

# Between Formal Structures and Informal Institutions - Behaviour of Members in Co-operative Enterprises

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## **Abstract**

*Co-operatives providing welfare services form a new group of enterprises in the Nordic countries. These co-operatives may differ from other providers of welfare services because of the interests of their members and the institutional structures of co-operatives. The focus in earlier studies of co-operatives has most often been on one of these aspects. In this paper it is suggested that new institutional theory may provide a more appropriate foundation for studies of these aspects of co-operatives. Members may try to change institutional structures of co-operatives so that they better serve their interests, but existing institutions also provide limitations for the behaviour of members. Special attention should be given to this two-way relation in order to determine how co-operatives may differ from other providers of welfare services. In this paper empirical findings from Swedish co-operative day care nurseries are presented to illustrate the relationship between institutions and the roles of members in co-operative enterprises providing welfare services.*

## **On third sector and power of individual members**

The support for the strong welfare state has been relatively unchallenged in Sweden during the last few decades. However, the number of private or semi-private providers of welfare services has slowly increased. The political parties mainly support the current role of the state as the main provider of welfare services even though the bourgeois parties in most cases support the increased number of private enterprises, voluntary organisations, and co-operatives as complements to public provision of services. The citizens seem to be more restrictive in their attitudes even though there are signs of increased interest in some kind of welfare mix. Especially attitudes towards the third sector have become more positive among both the political parties and citizens.<sup>1</sup>

As the third sector is an analytical concept that refers to particular groups of agents sharing a number of characteristics, rather than a juridical concept referring to a legally defined group of organisations and enterprises, it is a matter of definition which agents are included under this concept. There is not one commonly accepted definition of the third sector and several other concepts

with similar or related meaning, like voluntary sector, non-profit sector, and social economy, have been presented.<sup>2</sup> However, it is important to note that, despite the lack of commonly accepted definition, the concept of third sector clearly has positive connotations in Sweden.

It is not possible to discuss in more detail the characteristics of the third sector in this paper. The focus here is on one of the most interesting characteristics of the third sector and, possibly, of the co-operatives that may partly explain the positive attitudes towards these groups of agents in provision of welfare services.

It has been assumed that the organisations of the third sector share characteristics like multiple goal structure, informality of social relations and flexibility. These kinds of assumptions, however, often mislead as they simplify too much the reality and idealise the differences between sectors.<sup>3</sup> It is more appropriate to emphasise the importance of the members in the formation of activities since this does not assume characteristics for the organisations, but emphasises the rights and responsibilities of individual members as characteristic of the third sector. To some extent, this point of view unifies discussion of the third sector and civil society.<sup>4</sup>

### **On co-operatives and provision of welfare services**

Co-operatives form a group of enterprises that are characterised by their form of ownership - co-operatives are usually owned collectively, either by consumers or providers of goods and services. Some traditional examples of these enterprises are retail and farmer co-operatives. This form of ownership prevents ownership by those not using the services of the co-operative or working in the co-operative. This means that members of co-operatives have double roles, either as consumers and owners or as personnel and owners.<sup>5</sup>

Members of co-operatives have the possibility to participate in the governance of their enterprises. All members have one vote in the decisions of co-operatives and they may become members of executive boards. Despite these formal rules supporting the active participation of members, the level of active participation in many co-operatives has become much reduced. Particularly in many consumer owned co-operatives, positions of members do not differ remarkably from those of customers of other enterprises.<sup>6</sup>

During the last two decades the emergence of small co-operatives providing commodities not earlier provided by co-operatives has led to the introduction of the concept of "new co-operatives" in the Nordic countries. These co-operatives do not formally differ from "established co-operatives". However, it has been assumed that in

their new fields of activity, small size and possibly also the more active roles of members justify consideration as a special group of enterprises. In the Nordic countries the largest group of new co-operatives is found in Sweden where, for example there are over 1,000 co-operative day care nurseries and about 100 co-operatives providing sick- and health-care. Due to the high number of parent co-operatives involved in day care activities, the majority of co-operatives providing welfare services are consumer co-operatives i.e. owned by the users of the services. However, the number of worker co-operatives, has started to grow during the 1990s. Just like most groups of new co-operatives, the co-operatives providing welfare services are still a marginal phenomenon. They are nonetheless important for some groups of citizens because of the lack of other providers of these services, or because their form of ownership better suits some groups of customers and workers.<sup>7</sup>

The co-operatives may differ from other enterprises in at least in two ways. Firstly, the form of ownership may affect the goals of these enterprises so that they are more oriented toward the varying interests of their members instead of maximising an economic surplus. These goals are naturally not mutually exclusive or independent from each other. Secondly, the members of the co-operatives may have better possibilities to influence the activities and commodities of the co-operatives than do the customers or personnel of other enterprises. However, both of these differences depend to a large extent on the activity of the members. If members do not participate in decision making, the differences between the co-operatives and other enterprises may decrease significantly.

The behaviour of members, like their participation in the governance of co-operatives, has most often been explained by looking at the benefits and costs of activities.<sup>8</sup> In contrast, attempts to clarify how the institutional structure of co-operatives affects the behaviour of members and how the interests of the members and structure of the co-operatives are related have been rare. For these reasons, the aim of the paper is to investigate how the behaviour of members, for example participation in decision making, is affected by formal and informal rules that enforce constraints on behaviour within co-operative enterprises and how the interests of members and rules of co-operatives are related.

The empirical part of the paper consists of some description of the day care nurseries owned by parents. This group of co-operatives is chosen due the high number of these enterprises. The roles and power of parents owning their day care nurseries are also affected by the roles of staff personnel (who are usually not members of the co-operative) and by the role of the public sector in funding and

controlling service production. In this paper the roles of personnel are also discussed, while the role of the public sector is discussed elsewhere.<sup>9</sup>

### **Earlier theoretical studies of behaviour of members**

There have been several attempts to devise typologies of the behaviour of members of co-operative enterprises. Some of these typologies are influenced by a typology of Albert O Hirschman.<sup>10</sup> Hirschman's typology does not primarily address co-operatives and its suitability as such for co-operative studies is therefore questionable. For this reason the purpose of the following description of the typology is not to summarise the main ideas of Hirschman's study. Rather, Hirschman's key concepts, relevant to the study of co-operatives, are presented. The focus is on actors' behaviour within enterprises owned by their members.

Hirschman<sup>11</sup> assumed that customers of enterprises are not limited to the "exit" possibility when dissatisfied with the commodities provided. Rather, customers may act in markets in the same way as they act in politics. In both of these arenas citizens may choose either the "exit" alternative which means that they leave the enterprise/political party or they stop using its services/stop voting for it. However, they may also express "protest" (voice) which means that they may try through active participation to change the things they are dissatisfied with.

In enterprises owned only by members, members may choose either to exit or to protest when dissatisfied with their enterprise. Dissatisfied members may therefore either stop using commodities/resign, or they may try to influence the activities of their enterprises to make them better serve their interests. The choice between exit and protest may be based on the characteristics of the members. According to Hirschman, on the one hand the "loyalty" of members increases the probability of protest and decreases the probability of exit. On the other hand, members' calculations of the costs and benefits of their protests and their prospects of changing the things that have caused dissatisfaction affect the decision between these two options. Earlier experiences among members are decisive of whether protest is seen as an effective way to bring about change. For these reasons it is possible to conclude that Hirschman's model is based on a) the behaviour of individuals that may be based on loyalty ie on bounded rationality or irrationality, or on calculations of costs and benefits ie economic rationality, but also on b) characteristics of organisations that either support protest or exit habits.<sup>12</sup>

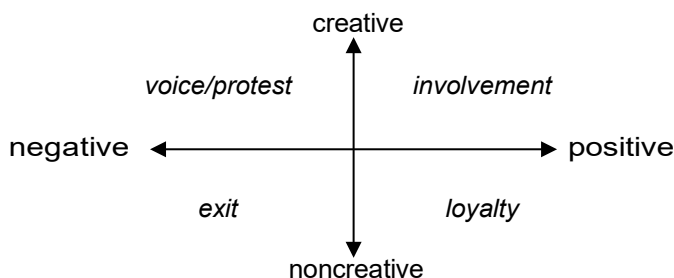
One of the problems of Hirschman's typology when applied to

co-operative studies is that active participation of members is discussed only in the case of dissatisfaction. Members of co-operative enterprises may also be involved in activities without feeling dissatisfied ie they may participate in the activities of their enterprises for a variety of reasons. Furthermore, the possibility that members might remain passive in the case of dissatisfaction is not properly discussed.<sup>13</sup> Finally, the possibility that members could change the rules of behaviour is not analysed. This last option is important because members may not only try to affect the goals and outputs of their organisations, but also of the way different actors, like members, may behave and affect these outputs. In some sense Hirschman takes characteristics of organisations as given even though they can be challenged.

Yohanan Stryjan<sup>14</sup> is one of the researchers that has developed Hirschman's typology for studying co-operatives. As part of this development, Stryjan has introduced the concept of involvement and has modified Hirschman's concept of loyalty in a way that includes both active (creative) and passive (non-creative) forms of behaviour. In addition, positive and negative forms of behaviour have been separated in the typology.

In Stryjan's typology members who are dissatisfied with their enterprises may choose to either exit or protest. Both alternatives may lead to changes within enterprises, but, from the point of view of these members, not necessarily in the wished for direction. Exit of dissatisfied members does not leave space for participation in favour of changes and protest may lead to sanctions that worsen the situation of the protesting members. Positive members, in turn, may either be loyal or involved. Loyal members are passive which means that they follow rules and do not try to influence the activities of their enterprises. Involved members, in contrast, are willing to invest their resources in the activities of the co-operatives so that their interests are better served or because they regard participation as such as something valuable. In reality members may move between these forms of behaviour. For example, occasionally loyal members may become involved, or involved members may start to protest. The difference between getting involved and protesting is not based only on the behaviour of members and their attitudes towards co-operatives. Instead, it is possible to define the line between them so that the activity that is accepted in an enterprise is something positive (involvement) and the activity that is not accepted is something negative (voice/protest). This means that the same kind of behaviour may be classified differently in different enterprises.<sup>15</sup>

Figure 1: Stryjan's Model of Alternative Forms of Behaviour<sup>16</sup>



In Finland Ilmonen, Laakkonen, Laurinkari and Suonoja have developed typologies of members and their behaviour. In these typologies both economic and social/political motives of members are included. The main idea of the different typologies is that the behaviour may be based on either economic-pragmatic calculation of benefits and costs of activities or on ideal-political orientation of members. The importance of ideal-political motives has drastically decreased in most of the established co-operatives during the last decades, but it is not clear what importance other non-economic motives play in smaller co-operatives.<sup>17</sup>

Furthermore, several ideal types of members have been presented. In the early co-operative studies "homo cooperativus" was an ideal type of member whose basic characteristic was solidarity. It was assumed that behaviour could be explained by the common interests of members. The ideal type has not been used in more recent analyses. Instead, "homo economicus" has become the most important ideal type, borrowed from economics. Homo economicus is an ideal type characterised by selfish and economically rational individuals. There have also been attempts to combine these two models and to include either social or political ambitions among the goals of homo economicus.<sup>18</sup>

The earlier typologies and ideal types are often based on assumptions about different characteristics of members. It has been assumed that differences in behaviour could be explained by differences in motivation. In Stryjan's model, however, constraints on behaviour based on rules of enterprises are also taken into account. It is necessary, however, to combine these two aspects in order to determine what is typical behaviour for members of the co-operatives and, based on the behaviour of members, how the co-operatives may differ from other enterprises and organisations. In addition, the rules of the co-operatives may also change due to the behaviour of

members. For these reasons it is also necessary to discuss the reciprocal relationship between the interests of the members and the institutional structures of the co-operatives. In the following section theories of new institutionalists are used to develop a preliminary model of the relationship between the behaviour of members and the rules of behaviour within co-operatives.

### **Institutions and behaviour**

The following ideas about the relation between institutions and the behaviour of members within these institutions are borrowed from a group of researchers known as new institutionalists. These researchers, however, differ remarkably from each other. This is primarily due to the relative novelty of this school and its interdisciplinary nature. The researchers have at times been divided into economic, sociological, and historical schools.<sup>19</sup> In this paper some of the differences between these groups are discussed, but the basic ideas of the group as a whole are the focus of the presentation. This leads naturally to some oversimplifications that do not do justice to all of the nuances within the school.

New institutionalists have studied the behaviour and the activities of both groups of individuals and of organisations. It has often been assumed that behaviour and the activities are influenced by institutions. Despite agreement on this, these researchers have defined institutions in a variety of ways which has led to remarkable differences, both in their theoretical constructions and in their empirical use of theory. For example, informal rules that structure actors' conduct and formal organisations have sometimes been included in the definition of institutions.<sup>20</sup> Nevertheless, it is necessary to separate these concepts from each other. First of all, the rules of behaviour and organisations must be separated. This is obvious when the new institutional theory is used in empirical studies. Social policy provides an excellent example to show why both rules of behaviour and organisations should not be defined as institutions. For example, rules that define the rights of individuals to receive social services may be held constant even though the organisational structure of agencies connected to the provision of services change. Therefore, the concept of institutions should refer to rules that enforce constraints on the interaction between different agents as individuals, organisations, and the state.<sup>21</sup>

It is not always clear whether only formal or both formal and informal systems of rules should be understood as institutions. The first approach has the advantage that the definition does not become too wide. However, in some areas of study incorrect and

misleading conclusions about reality may be arrived at if concentrating only on formal institutions.<sup>22</sup>

Even though institutions within organisations constrain individuals' choices, institutions do not necessarily change the basic motives of individuals.<sup>23</sup> Following the argumentation of the economic approach that has been popular in both co-operative and institutional studies, it is reasonable to assume that institutions restrict the choice-sets of members who adapt their behaviour in order to maximise their own benefits. Institutions and possibly sanctions and rewards connected to them may change the consequences of the different alternative forms of behaviour. In this approach individuals' self-interest is the motive for any behaviour and modifications in behaviour are seen as responses to the changes in incentives.<sup>24</sup>

There are also new institutionalists who assume that institutions affect the motives (interests) of actors, and not just their strategies to reach particular goals.<sup>25</sup> Most often it is claimed that the actors make judgements concerning correct and acceptable behaviour which are not necessarily based on calculations of consequences. They may instead be based on the "experiences of others in comparable situations and by reference to standards of obligation".<sup>26</sup>

## **Between formal and informal institutions**

### *Interests of members affect institutions within co-operatives*

At the beginning of the paper, it was suggested that co-operatives providing welfare services may differ from other enterprises due to their form of ownership. The ownership by the consumers of services or personnel means, in principle, that members may have better possibilities to influence services they receive from their enterprises or that personnel may influence their working environment.<sup>27</sup> Regardless of form of ownership, both formal and informal rules of co-operatives may constitute constraints on behaviour of members due to common or conflicting interests of members. These constraints are formed in negotiation processes that take place in all organisations throughout their existence.<sup>28</sup>

In the following table four ideal types of situations within co-operatives are presented; different alternatives may exist side by side. The table consists of two dimensions, namely, interests of members and form of rules. Three aspects of each alternative are presented: 1) channel of participation of members, 2) character of interests, and 3) central characteristics of alternatives. The model is based on the



assumption of rational (calculative) behaviour of members and an alternative point of view on the rules is presented subsequently.

*Table 1: Model of interests of members and rules of co-operatives*

|              |                 | <b>Interests</b>  |  |
|--------------|-----------------|---|--|
|              |                 | <i>Common</i>   | <i>Conflicting</i>   |
| <b>Rules</b> | <i>Formal</i>   | Democratic management, interests of members as a group, active participation of members is possible.  | Democratic management, interests of different groups of members, struggles over outputs and formal rules.  |
|              | <i>Informal</i> | Informal contacts, interests of members as a group, active participation or informal co-operation supported, informal rewards connected to participation if it increases profitability. | Informal contacts, interests of different groups of members, informal selection processes to executive boards, informal rewards connected to participation if it increases own group's benefits. |

Formal rules of co-operatives emphasise the importance of democratic management. All members have basically the same possibilities to affect daily activities and thus to form co-operatives. The options presented by Stryjan<sup>29</sup> may be available to all members, but even in the case of common interests of members, possibilities for certain forms of behaviour may be limited.

Starting with restrictions that affect all enterprises, a lack of alternatives prevents exit, and larger organisations have restricted opportunity for the involvement of members. Formal rules of co-operatives may also restrict the participation of members in other ways. When the profitability, flexibility or rational decision making of a co-operative worsens due to the active participation of its members, formal rules may be reformed so that rationalisation of decision making within the co-operative is supported instead of the active participation of the members.<sup>30</sup> In small co-operatives this may mean, for example, increased power for personnel, executive boards or other important groups. Furthermore, as stated earlier, the members may move between alternatives presented by Stryjan. For example, if the

involvement of members (all members) is not supported or accepted, members may move either to loyalty, protest, or exit.<sup>31</sup>

Members and employees of the day care nursery co-operatives are two groups of agents that in several ways form the roles of each other. There are examples of where parent members are involved in most issues concerning both the daily activities and general planning of the co-operatives. However, there are also co-operatives where the power has in practice been moved to employees. One of the explanations is that the staff in many cases have better opportunities to affect decision-making due to their knowledge and full-time employment. This kind of development has in many cases been supported by parents who have limited resources to participate in the activities of their co-operatives. However, the roles of these two groups are not always clearly defined. For example, parents in some cases seem to think that they know what is best for their children even though they do not necessarily have the capacity to plan activities so that they would best serve the needs of larger groups of children. This kind of situation can easily lead to conflicts which in turn affect the roles of parents in the long run, either by increasing or decreasing their power. Besides the conflict perspective it is necessary to add that in many cases the parents become involved when needed even though the staff are the most involved group of agents. This is the solution that seems to work in several cases.

If members have common interests and if profitability of activities depends on the involvement of members, there is a possibility for the development of informal rules supporting involvement. The probability of developing informal rules among members is connected to the size of co-operatives as possibilities for interaction between members vary considerably. The more contact members have and the better they know each other, the easier it is to establish informal rules of behaviour. The best possibilities to introduce new rules are, quite naturally, in relatively small co-operatives. The development of informal rules is also connected to the duration of membership and the possibilities to follow up and control the behaviour of other members. Interest in investing resources in the development of new rules of behaviour may be limited if people do not stay members long enough to compensate for the possible costs of developing, establishing and maintaining new rules.<sup>32</sup> In summary, when the success of co-operatives however they are defined, depends on the activity of members, those members may have the motivation to participate in activities of their enterprises and even to establish informal rules supporting involvement of other members. Naturally, the problem of 'free riding' may exist in this kind of situation.<sup>33</sup>

Within the day care nurseries, the development of informal rules affecting the activities may occur easily due to the small size of these co-operatives. This is not however, entirely positive for the enterprise since easily changing practices can lead to problems of free-riding and lack of continuity. For example, in some co-operatives the reluctance of some families to participate in compulsory tasks (eg cleaning, working etc) has led to friction between members. This is against the formal rules and has led to dissatisfaction amongst the membership and decreased motivation to take care of one's own responsibilities. In this situation, both formal and informal institutions are re-formed in negotiations and, as a consequence, the possibility of new roles for members emerges. It is also necessary to note that despite the equal rights and responsibilities of the members, it is usual for members to receive varying levels of benefit by compensating them economically.

Within democratic management there is room for conflicting interests, which may lead to constraints on the behaviour of members. As in the case of common interests, formal rules may change so that they prevent and/or support the active participation of certain groups of members. There are examples of this kind of conflict in established co-operatives. Even change in the form of ownership is possible due to conflicting interests. The balance of power between different groups and different bargaining positions may explain which rules may be challenged and which groups will have the possibility for this kind of activity.

In the case of conflicting interests, informal rules of behaviour may support and prevent participation. Leaders of co-operatives, staff or otherwise active groups of members may establish informal forms of co-operation that will increase their power. For example, selection into leading positions within co-operatives may to some extent be based on negotiations outside of the formal decision-making process. Powerful groups may also restrict involvement of other groups of members through the use of informal rewards and sanctions. Even though acceptance of or adherence to these kinds of rules could constrain behaviour, learning these rules may be important for members for several reasons. To follow rules may be rational because of the rewards and the sanctions connected to them. Acceptance of other members, possibilities for beneficial co-operation and positive responses<sup>34</sup> may to a large extent be based on relations in which informal rules play the most significant role.

The co-operative environment has great potential for conflict. In co-operative day care nurseries different backgrounds, resources and goals of parents are some of the most important sources of disagreement. There are several examples of co-operatives where

practical issues have led to conflicts; the problem of free-riders and different possibilities to participate in activities of the co-operatives have already been identified. The problems are not, however, always practical. Power as such, has also caused problems. For example, in one of the co-operatives in the Goethenburg region some of the academic members are accustomed to holding the power. In reality other members have no prospect of being elected to executive boards etc. In practice informal contacts with the powerful members are the best means by which to affect decision-making in this situation. It is also worth noting that co-operatives change over time. For example, during the first years members have in many cases, similar background and common goals. During the subsequent years most members leave, to be replaced by new members. In many cases, this leads to new negotiations of the goals and practices of the co-operatives.

### **Institutions within co-operatives affect interests of members**

Even though members may be involved in establishing rules of behaviour, it must be remembered that the relation between members and institutions is reciprocal. Both formal and informal rules are closely related to the interests of members, but it is possible that within organisations there are many relatively independent institutions. It is possible that rules are a product of long processes that do not necessarily produce "rational" systems that are best suited to the interests of any group of actors. This is why the history of organisations must also be taken into account if one is interested in the way institutions constrain behaviour. Once established, rules do not normally disappear rapidly even though they may change over time.

Even though the rules of behaviour may be challenged, it is also possible, as some of the new institutionalists suggest, that some forms of behaviour are accepted by actors without a calculation of their consequences. This means that existing ideals of behaviour may be followed to some extent even though following the rules would not be the most beneficial alternative for members. This opens up for the possibility that, in some co-operatives, certain kinds of behaviour of members are encouraged, for example active participation or passive roles, in ways that create differences between co-operatives. In addition to expectations directed towards whole groups of members, there may be expectations that treat individuals differently. Occupation, age, and gender are some examples of important factors that are often connected to different expectations.<sup>35</sup>

The co-operative day care nurseries in Sweden do not form a homogenous group of enterprises. Some of the co-operatives are in fact grounded because of pedagogical/ideological/religious reasons which directly affect the goals and practices of the co-operatives. This kind of common background of parent members and staff lead, basically, to goals of co-operatives that are not as easily changed as the goals of other co-operatives. This does not rule out the possibility of a struggle for power and different views regarding roles of members and staff. However, most of the day care nurseries do not have a specific orientation and most of the parents joining the co-operative have chosen this form of day care for practical reasons - lack of other alternatives, proximity to home etc. For this reason and because of the relative short history of co-operative day care nurseries most of parents have only limited knowledge of their own role within this form of day care organisation. As a consequence, roles of parents and their preferences are formed in many cases after joining. Several studies have shown parents in most cases find the co-operative form as something positive and that parents after some time start to appreciate the potential benefit from participation in decision-making. In other words, parents are socialised into the co-operative institutions relatively rapidly and despite their increased responsibilities, would seldom prefer to change to municipal day care.

## **Conclusion**

Differences between co-operatives and other providers of welfare services, as well as differences between co-operatives and other organisations in general, are to a large extent due to the roles of members. Members in co-operative enterprises are both owners and consumers of services or owners and employees. Furthermore, the formal rules of co-operatives provide a possibility for members to participate in decision making which may lead to an orientation towards the interests of members instead of the interests of external investors. Naturally, these are not necessarily contradictory. In practice, however, in the case of co-operatives providing welfare services, an important issue is who leads the activities of the co-operatives and which goals are prioritised.

Formal rules of co-operatives emphasise the centrality of members and provide them with a possibility to influence activities and the development of their co-operatives. When success of co-operatives depends on active participation of members and when members have common interests, there is a possibility that both formal and informal rules of co-operatives support involvement

of members. However, the conflicting interests of groups of members and possibly between members and managers, may lead to the establishment of rules of behaviour that restrict the active participation of members or some groups of members. This kind of development changes situations within co-operatives so that the goals of enterprises depart from the interests of members or some groups of members.

The co-operative form as such does make a difference, but due to the changing nature of institutions, the special nature of co-operatives providing welfare services cannot be taken for granted. Knowledge of the goals of members, the power of different groups within the co-operatives and the actual development of institutions is needed before conclusions about differences between co-operatives and other providers of welfare services can be drawn.

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