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Editorial

In the last issue, John Kay proposed a 'customer corporation' as a way of taking back consumer control of the UK's privatised utilities. Readers were both intrigued by his references to a consumer co-op model, and disappointed by the lack of firm consumer ownership and board representation in his proposals. Gerald Holtham's reply to Kay argues that he did not go far enough, and that we need a fully mutual society, or at least majority ownership by consumers. Drawing on evidence from utilities in the USA (some of which are consumer co ops), he shows how mutuals really can bring the consumer into decision making and can protect their interests more effectively than can an external regulator. In future articles, we hope to explore further the experience of utility co-ops around the world, and to encourage further work on the mechanics of conversion from private utilities to mutuals, along the lines of the gradual leveraged buyout which Holtham suggests.

We continue the theme of the future of mutuality by publishing edited versions of keynote speeches at our highly successful 1996 annual conference. But we have taken the opportunity to expand the debate to the even wider question of what we, as co-operators, mean by a 'stakeholder society'. An excellent start has been provided by Shann Turnbull in a long and exciting article which identifies a specifically co-operative approach to stakeholding. Drawing on what he calls the 'control architecture' of the Japanese keiretsu and the Mondragon co-operatives, he provides a strong argument for a very concrete form of stakeholding. From the point of view of the Journal, two things should follow from this article. We should be seeking to enter the rather soggy debate about what the British Labour Party means by stakeholding, and to sharpen it up in the direction of a co-operative alternative. And (more uncomfortably) we should be willing to spell out just what Turnbull's argument means for corporate governance in consumer co-ops.

We recently published a polemical article from Peter Davis arguing for a 'value-based' management in co-operatives. In this issue, he applies the argument to worker co-ops, providing a comprehensive demolition of the 'workers control' model of

management, emphasising instead the need for a shared culture between managers and shop floor workers and for managers to be effective leaders. Then he reviews the literature on human resource development (HRD) in co-ops and outlines a comprehensive distance learning programme for co-operative management development. What should be most gratifying to co-operators about this article is that Peter is practicing what he preaches: the Leicester University Unit for Membership Based Organisations has launched a set of distance learning courses for co-operative managers worldwide.

Finally, Rita Rhodes begins what we hope will be a series of short, descriptive articles on co-operation in one country. We need to know what is happening around the world, and this is one quite effective way to find out.

The Water Industry: Why It Should Adopt the Mutual Society Model

Gerald Holtham

There is widespread discontent with the performance of regulation in the water industry following privatisation. In an article in the September *Journal*, John Kay proposed a solution in the form of new public interest companies with statutory obligations. I shall argue that this solution is not adequate to the task and Kay was wrong to reject a more radical reform, namely mutualisation.

In his article, Kay drew attention to the low initial sale price of water companies and the subsequent super normal returns for shareholders and he identified two problems that still beset the industry. The first is that there are only implicit and very weak mechanisms for securing a good share of on-going efficiency gains for customers. The second, and related, problem is that, in the public mind, the system lacks legitimacy. The public persists in regarding water as an essential public service. A system that encourages managers to believe that water companies are capital market vehicles to be manipulated to maximise shareholder value and opposes that viewpoint only with a regulator supposed to defend the consumer interest, will never achieve acceptability. The problems of asymmetric information and regulatory capture are obvious and endemic. The present system dooms the industry to an adversarial relationship between companies and regulator. Both sides will play games, the companies to protect profits and the regulator to protect his political position.

Ultimately, this is not a good situation even for the companies. The great gain from privatisation was to give managers freedom to manage without unnecessary bureaucracy or political interference. But company success now always looks like regulatory failure and sets up political pressures. Political feedback then creates perverse incentives.

That is John Kay's diagnosis of the situation. He points out that the current situation is supposed to incentivize shareholders and, through them, managers. Normally that is appropriate; in

a competitive product market it is possible to serve shareholder interests only by serving consumer interests. There is no necessary conflict between the two. In a monopoly, of course, that is not so. There is a potential conflict of interest. Despite the ingenuity of the government and regulator, over ninety per cent of water will continue to be supplied under monopoly conditions.

Now, given a potential conflict of interest, water companies are not in a position to exploit shareholders since they face a competitive capital market. They have to make and pay adequate returns if they are to attract new capital, be it equity or debt. They can, however, take advantage of consumers. Ideally, therefore, managers should be incentivized to serve the consumer interest. They can only do so if the company stays solvent, invests and is able to attract funds to do so. Given the structures of the markets, the shareholder interest will look after itself in a way that the consumer interest cannot.

Having seen that clearly, and argued it cogently, John Kay proposes the following solution. He wants to define a new kind of company, the customer corporation, subject to a statutory duty to provide customers with what they need at the best price and quality possible. He believes that is what managers want to do anyway and, given that statutory obligation, the present system of appointing boards would be serviceable. Directors would have to balance the -statutory duty with the traditional duty to look after shareholder interests but nothing else need change.

His customer corporation could be owned by an ordinary plc but its accounts, balance sheet and cash flow would be ring-fenced. It could only undertake activities covered by its licence. The regulator would, Kay assumes, have much less to do but one duty would be to police the ring fence and to ensure that plcs were not appropriating the customer corporation's assets or revenue stream.

Kay does not think consumer ownership or representation on boards is a good idea. The only arguments he adduces against these things, however, is the risk of boards divided among themselves and the competitive failure of co-operative retail and wholesale societies in the UK.

In my opinion, Kay runs a great race but stumbles at the last fence. He wants managers to believe it is their primary job to serve the customers but there is nothing in the governance

structure of the public interest company he proposes to encourage that. He is trusting to a cultural hang-over from nationalisation when water utility managers regarded themselves as public servants. It seems a frail reed to lean on so strongly. On the other hand, managers would behave as he wants if the governance structure of the company reflected his priority, if, in other words, the board was ultimately responsible to the consumer. John Kay resists this conclusion out of a general wish to de-emphasise the importance of shareholders. All companies, he believes, are a coalition of interests in which managers have to balance the interests of different stakeholders. He believes that a supposed management wish, in the water industry, to think more about customers is being thwarted by the excessive power of one stakeholder, namely the shareholder. He wants to counter that but has no wish to buttress what he sees as the false doctrine of shareholder primacy by protecting consumers through the device of making them shareholders.

However, if we are not fighting a shareholder versus stakeholder battle on a wide front but are concerned merely with the good governance of the water industry, mutualisation or the creation of consumer co-ops is the obvious solution. This would resolve the inappropriate incentives in the current structure and reduce the importance of the regulator without opening the door to increased political interference and all the consequences of government failure.

Despite Kay's reference to the failure of wholesale and retail co-ops, the empirical evidence is not against mutualisation. The governance structure of retail co-ops was complicated, politicised, and slow-moving but that is not inevitable. Building society boards work much more like those of plcs, and on most measures of efficiency, mutuals have outperformed plcs in the UK financial sector. Over the past ten years, the ten cheapest lenders in the financial sector have all been mutual building societies. Bank of England data show savers have enjoyed higher returns in building societies than in banks for similar term deposits and borrowers have, on average, borrowed more cheaply from building societies. Yet no such society has ever gone bust and no depositor has ever lost money. The current fashion for demutualisation in the sector has more to do with the benefits that current members and management can obtain at the expense of potential future members than with considerations of

efficiency.

The United States also provides an interesting comparison since its electricity utilities include plcs, publicly owned companies and consumer co-operatives. Some 60 studies have been carried out comparing the different forms in terms of costs and returns, measures of static efficiency, and rates of innovation. In a survey of all this work, Lon L Peters found there was no significant difference in the efficiency of plcs and co-ops. Of the 60 studies, 25 found plcs better in some way, 19 found non-plcs better in some way and 16 found no difference. Findings that one or other type of company was better were generally not robust to small changes in method.

The evidence seems to be that we can switch the incentives that managers face, to the general advantage, without suffering any necessary loss of efficiency. Yet the common objection that mutuals or consumer co-operatives are somehow less efficient than plcs is based less on evidence than theoretical arguments. The following propositions are typical:

- if customers get equal shares in the mutual (one member one vote), all shareholders are "small", and the absence of large shareholders weakens practical accountability;
- it may not be worth the while of any shareholder or member to exercise control, given the costs of doing so and the limited benefits;
- there is no real market in company control and so no takeover threat.

However, none of those arguments is particularly strong. Members can appoint a company senate or remuneration committee to set the incentives for managers and these can be as strong as they like in terms of bonuses for meeting performance criteria. Other management teams can offer themselves to members and bid for a franchise to run the company, promising better performance, or accepting weaker incentives. Large customers may only have one vote but their commercial exposure to the water company should give them an adequate incentive to lead and organise consumer representation in order to maintain accountability. Representatives of smaller consumers would surely become active if it appeared the larger members were taking advantage of them. Since no-one would

have the ability to "exit" - everyone needs water - the right to "voice" would be exercised.

While there are theoretical problems in the principal/ agent relationship of members of a mutual and its management, the same is true of a plc - 'recall the many recent debates about corporate governance to which Kay is a distinguished contributor. If anything, economic theory tends to support the view that the mutual form is likely to lead to more socially efficient outcomes where there is monopoly. Oliver Hart and John Moore analysed the case of a stock exchange and asked whether it should be owned by its members or by an outside capitalist. The structure of their argument applies to other forms of enterprise too - they also apply it to a golf club. They find that, so long as all customers are treated similarly (e.g. all customers are charged the same price), outside ownership becomes more efficient in allocating resources, relative to a mutual structure, as the market becomes more competitive. When there is monopoly, the mutual structure is likely to be better.

In the case of water, so long as the consumer interest was clearly predominant, it would not be necessary to go all the way to full mutuality. A consumer majority holding that left some shares in individual or institutional hands would do. The private shares would fetch a lower price since they could never confer control of the company. Pure equity would therefore be somewhat more expensive for the quasi-mutual water company, but that would simply incline it to raise more of necessary capital by issuance of preference shares or debt. Since the water business is a very low-risk, stable and mature business it is appropriate for companies to carry more long-term debt than they typically now do. US electricity co-ops are 100 per cent debt financed.

Private holdings would enable plc companies to continue to hold shares in water companies but, in that case, separate accounts and balance sheets would be obligatory just as in the case of Kay's public interest corporation. Another common advantage would be a considerable reduction in the scope of regulation. Price control would not be required. The regulator would merely police the operation of the quasi-mutuals, their relationship with any plc shareholders, and publish comparative data on the performance of different companies. However, I believe a structure of the type I propose would more surely resolve the current problem that customers do not stand to gain

from efficiency gains and would improve the distribution of benefits between customers and shareholders.

Mutualisation could be brought about gradually if water companies used cash flow to repurchase their own shares, which could then be placed in trust for consumers. Given the difference in return on debentures and water company shares, it would be appropriate to issue debt for share repurchase - a leveraged buy-out on behalf of customers. Over time, a rising proportion of the company would be owned by the consumers. Dividends accruing to shares in the trust would be paid out to consumers annually as a rebate on water bills. Consumers would be encouraged to develop representative structures so that they could vote the block of shares. There is no obvious reason why companies should do this voluntarily so the government should apply fiscal incentives or penalties to set the ball rolling.

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Co-operation in Mongolia: A Tale of One City and Two Visits

Rita Rhodes

The city is Ulan Bator, the capital of Mongolia and the first visit was made during the winter of 1991 and spring of 1992. For six months I worked on a training programme under the auspices of UNIFEM, the United Nations' Fund for Women, and the Co-operative Branch of the International Labour Organisation. The aim of the programme was to assist the Mongolian Women's Federation train Federation members in forming workers' co-operatives. It was hoped that these would help to combat rising unemployment among women, caused largely by the privatisation of state industries, and also encourage the development of democratic skills. The second visit occurred four years later - last spring. I was then invited to present a paper on co-operative human resource development and the Mongolian co-operative movement in the context of democratisation and structural reform to a National Workshop on Co-operative Reform and Development in Ulan Bator. This was organised jointly by the Union of Mongolian Production and Service Co-operatives and the Co-operative branch of the International Labour Organisation. Together the two visits gave some idea of the problems that co-operatives face in a transitional period, and the rest of this article expands on some of the impressions gained.

By the end of the first visit, I was not at all optimistic about the prospects for Mongolian co-operation. A number of factors were working against the restructuring of the existing state-directed movement into one made up of voluntary societies. One was people's attitudes which had been shaped by 70 years of communism; Mongolia was, in fact, the world's second oldest communist country. Its People's Revolutionary Party had come to power in 1921, throwing off two centuries of Chinese domination but then the country became a Soviet satellite state. Almost 70 years later the collapse of communist regimes in central and eastern Europe triggered unrest in Mongolia. In July 1990 elections broke the hold of the People's Revolutionary Party and a transition to a more liberalised economy began. However,

communism had deep roots and had shaped people's attitudes in many ways. For example, some officials tended not to be sympathetic to, or were sceptical of, voluntary co-operatives: I later learned that a number of these officials became prominent private entrepreneurs. Ordinary people, on the other hand, were used to the state organising their lives and showed few signs of individual initiative. An example in this respect was a lack of tradition of private savings, a fact that would later impinge on people's ability to subscribe co-operative share capital. This situation was not helped when the 10,000 Tugrik voucher they received from the privatisation of state industries was quickly wiped out by rampant inflation. Another factor militating against support for voluntary co-operatives was that ordinary Mongolians had developed a healthy disregard for state co-operatives. They were therefore little inclined to experiment with another form of co-operative, particularly one that was still collective but in which they would have to take responsibility.

Such unfavourable attitudes were compounded by bad conditions that were worsening by the day. Mongolia was already classified by the UN as an LOC - a Least Developed Country. Its two main staples were meat and flour. Vegetables were seasonal and limited by severe climatic conditions which permitted only 120 growing days in a year. Most other goods had to be imported, mainly from the Soviet Union, although there were undeveloped oil reserves in the west of the country. The break up of the USSR caused considerable disruption to supplies. Previously well-stocked food shops became empty. Supplies of medicines and drugs fell dangerously low and broken windows could not be repaired because no glass was coming in from Russia. During my first visit, bakeries came to a standstill because there was no yeast, but that dilemma was solved when the government sent a 'plane specially to Beijing to bring back a consignment.

Alongside of food shortages there was rising inflation. That reached an annual rate of 350 per cent between my two visits, but by last May (1996) was down to some 50 per cent. During my first visit further problems were created by procurement systems breaking down. An example was the state leather factory in Ulan Bator which temporarily ceased production because it was not receiving skins: Mongolia then had a livestock population of 25 million! Unemployment, previously unknown, was rising. By May 1992 it was estimated to have risen to around 100,000,

out of a total population of just over 2 million. But then, it was not possible to be certain because systems for recording unemployment were new and uncertain, never having been needed before. Unemployment benefit was 280 Tugriks a month, then about US\$1.50.

Such a situation pointed to the fact that there was little infrastructure. Its institutions were often inappropriate for a liberalising economy and its physical features were even more limited. In a country four times the size of France, there were around only 1,700 kilometres of metalled road, running north and south of Ulan Bator. Local markets were therefore limited in size which had implications for production levels.

Linked to the question of poor infrastructure was inappropriate legislation, certainly as far as voluntary co-operatives were concerned. We should perhaps note that the first Mongolian co-operatives had been consumer societies which began forming in the 1920s. Workers' co-operatives followed a decade later while agricultural societies did not appear until the 1950s. It was shortly after this that the state began to intervene in co-operatives, first in consumer Societies. Impressed by state-run enterprises in China and wishing to encourage cross-border trade; the Mongolian government dissolved consumer co-operatives in 1959 and converted them into state-owned businesses. During the late '60s and early '70s, agricultural co-operatives also came under increasing government control as a means of setting production targets and prices. Workers' co-operatives soon followed, and by 1974 no independent societies survived

However, it was among workers' co-operatives that the first signs of independence began to appear. New ones developed in the late 1980s and were strong enough to form the Mongolian Union of Production and Service Co-operatives in 1990. This began to spearhead moves to create a more favourable climate for the development of independent co-operatives, including pressing for a new Co-operative Act. For a number of reasons, it was not immediately successful, but the main one was the passing of the Economic Body Law in 1991. This encompassed all types of business and, unfortunately, included no special category for co-operatives. Consequently, they could be private businesses, joint stock businesses or partnerships but with the label "co-operative"! Worse still, there was a strong reluctance by Mongolian civil servants and the government to consider even

amending the legislation, let alone repeal it. While the Mongolian Parliament might no longer be under the control of a single party, it was not yet versed in the ways of passing, repealing or amending legislation. In any event there had been strong opposition to passing an act that allowed private enterprise. In these circumstances a reluctance to engage in further battles was perhaps understandable. Another factor compounding the difficulties was that, with the state only just beginning to pull back, there was limited knowledge about the variety of business forms that existed in other countries. In the final analysis the Economic Body Law was inappropriate for co-operatives and also laid down a bureaucratic procedure of registration through local authorities.

When I left Mongolia at the end of my first visit, the Mongolian Union of Production and Service Co-operatives was drafting proposals for new co-operative legislation but was not confident of success. On my return last May, I found that they had ultimately been successful with the passing in 1995 of specific co-operative legislation. This represented quite a turn round and far greater co-operative progress than I had expected. Besides the Union of Production and Service Co-operatives there were now two further Unions, one among consumer societies and the other among agricultural co-operatives. Societies in both sectors had been helped by their counterparts in Japan and also through links with the regional office of the International Co-operative Alliance in New Delhi. Indeed, the Mongolian Central Consumer Co-operative Union, formed in 1992, had affiliated to the ICA in 1993. In 1992 also the National Association of Mongolian Agricultural Co-operatives had begun to form. However, delays in the process of privatisation meant that its rules had not finally been agreed until 1994.

I returned to Mongolia to find that not only had the co-operative sector grown but that it had been successful in getting a separate Co-operative Act. Moreover, it had sufficiently grown in confidence to be aware of deficiencies in this new legislation and was already considering drawing up proposals to amend and improve it. There had obviously been increased awareness of what was specifically co-operative and also greater sophistication among Mongolian parliamentarians in handling legislative changes. It was thus a great pleasure to meet the presidents of the three national co-operative unions and to hear

their contributions to the Workshop. Each described the difficulties of transition that their sectors had experienced. For example, there had been a decline in the number of co-operatives in the shift from state to voluntary societies. There had also been the problem of co-operative property which, as one president said, had been lost to the state on three occasions but had now been "put into the stock market and therefore privatised." Another problem had been that of trade being hampered by increasing poverty. However, in some areas this poverty was causing some to look anew at possible co-operative solutions. In the agricultural sector, however, it was thought to be a race against time to teach cattle breeders about co-operatives before they fell too far into the hands of traders and money lenders.

Inflation complicated everything. However, one co-operative I had met four years previously, and was able to revisit, showed that it could still function despite it. Organised as a workers' co-operative it had first opened a shop and had since built a restaurant and a hotel. Such expansion must have required much nerve during a period of rapidly rising prices. However, the Co-op was now reaping the reward with a thriving trade among the growing numbers of foreign skilled and technical workers passing through Ulan Bator.

Despite all the above difficulties a stronger co-operative identity appeared to be emerging in Mongolia. Thus, the workshop was able to debate distinctly co-operative issues. One was whether it was best to have a single Co-operative Act or whether it might not be desirable for each sector to have its own act. Workshop participants made it clear, however, that whatever kind of co-operative legislation they pressed for in future, they would ensure that it reflected international co-operative principles. Another distinctly co-operative issue concerned taxation. Mongolian co-operators were chaffing under a "double taxation" whereby members' dividends were also taxed (sounds familiar!). There was also discussion on what the functions of co-operative unions should be.

The cumulative impression from these discussions was that Mongolian co-operators were anxious to learn what was happening in co-operative movements in other countries and to establish links. Besides the practical aspects of voluntary co-operation, they also seem keen to popularise its underlying ideas. A heartwarming incident illustrated this. During my first

visit I left a number of copies of Will Watkins' book *Co-operative Principles - Today and Tomorrow*. Imagine my pleasure, therefore, when I found on my second visit that the President of the Mongolian Union of Production and Service Co-operatives had had one of these copies translated into Mongolian and some thirty duplicated copies distributed. Will was a past and much-admired President of the UK Society for Co-operative Studies. I am sure that its other members will share my pleasure that his work survives, and his co-operative advocacy continues. I can almost hear him chuckling at the thought of being translated into Mongolian!

Rita Rhodes is an author and writer on International Co-operation.

John Morley OBE: A Profile

Lily Howe

John Morley was a broad man of quality who gave of his talents in many places and in diverse fields. Most notable was the outstanding intellectual and realistic leadership he gave to agricultural co-operatives over many years. A president of the UK Society for Co-operative Studies for 10 years until he died last October, he carved a life exceptionally rich in experience and interests, moving from one environment to another with easy grace. John's talents and open, inquiring mind quickly absorbed him into different spheres, his personality - he had a fine sense of humour - attracting firm friends.

In his middle years he could have been found totally at home in London's Athenaeum, quizzically quoting Proust in asides when debating with colleagues how best to move forward in seemingly intractable situations. His later life centred on his retirement village where his cultural interests continued when he entered into the community through his writing and artistic skills.

John succeeded in two professional careers: the first overseas in the Colonial Service; the second in the UK where his major role was in agricultural co-operative development. His earlier student years indicated the breadth of his talent, for even as a student he was broader than a scholar. Achieving first class honours in Classics and an upper second in History at Corpus Christi, Cambridge, his lifelong practical skills helped him also to qualify as a pilot in the University Air Squadron.

Then followed 20 years of overseas service, his last four-year assignment in the Gold Coast, now Ghana, where he was Special Commissioner for Development Corporations and Marketing Boards, stimulating his interest in co-operatives and forging the link for his second career in the UK. The scope of his exotic background in times before the world became a much smaller place would have surprised many co-operative colleagues in later life.

His Colonial Service career began as a District Officer in Northern Nigeria. But with the outbreak of war, John born in

1914, was commissioned in the West African Frontier Force and posted to Eritrea. There he assisted in setting up a British Military Administration for the former Italian colony and was awarded the MBE. Next came two years of similar service in the newly liberated colony of Singapore where he was demobilised as a Lieutenant Colonel in 1946. He stayed on in Singapore in the Colonial Secretariat and then moved to Kuala Lumpur in the Malayan Federal Secretariat. There he was appointed Deputy Economic Secretary and was for a time a member of the Executive and Legislative Assemblies.

His last assignment to the Gold Coast came when the Colonial Service was rapidly contracting as colonies and protectorates became independent. At 42 in 1956, with a wealth of executive experience together with first hand knowledge of developing countries in Africa and of future tiger economies further East, he returned to England to join his family and to seek a new job.

John's agricultural co-operative career began the same year when he was appointed chief executive of the Agricultural Central Co-operative Association, soon becoming recognised as an expert in his new field. As Britain prepared to join the European Community the Central Council for Agricultural and Horticultural Co-operation, later to form the basis for the national food promotion agency Food from Britain, was established. John was appointed planning officer helping to develop agricultural marketing structures. Later he became vice-chairman of the European Agricultural Confederation. In 1983 he was appointed OBE for services to agricultural co-operation. Earlier, in 1975, his book "British Agricultural Co-operatives" was published, soon to be regarded as a standard reference book. He loved to write, and colleagues recall the elegance of long sentences beautifully constructed.

John expanded his interest in other co-operative sectors when in 1978 he was appointed to the first board of the Co-operative Development Agency. Originally set up by parliament with considerable advisory and promotional powers to assist broad co-operative development the CDA became over the years, after an early change of government and reduced funding, mainly concerned with facilitating the growth of employment generating worker owned co-operatives. John was one who held to the original broader view. He was a firm advocate of co-operation between co-operatives: between sectors and between individual

organisations. He drafted a constitution for an organisation he envisaged could bring together all forms of co-operatives in the UK. Following the demise of the CDA in 1990 this draft was used as the basis for the UK Co-operative Council, set up by the co-operative movement, which happily is fulfilling the original vision of the CDA without being subject to outside control.

Parallel with his professional life was John's long, dedicated voluntary service to the Plunkett Foundation. This began in 1959 when he became a trustee, going on to chair the Foundation with style and impeccable courtesy from 1979 to 1984. Like the distinguished chairmen before him he gave the Foundation authority, time and thought, his overseas experience contributing to the expansion and quality of its world-wide development work.

When he retired from active involvement in Plunkett he maintained a lively interest becoming an honorary trustee and in 1996 the Foundation's first Fellow. Early that year he quietly deposited with Plunkett a gift with which the Foundation proposes to establish an International Leadership Programme, inviting other donations.

In retirement, their three children having left home, John and his wife Pat moved from Surrey to Langstone, Havant, where in his seventieth year he took up sailing - "in a very small boat" he used to say. In his later years John was assailed by Parkinson's disease. But he was not a man to allow this to diminish him. His gardening he had to forego. Then his creative skills turned to family and local history and to restoring chairs with caning, rushing and tapestry covers. John's skills were matched by those of Pat with her painting, glass engraving and writing. Together they put on exhibitions of their work one of which he was planning in the days before he died.

Men of John Morley's quality and breadth are rare. That he chose to give so generously of his talent and his time to the co-operative concept is a stimulus for future development.

Lily Howe served with John Morley as a Plunkett Foundation trustee and as a CDA board member.

Stakeholder co operation

Shann Turnbull

Abstract

Some of the most successful businesses in the world involve employees, customers, and suppliers in their control. This paper describes why this is so and how stakeholder governance could be introduced into English speaking countries. The competitive advantages of establishing co-operative relationships with stakeholders is illustrated by analysing a Japanese keiretsu and the stakeholder co-operatives found around the Spanish town of Mondragón. These are shown to share common features in their information and control architecture which are also shared by all living things which depend upon obtaining feedback information from their environment to exist. Elements of information theory, which is used to design self-regulating devices, are introduced to indicate how firms could be designed to mimic life forms to become self-regulating. Beside introducing competitive advantages, this would minimise both the internal and external costs of regulation. The paper recommends that governments provide leadership in introducing competitive self-regulation using the strategy proposed by the US Vice President. The result would be to create a "Stakeholder Economy".

There is an abundance of compelling evidence that co-operative relationships with strategic stakeholders provide firms with competitive advantages. The evidence is particularly persuasive as much of it arises from the for-profit sector. However, the participation of stakeholders in the governance of firms seems to be largely ignored, even by those who profess co-operative values. There are a number of possible reasons for this neglect. There is the cultural hegemony of competitive values which inhibits those with co-operative values from promoting participation outside a business in case they are seen to have questionable business acumen; there are industry and legal concerns in establishing formal relationships with customers and suppliers and there is lack of experience and knowledge of how to structure value-adding relationships with external

stakeholders. The objective of this paper is to make a contribution towards countering these reasons.

Who are stakeholders?

First, let us consider who are stakeholders. An accepted definition of a stakeholder is still evolving in the academic literature. A leading contributor is Freeman¹ who, quoting the Stanford Research Institute (SRI) describes "those groups without whose support the organisation would cease to exist". Freeman had his own definition which is widely used: "A stakeholder in an organisation is any group or individual who can affect or is affected by the achievement of the organisation's objective". Clarkson² considered this definition too broad and defined stakeholders as "persons or groups who either voluntarily or involuntarily became exposed to risk from the activities of a firm". However, this definition does not make it clear if a person would be a stakeholder if they were not at risk but could obtain a benefit. This uncertainty is removed by the definition of Donaldson and Preston³, who state: "Stakeholders are identified through the actual or potential harms and benefits that they experience or anticipate experiencing as a result of the firm's actions or inactions". Preston⁴ qualifies this definition by stating "persons and groups who gain only when the organisation as a whole loses are not stakeholders, although they may well have an interest - albeit a negative one - in its activities".

The academic nuances in defining a stakeholder need not concern those interested in the practical matter of how stakeholders might make a contribution to sustain a business and add value. From this perspective it is clear that it makes sound business sense to at least concern ourselves with "those groups without whose support the organisation would cease to exist". As the very existence of a firm is dependent upon such groups I will define them as strategic stakeholders. As employees, customers and suppliers are essential for a modern firm to exist, they meet the test of being strategic stakeholders. Suppliers would include members of the host community. Investors without any other role may not be essential, as occurs with labour owned firms. Even when investors are required, they may not remain essential for an unlimited time. Firms become self-financing and may even buy-out their original investors as occurs with management buyouts

FIGURE I

Investor view of a firm (Adam Smith)

(Marxist and financial economists reverse the customers and investors arrows!)

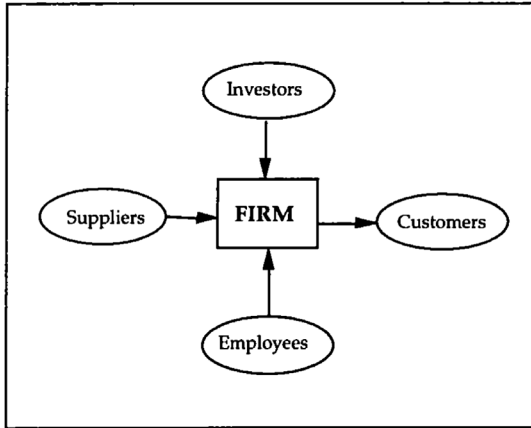
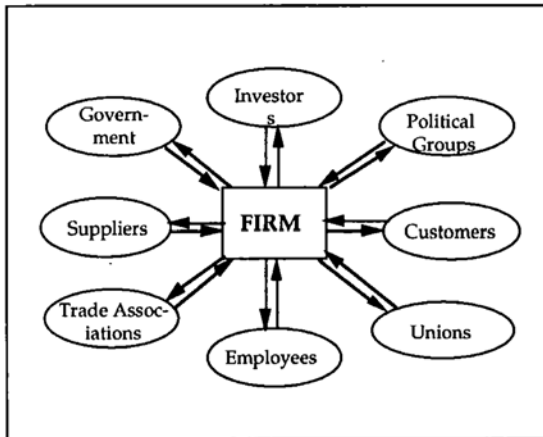


FIGURE2

Stakeholder view of a firm



and 100% employee-owned companies. The property rights of investors in firms established as a joint venture commonly expire after a specified time, especially for foreign investors in some countries.⁵ Investors may not, *per se*, always meet the test of being essential for the firm's existence.

The stakeholder view of a firm

In defining "Stakeholder Theory" Clarkson states:

"The firm" is a system of stakeholders operating within the larger system of the host society that provides the necessary legal and market infrastructure for the firm's activities. The purpose of the firm is to create wealth or value for its stakeholders by converting their stakes into goods and services.⁶

Figures 1 and 2 are used by Preston⁷ to illustrate the difference between an investor view of a firm and a stakeholder view. The arrows are used to indicate the direction of contributions made by the various stakeholders from the various viewpoints. As noted by Kay,⁸ the legal obligation of directors is to investors rather than to customers, i.e. it follows the viewpoint of Marxists and financial economists. The stakeholder view recognises that firms do not exist in isolation. Both their existence and their operating discretions are subject to other agents in society. Society creates the laws which allow firms to exist and operate. These are becoming increasingly complex and burdensome. Later I will outline how these burdens can be reduced by adopting the lessons of nature in managing complexity.

In the last century, European and US companies were chartered for a specified time as were firms established under the Queensland Mercantile Act of 1867.⁹ In the US, charters could be cancelled earlier for "fraud, negligence, misconduct", "abuse or misuse of its power, privileges or franchises", or "acts contrary to public policy".¹⁰ Charters did not provide investors with limited liability at that time. The purpose of a charter was to allow the enterprise to exist as a business entity or in the words of the RSA,¹¹ a "licence to operate".

Delaware voters passed a constitutional amendment in 1831 limiting all corporate charters to twenty years. Other states, including Louisiana and Michigan, passed constitutional

amendments to place precise time limits on corporate charters. President Andrew Jackson enjoyed wide popular support when he vetoed a law extending the charter of the Second Bank of the United States in 1832. That same year, Pennsylvania revoked the charters of ten banks.

During the 1840s, citizens in New York, Delaware, Michigan, and Florida required a two-thirds vote of their state legislatures to create, continue, alter, or renew charters. The New York legislature in 1849 instructed the attorney general to annul any charter whose applicants had concealed material facts, and so sue to revoke a charter on behalf of the people whenever he believed necessary.¹²

During the last century, accountability to a broad constituency of stakeholders transcended accountability to investors. This state of affairs was reinforced by a broadly based grass roots political mandate to amend state constitutions. The possibility of the "licence to operate" being cancelled provided a very strong incentive for investors to control managers so that the business operated in a socially responsible manner. This has profound significance for what is now called "corporate governance". Last century, unfair trading did not result in a fine as occurs today but in a company losing its right to exist! I will develop this point later. There are also important lessons in the way firms have persuaded legislators during the last century to reduce their social accountability.¹³

A devastating description of how these processes are still proceeding in the US was presented earlier in 1996 by Monks.¹⁴ The process by which US directors have reduced the ability for even their shareholders to vote them out of office or elect individuals whom the directors do not favour, is described by Gordon.¹⁵ This has allowed many US Chief Executive Officers (CEOs) to control the composition of their board. This power has enabled them to persuade their boards to pay them millions of dollars in annual remuneration. Fukao reports: "that US CEOs receive about two to three and half times as much money as Japanese Managers".¹⁶

Competitive advantages from co-operative stakeholder relationships

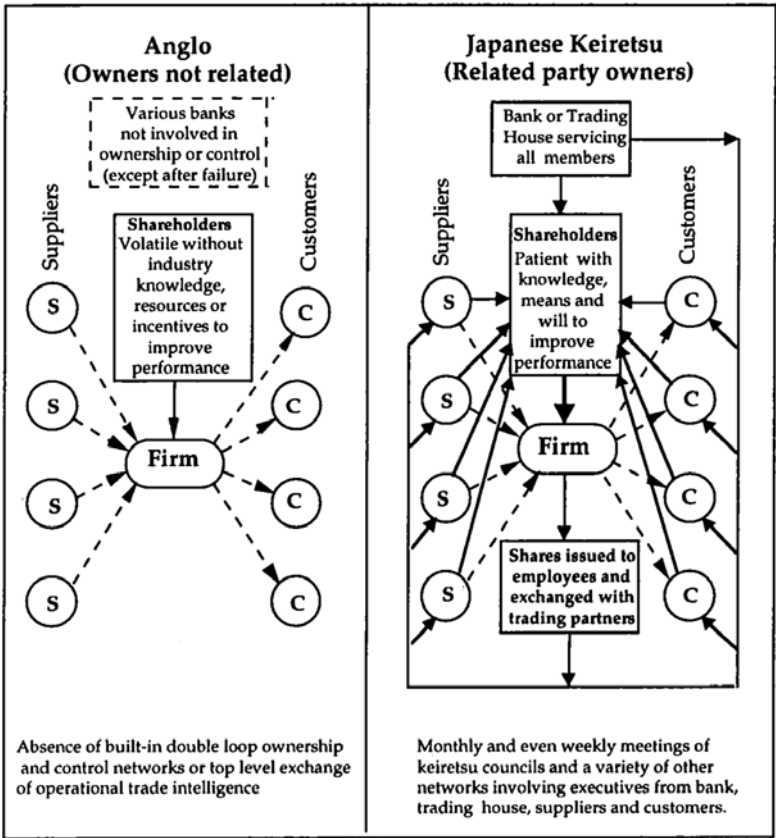
Let me illustrate with practical examples the nature of the

competitive advantages which can be obtained from the establishment of stakeholder relationships. The first example involves firms in a Japanese keiretsu and the second example the stakeholder co-operatives found around the town of Mondragón in the Basque region of Northern Spain.

Analytica reports that: "It has become standard practice among Japanese companies to exchange small amounts of stock with lenders and business partners as a gesture of goodwill, sincerity and commitment".¹⁷ These shares are rarely sold, creating a stable block of shareholders who typically own 60 to 80 per cent of all shares. Only 20-30 per cent of all shares tend to be in general circulation. According to the International Labour Office, "Over 60% of companies have ESOPs" with profit sharing bonuses being equivalent to around 25% of employee pay, which makes Japan "the country where the financial participation process is the most advanced".¹⁸ As a result, a controlling interest in many major Japanese companies is held by strategic stakeholders. The arrangement is illustrated in Figure 3 for a company which is a member of a *keiretsu*. A keiretsu is a group of companies with related trading interests through being suppliers or customers of each other and a lead member who may be a bank or trading house. The CEOs of each strategic stakeholder meet monthly, and sometimes even weekly, as a keiretsu council. There are a number of very persuasive competitive advantages provided to a business through establishing close co-operative relationships in this manner.

The first advantage is that the controlling shareholders obtain expert inside information, *independent of management*, on the performance of management. Compare this situation with "Anglo" firms with a unitary board as found in England, US, Australia, and other English-speaking countries. Even if the executive directors are themselves experts, they may not obtain information which reflects the viewpoints of their customers, suppliers, and workers. Even if executives did obtain such information from their strategic stakeholders, the outside directors would need to obtain it independently of management to allow them to carry out their legal obligations to diligently monitor and evaluate management in either private or public sector corporations.¹⁹ However, when a director is truly independent she/he cannot have access to inside information to evaluate management. Nor is he/she likely to have specialised

FIGURE 3.
Comparison between Anglo and Japanese
dispersed ownership and control architecture



S = Supplier
 C = Customer

Ownership ———→
 Trade activity - - - ->

Source: Analytica 1992

firm or industry specific information to add value. In referring to independent outside directors, Hawley and Williams state that:

Directors inevitably can not know as much about the firm as management. Most importantly, directors do not devote their entire professional efforts to a single company and therefore are not enmeshed in the day-to-day information flow of the company. This is compounded by management's control of the information that does reach the board. The result can be a board knowing too little, too late and, even if it is willing and able to act to confront a growing problem or crisis, it is often unable to do so.²⁰

The question of directors being "willing and able to act" is the second advantage of involving strategic stakeholders. Even if independent directors on a unitary board have the knowledge to act, they may not have the will and power to act because they are loyal or obligated to management and/ or hold their board position at the grace and favour of management.²¹ Compare this situation with members of a keiretsu council where each member is a CEO with his own independent constituency with expert inside knowledge and a long term interest in being associated with a value adding trading relationship. While each CEO may not hold sufficient votes to take any decisive action alone, his colleagues do have the numbers to act. And act decisively and constructively they do. Kester describes how Akai, a consumer electronics firm, was re-organised by its customers, suppliers, and bankers when it began to fail.²² Identical mechanisms exist for the stakeholder co-operatives in Mondragón.

A third problem with a unitary board without oversight by strategic stakeholders is that management may not be adequately informed. This problem is inherent in all hierarchies be they made up of private sector executives or officials in government bureaus. For individuals who do not act as a team but establish coalitions of personal interests, Downs describes four biases:

1. Each official tends to distort the information he passes upward to his superiors in the hierarchy. Specifically, all types of officials tend to exaggerate data that reflect favourably on

themselves and to minimize those that reveal their own shortcomings.

2. Each official tends to exhibit biased attitudes towards certain of the specific policies and alternative actions that his position normally requires him to deal with. These attitudes will result from his biases in favour of policies that advance his own interests and the programs he advocates and against those that injure or simply fail to advance those interests or programs.

3. Each official will vary the degree to which he complies with directives from his superiors, depending upon whether those directives favour or oppose his own interest.

4. Each official will vary the degree to which he seeks out additional responsibilities and accepts risks in the performance of his duties, depending on his own particular goals.²³

Directives from a superior usually require interpretation by a subordinate to be put into practice or passed down to the next level of the hierarchy. This allows considerable variance to occur in the way decisions are implemented. Reports on how decisions are implemented, and their consequences need to be condensed as they pass up the hierarchy. "The need for condensing information is an essential part of the bureau's communication process. Otherwise, the top man would be buried under tons of facts and opinions."²⁴

Information integrity

The cumulative affect of condensing qualitative information was examined by Tullock.²⁵ Tullock assumed that the quantity of information gathered by each official at the lowest level of the hierarchy was one unit of data for each unit of time. He considered the example of a hierarchy with seven levels with each level having a span of control of four people. This would mean that there would be 4,096 officials at the bottom level collecting 4,096 units of data in each time period. If the average official screens out only half the data given to him then the top official will receive a total of 1/64 of all the information, or 64 units per time period. The winnowing process will have omitted 98.4% of the data originally gathered.

However, the quality of the information at the top of the

hierarchy "will probably be very different from that originally put into the communication system at the lowest level".²⁶ The substantive content of the information would be subject to distortion from the biases of each official who was responsible for its condensation as it passed through each level in the hierarchy. Yet it is the qualitative aspects of employee relations, product quality, customer service and supplier relations that provide competitive advantages. The integrity of qualitative information²⁷ and the integrity of the parties to the transaction²⁸ can be a deciding factor if business is to proceed. To minimise transaction costs and risks, trust needs to be established. The participation of strategic stakeholders in the governance of a firm provides a basis to establish trust and so more efficient and effective communications than can be established by market relationships.²⁹

Firms exist because market price signals cannot be used to communicate qualitative information like trust, or if they can be used, price communication is not as efficient as people communicating directly between themselves with sight, sounds and symbols through working together in a team, group, or hierarchy. In other words, firms exist because they economise the volume of information required to organise economic transactions. By economising information, firms reduce the cost of transactions. Firms exist because markets fail to economise the cost of organising transactions.³⁰ Stakeholder participation provides a way to further decrease the need and cost of obtaining information through markets. It is well known that bad news travels slowly or not at all. There are substantial incentives for subordinates to withhold, or selectively report any information to their superior which may reflect on themselves. There are likewise substantial incentives for subordinates to report information which can excuse poor performance. In a keiretsu, the subordinates in the supplier and client organisations will be selecting quite different information to report up the hierarchy than the subordinates in the producer firm. The parallel channels of information from strategic stakeholders with different perspectives provide the basis for a keiretsu council to obtain more accurate information than can be obtained by directors without access to strategic stakeholders.

However, beside stakeholder participation providing advantages in corporate governance it can also provide important

operational competitive advantages. Modern management techniques such as Just In Time (JIT) delivery of supplies, Total Quality Management (TQM) of output, other quality assurance processes, worker participation, and autonomous learning centres, contribute to non-market relationships. All these relationships involve the participation of strategic stakeholders in the information and control system of a firm. Jones states: "The firm will gain competitive advantages if it is able to develop relationships with its stakeholders based on mutual trust and co-operation".³¹ He points out that American auto firms are not as competitive as Japanese firms because they incur the costs of bureaucracy from vertical integration. Japanese firms avoid these costs by establishing trusting relationships with their suppliers. Likewise, US firms incur more transactions costs from employee turnover than Japanese firms. Processes for defining and auditing quality production have now been established by the International Standards Organisation (ISO). In some firms, ISO processes are becoming institutionalised as a governance mechanism for productive activities through the establishment of forums constituted by, and accountable to, strategic stakeholders. A keiretsu council is composed of strategic stakeholders who have the knowledge, means and incentive to improve operations as they did for Akai.

All the above competitive advantages of a Japanese keiretsu are shared by the Mondragón stakeholder co-operatives which have woven a much richer web of strategic stakeholder participation. The information and control architecture of a typical industrial co-operative is shown in Figure 4. Figure 5 shows the architecture of a "Relationships Association" or Group of industrial co-operatives which follows the pattern established in Figure 4. This recursive pattern is replicated in the architecture of the whole group which constitutes the Mondragón Corporación Cooperativa (MCC) outlined in Figure 6.³²

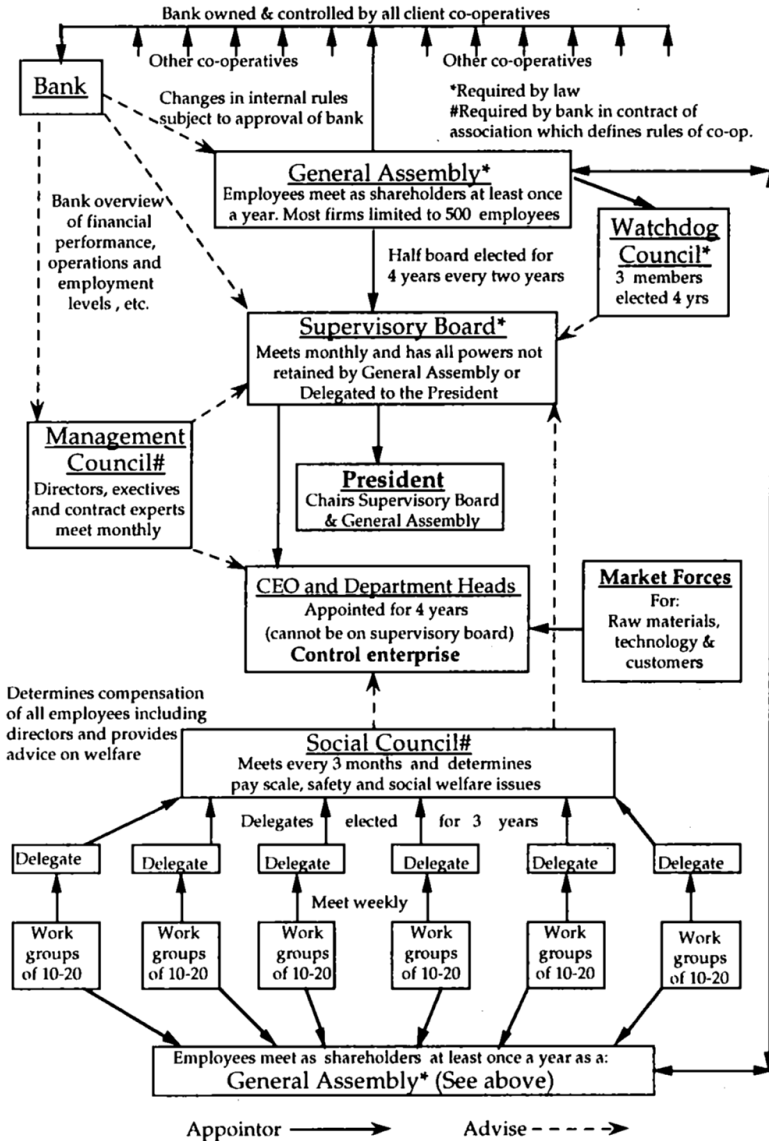
Stakeholder participation as a strategic variable

The corporate architecture in Mondragón is treated as a strategic variable rather than being culturally determined and fixed as it is in Japan and elsewhere. The control of each type of Mondragón firm is designed to match the nature of its business.

Control in Mondragón co-operatives is exercised through a

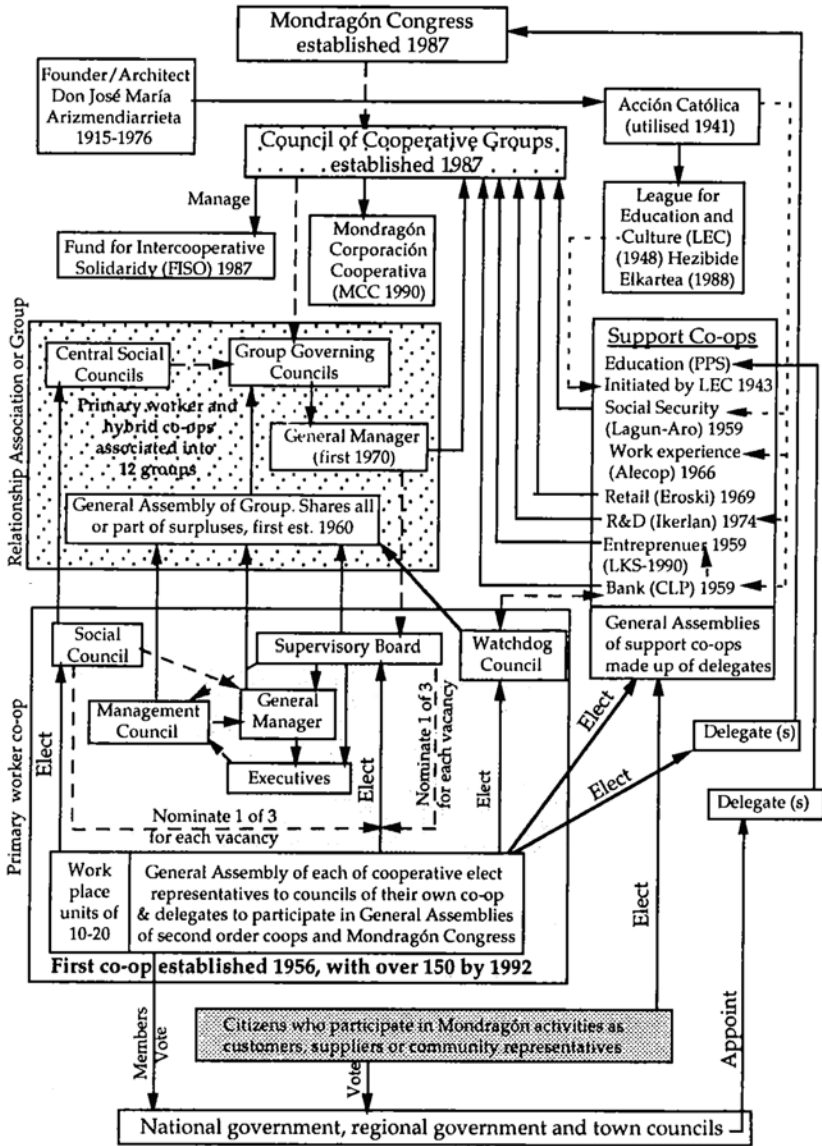
FIGURE4

Governance of Mondragón Worker Cooperatives



Sources: Ellerman 1982; Whyte & Whyte 1988; Morrison 1991

FIGURES
Mondragón Cooperative Social System
 (with dates of establishment)

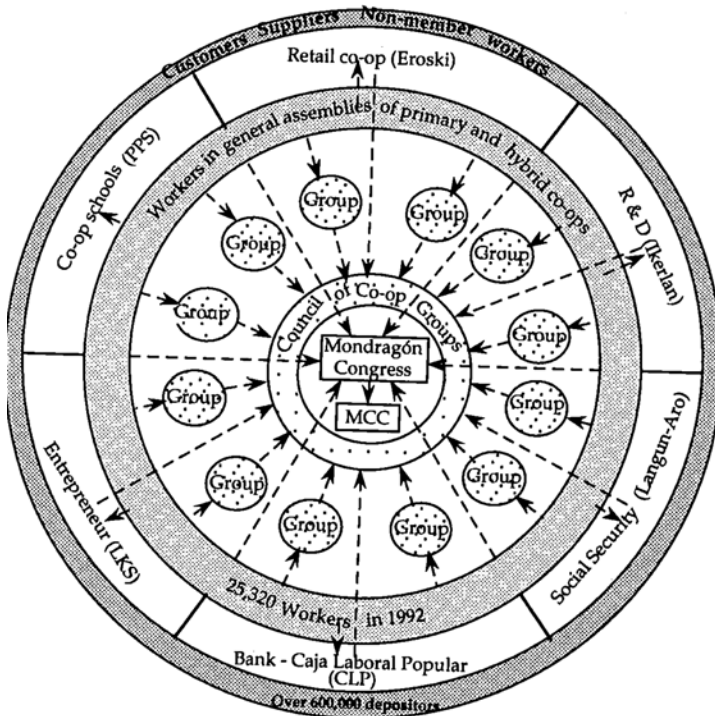


Vote, appoint, delegate, manage: —> Advise or nominate: - -> Start up: - ->

Sources: CLP, 1992; MCC, 1992; Mollner 1991; Morrison 1991; Whyte & Whyte 1988

FIGURE 6

Control Network of Mondragón Activities



More than 150 primary worker and hybrid co-ops are associated into 12 groups or relationship associations
 Total 1992: Assets US\$6.3 bn.; Sales US\$3.0 bn.; Exports US\$380m.

Sources: Whyte & Whyte (1988); Morrison (1991); MCC (1992)

supervisory board (as shown in Figures 4 and 5). Like a keiretsu council, only strategic stakeholders participate in the supervisory board which represents a "stakeholder council". By definition, independent directors cannot be stakeholders with an operational interest. As there is little point in having such people involved in the governance of a Japanese keiretsu or Mondragón co-operative, few are found. Compare this situation with Anglo firms where independent directors are perceived as a requirement of good corporate governance.

The opposite situation is found on the supervisory boards of Mondragón industrial co-operatives where only employees are appointed! As each industrial co-operative is a member of a Relationship Association or Group (as shown in Figures 4 and 5) and the Group has as its members supplier and client companies, like a keiretsu, all strategic stakeholders participate in control of their members. Customers appoint half of the supervisor board and the chairman of the large retail chain store *Eroski*. Firms which process primary products like *Miba*; *Barrenetxe*; *Behi-Alde*; and *Udala* have half their supervisory board appointed by workers and the other half by the farmers who are their suppliers. The student work experience co-op, *Alecop*, has its supervisory board made up of its three strategic stakeholders with equal numbers of staff, students, and parents. The composition of the supervisory board of the piggery, *Artxa*, reflects the proportion of value added by each class of stakeholder being the customer (*Eroski* retail store); pig farmers (*Anoga*) who fattened progeny for the co-op under contract; a supplier of feed, equipment, and veterinary services (*Miba*), and workers of *Artxa*.³³ Co-ops which support other co-ops and have them as shareholders are described as secondary co-ops. These include the bank, *Caja Laboral Popular* (CLP), social security co-op, (*Lagun-Aro*), and the industrial research and development co-op, (*Ikerlan*). Their supervisory boards have an equal number of workers and clients, i.e. respectively, bank borrowers, welfare beneficiaries and users of research. In this way, the secondary co-ops obtain the "quality of information" and "incentives to efficiency or protection of customers" as suggested by Kay³⁴ for a "Customer Corporation".

The incentive architecture of Mondragón firms is also radically different from that found in traditional for-profit or not-for-profit firms analysed by academics. While suppliers and customers

can also be members of a firm, profits are not shared according to the value of good or services traded as is commonly found in Anglo co-operatives. All profits accrue to the workers even though control may be shared with other stakeholders. However, workers in support firms share in the profits of the organisations which they service. Bonuses for workers in the CLP are based on the average profits and losses of all firms which are financed by the bank. The bank is owned and controlled by these firms. The allocation of funds and the terms of loans are not just determined by financial markets or the authority system within the bank but by external relationships and values.

On the borrowing side, interest payments by co-ops with trading difficulties may be waived and such forbearance extended to principal repayments.³⁵ In this way the cost of finance becomes a variable instead of the cost of labour, consistent with a value system of labour having priority over capital. Notwithstanding this approach, "the bank is among the one hundred most efficient financial institutions in the world in terms of the profit over total assets ratio".³⁶ For depositors, the bank organises regional consultative councils to exchange information on the requirements of their customers. (Similar consultative meetings are organised by the retail co-op which has both its workers and customers as members.) A unique feature of the bank is that it periodically adjusts all loans and deposits for inflation or deflation of the currency to keep purchasing power constant.³⁷

The governance of transactions by stakeholder relationships

Firms in Mondragón are formed to create socially satisfying employment. More fundamentally, managers are accountable to the workers to reverse the power relationship on which many theories of the firm are based. The institutional arrangements established in Mondragón illustrate how to create "an environment where there is no perceived threat of opportunism, even from opportunists".³⁸

There is no entrepreneur,³⁹ experimenting on ways to reduce the costs of transactions within his authority. "Mondragón makes it clear that market or planning decisions are value decisions".⁴⁰ However, this is seen as an advantage by Bradley and Gelb⁴¹ who favourably compare Mondragón with the "enriched employment relationship extending far beyond the cash nexus"

of Japanese firms and X-inefficiency⁴² found with "Western" practices. Morrison⁴³ quotes the founder of Mondragón, Father Arizmendi as saying:

A company cannot and must not lose any of its efficiency just because human values are considered more important than purely economic or material resources within the company; on the contrary such a consideration should help efficiency and quality.

Arizmendi anticipated the analysis of Tullock⁴⁴ and Downs⁴⁵ concerning the inefficiencies of bureaucracies analysed earlier. Whyte and Whyte⁴⁶ quote Arizmendi as saying:

Any system of organisation which attains a certain size runs the risk of being undermined, if within it flourishes a typical bureaucratic and functionary spirit, a fearful illness which degrades any achievement no matter what is its nature, as it blocks the dynamic agents which strive to maintain efficiency in response to changing conditions.

An incentive to form new firms to create jobs and for groups to pool labour is shared by all workers in the Mondragón system through their social security and health insurance support co-op Lagun-Aro. The level of contributions by all workers to Lagun-Aro depends upon the need to provide unemployment and health care payments for workers. This provides an incentive for members to find new jobs for displaced workers and organise transfers within and between groups of firms. It also provides incentives to implement health maintenance and preventive medicine programs.

The ability to create new firms is provided by the co-op bank with a co-op that act as an entrepreneur (LKS). This role may also be assisted by support from Group management. When employment in any industrial co-op approaches 500, part of the business is transferred to a new co-op. It is through this process that many Mondragón firms become a supplier or customer of other firms in their groups in a similar way to keiretsu firms. "In practice, the Mondragón co-operatives have collapsed the roles of worker, capitalist, and entrepreneur into the same group of people".⁴⁷ As the bank was initially limited to lending to its

members, the rapid growth in its deposit base provided an additional incentive to create new client-owners.⁴⁸ As a co-op, the bank was initially restricted to making loans to its members located in the four Basque provinces of Spain. A general banking licence was not obtained until 1991.

Many European and Japanese banks have an equity interest in their major clients which provides a basis to establish an active relationship in the control of their borrowers. In Mondragón, the ownership of the bank is held only by its borrowers. However, this subservient relationship does not allow the owners to exploit their banker as each member co-op must enter into a contract of association with the bank. It is this contract⁴⁹ which defines the legal architecture of each co-op and how it operates. A condition for new firms to be created or to become part of the MCC is that they adopt a self-governing information and control system. Member firms are always free to leave the system; four left in 1992.⁵⁰

To minimise the cost of government regulation, a self-governing architecture should likewise be a condition for firms to obtain a licence to exist and operate in Anglo cultures. In other words, all social institutions, and firms in particular, should be required to adopt self-governing features in their corporate by-laws or Articles of Association to obtain a licence to exist and/or operate. In this way, governments could "imprint the DNA" of social institutions to reduce the role of government.⁵¹ Stakeholder participation is a condition precedent for self-governance.⁵²

When a firm is under stress, it is its Watchdog Council which is responsible for mediating assistance from the Bank. The bank made a number of interventions during the deep and long Spanish depression between 1976 and 1983. "During 1983, thirty-four of the one hundred worker co-operatives required help from the intervention department".⁵³ However, "During the thirty-two interventions in 1983, only two chief executive officers, six department managers, and three chair-persons of governing councils were replaced".⁵⁴ It was in 1983 that the bank formalised intervention activities into a specialised department and shut down two of the only three firms which have ever been terminated since Mondragón was established in 1956. The re-organisation of a Mondragón firm under stress may involve changes which require sacrifices of not only workers in the firm but in member firms of its group as well as its bankers. Sacrifices

by workers are negotiated through the social council of the firm under stress. The group social council may also be involved as well as the other governing organs of the firm, its group and support organisations. The re-allocation of resources is governed by neither markets nor an authority system but through negotiations with related parties.

Although a third of all Mondragón firms were under stress in 1983, this does not reflect unfavourably on their relative competitiveness. Mollner reported:

Mondragón productivity per worker is the highest in Spain and their absenteeism rate has been consistently less than half that experienced by conventional firms. Throughout the 1960s and 1970s, Mondragón was more than twice as profitable as the average conventional Spanish firm. Mondragón has consistently out-performed conventional firms even in hard times. Between 1975 and 1983 there was a deep recession in Spain. The Basque economy overall lost 20 percent of its jobs, with industrial positions decreasing by 31 percent. By the end of 1982 about 178,000 workers were out of work in the Basque region, representing an unemployment rate of 18 percent. During this same period, Mondragón increased owner-worker jobs by 36 percent, with most of them in the industrial sector. Mondragón not only protected its 11,000 existing jobs, it also created 7,000 new ones and created 37 new co-operative enterprises. In 1985 the unemployment in the Basque country was 27 percent. According to the definition of unemployment customarily used in the United States, only 0.6 of the members of the co-operatives were unemployed. In terms of total industrial output, Spain's grew at an annual rate of 1.5 percent during the deep recession years of 1976 to 1983. Mondragón averaged 6 percent during the same period.⁵⁵

A World Bank study by Thomas and Logan reported:

Various indicators have been used to explore the economic efficiency of the Mondragón group of co-operatives. During more than two decades a considerable number of co-operative factories have functioned at a level equal to or superior in efficiency to that of capitalist enterprise. The compatibility question in this case has been solved without doubt. Efficiency

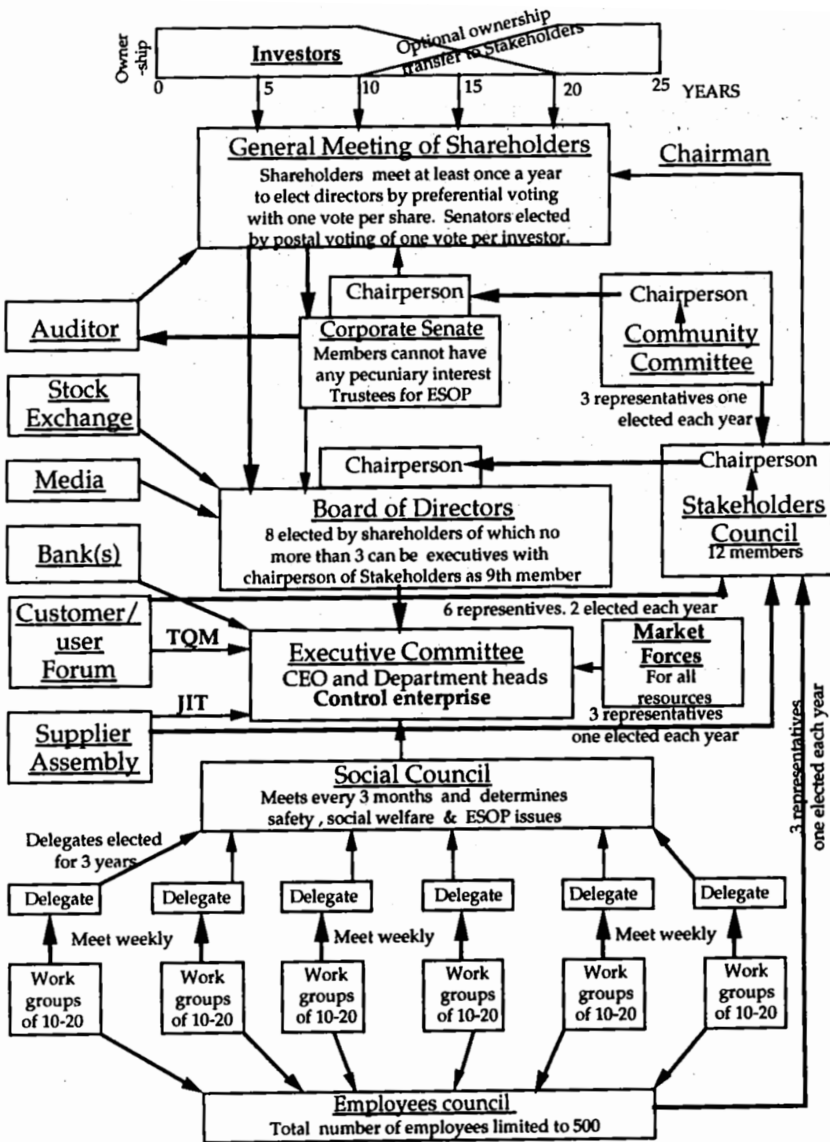
in terms of the use made of scarce resources has been higher in co-operatives; their growth record of sales, exports, and employment, under both favourable and adverse economic conditions, has been superior to that of capitalist enterprises.⁵⁶

The practice and success of stakeholder participation

The record of Japanese and Mondragón firms is outstanding. It provides compelling practical arguments for involving strategic stakeholders in the control of business. The idea of introducing stakeholder participation in the UK has been proposed by the leader of the Labour Party.⁵⁷ With a general election due in 1997, this has politicised analysis. Analysts whom one would expect to be economic rationalists have recently expressed concerns over stakeholder participation⁵⁸ or have rejected it out-right.⁵⁹ Sternberg assumed that stakeholder participation would not "maximise long-term owner value" for firms with investors. However, stakeholder participation can be designed to protect and enhance long term ownership value provided that the business has an appropriate control architecture as illustrated in Figure 7.⁶⁰ But do not just rely on my analysis. The recommendations of Harvard Professor Michael Porter also directly contradict Sternberg. To make US companies more competitive with Japanese and German firms, Porter⁶¹ recommended policies to "encourage long-term employee ownership" and "board representation by significant customers, suppliers, financial advisers, employee, and community representatives". Porter⁶² also suggested that "Ownership should be expanded to include directors, managers, employees, and even customers and suppliers" i.e. for strategic stakeholders to participate not only in control but also ownership.

Even without introducing any changes in ownership it is possible to introduce stakeholder participation along the lines illustrated in Figure 7 without changes in corporate law. Only changes in the constitutions of corporations are required. Government approval is not required for members to change the Articles of Association or corporate by-laws of corporations. However, in providing firms with a "licence to operate", governments could well require firms to establish "stakeholder councils" to act as an internal watchdog to protect consumers, employees, and customers. This could increase the effectiveness

FIGURE 7
Stakeholder Governance



and efficiency of protecting stakeholders while at the same time reducing government expenditures in consumer protection, industrial health and safety, equal opportunity employment, environmental protection, and fair trading, etc. All this while providing competitive advantages for the business!

Notwithstanding the concerns of the *Economist*,⁶³ the practice of involving strategic stakeholders in business is spreading through Anglo cultures. So powerful is the belief in stakeholder participation that investors commonly agree to dilute their equity to allow strategic stakeholders to share ownership in either privately held start up companies or in very large public corporations. However, in Anglo cultures, this participation is usually limited to employees. Employees, as a group, are now appearing as the biggest shareholders in many of the largest corporations in many Anglo countries. In Australia, over 7% of our largest company, BHP, is owned by its workers, Lend Lease has 18% employee ownership while our largest retail chain, Coles Myer, has employee ownership of around 3%. "Of the approximately 7,000 companies listed on American stock exchanges; about 1,000 firms are at least 10% employee held".⁶⁴

In Anglo cultures, there are compelling pragmatic reasons for introducing stakeholder participation. A number of studies by the National Centre for Employee Ownership (NCEO) in the US have shown that corporate performance is improved by employee ownership.⁶⁵ An important finding of the studies was that performance was improved with active participation by employees in control. A 1987 report by the General Accounting Office of the US government found "that firms that combined ownership with participation had a productivity growth rate that was 52 per cent higher with Employee-Share Ownership Plans (ESOPs) than they would have achieved without. *Equity Report* quoted the *Wall Street Journal* of February 13th; 1992; which stated that: "when employees own a big stake, it's a buy signal for investors". Australian research has also shown that employee ownership significantly improves corporate performance.⁶⁷ The ability of stakeholder ownership and control to improve corporate performance is consistently supported by evidence from around the world. Empirical evidence does not support rejection of stakeholder participation. The theoretical arguments outlined above which support stakeholder participation are persuasive. Theoretical analysis also provides compelling arguments for the introduction of

stakeholder participation as a matter of public policy as well as for private profit. I will conclude by considering these issues.

Stakeholder governance instead of government regulation.

Firstly, I want to define the way in which I am going to use words like regulate, self-regulate, govern and self-governance. The word "regulate" will mean that control is exercised to meet some established standard. Intrinsic in this meaning is the necessity to obtain feedback information to inform the controller(s) of any differences between the actual and desired outcome. Defining the word in this way means that while regulators must be able to control, controllers may not be regulating. Self-regulation requires that the people being regulated are responsible for making the system of regulation work in achieving the required standard of performance. The word "govern" is ambiguous and could mean either control or regulate. The word "governance" will be used to describe a *system* of regulation where the standard of performance against which the system is being regulated may be subject to change by the people being regulated. Self-governance will be taken to mean that controllers are subject to being regulated by the people being governed. In political terms this is described as democracy or "rule of the people, by the people, for the people".

Firms controlled by agents who are, or can be, affected by the firm will be described as having "Stakeholder Governance".⁶⁸ In this situation, stakeholders can appoint and/or influence the controllers and so determine the way the firm can, or could affect them. Stakeholder governance meets the test for self-governance as defined above. Stakeholder governance can produce self-regulation when the performance objectives established by the stakeholders are consistent with those established by the host society of the firm. When stakeholder participation is sufficiently wide to reflect the concerns of the host society, the need for government bureaucracies to intercede as regulators is eliminated. If stakeholders in any particular firm or industry are not sufficiently wide to reflect community concerns, then self-governance can still be achieved by introducing self-governance into government bureaucracies.⁶⁹

Firms can only become self-regulating when they have a reliable information system providing feedback details on their performance. Stakeholder participation in the control architecture

of firms provides a basis for obtaining reliable, quick, and cheap feedback information. Such information can also be used to minimise operating costs and increase operating effectiveness. Self-regulation and competitive advantages represent two sides of the same coin. The need for information from strategic stakeholders was recognised by Porter⁷⁰ who noted that: "Both Japanese and German companies practice a form of decentralization involving much greater information flow among multiple units in the company, as well as with customers and suppliers". The establishment of additional communications channels provides the means for reliable messages to be transmitted over unreliable channels.⁷¹ Access to reliable information is a necessary but not sufficient condition for regulation, self-regulation, and self-governance. So, a condition precedent for assuring self-regulation and self-governance is the presence of multiple independent channels of communication. To permit information channels of social institutions to be separate they need to have independent authority systems like the CEOs of keiretsu firms or the members of a Mondragón Social Council or Watchdog Council.

The term "compound board" will be used to describe firms which have more than one centre of authority. Compound boards are common in Europe and are mandated for larger enterprises.⁷² Another reason for compound boards is to improve the integrity of the decision making and control system. Operating integrity of a social system can be corrupted by human failings. The corrupting influences of power are well known. Absolute power can corrupt absolutely.

The corrupting influence of absolute power can be avoided by the division of powers in a compound board to establish checks and balances.⁷³ This also introduces the advantages of specialisation in decision making and control. Compound boards allow a reduction in the knowledge and information processing abilities of individuals who participate in control. It is through specialisation that compound boards can allow ordinary people to achieve extra-ordinary results as demonstrated by Mondragón co-operatives. It also increases the number of individuals who can formally participate in control.

Unitary boards have greater exposure to information overload from lack of specialisation in decision making, information distortion from lack of independent channels of communication,

and corruption from absolute power. Unitary boards have powers in excess of those required to add value.⁷⁴ Powers not required to add value are: the determination of the accounting procedures by which profits are defined and the performance of directors evaluated; selection, control and payment of the auditor; selection and control of experts appointed to advise stakeholders; level of their own remuneration; their own retirement; selecting new board nominees, and control of general meetings of members to whom they are accountable. The handing over of these powers to an independent authority centre can only provide operating advantages for a board of directors by reducing information overload, distortion, and the temptations of absolute power.

One of the most notable features about worker owned companies around the world is that they do not survive over the longer term with a unitary board. All well established worker owned businesses with more than a few hundred members have compound boards, even if unitary boards are the dominant form in their host culture.⁷⁵ A worker co-op or ESOP may get established with a unitary board with dedicated and committed leadership, but rarely do they survive leader succession. It is in the process of managing succession that the conflicts of interest in a unitary board can become fatal for the enterprise. Survival may depend upon the existence of a de facto compound board formed by the involvement of a banker or other stakeholder. The existence of a compound board also makes it practical to involve strategic stakeholders as otherwise their participation would introduce counter-productive conflicts of interests. This point was overlooked by Porter.⁷⁶ In discussing mutual organisations, Llewellyn⁷⁷ noted the "complexity of agency relationships, creates potential (and unnecessary) conflicts between customers and shareholders".⁷⁸

Operating advantages of self-regulation

Compound boards can also become operationally important as firms increase in size and complexity in an analogous way to the advantages obtained from dividing the operations of a firm into separate divisions. Williamson⁷⁹ explained how low frequency strategic information is separated from high frequency operating information with the operating information being processed in parallel through the adoption of a divisional structure. Each

division may typically have its own sales, manufacturing, engineering, and finance department. The decomposition of communications into operating and strategic information reduces information overload and provides a basis for establishing what is described in cybernetics as "double feedback". Williamson quotes Ashby⁸⁰ in noting that the survival of any organism under natural selection is depended upon developing "two readily distinguishable feedbacks". Cybernetic analysis demonstrates that double feedback is an essential feature for the self-regulation for any living thing, machine, device, or organisation. The ability of any living thing, machine, device, or organisation to constructively adjust to a changing environment depends upon its information and control system. The Law of Requisite Variety⁸¹ requires sufficient variety in the information and control systems to match the variety of changes in the environment to which a response is required.

The ability of a control centre to regulate in a timely fashion is improved by expanding the capacity of its information channels.⁶² The capability to process increased information may depend upon parallel processing. This is described as "distributed intelligence" which the US Vice President considered a powerful metaphor in defining the role of government.⁸³ Unitary boards do not represent distributed intelligence or variety in information and control. We must conclude that firms with a unitary board lack the capabilities of those with compound boards. From purely cybernetic considerations we can state that (i) the participation of strategic stakeholders in the control system can increase the capability of firms to adjust to changes in their environment and (ii) compound boards can increase the capability of a firm to process information. In other words, a necessary condition for firms to have superior performance and competitive advantages is to have a governance architecture which uses compound boards and the involvement of strategic stakeholders. A more general formulation of this conclusion is that the ability of social institutions to become self-governing is dependent upon them having requisite variety in their information and control systems from stakeholder participation:

Role of government

The Law of Requisite Variety can be proved mathematically by

information theorists and is generally applicable. It applies to both the regulation of firms, or to governments who seek to regulate firms, or the complexity of the financial system. It means that centralised regulation of any complex system is not feasible because requisite variety is not available. This is why socialism does not work and central banking can be counter productive in managing the variety of circumstances found in a complex economy. It also explains why "the cumulative pattern of regulation has had unintended consequences".⁸⁴ The Law of Requisite Variety also explains why self-regulation does not and cannot work when organisations have a centralised control system as this denies requisite variety to manage complexity. It explains why attempts by governments to regulate complex systems cannot be effective and are likely to become more counter productive as complexity of society increases. Evidence of regulatory failure of privatised utilities in England is described by Kay.⁸⁵ There are also important lessons for the current Australian Financial System Inquiry which was set up by the government to consider the establishment of one or more centralised "super-regulators". Any meaningful protection of consumers in the financial system will require a system of regulation which has sufficient variety in its information and control channels to match the complexity and variety of financial products. Stakeholder participation will be required to provide requisite variety. Compound boards will be required to allow power to be shared with stakeholders as well as providing requisite variety of information and control for self-regulation.⁸⁶ The above observations are quite general and could be applied to the problem of regulating privatised utilities analysed by Kay in a previous issue of this Journal. While the above proposals are different to those considered by Kay,⁸⁷ his words are still applicable when he said "The essence of these proposals is that many of the duties of the regulator are taken over by the board of the customer corporation".

The role of government needs to change from trying to regulate with direct interventions to indirect methods as found in nature. Elements of this indirect approach already exist in Australian company law. One example is the requirement for larger companies to have an auditor. However, the inability of this requirement to protect investors and creditors has created what is described in the literature as an "expectation gap".⁸⁸ Auditors

do not have the power or incentive to provide meaningful stakeholder protection when they report to a unitary board.⁸⁹ Allowing corporations to exist with unitary boards increases the cost of monitoring and regulation by government. These costs could be privatised, while providing operating advantages to companies, by requiring the adoption of an architecture which introduces inbuilt consumer protection. The establishment of stakeholder councils, constituted independently of the board, provides a means to: (a) evaluate "corporate social performance";⁹⁰ (b) undertake social audits;⁹¹ (c) provide financial auditors with the power and incentive to blow the whistle when appropriate, and (d) take on the role of an ombudsman to evaluate concerns of employee, suppliers, and customers. Stakeholder participation in this way could be condition precedent for a firm to obtaining a licence to operate in certain activities. Firms in the securities industry are a case in point. The introduction of arrangements for government agencies and private sector businesses to share power with their clients, customers and suppliers would create a "stakeholder economy".⁹² There also exists the opportunity for democratising ownership as well as control.⁹³ Stakeholder participation provides profound advantages for governments, firms, and their stakeholders. In either the public or private sector, stakeholder participation offers a way to increase efficiency, effectiveness, and the quality of democracy.

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Notes

- 1 Freeman 1984
- 2 Clarkson 1994
- 3 Donaldson and Preston 1995:85
- 4 Preston 1996
- 5 Other possibilities are described in Turnbull 1994b, 1997
- 6 Clarkson 1994
- 7 Preston 1996
- 8 Kay 1996:29
- 9 Turnbull 1990:10
- 10 Grossman & Adams 1993:7
- 11 RSA 1995
- 12 Grossman & Adams 1993:12-13

- 13 See Grossman & Adams 1993
- 14 Monks 1996
- 15 Gordon 1993
- 16 Fukao 1995
- 17 *Analytica* 1992:130
- 18 *Equity Report* 1992:10
- 19 Turnbull 1995a; 1995b; 1995e
- 20 Hawley and Williams 1996:64-5
- 21 This was found to be a major problem for US firms in a report into their competitiveness by Regan 1993
- 22 Kester 1991
- 23 Downs 1967:77/8
- 24 Downs 1967
- 25 Tullock 1965
- 26 Downs 1967:116-118
- 27 Akerlof 1970
- 28 Klein, Crawford, & Alchian 1978
- 29 Jones 1995
- 30 Coase 1986; Alchian and Demsetz 1972
- 31 Jones 1995:423
- 32 A detailed analysis of how the system operates will be found in Turnbull 1995c
- 33 Anoga is not part of the Mondragón system being the Asociación Norte de Ganaderos Northern Livestock Farmers Association
- 34 Kay 1996:41
- 35 'During the severe Spanish recession of the early 1980s, the CLP wrote off more than one million dollars in co-op loans and declared an interest moratorium on about 40 per cent of the rest.' Quoted in Morrison 1991:114
- 36 MCC 1994:11
- 37 Mollner 1991:126
- 38 Ghoshal and Morgan 1996:26
- 39 As assumed by theorists such as Coase 1986 and Williamson 1975; 1985; 1990
- 40 Morrison 1991:98
- 41 Bradley and Gelb 1983:30
- 42 Leibenstein, 1987
- 43 Morrison 1991:111
- 44 Tullock 1965
- 45 Downs 1967
- 46 Whyte and Whyte 1988:100
- 47 Morrison 1991:100
- 48 CLP 1992
- 49 Set out in Appendix B of Campbell, et al. 1977
- 50 CLP 1993
- 51 As proposed by the US Vice President Gore 1996a, 1966b
- 52 As described by Turnbull 1997
- 53 Whyte and Whyte 1988:170

- 54 Whyte and Whyte 1988:172
- 55 Mollner 1991:128-9
- 56 Thomas and Logan 1982: 126-127
- 57 Blair 1996
- 58 *Economist* 1966a
- 59 Sternberg 1996
- 60 Details of Figure 7 are described in Turnbull 1994b. Other concerns of Sternberg are discussed in Turnbull 1997
- 61 Porter 1992:16
- 62 Porter 1992:14
- 63 *Economist* 1996a
- 64 Tseo 1996:66
- 65 *Equity Report* 1992:7-8
- 66 *Equity Report* 1992:7-8
- 67 *Equity Report* 1992:2-4
- 68 Turnbull 1997
- 69 As described in Turnbull 1994b, 1995a
- 70 Porter 1992:11
- 71 Ashby 1968:190. Ashby was a pioneer in the science of information and control which is called cybernetics. Cybernetics is based on information theory which has a rigorous mathematical basis.
- 72 Analytica 1992, Turnbull 1995e
- 73 Tricker 1994:247
- 74 Turnbull 1993, 1994a
- 75 Bernstein 1976
- 76 Porter 1992
- 77 Llewellyn 1996:58
- 78 Mondragón shows how an appropriately designed compound board can allow the Porter recommendation to be implemented while avoiding the concerns of Llewellyn and Williamson 1985:308. My suggestion for listed firms in Figure 7 follows the Williamson view that representatives of an "interest group", who are not investors, be limited to "informational participation" like suppliers and customers in a keiretsu.
- 79 Williamson 1985:282
- 80 Ashby 1968:131
- 81 Ashby 1968:202
- 82 Ashby 1968:211
- 83 Gore 1996a
- 84 Porter 1992:15
- 85 Kay 1996
- 86 The need for power sharing to protect the interests of stakeholders is described by Hill and Jones 1992
- 87 Kay 1996:45
- 88 Schelluch & Green 1996; Guthrie & Turnbull 1995
- 89 The need to adopt a compound board in the UK is recognised by Hatherly 1995 and Tricker 1994:247
- 90 Clarkson 1995

- 91 Turnbull 1995d
 92 Blair 1996
 93 Turnbull 1975, 1994c, 1977

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Management Development for Co-operatives - A Review

Peter Davis

There has been considerable research in recent years on the appropriate content and methodology for the delivery of co-operative management development. As a result, a clear picture is beginning to emerge as to the priorities for the delivery mechanisms although the philosophy and approach towards content is less clear.¹

The content of co-operative management development

The nature of co-operative management is a matter of contention. I have in a previous article discussed the debate within mainstream service co-operatives concerning the role of professional management. I will, therefore, only give a brief outline here of the main approaches.² Essentially there are two. First, there are those who tend to see management primarily as at the service of an elected lay leadership made up of members who determine policy for management to administer. This approach emphasises the need to control management. As a result, it concentrates on procedure, governance and direct member led democracy determining decision making. Second, there are those who see culture as more significant than process in ensuring the direction and quality of co-operative activities. They believe that in a modern co-operative movement the lay board must be led by a value-based management rooted in the co-operative heritage. This, it is argued, provides the essential quality of leadership necessary for the survival of co-operatives into the next century.

The debate takes on a different emphasis from the perspective of the productive co-operative. Here a third approach to the concept of co-operative management can be identified. This approach sees co-operative management as a case of direct collective worker control of decision making. Management is seen simply as a co-ordinating mechanism, only necessary in larger scale co-operatives in order to keep workplace based collective decision-making on a common track. This is the worker

control model of co-operative management. It can be illustrated from one training manual produced by the Industrial Common Ownership Movement (ICOM) for the British worker co-operative movement. Management is depicted at one stage as being purely a service function to ensure the cohesion of the independent self managed operational units and, according to the authors, management ... "will not be concerned with the internal matters within the operational units."³ Such a view of the internal autonomy of the work group ignores technology and the need to determine acceptable levels of unit costs in terms of the organisation's competitive position. It also either assumes a static position for the configuration of operations or that the operating unit itself will be in a position to transform itself even to the point of self elimination if necessary.

Devolved responsibility to the work group is not the same as unit level autonomy within organisations. Autonomous work groups that are really autonomous in the worker control approach run the risk of transferring "them and us" attitudes across lines of demarcation rather than hierarchical lines of managerial authority. The Viable Systems Model in the ICOM training manual has five separate levels to run the co-operative's democratic management on the worker control approach.⁴ The fifth level, concerned with the development of policy, suggests that policy in a large co-operative could be determined at a yearly meeting of members as opposed to a traditional company where it suggests shareholders or owners make policy.⁵ In fact in both cases it is professional management that really determines policies that, if successful, will get the support of the shareholders whether capital based or member based. This has been understood ever since the managerial revolution thesis was first proposed and it has only been seriously challenged by the work of Zeitling and Scott.⁶ In neither of these two cases do the authors suggest, however, that the shareholders make policy. They do, however, argue that ownership provides the power and sanction to depose a poor management that does not operate in the shareholders interests. This is I believe practically the same situation for shareholders in membership-based organisations. One example of the weakness in practice of the worker control approach for larger scale co-operatives is the unwillingness of the British wholefood co-operatives to co-operate. The decision by a significant segment of the wholefood wholesale co-operatives

not to participate in a national marketing strategy does not appear to be based on any commercial or co-operative criteria but on parochial issues.⁷ Those that did attempt to collaborate in fact lacked the expertise and the authority to really get decisions taken quickly and move them through to the marketplace.⁸ This episode illustrates the weaknesses of organisations that interpret democracy and co-operation as a micro level operating group exercise in direct democracy. Instead, co-operative democracy should be understood as a macro level activity embracing the whole association of labour by hand and brain. Unity and solidarity require a macro level participation in the development of goals and policies for their implementation, not micro level work group autonomy.

A co-operative line management that is genuinely based on co-operative values and committed to co-operative purpose is the only way such a mass social movement can be mobilised, coordinated and lead. Such a structure does not preclude worker involvement, it rather establishes the conditions for such involvement in mutual co-operation with the other stockholders both within the association and those outside that are affected by its activities. Direct democratic control by members is essential for maintaining accountability and ownership but it can never be a vehicle for the final determination of business policy. Members' inputs can provide crucial material in the process of defining policy. Democracy is one, and only one, aspect of the co-operative identity. It must never be placed above or in place of the other principles and purpose. It is the totality of principles and values that determine co-operative identity. A professional value-based management committed to the achievement of the overall co-operative purpose, and accountable to the direct membership and the wider movement, may provide clearer direction for the co-operative association and its business.

Self management skills including "co-operative working" through group-based decision making are important for the success of those worker co-operatives who choose to stay small scale. Such co-operatives may well provide a better service to customers and a good quality of life for members.⁹ The problem is that many writers in the co-operative tradition appear to expect direct or near direct control to be possible at whatever the size and complexity of co-operative business. Some of the literature identified with the worker control model of co-operative

management does appeal to involvement strategies within mainstream management.¹⁰ Participatory management styles, however, can operate within organisations with vastly different ownership structures. This does not generally produce the objective of collective management in the "workers control" tradition. Process based strategies involving consultative and negotiating machinery may simply institutionalise a "them and us" culture and may in some management eyes leave the co-operative at a competitive disadvantage in terms of shop floor resistance to change.

Much of the decision making that is central to the direction of the organisation is not encompassed by the tasks undertaken on the shop floor. It was an article of faith with both Taylor and Mayo that the shop floor workers needed the expertise of management. Devolution of management assumes that the relevant information is not only available to operational units on the shop floor but that the workers can correctly and dispassionately evaluate this information. As Michael Jones, a long-standing advocate of worker ownership and involvement, puts it,

It is of course essential for any co-operative to set parameters regarding the types of decisions in which different categories of workers could, and should, be involved. Especially in larger worker owned businesses it is essential that managers are allowed to make management decisions with a minimum of input if they are of a purely business nature.¹¹

This is not to argue that in large scale co-operatives we must rely on standard management as seen in the capital-based business world. Without the right management culture changing to member ownership can be problematic from both shop floor and management perspectives. This is true not just for larger worker co-operatives such as the Mondragón Group and the Scott Bader Commonwealth but for all forms of co-operative.

We need a change in culture where management and shop floor are seen as all part of the same community of interests. It is the shared values arising from the co-operative purpose and co-operative community that enables real mutual empowerment, leading to the realisation of the objectives of solidarity both within and without the co-operative. The ideology of micro level worker

autonomy will more often than not only frustrate the all-important macro level solidarity of the people. Such solidarity can only be achieved by a management culture based on an understanding of co-operative purpose and the adoption of co-operative values. Without this adoption of value-based management, it is doubtful whether rules concerning participation in management - like those adopted by the Mondragón Co-operative Group - will increase the level of involvement or identity with the goals of the co-operative felt by the shop floor member. These measures are equally unlikely to enable the business to survive let alone prosper if the management itself has been left in the hands of people untrained and unsympathetic to the co-operative purpose.¹² The worker control approach has a socially static view of management. It implies that this segment of intellectual labour has always to be hostile to the shop floor and to real co-operative purposes. This view of management does not detach the individual manager from his or her context in share-based business and the culture that pervades it. Capital based organisations dominate the economy and the values underpinning management development. It is to counter this that co-operatives have placed such emphasis on education.

Managers in a membership-based organisation have the potential to operate as leading the association of labour as a whole and indeed being recognised as part of that association. What is needed are management development programmes that enable managers to provide the leadership, direction, and innovation that labour in all its manifestations so desperately needs. By labour I include the activities of managers, small family business and self employed, those engaged in family based domestic activity, farmers, and fishermen, as well as industrial and service workers, in the processes of creation and consumption of goods and services. Such a view of management as not just intellectual labour but as the leadership of labour can only arise based on values and purposes derived from the co-operative programme and operated within the co-operative context. This clearly requires a specific co-operative management culture and values to inform the content of co-operative management development. Such programmes do not replace the need for democratic accountability or for rigorous systems to ensure good governance. Individuals can always be corrupt in any context. Whether it is a worker falsifying clock cards, using up sickness

"entitlement" or a manager agreeing deals/sales etc for a personal pay off, we should never forget the frailty of human nature and the greater opportunity that knowledge brings for corruption as well as enlightenment.

The issue is not whether to have democratic elected boards and codes of conduct to which the professional manager is accountable. The issue is that none of this is going to enable the co-operative movement to grow and develop or take advantage of the commercial and social opportunities as they arise. Democratic boards will only rarely produce the flexibility, knowledge, and skill to exercise the necessary leadership. This is top professional management's role. The co-operative difference should be that in this case they lead, and are full members of, an otherwise democratically elected board. Unfortunately, most co-operative educationalists have failed to recognise or accept that leadership is most effectively exercised by individuals and that in today's environment those exercising leadership must be professional. Much recent research shows a growing recognition of the importance of co-operative leadership and management development across international boundaries. Most of this work, however, fails to recognise the particular importance of professional management or to account for this in their development strategy. An example can be provided by a recent Swedish Co-operative Centre report on training for co-operative leadership. This was the result of a series of evaluation seminars undertaken with African and Asian co-operative managers and development workers during the period Sept-Oct 1992.¹³ The participants at these seminars identified a common stock of co-operative knowledge, skills and attitudes that it would be essential to address in an international training programme for any identifiable group of co-operative leadership, whether professional and executive management, lay directors or government officers and development workers. This common stock of categories identified were as follows:

- i. The political, economic, and social changes and development effecting the co-operatives both international and domestic.
- ii. Management information systems involving new technologies, management techniques, strategic planning, and control.

- iii. Leadership skills and attitudes.
- iv. Co-operative values and principles.
- v. Gender sensitisation.
- vi. Protection of the natural environment.

The report concluded "in the context of new economic policies oriented towards the market economy, the need for greater emphasis on these aspects in the training programme should be stressed, ideally by combining and analysing linkages between co-operative values, socio-economic objectives and competitive strengths of the co-operative. Priority should be given to issues and topics related to technical and commercial aspects of management."¹⁴

The report's priority regarding technical and commercial aspects of management training in respect of leadership is at the heart of the question. It shows that the authors are still thinking of the lay board as providing professional skills and leadership. It also demonstrates their failure to recognise the strategic relevance of co-operative purpose and values for top management. Priority for technical subjects may be correct at introductory and intermediate levels of management development but those advanced levels of provision concerned with leadership training must emphasise co-operative purpose, values, and culture in order to ensure the effective strategic application of managerial skills and knowledge. Particularly those relating to the definition of objectives, the identification of standards of quality, and the development of policy and strategy consistent with the successful growth of the whole co-operative association. The report makes no mention of the differing levels of understanding and attainment required. The common components will have to have very different content and learning strategies when applied to the various groups with distinct roles and backgrounds that contribute to co-operative leadership. That priority must be given to co-operative executive management development does not appear to be recognised by the authors of the Swedish report.

Delivering co-operative management development

Looking at the issues of delivery we can say firstly that our management development programmes must provide the

individual manager with the flexibility to tailor their learning to suit their individual development needs both in terms of content and delivery. This theme was particularly emphasised in the report from U.S. Department of Agriculture entitled *Co-operative Education - Task Force Final Report*, A.C.S. Service Report 35, published in July 1993. The report concluded "Materials must be individualised both in use and in message. Distance learning, small group methods, or one on one learning would be of increasing importance in some circumstances. Materials and systems that constrain the educator/facilitator or the audience in terms of time and contents will lose out to those that don't. Materials and programmes must be built using technologies that allow the individual user to have complete control over the timing or schedule of use."¹⁵

This American research identified the need for co-operative management training to broaden its perspectives to allow for cross-fertilisation between various co-operative sectors: "bridges must be built between agricultural and other segments of our educational system, especially in the fields of business, economics and sociology. Collaborative research and curriculum development is required."¹⁶ That the current provision can be described as segmented, and incomplete is not in doubt. Many audiences for co-operative management development are inadequately served by materials that rarely go beyond the introductory level.¹⁷ The way to overcome the perception of co-operative sectional exclusiveness and the consequential fragmentation of development provision that flows from it is to recognise the common co-operative purpose, values and methods found in all co-operative associations.

Managerial knowledge may be specific to a given field of activity but managerial culture, values, and many of the recognised skills of effective management are clearly transferable. Building links to the various sectors within the educational system is helpful as the American report recognises. If such resources are to be successfully adapted to meet the management development needs of membership-based organisations there needs to be a recognition by the institutional providers of management education of the different context provided by co-operative purpose and structure. This recognition leads co-operatives at their best to develop a distinctive co-operative management and organisational culture. In the United States it

was felt that a national clearing house was needed to collect information and descriptions of co-operative educational programmes and materials in order that a general upgrading in overall standards of co-operative management development and member education could be progressed.¹⁸ Co-operative case studies capable of use as vehicles for management development are few and far between at present.

The particular context within which co-operative management training is being delivered is recognised as being highly significant by the Swedish conducted seminars referred to in the previous section "... Co-operative leadership training programmes cannot be properly prepared without first considering what kind of co-operative development the participants are supposed to be involved in and promote on the completion of their training."¹⁹ The report concluded that regional and international training programmes should be designed to provide primarily training in those areas and for those categories of personnel who national movements training provision was unable to cater for. This implies that introductory training would be provided locally but that the more advanced levels of training, particularly at graduate and post-graduate levels could in fact be more effectively provided at the international level.

The relevance of international experience for the provision of co-operative management development was further underlined in *Report 2* of the meeting of experts of Co-operatives, Geneva, March 29 - April 2, 1993. The report entitled *The Role of Human Resources Development in the Economic Viability, Efficient Management and Democratic Control of Co-operatives*, published by the ILO had this to say on the question of learning:

New approaches to training programmes include distance education for co-operative staff, managers, and board members. Such courses are being offered in Costa Rica, Kenya, the Philippines, United Republic of Tanzania, Uganda, and Zambia to name only a few. Mass media can be used for co-operative HRD especially in those countries where the co-operative structures are weak or more informal. In the few cases where mass media was used in the past, it was conceived as co-operative education for the general public and information for potential members as, for example, in Botswana, Cameroon, United Republic of Tanzania and Zimbabwe. Recently mass

media has been used for tailor made distance learning programmes in co-operative management, e.g., the Costa Rica programme of Alice Coop. These training approaches are of particular interest in countries where co-operatives are disbursed over large areas, for example in Argentina, Australia, and Brazil.

They can also be an advantage in small island economies such as those in the Caribbean or South Pacific regions, where co-operatives need to take advantage of co-operative experiences and potential in neighbouring countries and where the maintenance and operations of a specialised training institution are too costly compared to the size of the population. Distance education and training were also introduced as correspondence courses in Kenya, United Republic of Tanzania, Uganda and Zambia because of financial constraints, the large number of trainees, and the inability of trainees to absent themselves from the workplace.

The use of mass media and correspondence courses for distance education and training also reduces the migratory effects of training which takes place over long periods in urban areas.²⁰

It has been recognised in some of the literature that development agencies both in the west and the third world that have been supporting co-operative HRD activities for many decades had not been, in general, particularly successful and that the issue of setting effective standards for training policies and programmes conducted by agencies like the ILO had not been effectively established in all cases. Paragraph 38 of the *Report of the Meeting of Experts on Co-operatives*, Agenda item 6 clearly indicated the need for collaboration with established and recognised providers of higher education,

Co-operative human resource development should form part and parcel of general education and be promoted at all levels of the education system. It should be included in the curriculum of education institutions, and it was noted the co-operative studies should be offered at Universities and Colleges as part of the course of economics and business management since co-operatives were among the forms of business enterprise

but having special characteristics. The meeting agreed that the establishment of School and University based co-operatives should be encouraged because they could provide business experience to youth whilst instilling in them the principles and values of co-operation. Furthermore, co-operative human resource development should be linked with vocational training programmes since co-operative enterprise could provide self employment opportunities for the trained. It was also observed that where desired, recognition be given by the Ministry of Education to Diploma and Degree courses in co-operative studies.²¹

Distance learning

Advanced programmes leading to master's level accreditation for co-operative management by distance learning are clearly one important way to meet the needs and the challenges identified in the many reports (including those cited above) on co-operative HRD²² distance learning provides wide access and flexibility at prices that are affordable to very much wider sectors of the population than would otherwise be able to have access to University level programmes and expertise. Distance learning may be more adaptable to the social as well as economic character of the co-operative enterprise with its importance for mobilising vast numbers of the world's poorest and often socially excluded peoples both because of its low costs and because of the co-operative context for its delivery.

There are two elements that could support a co-operative management distance learning based programme. First, such a programme provides the flexible response needed to enable entrants to cope with the materials at an appropriate level whether elementary or fast track development.

- a) Assessment structures can permit individuals to work through the materials at the level of achievement that meets their development needs and that of the co-operative society to which they belong.
- b) Assessment levels can provide clear criteria for identification of those individuals capable of development to achieve higher academic standards that will enable them to benefit from further development.

- c) Time and place as well as pace and depth flexibility are also important aspects of distance learning provisions enabling the most effective individual integration of work and study.

Second, distance learning does not have to mean learning in an unsupported environment. At the heart of the co-operative idea is the belief in association or community as the best grounds for self help. This is particularly relevant to the process of learning and self development. Learning is a social process. If we apply the idea of mutuality to the learning process in an organisational context we note immediately the mutual benefit for the individual student and their organisation. We can recognise that co-operatives can potentially provide enhanced resources and support for the distance learning student because of the co-operative values and culture that may not always be available to distance learning students in other contexts. These include: -

(a) Horizontal strategies.

1. Co-operative groups in villages and urban communities and functional settings in more complex co-operative business environments can provide a framework for peer group learning and course member support networks.
2. Co-operatives have education as a key principle thus local resources in terms of facilities, equipment, finance, monitoring, and mentoring may be more readily available to support the student.

(b) Vertical strategies.

Structured guidance for interaction with superiors and subordinates within management hierarchies to facilitate learning and development is particularly relevant to organisations which boast that education is one of their guiding principles and is central to their organisational culture and development strategies.

(c) Networking strategies

1. The widespread network of development and promotional agencies that exist to support co-operatives such as the ICA, ILO Co-operative Colleges, Government Departments, Funded Projects, Open Colleges, etc means that there exist opportunities for otherwise under resourced individuals to get access to sophisticated resources and materials to support their learning, such as: study skills; access to New

Technology; access to institutional resources such as libraries; access to locally based tutorial support; access to supplementary/additional training facilities through local co-operative development programmes.

2. The range of assignments can include some that will encourage networking and other means of accessing the wide range of development facilities that exist in most environments where co-operative development is taking place.

(d) Individual strategies.

People who join and become active in co-operative enterprises are motivated individuals who believe in a philosophy of self-help and self-improvement. They have the attitude, commitment, and motivation to try hard and to succeed. This is equally true of individuals who aspire to positions of responsibility in the management of any form of organisation. The programme materials whilst encouraging candidates to network and to utilise the various opportunities that exist will also emphasise their personal responsibility for learning and provide guidance on time management and other self management techniques and study methods that can help them.

Towards a distinct co-operative management development programme

The need for progress towards a management development programme that differentiates co-operative management culture from general management culture is beginning to be recognised at the highest levels within co-operative management today.²³ It was very much part of the international debate on the draft statement of co-operative identity finalised at the International Co-operative Alliance Congress held in Manchester in September 1995. The Postgraduate Diploma/Masters Programme in Co-operative Management and Organisational Development and the Postgraduate Certificate Programme for Credit Unions by distance learning provided by the University of Leicester Management Centre's Unit for Membership Based Organisations is our institution of higher education's response to this acknowledged co-operative need.²⁴

We are offering the programme in English globally in the belief that a truly international co-operative management programme

will help co-operatives to break their isolation. It will enable the development of a global and therefore transferable management culture and based on best practice within the co-operative sector to rival that of the well-defined management cultures of the movement's transnational competitors. This will help to facilitate what has long been acknowledged to be the Achilles heel in the world co-operative movement - the protecting of co-operative purpose and integrity whilst adopting a professional management structure and culture. Second, it could support the development of improved co-operation between co-operatives. This latter point is of growing urgency in the face of the opening up of national markets to growing external competition at the level of the national and regional economies within which most co-operatives have traditionally traded. The social impact of this intensified competition combined with an ideology of individualistic materialism is seen in the weakening of community, increased levels of urban and rural poverty, unemployment, and social exclusion.

The fragmented and often un-validated programmes provided for co-operative management and members do not provide an adequate incentive for people to undertake co-operative management development. We need to develop advanced validated management development programmes that will enable co-operative managers to match the mobility of their capital-based colleagues and enrich the wider co-operative movement. In today's global economy the movement does have the size and diversity to sustain the emergence of a co-operative management with international experience and perspectives. Co-operative management development programmes must be provided that incorporate co-operative values with the global perspective in their understanding of the business environment and strategic management. Our aim must be the development of professional managers who recognise the continuing relevance of the values of co-operative association in providing a framework for doing business that leads to increased social justice and solidarity within the disciplines of a market economy.

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Co-operatives and the 'Conversion Syndrome' Abroad

Rita Rhodes

This paper attempts to describe the experiences of co-operatives in other countries as they decide to become investor, rather than member, owned businesses. It will look at the reasons for such conversions, the forms they take and attempt to assess what lessons might be learned from them. The extent of these conversions naturally varies from country to country, but Australian co-operators have been sufficiently concerned by it to refer to it as the "Conversion Syndrome".¹ Hence, the title of this paper.

The paper has been approached from two angles, the geographical and that of experiences in different co-operative sectors. Examination of these has been assisted by information sent by a number of co-operative organisations which is acknowledged with thanks. Such information was necessarily diverse and has not permitted a scientific or exhaustive survey. However, it appears to suggest that the conditions and impetus for conversion occur in many countries, and that some types of co-operative are more prone to it than others. Prominent among these are co-operatives in the agricultural sector where, for more than a decade, a combination of the need for more capital and the desire of some members to increase their personal returns has led to structural changes.

Privatisation describes not only those co-operatives demutualising but also the state co-operatives in central and eastern Europe, Russia and elsewhere which are becoming companies or voluntary co-operatives under programmes of liberalisation or restructuring. These have been excluded because, although collective, they were not voluntary and therefore mutual in the sense that we use the term in free market economies. Moreover, their conversions are occurring in a phase that is

temporary and unlikely to be repeated. Excluded also have been mutual organisations which are not specifically co-operatives such as other friendly societies in this country and mutual insurance businesses elsewhere. A problem throughout this paper has been one of definition. Terms such as "mutuals" and "co-operatives" can change under different countries' legislation which sometimes provides that co-operatives be registered as companies. At the outset we should also note a number of background factors.

Background to present situation

A number of world-wide common factors are creating a favourable climate for conversion. One is increased privatisation, illustrated by events in this country over the last 15 years, and followed to a greater or lesser extent in many other countries. Accompanying this have often been measures of deregulation aimed at increasing competition. The result has been that competition is now occurring more frequently on a global scale. In some countries deregulation has involved the lifting of import barriers which have left certain industries, and the co-operatives operating within them, more vulnerable. Alongside such developments new patterns of trade are resulting from the growth of large trading areas, such as the Americas, Europe, and the Pacific rim.

All these factors - privatisation, deregulation, and increased competition - create a climate in which privatisation becomes more popular and mutuality less so. Each will be seen at play in the following surveys.

Geographical survey

Moving from east to west, we are told that in Japan there have been few, if any examples of demutualisation. On the other hand, there is increasing pressure from competitors who are challenging Japanese co-operatives' success on the basis of their special characteristics or advantages. There are also changes in the Japanese economy which are prompting co-operatives to reorient themselves. For example, the agricultural co operative insurance business, having noted that Japan's "socio-economic environment is drastically changing ... due to the liberalisation and

globalisation of financial business, deregulation, development of information-oriented society, the greying *of* the population etc", has decided to try to secure its position in two ways. One is to give priority to promoting members' interests. The other is to strengthen the links between primary societies and federations so as to be able to strengthen the technical ability of staff and to rationalise business operations.²

By contrast, in Australia conversions are already more advanced. Australian concern about conversions appears to lie more in the size and strategic nature of the societies involved rather than in their number. Only 49 co-operatives, out of over 2,300 were listed as having converted, but they represented "hundreds of millions of dollars (Australian) of annual turnover". Of these, nine were building societies, one an insurance co-operative, and another a credit society. The rest, termed "general co-operatives", included a number related to agriculture: sugar milling, dairy, ginger growers, citrus, egg, butter, abattoirs, and fruit juices. Worse still, a report suggests that "In the past two years there ... is hardly a significant co-operative that hasn't considered its corporate structure or the adequacy of its capital structure". It is thus feared that if the trend continues, a "critical mass" will be lost from the co-operative sector. The exception to this trend has apparently been among credit unions which have built strong representative and commercial structures, together with a good record of serving and assisting their members. They are held to have proved successful in a highly competitive industry and one that has been subject to deregulation.

A thread running through the arguments that other co-operatives used for conversion is that it is difficult to reconcile the co-operatives' de-emphasising of the role of capital with the need to obtain sufficient funds to remain competitive. Competition has undoubtedly increased as the Australian economy tries to strengthen its position in a region containing a number of "tiger" economies. Consequently, State and Federal governments have lifted regulatory restrictions on financial and rural industries which had already been adversely affected by relaxed import restrictions. Australian co-operatives claim that to be able to compete more effectively in this heightened competition, they require greater flexibility in their funding.

An interesting element in their situation is that, unlike co-operatives in many other countries, Australian societies have

not developed second or third tier co-operative structures. Cronan suggests that had they done so - and particularly a co-operative bank - some of their structural weaknesses could have been remedied. Experience elsewhere suggests that he is right. In this context we have already noted the moves by the Japanese agricultural co-operative insurance group to strengthen links between primary societies and federations. Cronan also brings out in his survey the importance of appropriate co-operative legislation and linked to that, the role of members. These are two constant features throughout the rest of this paper, but they are perhaps seen most clearly in an Indian case. It concerned the Development Co-op Bank of Bombay whose attempt to convert also illustrates the fact that reasons, other than access to capital, can prompt changes in business form.

At a special General Body meeting in January 1995, the bank decided to convert into a Joint Stock (Banking) Company. Two members subsequently challenged this decision in court. They wanted it "declared illegal, null and void" on the grounds that the General Meeting had been illegal because insufficient notice had been given and over 90 per cent of the members had not received the notice. They also asserted that the bank should first have been dissolved as a co-operative before its status was changed and asked that the bank should continue under the Maharashtra Co-operatives Society Act 1960 and Multi-State Co-operative Societies Act 1984. The Judge found for them.⁴

The Indian press quoted one of the two members who brought the case as saying that the move to change the bank to a Joint Stock (Banking) Company, "had been done by the president of the Co-operative Bank to retain power in his own hands." If correct, it suggests that some conversions could be driven by officials anticipating advantages for themselves, either in terms of status or financial reward. In the context of this paper, though, the significance of the Indian case is that members were aware of what was happening, they were prepared to challenge it, and their position was strengthened by co-operative legislation.

Another factor at play in India is the continuing liberalisation of the economy under which many co-operatives are able to move away from their earlier close relationship with government. This is giving them greater freedom to face increasing competition and to consider other forms or organisation. Over the last few years, some large co-operatives, including dairy and sugar

societies, have campaigned for "company" status. The idea of "co-operative companies" has gained ground. Shah suggests:

The idea of a co-operative company is an ideal response to this need to promote member-first model of co-operatives which has greater chances to survive and compete in an economic environment which is increasingly throwing farmers and their organisations to compete with private and multi-national enterprises.⁵

Supporters of this idea urge that special provision be made in companies' legislation for the registration of Multi-state Co-operative Companies which would facilitate the business of large co-operatives operating in more than one Indian State. They also claim that Co-operative companies would differ from ordinary companies inasmuch as only their users could enrol as members at a fixed membership fee. Equity capital, however, could be contributed by non-members but these would not have the right to vote or seek election to the board. Another advantage claimed for co-operative companies is that they would have more flexible and less bureaucratic audit procedures than co-operatives because they would come under the Companies Act.

From the above it would appear that a hybrid organisation would be created. Elsewhere it seems that clear cut conversions do not always occur. Ambiguities can arise from the legislation under which they take place, or the form they ultimately take. For example, in some countries, co-operatives can register under co-operative, or companies' legislation. In Kenya and Zimbabwe, the more commercial agricultural co-operative enterprises can register under either. However, in Kenya, the Kenya Planters Co-operative Union, the Kenya Creameries Company, and the Kenya Farmers Association, have opted to come fully under the Co-operative Societies Act. In Zimbabwe though, co-operatives with dual registration have decided to operate only under the companies Act.⁶ A further confusion can arise when co-operatives decide that part of their operations will take the form of shareholding company. Such examples can be found among agricultural co-operatives in Scandinavia and Ireland.

In Denmark, changes in milk quotas and other regulations, as well as the growing internationalisation of food processing, have increased pressures on Danish agricultural co-operatives. Their

resulting dilemma has been summed up thus:

To secure the future development of the food processing co-operatives and the internationalisation of co-operative activities, it is important to establish models for providing risk-bearing capital which will ensure that co-operative members, as well as institutional investors, are able to protect their interests, and these models must preclude the possibility of members losing total control of the co-operative.⁷

They have evolved three ways of providing risk-bearing capital. One has been to take external capital but not to allow its providers internal influence in the co-operative which retains its existing structures. A second way has been the outright conversion of a co-operative into a shareholding company of the type we have seen in Australia. In this the original co-operative members may, or may not, hold the majority of shares. Even where they do, as we shall shortly see in Ireland, they may not continue to do so in the long run. A third way attempted by two large organisations in Danish co-operative food processing has been to place "particular aspects of the organisation under the control of a special shareholding company, thus allocating certain co-operative activities to the control and aims of the total group of investors, co-operative as well as institutional".

In Ireland, where agricultural co-operatives are to be found in the dairying, cereal and meat sectors, a not dissimilar situation has arisen. However, its problems were compounded in the late 1980s by predators, including the now discredited Goodman International. To try to improve the co-operative position; the Irish Co-operative Organisation Society (ICOS) urged mergers among societies in an attempt to reduce their fragmentation. ICOS also advised and gave assistance to co-operatives which wished to consider going down the plc route as a means of attracting necessary additional capital. Its main concern was to ensure the survival and development of "farmer-controlled" businesses. To do this, ICOS urged that 51 per cent of equity should remain in a co-operative's hands.⁸

A number of large Irish co-operatives have since gone down this route, including the Irish Agricultural Wholesale Society. Safeguards were built into their new rules requiring that 'if a co-operative's shareholding was to be allowed to drop below

the 51 per cent level, at least 75 per cent of members present at a Special General Meeting should have to vote in favour of this. A second Special General Meeting would then have to be held within 28 days at which the Resolution passed at the first meeting would have to be ratified, again with 75 per cent of those present voting in favour. Despite such safeguards, it is understood that two of the large co-operatives which went down the plc route are currently considering reducing their societies' holding to below 51 per cent.

Reducing co-operative fragmentation, and improving market share and profitability, have not been the only issues in the Irish situation. Another motive shown to exist in conversions is the widespread perception that money invested in co-operatives is "dead money" because co-operative shares cannot be traded. This also seems to be a factor in American conversions.

These can be typified by the cases in the late 1980s of six agricultural co-operatives: poultry marketing, rice milling and marketing, milk producers, cotton growers, a poultry marketing and purchasing co-operative, and a farmers' marketing and purchasing co-operative. These restructured in various ways. Three became companies, one was "acquired" by another co-operative, while the other two offered shares of their subsidiary corporations to the public. Schrader shows that each case had different features but summarised their underlying motives as being a "combination of financial pressures on farmers, a bull market in corporate equities, and lack of means for patrons to capture appreciation in the value of a co-operative as a going business".⁹ He notes an important tension in such co-operatives which occurs when a co-operative that "produces net earnings in excess of the opportunity cost of equity capital may be worth more to investors as an ordinary corporation than it is to many co-operative patrons". To some extent this could be offset if farmers viewed their business as a family operation that would be passed down the generations, and if membership of a co-operative was based on the ownership of land which enabled a successful co-operative's performance to be eventually capitalised in the value of the land. "Thus, the patron does receive a price reflecting the value of the co-operative as a going business when he ceases farming as part of the price for or rent from the land associated with membership."

Sectoral survey

In comparison with agricultural and food processing co-operatives, there is no great movement towards conversion among workers' and housing co-operatives and credit unions abroad. Among consumer and financial co-operatives, however, the picture was somewhat different.

Consumer co-operatives show that, besides outright conversion, partial demutualisation can result from gradual changes. If two defining features of mutuality are taken to be the trading of members with each other to provide goods or services, and reliance on their own capital to do so, then we must conclude that some modern consumer movements are no longer fully mutual. Indeed, the Industrial Common Ownership Movement (ICOM), suggests that, because large retail societies trade extensively with non-members, they are not mutual organisations. On the other hand, ICOM classifies smaller food co-operatives which buy from wholesalers and distribute solely to their members, as mutuals.¹⁰

Perhaps this is over-simplifying because a movement as old as the British consumer movement is mutual in other ways such as through the transfer of assets from generation to generation and through the links of our federated system. Nevertheless, we have to admit that there have been massive changes among overseas consumer movements. Only two of these, the Dutch, and a large part of the German, have converted outright; even so this did not save them. Finnish experience is more mixed. In 1983, under company legislation, one of the country's two largest co-operative groupings, comprising 39 regional societies and their wholesale, merged to form the Eka Corporation. By the early 1990s, with a downturn in trade, accentuated by recession and the collapse of the USSR, as well as poor performances in building and insurance subsidiaries, a loss of confidence occurred. In 1993 business creditors brought bankruptcy proceedings which resulted in a restructuring and the creation of a slimmed down holding company. Today that concentrates on the retail and hotel trades and still considers itself a co-operative.¹¹

As far as Austria is concerned, Konsum Osterreich's problems and weaknesses were not solved by its merger with the more successful Swiss MIGROS. Its bankruptcy was delayed, not prevented.

The Swedish consumer co-operative movement has also been forced to make major changes¹³ but, like its Finnish counterpart, these are perhaps too recent to allow conclusions to be drawn. We can note that conversions of the kind we have seen elsewhere have played little part in the decline of consumer co-operative movements. We should observe also that, in part, changes in retailing are the other side of the coin of what is happening in the food processing industries and to the producer co-operatives operating within them. In retail societies these changes have necessitated considerable rationalisation and distribution through larger outlets. In turn these have made it necessary to find new sources of capital, causing members' share capital to decline as a proportion of a society's total capital. Consequently, members' mutuality based on capital, has been weakened at a time when their mutuality based on trade has also declined through the need to increase sales to non-members.

The effects of a changing environment can also be seen among co-operatives in the financial sector. Insurance societies seem particularly worried by demutualisation threats. These are occurring as a result of governments' new policies and regulations, the effect of which has been to harmonise far more the capital requirements and taxation policies relating to insurance and financial services. As a result, the capital requirements of co-operative insurers have been increased, so reducing their earlier competitive advantage. To some extent that had resulted from their being mutual insurers within the social economy and thus being allowed lower capitalisation. However, changes to this requirement are necessitating increased capital and that is leading some of them to consider demutualising.

The International Co-operative and Mutual Insurance Federation (ICMIF) has been sufficiently concerned to try to monitor the changing situation and to "identify means for financing co-operative and mutual insurance activities which reflect their values and principles". The Federation is also attempting to suggest "modern interpretations of co-operative principles that - while upholding the spirit of self-help organisations - encourage and support popularly based insurance companies to successfully operate in a competitive environment."¹⁴ In a recent report, it noted the distinctive situation in Japan where co-operative insurance is more closely

tied in with other co-operative activity than is commonly the case elsewhere:

Every co-operative federation is made up of primary co-operatives that join the federation and have individual members that possibly become "mutual" insurance policyholders. A large part of a co-operative federation's capital is composed of share capital from the primary co-operatives, and for co-operative federations are not to raise capital from the market.

Earlier, reference was made to moves by the Japanese agricultural co-operative insurers to prepare for changes in the Japanese economy. Their proposals can now be placed in a structural context where they will perhaps lend weight to the view expressed by Cronan that Australian co-operatives suffered from not having second and third tier organisations. British co-operative history and theory illustrates the truth of this and the benefits that can arise from federal mutuality.

The ICMIF report asserted that, "Demutualisation may not be the best and most practical option to raise capital, but it is the most emphasised in literature." This points up the need to develop counter arguments which could usefully build on the views of Schrader and Conran touched upon earlier. Schrader suggested that, in agricultural co-operatives at least, other returns than the short-term financial should be emphasised. Moreover, both he and Cronan felt that co-operatives had insufficiently explored the ways in which their members might be encouraged to contribute more capital, and the terms on which they would do so. Such possibilities should be kept in mind when we come to consider future strategies.

In doing so we should take into account reasons for conversions suggested above. Important among these were changes in the overall environment, particularly in the nature of markets as in food processing industries and in countries where protectionism has been reduced. Increased competition has necessitated increased capital. Consequently, co-operatives have been more ready to rationalise structures or to consider going down the plc route as a means of raising external capital. Conversions are also more likely to arise in economies that are restructuring and liberalising. They could occur when interest groups, such as

co-operative officials, anticipated personal benefits, or result in a blurring of the co-operative form, as with the idea of "co-operative companies" in India.

Elsewhere interaction with the wider economy could be a predisposing factor. We noted Schrader's view that conversions were likely to increase if financial pressures on co-operative members occurred when there was a bull market in corporate equities, but co-operative members were unable to benefit from the appreciation of their society's assets. The problem could worsen when a co-operative producing net earnings in excess of the opportunity cost of equity capital could be worth more to investors as an ordinary corporation than it was to its members. The problem of meeting the need for increased capital was exacerbated by members being either unable, or unwilling, to contribute more. An inhibiting factor was considered to be co-operatives' traditional preoccupation with service to members rather than return on capital. This view strengthened where rules laid down that collective or inalienable reserves should be held, giving rise to the belief that money put into a co-operative became "dead money".

With these issues in mind, we should now consider strategies to counter the apparent trend towards conversions.

Strategies

This trend cannot be quantified. Indeed, it may not exist. For example, the conversions that are occurring could be offset by the formation of new co-operatives: the extent, shape, and nature of the co-operative sector is always changing. However, the above evidence suggests that there is a trend, particularly in some types of co-operative. Moreover, that the current climate is likely to encourage it to continue.

Given the central importance of the question of capital, the study commissioned by the UKCC and undertaken by the Plunkett Foundation into the Financing and Taxation of Co-operatives, will be eagerly awaited. We cannot yet know what that will say. Nevertheless, it seems reasonable to suggest that it could usefully be augmented by other lines of research. One would be to examine Schrader's assertion that "Demutualisation may not be the best and most practical option to raise capital, but it is the one most emphasised in literature."

If he is found to be right we will need to reshape the literature with counter-arguments. One might build on Schrader and Cronan's view that members could be encouraged to contribute more capital. We have perhaps been over influenced by co-operative officials' concern that members' share capital is easily withdrawable. We have therefore been slow to consider other forms of members' funding, particularly forms that allow members to benefit from any appreciation of a society's assets. The question of member benefits is central. History shows that co-operatives have been most successful when they have conferred tangible member benefits. That success has been reinforced when there has been a clear link between the money members put in to a co-operative enterprise and the benefits their enterprise provides in goods or services. History has also shown that self-financing has been the most economic form of capitalisation in co-operatives, also that if members are sufficiently motivated, they will save in order to make high initial contributions. Rochdale and Mondragon are the classic examples.

We should recognise, however, that different types of co-operative need different levels of funding which suggests a second and related line of enquiry. This should be into the question of whether capital problems could be more easily handled if each type of co-operative had its own set of working practices like the original Rochdale Principles. These undoubtedly helped the growth of consumer co-operatives by providing a formula for success, but they have proved less relevant to other types of co-operative. The ICA's reviews of Co-operative Principles in the 1930s, 1960s and 1990s, have been complicated by the aim of producing a statement to encompass all types of co-operative. Unity should be valued but we should perhaps recognise that it is more likely to occur in the movement's underlying philosophy than in the working practices of its different sectors. Capital is an obvious example but, historically, there have been other difficulties. For example, open membership has always been easier in consumer, thrift, and credit societies. Initially retail co-operatives advocated no credit trading, but this soon became impracticable in the wholesales they created and later in agricultural and industrial producer societies. The present spate of conversions highlights the different capital needs of different types of co-operative. It therefore raises the question of whether there might be merit in encouraging different types of

co-operative to have their own sets of working practices in the way that credit unions have devised theirs. All would be brought together, though, through a shared philosophy.

This brings us onto the third line of possible enquiry namely, how best to deploy an important part of that philosophy, co-operative economy: it should become a central plank in counter-arguments against demutualisation. It would go beyond the economic argument so far used in the debate which has been that members of privatising mutuals may receive an apparently generous one-off payment, but their changed economic status will not necessarily be to their long-term economic advantage. Philip Ireland, in a recent article in this Journal,¹⁵ touched on this and had resonance with the long-held co-operative view that economic activity undertaken on a mutual basis can produce economies which are unlikely if the same activities are undertaken for profit in a share-holding company.

Co-operative economic theory needs to be revised and redeployed in face of threats of demutualisation.¹⁶

Making the best use of counter arguments requires that you have a clear picture of what is happening in the conversion scene. Australia seems to have been the only country, and the International Co-operative and Mutual Insurance Federation the only co-operative sector organisation, to have carried out detailed surveys. A similar survey should be conducted in this country. In the meantime, I hope that this paper will have helped to set the scene by showing what has been happening abroad.

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Building Societies at a Cross Roads

Adrian Coles

A few years ago, there was relatively little interest in the affairs of the various sets of UK mutual institutions from the staff of other mutuals. Thus, building societies, friendly societies, co-operatives, industrial and provident societies, and mutual life insurance companies saw themselves as quite separate from each other with relatively little in common. This perception is beginning to change, hugely, one fears, as a result of the de-mutualisation of some of the largest building societies and insurance companies, and the implications that this might have for other mutual and co-operative bodies. It is important, however, that the various mutual bodies come together not only as a result of their fears for the future, but also because the current situation presents a range of opportunities to emphasise the distinctiveness of mutual institutions. This paper covers the background to the decisions by a number of large building societies to de-mutualise, discusses briefly some of the factors that lead to de-mutualisation of building society type institutions abroad, but which are not present in the UK, and, most importantly, looks at what I have termed the "new mutualism" from which building societies are redefining their reason for existence. The final part of the paper discusses the opportunities which are available for greater co-operation between mutual institutions.

Trends in the housing market

In order to understand what is going on in the building society sector it is necessary to take a step back and examine trends in the housing market over the last ten years. As is well known, there was a boom in housing market prices and activity in the late 1980s, followed by a very sharp recession in the early 1990s. The housing market is now improving marginally, both in terms of activity and prices, but is extremely unlikely to return to the conditions which characterised even the mid-1980s, let alone those years towards the end of that decade.

There are a range of factors suggesting that there has been a fundamental change in the way the housing market behaves, in summary, they are as follows:

(a) Much lower rates of inflation than used to be regarded as normal. In the past high rates of inflation destroyed the value of outstanding mortgage debt, while at the same time leading to rapid increases in the value of houses purchased with that debt. Low inflation and relatively high real interest rates mean that the real costs of house purchase have increased significantly. Moreover, it is now more difficult for people to use the profit from the house that they are selling (because in many cases that profit no longer exists) in order to finance a house purchase. Transaction costs must be financed from savings, for which there are various alternative uses.

(b) Government assistance to owner occupation has been reduced. In particular the retention of the £30,000 tax relief limit, the abolition of higher rate relief, and the reduction in the standard rate of relief to 15% means that during 1996 tax relief will account for about 7% of all mortgage interest payments. In the mid- 1970s the equivalent figure was 40%. In addition, the government has made fundamental changes to the system of income support for unemployed mortgage holders, which make borrowers much more exposed to the impact of unemployment.

(c) Conditions in the labour market have changed significantly. There is much greater variation in levels of employment and unemployment than was the case before 1980. More short-term contracts, more part time jobs, greater reliance on self employment, later entry into the jobs market and earlier retirement are all features of the new employment scene. All of these factors militate against the tradition 25-year mortgage, although their impact has been ameliorated to some extent by the significant improvements in mortgage design becoming apparent in products launched over the last two years.

(d) Demographic change. There was a one third reduction in the birth rate between the 1954 post-war peak and 1977. The corresponding shift is of a one third reduction in the number of 25-year-olds 25 years later. The peak in the number of people in their mid 20s occurred in the late 1980s and the 1990s is seeing a continuing reduction in the number of first-time buyers, although there is a continued rapid creation of households in other age groups as a result of divorce, immigration and a sharp

expansion in the number of very elderly people.

(e) There has been increased interest in the private rented sector, government controls on rents have, broadly speaking, been abolished, the business expansion scheme provided a short-term boost, and demand for rented accommodation has been increasing, particularly among young people.

The effect of the smaller housing market

In 1996 it is likely that mortgage net advances will amount to little more than £16 billion, compared to a peak figure of £40 billion in 1988, with transactions down from 2.1 million to 1.2 million. Both figures have changed relatively little over the last two or three years. However, until recently the mortgage lending industry had in place an infrastructure that was designed to cope with the much higher levels of lending which people came to regard as normal in the 1980s. As the housing market recession continued and as the realisation grew that there would be no return to the old conditions, it was argued by many that there was a need for rationalisation in the market.

In the spring of 1994, the Cheltenham & Gloucester Building society announced that it intended to transfer its business to Lloyds Bank, with the ultimate intention, now fulfilled, of becoming the bank's specialist mortgage lending arm. Cheltenham & Gloucester was relatively underbranched but very efficient and is now able to distribute its products through the Lloyds Bank branch network, and processing of both Lloyds and C & G is centralised in Gloucester, enabling Lloyds Bank to use the capital previously tied up in mortgage processing to greater effect. Other mergers that have taken place, between the Halifax and the Leeds, and the Abbey National and National and Provincial have resulted in branch closures, and arguably in economies in mortgage processing.

The impact on mutual building societies

The Cheltenham & Gloucester announcement significantly changed the environment in which building societies operate and, more particularly, merge. Members of building societies suddenly realised that their membership was worth a great deal even though they had paid nothing for it. The average payout

to Cheltenham & Gloucester investors made by Lloyds Bank to effect the change of ownership, was over £2,000. It is not possible to do this in the event of two mutuals merging because large payments can be made only if the reserves of the society are, in effect, either turned into shares and traded, or purchased for cash by another institution. The management of any large building society intending to merge needs to take account of the possibility of a hostile bid from another financial institution emerging which would result, if implemented, in a significant payout to the members of the society seeking to merge. There is at least a chance that the members would reject a recommendation to merge with another society if there was a chance of an alternative corporate strategy releasing value to them. It is for this reason that since the announcement of the Cheltenham & Gloucester /Lloyds Bank proposals there have been relatively few mergers and those that have taken place have involved relatively small societies for which conversion is effectively impossible.

There has also been a significant impact on the continuing business operations of building societies. Given that membership of a building society has now been revealed to be worth a great deal but can be acquired at zero cost merely by opening a savings account, press speculation about the identity of those building societies likely to announce conversion in the near future has resulted in long queues of people outside building society branches seeking to open accounts. Indeed, on occasion, some societies have been besieged by bounty hunters seeking something for nothing. This has drastically affected the level of service which those societies have been able to offer to their genuine and long-standing members, and also forced many societies to increase the minimum sum required to open an account, thus denying savings facilities to those of modest means.

A final matter for consideration, which was not the subject of debate before the Cheltenham & Gloucester announcement, is the duties of directors. Members of boards of building societies have been forced to examine their role. Are directors of building societies trustees of the funds built up by past generations of members for the benefit of current and future members? If so, they are not morally in a position to release those funds to those who happen to be members at any single point in time. Alternatively, is it the duty of the directors to look after the best

and immediate interests of the current members and to return value to them in the form of a share of the reserves which, legally at least, today's members appear to own?

Advantages of the pie format

The key advantage of the plc format is that it enables the institution concerned to more readily take part in the rationalisation of the mortgage lending and financial services industries. As noted above it is now difficult for two individual building societies to merge. Perhaps even more importantly, a society that has converted to plc status can issue shares. In other words, it can print "money" in order to acquire other institutions. This key advantage is not available to mutual institutions. They have to purchase with cash that has been built up as a result of retaining profit.

The second factor is the five years' protection from takeover given to converted societies. This is a feature of the Building Societies Act 1986 and was introduced because it was felt that fledgling converted societies would need protection from takeover during their early years in the stock exchange jungle, following the protection deemed inherent in building society status. It has now become apparent, however, that building societies are somewhat less protected from hostile takeover bids than was originally believed, thus increasing the apparent attraction of the five-year protection from takeover granted to newly converted societies.

There are a range of other advantages claimed for conversion. Some societies feel that they will have greater freedom to operate under the banking legislation compared to building society legislation. However, the Government is proposing new building society legislation which, if enacted, will provide much greater freedom to building societies. Some have claimed that the plc form of ownership engenders greater accountability on the part of managers to owners. In the stock market context, a poorly performing plc will find its share price falling, and the management exposed to takeover bids from other individuals who think that they can do a better job. The last five years have shown that building society managements that are perceived as weak and indecisive, or who have adopted an unwise lending policy, face the same fate.

Some converting societies also argue that it is important that diversification into new and unfamiliar areas is supported by risk capital rather than the capital built up from the relatively safe savings and mortgage business. A number of mutual societies would accept this argument. Finally, it is suggested that the size of an organisation itself precludes organisation along mutual lines. This is the subject of some debate. It has clearly not persuaded the large mutual institutions in Europe (for example, Credit Agricole in France and Rabobank in the Netherlands) to give up their current status. On the other hand, some might find it difficult to discover a mutuality of interest among the ten million members of the Halifax Building Society.

Developments abroad

It is interesting to note that the key factors involved in the conversion of building societies and building society type organisations to stock status in overseas Anglo-Saxon countries (notably the USA, South Africa, Australia, and New Zealand) have not been a feature of the debate in the United Kingdom. There are four such factors:

- (a) The desire to obtain bank status. In all of the countries mentioned, building societies and other similar organisations were regarded as second rank institutions, not as important, or as safe, as banks. A key incentive to convert to stock status was to be able to call the institution a bank, so giving the institution status and prestige. It is notable that in this country those institutions that have converted, or intend to, do not and will not use the word "bank" in the name of their organisation. It is Abbey National plc for example, rather than Abbey National Bank plc.
- (b) Corruption - One of the reasons for the poor name of building societies in Australia and thrifts in the United States was a not entirely undeserved reputation for corruption, which contaminated the entire sector. No such suggestions have been made in the United Kingdom.
- (c) Wider powers-The UK Government has adopted a relatively liberal attitude towards granting building societies new powers. It is likely that had this approach not been followed, the current wave of conversions would have occurred much earlier.
- (d) Capital - In America especially, business conditions resulted

in the decimation of the capital base of the thrift industry. In order to restore capital positions, it was necessary for the thrifts to issue shares not for free, but paid for, in order to recapitalise the business. British building societies are relatively well capitalised, and again, this has not been a motivation for conversion.

Interestingly and as noted earlier, there has not been a similar wave of de-mutualisation in continental Europe. Indeed, it appears that the statutory machinery to enable conversion to take place does not exist, and there is a general prohibition in French, Dutch, and German legislation on the payment of any share of the profits of a mutual organisation to its members.

New mutualism

So far this paper has identified the reasons for conversion taking place. In summary they relate to the decline in mortgage market activity, the perceived need for rationalisation in the mortgage lending sector, and the greater ease with which this can be undertaken within the pk rather than mutual format. Some might take this to be a convincing case for de-mutualisation. Why then have 70 odd societies set their face against this course of action? If the key advantage of a pk is the ability to issue shares or to print "money" in order to acquire institutions, the key advantage of mutual institutions is that they do not need to pay for their capital. The ability to issue shares comes at a heavy price - the payment of dividends. Many continuing building societies have taken the view that they are now in a position to, in effect, pay a dividend to their customers by holding their mortgage rates lower and their savings rates higher than the converting societies or the banks. The Britannia Building Society has gone down a so far unique route, offering its members a share of the profits made by the organisation, that share being dependent on the nature and extent of each member's relationship with the society. It might be asked why it took societies so long to wake up to the crucial advantage of their corporate status. The answer is that the early 1990s were characterised by a rapid growth in arrears, and most notably repossessions, on which all mortgage lenders, including building societies, made significant losses. Homes that were repossessed could not be sold so as to cover the outstanding mortgage debt, and the reduction in house prices

was such that even the mortgage indemnity payouts from insurance companies did not cover the losses. During the first half of the 1990s both building societies and banks were forced to repair the damage to their balance sheets caused by the recession. Now that that repair job is complete, ways of returning value to members can be examined and implemented.

The second element of the new mutualism is unrestricted powers for building societies. Until the passage of the Building Societies Act 1986, building societies were effectively governed by legislation that was passed in 1874 (although various 20th century acts amended this very marginally). The 1986 Act enabled societies to diversify into a wide range of areas related to savings and mortgages, such as house building, estate agency, credit cards, cheque books, insurance broking and insurance underwriting. However, building societies were still left at a disadvantage compared to other financial institutions in that the legislation was very prescriptive. Building societies could only enter those markets and could only undertake business in a manner prescribed by the legislation. It remained illegal for a building society to undertake any function not mentioned in the legislation.

Proposed new legislation would change the basis of the controls on building societies so that rather than being allowed to do only those things permitted in the legislation, they would be allowed to do anything unless it is expressly prohibited by the legislation. The Bill proposes that 75% of building society lending shall be on the security of housing (irrespective of whether it is owner occupied or rented) while the remaining 25% can be invested in any asset. There may well be a debate about the wisdom of allowing specialist financial institutions to diversify; on the other hand, some may question the wisdom of forcing building societies to keep all of their eggs in one basket - the housing market. Those who fear that building societies may be stirring up difficulties by moving into new and unfamiliar areas will be reassured by the fact that it is proposed to strengthen the powers of the Building Societies Commission, probably the most successful of the financial services regulators created in the 1980s. Indeed, the building society sector has been almost unique in not being rocked by scandal in recent years. There has been nothing to match the disasters that have hit Barings and BCCI in the banking sector, Barlow Clowes and Roger Levitt in the

financial advisor area, Maxwell and the sale of personal pensions in the pensions area, or Morgan Grenfell in the unit trust market. Repeated market research exercises show that building societies have a uniquely warm relationship with their customers which is based partly on the skills to be found within the supervisory regime.

The third element of the new mutualism is accountability of societies to their members. Building societies have been accused of not being as accountable as plcs. There is not space to go into that debate within the confines of this paper, however, the new legislation proposes a range of initiatives, many suggested by building societies and the Building Societies Association (BSA), to improve accountability. These include the granting of voting rights, currently held only by investing members, to borrowers, the requirement to hold a ballot to determine the membership of the board even where the number of candidates equals the number of vacancies, a requirement to list candidates in alphabetical order, an obligation to consult members where the society is making a significant investment outside its core business areas, and an obligation to list the results of the elections for the board in branches. The Association has taken two initiatives. First, it has published a booklet *Your Rights as a Member of a Building Society* which describes the constitutional (rather than contractual) rights relating to various corporate governance issues of members of a building society. The Association has also sent to its members a circular giving advice on the nature of the information which they should give to individuals contemplating standing for election to the board.

Finally, new mutualism has rediscovered the ethic of being a mutual institution, of realising that building societies exist to serve customers and their local communities, rather than any other group. A number of societies have taken various initiatives to abolish obsolete savings accounts, and also to offer special benefits to long standing mortgage customers not available to new borrowers. Most societies also provide assistance to a range of local charitable and community organisations operating in the area of their head office, ranging from Citizens' Advice Bureaux giving money advice, to sponsorship of local sports leagues.

I indicated at the beginning of this paper that there was renewed interest in encouraging co-operation between mutual

institutions and a realisation that some of the issues which faced building societies, industrial and provident societies, credit unions, co-operative organisations and mutual life companies in today's environment were very similar. This year the BSA has hosted two lunches at which the guests have been leaders of various mutual institutions. Guests have included senior executives from friendly societies, mutual life companies, BUPA and the Automobile Association, and work is currently being undertaken within the BSA on whether there is scope for further joint work between mutual organisations.

Building societies have been through a period of self doubt and confusion as each has examined why they exist and what they should be doing. They have learnt that success in the past is no guarantee even of existence in the future. Some have concluded that their future lies outside the mutual structure. Others, however, have taken the initiative and brought new life and vigour to the concept of building societies. One of the most fascinating experiences in British commercial life is about to begin, with direct competition between mutual and stock-based institutions in one of the key financial markets. For both sides, the stakes are high, as the market will show which of the two approaches adopted by those institutions currently called building societies proves successful.

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The Renaissance of Mutuality: Britannia Building Society

Gerald Gregory

There was a time - say a year to 18 months ago - when any speech with the title "The future of mutuality" was due to attract wisecracks from the media and commentators. Bound to be a very short speech, they may have said. Don't use mutuality and future in the same sentence, they could well have added.

Mutuality is enjoying a renaissance. The debate continues, but I think it's fair to say that today mutuality is recognised as a viable, sustainable means of conducting financial services business now and in the long term. What has shifted opinion? Those major building societies which have rejected the headlong rush to conversion and plc status have re-committed to mutuality and used their creativity to modernise and adopt it. Societies are proving that modern mutuality is alive, kicking, and relevant to the current and future needs of their members. I hope you will not call me immodest if we at Britannia claim that we are playing a leading role in this renaissance. We emphasised our commitment to mutuality by becoming the first building society to introduce a Members' Loyalty Bonus Scheme. It is the only Scheme which gives building society members a direct share in the profits. No dedicated commercial man should waste an opportunity to pitch for business, so I will save for later a more comprehensive explanation of our Scheme, how it works and how it is being received by our members. First, I'd like to explain to you why we felt it necessary to take this step, and I'll close by sharing some thoughts on how Britannia may continue to develop its mutuality, and indeed how mutuality itself may develop.

The great Mutuality v plc will run and run. You will all, I suspect, have heard the arguments for and against. Sadly, the debate has often come down to the quick buck issue. Many speculators have invested a few hundred pounds in building society membership in the hope that the society (or societies) they've joined will convert to a plc. They hope for a windfall payment from distribution or reserves, but where has this money

come from? A society's reserves have been built up by its members over generations to provide savers with security for their savings and protect borrowers from the worst effects of the interest rate cycle. No one has an individual right to those reserves. They are there for all members, present and future; this is not just a legal issue, it is a moral issue too. Do we really believe that someone who has held a few hundred pounds in an account for a year or two should be able to walk away with funds built up over many years by thousands of others? Clearly this is nonsense, reserves are just not up for grabs. The 'give us the money and we'll run brigade see a commitment to mutuality as nothing more than a barrier to a fast buck. They clearly think it is a good thing that some societies have decided to become plcs purely on the basis that they'll get their windfall. It's very interesting to note how many self-confessed speculators fully intend to put any windfall profits back into a building society. Even those people who are attracted by the prospect of getting something for little or nothing seem to realise, in their heart of hearts, that there's always a price to pay. Our view is that this price is simply too high.

It is easy for mutuals like Britannia to appeal to the emotions and say: we're not converting because we're not selling our birthright. Frankly, that is not enough, and it provides ammunition to those who, quite wrongly, attack mutuals as being quaint anachronisms. The acid test in the Mutuality v plc debate is: what is in the best interests of our members now and in the future? Level-headed commercial logic has to be applied. Indeed, the board of any building society is charged with doing so. It is their statutory duty. What matters, what really matters, is this: how should our business be constituted to that we can best meet our members' needs? At Britannia, our board examined in incredible depth all the options available for the development of the business, as any organisation worth its salt needs to. Continuous improvement is a fact of business life.

When the Halifax announced its conversion plans most society boards would have re-examined their strategy to ensure they were not missing a trick - if the largest mutual is giving up there must be a reason for it. The commercial logic runs that the mortgage market is commoditised and therefore only the most efficient can survive and cost efficiency= scale. The only problem is that there is no connection between scale and efficiency. The

board looked at conversion and rejected it, unanimously, in favour of a modern form of mutuality. The core of our argument is that as a mutual society, we exist solely to serve the interests of our owners - the members. There is a perfect alignment of interests when members are both owners of the society and valued customers. Our 1.6 million members own Britannia and they have a direct say in how we operate on a one person, one vote principle. It is direct accountability. Our competitors who are intent on becoming pies are placing themselves in the unenviable position of having to mediate between customers and shareholders, whose interests will almost inevitably conflict.

If I can move outside the financial services arena for a minute, there is an interesting comparison to be drawn between pies in the very competitive, consumer orientated financial services market and some of the more recent developments in supermarket retailing. Efforts are being made by some of the larger supermarket chains to make us all feel like valued members of a club. Affinity cards offering long term benefits of one sort or another are everywhere, and very welcome they are, too. But in this rush to lock customers in with special deals, quoted retailers run the risk of narrowing their profit margins to such an extent that the City loses interest. In fact, supermarket chains have historically been lacklustre stocks for precisely this reason - the fight to keep customers has left shareholders looking elsewhere for better returns.

It is a matter of record that banks have historically offered a poorer deal to their customers than have building societies. This is reflected both in interest rates charged and offered, and in levels of service. The July issue of *Which?* featured an article on "How to cut the cost of your mortgage" which explained how lenders can offer such large cashbacks and discount deals "because they have a huge book of existing customers paying the standard variable rate" and so existing borrowers subsidise new business. In contrast the article promoted Britannia stating, "a few lenders including Britannia offer loyalty bonuses to long term borrowers". Clearly we are adding value to all members without penalising our existing members. I cannot believe that there is no connection between this and a desire to keep shareholders happy with ever higher profits and dividends. With the privatisation of water board, British Gas and other utilities, the philosophy of short-term gains has become increasingly

apparent from a shareholder point of view, where they are interested in the profit margin of the company.

My point is that plcs in competitive consumer industries inevitably have to juggle between customers' and shareholders' needs. One group can easily be disappointed. It remains to be seen who the losers will be when the rash of building society conversions has died down, but if I were a member of a converting society, I would be asking my managers some very hard questions about where they anticipate their loyalties will lie. Unless they are content to be seen as an under performing stock, these managers will inevitably find themselves listening carefully to the demands of City institutions whose financial muscle will easily outweigh the interests of ordinary shareholder, let alone customer. Would the average plc shareholder-customer really be able to influence the future direction of their chosen financial institution if their interests clashed with those of a major pension fund or corporate investor?

At Britannia, we encourage members to nominate directors to our board so that we can be sure we are representing their interests fully and properly. This year there was a 60% increase in members voting. If anyone wants to change the direction that Britannia is taking, they can do it by persuasion, not by flexing financial muscle. I believe this is a valuable way of making sure that we continue to serve the interests of our members, rather than those of some external body more interested in short term profit than long term service. Nevertheless, we still have to be competitive, and we have to offer our customers the services they demand. According to plc enthusiasts, this requirement presents us with grave problems.

The argument is that building societies are so constrained by the legal framework that has grown up around mutuality that they can't develop away from their core of mortgages and retail services. Not only are they forbidden by law from moving into new areas, but they can't borrow the funds they need to provide the necessary infrastructure. Our customers, we are told, are crying out for ever newer and more sophisticated products that can only be provided by plcs. I don't accept this for one minute. The average customer in the street would be hard pressed today to tell the difference between the range of personal finance products being offered by any top ten bank and those offered by any top ten building society. It wasn't always like this. You only

have to go back ten years to find a market in which the breadth of choice available to customers was nothing like what it is today. Then, you went to your mutual building society for a mortgage and a savings account, and to your publicly quoted bank for a current account and possibly a personal loan. Your insurance would probably have been arranged for you by a broker who you went to see independently of your bank or building society. Leaving aside the endowment policy bought when you took out your mortgage, any other life cover would probably be set up the same way.

Compare this with today's world and it's simply not credible to claim that mutual societies cannot expand into new areas. Current accounts, unsecured lending and insurance are now everyday products for building societies. We are fully accepted by the public as mainstream providers of these services, and they contribute a healthy slice of our revenue. Even those restrictions which were written into the 1986 Building Societies Act have been steadily relaxed by successive Government reviews. The Government has now decided to move away from a legislative regime which prescribes in detail the activities which societies may undertake. Instead, societies will, in future, be free to pursue any activity not explicitly ruled out by the legislation - provided we retain, as our main purpose, lending secured on residential property, funded in the main by our retail customers. Only the most gung-ho of building society chiefs could see that as a serious constraint on the business. Certainly, we at Britannia now see no obstacles at all to providing our members with virtually all the personal financial services they could possibly need. Having said that, those building societies which have become banks haven't yet shown any signs of seriously expanding the range of service they offer. In fact, as a building society, the Cheltenham & Gloucester made a distinct virtue of confining themselves to their core business of mortgages and savings.

The only area which mutuals are still largely barred from is lending to companies, and that, perhaps, is a good thing. Certainly, Abbey National has shown no inclination to move into corporate lending, and its standing in the market, by comparison with the other major banks, has benefited immeasurably from this restraint. So, if mutuals aren't constrained by law from providing the services their members are

demanding, are they stopped by lack of capital? This question is tied very closely to the issue of providing the owners of the organisation with value. All too often it's the people who say that mutuals must convert so they can tap the equity markets for capital, who then criticise us for not distributing retained profits to our members. You can't have it both ways. Either we don't have the funds we need to expand, in which case we don't have any retained profits to distribute, or we do have massive reserves, in which case investing some of them in the business to provide more and better services for our members is a perfectly reasonable way to provide them with value. The way in which building societies behave is driven by our members, not by external shareholders and their day-to-day requirements. Building societies have strong reserves to protect savers and our record in the industry of no saver losing capital is a proud one. Compare this with the BCCI or Barings collapse or the plc casualties like Polly Peck and Maxwell.

Our Members' Loyalty Bonus Scheme gives us a visible point of difference from other societies as our scheme awards our loyal customers with an annual one-off payment. We believe it is a first-class example of modern mutuality in action. The Nationwide and Bradford and Bingley have chosen to demonstrate their commitment to mutuality through shaving percentage points off rates. We believe that straightforward changes in mortgage and savings rates are not enough to show that a society is fully committed to serving its members. Customers are already used to rates rapidly changing in the marketplace, and the effect of another rate change would have little impact in comparison to an annual bonus. Having made that point, there's clearly a strong case for recognising customer loyalty with some form of special concession or reward, and that is what we are doing with our Member's Loyalty Bonus Scheme. This shouldn't be confused with a shareholders' dividend. Rewarding our members for their membership has little in common with rewarding shareholders for their equity holding in a company; a dividend, as I understand it, is a reward for risk capital, which is paid as a distribution of profit.

Given that generally speaking our members have no invested capital in their society, the concept of dividend as a reward for risk is nonsense. However, the profits of the Society's business are generated by the behaviour of our members, and it is entirely

appropriate that profits in excess of those required to maintain the capital base of the society should be returned to the members. The manner of distribution should ideally reflect the contribution that the member has made to the profit. We didn't come to this conclusion without checking it with our customers; the development of the Scheme - which has taken 18 months - has been the most heavily researched strategic development the Society has ever undertaken and what's more it has been the most enthusiastically received strategy welcomed both by staff and customers; our Scheme has been designed to be fair and equitable to all our members and was introduced to specifically reward long-standing members for their loyalty and to add value to membership. It offers annual cash payments to members with qualifying mortgage or investment accounts. In the first year, we expect to pay out around £35 million - around a third of our profits. The payments will come from the profits made over and above those we need to support and develop Britannia's business and will not dilute the society's capital strength. We see it as a classic virtuous circle because the better the society does the more our members will get.

Members earn points each year depending on the size of their monthly mortgage payment, the amount they have invested in qualifying accounts and how long they have been with Britannia. Those who have been members for between five and nine years will have their total points multiplied by 1.5. From year 10 onwards, their points will be doubled. At the end of each year, we will declare a value per point depending on our profits. Each member will receive a loyalty bonus depending on how many points they have earned during the year. A typical customer will receive £49, during February and every subsequent February - it is also within the power of customers to increase their payment by changing behaviour - buy more of our products and your bonus will increase. Our research has shown that consumers will change their behaviour to receive payments of £50 - remember a typical new mortgage advance would qualify for an annual bonus of approximately £100.

Our Loyalty Bonus Scheme is not an alternative to competitive, innovative products and service - members will get these as well. We set out to make our Scheme fair and transparent and before we launched it earlier in 1996, we market tested it extensively among our members. It has been received

With enthusiasm. Currently, we are in the process of registration. So far, of 1.6 million members mailed with the details, 700,000 have registered. The more products our owner-members have with us, the more they get. What we have said to our members is that after the first year we are prepared to adjust the Scheme if there are some features that could be improved. Any responsive members' organisation should behave this way.

So where do we go next? One virtue of being a mutual organisation with a long-term view is that we don't have to follow every fashion and run off down every blind alley for fear of falling behind our competitors in the race for short term profits. We can take a more measured view of what our members really will find helpful. Our corporate objective has been changed from volume and profit targets to an objective of maximising profits for eligible members. In the past, new customers tended to benefit from new mortgage deals at the cost of existing members, but our aim is to take out the cross-subsidy element between new and existing members. This will become more and more visible in our product design. In effect we're less interested in volume and more concerned with membership and profit.

As a modern mutual building society with no external shareholders to consider, it is very important that we get our message across and details of our Members' Loyalty Bonus Scheme to as many people as possible. Hence our decision to be the first society to make mutuality and our Scheme the centrepiece of an advertising campaign. The advertisement asks: "What kind of society do you want to be part of?" and outlines what makes mutual societies different from banks. To emphasise Britannia's commitment to mutuality we also changed our company branding to read Britannia - The Sharing Society. This is tangible evidence that we are a modern mutual determined to remain a successful member organisation.

Registration packs for the Members' Loyalty Bonus Scheme have now been sent to members, who are being asked to complete and return their forms. The enthusiasm with which the Scheme has been received has been extremely encouraging. It has also given Britannia an excellent opportunity to segment the database and build up a product picture of each customer across all their holdings. By storing information in this way, future product development and marketing campaigns can be planned with even greater knowledge of the existing customer base and

requirements. Understanding our customer base is vital to sustaining mutuality in the future and as a mutual organisation we are dominated by members' interest rather than the short-term needs of shareholders. Compiling customer information in this way shows further evidence of Britannia's commitment to mutuality and effort to maintain a competitive edge for its members.

The explicit benefits of mutuality and members' ownership of the society must be visible. Our Scheme goes beyond simple pricing and represents an unequivocal commitment to visibly rewarding members for their continued, long-term support. The key point is that we will remain a mutual. Touche Ross, in their recent study of the future of building societies, concluded "Mutuality is, and can continue to be, a valid and viable form of business entity. Indeed, it seems to have a number of highly desirable aspects. Despite this, its continuation is far from assured and depends very much upon the building societies' own determination to survive." Touche Ross clearly think, as I do, that mutuality is not a soft option. If we are to continue in business, we will have to be as good as the best, and deliver value to our members that is at least comparable to what they could expect from the best plc. At Britannia, we are determined to survive and prosper as a well managed, mutual organisation. We have far more to offer than the prospect of a quick buck. We want our customers to be able to enjoy the tried, tested, and trusted benefits of mutuality for a long time to come.

Gerald Gregory is Director of Marketing and Mutuality at the Britannia Building Society.

The Work of the UK Co-operative Council.

Peter Walker

The UK Co-operative Council (UKCC) was established in 1991 as a replacement for the "Co-operative Forum" which operated under the state-funded Co-operative Development Agency (CDA). The CDA had, for more than a decade, worked to support co-operatives and the development of co-operative enterprise throughout the UK before it was wound up by the Government in 1990. The UKCC was set up to promote and encourage the development of all forms of co-operation" but, unlike the CDA, was established by the various national co-operative federations themselves with the support of the Co-operative Parliamentary Group, the Society for Co-operative Studies, and other key players in the co operative sector.

I often hear people refer to the UK co operative movement when in fact what they usually mean is the retail movement, i.e. 30 plus retail co-operative societies, or perhaps they mean the consumer movement, i.e. retail societies plus the Co-operative Insurance Society (CIS), Co-operative Wholesale Society (CWS), and The Co-operative Bank. The fact is that consumer co-operatives are only part of the total co-operative movement, or co-operative sector as we prefer to call it in the United Kingdom. There are hundreds of agricultural co-operatives which, on a total turnover basis, are bigger than the consumer co-operatives plus housing co-operatives, credit unions, community co-operatives, health & care co-operatives, and worker or employee-owned co-operatives. Each of these different types of co-operative has its own national federation such as the Co-operative Union for consumer co-operatives, ICOM for workers' co-operatives, or FAC for agricultural co-operatives. It is these national apex bodies representing the different types of co-operative that make up the membership of the UKCC and it is their representatives, 13 in all, who sit on the Council, decide on our priorities, and provide the funds, either in cash or contributions-in-kind to enable the UKCC to carry out its work. The UKCC is therefore self-funding, non-political, and independent of government and, for that matter, any other body.

The UKCC's role is basically threefold:

1. To promote the common interests of co-operative organisations of all kinds and the development of co-operative forms of enterprise throughout the UK.
2. To raise the profile and represent the interests of co-operatives to the Government, media, other key decision makers and the public in matters where a cross-sector view is relevant.
3. To make provision for discussion and debate within the total UK co-operative sector and to broaden the understanding and encourage collaboration between the different forms of co-operative enterprise.

Our role is therefore to promote and represent the interest of co-operative enterprise per se but only when a cross-sector view is relevant, and it is certainly not to represent the interests of any one particular type of co-operative enterprise or take over the role of any of the various national co-operative federations. Clearly this point is not understood by some people in the retail sector who keep writing to the *Co-operative News* complaining that the UKCC is usurping the role of the Co-operative Union. On the other hand, perhaps I'm wrong, they do understand but they are just jealous of the success of the UKCC.

For success is undoubtedly what it is - in just five years we have established the UKCC as the one body that is recognised by Government, the Opposition, the European Commission, and other influential bodies to speak on behalf of the total UK co-operative sector on matters of common interest. We have carried out a number of major projects on behalf of, and in partnership with, the UK Government and the European Commission. We have brought together the disparate parts of the total UK co-operative sector far more effectively than the old CDA ever achieved, with the effect that these different forms of co-operative enterprise now understand much better the role and aspirations of their colleagues in other types of co-operative enterprise which has led to many fruitful collaborative projects. Through the UKCC's Legal Working Group we have managed to get all the different parts of the co-operative sector to agree on one proposal for a new UK Co-operatives Act, which has the support of the Co-operative Party, and we have the commitment of the Labour Party to introduce new co-operative legislation when they come to power. We have also produced proposals for

a new European Co-operative Statute but again, perhaps we will have to await a Labour government to see any progress on that front. However, at the request of the present government, we have produced in partnership with ICOM a Resource Pack for Business Links, Training and Enterprise Councils, Enterprise Agencies etc., which seeks to raise the awareness of the co-operation option, particularly employee-owned co-operatives, among business advisers. The pack has been so successful that the Department of Trade and Industry (DTI) agreed to fund a reprint, and we are still receiving on a daily basis, requests for copies and further information from business advisers, solicitors, accountants, family businesses, academics, and the media.

Another successful initiative was the publication of the UKCC's book, *The Co-operative Opportunity*, which has since been widely acknowledged as the most comprehensive account of the co-operative form of business enterprise, at national and international level, to be published for many years. In Europe, the UKCC joined forces with Department 23 of the European Commission to commission research into non-user investor members in co-operatives within the EU nations, resulting in the publication of another significant report which could have far reaching consequences for co-operative development in the longer term.

More recently we persuaded the Department of Health to fund a major research study into the role of co-operative principles and structures in *Health of the Nation* activities. The UKCC Chairman, Lord Carter, and myself were invited by the Department to join a Steering Group overseeing this project. The resulting report, "Co-operating for Health", is now published and includes many examples of health and care centres already operating either as co-operatives or following co operative principles.

Another area that we have tackled on a cross-sector basis is that of the financing and taxation of co-operatives, an area where many people have argued that co-operatives are not allowed to operate on the same basis as other forms of enterprise - the search for the so-called "level playing field". The UKCC therefore commissioned the Plunkett Foundation to carry out research across the total co-operative sector in the UK and examine the practices in Europe and elsewhere..

One of the main functions of the UKCC is to promote

co-operative enterprise to influential bodies and individuals. There is no doubt that there is widespread ignorance of the diversity of the co-operative sector, how co-operative enterprise differs from other forms-of business and what contribution co-operatives can make to the total economy of the UK. If one examines the teaching of co-operative enterprise in schools and colleges, it is perhaps not surprising that this ignorance exists. Despite some sterling efforts in certain co-operative sectors and in a few geographical areas of the UK, there is no national resource material available to schools/colleges which seeks to explain the total co-operative sector from a business enterprise perspective. The UKCC is therefore seeking to persuade the government to support the provision of resource materials for all those throughout the UK studying Business Studies and Economics at GCE A and AS level, plus GNVQ and their equivalent in Scotland and Northern Ireland. Such material would explain why co-operatives are different from other businesses and the fact that all co-operatives, whether retail societies, agricultural co-ops, or housing co ops, are owned and controlled and should be run for the benefit of their members. In other words, they are in essence mutual organisations.

Early this year, the UKCC produced a paper on mutuality which did not seek to argue the case for mutual status but simply outlined what was currently going on in the main sectors of the mutual family, i.e. building societies, co-operatives, and mutual insurers. I think I dare say that it is one of the few papers produced that looks at what is currently happening across the whole mutual family. The UKCC Fifth Annual Forum will examine, under the title *The Future for Mutuality*, what mutual organisations can and should do to convince their members and the world at large that maintaining mutual status is in the long-term interest of their members and the country as a whole.

Peter Walker is Chief Executive of the UK Co-operative Council.

The Society for Co-operative Studies

Report of Annual General Meeting

The Society held its Annual General Meeting at the end of its highly successful Conference Weekend. Fifty-two members were present in the Marshall Room at the College at 11.15am on Sunday September 15, 1996, and apologies for absence were received from Garth Pratt, Brian Rose, Lily Howe, Alex Wilson, Mervyn Wilson, Jean Gaffin, Graham Melmoth, Alan Gill, David Allonby, George Cunningham, David Rushton, Peter Clarke, Tom Carbery, Bob Marshall, Kathryn Smith, Roger Spear, and Alan Harvey.

Minutes of previous meeting

The minutes of the meeting held on October 1, 1995, were approved as a correct record.

Annual review by Chairman

Following a short analysis of the modern fashion for assuming that "change" and "new" necessarily meant "better", and while pointing out that "good" and "bad" could not be replaced with "new" and "old", the Chairman noted however that in his short year as Chairman of the Society just about everything of any consequence had changed, with many new features being adopted.

It was the first year operating under the new constitution. The first year operating with a new charitable status. The first year with a new Secretary - and after very many years, the first year with a new Editor of the journal. After an equally long number of years the journal had also got a new format and that was only the beginning of further improvements and even the age-old logo had been changed. Equally, for the first time in many years there was a proposal to increase the subscription - another change, which needed to be seen as an improvement!

In particular during the year, the Committee had strengthened relationships with other organisations. The relationship with the Co-op College had improved after many years, with a member

of the college staff co-opted onto the committee. Reciprocal representational arrangements were underway between ourselves and the Plunkett Foundation. Arrangements for the joint exchange and circularisation of information and minutes with the UKCC had been developed; and equally a closer association, and developing joint approaches, were underway with the Open University.

The Congress fringe meeting had been the best ever. The Secretary's printed report showed in more detail the full extent of the year's progress, and that was due to the contributions that all the officers were making, voluntarily, in giving their time and efforts on the Society's behalf - and to whom all members were grateful and expressed thanks.

Secretary's report

The Secretary's report had been included in Journal No 87, September 1996. Areas covered in the report were - Committee Meetings; New Society Logo; Journal Editor; The Journal; Financial Position; Fringe Meeting; Internet Developments; Membership Subscriptions; Registration of New Constitution; Mutuality; Developing Closer Links with the Co-operative College and The Society's External Relations. The report described a year of steady progress for the Society. It was agreed that in next year's report the attendance figures of Executive Committee members would be included and that the first names of the Executive Committee would also be included.

Treasurer and Membership Secretary

The Treasurer and Membership Secretary's report had been included in Journal No 87, September 1996. It was noted with pleasure that 37 new members had recently joined the society, and 14 new subscriptions had been received from overseas. The content of the Accounts were noted and approved. The meeting expressed their thanks to the Society's Auditor for his work on behalf of the Society.

Editor

Johnston Birchall reported upon his first full year as Journal

Editor. The year started with a retrospective look at the College and members expressed their appreciation to Len Burch for his excellent article included in that issue (No 85). The new Journal format had been introduced in Journal No 86 (May 1996) and No 87 (September 1996) and had been well received. The Editor asked members to let him know if they had any criticisms regarding the new format as he greatly valued the opinions of readers. Johnston Birchall made specific reference to the establishment of an Academic Advisory Board, the appointment of a Production Editor, the recent publication of a News Letter and the greater emphasis being placed on marketing the Journal. Members commented upon the improved layout and content and the need for the Journal to retain a proper balance and always mindful of who pays the bulk of the subscription income.

Regional reports

A letter from Alan Harvey was read out by the Chairman requesting that consideration be given to resurrecting the London meetings of the Society. After careful consideration Fred Broughton agreed to arrange a London Conference.

Consideration would also be given by the Executive Committee to sponsor regional meetings and possibly link with other events taking place. Alan Wilkins indicated the plans that were in hand to hold Society meetings in the Midlands.

Election of Honorary Officers and Executive Committee 1996/97

Members expressed the need for Committee members to attend meetings on a regular basis and then the meeting proceeded to appoint the following officers and committee members for 1996/97 -

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| • Chair | Len Burch |
| • Vice-Chairs | Peter Davis and Rowland Dale |
| • Secretary | John Butler |
| • Journal Editor | Johnston Birchall |
| • Treasurer & Membership Secretary | Frank Dent |

- Additional Committee Members
 - James Bell
 - Rita Rhodes
 - Jim Craigen
 - Martin Stears
- Immediate Past Chair
 - Peter Clarke
- Auditor
 - Peter Roscoe

Presidents

The existing Presidents of the Society, Professor Tony Eccles, Dr Robert Marshall, John Morley, Dr Alex Wilson, Lord Young of Dartington, Graham Melmoth, and Professor Tom Carbery were re-elected.

Subscriptions

The Treasurer reported upon the proposed rate of subscriptions for year ended March 31, 1998. After careful consideration it was agreed that the basic and sponsorship waged rates both be increased by £2 to £9 and £14 respectively and the unwaged and organisation rates remain unchanged.

Conference/Annual General Meeting 1997

The meeting agreed that the 1997 Conference and Annual General Meeting would be held at Stanford Hall during the weekend September 20/21, 1997.

Appreciation

Len Burch was thanked for his successful year as Chairman and the way he had conducted the Weekend Conference and Annual General Meeting. The Secretary was also thanked for the hard work undertaken in organising the Annual Conference and his efforts during a very busy and eventful year for the Society.

September 1996

John Butler: Secretary