meetings in societies only happen once per year. There are few feedback mechanisms from members to management or apex institutions.

The low score on organisation flexibility indicates a lack of dynamism in the movement. Many societies are happy to remain simple and not develop – a number said that they did not want to develop new products or get new members. Moreover, decision making in co-operatives is slow.

The effectiveness of the overall movement is limited by a lack of co-operation and coordination between the different levels of the movement. Until the transformation of the support structure described above is complete, it will be difficult to centralise any operations and the effectiveness of the movement as a whole will be reduced. The limited integration of the movement also impacts the staff development performance. Beyond initial basic training within by the co-operative department, there are no systems to develop the skills of staff working within the societies. While processes are simple, this should not be a problem, but once co-operatives start to develop, more staff development will be required.

Conclusions

In summary, while some societies have developed more sophisticated processes and products, most societies have very simple processes and systems. They will not be able to reach their potential, or grow in a more favourable macro-economic climate, unless they reform their operations considerably. To achieve this reform, societies would benefit from increased support from an apex body, such as CCS, to define standard processes and procedures. More importantly, however, they need to achieve a 'culture change' to become more focused on their members and more ambitious in their goals.

Impact, sustainability and projections

Credit co-operatives in Myanmar are already providing useful services to their members. They are the only source of finance and, especially within the Bazaars, are supporting the development of micro-enterprises. While the co-operatives are not focusing on the poorest groups, they are certainly not the preserve of the wealthy. Some co-operatives are already providing micro-finance services. Overall, the co-operative movement has a clear positive developmental impact and, with further development, this impact is likely to increase.

The existing departmental co-operatives appear sustainable. They are financially viable on-going operations, those that use volunteers have low costs and they have simple operations. They do not face competition and are reported to have no bad-debt issues. They are likely to continue, although may well continue to decline slowly without external support, mobilisation and product development.

Bazaar co-operatives are potentially more dynamic. Some have already developed their product range and are trying to expand their membership by allowing other groups to join. These societies are likely to be an example for other societies and, by operating at scale, are financially viable and so can grow. Smaller bazaar co-operatives may face financial difficulties, since they have high costs in comparison to their assets (due to having staff) and limited revenues from enforced low net interest margins. It is likely that in time the bazaar co-operative market will move from having a large number of small societies to having a smaller number of larger and more financially viable societies.

Critical success factors for developing the Thrift and Credit Co-operatives

The above investigation indicates that the future success of the movement will depend upon:

1. An active and dynamic leadership in the societies – with leaders focused on growth.
2. A regional / national support structure that helps societies develop and in time takes responsibility for some operations.
3. Dissemination of best practice from more successful co-operatives to other societies, including new products, processes and customer acquisition techniques.

Short-term strategic priorities for thrift and credit co-operatives

The above analysis indicates the major needs within the Thrift and Credit Co-operatives, which can be summarised into three themes.

Development of national support

This requires organisation development at the various organisation layers. The first step is to create a 'vision' (or a set of alternative visions) for how the movement should develop. This vision would identify priority inputs that the support agencies should provide to the movement. These priority inputs are likely to include: liquidity funding, tools to help societies plan, standard products that societies can roll-out and a newsletter that provides examples of successful societies. By identifying these priority inputs, the support structure will reduce its 'business as usual' activities and increase its focus on 'new project areas'.

Culture change in co-operatives

This is a fundamental requirement for their development. Culture change can be achieved by identifying areas where the current culture needs reforming, making a clear definition of the cultural change required and identifying specific actions that will achieve the change. Responsibility for this culture change sits with CCS, the Department of Co-operatives and the societies themselves. CCS can create tools and processes that generate a change in culture. The Department of Co-operatives can ensure that its' staff focus on effective regulation.

Some societies have already expanded their customer base and product set, allowing them to grow and achieve economies of scale. A large number of societies have not, however, made this transition – currently only offering very simple products and limiting their membership base. These less active societies need to scale up their operations.

While responsibility for this change to operations ultimately rests with the local leadership of the societies, the central support agencies can help. For example, they can run 'business development' programs for high potential societies, helping them implement a range of reforms. They can inform societies of the opportunities to implement new products, especially savings products. They can help disseminate the lessons from the more successful societies to others.

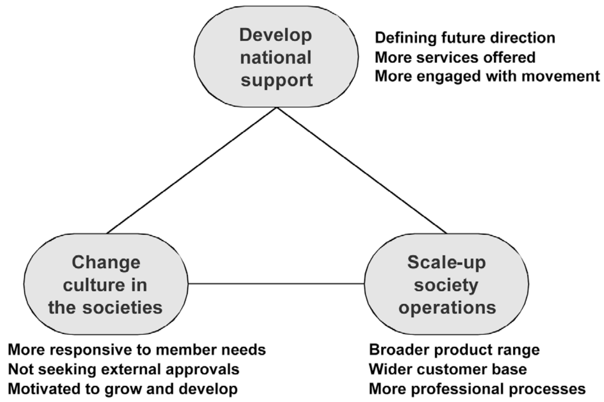

Fig 5: Short-term priorities for development of thrift and credit co-operatives in Myanmar

Longer-term development opportunities

The immediate priority is to grow the thrift and credit co-operative societies so they are providing a broader range of services and serving more customers. However, once this transformation is achieved, the societies will soon find that they need to reform their processes to handle the increased volumes of transactions. At this stage, societies should consider implementing IT systems to automate transactions and accounting processes, centralising some processing functions, such as credit document preparation or regulation submissions and creating support teams to help societies improve their efficiency. Since most

Area	Cultural change required	Example actions to create culture change
1.Member orientation 1.1Service orientation	Society leaders focused on member needs	CCS to request each Board of Directors to create a simple (one page) plan of actions for the next year to address member needs Societies to have more frequent member meetings, with more time to discuss member issues Larger societies to create an anonymous suggestion box
2. Organization flexibility 2.1 Motivation for change	Society leaders more motivated to develop their societies	CCS to create guidelines for remuneration to Board of Directors members, based on membership and / or profit growth CCS to promote new ideas and 'Best Practice' to societies, perhaps through a newsletter
2. Organization flexibility 2.2 Clarity of Direction	Future direction for societies planned and understood by whole movement	Dept of Co-ops / CCS to create a strategy paper that describes the 'society of the future', covering: products offered, society size, CCS areas of support CCS to study likely future needs (e.g. IT, new products, insurance, etc.)
4.Staff development 4.1Staff recognition	Motivation of staff in Societies increased	CCS to create a simple staff evaluation form, to be completed every 6 months. Society managers to fill-out forms Society leaders to give staff targets for new member mobilisation, increase in deposits, etc.

Table 2: Initial description of culture change priorities

societies are located in urban areas, with good communications, efficiency improvement programs should be relatively simple to implement. Central support agencies should lead this efficiency improvement program.

Once a society model is well developed, the model may be applied to other areas. Most societies are located in urban areas at the moment, yet there is likely to be a major demand for non-agricultural credit in rural areas. Additionally, there is likely to be significant demand for more products, such as insurance, longer-term loans, or leasing, which could be sold through the existing co-operative societies, with the societies acting as a sales agent. It should be possible to start to roll-out these services in two to three years, once the institutional basis of the existing co-operatives is strengthened.

Vertical Markets and Co-operative Hierarchies. The Roles of Cooperatives in the Agri-Food Industry

Kostas Karantininis and Jerker Nilsson, Editors, (2007) Springer, The Netherlands.
ISBN - 10-4020-4072-5 (HB) ISBN - 10-4020-5543-0 (e-book)

This scholarly book is the work of twenty-three internationally recognised academics providing 16 papers variously on aspects of agricultural co-operative economic and commercial performance and business organisation. Written primarily for the specialist agricultural economist and student of agricultural economics and business it is dedicated to the memory of one of the great intellectual forces of Greek and indeed world agricultural economics the late Prof. Konstantinos Oustapssidis formerly of the Aristotle University of Thessaloniki, Greece. For those interested in the development of ideas in the discipline of agricultural economics this book contains a select bibliography of some of the late Prof Oustapassidis seminal works.

The range and scholarship of this work make it a must for any university library with departments specializing in agricultural economics. There is far too much depth of content to do more than mention the range of topics here. The authors discuss problems of structure, networking, innovation, performance, governance, leadership and consumer attitudes and there are in addition some interesting materials on the dairy sector in Europe and demutualisation in the United States. I will discuss below some of the ideas by one of the contributing authors Anastassios Gentzoganis, chapter 9 “Regulation, Governance and Capital Structure in Co-operatives”. I select this chapter because, its introduction at least, links to the concern of the other book I have reviewed for this issue - that of lack of capitalisation in co-operatives.

Co-operative Capital. A new approach to investment in co-operatives

Jim Brown, Co-operative Action, Manchester, UK. ISBN 0-9548652-0-0 (PB)

This book is something of a collective effort. Jim Browns acknowledgements read rather as a who’s who of the UK Industrial Common Ownership Movement. The book has chapters by Andrew Bibby, Chapter 3 on current investment practises and Chapter 4 on the ethical investor and Charlie Cattell wrote Chapter 7 “An equity Model for Co-operatives”. The book also used research by Dr Rebecca Harding and Jamie Hartzel and a number of others are named as making a contribution to the project as a whole. This work is a book for practitioners rather than academics. Not that it is not of considerable interest to academics as a source of evidence of just how far the Industrial Common Ownership Movement have travelled from its original fixation on collectivism and antipathy towards any form of co-operative ownership / management model that deviated from direct collective worker control. In fact the book in its advocacy of external capital investment to assist the development of worker co-operatives is developing a model of external investment in worker co-operatives that was first established over a century ago in England by Thomas Blandford. Blandfords’ Co-operative Productive Federation (CPF) arose out of a reaction to the consumer co-operative ideologues determination to eradicate profit sharing with the workers from the by then firmly “consumer co-operative” movement.

I do not agree with the books opening premise that traditionally co-operatives have preferred debt to equity as the CPF example illustrates this was not the case. This is rather the perspective of a certain cul-de-sac of micro co-operatives that came into existence as part of the ICOM initiative from the 1960s onwards. In the beginning, contrary to both Consumer Co-operation and CPF perspectives, the British Co-operative Movement took a much more macro labour market based perspective. Closely allied to the early trade unions, many of which had the establishment of co-operative ownership in their constitutional aims, the approach was to mobilise not investment income but discretionary wage income. (1) By raising small amounts of gifted money or small savings the movement hoped to establish economic organisations under popular ownership and control. Giving away capital as consumer dividend or as worker profit sharing went against this earlier principle, established by William Pare at a conference at which Robert Owen took the chair, that none of the surplus should be divided.

Aside from questions of co-operative history, I do congratulate Jim Brown and his co-authors for producing an ethical and practical alternative to the current market for capital. The practical proposals and analysis deserve serious attention and discussion. I just hope that the beleaguered Trade Union and Consumer Co-operative sectors alongside the miniscule Credit Union and lager but diminished Building Societies can be persuaded to enter into the dialogue. But why I wonder do we want to go cap in hand to the State – not an option surely co-operative movements that wish to retain their autonomy should relish? Why not ask the trade unions to request of their members a voluntary co-operative job-creation fund donation of 5p per week? Not unlike the political levy? If only a million TU members agreed in a matter of the first two years a bigger sum than the £20 million (p142) the books authors aspires to would have been raised - one that ICOF experience demonstrates could be recycled many times and would be continuously building via trade union collections so that the size and scale of the employment opportunities could themselves grow, possibly permitting the purchase of innovative patents for co-operative ownership. (2)

Regulation, Governance and Capital Structure

In the Karantininis and Nilsson edited books', Chapter 9. "Regulation, Governance and Capital Structure" Anastassios Gentzoglanis, from the Centre for the Study of Regulatory Economics and Finance University of Sherbrook in Quebec, Canada takes a stand which could be seen as an academic endorsement for the aim in Jim Browns book to establish a market for co-operative capital. Gentzoganis identifies the lack of tradability (p151) of ownership rights as a significant factor in explaining the "underperformance" of capital in the co-operative context. Even accepting, as Gentzoganis does, the sub-optimisation of capital in co-operatives as correct we must say that the proposition itself tells us more about how the co-operative purpose is misunderstood than it does about the economic efficiency of the co-operative business model. Co-operatives are of course primarily the result of members' lack of capital. We first of all need to recognise this or we miss the point of co-operatives as alternatives to the capital based business model. Membership of co-operatives is not determined on grounds of a "rational choice" between the relative efficiency of capital employed in alternative contexts but a choice made out of the necessity arising from the deficiency of capital. It is not that co-operative members are deprived of more profitable opportunities by the co-operative structure; on the contrary it's because of the co-operative structure that they have profitable opportunities at all. (p152) The second fundamental rational for co-operatives is the delivery of services at quality levels that are not available in any alternative format at an equivalent standard. I believe that co-operative shortage of capital is not an economic question at all but rather a political one of raising the conscious and then subsequently mobilising small sums of discretionary income from the people whose existence in terms of family farms, local employment and through the lack of other services are threatened by the *capital dominated* market economy – not market economy per say.

However, let me state that this issue driving Jim Browns book is not central to the analysis of Gentzoganis' chapter which rather seeks to explain the alleged sub-optimisation in terms of co-operative governance systems. Here I agree the relative lack of external tools (capital market regulation through the share price) to control management in co-operative as opposed to capital based firms is a real problem particularly as co-operative managers are often in positions vis a vis their boards of relative intellectual/educational as well as informational advantage. From this standpoint Gentzoglanis examines four models of co-operative governance (the simple finance model; the stewardship model; the stakeholder model, and the political model) in a clear and to the non specialist accessible language. I do recommend this chapter and the whole book to readers to examine as an intelligent contribution to the debate on how to overcome problems of measuring and evaluating co-operative performance, strategy and capital formation.

Towards the end of Gentzoganis' analysis the author gives some acknowledgement to the different purposes of co-operatives to capital based business. He concludes that co-operatives operating with powerful managers, by pursuing their own interests, rely on higher equity to asset ratios than those of non – powerful managers (due to members' reluctance to take the risk with their personal equity – see pp163-164). Gentzoganis may also be on to something in his raising the possibility unification of co-operative governance models. What his regulatory approach lacks is any consideration of management methodologies as being themselves important regulatory mechanisms. (3)

Notes

1. A mixture of profit sharing and the insistence on returns by the outside investors (often consumer co-operatives) undoubtedly restricted the opportunity for growth of Bland fords' CPF Co-operatives. J.F. Bray and William King both saw small savings as the way to liberate labour. For King retailing was merely a low capital requirement strategy for accumulation not distribution of capital.
2. Davis, P. (2000) Chapter 7 "Co-operative Strategies for Trade Unions" in Labour and the Family, Harokopia University, Athens, Greece and Leicester University, England. "Co-operative Development as a Trade Union Strategy" (1988) in *Journal of Interdisciplinary Economics,* University of Exeter, Spring, 1988.
3. Davis, P. (1999) *Managing the Co-operative Difference*, ILO Co-operative Branch, Geneva.

The Editor

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