

# The shaping of credit union development: the identification of a typology of factors that have contributed towards credit union growth in the United States of America, Republic of Ireland and Great Britain

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## Summary

*A credit union is a financial co-operative that is owned and controlled by its members for their benefit and the local community. The origins of the movement can be traced back to Rochdale in Great Britain, from where it spread to Central Europe, the North American Continent and the rest of the World. The Rochdale Society of Equitable Pioneers served as a precedent and inspiration to many co-operative societies around the world.*

*There are a number of factors that have assisted the development of credit unions – economic hardship, the co-operative movement, the influence of several pioneers and a credit union legislative framework. It is these factors that this paper concentrates upon, in three differing credit union jurisdictions – Great Britain, the Republic of Ireland and the United States of America.*

## Introduction

A credit union is a financial co-operative that is owned and controlled by its members for the benefit of the local community. There are a number of factors that have contributed towards the development of credit unions – economic hardship, the co-operative movement, the influence of several credit union pioneers and a credit union legislative framework. This article offers a detailed consideration of the major factors that have propelled particular credit union industries, discusses the historical development of the credit union movement and identifies a typology of factors that have contributed towards the evolution of credit unions.

## Stages of development

The following analysis examines the development of credit unions in an international context. According to MacPherson (1999) their development can be divided into three stages. During their *formative* stage, a credit union is heavily reliant upon the support of its members, other institutions, government departments and funding agencies (ibid). Credit unions are rarely in a position to be self-sufficient during this stage and they need to utilise networks provided by such institutions as churches, co-operatives, trade unions and professional

associations (MacPherson, 1999; xv). Throughout this stage, credit unions have a limited set of needs, such as education and training, promotion, lobbying of government to secure appropriate legislation, the provision of insurance services and the procurement of inexpensive supplies, the need for which can be met by central organisations (ibid; xvi).

The second stage in the development of credit unions is the *national stage* (MacPherson, 1999). During this stage, regional and national representative bodies are required to undertake more activities that relate to the expansion of the movement. Therefore, it is unsurprising that the transition from stage one to two brings about periods of intense debate over such issues as funding, control, the role of volunteers and the different type and size of credit unions (Sibbald et al; 2002). On occasion, it can lead to serious fragmentation with the creation of rival groups of credit unions and credit unionists (Donnelly and Haggett, 1997). However, this stage of development is normally creative and it is at this time that credit unions reach out to larger constituencies, provide more services to their members, and begin to have a significant impact on the general economy.

The third and final stage is the *International Stage*. At this stage the growth of credit unions incorporates a number of important concepts such as globalisation and internationalisation. MacPherson (1999; xv) argues that the concept

of globalisation “will surely reshape the credit union world”.

In Sibbald's et al (2002; 402) three stages of development of credit unions, the *nascent stage* is very similar to that identified by MacPherson (1999; xv). Here, credit unions are run by volunteers and receive financial assistance from local authorities and other organisations (Thomas and Balloch, 1993). The second stage is the *transition stage*. Credit unions have moved away from maintaining their core values to a more professional and economic outlook. Sibbald et al (2002; 402, 403) suggest that credit unions hire paid employees and have a professional management team. Finally, at the *maturity stage* credit unions are characterised by large asset and member size offering their members an expansive array of products and services (ibid; 404).

As well as identifying stages of development it is also important to identify factors that have influenced their historical development. The following section examines these to arrive at a typology of developmental factors.

## Typology of factors

By offering a classification of factors influencing credit union development the typology provides a useful device for analysing their development. The power of typology as a tool for research and classification and is recognised in a number of studies (Rich, 1992; 758). Levi (1997) stated that the applicability of typology to research issues in co-operative forms of organisation is also an important element of the research armoury. The benefits of a typology include, for instance, easier recognition of fundamental structure and relationships and the provision of a platform for theory development. Three factors have been identified as the main ones contributing towards the development of credit unions. These factors are: economic hardship and the emergence of the co-operative movement, the influence of pioneers and a flexible legislative framework.

## Economic hardship and the emergence of co-operatives

The first factor that contributed towards the development of credit unions in many jurisdictions was harsh economic conditions and the emergence of co-operatives.

## Great Britain

MacPherson (1999; 2) states that credit unions could be seen as having their origins in the 1840s, when the organised co-operative movement began to emerge. Co-operatives were established in the early part of the nineteenth century as a direct response to the conditions of the Industrial Revolution. Such societies were established to circumvent the harsh economic conditions, improve the standard of living and restore a sense of community. The Irish League of Credit Unions (1996) argued that co-operatives in Great Britain were an attempt “by craftsmen and small producers to improve their standard of life”.

He added that it was a turbulent decade for much of the world, a time when people in most countries suffered as a result of severe economic depression, social dislocation and political unrest (ibid). After the defeat of Napoleon in 1815, Great Britain was at the height of her power and prestige and the period following Waterloo saw mass industrialisation, the advance of the capital economy, a new social and political era and a significant increase in business growth (Lowe, 1989; 1). These events led to prosperity in certain parts of the country but also brought innumerable problems – poverty, discontent and violence. Stockey (2001) states that:

An unfortunate but unavoidable fact is that the early 1800s were a period of substantial upheaval for the British economy. The country was fighting a long series of wars that drained resources and disrupted trade. In addition there were several years of devastating crop failures in the 1800s.

The need for armaments during the Napoleonic War acted as a stimulus to the metal industry and resulted in the widespread adoption of coke-blast furnaces for producing iron. Mokyr stated that some iron works grew at an unprecedented rate (Mokyr, 2001). Justman and Gradstein (1999) state that Great Britain experienced dramatic changes in the size and distribution of income in the aftermath of the Industrial Revolution. They conclude that wage levels increased and after 1820, the living standards of the middle class rose. Stockey (2001) states that:

The Industrial Revolution marked the beginning of the modern economic era: the

faster growth and real wage increases, and dramatic shifts in the allocation of labour and composition of output across sectors begun during that period have continued ever since.

The main expansion took place after 1815, and this dramatic industrialisation and population expansion brought with it enormous problems of overcrowded towns, excessively long hours, child labour and dangerous working conditions.

There are a number of reasons why the Industrial Revolution caused widespread economic hardship in Great Britain (Fairbairn, 1994). Firstly, advances in technology in agriculture, factories and mines reduced the demand for labour and caused hardship in certain trades (Richards, 1973). Mokyr (2001) states that the Industrial Revolution represented the rise of the factory which resulted in a radical change in production and technology. Secondly, the end of the Napoleonic wars (1793-1815) brought a sharp fall in corn prices, causing bankruptcies among poor farmers (Lowe, 1989). Thirdly, there was a sudden industrial slump that caused widespread unemployment. Fourthly, the Government stopped buying armaments, exports fell by 30% by 1818 and over 500,000 people were unemployed. Lowe notes that these problems were exacerbated by the system of enclosures; the Speenhamland System and new machinery which put people out of work. Industrial conditions caused particular economic hardship. Some of the Government's solutions to the economic hardship made matters worse (ibid).

Lowe (1989) states that more serious than some of the economic factors were the obstacles that arose from the operation of the Poor Law, especially from the conditions of settlement. This system was unable to cope with the increasing number of poor people during periods of unemployment and low wages. The Poor Law Amendment Act 1834 amended the 1601 Poor Law and the amendments were ineffective despite reducing the poor rates. The Act was criticised by the working class and humanitarians. Its main problem was that it ignored the causes of poverty and unemployment. Stockey (2001) states that:

The Industrial Revolution is then modelled as having consisted of three events: a dramatic improvement in the technology for producing energy, a moderate improvement in the technology for producing

manufactured goods and a large increase of foreign trade.

A direct result of the harsh economic conditions was the emergence of the co-operative movement. Lowe (1989) notes that one of the main themes of the nineteenth century was the emergence of working-class movements like the chartists, trade unions and the co-operative movement to combat the effects of the Industrial Revolution.

Robert Owen, who influenced the creation of two famous co-operative experiments in Rochdale and New Lanark, principally led the co-operative movement (ABCUL, 2002; 3). The most prominent co-operative influenced by Robert Owen's ideas, the Rochdale Pioneers, opened their famous co-operative shop on Toad Lane in 1844 (Fairbairn, 1994). It was an important step in the social and political change that was taking place throughout Europe and in which the people of Rochdale can justifiably claim to be leaders. The owners of the Robert Owen New Lanark Mill agreed to invest its profits in such a way as to limit their returns and reinvest the capital so that the entire community benefited (Harrison, 1969). By 1848 the co-operative had 140 members and the Society's membership increased to 390 and by 1880 the national membership of consumer societies had reached over a half a million people and by the turn of the century 1.5 million.

The members of the Rochdale Society of Equitable Pioneers subscribed to shares and paid small amounts to raise sufficient funds in order to purchase goods below the market value and then resell them to the members at a saving (Fairbairn, 1994). The Equitable Society of Pioneers, as the Rochdale association was formally called, was primarily concerned with providing good-quality consumer goods at fair prices to its members. Moody and Fite (1971) argue that these co-operatives were the result of the "growing complexities of modern economic life for both farmers and workers".

Importantly, the Rochdale Society of Equitable Pioneers developed a number of principles that have assisted the development of credit unions (ibid). The principles were open membership, the democratic control of the organisation (Croteau, 1963), a limited interest on share capital and the return on member's interests being in proportion to the member's patronage (Moody and Fite, 1971; 1). The principles advocated by the Rochdale Society of Equitable Pioneers remain an important part

of the movement, and illustrate why credit unions are a unique financial co-operative (Birchall, 1997). The International Co-operative Alliance statement on co-operative identity states that all co-operatives are based on the following values – self help, self-responsibility, democracy, equality, equity and solidarity (ibid).

These principles can be directly related to the statutory objectives of credit unions in Great Britain, as stated in the Credit Unions Act 1979, and in the Republic of Ireland (Ireland) as defined in the Credit Union Act 1997 (Ryder, 2003; 51). These objectives are consistent with the international co-operative principles. The general co-operative philosophies are still central to the objectives of credit unions. It can, therefore, be argued that economic hardship in Great Britain resulted in the creation of a number of co-operative societies that influenced the development of the modern day credit union.

Despite the early development of co-operatives, credit unions emerged later in Great Britain when compared to Ireland and the US for a number of reasons. First, credit unions in Great Britain have been held back by a restrictive legal framework (Griffiths and Howells, 1991; Ryder, 2003; HM Treasury 1999a, 1999b; ABCUL, 1997; Lewis, 1982). Second, local authorities and the Government have used inappropriate development models which have led to the creation of small unsustainable credit unions (Jones, 1999; Jones, 2001; Davis and Brockie, 2001; McCarthur et al, 1993). Third, credit unions in Great Britain have become too reliant on state funding (Donnelly, 2000; Hayton, 2001). Fourth, credit unions in Great Britain are *immature* when compared to the Irish and US movements (HM Treasury, 1999b). Finally, credit unions are not represented by a single trade association, a factor which has assisted the development of credit union in both Ireland and the US (Donnelly, 2000; Ryder et al, 2002). Despite these factors however, credit union membership in Great Britain continues to grow, but not at the same rate as evident in Ireland and the US (Ferguson and McKillop, 1997; Sibbald et al, 2002).

## Germany

Black economic conditions were also a factor that contributed towards the establishment of the co-operative and credit union movement in

Germany. In 1846 and 1847, people in Germany faced similar economic difficulties to those experienced in Great Britain in 1844. The first credit unions were founded as a direct reaction to economic poverty of the underprivileged (Johnson, 1993). A crop failure and one of Germany's harshest winters caused the worst economic difficulties ever faced (ibid). This culminated in an economic depression, high unemployment and the closure of numerous businesses. The only source of credit available at the time was via moneylenders who charged extortionate rates of interest (Moody and Fite, 1971). MacPherson states that in 1846 a famine swept much of the German countryside and many peasants had little to eat other than small potatoes, chicory, broth or sauerkraut (MacPherson, 1999). In the following year, the economy improved but the need for credit became critical as farmers tried to achieve a semblance of economic security.

As a result of the harsh economic conditions, there was a peasant uprising in both urban and rural areas of the country (Schulze, 1998). The sheer force of the rebellion was enough to convince the aristocracy that a revolution was in the making for Germany. The uprising in 1848 was not simply due to the potato famine and the widespread starvation present in Germany at the time (ibid). While these were factors, the main grievance was that people's livelihood was adversely affected by the Industrial Revolution (Borchardt, 1972). The Industrial Revolution in Germany brought an era of technological development that threatened the long-term livelihood of the population. It has been argued that famines have been a part of life and artisans who have been able to make a living were finding it very difficult to compete with the large factories. It has also been argued that the Industrial Revolution was taking over Europe and the aristocracies were ready to benefit at the expense of the lower classes:

Close behind this came the highly developed readiness of the aristocracy to invest in manufacture, a far reaching system of trade, banking and credit ... which, together, made it possible for an extraordinary rise in production to occur within a few decades (Schulze, 1998).

In response to those problems, co-operatives of all kinds were formed, including 'bread

unions' that distributed flour to the hungry and sold bread to the poor at very low prices. It was within the specific context of that economic crisis, as well as the unrest associated with the 1848 revolutions, that the German co-operative banking movement took place (MacPherson, 1999; 9). This represented a lifeline to a large part of the population. It was assisted by several pioneers, who included Herman Schulze-Delitzsch (Schulze-Delitzsch), Friedrich Wilhelm Raiffeisen (Raiffeisen) and Victor Aime Huber (Huber).

### **The United States of America**

Just as economic hardship contributed to the development of co-operatives in Germany, so in the United States of America (US) the role of economic hardship cannot be overestimated. It can however be contrasted with developments in other countries. MacPherson (1999) states that the emergence of co-operatives in the US differs from their development in Europe because the movement was less reliant upon government assistance.

Moreover, when the early co-operatives in the US were founded at the start of the nineteenth century they were not a reaction to the Industrial Revolution and the resultant economic hardship. Initially, the co-operatives were influenced by Robert Owen. Harrison (1969) notes that "in the fall of 1824 ... Owen shifted the scene of his operations to the New World, and early in 1825 launched his first community at New Harmony, Indiana". In 1862 the first Rochdale-model co-operative was established in the US. The Union Cooperative Association No 1 of Philadelphia was organised in 1862 with bylaws obtained directly from Rochdale (*ibid*). Robert Owen also influenced the establishment of a number of co-operatives in the US - Indiana, Ohio, New York, Pennsylvania, Tennessee, and Ontario in Canada. Approximately ten "Owenite communities were founded in North America in the 1820s" but none of them lasted more than two or three years (Harrison, 1968; 325). Fairbairn (1994) disagrees with Harrison, noting that "the first Rochdale-model co-operative on the continent was in Stellarton, a mining town in Nova Scotia, where a store opened in 1861". Such co-operatives were created in industrial communities and the largest of these co-operatives was the British Canadian society in Sydney Mines (*ibid*).

As information regarding co-operative credit spread from Europe to North America, in 1864 several unions of German craftsman in New York City organised a city-wide organisation called 'Arbeiter-Bund' (Moody and Fite, 1971). While other organisations of this type concentrated upon shorter hours, higher wages, or political activity, this organisation comprised devoted followers of Schulze-Delitzsch. They sought to establish a bank, a hospital, home-building societies and producers of co-operatives all according to his principles of self-help. The ethos of Richard Owen and the Rochdale Society of Equitable Pioneers also influenced the Grange Farm Movement in the Mid-West, which resulted in the creation of thousands of farmer-owned stores (Fairbairn, 1994; 18).

Mattson (1999; 1021) states that credit unions arose in the US in the early part of the twentieth century to serve the financial needs of the working class, who were ignored by banks that only catered for corporations and successful individuals. As a result of this snub the loan demands of the blue-collar workers went unsatisfied and such people were forced to either go without a loan or turn to loan sharks. MacPherson (1999) states that banking history in the US was dominated by periodic outbursts from people unhappy with the traditional banking system. It is, therefore, unsurprising that credit unions began to meet this gap in the financial services sector.

The US in the 1920s enjoyed a period of economic prosperity. Novajovsky (2000; 221) states that, during this period, credit union funds accounted for only eleven million dollars in assets or 0.16% of total funds held by financial intermediaries. However, the period of economic prosperity ended in October 1929 with the Wall Street Crash. As a result, there was a dramatic increase in poverty, unemployment and homelessness. These factors, and the failure of many financial institutions, contributed towards a demand for credit unions (Bernstein, 1954). The Wall Street Crash plunged the country into the Great Depression. This turned out to be the worst economic slump ever in US history and one that spread to virtually the entire industrialised world (*ibid*).

The impact of the Great Depression upon the US economy was catastrophic. Halloran (1968) states that 25% of the nation's work force was unemployed and practically everyone felt

the pinch of economic deprivation. For the first time, many Americans were forced to question their vague philosophical belief that poverty was a self-imposed condition brought on by laziness and moral degeneracy. The Great Depression was a unique experience for America, which was faced for the first time with a critical situation of widespread, persistent poverty which affected not just relatively small groups but the average person in the street (ibid; 207).

The fledgling credit union movement grew during this trying economic period as people were forced to look for alternative forms of credit. As bank after bank closed people lost faith in the existing financial system and welcomed the credit union alternative. In fact, credit unions did so well during the Great Depression that the movement sought federal legislation allowing the formation of credit unions in any state in the country. An extensive grassroots campaign culminated in the passage of the Federal Credit Union Act 1934 (FCUA 1934).

The Great Depression turned out to be a boon rather than an impediment to the movement. Credit unions continued to grow throughout the Great Depression while many other financial service providers failed or turned away from consumers. Moody and Fite (1971; 127) state that hundreds of banks were unable to survive the depression and closed. In 1931 2,298 banks suspended operations and the following year the number was still high reaching a number of 1,456 (ibid).

A Princeton University study of the ability of different kinds of thrift plans to survive the adversity of the Great Depression found that 34.5% of all bank deposits had been lost, as had 35.9% of company investment funds, and 32% of investments in building and loan societies (MacPherson, 1999). In contrast, only 6.7% of investments in credit unions had been lost (Bergengren and Doig, 1942; 11). It is important to note that as a direct result of the suspension of banking operations and the loss of money, people lost faith in the banking industry. The credit union record of solvency was superior to that of banks. For example, in December 1931, 512 banks closed and at the same time some thirty credit unions had been organised. Johnson (1993) states that during the Great Depression the number of credit unions grew by 107%, when the number of banks fell by 50%. While the Depression was a period of great pain to many people, the credit

union movement provided relief from financial hardship. In fact, additional credit unions opened doors even at the heart of the Great Depression. Novajovsky (2000; 223) states that from 1931-1933, during the worst years of the Great Depression, credit unions continued to grow. Kroos and Blyn (1971; 193) support this view and state that by 1933, there were 2,000 credit unions, which held \$40 million in savings. Moody and Fite (1971) argue that the Great Depression helped the development of credit unions by stimulating the co-operative idea:

The depression put citizens in the mood to try different approaches to their credit problems. The credit union movement undoubtedly benefited from a widespread desire to depart from traditional practices and experiment with new systems.

Despite the general consensus that credit unions benefited from the Great Depression there were a number of states where their numbers dropped. For example, between 1929 and 1933 the number of credit unions in Massachusetts dropped by 5.7%, membership declined by 4% and their assets fell by 25% (ibid). Moody and Fite (1971) state that "considering the severity of the depression, this record was not bad". Overall however, during this period, people began to distrust banks. The population needed access to affordable credit and the Government seized the opportunity to promote the development of credit unions (MacPherson, 1999).

Clearly, then, the harsh economic conditions in all these jurisdictions contributed towards the development of the credit union movement. The response was the formation of a large number of co-operatives that were established by several pioneers of the credit union movement. Ward and McKillop (2003) state that the success of the co-operative movement was due to a number of factors, including the volatile economic and social climate at the time. Fairbairn (1994) states that the reaction to the harsh economic conditions at a local level was the establishment of temperance groups, building societies, political grouping and the co-operative movement. Moody and Fite (1971; 36) take the view that:

Co-operation of all types, therefore, can be looked upon as an attempt by ... craftsmen, and other small producers to improve their position in a nonfeudal, modern capitalistic society. They were also concerned with restoring the spirit of community.

Co-operation in Great Britain was a product of craftsmen and other small producers attempting to restore community spirit. The Industrial Revolution led to significant changes in communities because people moved from the countryside to the industrial cities seeking employment (ABCUL, 2002; 3). This was an important driving force behind the growth of the co-operative movement and it was an attempt to restore a "spirit of community both in towns and in the countryside" (ibid). This was also a factor that influence the growth of co-operatives in Germany and North America (Moody and Fite, 1971).

## **The influence of Pioneers and the development of the co-operative movement**

### **Great Britain**

In Great Britain, the Industrial Revolution and the subsequent economic hardship clearly provided the stimulus for Robert Owen to develop a series of co-operatives, the New Lanark Mill and to influence the Rochdale Society of Equitable Pioneers. Moody and Fite (1971; 1) describe them as "two notable and widely publicised co-operative experiments". Lowe (1989; 1) states that Robert Owen became one of the most remarkable industrialists and reformers of the nineteenth century, whilst Sibbald et al (2002; 408) states that much of the inspiration for co-operative ideals in the nineteenth century can be traced to the experiments of Robert Owen. The success of this co-operative led to the Rochdalian principles being exported internationally. As we have seen, by 1870, Germany, France, Italy, the Republic of Ireland, Denmark, Norway, Finland, Canada and the US all had co-operatives that were formed using the Rochdale principles as a guide (Fairbairn, 1994). The Rochdale co-operative thus became the inspiration and model for a movement that now includes nearly 700 million people around the world (ibid).

Interestingly, however, despite the influence of Robert Owen, Great Britain has lacked a modern day pioneer to assist the development of credit unions. Sibbald et al (2002; 84) states that:

It may be argued that the failure of the movement in Great Britain ... is the lack of

charismatic personalities. ... the movement is very much in need of a white knight to spearhead its development.

For Sibbald *et al*, then, one of the problems of credit union development in Great Britain is one of leadership. The first credit union was not established in Great Britain until 1964, and the *real* growth occurred as a result of the CUA 1979 and the policy adopted by the Government (Drakeford, 2002; McCarthur et al, 1993; Ryder, 2001).

### **The Republic of Ireland (Ireland)**

The co-operative movement and the influence of pioneers clearly did play a very important role in the development of credit unions in Ireland. McCarthy's (1994) work indicates that the first credit union in Ireland was established in Carrigaline, County Cork in 1813, but concludes that there is little information about this credit union. Quinn (1999) takes the view that the root of the credit union movement Ireland was in the wider context of the co-operative movement. Robert Owen visited Dublin in 1823 and his series of speeches influenced those who listened to his ideas about co-operation in what Quinn calls a "new moral world" (ibid). Following Owen's successful meeting at Dublin's Rotunda, the Hibernian Philanthropic Society was formed in order to disseminate the values advocated by Robert Owen (Quinn, 1999). John Scott Vandeleur, a County Clare Landlord followed on from the establishment of Ireland's first credit union in 1813 by founding Ireland's first formal co-operative at Ralahine, County Clare (ibid). What emerged was an advanced experiment in labour relations and worker participation. A proposal was put to the workers on the Ralahine Estate in 1831 and led to the establishment of a co-operative farm. The aims of the co-operative were fivefold: the acquisition of common capital, mutual assistance against poverty, the attainment of a higher quality of life, the mental and moral improvement of its members and the education of children within the co-operative. The experiment lasted from 1831-1833 and was highly successful (Quinn, 1999).

The co-operative sector in Ireland began to flourish some years later under the leadership of Sir Horace Plunkett, George Russell and Father Tom Finlay, who collectively established

the Irish Agricultural Co-operative Society to meet the needs of local farmers. Sir Horace Plunkett's ideals of "Better farming, Better business and Better living" were translated into practical initiatives at the start of the twentieth century (Leachy, 1983; 33-44). As a result of the work undertaken by Plunkett, Russell and Finlay, a number of agricultural credit societies were created and they became known as "village or agricultural banks" (Quinn, 1999). According to Quinn the first such society was established in Doneraile in 1894. The features of this society were five fold: its membership was confined to the local parish or village, loans were granted for a productive purpose, loan applications were scrutinised by its members, each member of the society would be held liable for its society's debts and its operation was based upon the trust and honesty of the members (*ibid*). These features were very similar to those used by the modern day credit union. For example, Irish credit unions are only allowed to offer loans provided they are for a "provident or productive purpose" (Credit Union Act 1997, section 35(2)). Membership is limited to a common bond and credit unions are reliant on the trust of their members (Ryder and Baker, 2003).

Despite their impact upon the development of credit unions in Ireland, these societies had a number of identifiable weaknesses that led to their demise (Quinn, 1997). These included insufficient deposits to meet the demand for loan applications, a reluctance to disclose an individual's business and their dependency upon state aid (*ibid*). Quinn (1999) concludes that, despite their failure, the credit societies nevertheless fulfilled the purpose of combating indebtedness amongst farmers. The influence of pioneers in the development of co-operatives and ultimately the credit union movement is illustrated by the fact that the societies created by Plunkett, Finlay and Russell were based upon the same principles advocated by the German Raiffeisen Societies. These were to become central to the modern day credit union. According to McCarthy, such principles included the pooling of the members' savings and granting loans from this pool at low rates of interest (McCarthy, 1994). In Ireland, a total of 76 of these banks were in existence by 1906, growing to 268 by 1908 (*ibid*).

During the First World War, Irish farmers enjoyed a period of prosperity and this ultimately led to a decrease in the number of

credit societies so that by the 1930s only 50 credit societies remained (McCarthy, 1994). These societies failed to live up to the expectations of their founders and despite their failure to expand following World War I, they did "provide a base for credit union ideas and salutary lessons in pitfalls to be avoided" (Quinn, 1999). The Irish Banking Commission declared that there was little probability that such societies would develop in Ireland (*ibid*).

Clearly though, as Quinn (1999; 21) states the pioneers of the Irish co-operative movement provided the inspiration for the Irish credit union movement. In the 1950s, educational lectures were organised in University College Cork by Professor Alfred O'Rahilly. Father Edward Coyne, the then President of the Irish Agricultural Co-operative Society, directed an evening Diploma course in Social and Economic Science at the University of Dublin that heavily influenced the development of credit unions in Ireland (Culloty, 1990). Seamus MacEoin, a civil servant who completed the Diploma at the University, was "profoundly affected" by the course. He established an economic study panel to debate contemporary social issues (Quinn, 1999).

The members of the panel presented papers to highlight issues that they felt were important. Seamus MacEoin spoke about the co-operative movement at an open meeting in December 1953. His paper stimulated great interest. Among the audience was Nora Herlihy who went on to become an important pioneer and leader within the credit union movement. As a result of this public meeting in Dublin, an initiative was taken to combat the difficulties caused by unemployment and emigration through worker co-operative development and low-cost credit (Quinn, 1999). By 1958, the first credit union was established at Donor Avenue, Dublin 8 and Dun Laoghaire, which was confined to members of Dun Laoghaire Grocery Co-operative (*ibid*; 19). Herlihy was influenced by the writings of a Monsignor Moses Coady, who had formulated a co-operative philosophy (Quinn, 1999; 19).

Her influence upon the development of credit unions was unprecedented. Herlihy was appointed a member of the Government's Committee on Co-operative Societies (*ibid*), which recommended that credit unions should have their own separate and distinctive legislative framework, since existing legislation was inappropriate. As a result Herlihy drafted



the Credit Union Bill, signed into law as the Credit Union Act 1966 (CUA 1966). Quinn (1999; 20) states that "Herlihy was justly proud of the efforts of herself and the other pioneers" and that this legislation was vital to the growth of the Irish credit union movement. Clearly, these pioneers played a key role in pushing for legislative change in the frameworks of credit unions, and ultimately their development.

## Germany

Three leaders were particularly important in shaping the co-operative and credit union movement in Germany. Huber, a physician, travelled extensively in France and England from the 1820s to the 1860s (Moody and Fite, 1971). He became an important, if somewhat iconoclastic, advocate of all kinds of co-operative endeavours in Germany (Tucker, 1922; 20). In 1861 Huber published *Lectures on the Solution of the Social Problem* in which he discussed credit unions. He published a series of tracts recommending co-operative banking, in which he argued that financial co-operatives, if extended to all types of people, would improve their living conditions. However, Huber only founded two such associations, and as a result the development of practical co-operatives was left to others (Moody and Fite, 1971; 3).

The second influential pioneer was Schulze-Delitzsch, who in 1850, formed his first co-operative society (MacPherson, 1999; 5). This society was founded to provide craftsman with co-operative insurance against death and sickness, after Schulze-Delitzsch discovered that there was a need for credit among craftsman and small shopkeepers (Moody and Fite, 1971). Each member of the society paid an entrance fee of \$2.50 and deposited their savings in the credit society to provide working capital: loans were then granted to members for a productive purpose (ibid). Borrowers had to join the association and contribute 'five cents a month' towards its capital. Membership was open to anyone who was willing to accept the requirements, a membership fee being charged to cover administrative costs (Moody and Fite, 1971). Schulze-Delitzsch stressed the democratic control of his people's banks. The principles they embodied have made a major contribution to the practice of modern day credit unions (Griffiths and Howells, 1991; 205). By 1859, there were 183 Schulze-Delitzsch credit

societies with 18,000 members.

Schulze-Delitzsch was a remarkable organiser in three respects. First, he was very effective in travelling throughout Germany encouraging the formation of local co-operative banks. Second, he was adept at creating an intricate infrastructure of regional and national banks. Third, he ardently pursued the passage of legislation for co-operative banking, a difficult struggle because of the opposition from other banking institutions and political foes. In 1867, he successfully introduced legislation on co-operative banking into the Prussian legislature. This essentially became the basis for the German law that was passed in 1871 (MacPherson, 1999). As with Herlihy in Ireland, Schulze-Delitzsch assisted the development of co-operative societies in two ways, first by encouraging their development and second by pursuing the enactment of legislation for them (Griffiths and Howells, 1991; 205). When he died in 1900, there were 4,000 such societies with 446,000 members in Germany.

The influence of Schulze-Delitzsch on the development of the credit union movement cannot be underestimated. Henry W Wolff states that Schulze-Delitzsch was a 'born economic missionary' (Moody and Fite, 1971; 7). Before his death, a rival type of co-operative appeared in Germany, set up by Raiffeisen. Schulze-Delitzsch saw this as a competitor to his own type of co-operative and believed that it was less secure than his own societies and feared that they would fail. In fact they did not.

As the idea of co-operatives spread from the cities into the countryside, it began to be seen not just as a source of credit but: a means to fight poverty and usury, and thereby to make permanent improvements to people's lives (MacPherson, 1999; 7). Raiffeisen was instrumental in the expansion of the credit union idea to its full potential for he came to see co-operative credit as an answer to the pressing economic difficulties in Germany. He organised his first credit union in 1849 when he was mayor of Flammersfeld. His first co-operative venture was very similar to that of Schulze-Delitzsch. The suffering caused by the famine of 1846 and 1847 profoundly moved Raiffeisen, but whereas Schulze-Delitzsch concentrated upon urban areas, Raiffeisen concentrated upon rural areas (Moody and Fite, 1971). His second credit union, the Heddesdorfer Welfare Organisation, revealed his interest in Christian charity and welfare work since it promoted the care and

education of destitute children. Two more credit unions were established in 1862 with the Heddesdorfer Society following in 1868, but it was not until 1874 that they became known outside their immediate localities.

Raiffeisen's credit unions grew slowly; rapid expansion did not begin until 1880. At the time of his death in 1888 there were 423 of his societies in Germany. Ward and McKillop (2003) take the view that the growth of these societies:

... could be the additional financial exclusion that exists in rural areas, particularly at that time. Rural communities would have more of a need of co-operative financial institutions, as banking facilities would have been either unavailable, or too far way to make their mark.

Raiffeisen aimed to ease the credit problems of poverty-stricken and indebted German farmers. His movement actually grew into Germany's biggest co-operative movement (Watkins, 1986; 160). Moody and Fite (1971; 13) concluded that "the Raiffeisen co-operatives enjoyed a much larger growth than the Schulze-Delitzch organisations. In 1913 there were 25,576 rural co-operatives".

## Italy

Schulze-Delitzch and Raiffeisen also influenced the development of co-operatives in Italy. Their efforts served both as an inspiration and as a precedent to other pioneers. In 1864, Luigi Luzzatti (Luzzatti), a 23-year old Italian scholar who visited Germany to study co-operation was 'greatly influenced' by Schulze-Delitzch and Raiffeisen. Upon returning to Italy, he wrote a book on the subject, and then continued to expound his ideas as a professor of political economy at the University of Padua. Luzzatti established his first co-operative bank in Milan, later known as the People's Bank of Milan.

Luzzatti's people's banks bore a resemblance to Schulze-Delitzch's ideas, but there were some differences. Both Schulze-Delitzch and Raiffeisen had insisted that unlimited liability was a basic principle for their co-operatives. However, Luzzatti decided that the Italians would never accept unlimited liability and he also rejected the Schulze-Delitzch principle of high-priced shares to provide working capital. He decided that officers of his

banks should serve without compensation. By 1909, the People's Bank of Milan was one of the largest banking institutions in Italy, with 70 unpaid staff and 100 salaried clerks. It numbered 25,000 members, had capital of nearly \$2m and savings of over \$32m. At the time, it served as a model for numerous other banks in Italy (MacPherson, 1999; 6).

A counterpart of Luzzatti's in Italy was Leone Wollemborg, who emphasised the establishment of co-operative banks for farmers. Such societies were very successful in Italy, and by 1913 there were 2,000 rural banks in Italy. MacPherson (1999; 9) highlights the importance of Luzzatti and Wollemborg.

The systems developed by Luzzatti and Wollemborg became well known in other countries, as well as in North America and would play an important role in defining the nature of credit unions when they emerged in the US.

## The United States of America

As in Europe, the development of credit unions in North America was also assisted by the invaluable work of several pioneers. Alphonse Desjardins (Desjardins) was born in November 1854 in the town of Levis in the province of Quebec in Canada. After obtaining a college degree in 1870, he embarked on a newspaper career as a member of the editorial staff of the 'Echo' of Levis. He became interested in the problem of usury as a result of the frequent mention of this problem in Parliament, to which the Echo had assigned him as a reporter. In 1897, the Canadian Parliament debated a Bill to outlaw usury. Desjardins was horrified to hear of a case where an individual had been charged 1,200% interest on a small loan and this spurred him to action the remainder of his life attempting to alleviate poverty. He was enthused by the writings of Henry W Wolff and Luzzatti, and promoted the idea of co-operative banks in his own town.

In December 1900, Desjardins called a meeting of the townspeople of Levi to outline a plan for a 'caisse populaire' or people's bank. Of the 128 people who attended the meeting, 80 signed up as members and 'within a month contributed \$26.40'. He called his credit union 'La Caisse Populaire De Levis'. This started the Mouvement de Caisses Populaires Desjardins in Quebec, an organisation modelled upon both the Schulze-Delitzch and Raiffeisen credit co-operatives. However, this credit union

adopted the Italian system in respect to the limited liability of members. One of its primary goals was the encouragement of thrift among the society's members. The society grew and accumulated \$80,000 in assets and granted 2,900 loans. Before his death in 1920, Desjardins had organised 175 such societies in Quebec, playing a vital role in the beginnings of the genuine co-operative banking movement in Canada.

In 1909, Desjardins also founded the first credit union in the US, in Manchester, New Hampshire. His co-operative banks were not considered regular financial institutions, but were an expression of high social ideals. By 1907 there were three. This grew to eleven by 1908 fifteen by 1909, and by 1914, there were 150 such organisations in the US. Thus Desjardins was also the founder of the movement in the US.

Another pioneer who influenced the development of credit unions in the US was Pierre Jay. Jay, the Commissioner of Banks in Massachusetts, became worried by the financial problems faced by small entrepreneurs. Like Desjardins before him, Jay was concerned about the activities of pawnbrokers and moneylenders and concluded that co-operative banking was a practical solution for credit problems. Pierre Jay undertook a detailed study of unauthorised banking practices in Massachusetts. He discovered that there were six associations which provided their members with the ability both to save and to obtain loans. This discovery led Jay to sponsor a legal project to authorise the organisation of credit unions, Desjardins was invited to participate in the preparation of the legislation (Moody and Fite, 1971). As a result of this work, the Massachusetts Credit Union Act became law on the April 15 1909 (Clark, 1943; 241). The legislation defined a credit union as a co-operative association formed for the purpose of promoting thrift among members; seven people were required to apply for a charter and each paid a small entrance fee (MacPherson, 1999). Again, the role of pioneers in pushing for a distinctive legal framework was vital, as in Ireland and Germany.

Another important figurehead, Bergengren (1936) took the view that it was essential to have legislation to make it possible to organise and develop credit unions everywhere. Burger and Dacin (1991) state that as a direct result of the Massachusetts law, by 1933 thirty-eight states

had enacted similar laws that permitted the establishment of credit unions, thus illustrating the significance of the Massachusetts Credit Union Act. Bergengren believed that for continued expansion of credit unions it was necessary to have a federal credit union law. Furthermore, he felt that such a law was necessary in order to facilitate the organisation and growth of credit unions in states where legislation had not been passed, to ensure the protection of credit unions against the possible repeal of state laws, and to bring some kind of general order to the fragmented state laws under which credit unions operated (Bergengren, 1936).

What becomes clear from the early and later development of credit unions in Germany, Ireland and the US is the importance attached by the early pioneers to a suitable legislative framework for credit unions. Interestingly, however, this aspect of the credit union environment seems to have been largely ignored by analysts of the movement. This gap is all the more significant given the vital role played by a flexible legislative framework in the US, Germany and Ireland. It is to this that we now turn.

## **The Importance of Credit Union Legislation**

Clearly, one of the most important factors that has contributed towards the development of credit unions is a flexible credit union legislative framework. In 2002, the World Council of Credit Unions (WOCCU, 2002; 8) highlighted the importance of such a legislative framework:

Credit unions have been important contributors to economic and social development for over 150 years in all regions of the world. Credit unions are now significant participants in the national financial markets of many ... economies. In many jurisdictions, however, legislation has not kept pace with the development of credit unions.

Legislative deficiencies jeopardise the safety and soundness of credit unions by restricting their ability to meet their members needs. Jurisdictions lacking an adequate statutory framework have hampered the development of credit unions (ibid). WOCCU (2002; 8) states that:

Credit unions lacking adequate legislation often find themselves limited in mobilising savings and making loans to lower - and middle - income groups they generally serve. Also they are unable to participate fully in national financial markets, where their services could contribute to greater economic efficiency and expanded development opportunities for current and potential members.

The creation of enabling legislation also seen as critical to establishing sound, sustainable credit unions and that it is the ultimate objective of the credit union movement in any jurisdiction to pursue the enactment of legislation specifically for credit unions (*ibid*; 1).

### **The United States of America**

In the US, credit unions are legislated under both state and federal laws (Reichert and Rubens, 1991; 15). The importance of state legislation to the development of the legislative framework cannot be underestimated because such laws served as a precedent for the FCUA 1934.

Following the creation of the first credit union in the US in 1909 (*ibid*), Massachusetts was the first state to enact legislation in 1915. By 1931, some 16 states did not have legislation authorising the creation of credit unions. During the next two years, laws were enacted in six important states including the District of Columbia (Moody and Fite, 1971). Congress believed that following the Great Depression the nation's economic recovery hinged on expanding access to credit and restoring the eroding purchasing powers of the workforce (Masset, 1999; 387). Hicks (1999; 1203) adds that, "Congress chose a national credit union system as a vehicle for economic recovery because of its potential for rapid development and the success of existing credit unions". Croteau (1947; 12) says that the FCUA 1934 influenced the growth of credit unions, and highlighted the importance of a legal framework in the US.

The aim of the FCUA 1934 was to establish a Federal Credit Union System, to make more available to people of small means credit for provident purposes through a national system of co-operative credit (Burger and Dacin, 1991; 12). The FCUA has been described as the greatest single step forward in the history of

the credit union movement and provided a strong push for the industry (Moody and Fite, 1971; 166). During the three years after the Act, membership and the number of credit unions more than doubled (Johnson, 1993), and by 1939 there were approximately 4,000 federal credit unions.

### **The Republic of Ireland**

A flexible and appropriate legislative framework is a factor that has assisted the development of the credit union movement in the Ireland (Sibbald *et al*, 2002). Until 1966, credit unions in Ireland were regulated under the Industrial and Provident Societies Acts 1893-1913 (Griffiths and Howells, 1991). Donnelly stated that this legislation was "too general to adequately deal with credit unions" and the Government sought to introduce specific credit union legislation (Donnelly, 2000).

A flexible and appropriate legislative framework came in the 1960s. The CUA 1966 was a landmark event in the development of the credit union movement in Ireland. Quinn (1999; 22) states that "this legislative reform was vital to the growth of the Irish credit union movement". He adds "the Act was a landmark for the wider co-operative movement because of the statutory recognition of co-op concepts including the mutuality of members in the ownership and organisation of their societies" (*ibid*; 23). Donnelly (2000) also concludes that the CUA 1966 had positive impact upon the development of the credit union movement in Ireland and that it resulted in the steady growth of the movement. All writers thus concur that a flexible legislative framework has assisted the development of credit unions in Ireland.

The 1966 legislation was amended by the CUA 1997. Sibbald *et al* (2002) point out that "a clear indicator of the advance of credit unions in Ireland, at least in legislative terms, can be witnessed with respect to the Credit Union Act 1997".

### **Great Britain**

In Great Britain, credit unions were initially registered and regulated by the Companies Act 1948 (CA 1948) and the Industrial and Provident Societies Act 1965 (IPSA 1965). These statutory provisions were inappropriate for the development of credit unions, which needed their own legislative framework

(Griffiths and Howells, 1991). The Registry of Friendly Societies took the view that the CA 1948 and IPSA 1965 did not provide an entirely suitable statutory framework in which to embody the operation of credit unions. Furthermore, neither piece of legislation provided any kind of prudential or supervisory requirements. In 1979, the Labour Government decided to proceed with the creation of an appropriate statutory framework (Registry of Friendly Societies, 1996; 3).

The Credit Union Bill was introduced to the House of Commons on January 26 1979 and received Royal Assent on April 4, 1979. At the time of Royal Assent, a total of ten credit unions had registered under the CA 1948 and four had registered under the IPSA 1965 (*ibid*). McKillop *et al* (2002; 1565) state that as a result of the CUA 1979, the movement gained 'significant positive impetus'. After the introduction of the CUA 1979, there was a significant increase in the number of credit unions, and by 1982, an additional 79 credit unions had registered. This is a view supported by Hickson and McKillop (1996; 134) who stated that "it wasn't until the passing of the 1979 Credit Unions Act that the institution spread rapidly".

## Conclusion

A common factor in the development of credit unions was harsh economic conditions, which played an influential role in the original development of credit unions in a number of jurisdictions. In Britain, and Germany economic hardship was an equally important factor in the

development of credit unions when their harshest winter led to wide scale unemployment and poor living conditions. Within the US, the economic hardship combined with the reluctance of banks to provide loans played a very important role in the development of credit unions. The development of credit unions was also assisted by the Wall Street Crash and the subsequent Great Depression, which culminated in the virtual collapse of the commercial banking sector in the US. The Great Depression provided credit unions with an ideal opportunity to exploit the fact that, for the first time, many Americans experienced real poverty. Credit unions were the only financial institution in the US to increase in numbers and membership. As a direct result of this growth, Congress saw credit unions as an ideal tool to boost the worsening US economy. The development of the movement was galvanised by a federal credit union law.

This typology has also identified the importance of the second and third factors – the co-operative movement and pioneers. The co-operative movement was a direct response to harsh economic conditions. The co-operative model developed by Robert Owen influenced other pioneers in Central Europe and the North American Continent. Both in the US and Ireland pioneers assisted the development of credit unions and played a prominent role in the development of an appropriate and flexible statutory framework. These factors assisted, and contributed, towards the development of credit unions.

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