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BOOK REVIEWS

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Editorial

In this issue of the journal it is our sad duty to pay tribute to the late Dr Yair Levi. It was only a year or two back that, overdue but well deserved recognition was accorded Yair by the ICA Co-operative Research Community at one of its international conferences. The New Harmony Press is very proud of its publication of papers selected by Yair Levi under the theme of co-operative responses to globalization. This issue of the journal carries an advertisement with the full details of the book. The papers are selected from those published over the many years of Yair's distinguished editorship of the well respected *Journal of Rural Co-operation*. Yair added an overview forward and conclusions and produced a comprehensive key word and an author index. On behalf of all our readers and contributors we salute Yair's contribution to co-operative research and publication and offer our sincere condolences to his family.

Our special guest paper, *On Surpluses, Profits and Net Incomes in Co-operatives* comes from Greece by *Constantine L. Papageorgiou and Olympia Klimi-Kaminari*, is a seminal contribution to a very contemporary debate about appropriate approaches to taxation of co-operative surpluses. The authors make a robust academic case against co-operative surpluses being treated in the same way as corporate capital based business profits. On the same topic we also carry an interesting practitioner perspective from India by *Veena Nabar, Co-operatives and Taxation Reform in India*, who currently has an important role facilitating the new Indian governmental committee exploring co-operative reform and restructuring.

Our other refereed papers are both from Finland. *Routes to Employee Commitment in Worker Co-operatives* by *Terhi Tuominen and Pia Heilmann* provides a scholarly review of the literature on employee commitment in the context of worker co-operation and adds new insights from the authors' own research including what the authors claim is a new conceptual framework based on group dynamics. They go on to isolate those features of worker co-operatives that may particularly facilitate this process. In the paper *Co-operatives – Flexible Form of Self-Employment in Competence Based Business* by *Eliisa Troberg* we get an interesting paper looking at a new area of business development which the author claims is particularly suited to the co-operative business model.

We are delighted to include a very important empirical case study from Israel. *Raffi Goldman's* case study *Change and Continuity in the Israeli Co-operative* examines innovation and entrepreneurship in the context of growth from small agricultural kibbutz to a multinational business with all the trials and difficulties of management and organizational development in this context candidly presented. It is very much the stuff for which this journal was intended. The requirement for developing professional management and scale in order to maximize business potential and service to communities is clear. In this case the business is delivering technological innovations to improve the productivity of the small farmer. In the process of success and growth serious dilemmas and challenges are presented that lead if we are not vigilant to demutualisation. The editor repeats here his oft-stated claim that the problems of managing big co-operatives co-operatively remains the challenge for the modern movement.

We also carry two more lively opinions with an Indian theme, one by an experienced executive manager *M. L. Khurana, Co-operative Housing Movement: creating safer cities and vibrant communities*. This paper explores the challenges of growing urbanisation and the contribution housing co-operatives can make both to improving the urban context for the poor but also in encouraging people to stay in their rural areas. The other opinion again goes to the very heart of our journal's *raison d'être* where *L.D. Abuja* in his paper *Challenges of Leadership and Professional Development in Indian Co-operatives* takes a controversial and candid look at the state of leadership in the Indian Co-operative Movement.

We add a new feature, Executive Reports, which provides brief notes on contemporary happenings in the co-operative movement around the world. This issue we welcome back from India *Sanjay Verma* with *Notes on developments in the Indian Co-operative Movement* and from Africa, *Owen N. Koimburi Njenga* has penned *Notes on developments in the Kenyan Co-operative Movement*. Also from Africa this time from Nigeria we have a research report from by *Prof Remy Adeyemo* entitled *Consumer Co-operatives in Nigeria: a study in consumer perceptions* with a constructive commentary by *Prof Suleman Chambo* from Tanzania.

A further new development in terms of the journal's content is the inclusion of Postgraduate Research Discussion Notes led by a preliminary orientation paper from a new PhD student *Wanna Prayukvong* from Thailand. Not that this in itself is new as our first issue included such a paper (also from Thailand) but what is new in the case of the paper *A Buddhist Economics Approach to Business Management* is that following the seminar discussion it was thought to be a good idea to include responses, one Islamic and one Christian to *Wanna's* paper by some of the participants to the seminar. I am grateful for a clear exposition of the Islamic perspective from *Mubideen Adesokan* and *Ibrahim Umar*.

I regret however to have to report that I have had no response from the UK Co-operatives Group to the last issue's Editorial comments on the sale of *Shoefayre* to the private sector.

It is with deep regret that we announce the very recent death of *Savvas Droussiotis*, a key figure in the development of the co-operative movement in Cyprus, whose influence and reputation went far beyond the island community he served all his life. He was responsible for the publication of *AKAMAS* a magazine which is currently distributed in 12 countries. Mr. *Savvas Philippou Droussiotis* was born on the 21st of February, 1933 at *Droushia*, Cyprus. He graduated from the Economic Lyceum of *Nicosia* in 1954. In 1970 he gained a diploma in journalism by correspondence and in 1973 a diploma in Business Administration from the College of Arts and Science. He will be best remembered as the founder and manager of the Co-operative Bank of *Ayios Dhometios* which he led for 42 years. *Savvas* was also an energetic president of the Co-operative Secretaries and Managers Association of Cyprus.

I first met *Savvas* when he invited me and three other academics to address an international seminar organised by the Co-operative Secretaries and Managers Association. He graciously translated and published all four papers to ensure the widest possible circulation of our ideas amongst his fellow Greek Cypriots.

Savvas contributed to a variety of other community associations, committees and councils. He also founded an extraordinary community development project in his home village of *Droushia*. The *Droushia Heights Hotel*, built from scratch, became a centre for establishing local cultural activities and providing local

employment and an inflow of foreign exchange benefiting the small family businesses operating in and around the village. The hotel focused on a customer segment concerned with local habitat, such as naturalists, and with local Greek culture. In many ways his ideas were ahead of the times and he can be seen as one of the early pioneers of eco-tourism. He raised the money in a typical communitarian way by asking for donations towards the capitalisation of the programme from families and those descendants of villagers now dispersed around the old and new worlds.

Savvas was a member of the British Institute of Management and he was honoured many times from different Associations. After his retirement he continued to write and publish books on Greek culture.

Mr *Savvas Droussiotis* was married and leaves a widow *Mrs Anthi Droussioutou*, and a daughter and grand daughter to whom on behalf of our readers we offer our sincere condolences.

Finally my thanks to *George Alexopoulos*, *Robby Tulus* and *John Donaldson* for assistance with production of the Journal and my sincere thanks to all the contributors from ten countries for their ideas, opinions, and findings.

Peter Davis
September 2008

Mission of the Journal

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

On Surpluses, Profits and Net Incomes in Co-operatives

“Wisdom begins where the meaning of the terms used are clearly defined” (Antisthenes)

Constantine L. Papageorgiou and Olympia Klimi – Kaminari,

Abstract

The terms “surpluses”, “profits” and “net incomes” are used by students and researchers in the area of social economy and particularly in relation to co-operatives. However, it seems that not all users of these terms understand the same things to be expressed by these terms. Yet, society and state authorities and legislators should become familiar with the content of these terms as often they are called to take decisions on issues of social economy. A clarification of the meaning of these terms would, on the one hand, facilitate the communication and mutual understanding of the students and researchers of the co-operative phenomenon and, on the other, probably more importantly, would guide policy makers to take appropriate measures especially in the area of corporate taxation of co-operatives.

This paper argues that:

- a) the terms “surpluses” and “profits” are distinctly different from each other,
- b) the term “net income” (used principally in U.S.A. literature) includes both surpluses and profits,
- c) surpluses should be, by definition, exempted from corporate taxation but profits (if any) should not,
- d) co-operatives are not profit-making enterprises,
- e) co-operatives constitute a most important component of the social economy, and
- f) there is no difference of essence between co-operatives and mutuals with reference to surpluses.

Key Words

Co-operatives, Corporate Taxation, Net Income, Not for Profits, Profits, Surpluses

Introduction

Although co-operatives are not a new phenomenon in the economic world and although they play a quite important economic and social role, their nature and amalgam of economic and social characteristics confuses those who see the world in black and white.

In drafting the Treaty of Rome for the establishment of the European Economic Community (in 1957), it had to be decided whether co-operative societies are “profit-making” or “non-profit-making”. Article 44 (now 48) of the Treaty¹ stated that:

“‘Companies or firms’ means companies or firms constituted under civil or commercial law, including co-operative societies, and other legal persons governed by public or private law, save for those which are non-profit-making”.

The above definition allows for two readings:

- a) That co-operatives are the same as conventional companies, i.e. profit-making bodies, or
- b) That some co-operatives are the same as conventional companies, i.e. profit-making companies, whilst some others may be non-profit-making bodies.

The first interpretation has been adopted by the prevalent definition of the Non-profit Sector in the U.S.A.. This has led to the exclusion of co-operatives from the Non-profit Sector. The O.E.C.D. publication on the non-profit sector has also adopted this approach². The bulk of work that has been done by Johns Hopkins University on the non-profit sector³ has proliferated the adoption of its definitions. The second interpretation has been adopted by the Canadian Co-operative Association, which claims that co-operatives may be distinguished in “for profit” and “not-for-profit” ones depending on whether they return surpluses to members or not⁴.

To add to the confusion, despite the classification of co-operatives (or part of them) by the Treaty of Rome in the profit-making enterprises, the Commission of the European Union places the co-operatives in the same group with mutuals, associations and foundations. Also, other organs of the E.U. consider co-operatives as a principal constituent of their definition of “Social Economy” or the Third Sector⁵. In general it can be said that no consensus has been found yet in the E.U.

As an alternative term to the non-profit making enterprise with reference to co-operatives, it has been proposed the term ‘not-for-profit’, defined as the organization different from the ‘for-profit’ ones (i.e. the

investor owned firms) by stressing that co-operatives do not distribute profits to shareholders (i.e. dividends on capital). In other cases it has been suggested to replace the term 'non-profit making' by the term 'non-distribution of profits', a concept significantly different.

In other cases, again, the "non-distribution" of profits is regarded as equivalent to the non-distribution of surpluses. In this case "profits" and "surpluses" are used interchangeably.

The authors of this paper are convinced that in order to clarify the situation, it is necessary to start from the definition of the terms used. This will be attempted in what follows, with particular reference to co-operatives. This may help to bridge the conceptual difference between the "old" and the "new" world (EU and USA), although the European Union itself needs to sit down and reconcile between the definition of Article 48 of the Treaty and the inclusion of co-operatives in its variants of definitions of Social Economy.

How "profits", "surpluses" and "net income" are currently defined?

Both legislators and scholars on co-operatives use in a variety of ways, and often vaguely, the terms "profits", "surpluses" and "net income". Here are some examples of the variety of uses:

- "The **profit** or loss of a financial year resulting for the members from the adoption of the annual accounts shall be distributed among the members ... in proportion to their credit balance established at the end of the previous financial year."⁶
- The **surpluses**, if any, remaining after making provision for payment of limited return (to capital) and reserves ... may be distributed as patronage bonus amongst the members in proportion to their participation in the business of the Producer Company ...⁴⁷
- "**Surplus**' in relation to the co-operative means the excess of income over expenditure after making proper allowance for taxation expense, depreciation in value of the property of the co-operative and for future contingencies"⁸
- "In a co-operative business, any **surplus** at the end of the fiscal year is allocated to members' accounts as a patronage refund ... in proportion to total members' use of the co-operative ..."⁹
- "The net **profits** of the co-operative are directed to the formation of reserves and to distribution among the members"¹⁰
- "From the gross receipts of the co-operative are subtracted all kinds of expenditure, losses, depreciation and interest (if any) on obligatory and voluntary shares. The remaining amount consists of surpluses and profits. **Surpluses** are the amounts deriving from the transactions between the co-operative and its members. Any excess is deemed to derive from transactions of the co-operative with third parties and constitutes **profits**"¹¹
- "The **net surplus** shall not be construed as profit but as excess of payment made by the members for the loans borrowed or the goods and services bought by them from the co-operative and which shall be deemed to have been returned to them if the same is distributed"¹²
- "**Surpluses** are any amounts remaining after securing in a general reserve, the capital needed to finance the expansion of the business"¹³
- "A **surplus** arises when the co-operative is able to retain some of the proceeds from sales of members' produce or from members' purchases from the co-operative"¹⁴
- "At the end of each year, after paying all expenses (e.g. interest payment to savers, administrative costs, salaries for hired staff and contributions to the co-operative reserve fund), the co-operative will sometimes have **surplus** or extra income. This surplus income is not profit but is refunded equally to the members who paid interest on loans. The co-operative distributes this interest refund according to how much interest each borrower paid. This helps to reduce the cost of loans. The surplus can also be used to increase the interest paid to savers"¹⁵
- "The co-operatives' **net profit, that is its surplus**, is shared out thus: Not less than 10 per cent has to be contributed to finance social services in the community such as education, not less than 20 per cent to the coop's collective reserve funds and up to 70 per cent may be credited to members capital accounts"¹⁶
- "**Surplus** is the difference between income and expenses (for profit and non-profit alike)"¹⁷
- Patronage allocation in the distribution of **net income** to members doing business with the co-operatives based upon the amount of the business"¹⁸
- Co-operative **net margins** may be distributed as cash patronage refunds, non-cash patronage refunds, dividends on capital stock and unallocated equity"¹⁹

- The **surplus** is exactly the difference between the total income of the co-operative and its total expenditure²⁰
- “**Surplus**” of co-operative for any financial year of the co-operative means the amount that remains after deducting from the operating revenue charges to members and patrons and other revenue in that financial year²¹
- Most States follow Federal rules in taxing co-operative net income ...²²

The preceding small collection shows that despite the standardization of the co-operative Principles (ICA), the terms used and the understanding of the terms that have been used differs around the globe. Although it seems that there is a general consensus regarding the way of allocation of surplus, following the third co-operative principle, the way of defining what is surplus (or profit or net income) in co-operatives requires some further specification. In some cases it is clearly stated that in co-operatives surpluses are not profits but in others the two words are attributed the same meaning.

A proposal to define “surplus” as distinct from “profit”

In commercial businesses, profit is the money left after all expenses are paid. It is the compensation of the entrepreneur for his management effort and his risk-taking and also the remuneration for the use of capital.

The entrepreneur in his everyday business enters into contracts, under specific terms, with owners of the means of production (principally labour and capital) and with his customers (regarding prices of end products). Depending upon his efficiency, and ability in bargaining, he (normally) manages to establish a difference between the overall cost of production of his goods or services and the prices he charges for his products or services. The entrepreneur’s permanent ambition and measure of success is to maximize this difference, which is the outcome of his labour and the capital he has under his command. If specific remuneration is attributed to managerial service and to capital use, the excess is profit.

If the manager himself is the owner of the capital used, any profit is his and he can choose the way of presenting it, either by giving his managerial service a specific price and the remaining as compensation to capital or by giving a specific remuneration to capital (e.g. bank rate) and considering the excess as compensation to his managerial work. For the tax authorities, the first alternative is acceptable.

If the manager is an employee of the capital owners, the excess obtained after payment of the managerial service belongs to the capital owners. Normally, the manager aims at maximizing the compensation to capital and expects that this will reflect onto his income, either in the form of higher salary or bonus for his achievement.

In the case of co-operatives, things are different. Firstly, capital, either supplied by members or borrowed, receives limited and, at any rate, specified compensation. Secondly, the fundamental characteristic of co-operatives is that owners and users of the services of the joint enterprise are the same persons. The co-operative is governed by a group of the members-users of its services. The same persons (members-users) are taking any risks involved and also the members are involved in the activity of the co-operative as suppliers or as customers or both. Let us consider the cases below.

A Marketing Co-operative

It is easy to understand the case of e.g. a marketing co-operative of agricultural products. In this case, what members attempt to do by means of their co-operative is to get the best possible price for their products.

The co-operative in this case makes an advance payment to its members for their products, as close as possible to the expected selling price minus handling costs. The members decide the amount of the advance payment. If, for example, the selling price for apples is expected to be 60 cents and handling costs are estimated at 10 cents, the members may decide to set advance payment at 50 cents. When all goes according to plan, at the end of the year there will be no excess of receipts over costs (zero surplus).

In most cases, co-operatives tend to account for adverse evolution of selling prices, so, in cases like the above, decide to make advance payment at, say, 40 cents. If the market evolves normally, apples will be sold at 60 cents and handling costs will be again 10 cents. In this case the co-operative needs to return to its members the difference of 10 cents, it had provisionally retained. These 10 cents multiplied by the kilos handed over by the co-operative will appear as surplus of receipt over costs.

It is clear that this excess surplus is artificially produced and it is up to the members to decide (or to make advance estimates of) its size. An alternative is open to co-operatives: to make higher than realistic advance payments and at the end of the year ask members to cover the derived losses (negative surpluses).

A Supplies' Co-operative

The case of an agricultural supplies' co-operative is even clearer. A co-operative supplying fertilizers to its members aims at taking advantage of its bulk purchases in order to bargain for lower prices from the fertilizer company. These lower prices are the sole reason for the members to form their joint enterprise.

Once buying prices are set, the co-operative has to fix its selling prices to its members, by taking account of transportation, storage and other handling costs. If the fertilizer company's price is 30 cents and all additional costs amount to 10 cents per kilo, the co-operative will consider setting its selling price at 40 cents or above. Diligently run co-operatives set a selling price at, say, 45 cents, for giving the joint enterprise an allowance for growth and improvement. The excess of 5 cents per kilo is a willful offering, a kind of investment capital supplied by members. The alternative open to members is to pay 40 cents per kilo of fertilizer (resulting into zero surplus) and, subsequently, pay to their co-operative at the end of the year, 5 cents per kilo of fertilizer bought from the co-operative.

Obviously, again, surplus is an artificially created fund, decided by members, who have also the alternative to annihilate it.

A supplies co-operative usually sells also to non-members, charging them the same or higher price. In such a case, the difference between the price charged and the overall cost to the co-operative cannot be interpreted in the way presented above for sales to members. The resulting difference in this case is profit (not surplus), because the co-operative acts as an intermediary between a private seller (fertilizer company) and a customer (a non-member), i.e. exactly as any other conventional private enterprise. No member is involved.

In conclusion, in the present case we may have the presence of both surplus and profit in a mix of various proportions.

A Workers' Co-operative

A workers' co-operative aims at achieving better reward for its members' work by embodying in the work the entrepreneurial risk and its reward, if successful. After paying for materials, rents, depreciation of property assets, etc., the remaining amount is attributed to labour.

A workers' co-operative normally requires work at a variety of levels and specialties. The remuneration of members may be equal or unequal to what the market offers. What the market offers should be considered as

the minimum if the co-operative has any reason to exist.

A successful co-operative rewards its member-workers better than the market. Technically, this takes the form of surplus (i.e. gross income higher than cost, including members' initial payments). The existence of surplus is an indication that workers have been underpaid, so, it is returned to them, in proportion to their initial payment.

Given that the decision to set the level of wages and salaries of the members of the workers' co-operative is taken by the workers themselves, it is clear that the level could be set at a higher level not allowing for any surplus to arise. Thus, surplus is the outcome of the inability to evaluate accurately the work imputed by the members.

In case the workers' co-operative employs non-members (e.g. temporary workers), the residual amount after meeting all kinds of expenses (often called net income) contains also an element of profit that should be treated differently (and in no case distributed to members).

A Producers' Co-operative Super-Market

More complicated is the case of a producers' co-operative super-market, where members may appear both as suppliers and as customers.

The co-operative super-market, owned by a co-operative of agricultural producers, sells both the agricultural products of its members but also many other items deriving from a multitude of third parties.

The super-market buys products from its members and from non-members and sells goods to members and to non-members. We assume that for every product the super-market succeeds to have a positive difference between the selling price and the overall cost.

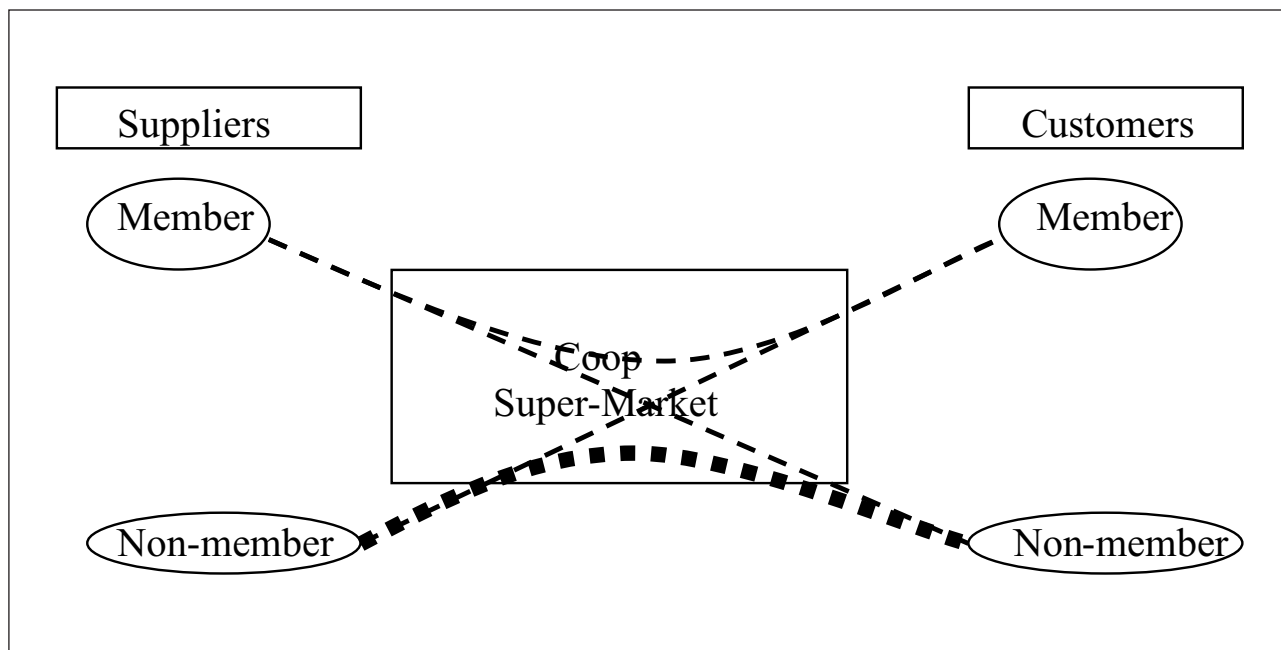
When the super-market sells e.g. olive oil originating from a member to a non-member customer, we have the case of the marketing co-operative presented above.

When the super-market sells e.g. detergents bought from a chemical company to members, we have the case of a supplies co-operative above.

When the super-market sells e.g. olive oil originating from a member to another member-customer, the resulting difference (between price and cost) is again surplus that has to be shared between the member provider and the member customer, in proportions that should be a subject of further elaboration, if one is willing to be fair to both.

When the super-market sells e.g. detergent bought from a chemical company to non-member, it behaves in exactly the same way as any other conventional profit-making firm. The resulting difference, between price and cost, is a profit.

One can visualize this complex of relations as follows:



In conclusion, where members are involved in the transactions of a co-operative, any resulting positive difference between receipts and costs constitutes surplus and it is equivalent to members' voluntary contribution to the co-operative. This may be returned to members in the form of patronage refunds. As D. Cobia²³ puts it: "patronage refunds should be viewed as adjustments to prices. They are the result of a supply co-operative charging too much for supplies or a marketing co-operative underpaying the patron". M. Abrahamsen²⁴ also asserts that "patronage refunds result because co-operatives, like most other businesses, cannot estimate with certainty their exact operating costs at the time they occur. To be on the safe side, co-operatives therefore seek to operate with sufficient margins, so that their income exceeds their outgo". And further "... co-operatives that return patronage refunds to members have no profits as legal business entities".

When no member is involved in the transactions of a co-operative (or, in other words, when the co-operative acts as an intermediary between third parties, the resulting difference between receipts and costs constitutes profit. This clear distinction between surpluses and profits can better support the thesis of Yair Levi²⁵, that co-operatives are non-profit and that the

Johns' Hopkins scholars should include them in the non-profit sector.

If the proposed specification of the terms "surplus" and "profit" are accepted, it would be compatible to reserve the term "net income" as an umbrella term to include both. In fact this is a way commonly used in the U.S.A., where the internal rules of co-operatives usually

make provision for refunds both to member-patrons and to non-member-patrons. Under the preceding proposal, profits correspond to the part of net income arising from business with non-member patrons.

Impact of the recognition of the true nature of surplus

Two major impacts are expected to be experienced from the recognition of the true nature of surplus in co-operatives:

- The tax treatment of co-operatives, and
- The recognition that co-operatives are not "profit-making" or "for-profit enterprises"

The tax treatment of co-operatives

One can distinguish three different treatments to which co-operatives are subjected regarding the attitude of tax authorities in the European Union countries. According to the first, the specific nature of the surplus in co-operatives is (openly or intrinsically) recognized (as deriving from the transactions with its members) and this results into exempting co-operatives from corporate taxation. According to the second treatment, co-operatives are considered as any other business and hence are subjected to the same

rules. According to the third treatment, some categories of co-operatives or some activities of co-operatives are exempted from corporate (income) taxation.

With reference to the European Union (of 15)²⁶, co-operatives are exempted from corporate tax in the surplus (or "profit") arising from transactions with members in Germany, in the Netherlands, in Sweden, in Finland, in Denmark and in Greece (since the year 2000). In Denmark, co-operatives showing transactions with non-members exceeding 25 per cent of the total for three consecutive years, are taxed as corporations, obviously because the profit component is significant and there is no easy way to separate surpluses from profits.

Agricultural co-operatives in Germany and in the Netherlands are considered as an extension of the individual agricultural enterprises. It should be understood that refunds to members from the surplus are added to the personal income of members where they are taxed.

Tax authorities treat co-operatives in the same way as any other company in Austria and in Ireland. In the latter country, co-operatives lost their special tax treatment in 1994.

Intermediate treatment is enjoyed by co-operatives in the remaining E.U.-15 countries. In Belgium, "profits" distributed to associates as dividends are exempted from corporate tax up to €130 per associate. The remainder is taxed at 25 per cent or 15 per cent for shares issued as of 1st January 1994.

In Spain, registered (protected) co-operatives are entitled to tax advantages: reduced rate of corporation tax of 20 per cent. This rate applies to "profits" arising from the transactions with members as long as the transactions with members exceed 50 per cent of the total.

In Portugal, co-operatives are subject to the income tax system for corporate bodies. Agricultural co-operatives are exempted from direct taxes on revenues from transactions with members. Similarly in the U.K. an agricultural co-operative may be exempted from corporation tax if the Inspector of Taxes has granted it mutual status.

In France, co-operatives that carry out certain activities (like the joint use of agricultural equipment, artificial insemination or wine making) are tax exempted. Other co-operatives are subject to the corporate income tax base on which the tax levied is cut by 50 per cent. Returns from activities with

members are exempted from the corporate income tax. Returns from transaction with third persons are not.

In Italy, the tax rate for co-operatives is lower than for capital companies (corporate income tax 37%, local income tax 16%). Co-operatives are exempted from these taxes as long as the members' remuneration is more than 60 per cent of the added value. Agricultural co-operatives are exempted from direct taxes when they raise livestock with feed from land belonging to members (at least 25%) or when they handle, process or market at least 25 per cent of farm and livestock products or animals supplied by members.

In Luxembourg, agricultural and trading co-operatives enjoy tax exemption in so far as their activities involve the common use of machines and agricultural facilities or the processing and purchase of agricultural or forestry products, originating from farms of their members.

Finally, in Greece, non-agricultural co-operatives receive the same treatment as capital companies with reference to corporate tax. Agricultural co-operatives are exempted from corporate taxation for the surpluses deriving from the members' transactions with their co-operative, but they are taxed normally for the profits deriving from the transactions of co-operatives with third parties.

The preceding review for the tax treatment of co-operatives in the E.U.-15 countries shows that with the exception of a small number of countries, co-operatives are subjected to tax treatment guided by policy considerations. This explains the differentiated treatment of agricultural co-operatives, although all kinds of co-operatives follow the same rules (Principles). Further, it is surprising that in a country like France returns to members deriving from transactions of their co-operatives with third parties are allowed. It appears that similar treatment is hidden in the rules applied in other countries, also.

One is tempted to conclude that either the "co-operatives are little or poorly understood"²⁷ or some governments choose to present as concessions to co-operatives a tax treatment that co-operatives deserve due to their particularities.

The recognition of co-operatives as non-profit making enterprises

Those legislators or scholars who recognize the particular nature of co-operatives and as a result support the exemption of surplus (however it may be termed) from corporate taxation, intrinsically profess that this is not profit in the usual sense of the word. It

is a refund, a return of an amount of money, because the service enjoyed by those who used it had been overcharged due to mis-calculation or because members so decided.

The members, for example, of a supplies' co-operative manage to buy their fertilizer cheaper, because they buy in bulk. It is like the 500 members of the co-operative visiting the fertilizer company and asking for a discount. Otherwise, they will turn to another company. If they succeed in their bargaining, should they be taxed on the discount?

Where this simple truth has been recognized, the surplus deriving from the transaction between members and their co-operative is exempted from corporate taxation. If surplus is returned to members, it is added to the members' income and becomes subject to personal income taxation. The USA Internal Revenue Code provides for the single tax treatment of co-operatives²⁸ as do several countries of the E.U.-15, mentioned earlier.

In view of these, one can classify co-operatives in the non-profit-making enterprises in their dealings with their members. When co-operatives undertake roles similar to 'companies or firms' (in the terminology of the Treaty of the E.U.) they make profits. In so far as this latter role is kept to a small proportional scale, the classification of co-operatives cannot be changed.

Co-operatives and social economy

If someone makes a box, he decides to make it big or small and also, if one has to split a continuous variable into parts, he specifies the criteria for splitting. In analogy, it cannot be said that it is right or wrong to define the social economy and its contents in some way different from e.g. the non-profit sector. It is the job of the scholars to research whether the contents of the two groups of legal entities coincide or differ. It is often even futile to try to reconcile the titles put to the 'boxes'. It is more useful to deal with the criteria followed for inclusion in or exclusion from the 'box'.

B. Lorendahl²⁹ has made a painful effort to shed some light to the 'terminological salad and definitional pot-pourri' as he calls it (borrowing the expression from Perri (1994) and he concluded as follows:

"Co-operatives are an integral part of the social economy and hence of the third sector, but should not be included in the 'ideal' (specific Swedish legal form) or non-profit sector. This proposition is consistent with the view of Salamon and Anbeier (1992). But it does not seem warranted, as suggested by these authors to consider them

parts of the business sector. The rationale for this is their special identity and values, being 'associations of persons' more than 'associations of capital' and above all – with respect to the definitional discussion above – being non-profit distributing".

For reaching agreement with Salamon and Anbeier that co-operatives should not be included in the non-profit sector, Lorendahl has indirectly accepted that surpluses and profits are the same thing. So, he arrived at the corollary that co-operatives belong to the business sector, to which he objected.

In an attempt to answer the question if a co-operative is non-profit, and without making the distinction between the terms "profits" and 'surpluses', the Canadian Co-operative Association and the Conseil Canadien de la Cooperation³⁰ conclude that:

"A co-operative may decide not to distribute any surpluses and therefore, in some situations will meet the definition of a non-profit organization. There may, therefore, be two kinds of co-operatives:

for profit co-operatives: *those in which members may redistribute any surpluses of the enterprise among themselves in the form of returns proportional to their business transactions with the co-operative during the fiscal year;*

not-for-profit co-operatives: *those in which any operating surpluses of the enterprise may not be distributed to the members and must be returned in their entirety to the co-operatives' general reserve (for example, housing, day care, health and other similar co-operatives)".*

If such a distinction is made, some co-operatives will qualify to be included in the 'Social Economy' and some others will not, because they will not meet the qualification criteria³¹.

Further, if co-operatives set a rule that surpluses deriving from members' transactions with their co-operatives shall not be distributed to their members, they will deviate from both the universally accepted International Co-operative Principles adopted by the International Co-operative Alliance as rules characterizing co-operatives and, also, from the basic Rochdale rules. In addition, such a criterion is unstable, because it is possible for a co-operative to accept the non-distribution of surplus rule and at the same time make efforts to keeping surpluses at zero or close to zero levels.

From the above, it appears sensible to conclude that by accepting this papers suggested definition of surpluses and profits, it becomes clear that co-operatives are 'not profit-making', and 'not profit distributing' and are 'not-for profit' enterprises, even if under specific situations they realize some profits not deriving from their members' involvement, not belonging to their members and not distributed to their members.

According to European definitions³², co-operatives are an integral part of social economy, together with mutuals, associations and foundations, because the 'box' has been made to include legal entities with the following characteristics:

1. Their primary purpose is not to obtain a return on capital. They are by nature, parts of a stakeholder economy, whose enterprises are created by and for those with common needs and accountable to those they are meant to serve.
2. They are generally managed in accordance with the principle of 'one member one vote'.
3. They are flexible and innovative – Social economy enterprises are being created to meet changing social and economic circumstances.
4. Most are based on voluntary participation, membership and commitment.

In a more concise form J. Defourny³³ presents the distinctive characteristics of social economy as: absence of a profit motive, freedom of membership, democratic management and independence from the public authorities.

Being an 'ambiguous and indefinite concept' according to J.L. Monzon Campos³⁴, social economy in Europe is often used as synonymous to the third sector, with basic constituents co-operatives, mutual societies, associations and foundations. In the glossary of the OECD publication on the non-profit sector, however, co-operatives are not considered as part of the Third Sector.³⁵

Co-operatives and mutual societies

Most of the rules of mutual societies are the same as those of co-operatives. The difference lies in the economic participation of members. In co-operatives, members contribute the capital and this capital is variable (because of new memberships or withdrawals). Surpluses in co-operatives are used for their development or for purposes agreed by the members or are returned to members in accordance with their transactions with the co-operative.

Mutuals, usually, do not have share capital. They charge members for the services provided. In order to cover costs, they need to charge members at cost or somewhat above it, if they want to be on the safe side or in order to improve their services. Normally, mutuals do not distribute surpluses to members (although there are exceptions, e.g. Germany, France, Spain).

Going back to the definition of surplus in co-operatives as the excess of payment made by the members for the goods and services bought by them from the co-operative, one can see no difference between co-operatives and mutuals with reference to this element. Both can keep surplus at zero level or give it a considerable size, if they so wish. In essence, the possibility to distribute the surplus to the users of the serviced makes co-operatives more flexible.

If the above argument is correct and if universities and hospitals, operating under the mutual form, are classified as non-profit-organisations, one wonders why co-operatives should be classified differently.

Conclusion

Co-operative literature needs to standardize the meanings of the terms used especially in connection with the economic functioning of co-operatives. If the term surplus in co-operatives is reserved for the excess payment made by the members for the goods and services bought by them from their co-operative, or of withheld amounts by the co-operative from its members for the goods and services offered by them to their co-operative, it will become clear that co-operatives are not profit making enterprises and will be entitled to demand appropriate treatment and recognition by legislators and the society.

Notes

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- 3 e.g. Salamon, L. et. al. *Global Civil Society – Dimensions of the Nonprofit Sector*, The Johns' Hopkins Centre for Civil Society Studies, Baltimore MD, 1999, and Salamon, L.M. et. al. *The Emerging Sector Revisited – A Summary*, The Johns' Hopkins Comparative Nonprofit Sector Project, Phase II, 1999
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- 5 e.g. European Conference on the Prospects of Social Economy within the Framework of Sustainable Development – European Resolutions, 2001 or CECOP discussion document for developing a common position addressed to European Social Economy organisations
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Routes to Employee-Commitment in Worker Co-operatives

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Abstract

In recent years, employee-commitment has received much scholarly attention in various contexts. For example, research has produced various definitions, measurements and consequences of it. However, routes to employee-commitment in worker co-operatives have not been much studied, even though worker co-operatives play a major role in many economies in various fields of industries. More specifically, distinct characteristics related to co-operative entrepreneurship has not been adequately investigated. In this paper, we build on literature on employee-commitment and co-operative entrepreneurship in order to get a deeper understanding of the routes to employee-commitment in worker co-operatives.

Key Words

Employee-Commitment (EC), Worker Co-operatives, Employee Ownership

Introduction

Organizational commitment (OC) has received much academic and societal attention during the recent decade (e.g., Swailes, 2002; Allen and Grisaffe, 2001; Dessler, 1999). For example, OC has been widely studied in organizational behaviour and psychology and it has produced various definitions of its construct and development (e.g., O'Reilly and Caldwell, 1980; Hrebiniak and Alutto, 1972) as well as the consequences and measurements of it (e.g., Mathieu and Zajac, 1990). According to Porter et al. (1974, 604), OC can be defined as;

“a) a strong belief in and acceptance of the organization’s goals and values; b) a willingness to exert considerable effort on behalf of the organization and c) a definite desire to maintain organizational membership”.

Most often, OC can be divided into *employer-commitment* (e.g. Bragg, 2002) and *employee-commitment* (EC) (e.g. Allen and Meyer, 1997) in that, for example, OC has many positive outcomes to the employees and employers. In organizations where EC is strong, personnel have achieved higher degree of production, better service quality, productivity and

effectiveness compared with the organizations where an employee’s commitment is weaker (e.g. Bragg, 2002). Further, an employee’s job performance is better when the employee is strongly committed to the organization (Meyer et al. 1989) and an employee experiences greater job satisfaction under the conditions of strong EC (Glisson and Duric, 1988).

EC is seen as important since organizations are competing for skilled and motivated personnel. However, various trends in our operational environment – such as globalization and employees’ job insecurity - have decreased the level of EC (See, e.g. Chirumbolo and Hellgren, 2003). For example, in investor-owned companies, many factories have been shut down in various countries – since companies move their production to countries where the production and labour is cheapest in order to maximize their profits to shareholders. Based on these notions, it can be argued that the preconditions for strong EC are not as or favourable as in the past.

In this study we focus on employee-commitment (EC) and define it as *a psychological condition that describes the employee’s relation towards an organization*. Consistently with the research of Allen and Meyer (1997), our definition of EC includes affective, normative and continuance commitment.

Even though EC has been studied in various contexts (e.g. Buchanan 1974, Porter et al. 1974, Allen and Meyer, 1997, Curtis and Wright, 2001, Bragg 2002), it has rarely been studied in the context of co-operative enterprises (e.g. Troberg, 2000). Co-operatives are a specific type of enterprises in which economic, social and societal related goals are combined. According to ICA (International Co-operative Alliance)

“a cooperative is an autonomous association of persons united voluntarily to meet their economic, social and cultural needs and aspirations through jointly-owned and democratically-controlled enterprise” (Nilsson, 1996, 635).

For example, in worker co-operatives, employees democratically own and manage the enterprise. Pierce et al. (1991) and Wetzel and Gallagher (1990) have suggested that employee ownership is significantly related to the level of EC in worker co-operatives.

This article is based on a conceptual analysis of past literature of EC and co-operative entrepreneurship, by which we aim to get a deeper understanding of the potential routes of EC in worker co-operatives. Our paper proceeds in four sections. First, we review the definitions of EC. In the second section, we draw the alternative routes to EC from the past literature. In the third section, we analyze the specific characteristics of employee ownership and co-operative entrepreneurship. Finally, we present the possible routes of EC in co-operatives and present the conclusions of our study.

Definitions of employee-commitment (EC)

EC can be conceptualized in several ways. For example, an EC emerges when an employee identifies, adopts, accepts and trusts the values and goals of an organization (Curtis and Wright, 2001; Buchanan, 1974; Porter et al. 1974). In addition, EC emerges when the employee identifies the tasks of an employer (Buchanan, 1974) and has a willingness to exert considerable effort on behalf of the organization (Curtis and Wright, 2001; Porter et al. 1974). An employee's commitment is regarded as strong when she/he has a desire to maintain organizational membership and has feelings of loyalty and attachment to the organizations (feeling of belonging) (Curtis and Wright, 2001; Buchanan, 1974; Porter et al. 1974).

When considering the appropriate definitions of EC, it is argued that most theorists agree that EC can be seen in terms of three dominant dimensions: 1) affective, 2) normative and 3) continuance commitment. Affective component refers to employee's emotional attachment to, identification with and involvement in the organization. Continuance component refers to commitment based on the costs that employees associate with leaving the organization. Normative component refers to employees' feelings of obligation to remain with the organization – and it is affected by the socialization process of individuals. (e.g. Allen and Grisaffe, 2001; Allen and Meyer, 1997, 1990)

EC can be divided into four types of commitment; 1) want to, 2) have to, 3) ought to and 4) non-committed. The strongest level of EC is "want to" commitment. In the extreme, these are the truly dedicated and loyal employees. "Have to" commitment refers to lower level of EC. At this level, employees stay in their organizations because it is necessary for their well-being - some stay because they cannot find other jobs or because they are not employable elsewhere. The third type is "ought to" commitment - these are the employees who stay because they feel obliged to their

employer. The weakest type of EC is non-committed personnel - they are actively looking for other employment. These workers are halfway out of the door. In today's market, they make up about 25 to 30 % of the workforce. (Bragg 2002, 19)

Routes to employee-commitment (EC)

In the research of EC, it is often suggested that there are at least two possible routes to the development of EC. First, *personal* (e.g. Allen and Meyer, 1997) and *psychological factors* (e.g. Porter et al. 1974) have an effect on the emergence of EC. In addition, *organizational* and *job-related characteristics* (e.g. Allen and Meyer, 1997; Mathieu and Zajac, 1990) have an effect on the emergence of employee's commitment to the organization. Regardless of the wide scholarly attention on EC, the possible routes to the EC has been primarily explained by either employee's personal or organizational characteristics (See e.g. Mir et al. 2002) The role of groups and group relationships (in organizations) as mediators of EC has not received much scholarly attention (cf. Mathieu and Zajac, 1990).

In this section, we analyze the interaction between personal and organizational characteristics in the development of EC. Secondly, we analyze the role of group dynamics in the same context. Finally we present that the EC is a result of an interplay between personal, group and organizational characteristics in which affective, normative and continuance evaluation takes place. EC develops from identification, attachment, involvement and loyalty in which psychological contract between employee and employer occurs (e.g. O'Reilly and Chatman, 1986).

Interplay between personal and organizational characteristics as a route to the development of employee-commitment (EC)

Personal and organizational characteristics have a strong influence on the development of EC. Personal characteristics include for example, sex, age, marital status (e.g. Mathieu and Zajac, 1990), personal needs and motivators (e.g. Mowday et al. 1982), values (e.g. Mayer and Schoorman, 1992) and a person's identity (e.g. Kanter, 1972). Organizational characteristics include factors such as size, centralization, structure and values of an organization as well as job-related characteristics in the organization (Allen and Meyer 1997, Mir et al. 2002). In the development of EC, an employee tries to optimize his/her personal characteristics (e.g. values, identity) to the

organizational characteristics (e.g. organizational values and identity). For example, if personal and organizational characteristics fit well together, an employee is likely to develop feelings of commitment to the organization (cf. Heilmann, 2004).

In different stages of the development of EC, an employee uses *affective, continuance and normative evaluation* between his/her personal and organizational characteristics. The employees emotional (affective) attachment to the organization appears as a willingness to be a member of the organization. Continuance commitment refers to positive and negative aspects of the organization which are valued by an employee whilst normative commitment is based on the sense of duty of an employee. (See Curtis and Wright, 2001; Allen and Meyer, 1997)

An employee compares his/her personal characteristics (e.g. identity or values) to those of the organization and if they match well together, an employee is likely to develop commitment toward the organization. In the development of EC (attachment, identification, involvement and loyalty) an employee uses affective, continuance and normative evaluation (e.g. Allen and Meyer, 1997). In the past literature of EC, a psychological contract (e.g. Rousseau and Schalk 2000, 2) has often been linked to the EC. Psychological contract can be identified as invisible glue between individual and organization (Herriot 1992, 6). This means that both employee and employer have reciprocal rights, obligations and expectations of their exchange relationships which occur either in the formal or informal contract (See Schalk and van Dijk, 2005, 37; Janssens et al. 2003, 1350; Schalk and Rousseau, 2001 and Rousseau, 1995).

Strong group cohesion as a route for development of employee-commitment (EC)

So far, the influences of group relationships to the emergence of EC have been examined in only a few studies and represent neglected areas (Mathieu and Zajac, 1990). Wiener (1982) suggest that organizational environments (e.g. groups) may act as normative influences and affect members' organizational commitment by shaping their belief system – in this sense, organizational contexts (such as group relationships) may influence an individuals' predispositions to become committed, (Mathieu and Zajac, 1990).

Personal characteristics – such as an employee's values and identity show up in the work situations as to how

an employee co-operates with his/her workmates and how he/she identifies to a particular organizational group and to the norms and rules of exchange in that group. Personal characteristics have also an impact on *how willing a person is to co-operate with his/her colleagues in the workplace and associate with them in the leisure time*" For example, employees' differences in individualism-collectivism have effects on cooperation in groups (Wagner, 1995). That is, individualists who feel independent and self-reliant are less apt to engage in co-operative behavior, and collectivists who feel interdependent and reliant on groups are more likely to behave co-operatively (Ibid). Further, collectivists emphasize group interests over their individual needs and desires, and tend to look out for the well-being of the groups to which they belong, even when such actions sometimes require sacrificing personal interests (Wagner and Moch, 1986).

Curtis and Wright (2001, 57) have also noticed the role of group cohesion in the development of employee-commitment. Fitting in with the team or with colleagues is important to the development of an emotional attachment at work – this can be regarded as *"togetherness feeling"* among colleagues (Heilmann, 2004, 192). In other words, an employee identifies him/herself to a certain group and develops feelings of commitment to the group's operation and decisions. Group identification exists when a member feels, thinks and behaves according to the norms of the group (Stoel, 2002) which enhances the probability that group members establish same social identity (e.g. Hogg and Terry, 2000; Gundlach et al. 2006). When group members share same social identity and experience feelings of *"belonging"*, group cohesion strengthens. In a highly cohesive group, members actively participate and commit themselves to the group operation and remain united in the pursuit of its goals and objectives (Carron, 1982: 124; in Cota et al.1995).

The rules and norms of the group have an impact on whether an individual develops feelings of commitment to the organization. For example, if a team is committed to the goals and decisions of an organization, a team member is more likely to commit to the rules and norms of the organization. Based on these notions, it can be argued that strong group cohesion and sense of *"belonging"* enhances the development of EC. Next figure (Figure 1.) presents the role of group dynamics in the emergence of EC in organizations:

The Figure 1. shows that high commitment to the group's rules and norms may not always be a benefit,

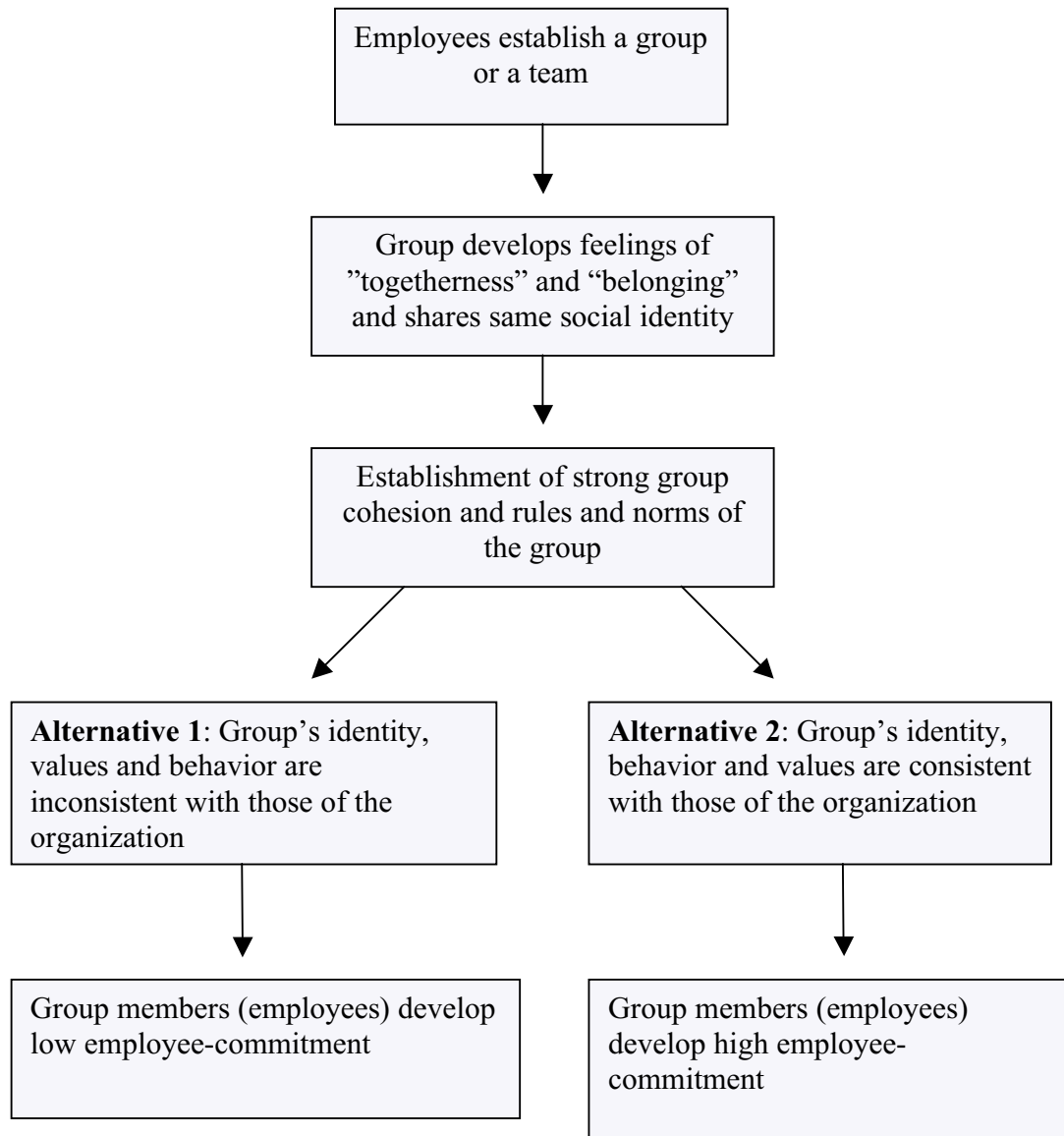


Figure 1. Group dynamics as a route to employee-commitment (EC)

either for the employee or for the organization. For example, if a person is more committed to the rules and norms of a group than those of the organization, an employee's commitment to the organization may not develop so strongly.

Employee ownership and co-operative entrepreneurship

There are various forms of employee-ownership (e.g. social ownership, worker/producer co-operatives, direct ownership and employee stock ownership plans) which each carry different facets of employee ownership and control (Pierce et al. 1991). However, they all share a common purpose: to provide a capital ownership stake for workers. In addition to the formal

definitions of ownership (right to control the firm and right to appropriate firm's profits) (e.g. Hansmann, 2000), ownership can be also regarded as a "psychologically experienced phenomenon" which operates directly and/or independently on employee attitudes, motivation and behaviors (Pierce et al. 1991). Employee-owned firms often have democratic governance and ownership structures (cf. Hansmann, 2000) which may in turn, have many individual and organizational outcomes. For example, Logue and Yates (2006) and Hansmann (2000) have argued that productivity in worker-owned enterprises equals or exceeds those of the conventional enterprises.

Democratic ownership structure can be divided into individual, collective and social type. Individual type of democratic ownership structure means that surplus

can be paid out individually to the employees (e.g. extra monthly payment) and they can withdraw their accumulated capital when they leave the firm. Collective type of ownership means that surplus cannot be paid out to the individual employees – instead they can use it for collective consumption (e.g. daycare for their children). In addition, in collective type of democratic ownership, the employees cannot withdraw accumulated capital when they leave the firm. Thirdly, in social ownership structure, the right to surplus, wealth and control lies in higher democratically elected bodies either on industry, regional or national level. (Mygind, 1992)

As presented earlier, worker co-operatives represent one form of employee ownership (Pierce et al. 1991). In contrast to the private sector organizations, co-operatives carry social and economic objectives in their operation (Troberg, 2000; Wetzel and Gallagher, 1990). Co-operative organizations have often been established as an initiation of weaker actors in the markets to pool resources and to increase their negotiation power in the markets. For example, worker co-operatives are enterprises which are owned and controlled by their members and their main objective is usually to create employment and retain control over labor power (Staber, 1992, 1192).

Research on worker co-operatives has received much scholarly attention during the recent decades (e.g. Hunt, 1992; Moss, 1991). More specifically, many of the researches conducted in worker co-operatives have mainly focused on to discuss the problems of their management and / or why they have failed in market circumstances (e.g. Ernberg, 1993; Cornforth and Thomas, 1990; Staber, 1989; Cornforth, 1983). However, research on the potential benefits of worker co-operatives has remained somewhat unclear. According to Cornforth (1983, 166), worker co-operatives differ from one another in their organizational characteristics (e.g. objectives) and their economic circumstances. Based on these differences, there can be distinguished at least five different employee-owned co-operatives (Cornforth, 1983):

- a) “Endowed” Co-operatives
- b) “Worker Buyout” Co-operatives
- c) “Defensive” Co-operatives
- d) “Alternative” Co-operatives
- e) “Job creation” Co-operatives

Endowed co-operatives are those that have been “given away” by their original owners to the employees. They have arisen from a successful

business, but may have problems in developing genuine democratic control. *Worker buyout co-operatives* are those where the workforce have bought out the original owners whilst *defensive co-operatives* are formed by employees in order to preserve jobs on the closure of a business (the co-operative is usually seen as a last resort to save jobs when other forms of action have failed). The members of *alternative co-operatives* are usually middle class, well educated and have a strong commitment to democratic ideals and producing for social needs rather than profit. *Job creation co-operatives* have been established in times of high unemployment and they have been formed in order to create new jobs. (Cornforth, 1983, 168-169) Whilst ownership and governance may be broadly similar these differences identified by cornforth may have a profound impact on organisational culture and values.

Routes to employee-commitment in worker co-operatives

According to Oliver (1984, 43), commitment of an employee to the co-operative is a sum of individuals’ expectations and values and perceptions of work environment (organizational rewards, opportunities and constraints) which the organization offers. Further, Oliver (1984, 29) argues in his study that organizational commitment of workers’ co-operatives is higher than in other organization forms because there is “*a closer match between the values and goals of the members of the co-operatives and what the co-operatives provided as work organizations.*”

Co-operative entrepreneurship has many distinctive features which have an affect on the development of employee-commitment. For example, the ownership structure of co-operatives (See e.g. Hansmann, 2000) is different from, for example, investor-owned companies. In employee-owned co-operatives, employees democratically own the enterprise and can participate to the decision-making process.

Employee ownership is seen as a route to increased employee satisfaction and commitment and from a business-efficiency perspective, it is seen as a way of encouraging a “*responsible*” attitude on the part of the workers and as a means of establishment of a community of interests between management and workers. In addition, employees who have strong participatory values seem to have high commitment in worker co-operatives where as those with strongly instrumental values have relatively lower commitment. (Oliver, 1990).

Incentives related to loyalty and commitments are especially important in sustaining any co-operative organization. Loyalty in co-operatives requires minimum mandated levels of participation where as commitment refers to “*effort above minimum levels*” and is required when member performance beyond passive join and remain is involved in producing collective good. Establishment of high employee commitment is important in terms of reducing the problem of “*free riding*” in co-operatives. (Carney, 1992)

Organizational characteristics of co-operatives as means of increasing the level of employee-commitment (EC)

Organizational characteristics related to co-operative organizations have some unique features when evaluating their potential role in the development of employee-commitment in worker co-operatives. For example, type of ownership may foster employee’s feelings of commitment to the organization. According to Pierce et al. (1991), formal ownership means right to equity, influence and information and under conditions of strong sense of ownership legitimacy, there is a positive relationship between formal and psychological ownership and that psychological ownership has an effect on the development of the EC.

According to Stryjan (1983, 271), worker management have a great contribution of maintaining equality, information flow and social contact with workers which enhance the social integration, solidarity and improved control of the managerial level. Based on this notion, worker management can potentially increase the level of EC in worker co-operatives. Moss (1991) has suggested that organizational democracy can enhance efficient and psychologically satisfying work situations (e.g. increase the level of EC). Employee ownership also fosters the feelings of employee power and responsibility (Moss, 1991, 192).

According to Wetzel and Gallagher (1990), EC may be a function of employee ownership. Worker co-operatives have greater EC than workers in conventional organizations in that employees are more likely to feel that they participate in decision-making and therefore strengthen their sense of responsibility (Rhodes and Steers, 1981; in Wetzel and Gallagher, 1990). Davis is skeptical that co-operatives of any size can function without professional management and critiques the worker control view of management (Davis, 1999 pp30-35). Davis is clear that a managerial

structure based on co-operative values will incorporate employee involvement and encourage. He sees the co-operative context provides additional motivational potential to the employees through the following (Davis, 2004, 70):

- Ownership base
- Identity, values and principles
- Links to community
- Human centered business
- Greater social solidarity.

The development of community-based objectives in co-operatives can increase the sense of meaning and identity for the individual in the employment relationship itself (Davis, 2004, 66). Further, Davis argues (2004) that the “*social performance*” of the co-operative and individual employees’ contribution to this, could make for improved member relations, contribute to team building and satisfy employee esteem needs. If the conditions suggested by Davis (2004) are fulfilled, EC is likely to increase. The management of co-operatives may also foster the development of EC. For example, the following principles of cooperative management can potentially increase the level of EC in worker co-operatives (Table 1.)

In terms of development of EC to the organization, so called *identification* (e.g. Mayer and Schoorman, 1992) to the organization has often been characterized as important. In worker co-operatives, participatory democracy (e.g. Rosner, 1991) can be an important means for members’ identification to the organization and therefore increase EC. Further, Moss (1991) argues that employee ownership can be considered as a means to achieve greater fit between individuals and organizations. In other words, EC is the result of personal, organizational as well as group characteristics (e.g. Bragg 2002). Employee ownership can increase EC because by participating in the governance of the co-operative, employees can achieve greater fit between them and organizations.

Characteristics for co-operatives are locality, regionality and permanence operation (cf. Tuominen et al. 2006) and because of the democratic and local ownership structure, worker co-operatives offer a stable place with a local identity to their workers. In sum, organizational characteristics related to co-operatives potentially enhance the development of EC in co-operatives and enhance the feelings of “*togetherness*” (See Heilmann, 2004), sense of belonging and sharing of same social identity (e.g. Gundlach et al. 2006).

The seven principles of cooperative management:
Pluralism – supports diversity, stakeholder relations, management and genuine democracy
Mutuality – reduces conflict, ensures fair treatment, transparency and equity in business and social transactions
Individual autonomy – ensures devolved responsibility and empowerment and supports a genuinely democratic culture where innovation is encouraged
Distributive justice – ensures proper distribution of surplus based on economic participation and fair trade across the supply chain
Natural justice – ensures elimination of nepotism, abuse of authority, fair treatment
People-centeredness – people in the community are subject not the object of co-operative management, organization and association
Multiple role of work and labour – all work and labour must always be managed and organized bearing in mind it’s personal, social, economic, environmental and cultural dimensions

Table 1. The principles of co-operative management (Davis, 2004)

Strong group cohesion as a means of increasing the level of EC in co-operatives

Worker co-operatives are usually established by a group of local people who know each other well, divide same ideas and background. For example, defensive co-operatives are formed by employees in order to preserve jobs on the closure of a business (Cornforth, 1983). This kind of situation fosters the sharing of same social identity (e.g. Gundlach et al. 2006), increases group cohesion (e.g. Carron, 1982) and feelings of togetherness among employees (e.g. Heilmann, 2004). Democratic governance of co-operatives and employees’ ability to participate to the decision-making process in worker co-operatives strengthens group cohesion and sharing of same social identity – which on the other hand, have an impact on the level of EC. Further, a group’s identity, values and behavior are likely to be consistent with those of the co-operative since group members (employees) have originally been responsible for establishing the identity, values and behavioral rules and norms of the organization (co-operative). Due to employees’ financial interest, organizational goals of wage effectiveness, group norms favoring productivity are more prevalent within worker co-operatives which lead to greater EC by creating peer pressure to make responsible work decisions (Wetzel and Gallagher, 1990).

When the group members in co-operatives are highly committed to the operation and rules and norms of the group, so called “group social capital”

(See Oh et al. 2006) is enhanced. Oh et al. (2006, 570) define group social capital as

“the set of resources made available to a group through group members’ social relationships within the social structure of the group itself, as well as in the broader formal and informal structure of the organization.”

In addition, Oh et al. (2006) argue that greater group social capital resources lead to greater group effectiveness (e.g. group performance and individual growth and satisfaction) and that there are many conduits through which group social capital resources flow – such as vertical and horizontal intergroup and intragroup relationships. For example, co-operatives often have close relations to their regions and different stakeholders in the community (as serving the interests of the wider community) (Tuominen et al. 2006). Further, Uski, et al. (2007) suggest that both formal and informal dimensions of co-operatives’ networks are of strategic importance for co-operatives.

Conclusions

In this article we have aimed to get a deeper understanding of the routes of EC (employee-commitment) in worker co-operatives. Our conceptual analysis explored the literature on EC (e.g. Bragg, 2002; Curtis and Wright, 2001; Allen and Meyer, 1997; Buchanan, 1974) and worker co-operatives (e.g. Troberg, 2000; Staber, 1992; Cornforth, 1983) in order to form a theoretical framework of the potential routes to EC in worker co-operatives.

In order to achieve our aim for this article, we first investigated the various routes to EC in organizations. As a result, we found out that there are two distinct routes to EC in organizations. The first route occurs as interplay between personal and organizational characteristics. Personal characteristics (e.g. Mayer and Schoorman, 1992; Mathieu and Zajac, 1990; Mowday et al. 1982) include such as age, sex, marital status, personal needs, motivators and values where as organizational characteristics include such as size, structure and values of an organization (e.g. Allen and Meyer, 1997). The interplay between personal and organizational characteristics occurs when an employee tries to maximize the fit between his/her personal characteristics (e.g. values) to those of the organization (e.g. values) and this optimal fit between personal and organizational characteristics operates as a route to EC.

In our study, we found out that the role of group relationships has not received much scholarly attention in the research on EC. By following the work of Wagner (1995), Curtis and Wright (2001), Heilmann (2004) and research on social identity theory (e.g. Gundlach et. al, 2006; Carron, 1982), we built a conceptual framework of “*group dynamics as a route to employee-commitment*” (See Figure 1., p.9). In this model, we argue that if the identity, values and behavior of a strongly cohesive group are inconsistent with those of the organization, the group members (employees) have weak commitment to their organization. In

contrast, if the identity, values and behavior of a strongly cohesive group are consistent with those of the organization, the group members (employees) have strong commitment to their organization.

After we had investigated the possible routes of EC to the organization, we analyzed the possible routes of EC in worker co-operatives (e.g. Carney, 1992; Oliver, 1990). Finally, we suggest that there are several organizational characteristics of worker co-operatives that have an effect on the EC in worker co-operatives. The following table (Table 2.) presents the organizational characteristics of co-operatives that can potentially increase the level of EC in worker co-operatives:

In sum, the main contribution of our article is that we have presented various organizational characteristics related to worker co-operatives which operate as routes to development of EC. In addition, we have presented a framework of group dynamics as a route to development of EC where as the past research on EC has mainly focused on personal and/or organizational characteristics. While this article is preliminary attempt to integrate research on EC and worker co-operatives, we would expect further investigation worthwhile. For future research it should be highly important to test our hypotheses empirically and especially to study the various dynamics of group relations which potentially foster the development EC in co-operative organizations.

<p>Organizational characteristics of worker co-operatives as means of increasing the level of employee commitment:</p>
<p>Employee ownership: Enhances the feelings of employee power and responsibility</p>
<p>Equality -principle: Members receive pay and surplus in relation to their contribution in a co-operative</p>
<p>Democratic governance: Employees ability to participate to the decision-making process increases EC and strengthens group cohesion and sharing of same social identity</p>
<p>Human centered values, identity and principles of co-operatives are likely to increase EC in worker co-operatives</p>
<p>Principles of cooperative management promote EC</p>
<p>A group´s identity, values and behavior in a worker co-operative are likely to be consistent with those of the organization since group members (employees) have originally been responsible for establishing the identity, values and behavioral rules and norms of the organization (co-operative)</p>

Table 2. Organizational characteristics of co-operatives as means of increasing the level of employee-commitment (EC) in worker co-operatives

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Co-operatives: flexible form of self-employment in competence based business¹

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Abstract

This article examines competence-based co-operatives and the effect of the co-operative form on the success of the firms in four branches: social and welfare, arts and culture, expert² and professionals³ co-operatives. Competence-based co-operatives have been a growing phenomenon in Finland during the last ten years. The study was carried out by reviewing longitudinal documentation material and interviewing the representatives of ten competence-based co-operatives. Seven success factors were identified in all of the co-operatives interviewed. The co-operative form seems to be a flexible form of organisation, which especially enhances innovativeness⁴. Innovativeness was one of the success factors.

Key Words

Employee Ownership, Competence-based Organisations, Worker Co-operatives

Introduction

Worker co-operatives were rare in Finland until 1995. In the 1980s, less than 10 worker co-operatives were in existence. At the end of 2004, the number of new co-operatives⁵ was over 1,400 (OT-lehti 4/2004). Of these, more than half were classified as worker co-operatives. The recession in the beginning of the 1990s was a major reason for the unemployed to begin the establishment of co-operatives. Spear and Thomas (1997) argue that the level of co-operative formations is strongly linked to the level of unemployment. Another major reason for the emergence of new co-operatives was the increase in knowledge-intensive⁶ services such as consulting, training, finance, information technology and media.

The number of competence-based co-operatives is expected to grow in the future, as more people employ themselves in knowledge-intensive expert and service branches in which joint entrepreneurship is a suitable form of enterprise (Karjalainen, Piippo and Pirinen 1998). Branches expected to show future growth include those of social and welfare, management and expert services, the service sector and teaching and culture. Flexible and agile structures are needed in

these sectors to facilitate employment (Wilenius 2004).

The key findings of a study of Finnish competence-based co-operatives are discussed in this article. The purpose of the study was to identify the success factors of co-operatives and the bearing that the co-operative form has on the success of the firms. The co-operatives were operating in four branches: 1. Social and Welfare; 2. Arts and Culture; 3. Expert, and 4 Professional Services. After a brief introduction to earlier research and methodology, the strengths and weaknesses as well as the factors leading to success are discussed. A major focus is on the impact of the co-operative form on the success of firms.

Conceptual framework of the study and the major proposals of earlier research

Earlier research of business activities of co-operative enterprises consists mainly of management and organisational theories and ownership theories (transaction cost and agency theory). In regard to management and organisational theories, the focus of this article is on *leading and motivating workers* because of the central role that workers play in competence-based firms. The competencies of the workers have a key impact on the success of the firms. The ownership theories explain why certain types of enterprises, such as co-operatives, are established and what kinds of challenges a collective ownership structure may create. These challenges may become a threat to the success of the firms.

Management and organisational theories

Knowledge society has greatly changed the management of firms. The importance of workers' competencies, interest groups relations and networking is increasing in relation to investments in technology, machinery and factories. When the importance of people in organisations increases, leadership issues become crucial. Managers have to understand better workers' behaviour and motivational aspects.

Commitment of the members to the organisation and motivational issues become central in future organisations (Sveiby & Lloyd 1987; Alvesson 1992 and 1996). If the key workers leave the company, the

company may suffer severe losses of its knowledge assets. In addition, in order to co-operate and work effectively in teams, workers have to learn to know one another. This means that they have to work a sufficiently long time for the same employer.

Intrinsic motivation⁷ of workers is a major issue in managing competence-based organisations, because it is a factor having a positive long term effect on workers. It is also a central element of creativity. Other elements of creativity are expertise and creative thinking (Amabile 1998). According to Amabile (1998) managers can influence all the three components of creativity: expertise, creative-thinking skills and motivation. Most easily managers can influence motivation.

Amabile (1998) has shown the linkage of intrinsic motivation to creativity. She has found in her studies that people will be most creative when they feel motivated primarily by the interest, satisfaction, and challenge of the work itself and not by external pressures such as competition, control, commands or financial remuneration. According to many studies major sources of intrinsic motivation are opportunities to use competencies and learn new ones as well as good collaboration with colleagues (Amabile 1997; Tampoe 1996; Kelloway and Barling 2000; Luoma, Troberg, Kaajas and Nordlund 2004).

Creativity is strongly linked to innovativeness which is one of the long-term success factors of firms. Innovativeness is the key factor contributing to the emergence of innovations. The role of innovations has become most important in today's world characterized by discontinuity. The life and work rhythms have become faster, new products and services are being developed continuously. Firms need radical innovations in order to gain competitive advantage (Koskinen 2006).

According to many researchers (e.g. Korhonen 1998; Nurmi 1998; Sveiby 1997), knowledge sharing and good co-operation within the organisation and with outside interest groups are crucial elements of today's organisations. Knowledge sharing and good co-operation are linked to innovativeness. New innovations are often developed in teams where workers' competencies complement one another. Effective and good ways of co-operation contribute to the success of the teams.

Ownership theories (transaction cost and agency theory)

Transaction cost theory explains why co-operatives are founded and which kinds of benefits the co-operative form may produce. According to this theory, co-

operatives are founded when there is a transaction-specific benefit to be achieved through the formation of a co-operative (e.g. Bonus 1986). Regarding co-operatives, transaction cost theory has mostly been used to analyse member transactions on the market versus their transactions with the co-operative.

Bonus (1986) and Nilsson (1991) are researchers who have examined interaction between members using transaction cost theory. According to Nilsson (1996, 641), the transaction costs will be low when human relationships are characterized by confidence, proximity and friendship. In today's organisations the role of co-operation between the members of the organisation is very important factor contributing to good knowledge sharing and the emergence of new innovative ideas. Good co-operation also increases the intrinsic motivation of the members (Troberg 2000).

Many studies (e.g. Nilsson 1996; Troberg 2000; Nilsson and Björklund 2003) have shown that transaction-specific benefits, such as a strong corporate culture with shared values and a flexible form of organisation, often emerge in worker co-operatives. These benefits motivate and commit the members and have a positive impact on the collaboration of the members.

Agency theory

The main concept of agency theory is that in an employee-owned firm there may emerge what are known as agency theoretical problems (Jensen and Meckling 1979; Vitaliano 1983; Schuster 1990, Hansmann 1996; Hakelius 1998; Nilsson and Björklund 2003) because of the joint ownership structure. When there are many owners in a firm from equal basis, it is likely that differences of opinion arise about the firm's policies. Worker/members may have different interests and aims arising from their personal circumstances. Also, the equal ownership structure may lead to slow decision making, because there are many decision makers in the firm. One type of an agency theoretical flaw in a co-operative is the different status of old and new members. Old members may experience that new members too easily benefit the work done by the old members.

Agency problems may lead to difficulties of management and jeopardize the expected positive effects of the co-operative form such as a collaborative organisational culture, solidarity, trust and well-functioning joint entrepreneurship (Troberg 2000). Development of leadership within the co-operative is a key factor in avoiding the emergence of agency theoretical challenges. It means that leadership is consciously and actively practiced by one or two

members in order to strengthen the organisational culture and to effectively direct the members towards common goals. A study made of Finnish knowledge intensive co-operatives showed that the successful co-operatives developed this kind of leadership which assisted in mitigating agency problems (Troberg 2000). The key factor was that there were two leader persons in the co-operatives who actively communicated with the members and the representatives of the interest groups and effectively directed the business activities of the co-operative. The co-operatives also had a team structure and the members continuously developed their competencies.

Methodology

The study was carried out in two phases. Firstly, the longitudinal documentation material of Pellervo (Confederation of Finnish Cooperatives), including all press reports about new co-operation in Finland in 1998-2001 and articles of new co-operation in the Finnish Journal of Co-operation in 1996-2005 was analyzed. The aim of this first phase was to identify the major strengths and weaknesses related to the co-operative organisational form as well as joint entrepreneurship in general. Extensive documentation material was used to obtain as broad understanding as possible of the strengths and weaknesses of Finnish competence-based co-operatives.

In the second phase of the study, the aim was to find out the success factors of the co-operatives and to research the impact of the co-operative form on the success of the firms. Identifying the success factors presupposes a deep and holistic understanding of the internal processes and structures of the firms as well as the experiences of the members involved in these organisations. For this reason the interview method was used. The information gained in the first phase of the study, especially the strengths and weaknesses found in the documentation material, formed the basis for interview questions and for understanding the success factors. In the second phase of the study, the persons interviewed in the co-operatives were asked to identify the most important success factors of their co-operatives and to explain them as extensively as possible.

The researched co-operatives in the second phase of the study were chosen from sectors in which several co-operatives have been established during recent years and which are showing growth. The selection criteria were: 1. The operations of the co-operative clearly focus on one of the chosen branches of the study: arts and culture, social and welfare, expert or

professionals' co-operatives; 2. The co-operative has been operating for at least for five years; 3. The co-operative has, to great extent, attained the aims set by the member/owners. The interviews were carried out between 22.9. and 10.12.2004.

The oldest of the researched co-operatives had been operating for almost 17 years and the newest for 5 years. Eight co-operatives out of ten had been operating at least for 7 years. The turnover of the co-operatives varied considerably: from 30,000 euros to over 3 million euros. The professionals' co-operatives had the largest turnovers and also the largest memberships. Four co-operatives out of ten had a turnover of more than one million euros. The smallest turnovers were in the arts and culture co-operatives. The aim of at least some of the members of these co-operatives was part-time employment.

The number of members in the researched co-operatives varied between 7 and 48. In the arts and culture co-operatives, the number of members varied between 15 and 20, in the social and welfare co-operatives between 7 and 9, in the expert co-operatives between 16 and 20, and in the professionals' co-operatives between 31 and 48. The professionals' co-operatives as well as one of the social and welfare co-operatives had employed workers in addition to the members; the other co-operatives employed workers only occasionally (for more information about the researched co-operatives and the interview themes see appendices 1 and 2).

Findings

Strengths and weaknesses found in the documentation material (the first phase of the study)

The following table presents the major strengths related to the co-operational organisational form as well as to joint entrepreneurship in general found in the press material of Confederation of Finnish Cooperatives.

The major strengths in regard to the co-operative form relate to organisational factors, the value basis of co-operation and some legal features. The organisational factors include the agile and flat structure and flexibility. People-centred values such as democracy, equality and solidarity originate from the democratic structure of a co-operative. The flat and flexible organisational structure and people-centred values contribute to social interaction, trust and solidarity of the members. These factors enhanced the management as well as motivated and committed the

Strengths Related to The Co-Operational Organisational Form		
Organisation	Value basis of co-operation	Legal features
<ul style="list-style-type: none"> • agile • flat; no hierarchy • flexible; suits people who look for a new way of working (distance working, part-time working) 	<ul style="list-style-type: none"> • people-centred values such as equality, solidarity and democracy appeal to today's people and motivate them 	<ul style="list-style-type: none"> • no starting capital needed; no great entrepreneurial risk • easy to join and leave a co-operative (e.g. compared to a firm of limited liability)
Strengths Related to Joint Entrepreneurship		
Equal ownership	Co-operation and synergy	Joint entrepreneurship
<ul style="list-style-type: none"> • equality due to equal ownership • opportunities to be involved in decision making and having an influence on the enterprise have a motivational effect on the members 	<ul style="list-style-type: none"> • different competencies complement one another; linking different competencies enables broader product or service offerings • support from others • social community 	<ul style="list-style-type: none"> • opportunities for self-employment (e.g. older people)

Table 1. Classification of the strengths of competence-based co-operatives.

members to the co-operative. Legal features such as no requirement for start-up capital and the ease of joining and leaving the co-operative were regarded as strengths. In some cases, however, they can become weaknesses in the form of a poor financial base and passive members. Joint entrepreneurship enabled the combination of several experts' skills and competencies as well as physical premises, equipment and marketing. Support from co-operation and synergy benefits were mentioned as major strengths of joint entrepreneurship.

The co-operational form produced some weaknesses. The weaknesses related to the co-operative organisational form as well as to joint entrepreneurship in general are presented in the following table.

The lack of a requirement for start-up capital led to passive members who did not actively work for and develop the organisation. The members also had a dual status: employee/employer. This dual status led to insufficient entrepreneurship when a member adopted only the role of an employee. When the co-operative grows, it can be difficult to determine the joining fees for new members. Agency problems such as slow and

difficult decision making processes and differing statuses of old and new members emerged in some co-operatives.

Internal conflicts sometimes occurred in joint entrepreneurship. New co-operation is not known in Finland and co-operation often suffers from a dated image. Many people regard a co-operative as a kind of an association, not a real form of a business organisation. On the other hand, in the field of arts and culture as well as in the social and welfare arena, the image of a co-operative as a not-for-profit organisation was even better than the image of a limited liability company.

Strengths and weaknesses found in the interviews (the second phase of the study)

The major advantages mentioned in the interview phase were due to joint entrepreneurship and the flexibility related to the co-operative form. The advantages of joint entrepreneurship included joint resources, support from other members (e.g. in decision making), open discussions, the opportunity to participate in decision making and advantages related to good co-operation. These factors motivated the members and had a positive effect on well-being at

Weaknesses Related to The Co-Operational Organisational Form		
Legal features	The dual role of the member	The dated image of a co-operative
<ul style="list-style-type: none"> no start-up capital; insufficient commitment of the members (passive members) 	<ul style="list-style-type: none"> employee/employer; often leads to insufficient entrepreneurship 	<ul style="list-style-type: none"> new co-operatives are not known co-operation has a dated image
Weaknesses Related to Joint Entrepreneurship		
Equal ownership	Co-operation and synergy	Joint entrepreneurship
<ul style="list-style-type: none"> co-operation does not function well; slow decision making the members have internal conflicts 		

Table 2. Classification of the weaknesses of competence-based co-operatives.

work. Good motivation of the members contributed to innovativeness and high quality of the work done.

There were some passive members in the successful co-operatives. These members acted as employees but not as entrepreneurs. However, the existence of the passive members was not a major burden in the researched co-operatives. A challenge of joint entrepreneurship was that in some of the researched co-operatives, the members had different aims and opinions which meant that the members had to balance the different views.

When the membership of a co-operative becomes large, the risk of conflict increases. In a large co-operative with more than 20 members, the danger of opposing groups exists. This had happened in one of the researched firms during a period of financial challenges. The situation was later resolved by better management and an improved economic situation.

A co-operative is a form of organisation with some specific features which can either be strengths or weaknesses. A major strength and at the same time a major challenge can be the flexibility linked to the organisational form. The fact that a co-operative needs no start-up capital suits competence-based businesses and the unemployed who want to start business. It may, however, lead to a poor financial basis. The ease of joining a co-operative is an advantage of flat and flexible organisations of the knowledge society. On the other hand, it may lead to insufficient entrepreneurship. Competent people, a good business idea, solid finances and a great amount of

entrepreneurial work are needed in order to succeed economically.

Success factors of knowledge-intensive co-operatives (the second phase of the study)

There is no uniform understanding of success in regard to co-operatives. According to Spear (2004), most members in co-operatives have no direct interest in profitability. In worker co-operatives, higher wages or better working conditions are likely to be more important than return on capital. The members' common aim is often employment. However, it is important to note that there are co-operatives which aim for growth and profit. In this study, three representatives out of ten stated that their co-operative aims for growth. One representative out of the three claimed that the objective of the firm is to make the best possible profit. Not-for-profit organisations are typical of the arts and culture sector in particular as well as of the social and welfare sector.

In this study, a successful co-operative was defined as a co-operative which had been operating at least for five years and which had, to great extent, fulfilled the aims of the owner-members. The major aim of the members in the researched co-operatives was to run a profitable business in the way that the members manage to employ themselves. In addition to employment, the members had other aims such as good co-operation and well-being. One of the interviewed persons argued that

“we are looking for well-being; working can be fun”.

Part-time working was preferred by some members in arts and culture and expert co-operatives. One of the reasons why members want to work less is that it gives them more time to do the work well. They are not in a hurry but can serve customers better which makes them happier and enhances their well-being. The co-operative business form seems to suit well the needs of today's workers as one of the interviewees stated:

"We have found a new way of working which is very modern and includes many advantages. Perhaps we are pioneers. Perhaps a co-operative is such a modern form of an enterprise that it is not widely understood. Even I do not always understand this form."

The following table summarizes the most important success factors found in all the researched co-operatives.

<ul style="list-style-type: none"> • Entrepreneurship in the form of stamina • Leadership in the form of directing the members towards common goals • Innovativeness • Continuous development of the activities • Good preparations of the business before the establishment of the co-operative • Good economy • Multiple networks and good relationships to interest groups
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Table 3. The success factors of the researched co-operatives.

Entrepreneurship, good finances and good preparations before the establishment of the co-operative were factors also found in the documentation material⁸ of the Finnish Confederation of Co-operatives. Leadership in the form of directing the members towards common goals, innovativeness, continuous development of the activities and multiple networks were factors which did not appear in the documentation material.

The importance of the above factors to the success of the co-operative varied in the researched co-operatives and also within one single co-operative over a period of time.

Entrepreneurship in the form of stamina was mentioned as the most important success factor in the majority of the interviews. Inevitably, entrepreneurship

is needed in all enterprises. In co-operatives, several members have to possess entrepreneurial skills. Many of the interviewed persons stated that perseverance is important, e.g., when negotiating different contracts in the social and welfare sector. During periods of economic difficulty, the members had been doing extra work. Some had been working without pay or lower salaries had been paid.

In every researched co-operative there are one or two persons who are the drivers of the firms. Because there are several owner-members in a co-operative, it is important that management is carried out well, coherently and in a manner which suits joint entrepreneurship. One of the members stated that

"commands and authoritarian leadership do not work in a co-operative."

Leadership carried out by these central persons has an effect on the quality of co-operation and on the motivation and commitment of the members. In the long run, the key members may change. This is why it is important that several members have management skills. In a small co-operative there is always the danger that the key members may overwork and become tired.

Innovation in the form of continuous development of new ideas and realization of projects is one of the success factors. The concept of innovation⁹ was discussed with the interviewees so that they gained the same understanding of the concept. Then they were asked, whether the co-operative form has any effect on innovation, and if so, which these effects are.

The findings show that especially, in the arts and culture sector, innovation is an extremely important factor affecting the firm's competitive capability. In the arts and culture sector, innovativeness means an ability to perceive trends and the ability to focus the business according to these trends. Innovation was also mentioned as a success factor in the social and welfare sector as well as in the expert and professionals' co-operatives but its importance was not as great as in the arts and culture sector.

A major advantage linked to the co-operative form which has an effect on success is flexibility. Flexibility appears in two ways. In many small co-operatives, the members can have an effect on how they work and how much they work. In expert co-operatives, many members prefer distance work, e.g. if they have small children. In the social and welfare sector, some people want to work only part time because of their age. This kind of flexibility motivates the members and makes it easier for them to live their lives. Another factor related to flexibility is that in many co-operatives, the members

have greater freedom than in traditional organisations to realize their own ideas. The following statements describe the flexibility:

“it would not have been possible to carry out certain crazy ideas in traditional organisations” and “to work in a co-operative means living with dreams; the worst thing is to kill people’s dreams” and “I have the freedom and opportunity to do the work I want to do. In a more traditional firm, I could not do that.”

The above comments show that flexibility of the co-operative form enhances the emergence of experimental ideas which can lead to innovations. The difference between a co-operative and a limited liability company can be seen in their basic nature. A co-operative is a member community and a limited liability company is a capital community. This difference is seen, for example, in the different aims of the firms. In a limited liability company there often is one main goal, which is growth. One member of a professionals’ co-operative stated:

“A co-operative is an environment which enables my working. The co-operative is not a value of itself which should grow but it is something which is needed so that I can work in peace. It is the enabler of my working.”

In a co-operative there may be several goals which, in the best case, are able to co-exist well. One interviewee stated:

“In co-operation, making money is not the only aim but the well-being of the members is also important. Economic and human issues communicate with each other in a good way.”

In practice, many co-operatives have to live with the pressure of different, sometimes conflicting expectations. A major challenge is to combine different expectations and wishes in a reasonable manner.

Continuous development of the firm’s activities includes the need for good planning of investments, personnel and marketing, development of effective ways of action and the quality of work, justified economic systems, and training of the members. Continuous development of the firm’s activities is linked to innovation. Innovative ideas are needed when developing the activities. In an expert co-operative, an interviewee stated that recruiting the right people is a very important issue. In all the researched co-operatives, development also means open discussions and taking into consideration the members’ different attitudes.

Good preparations of business activities before the founding of the co-operative are important. Because there are several owner-members it is important that the different aims and wishes of the members are discussed. The majority of the members in the researched co-operatives had had a joint training phase before the founding of the co-operative. The training period provided important business competencies and assisted in creating a community spirit.

Other success factors mentioned in every interview were good finances of the co-operative and multiple networks including representatives of different interest groups. The members always discuss the economic situation at their board meetings. An important issue is controlled risk-taking. Small co-operatives are careful when taking loans. Three co-operatives out of ten had taken loans for their operations. In the arts and culture sector, loans are needed for the realization of big productions. In the professionals’ co-operatives such as the truck drivers’, loans are needed because of the capital investments in the trucks.

The size of the membership is an important issue in competence-based co-operatives. Too large a membership may cause difficulties in decision making or team work. In all the researched co-operatives, the members had discussed the size of the membership and the policy on accepting new members. The majority of the co-operatives had a trial membership scheme or a requirement that applicants should first work in the co-operative before applying for membership. Most co-operatives were unwilling to accept new members because they already had their ideal number of members for carrying out operations. The co-operative with the largest number of members (48 members) had created a structure with self-managed teams.

The major factors typical of the different branches are summarized in the table as follows.

Theoretical contribution

The theoretical contribution of the study points to the co-operative form as a flexible instrument to enhance innovation in small firms. Innovation was one of the factors which contributed to long term success. In the study, innovation was defined as the ability to produce new ideas which could be concretized, e.g. in product development, marketing, sales, production, and logistics.

The flexibility of the co-operative form enhances innovation in three ways. Firstly, the structure is agile and flat which means that co-operatives are able to

<p>ARTS AND CULTURE</p> <ul style="list-style-type: none"> • there are economic risks related to artistic productions • the role of innovation is very important • the importance of the flexibility linked to the co-operative form is greater than in other researched branches • the non-profit image of a co-operative is a positive factor
<p>SOCIAL AND WELFARE</p> <ul style="list-style-type: none"> • the sector is going through structural change; new private actors are entering the market in addition to the public sector • entrepreneurship is moderate among the employees of the social and welfare sector • the not-for-profit image of a co-operative usually is a positive factor
<p>EXPERTS</p> <ul style="list-style-type: none"> • joint entrepreneurship enables the linking of the members' competencies and thus broader product or service offerings than an individual entrepreneur can offer • the flexibility of the co-operative form motivates the members to undertake part-time or distance work • there is no advantage due to the image of co-operation
<p>PROFESSIONALS</p> <ul style="list-style-type: none"> • the co-operatives are often founded following a possible bankruptcy or down sizing of a firm; the beginning phase is financially difficult • the members usually know each other well because of a common background • the aim is full employment and growth • there is no advantage of the image of co-operation; on the contrary the co-operatives have met prejudices, e.g. in the banking world

Table 4. Factors influencing the establishment of Competency Based Co-operatives.

react rapidly to customer requirements. The fact that the workers are the decision makers led to fast decision making. Secondly, the flexibility increases the members' intrinsic motivation, which has a clear linkage to creativity and innovation (Amabile 1998). Thirdly, the equality of membership enhances co-operation, mutual support and the sharing of knowledge and competencies. Good co-operation and the sharing of knowledge and competencies are prerequisites of innovation.

They strengthen members' intrinsic motivation and link different areas of expertise which may lead to new ideas and perceptions. Spear (2000) argues that well-

motivated members are likely to lead to efficiency gains. Davis, Schoorman and Donaldson (1997) state that if a mutual stewardship relationship exists, the potential performance of the firm is maximized. The following figure summarizes the effects of the co-operative form on the innovation of the firm.

The agency-theoretical flaws such as slow decision making were not found in the researched co-operatives. On the contrary, the interviewees described decision making as fast due to the agile and flexible organisational form. Multiple ownership was perceived as contributing to good discussions which enhanced business, as expressed by one of the members:

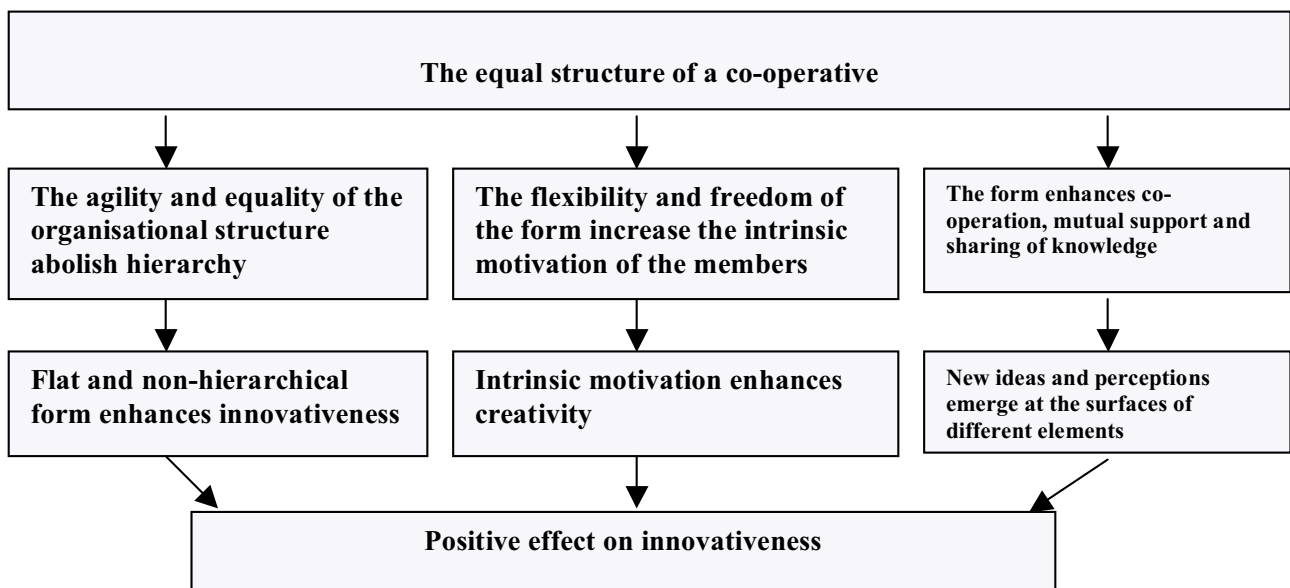


Figure 1. The effects of the co-operative form on the innovation in the firm

“A co-operative has the advantage that knowledge and competencies are shared.”

A major reason for the non-existence of the agency-theoretical flaws in the researched co-operatives might be their relatively homogeneous nature and small membership. As Nilsson (1996 and 2001) points out, no major agency problems emerge in co-operatives with homogeneous membership.

This study showed that good co-operation has a positive effect on the success of the firm in that it enhances innovation processes and motivates the members. New ideas were often born as a consequence of fruitful discussions and meetings of the members. The study showed that the active members are committed to the co-operative and motivated by intrinsic factors.

Conclusions

This paper has argued that the co-operative form has a positive impact on innovativeness in competence-based business. Innovativeness is one of the long term success factors of all firms and its significance will grow in the future as competence-based businesses increase in number. The co-operative organisational form is equal and flexible. It enhances co-operation and knowledge sharing because the members act from equal basis. In the competence-based business the core competencies of a firm often consist of the combinations of the members’ complementing competencies. A co-operative in which the members act from equal basis as joint entrepreneurs is a suitable

form of operating in the competence-based businesses.

In a society in which productivity and effectiveness are valued, there is a danger that employees become increasingly tired and depressed. The ageing of the population will increase this challenge. Organisational forms are needed which can employ older employees so that they can work according to their physical and psychological resources. Co-operatives have also employed disabled people.

The co-operative form despite its advantages, however, is not known or used very widely in Finland. Many of the researched co-operatives are pioneers in their fields of endeavour. Increasing networking, the growth of expert services as well as arts and culture firms and the striving of human beings to have an effect on their own working are trends which may increase the number of small, employee-owned firms in the future.

A competence-based co-operative is, above all, a form of enterprise which forms a network and a structure enabling self-employment rather than a company aiming to grow. It suits those sectors in which the competencies of the people form the most important capital of the firm, no large financial investments are needed and where the major aim of the owners of the firm is employment. In the sector of competence-based businesses, co-operatives may, however, have further opportunities for development as a flexible and innovative instrument for self-employment.

Notes

- 1 The term competence-based business means sectors in which the workers' competencies form the most important capital of the firm. These are sectors such as expert services (e.g. consulting, training), culture and media, social and welfare and professionals.
- 2 An expert co-operative refers to co-operatives of architecture, consulting, training, finance etc.
- 3 A professionals' co-operative refers to co-operatives of professionals such as truck drivers, textile workers and sign language interpreters.
- 4 In the study, innovativeness is defined as an ability to produce new ideas which can be concretized, e.g. in product development, marketing, sales, production, organizational processes and logistics. Innovativeness as a concept is very close to creativity. They have a slight difference. Creativity refers to the capability to produce ideas while innovativeness refers to the capability to produce and realize ideas.
- 5 New co-operatives are small co-operatives (delivery, marketing, worker) established in Finland from the 1990's.
- 6 A knowledge-intensive organisation is one that bases its competitive advantage on knowledge; and a knowledge-intensive product is one for which a large part of its added value is based on the knowledge incorporated in the product or its creation (Korhonen 1998).
- 7 Intrinsic motivation refers to a person's internal desire to do something. It is about passion and interest. The work itself motivates when the work is challenging (Thomas 2000).
- 8 The documentation material included press reports about new co-operation in Finland in 1998-2001 and articles of new co-operation in the Finnish Journal of Co-operation in 1996-2005.
- 9 In the study, innovativeness is defined as an ability to produce new ideas which can be concretized, e.g. in product development, marketing, sales, production, organizational processes and logistics. Innovativeness as a concept is very close to creativity. They have a slight difference. Creativity refers to the capability to produce ideas while innovativeness refers to the capability to produce and realize ideas.

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Appendix 1. The researched co-operatives

Arts and culture

Osuuskunta Lilith, Kikke Heikkinen, 11.11.2004

- production of music, videos and advertisements, organising of events and training
- year of establishment 1997
- number of members 20

Osuuskunta OTS Kapsäkki, Nina Maskulin, 26.11.2004

- production of artistic shows and programs
- year of establishment 2000
- number of members 15

Taideosuuskunta Piellos, Inkeri Rosilo, 10.12.2004

- dancing, theatre, music, visual arts
- year of establishment 1997
- number of members 18

Social and welfare

Osuuskunta Toivo ja Kumppanit, Coop Hope Co, Mikko Makkonen ja Eero Riikonen, 22.9.2004, 7.10.2004

- psychological therapy, social training, research and publishing

- year of establishment 1997
- number of members 9

Helsingin Idelia Osuuskunta, Marina Vesterinen, 9.11.2004

- children's day care
- year of establishment 1997
- number of members 7

Hoivaosuuskunta Näsin Helmi, Heikki Mäntynen, 17.11.2004

- wellbeing, medical care, social, cleaning and household services
- year of establishment 1998
- number of members 8

Experts

InnoTyöverkko Osuuskunta, Tuomas Seppänen, 15.11.2004

- business development, marketing and communications, development and wellbeing of personnel
- year of establishment 1994
- number of members 16

Arkkitehti- ja Insinööriosuuskunta Kaari, Tytti Tolvanen ja Sini Siitonen, 24.11.2004

- architecture and interior design, technical repair design
- year of establishment 1996
- number of members 20

Professionals

Kilon Osuus-Auto, Ari Savisalo, 9.11.2004

- truck drivers' co-operative
- year of establishment 1989
- number of members 31

Viittomakielialan Osuuskunta Via, Outi Huusko, 9.12.2004

- a co-operative of sign language interpreters
- year of establishment 2000
- number of members 48

Appendix 2. The interview themes

1. Basic facts about the co-operative

- Year of establishment
- Reasons for the establishment
- Background of the members
- The number of founder members, the present number of members, employees

- The business sector (the most important competitive advantage of the sector), products and services

- Turnover and its development

2. The aims of the co-operative

- Different aims of the co-operative; economic, social, other

- Attainment of the aims

3. Success factors

- The most important success factors of the co-operative

- The possible effect of the co-operative form on success

- The greatest challenges the co-operative is facing

- Challenges of the business sector

4. Strengths and weaknesses of the co-operative form and joint entrepreneurship in general

- Possible strengths of the co-operative form and their effects on the business

- Possible weaknesses of the co-operative form and their effects on the business

- Strengths and weaknesses related to joint entrepreneurship in general

Co-operatives and Taxation in India

Veena Nabar

Introduction

The subject of co-operative tax, issues as to whether co-operatives should be taxed at all and treatment of rebates/exemptions etc. is a much debated one. On the one hand, the nature and objectives of co-operatives provide the basis for the way in which it is pointed out they should be treated under the tax regime, the moot point being that co-operatives operate under the co-operation and mutuality principle and hence should be recognized as distinctly different business entities under the tax system.

As against this, it has been posited that one of the policy design principles of any tax legislation should be economic substance over form:

Economic transactions should be taxed on the basis of their economic substance – not their legal form. If there are tax advantages in deriving income through one type of entity rather than the other, that output puts form (the type of entity) before substance (economic income)¹.

Even this statement however is not inconsistent with the recognition that the nature of a co-operative's business with its members determines its eligibility to be tax exempt. A co-operative is an extension of the businesses of its owners. Its primary purpose is to provide services to assist members and their operations gain access to previously inaccessible markets, achieve savings on inputs to the members' businesses, and provide services that are not available from other sources.

The owners of a co-operative are people, entities or businesses that use its services. While Co-operative Acts in some cases do and should require that any person who ceases to use co-operative services ceases to be a member, and similarly that a major part if not the whole (say 90%) of business done by a co-operative must be with its members for it to qualify as a co-operative for tax purposes, it must be recognized that co-operatives and companies differ in a number of fundamental ways as presented below²:

1. Co-operatives operate under the principle of mutuality whereas companies operate under the profit first principle
2. A co-operative earns income from its member owners who participate in the services or

processes of the co-operative. A company earns its income its from persons who are primarily investors

3. As mutual enterprises, cooperatives do not have access to the range of financing instruments available to companies
4. The capital base of a company is protected by law, making it easier to raise debt finance to expand its activities. The capital base of the co-operative is, however, not protected by law and the number of issued shares in a co-operative varies according to the number of persons who are members at any given time
5. Shares in a co-operative can only be held by persons who use the services of cooperatives, whereas shares in a company are available to anyone who can afford to purchase them
6. Distributions made by a co-operative are largely treated as rebate to the member in proportion to the business done by them with a cooperative

Economic transactions with members of a co-operative are generally regarded as being on an at-cost basis, with any surplus distributed to members being regarded as a rebate, which is in effect a means of returning the difference between the final cost and the price charged to the member. It is essential that any tax legislation should recognize this mutuality principle that informs co-operative transactions.

The tax deductibility of rebates and bonuses is logical for agricultural co-operatives. In many sectors of primary industry goods/commodity are supplied to the co-operatives by members before the selling price is known. When prices are finalized, the co-operative has three choices in the case where surpluses result as follows:

1. Earned surpluses either in full or part treated as profit
2. Earned surpluses either in full or part accounted for as profit and forwarded to farmers as return on their capital i.e. dividends and
3. Earned surpluses either in full or part returned to the farmer suppliers in proportion to business conducted. Such resulting rebates, bonuses or back pays will be deemed to be purchase expenses and reduce the profit of the cooperative.

The emphasis of co-operatives is to return surpluses as a proportion of business conducted rather than as a return on capital. Thus rebates, bonuses and back pays feature prominently in the expense section of the profit and loss statements of most co-operatives.

The Indian case

The mutuality principle of co-operatives has been accepted in the Indian treatment of co-operatives for the purpose of taxation to a large extent, but only for primary co-operatives. In India, the Income-tax Act 1961 lays down the statute in respect of taxation. Section 80-P of the Income-tax Act, which replaced Section 81 which was the original section dealing with Co-operative Taxation in India's Income Tax law, by Finance (No.2) Act, 1967 w.e.f. 1.4.1968, governs the exemption, deduction, or taxation of co-operative societies for different types of income. The conditions, qualifications and limits of income of co-operatives eligible for exemption or deduction under both sections are almost the same except that Section 80P now provides for straight deduction, total or partial, of specified income instead of rebate as was provided under the original section. The Section 80-P itself has undergone several changes through several amendments introduced over the years, with the scope of exemption being changed by these amendments.

Section 80-P³ provides that any income of a co-operative society referred to in sub-section 2 of Section 80-P should be deducted from gross total income for computing income for tax purposes. The provisions for computing the total income of the assessee are both partial and total.

Co-operatives are also entitled to deductions under other sections of the Income-tax Act {Section 80HHA, 80 HHDM 801, 801A, 80J, 80JJ}, which are applicable to different categories of business or institutions across the board. The deductions eligible under these sections are first reduced from the gross total income to arrive at the income of the societies, which is then eligible for deduction applicable to co-operatives under the clauses of Section 80P(2).

Tax Exemptions for Co-operatives

The activities of co-operatives which are eligible for complete exemption from taxation under Section 80(P) are:

1. *Carrying on the business of banking or providing credit facilities to its members*
 - Providing credit facilities to members has been variously interpreted under various case laws⁴.

- Would comprehend not only the business of lending money on interest, but also the business of lending services for guaranteeing payments.
- The facilities of selling goods on credit to members is an activity of the business of selling of goods of which credit facility is only an incidence; it will not amount to providing credit facility to its members.
- Providing credit facilities to members means credit by way of loan and not selling goods on credit.

2. *A cottage industry*

A large number of weavers' cooperative societies⁵ have stated that deduction under section 80P(2)(a)(ii) has been denied to them merely because some payments have been made by them to outside agencies for dyeing, bleaching and transport arrangements. What constitutes a 'Cottage Industry' has been the subject-matter of discussion in a number of cases decided by various courts. Based on the ratio of these decisions, criteria have been laid down for a cooperative society engaged in cottage industry to avail the benefits under section 80P. In the case of a weaver's society, it has been clarified that so long as weaving is done by the members of the society at their residences or at a common place provided by the society, without any outside labour, such a society will be eligible for deduction under the section even if certain payments have been made to outside agency for dyeing, bleaching, transport arrangements etc., provided it satisfied all other conditions necessary.

3. *The marketing of agricultural produce grown by its members-*

The following clarifications emerge from various concerned case laws: Marketing is an expression of wide import and generally means⁶ performance of all business activities involved in the flow of goods and services from the point of initial agricultural production to the ultimate consumer. The marketing functions involve exchange functions such as buying and selling, physical functions such as storage, transportation, processing and other commercial functions such as standardization, financing, market intelligence etc.

4. *The purchase of agricultural implements, seeds, livestock or other articles intended for agriculture for the purpose of supplying them to its members*

Water has been judged as an article intended for agriculture⁷, accordingly water charges paid to the State Government by a society supplying water to

its members for purposes of cultivation are allowable as deduction.

5. *The processing, without the aid of power, of the agricultural produce of its members*
6. *The collective disposal of the labour of its members*
7. *Fishing or allied activities*

That is to say, the catching, curing, processing, preserving, storing or marketing of fish or the purchase of materials and equipment in connection therewith for the purpose of supplying them to its members, the whole of the amount of profits and gains of business attributable to any one or more of such activities.

Various Case Laws dealing with the Section 80P⁸ have mentioned the following:

- A liberal construction should be given to Section 80P and in case of a cooperative society having several objects, if it is established that the cooperative society is engaged in any of the activities falling under section 80P(1) or (2) (a) that would suffice to enable the society to claim the benefit of deduction, subject to such other provisions as enumerated and applicable.
- The society is not dis-entitled from claiming exemption only because it carries on certain activities, income from which is not exempt. The correct approach would be to grant exemption to the whole amount of profits and gains attributable only to actual sales or specified commodities to members.

In case of co-operative societies dealing with labour or fishing and allied activities, the Income-tax Act also provides that the exemptions would be contingent upon the society bye-laws restricting voting rights to the individuals who contribute their labour, co-operative credit societies that provide it with financial assistance or the State Government. Similarly, in case of primary co-operative societies engaged in supplying milk, oilseeds, fruit or vegetables grown by its members, such income is exempt from taxation provided that it sells its product to a federal co-operative society also in the same product line, the government or a government company. Other than these activities, co-operatives under section 80P (2) (c) are provided with a general exemption for consumer co-operatives (presently amounting to Rs 100,000/-) and in other cases (presently Rs 50,000/-).

Any income by way of interest or dividends derived by any co-operative society for its investment with any

other co-operative society is also fully tax exempt. Similarly, income derived by a co-operative society from letting out of godowns or warehouses for storage, processing or facilitating the marketing of commodities is fully exempt.

Recent tax changes to the Indian co-operative banks

In the last financial year, Co-operative banks, which were previously never under the ambit of income tax for the past hundred years of their existence, were brought into the tax net with introduction of the new sub-section 80P(4) withdrawing deduction earlier available to them under Section 80P(2). Accordingly, income-tax exemption is now allowed only for primary agricultural credit societies or primary co-operative agricultural and rural development banks.

The various reasons put forth by the government while levying tax on co-operative banks have been countered by the National Federation of Urban Co-operative Banks and Credit Societies Ltd. (NAFCUB) as below⁹:

Co-operative banks, like any other bank, are lending institutions and should pay tax on their profits.

This has been countered by pointing out that commercial banks and co-operative banks are not comparable. There is a significant difference in size, expanse, range and spread with average per bank net profits of commercial banks being a 100 times that of Co-operative Banks indicating that a large number of co-operative banks make marginal profits. The clientele of the two types of banks is also different - while commercial banks are accessed by high net worth individuals, corporate sector, government, municipal corporations, public sector undertakings etc., co-operative banks largely cater to people of small means and the marginalized. The limited area of operation and avenues of business of co-operative banks restrict their scope for spreading of risk, unlike commercial banks, which have no limits on geographical functioning and can entertain diverse business activities.

Co-operative banks also have limited avenues for earning. Unlike commercial banks whose income largely derives from fund and fee based activities, cooperative banks derive their income from lending and deposit collection. Similarly, there is a disconnect of capital markets and cooperative banks, which raise shares only from members and cannot issue instruments as do commercial banks. Co-operative

banks have more of directed lending and a limited surplus. The cost of funds of co-operative banks tends to be higher due to the nature of funds raised unlike commercial banks, which can access low cost funds and high volume float funds and government business. Finally, it has been argued that the total net profit of all cooperative banks is so insignificant that tax collection would also be further insignificant.

Co-operative Banks will be compelled to improve financial and accounting discipline only if they are brought under the tax net; and Co-operative Banks do not get their accounts audited.

It has been argued that cooperative banks have standardized accounting norms, draw up balance sheet as per RBI directions and get their accounts audited either by Chartered Accountants or Auditors of the Audit department of State Governments.

Nearly half of the co-operative banks are incurring losses and others will also incur losses, if they are not disciplined.

The NAFCUB argues that lack of timely support by way of infusion of funds has aggravated the problem and the losses of cooperative bank cannot be arrested by imposing income-tax. Constraints of size, professional competence, limited resources and access to low cost of funds are the issues which ought to be addressed at this juncture instead of imposition of income-tax. Disclosure norms, statutory audit etc. are all adhered to.

Only a small fraction of cooperative banks are brought under the tax net.

All co-operative banks without exception have been brought under the tax net. The few primary rural development banks which have been left out are not recognized as banks under the Banking Regulation Act.

Tax forgone under section 80(P) for co-operative banks is around Rs 1500 crores per annum.

The figure it is pointed out is much lower as per the RBI estimate.

Co-operative Banks are not Mutual Organizations and therefore cannot be treated on the principle of mutuality; and Co-operative Banks actually admit anyone as nominal members to fulfil norms on paper.

Co-operative Banks are predominantly mutual organizations with a very high percentage of their earnings coming from business with their members. Nominal member admittance is governed by the RBI stipulation.

As a general argument, it is pointed out that all countries recognized the need for a separate treatment

of taxation of cooperatives and do not impose income-tax on cooperatives including Co-operative Banks. The Co-operative Banks in India cater to a segment of population which is on the fringes and economically deprived. Even in the United States, the cooperative credit structure is subject to income-tax exemption. With taxation, banks will find it difficult to augment their results and make provisions for NPAs. It is argued that the move would have cascading ill effects.

The impact on higher tier co-operatives

It needs to be noted that Section 80P does not help a large category of co-operatives¹⁰, particularly the secondary and tertiary ones in the agricultural sector.

Processing co-operatives are denied the benefits of exemption even at the primary level, if they process member produce with the use of power. Sugar co-operatives for instance are primary societies and have to necessarily process their member produce with the aid of power, as soon as it is harvested as sugarcane is highly perishable. Hence while in effect, sugar can be claimed to be as much the produce of the members as sugarcane, it is not considered as such. This leads to iniquitous treatment for the sugarcane farmer, who may be at the same marginalized level of income as his counterpart growing agricultural produce other than sugarcane but is denied the benefits of favorable tax treatment, which the latter gets.

For assured off-take of their produce at a remunerative price, the farmers through their primary cooperatives have to go in for at least a second level cooperative, which would process (with the aid of power for any reasonable scale of production), and market their produce. Thus, if the farmers for strengthening their secondary or tertiary co-operative settle for a lower price to ensure retained earnings, a large percentage of this gets taxed away. This obviously discourages the build up of equity through retained earnings. "Merely because a primary is federated at district and state levels, it is unfair and fallacious to tax each tier for income as if they are separate entities. This becomes amply evident when we consider by analogy, a private enterprise that undertakes under one name all the activities that are performed by different tiers of the co-operative system and is therefore liable to be taxed for income in only a single instance.

There is a simple yet legal method for co-operatives to avoid being eligible for payment of income-tax. That method is to pay to the members, price differentials for their supply. However, this approach has severely undermined capital formation in co-operatives and consequently their growth"¹¹.

Conclusion

Co-operatives have to be recognized for what they are viz. their mutuality and this entitles them to special treatment in terms of the nature of their economic transactions with their members. The Indian case implicitly for a major part recognizes this mutuality, but restricts it only to primary co-operatives. More recently co-operative banks other than primary credit societies and primary rural development banks have also been exiled from the magic circle. The exclusion of co-operatives, from the exemption benefits, even primary ones that process member produce using power, is also highly iniquitous.

It is important that the mutuality aspect of the co-operative institutions, of all kinds and at all levels, is given due recognition in tax law. All co-operatives in consideration of the special nature of their economic transactions with their members should be eligible for equitable treatment and favorable consideration under the Tax regime. The case of secondary and tertiary co-operatives which are extensions of the primary co-operatives in terms of mutuality also needs special treatment and recognition.

Notes

- 1 Cooperatives Council of Australia Inc (1998): Cooperatives – Australians Extending their own Business.
- 2 Cooperatives Council of Australia Inc (1998) – ibid.
- 3 Govt. of India (2007): Income Tax Act, 1961, Rules & Regulations.
- 4 Tax Mann (2007): Direct Taxes Manual, Vol. 2.
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Challenges of Leadership and Professionalisation of Management in Co-operatives

L.D.Ahuja

Introduction

The Co-operative Movement in India is now 100 years old. It has played a pivotal role in the country's economy. This has been possible mostly due to committed leadership. As a matter of fact, the co-operatives have been acting as nursery for providing leadership to the country.

Today, when the movement stands at cross roads and is expected to poise for a major breakthrough in the wake of challenges posed by globalization and free market economy, unfortunately it is baulked and saddled with somewhat dwindling of committed leadership and lack of professional management. These days, upsurge is being witnessed in all walks of life all over the world. There is vibrancy in the air and establishments are seaming with leadership of a different kind who are equipped with the capacity not only to deliver themselves but are increasingly, ever than before, have become capable of taking the entire organization along with them.

Indian Co-operative Movement is, however, caught in the whirlwind and onslaught of market forces which enjoins upon the leadership not only to extricate it from morass but resurrect the same to its pre eminent place. This of course is a daunting task but not above their domain as there is resilience in the movement and it has taken deep roots in our system. Knowledge, capability and hard work are the hallmarks of a leader and bench mark for the generation both present and future. A leader must know when to be authoritative, participative and also when to delegate. A leader must be endowed with leadership and managerial skills either inborn or acquired. It is the onerous responsibility of a leader to run the institution as per its avowed objectives, lay down firmly the systems and invariably develop second line of leadership and so on.

Gone are the days when organizations were run on the whims and fancies of the leaders, possessors of capital and therefore of tools of "progress and development". Today, the entrepreneurs themselves are management experts and/or are aided by professionals of proven merit. They work as a 'Team' on the principles of delegation of authority and ensuring accountability. There is definitely more need

of these qualities in a leader of a co-operative organization because on the one hand he is expected to deliver the results and on the other he is supposed to hold the principles of co-operation dear and close to his head and heart.

The state of affairs of co-operatives in India

The Co-operative Movement in India is widely dispersed and covers a wide gamut of activities. Unfortunately, the misdirected politics of some political leaders who have entered the movement has caused more harm than good. The role of the State which is supposed to be a facilitator of public welfare and good has become problematic and the result is co-operative movement enslaved and bogged down by unwieldy rules and regulations. Like all walks of life, corruption too has raised its ugly head. For some co-operatives servant leadership has been replaced by selfish leadership.

The very idea of forming a co-operative is the removal of the institution of middleman. However, hat is really happening is that the middlemen have joined the co-operatives and thus hijacked these associations to further their own interests. Such people are unwittingly aided by the political travesty of legal framework for co-operatives in India that acts to prohibit their independent and autonomous functioning. Generally all over the world, co-operatives are autonomous bodies strengthening the social economy and civil society with governmental control and surveillance limited to the norms for ensuring good governance. This principle is being undermined in India where politics has struck at the very root of co-operatives.

Instances have come to notice where the primary milk producer societies supply milk to unions along political lines/ affiliations with utter disregard to economic viability. In the election of one federation, the voters were lured and entertained lavishly in a hill resort in the country to garner their votes. Many co-operatives have started hiring consultants who in connivance with the officers of financing institutions are able to secure loans, with utter disregard to the viability of the projects. Though such instances are still

unrepresentative of the movement in general they surely have brought disrepute to the movement as a whole.

The amount of state control of co-operatives in India has also led to the co-operatives developing a culture that is inimical to handling change and innovation. One clear evidence of this is to be found in the fact that co-operatives have a poor of adopting successfully appropriate technologies. The current situation requires a lot of soul searching. Corrective steps are required otherwise, the movement could be heading for decline and co-operatives will become the thing of the past. A great responsibility is thus cast on the current leadership who operate in this difficult regulative and cultural context. A lot will depend on their capacity to deal with these challenges in a principled co-operative spirit and perspective.

Yet sadly professionalism has taken a back seat in co-operatives. In a business organization, either professionals have to be placed at appropriate places or officials and lay-members and staff trained and equipped in a manner appropriate to their role in the organization and with the knowledge, skills and ethics that underpin a professional approach to management and operation. It may not be possible for each and every co-operative to afford the services of a professional. Therefore, the second alternative could prove to be more appropriate and productive providing the existing incumbents have the capacity and the motivation to develop both themselves and their co-operatives.

AMUL – Great example of leadership & professional management

The marriage of convenience between the leadership like Tribhuvandas Patel and professionals like Dr. Verghese Kurien led to the birth of AMUL which had a cascading effect and turned India into the largest producer of the milk in the world. This association empowered the poor people into productive members of the society. Dr. Kurien did not belong to Gujarat, yet he dedicated his entire life to the dairy co-operatives in this State. India's dairy industry became the largest rural employment provider and has more than doubled farm family incomes. The dairy co-operatives have become powerful agents of social change in empowering women and embedding democracy at the grass roots level. One cannot but wonder what India would be today if we had a thousand servant leaders like Dr. Kurien with his type of vision and commitment, dedication and national spirit. Such leadership is what

the co-operative movement must facilitate if the power of the ordinary people of India is to be mobilized for the welfare of Indian and indeed global society.

If we combine this farmer power with professional management, what could they not achieve? What could India not become? Dr. Kurien remained employee of farmers all his life and worked for social good. For persons like him money is not the only satisfaction. There are several other forms of satisfaction. In a co-operative, it is opportunity for professionals and leadership to serve their own people, most of them small and marginal farmers, landless labourers, youth, women folk and disadvantage sections of society. This is a home grown example of the servant leadership model of co-operative leader that the movement's management training and development practices should embrace and whose characteristics its executive and management recruitment and selection specialists seek to identify in potential recruits to management and board positions in co-operatives.

The interference of the government in co-operatives cannot but undermine the ultimate goal of all co-operatives to strengthen autonomy and community providing for a genuine independent civil society which lies at the foundation of any true democracy. In terms of an efficient pluralist and free market the work of the government is to regulate and facilitate co-operatives but they ought not to control them as this will hinder not enhance their development and efficiency. It is the duty of the leaders to vest people with power. Today, co-operatives cover 11 million dairy farmers in 24 States of the nation. Dr. Kurien was helped in his mission by political leaders like Sardar Patel, Morarji Desai and others. They believed "where co-operation fails, there fails the only hope of rural India." Dr. Kurien developed a model where people were at the top, professionals were their employees to provide technical, administrative and other strengths. Indians are an extremely intelligent people but we can progress only when we learn the secret of unleashing this positive power of people.

While loyalty and integrity are core values, there are other values too, which are a pre-requisite to achieve in any field. For example, the leader has to set a personal example and make others understand in what way 'change' is going to be useful. Managers and executives working in co-operative organizations must have clarity of thought and professional knowledge combined with a commitment to the values of economic democracy and service to others. They must enjoy enough

freedom to perform and adequate opportunities to work as a community of professional practice embedded in the economic and social community of their co-operative members. In Dr. Kurien's words "I was vastly benefited from the services of hundreds of truly outstanding young women and men who worked with courage, with unparalleled commitment, with little financial reward and less fame."

The problem with most co-operatives in India is not that politicians become Chairmen. It is that when they become Chairmen, they use the co-operatives to further their own political ends. AMUL had the distinction of having a Chairman of high integrity. The maximum salary Dr. Kurien ever drew was Rs.5,000 as Chairman and General Manager of Gujarat Co-operative Milk Marketing Federation. Dr. Kurien fought against the vested interests of unscrupulous politicians, bureaucrats, businessmen or institutions all his life. The creation of Institute of Rural Management (IRMA) for producing managers to make up for India's current deficit of managers in rural co-operative and other people centered organizations, committed to equitable and sustainable development is a positive development. Growth leads often to diversification of the activities which also is putting added pressure on the limited management capacity in many co-operatives that are growing successfully.

Recipe for co-operatives

Leaders have to be well informed and they should lead by example. Another challenge to the quality of leadership in India is that often the Chairman himself and / or his colleagues continue to enjoy the position for decades together when clearly new blood is needed. In this situation, the role of educated youth and the middle-aged assumes great significance. It is unfortunate that youth in particular are hardly evincing any interest in the co-operatives as the old leadership is seldom interested to yield its place to the rising generation. It is also a fact that no census of involvement of youth in co-operatives has been carried out. Another issue is how to overcome exclusion with induction of more women in the affairs of the co-operatives. A further important question arises in terms for the determination of appropriate expenses and levels of remuneration for co-operative lay and professional leaders.

What is the primary job of an efficient leader/manager? It is to bring in and groom the right people for their team. Once this is done, the manager must groom a successor that will be most appropriate for the organization.

Four crucial factors have to be borne in mind. Co-operatives:-

- i) Must acquire and equip themselves with the appropriate modern technology;
- ii) Must define 'standards' necessary to achieve and maintain world class quality;
- iii) Must put in place systems which will ensure that they consistently achieve the standards they have set for themselves;
- iv) Must adopt co-operative values as part of the tools and culture of both the organizational and associational aspects of the co-operative led from the very top.

These four requirements will not be implemented effectively without the adoption of a co-operative value based servant leadership at the core of the of the movements professional development strategy. These leaders will need to have the capacity to have in their team people with technology know-how, understanding of the key skills and techniques to develop good quality standards through customer relationships and member relationship standards and through the maintenance of close supplier relationships. It is also vital that the new breed of co-operative servant leader's are able to appoint staff who understand market research and have the capacity to adapt it to the co-operative purpose and values.

Professionalisation of management of co-operatives

Co-operative movement in India is the largest in the world with 5,83,580 co-operatives having membership of 242.004 million covering 71% of the households and 100% of villages. Direct employment generated by this sector is 1.20 million and self-employment generated is for 15.42 million persons. Providing leadership and professional management for such a large assembly of co-operatives is a Herculean task. It is essential that this is accomplished at the federal and large primary society level as a first step.

In the immediate context there is still an urgent need at the village and small primary society level of persons with sound basic skills and positive co-operative attitudes towards their fellows in the village community. These persons must have sound knowledge of the activities with which a co-operative is concerned in addition to maintenance of accounts and records. For example, a secretary and manager of a primary agriculture credit society must have the knowledge of the crops grown in the area of its

operation, inputs required, arrangements for timely supply of inputs, preparation of business development plans (BDPs), maintenance of stock/issue registers, preparation of balance sheet, furnishing of information to various authorities including BOM and arranging extension services, marketing of agricultural produce etc. to the best advantage of the farmer members.

It is appropriate that the Secretary should be an agricultural graduate or the capacity built accordingly. Similarly, handloom co-operatives must be guided about the latest designs, costing of the products, marketing strategies which are crucial inputs. Fishing co-operatives must have sound knowledge of pisciculture, maintenance of equipment, sale strategies etc. The poultry cooperatives must be oriented about the economies of scale, input cost and prevailing rates of products on day to day basis which can make or mar the institution. For all this, a great amount of expertise needs to be developed and professional touch ingrained. Secretary/Manager should be adequately paid.

National Co-operative Union of India through its country – wide network of training and education right from grass root to the national levels has been playing a crucial role in developing all sorts of expertise in the co-operative sector. It has embarked upon a unique project of establishing Jawahar Lal Nehru Co-operative International University to produce young managers and professionals for the co-operatives. It must be hoped that this important initiative of a Co-operative University will, when operational, go a long way to finding solutions to the many vexed issues of co-operative development including how they can better identify and develop their lay and professional leadership / management befitting the present times.



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Edited by Yair Levi

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Co-operative Housing Movement: creating safer cities and building vibrant communities

M.L.Khurana

Urbanization around the world

In 1800 only 2% of World population lived in towns of more than 5000 inhabitants and not more than 45 cities had population over 1,00,000. In 1900, cities were home to just 9% of the planet's population. However, 19th and 20th Century witnessed enormous growth of urban population and cities were not only able to sustain the pressure of increased population but also could not provide conducive environment and services to new entrants.

According to latest U.N. Report "State of World Population-2007 - Unleashing the Potential of Urban Growth" as of 2008, more than half the world's current 6.7 billion people will live in cities. Though mega-cities (more than 10 million people) will continue to grow, most people will be living in cities of 5,00,000 or fewer. By 2030, the urban population will rise to 5 billion or 60 per cent of World population. Globally, all future population growth will take place in cities, especially in Asia, Africa and Latin America. In Asia and Africa, this makes a decisive shift from rural to urban growth. The report adds that the rise in urbanization is inevitable and should be considered a positive development. No country in the industrial age has achieved significant economic growth without urbanization.

The United Nations population projections as presented in Table-1 shows that the growth of cities having more than 1 million population shall be more prominent in Asia, Africa and Latin America by 2015.

These cities would experience rapid population growth and consequent inadequate investment in environmental infrastructure or services. Again, the reducing availability of land coupled with sky-rocketing land prices compels people to take shelter in the urban peripheral areas. It also results in establishing squatter settlements that exhibit virtual mushroom growth thereby increasing urban population with declining civic amenities.

The factors for increasing cities population are more jobs in industry and service sectors than in agriculture and presence of agricultural opportunities in urban areas. The other contributing factors include better civic services, employment avenues, newer family formation etc. etc.

The Report urges upon city authorities and urban planners to make it a priority to provide shelters for the urban poor. They should offer the poor secured tenure on land outfitted with power, water and sanitation services. Those living in poor communities should have access to education and health care and should be encouraged to build their own homes.

Region	Total Population in all cities with more than 1 million residents (Population in Millions)			
	1950	1970	1990	2015
Africa	3	16	59	225
Latin America	17	57	118	225
Asia	58	168	359	903
Europe	73	116	141	156
North America	40	78	105	148

Table 1: Population in cities with more than 1 million population per Region (1950-2015)

Source: United Nations (U.N.) Population Division, World Population Prospects: Revision (UN, New York, 2004)

Today cities are reaching the limits of their carrying capacity to sustain human life. As the size of cities grow, pressure increases on basic services, infrastructure, housing. At present, cities are growing at such a fast pace that life is becoming miserable due to rising expectations and aspirations beyond the available means. This is a phenomenon found in most developing societies. Unemployment, rising prices, frustration contributing to corruption, delinquency, theft, crime and use of drugs etc. are the prominent causes that make people feel insecure particularly in big cities.

Social and environmental problems in cities

The cities around the world are facing a variety of social and environmental problems e.g. pollution, unemployment, poor health and absence of education. It generates societal crime because poverty and deprivation is the chief cause of eternal and perpetual crime.

During mid 70s and 80s, reported crimes world-wide increased by 5% per annum which was much faster than the growth in population. In the United States, there are two million victims of violent crimes every year. Four children get murdered every day in Brazil; while in Germany approximately 4 million women suffer from domestic violence. In Indian context, the Delhi High Court has rightly held that crime situation in the Capital was getting worse and has advocated strict action against the perpetrators.

The other major reason for violence, intolerance and social unrest is due to inequality and unjust distribution of fruits of development. The richest 2 per cent of adults still own more than half of the world's household wealth, perpetuating a yawning gap between rich and poor. The report from the Helsinki-based World Institute for Development Economics Research shows that in 2000 the richest 1% of adults (mostly living in Europe or the United States) owned 40 per cent of global assets. The richest 10 per cent of adults accounted for 85 per cent of assets. By contrast, the bottom 50 per cent of the world's adult population owned barely 1 per cent of the world's wealth.

Another Study have observed that in countries of European Union the social disparities within cities and also between city and region have widened. Urban safety and increasing feelings of unsafety have become a major issue. Besides, affordable housing is a Central urban issue in majority of the member countries of the European Union.

The consequences of looming urban violence are manifold. It not only destroys men and material but also breed suspicion and insecurity amongst human beings, resulting in intolerance, isolation and even violent reactions between the constituents. The phenomenon of urban violence is also bringing about major changes in the patterns of daily living. It has been observed, of late, that in some cities, cases of violence and insecurity curtail people's movements and even use of public transport. Grippled by fear, people particularly women dare not frequently come into streets, parks and other public places. The self imposed social isolation extended to large sections of the urban population thus adversely affects their mobility and consequent loss of productivity.

To tackle these problems, the governments have to drain out scarce resources for developmental work relating to upkeep of schools, parks, libraries etc. and combat other maladies e.g. drug-abuse, etc. for promoting societal homogeneity and stability. It is imperative to do so in order to curb the possibility of potential urban violence that may be caused due to prevalence of disparities between the poor masses and rather a minority section of economically affluent people who control the social and economic infrastructure in urban regions. Notwithstanding the fact that the urban violence is not a spontaneous phenomenon, it is rather the product of a society characterized by inequality and social exclusion.

Role of housing co-operatives

No community can afford to neglect the welfare of such a large number of its citizens suffering from evils of poverty, inadequate housing, health, education and basic services etc. They need to be made partners in every development programme through the medium of co-operatives to yield better results. The essence of co-operation is that individuals come together to achieve as a collective group what they cannot achieve as individuals.

The main objective of a housing co-operative is to provide its members with suitable housing accommodation at a reasonable cost and on easy terms of payment. The modern concept of housing does not limit the scope of housing alone, but a comfortable shelter with such surroundings and services to keep a man healthy and cheerful throughout his life. A housing co-operative, always strives to create conducive environment for fulfilment of the physical, social, economic and spiritual needs of its members. A co-operative also provides basic amenities like water, electricity, sanitary services, etc. to its members. Its

efforts are further directed towards building up a community life within the co-operative, based on good neighbourhood and fellow feelings and it transforms itself into a new community wherein “each is for all and all are for each”.

Instruments of improved social life

The essence of the co-operative movement is that members should themselves look after the management of their affairs including economic betterment and social welfare. The management of a housing co-operative is, therefore, not restricted or limited to management of housing estates, but encompasses all social and cultural activities as are to improve the social life within the cooperative system. The members themselves determine, by their collective wisdom, how the affairs of their co-operative ought to be managed.

Co-operative activities also include managing shops, laundries, etc., and provision of social, educational and cultural services (like running kindergarten schools, maintenance of play grounds, recreation rooms, cinemas, study groups, youth clubs, etc). Thus, housing co-operatives do not restrict its activities to merely creating better houses for their members, they rather aim at building up a new social life based on shared responsibility and shared benefits and free from crimes. In the process they create jobs for the needy. In India, housing co-operatives incidentally create 1 million jobs every year.

A New Life for Migrants

The history of housing co-operatives reveals that these have been instrumental in rebuilding the social life of people uprooted from their old surroundings. The pioneers of co-operative housing were people who had migrated to big cities in search of employment etc. Although they succeeded in finding work opportunities, they felt alienated and distanced from their old surroundings. To overcome the life of isolation in their new urban or metropolitan environs, they ventured into housing co-operatives which gave them not just housing but also an entire social environment based on sharing of their joys and sorrows.

A New Rural Community

Housing conditions especially, in villages in developing countries at many places are deplorable with inadequate houses and inadequate amenities. Housing co-operatives formed in rural areas have endeavoured to provide their members good houses with improved sanitary facilities. That is why rural housing co-operatives serve as catalyst for further improvement in

the entire village. When the villagers have themselves addressed to the task of housing and related improvement on co-operative basis i.e. instant construction of village schools, roads, etc., through collective action, they have significantly improved their societal life thereby reducing migration to cities.

Social achievements of housing co-operatives

The social achievements of housing co-operatives can be summarised as under:-

Social Activities and Services:

Besides laying out housing estates, the housing co-operatives have built schools, libraries, parks, etc. for the community.

Social Functions

Housing co-operatives organise special programmes for their members on occasions like New Year Day, Labour Day, Co-operative Week etc. They also organise tours and excursions on holidays. These functions bring people together and provide opportunity to understand one another.

Health Services

Many housing co-operatives arrange health services for the benefit of their members (dispensaries, first aid, family planning and welfare centres).

Youth Development

A number of housing co-operatives organise youth clubs and sports centres. Some co-operatives have opened gymnasiums and even play grounds. Others organise debates, publish newsletters, conduct essay writing competitions, etc. to encourage youngsters to participate in literary pursuits.

Ecological Improvement

Housing co-operatives pay special attention to improvement of the ecology of the concerned area. They plant trees and maintain gardens.

Women's Organisations

Housing co-operatives have been specially helpful in promoting women's organisations to benefit female members.

Transport Operations

Housing co-operatives also arrange special transport services for their members.

Promotion of other Co-operatives

Housing co-operatives have also been prompt to promote Consumer Stores, Thrift and Credit Co-operatives for the benefit of their members

Influence on Human Behaviour

One of the outstanding merits of housing co-operatives is the healthy influence they exercise on human relations. On account of better social and emotional interaction, the members of housing co-operatives generally display improved social behaviour and mental health. The incidence of addiction to drinking and juvenile delinquency are lower in housing co-operatives as compared to areas where people live in isolation, and are devoid of social activities.

Emotional Integration

Housing co-operatives have been instrumental in bringing about desired emotional and social integration. People of diverse religions, castes, sects, etc. voluntarily choose to come closer and live as one large family true to Aristotle's dictum that "man is a social animal".

Best Practices in Housing Cooperatives

The International Co-operative Alliance (ICA) and the UN-Habitat have been collaborating to promote housing co-operatives through a series of Memoranda of Understanding, publications, seminars and development projects. In pursuance of this, the UN-Habitat and ICA undertook case studies in countries like Ecuador, Estonia, India, Mexico, Namibia, South Africa, Uganda, U.K. and Zimbabwe to identify approaches to cooperative solutions for housing problems of the poor.

The case studies illustrate effectiveness of co-operatives in housing sector not only as provider of shelter to members, but as nucleus of socio-economic development in the field of employment generation, provision of financial resources and improvement in the quality of life of their members. These multi-dimensional contributions of housing co-operatives has been demonstrated in many countries viz:

Co-operative Housing Foundation of Canada dealt successfully with the problem of domestic violence by sensitizing their members and soliciting co-operation of Municipal Authorities and Women Organisations.

German Housing Co-operative Ludwig-Frank organised low income families of 15 countries to restore 400 apartments for them.

In Turkey, Kent Koop (Union of Batikent Housing Construction Cooperatives) in collaboration with Municipal Authority of Ankara and Workers' Unions constructed 43,000 housing units for 190,000 low-income people.

In India, housing co-operatives have substantially contributed affordable shelter to low and middle income families.

The potential role of housing co-operatives in solving the problems which are currently faced by our cities are outlined below:

- (a) **Housing for Homeless:** The problem of housing for the homeless has assumed serious proportions. Housing co-operatives can play a useful role in providing to the homeless not only shelter but also an environment in which they can live with dignity.
- (b) **Rural Migration:** Due to rapid urbanisation and industrialisation in the developing world, there is large scale migration of rural population to urban centres. The conditions of housing in which these people live are often miserable and crowded. Some are condemned to live in isolation having separated from their families. The best means for socially rehabilitating such people is through housing co-operatives.
- (c) **Slums Clearance:** Existence of slums is the bane of rapid urbanisation. In these slums, there is not only lack of living space, but also total absence of essential sanitary facilities. The problem of slums cannot be solved by individual efforts. Even the assistance of the government or the local authorities can be of minimal help. Co-operative efforts alone can succeed in building up the social life of slum dwellers.
- (d) **Industrial Pollution:** Problems of pollution are attendant on industrialisation. Today, largely on account of lack of proper planning in the location of industrial units or absence of adequate arrangement for clearance of pollution, people residing near factories and industrial plants are unwilling victims of industrial pollution. The modern world is, therefore, faced with the problem of large scale shifting of the population to safer zones. Co-operatives can play a useful role in performing this task. Although the state and local authorities may assist the people in building homes in safer areas, their social rehabilitation can be best achieved through housing co-operatives.
- (e) **Rehabilitation of Destitute People:** Floods and earthquakes are a spectre we see almost every year. Such natural calamities create the problem of rehabilitation of their victims. This gigantic task, can be most satisfactorily secured only through housing co-operatives.
- (f) **Social Evils:** The social life of people all over the world is infected with many evils on account of racial, linguistic and religious differences. Housing co-operatives wherein people voluntarily choose to live often maintain strict neutrality towards caste,

religion and language etc. perform moderating role in lessening the conflict as well as to fight the menace of drug addiction particularly amongst youth.

- (g) Ecological Improvement: Another problem faced by the modern world is the indiscriminate destruction of flora and fauna. The human society has been consequently condemned to suffer on account of constant droughts, floods, and other calamities. Housing co-operatives by planting trees and maintaining gardens etc. can create an awareness in the minds of the people towards preservation of ecological balance.

Conclusion

In conclusion, it can be said that the most significant social contribution of housing co-operatives is to create a new environment congenial for the upward social mobility of their residents. The various Governments must therefore address their priorities towards overall social development to remove disparities. They must find ways to help communities to deal with underlying factors such as homelessness, poverty, inequality, family stress, unemployment, absence of educational and vocational opportunities.

A time bound action programme to tackle the critical problems should be prepared and executed through public-private-co-operative partnership. This needs to be based upon a well articulated land management policy should also be formulated for land acquisition, land development and land disposal/utilization for housing low income families.

Though the latest UN Population Report-2007 says that most urban growth results from natural increase rather than migration, there is also an emergent need to discourage migration and reverse the existing trend through speedy development of rural areas and creation of small cities. Instead of forcing people to migrate and settle, infrastructure facilities like employment opportunities, better sanitation & hygienic conditions should be created in rural areas. The improved facilities of health and family welfare, access to safe drinking water, transport and communication facilities, education etc. and above all affordable housing if made available to the needy people in rural areas would pave the way for discouraging them to migrate to the cities.

Notes on current developments in the Indian Co-operative Movement

Sanjay Kurma Verma

Co-operative growth and diversification

During the month of September, the national level co-operative institutions in India continued to make rapid progress. Krishak Bharati Co-operative Ltd, a multi-state cooperative which is one of the leading fertilizer manufacturers in the country not only reaped huge profits but also achieved high production levels. Kribhco is one of the major success stories in the Indian co-operative domain. National Co-operative Agricultural Marketing Federation [www.nafed.org] whose main objective is to promote co-operative marketing of agricultural produce to benefit the farmers showed its intention to expand its seed business by entering into contract farming agreements with the state governments of Tamil Nadu and Orissa for seed production. NAFED last year had diversified into seed business considering the demands of the market. The policy shift of Nafed towards contract farming for expanding its seed business so as to increase its turn-over clearly showed that co-operatives, more particularly business co-operatives can not neglect their commercial aspects which is vital in the era of growing competition

Co-operative brand goes global

In India the milk co-operative brand of Gujarat Co-operative Milk Marketing Federation in the recent years has become immensely popular, and of late the private players have been trying hard to compete with Amul . but have not been successful till date. This clearly signifies cooperative supremacy. This fact was bolstered when a survey conducted by Global Market Research Organisation Synovate indicated that Amul has emerged as the leading brand in Asia. The survey based on research parameters will be an important reference point for the researchers who are interested in the subjects like brand building, customer satisfaction, etc.

Milk powder exports

The co-operative milk sector in the country throughout the month was worried over the ban on milk powder exports. The ban on dairy exports resulted into low returns for farmers and a dip in revenues of various

milk co-operatives including Gujarat Co-operative Milk Marketing Federation. The co-operative dairy revolution in India has empowered the dairy farmer in India, who has played an important role in the success of dairy co-operatives. Lifting of ban on milk powder exports would bring relief to the dairy farmers and support the global brand development but can the co-operative work with government to maintain the domestic price for the poor once export opportunities are available?

New Co-operative University

The Annual General Body Meeting of National Co-operative Union of India [NCUI] which is the apex organisation of the co-operative movement in the country was marked by key pronouncement from Mr G.H Amin, President, NCUI that Jawahar Lal Nehru International Co-operative University, first of its kind in the world would start its operations soon. The setting up of this University will be a definite step towards professionalisation of co-operative education in the country.

Whither the Co-operative Bank of India?

Co-operative Bank of India [COBI] organized an insightful conference on the important issues confronted by the co-operative banking sector in the country. The conference highlighted the demand of COBI for grant of license so that it could start its banking operations. The conference was unanimous in its view that considering the spread and strength of the co-operative credit structure in the country it is strange that operation of COBI has yet to commence.

Sugar cane

The State Government of Maharashtra towards the end of the month extended its guarantee for sugar co-operatives to help them raise fresh capital so that they may start crushing sugar cane. This brought a welcome relief to the co-operative sugar mills.

In Maharashtra in Kaigal, a co-operative sugar mill Chattrapati Shahu Sahar Karkhana showed its intention to go global as it announced that it will soon start its

carbon credit trading. It is in process of signing up with Austrian Government for sale of carbon credits which are aimed at reducing greenhouse emissions. This development clearly indicates that co-operatives in the small towns or villages in India are looking for innovations which can not only increase their revenues, but also contribute to better environment.

Tourism

Rajasthan which is one of the top tourism states in the country decided to commence a Rural Co-operative Tourism Scheme to make visitors aware of the rich culture of Rajasthan. The primary agriculture co-operative societies will implement the scheme in a few of the pilot villages. The co-operatives in Rajasthan are willing to forge links with the private parties to make their presence felt in an area which has tremendous potentialities for their growth. Can this example throw up a model for other states to ponder over, and implement it in their regions? It is an interesting research subject to dwell upon.

No jobs for life?

In Uttar Pradesh an ordinance reduced the tenure of co-operative officials to two years, a move which has been condemned by the co-operative movement. Strengthening co-operative democracy is the need of the hour considering the way in which co-operatives have tried to professionalise themselves while also trying to become self-reliant in the process. Notwithstanding this a two year period of tenure in any job with a degree of complexity seems too short a time and may lead to instability and make real change hard to follow through on.

Notes on Developments in the Kenyan Co-operative Movement

Owen Koimburi Njenga

Accounting framework for co-operatives

In Kenya the professional standards committee of the Institute of Certified Public Accountants of Kenya has just completed the preparation of a Template of illustrative financial statements for producer co-operatives and is about to finalise one for the savings and credit societies both of which are to be compliant with the International Financial Reporting Standards. Hitherto there was no such a framework and the Institute of Certified Public Accountants of Kenya felt it was necessary if the Kenyan Co-operatives are to prepare and report their financial statements for use by regulators and other potential foreign direct investors or other user of financial statements in accordance with the International Financial Reporting Standards. The illustrative financial statements will also be available for use by the regulators in the East and Central Africa region.

Coffee licences for co-operatives

The Kenyan Government has issued a directive warning that it intends to repossess licenses issued to coffee dealers who are also coffee marketing agents and auctioneers due to what they term as a monopolistic tendencies which the Government claims is impoverishing small scale farmers. This practice the Government has added has led to dwindling of coffee production. This normally happens when the company meant to market the produce on behalf of the co-operatives end up selling to themselves at negotiated prices as they are not independent. The Government has also simplified the procedure through which the co-operatives secure loans as well as cautioned them against taking excessive loans.

The government in addition asked the co-operatives to prepare strategic plans in order to improve on their managerial performance. This provides an important opportunity for the co-operatives to consider the issue of management leadership and governance afresh. Failure in this area means the fresh thinking and new models are required as well as a real commitment of resources. Skills and knowledge areas of competence are certainly generally poor in the Kenyan co-

operatives sector but equally important is the question of values and attitudes and recognition of the co-operative difference as more than a mere slogan but rather as a strategic weapon and competitive advantage.

ICO capacity building facility

Management development is also a pressing issue if the response to a new capacity building project for the East African coffee sector is to succeed following approval of a certification and verification capacity building project by the International Coffee organisation (ICO). Proposals for the project that aims to achieve high standards in the entire production chain were cleared by the ICO Working Council for submission to the UN backed Common Fund for commodities CFC for the financing.

Co-operative Bank shines on ICT

The Co-operative Bank has succeeded on the strength of the information super highway to record a super profit for the third year running since 2004. This growth is, however, tied very much to improvements in the agricultural sector especially the release of 5 billion debt owed by the coffee co-operatives to the Bank. This rescue plan was done by the government. The Co-operative Bank followed by other SACCO has introduced new financial products and increased the number of ATMs from 40 to 147 thereby becoming the bank with the largest number of unmanned network for a Kenyan Bank.

Recently the Bank has launched a visa branded debit card called 'Sacco Link' which will enable members of subscribing SACCOs to access money pay for goods and services at merchandise and other outlets using the card. More information can be accessed on www.co-opbank.co.ke.

Saccos get shs. 2billion arrears after government intervention

SACCO members can now access loans faster following government intervention through the introduction of stringent rules where the commissioner of co-

operative movement is mandated to demand arrears of loan and shares deducted by employers and not paid. The rules also allow the Commissioner to prosecute and attach properties for such defaulters. The short term loans advanced to these small scale coffee farmers through the above facility is small and can be repaid within three years.

According to the minister of co-operative movement the co-operatives are the main vehicles for individual development loans across all the sectors e.g. production, marketing of agricultural produce, handcrafts and housing.

Long-term loans made easier for coffee co-operatives

Managers for Coffee Development Fund (CoDF) plan to introduce a new product to cater for the farmers who need long term finance to rehabilitate their coffee production. CoDF already has 11 such co-operatives up from 5 when it was at the launched with the injection of 600 million KS. Statistics from the ministry of agriculture showed that the 1987/88 season the country recorded a volume of over 130,000 metric tones of coffee compared to just 50,000 metric tones in 2005/06 representing a slump of more than 50%.

The biggest challenge, however, for the CoDF is the low rate of loan repayment by the farmers, a position which has for many years has persuaded various financing and lending institutions to hold back lending for fear of incurring losses.

Performance of Public and Co-operative Firms: evidence from consumers

Remi Adeyemo

Abstract

This paper reports on a survey conducted in two different locations in Nigeria on 800 consumers between October and December 2005. The respondents were representatives of the general population that have patronized the two types of firms in the country. The objective of the study was to obtain consumers' subjective assessment of public and cooperative firms. Respondents were asked to first indicate type of firms that accomplished a particular criterion at the highest degree. If the consumer perceived a difference in criterion performance, he/she was asked to specify whether it was a small, a moderate or a large one. Responses were combined such that a seven – point scale was developed, centered on four, indicating to what degree the firm types were perceived to be performing differently.

The results from the study indicated that Co-operative firms were found to be outperforming public firms on five of the eight criteria uses, most dramatically for fairness and service of special consumers' needs. Convenience and location were believed to be more favorable to public firms. In general, consumers were more assertive in their assessment of Co-operative performance advantage. Older respondents gave better relative performance ratings to Co-operative.

Key Words

Performance, Public and Co-operative Firms

Introduction

The aftermath of independence dictated the need to consciously promote development through Public and Co-operative firms. Since then many co-operative and public firms have been established in the marketing and distribution of inputs and products but very few have achieved the goals set for them. In fact, most of the public firms have had limited success and this situation is not peculiar to Nigeria alone when viewed from a Continental African perspective. According to a survey of public and private enterprises in Africa, Frank (1971) came up with the conclusion that the basic cause of lack of success of public enterprise is

attributed to poor management and less sophisticated administration.

Other writers, Greenstreet (1973) and Ajuogu (1982) supported this view. In addition, Broadley and Auslan (1970), Teriba (1978) and Sionwanga (1980) have claimed that government was responsible for the difficulties experienced by public firms. However, this research will focus on the two types of firms – public and cooperative and the target group which they mostly serve.

The objectives of this preliminary study are to:

- commence an evaluation of the consumer's general subjective perceptions as much as they relate to the performance of co-operative and public firms on a broad spectrum of performance criteria.
- provide, through its findings, the basis for a development of the research tools and methods to evolve further research in Africa and stimulate debate on consumer co-operative strategy in Africa.

This study aims to contribute to our knowledge of the comparative performance of the two types of firms using consumer subjective evaluations as themselves a valid measure of performance in addition to the many other objective performance criteria measures.

Materials and methods

This study was conducted in October to December, 2005 on a total of 800 consumers drawn from different locations Southeast and Southwestern Nigeria. These include Lagos, Oyo, Delta, Edo, Rivers and Akwa-Ibom States. The study used a sampling procedure which was based on the ecological and political strata. These strata conformed to the Local Government structure while the sampling procedure focused on towns situated in the areas dominated by public and co-operative firms.

Section I of the survey contained 25 performance statements (some constructed in the negative form) based on the following strategy:

- AI. Respondents were asked to first indicate type of firm that accomplished a particular criterion at the highest degree. If the consumer perceived a

difference in criterion performance, he/she was asked to specify whether it was a small, a moderate or a large one.

- AI. Responses were combined such that a seven – point scale was developed, centered on four, indicating to what degree the firm types were perceived to be performing differently.

Criteria for the results

- BI. A score below 4 indicates that on the average consumers believed cooperatives were outperforming public firms.
- BII. A score above 4 is interpreted as favoring public firms.

Testing procedure

- CI. Scores were tested (+ - test) for statistical significance from the mid or neutral point on the scale (at the five percent probability level). If the null hypothesis (Score = 4.0) is rejected, then there is very likely a difference (in the direction indicated) in the population perceptions of the two types of firms.
- CII. Failure to reject the hypothesis suggests that consumers perceive both kinds of firms to be meeting that particular criterion equally well or poorly.

Generally, no indication of the absolute performance level is provided by these data.

Results and discussion

Characterization of consumers

As shown in table 1, the ages of the respondents varied from 20 to over 70 years. About 25% of the respondents were between 50 and 59 years in the Southeast while almost 22% of those in Southwest were between 60 and 69 years. Majority of the consumers are married. Sixty-two of the married respondents are from Southwest. When asked about their level of education 31% in Southwest have acquired secondary education while 25% have received University degree. In the Southeast 27% had Secondary education and about 28% already received various University degrees. In the same area almost 24% of the respondents have received technical certificates in several disciplines. All these qualifications combined have shown that our respondents should be in position to evaluate the firms that they do business with in their day to day activities.

It should be noted that the information contained in

table 1 matches closely population parameters (marital status, education and firm type) supported by previous works of Adeyemo (1994) and Adeyemo and Ajobo (1988). It would seem however in comparing table 1 to these works that consumers generally patronize and do business with all firms. Differences between consumers in the Southwest and the Southeast in all verifiable cases reflect true population difference; any differences in perception among consumers in the two locations identified should be interpreted with these basic demographic differences in mind.

Performance Perception Results

The primary question addressed in this study was whether consumers felt that one firm type was outperforming the other on various criteria. Table II provides the answer to this question for each of the 25 statement relating to a comprehensive set of criteria. This presentation of the results is called the detailed case, since all the statements are individually reported. Subsequent table and discussion will be based on the groupings of these statements.

Individual Performance

Co-operative firms were perceived to be performing better than public firms on 13 of 25 cases; public firms were believed to outperform co-operative in eight other cases. No difference between the two types of firms was found for four statements (Table II). Perceptions of strong differences favoring co-operatives were recorded providing consumers with greater voice in decisions that affect them (No. 4), public area (No. 5) have higher rate of returns on investments (No. 13) and providing greater enhancement for consumers welfare (No. 25). Public firms received higher performance ratings for better marketing services (No. 1), better information (No. 2) and the offer of varieties of supplies (No. 18). Consumers believed that neither co-operatives nor public firms have lower cost of doing business and create more competition among firms.

Group performance

The Co-operative-Public Firm comparisons are facilitated by a condensation of the 25 Statements into meaningful groupings. In this regard, eight performance categories were created into which one or more of the individual statements logically fall (Table III).

Within each group or category, the single average of all individual statements is used to represent the comparative performance score. Use of this procedure means that each statement in a given group has an equal weight as other statements in that group.

Table I – Characterization of Consumers

Characteristics	Southwest		Southeast	
	Frequency	%	Frequency	%
I Age of respondents				
20 – 29 years	30	7.5	35	8.8
30 – 39 years	62	15.5	58	14.5
40 – 49 years	81	20.2	83	20.7
50 - 59 years	85	21.3	99	24.7
60 – 69 years	89	22.2	73	18.3
Over 70	53	13.3	52	13.0
II Marital Status				
Married	246	61.5	231	57.8
Single	154	38.5	169	42.2
III Extent of Formal Education				
Elementary School	18	4.5	22	5.5
Adult Education	26	6.5	12	3.0
In-Service Training	44	11.0	56	14.0
Secondary Education	125	31.3	106	26.5
Technical Training	86	21.5	94	23.5
University Education	101	25.2	110	27.5
IV Categories of Consumers				
Civil Servants	110	27.5	112	28.0
Teachers	100	25.0	98	24.5
Self employed	80	20.0	88	22.0
Retired/Senior Citizens	66	16.5	70	17.5
Students	44	11.0	32	8.0
V Doing Business with Public Firms				
Yes	185	46.0	179	44.7
No	174	44.0	190	47.5
Uncertain	41	10.0	31	7.8

Table II – The Detailed Consumers Perception of Comparative Performance

Co-operative or Public Firms: do they;	MEAN(a) Score	FAVOURS(b)		
		Co-op (C)	Public (P)	Neither (N)
1. Provide better marketing services?	4.8		P	
2. Provide better information to consumers?	4.8		P	
3. Provide greater reduction to risk-facing consumers?	3.6	C		
4. Provide consumers with greater voice indecisions that will affect them?	2.7	C		
5. Make greater efforts to represent the interests of consumers in the public arena?	2.8	C		
6. Offer higher prices for commodities?	4.3		P	
7. Make greater efforts to Service the needs of Consumers who are Disadvantaged?	3.9	C		
8. Provide more liberal Credit Terms?	4.0			N
9. Establish programs and services which better meet consumers needs?	3.5	C		
10. Enable consumers to make greater adjustments in their purchases.	4.0			N
11. Give consumers prompt attention?	3.8	C		
12. Operate more efficiently?	3.5	C		
13. Have higher rates of returns on investments?	3.8	C		
14. Have more friendly relations with customers?	4.4		P	
15. Have more convenient places of business?	4.6		P	
16. Have better management?	3.7	C		
17. Have lower cost of doing business?	3.9	C		
18. Offer a wider variety of consumer goods	4.2		P	
19. Provide more accurate information about supplies and services?	4.8		P	
20. Take a more active interest in community affairs?	4.0			N
21. Provide information on future prices of commodities?	4.0			N
22. Demonstrate greater willingness to provide services which are important to consumers.	3.6	C		
23. Provide greater enhancement of consumers welfare?	3.7	C		
24. Have more ethical business practices?	3.5	C		
25. Make gifts for community services?	4.2		P	

a. - Based on a Seven-Point Scale where a score above 4 favours Public Firms and a score below 4 favours Cooperatives.

b. - Based on t-test of significance from 4.0 (two-tailed test, 5% probability level).

Table III – The Group Case of Consumers Perceptions of Comparative Performance

Performance Group (a)	MEAN	FAVOURS (b)	
	Score	Co-operatives (C)	Public (P)
1. Convenience/Location (8, 15, 18)	4.6		P
2. Friendliness (14)	4.6		P
3. Quality of Products and Services (1, 2, 19)	4.4		P
4. Fair Treatment (4, 11)	3.4	C	
5. Returns on Efficiency (12, 13, 16, 17)	3.4	C	
6. Community Service (7, 20, 24)	3.1	C	
7. Serve special consumer Needs (5, 9, 22, 23)	3.4	C	
8. Enhance Price Competition (3, 10, 21)	3.2	C	

a - Statement numbers assigned to each group are given in parenthesis.

b - Based on a t-test of significance from 4.0 (two-tailed test, 5% probability test).

However, weights for individual statements vary across group inversely with the number of statements included in that group. Co-operative firms receive higher ratings on five of the eight groups, while public firms were perceived to enjoy advantage in three areas (Table III).

Co-operative firms were believed to outperform public firms more strongly in the area of fair treatment (No. 4), serving consumer needs (No. 7) and efficiency (No. 5). The biggest advantage of public firms was in the area of quality products (No. 3). This quality aspect is, of course, but one of several included in that group and perceptions varied on individual Statements in that group.

Factors related to performance perception

Some factors related to respondents and their patronage was examined for their effects on comparative perception. Analysis of various models (with Scheffe contrasts), t-test, and Pearson correlation co-efficients were used. The findings are briefly noted. Only statistically significant relationships are discussed. Unless otherwise noted, all comments apply to the group cases.

Age of respondents

Older consumers perceived Co-operative firms performing significantly better relative to Public firms on the 25 statements than did younger consumers. Only in one statement, (No. 21) did older consumers

believe that Cooperative firms perform worse relative to public firms than did the younger consumers. The incidence of these correlations occurred in all the eight groups but were specifically concentrated on quality.

Educational level

As a consumer education increased he/she tended to rate public performance relatively poorer than that of Cooperative firms primarily in the areas of efficiency, returns on investment and better management.

Categories of consumers

Out of 17 of the 25 statements, civil servants and teachers gave cooperative firms a higher rating. These 17 students occurred in all the eight groups. Retired or senior citizens credited public firms for convenience or location. They placed more emphasis on nearness of firms to their homes.

Conclusions

In conclusion, if the findings of this study were to be reproduced in a longer term and more extensive sample then some support could be established for the view that consumers do appreciate how necessary Co-operatives have been to them historically. The key is to build on any positive perceptions and develop consumer co-operation and a branded social movement in Africa. Perceptions will only hold over time it is suggested if substance confirms expectations and here lies the challenge for retail management in the co-operative sector.

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Reflections on the research

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This research is important especially in the case of people having to observe differences between co-operatives and other types of organizations and make a judgment as to whether co-operatives are still relevant in the 21st century. This is important because there are people and especially policy makers in governments who still hold the view that co-operatives have outlived

their material relevance. I still remember the words of a former Japanese ambassador to Tanzania who once said "I think by promoting co-operatives, we have given small farmers the wrong institution to alleviate their poverty. We may need to give them another type of organization."

Therefore, studies such as this one are important in making the case for co-operatives and their relevance to human society. We need now to reproduce this work over a longer time period in order to secure the scientific foundations of the currently necessarily tentative findings based on data collected over three months.

The study uses consumer perceptions to evaluate public and co-operative firms. This provides some important information on subjective perceptions so important in determining consumer buyer behavior. This can change over time and needs to be continually supported by advertising and other promotional and merchandising based communications and not least supported by the real time experience of the consumer. Otherwise perceptions can change (possibly becoming degraded) over time. The differences between young and old respondents in the study gives some evidence of this process. A more widespread and longer term study may also bring out any basic confusion in perceptions that many people, anecdotally at least, appear to hold concerning the difference between co-operatives and public firms. There may also be some benefit in future studies disaggregating respondents who are members of co-operatives from non-members. Members may be expected to have different perceptions on their co-operatives when compared to non members but it needs to be clearly established as to content and degree.

Whilst perceptions are clearly an important performance measure for predicting consumer behavior I feel that the study would greatly benefit from more traditional performance measures as providing important criteria for measuring of real performance against the perception. If performance criteria suggest for example a successful society yet perceptions are negative the implications for work in advertising and promotion would be clear. On the other hand positive perceptions may be clouded by old loyalties or low expectations and should not become a convenient justification for ignoring the need for management and organizational development.

I would, therefore, hope to see included some parallel studies focused on a range of positivist quantifiable measures. One important example of

which is return on investment as a measure business performance when one is comparing the performance of the two types of organizations. In both case the use of this measure is different and less critical as a measure of performance than in the private sector. Co-operatives need to know their Return on Investment but for different purposes. ROI in co-operatives guides the organization where to invest for the benefit of their members. ROI in public firms guides the government where best to invest tax-payers money for public driven results. Other important performance criteria that parallel studies could adopt include sales volumes, economic impact, financial indicators and pricing policies. In the case of pricing policies those used by public firms for example are quite different from pricing policies used by co-operatives. Co-operatives are free to use differential pricing policies in favor of their members while public firms use more broad envelope pricing policies for the general public. These tools need to be developed in the study into a common yardstick to allow for a deeper comparison of performance between the two types of organizations in terms of their real time performance as opposed to the public's perception.

In co-operatives, services are to the members first and the general public later. In public firms, the general public comes first. That general public also includes the co-operative members. What needs to be evaluated, is, whether by forming co-operative organizations the members are adding value to what is already supplied by public firms or not. To evaluate the two types of organizations is both possible and relevant. More work is needed on developing competent criteria which uses comparable social, economic and business indicators alongside subjective measurements. Such a development of the research may also hold implications for business policy development by the co-operatives and for national policy formulation. Given the often thinly spread population base consumer co-operatives are an obvious business model for developing the retail sector in rural Africa and among its many poverty stricken city and urban areas. One needs more research to question whether in the consumer activity as in other areas of co-operative business however, performance, perception and potential are truly in alignment and if not why not?

Co-operative Entrepreneurship and Dilution over Time and Size

Raffi Goldman

Abstract

Perhaps the most interesting and significant achievement of the Israeli co-operative movement was the creation of the rural multi-purpose co-operative society known as the *kibbutz*. A careful study of the kibbutz provides a number of important lessons that may be relevant to the Co-operative Movement throughout the world. This case-study concentrates on the issue of change management: facing a number of dilemmas and even crises, how did one particular co-operative – *Kibbutz Hazerim* – manage a process of business and social change while seeking to preserve and strengthen its co-operative values? What can we learn about the dilemmas facing co-operative societies and their enterprises as they compete and become market leaders in a globalised economy? Does business success in the contemporary world market endanger the ability of co-operative societies to maintain their co-operative identity? How should co-operative managers involve their membership base in the processes of innovation and entrepreneurship necessary to grow and prosper in the global economy?

Key Words

Change-Management, Entrepreneurship, Co-operative Identity, Globalization, Kibbutz.

Historical origins

Kibbutz Hazerim was founded as a rural cooperative society in October, 1946. Thirty young men and women founded the village in the remote Negev desert plain as part of a settlement plan designed to promote Jewish settlement and determine the southern borders of the independent Jewish state. During the Israeli War of Independence in 1948, the tiny settlement was attacked and suffered its first casualty. But the Israeli military campaign to secure the area was completed by the end of October, 1948 and the members turned from war to the issue of developing their co-operative village.

The question of economic viability was a major concern from the beginning. Kibbutz Hetaerism was founded as an agricultural producer co-operative. The Israeli agricultural co-operative movement with which

Hetaerism was affiliated made the primacy of agriculture an important ideological principle. The settlement of the rural border region and the development of modern agriculture were regarded as the co-operative mission by the young members of the recently founded village. Never the less, the members were aware of the problems involved in realizing their dream. It was not at all clear that a viable agricultural economy could be developed in the Negev desert. There were no natural sources of water in the immediate region of the village and rainfall was scarce at best. In the first years, a majority of the co-operative's workforce were employed as hired workers by other more established co-operative villages. People traveled north to work, returning to Hetaerism at the weekend. The first attempts to plant commercial wheat fields failed for lack of sufficient rainfall. The first regional pipeline began supplying water on a semi-regular basis in late 1948. Even so, the lack of a secure supply of water severely limited the expansion of the agri-business in the first decade. Therefore, the need to develop additional, non-agricultural means of livelihood was obvious from the earliest days of the co-operative's existence.

An early attempt involved the development of a commercial carpentry shop. But the central focus of the co-operative management remained the extension and development of the agri-business. In the first half of the 1950's, the co-operative planted fruit orchards and raised vegetables and fodder for milking cows. The agri-business was extended to include a dairy farm and egg production. But the difficulties in developing a viable agri-business which would support a vibrant and growing co-operative community became even more serious in the second half of the decade. By the end of 1958, it was clear that Kibbutz Hetaerism faced an agricultural crisis which threatened the existence of the co-operative framework that had been developed. The salinity of the soil in the region seemed to make further agricultural expansion impossible. The existing agricultural business barely supported the 65 kibbutz members. Demographic growth based on agri-business was out the question.

The members of Hetaerism were faced with the dilemma of deciding whether or not to abandon the business they had struggled to develop and the village

they had built around it or to remain and continue the effort to solve the “salinity crisis” and save the co-operative. Suggestions to abandon the site and seek alternatives, including consolidation with another small co-operative in a different region, were debated throughout the first half of 1959. Agricultural experts presented the co-operative with technical solutions to the soil salinity. But the solutions involved significant investment and there were no assurances concerning the period involved before improvement of the soil would permit the expansion of the co-operative’s agricultural business. The uncertainty made the ongoing debate in the General Assembly even sharper. In August, 1959 the members decide by a majority of 40 to 11 with 12 abstentions to remain and continue the efforts to develop the kibbutz. In the end, the technical solution (leaching the soil) proved more effective and allowed for agricultural expansion more quickly than originally expected. The government aided with generous compensation leaving the co-operative in a reasonable financial situation despite the investment in leaching the soil.

Leaching the soil led to the development of the agribusiness. The production of cotton, vegetables and various grains was expanded. Extensive fruit orchards of peaches, apricots and pears were planted. The dairy farm and the chicken coops were enlarged. Never the less, the co-operative’s management team continued to be troubled by the uncertainty of the business development. It was becoming increasingly clear that the limitations of water and poor soil would make it impossible to depend on agriculture as the sole means of livelihood. The “salinity crisis” left the co-operative leadership with the understanding that the effort to develop non-agricultural means of production must be made a clear priority.

The early years of industrialization

In 1963, a decision was taken to begin a systematic search for an industrial plant that could be established in Kibbutz Hetaerism. Ezekiel Rot, the co-operative’s treasurer, was assigned the responsibility to organize the effort. There were a number of long discussions in the General Assembly concerning the practicality of establishing an industrial enterprise and what kind of enterprise might be suitable for the development of the co-operative. Various members questioned the practicality of the endeavor. The kibbutz numbered 80 members at this time. The development of the agricultural enterprises after the “salinity crisis” had been significant. Members expressed concern that the human resources of the co-operative could not be

stretched to accommodate another significant business development.

On the other hand, co-operative leaders such as Abby Ron and Uri Weber argued that the demographic forecast actually required the rapid development of additional sources of livelihood. The establishment of an industrial enterprise was, in their view, the only way to guarantee the demographic growth so necessary to insure the development of the kibbutz as a viable co-operative society. The supporters of the proposed innovation suggested that the establishment of an industrial enterprise would, indeed, actually solve a number of serious issues of human resource development. Agricultural labor was physically strenuous and impractical as an employment option as members got older. Industry could provide more varied and intellectually stimulating employment, requiring high degrees of technical and scientific knowledge and training. Wider participation of women in the business enterprises could be facilitated more easily in an industrial enterprise than in the agri-business.

But the advocates of industrialization proposed a clear set of criteria which would inform the search for a suitable enterprise:

1. The enterprise would serve as a source for the employment of kibbutz members only. No hired laborers who were not members of the co-operative would be employed.
2. The enterprise would require only a minimal investment which would not endanger the financial stability of the co-operative or involve it in serious debt service.
3. The enterprise would indeed involve a variety of employment opportunities for women and older men.
4. The enterprise would have some connection to agriculture in order to make use of the accumulated experience of the members and in order to serve the ideological goal of strengthening the agricultural and rural development of Israel.

The question of the type and nature of the enterprise which would be appropriate for the kibbutz was debated in the General Assembly which formally adopted the four criteria. In 1964, the recently elected treasurer, Uri Weber, took on the responsibility of identifying an appropriate enterprise which would meet all of the criteria that had been adopted. Weber investigated several possibilities and made a number of formal proposals to the Executive Committee of the co-operative. All of his proposals were rejected as not meeting the criteria that had been determined.

At this time, other rural co-operatives were also seeking to develop industrial enterprises. The background to these efforts was similar to that which had led the members of Hetaerism to their decision. The scarcity of water and suitably arable land and the relative saturation of the local markets made further agricultural expansion uncertain at best. A large number of co-operatives were undergoing identical demographic changes as the founding generations aged and the expanding younger generation sought appropriate employment.

On the other hand, the government's macro-economic plan for rural development called for industrial expansion. The government was offering generous credit arrangements in order to encourage the establishment of industrial enterprises in rural cooperatives. Co-operatives such as Kibbutz Hetaerism enjoyed high levels of member education. The members were oriented on production and economic growth and experienced in implementing business plans within the framework of a developing capitalist market economy. In addition, the management rotation systems regularly employed in kibbutz agribusinesses had led to the relatively high dispersion of managerial experience among the membership base.

On the other hand, the experience of Hetaerism and other similar co-operatives created a number of limitations which could interfere in the establishment of successful industrial enterprises. The ideological orientation on agriculture as a way of life made it difficult for many of the members of these rural co-operatives to envision adaptation to an industry-led business framework. The aversion to employment of non-co-operative members was also a limiting factor as was the aversion to creating a hierarchical working atmosphere which many associated with modern industrial plants. Never the less, the cooperative leadership of Hetaerism and other co-operative societies sought to overcome these constraints by adopting search criteria which addressed these issues while seeking to overcome the problems they faced concerning agricultural expansion and human resource development.

The Kibbutz Movement had established an Industry Association which helped the development of existing kibbutz enterprises and sought to promote the successful industrialization of additional societies. During this period the association was headed by Aryan Bahia, a member of Kibbutz Afikim, a large co-operative in northern Israel. Bahia was active in promoting industrialization of the kibbutz as the solution to the question of sustainable economic and social

development of the rural cooperatives. It was Bahia who arranged the first meeting between Uri Weber and Simcha Blass.

Simcha Blass was a well known Israeli water engineer dedicated to making the desert bloom. Blass noticed a hedge with one shrub noticeably healthier and taller than the others. Digging below the apparently dry surface of the soil, he discovered why: water from a leaking coupling was causing a small wet area on the surface, while an expanding onion shaped area of underground water was reaching the roots of this particular tree - and not the others. The drip irrigation concept was born and experiments that followed led Blass to create an irrigation device that used friction and water pressure loss to leak drops of water at regular intervals. Recognizing the high potential of his discovery, he began to look for ways to turn his idea into a product. His partnership with Kibbutz Hatzerim would revolutionize the co-operative. The development of the discovery by the members of Hatzerim would revolutionize world agriculture.

The creation of a successful partnership between Blass and the co-operative movement was not an easy affair. Blass and his son had been working on the development of the drip irrigation device for seven years. Despite an extensive set of field experiments, the results were not decisive. Their attempt to prove that the new irrigation technology would improve crop yields, save water and allow for the successful development of agriculture in various soil structures were inconclusive at this stage. The farmers in Israel were not convinced of the effectiveness of the technology and Blass found himself in financial difficulty, unable to market his product. He sought partnership with several large existing plastic firms but was rejected as they did not believe the new idea was commercially viable. It was at this point that Bahir introduced Blass to Uri Weber, the representative of Kibbutz Hatzerim.

Weber was impressed by Blass and the concept. From the beginning, Weber was convinced that the new technology had potential and could be commercially developed. He began a series of discussions with Blass and his son, Yeshayahu, about the possibility of establishing a plant for the production and marketing of their drip irrigation technology. But Weber and the leadership of Hatzerim were conscious of the fact that commercial success was dependent on more than successful negotiations with Blass. Of critical importance was the question of credit to farmers interested in purchasing the new product and reorganizing their irrigation system. Discussions with

the Ministry of Agriculture and other relevant government officials led to the decision of the Agriculture Bank (responsible at that time for development loans and credit to the agricultural sector) to extend credit under favorable conditions for investments in drip irrigation. In addition, the Israel Water Authority published new guidelines encouraging the use of drip irrigation in order to save Israel's precious water resources. Encouraged by government support, the leadership of Hatzerim decided to move forward to establish the new industry.

In June, 1965, Weber reported to the General Assembly and presented the case for the investment in an industrial plant for the production and marketing of drip irrigation equipment. The proposed factory seemed to meet the criteria that the cooperative had established in its initial decisions to search for a new additional source of livelihood. The risk involved was deemed minimal as the machinery necessary could be resold. In addition, the proposal was to use an existing building and avoid, for the time being, the expense of costly new construction. Blass would train the factory workers in the basic operational procedures as well as providing special training for field specialists who would provide on-site training and technical services to customers. He would also train kibbutz members in the science of planning and implementing large scale irrigation projects. The concept behind the product was exciting and had the potential to make a significant contribution to the development of agriculture and the rural development of Israel.

Weber reported on his investigation of the commercial potential imbedded in his proposal. Field experiments demonstrated that the technology allowed for savings in the amount of water applied due to decreased influence of evaporation during irrigation. The evidence showed a positive influence on vegetable production though the results in fruit orchards were less conclusive. The system promoted the application of fertilizers through the water pipelines which was promising and commercially significant. The Ministry of Agriculture was interested in promoting the use of the technology as it believed this would improve the production of winter vegetables for export. The establishment of the factory would employ eight members at the outset.

Despite the general agreement that the proposal was an exciting and positive step forward, the members raised practical issues. Weber clarified the uncertainty concerning the extent of the potential market for the new product. Questions were asked concerning the existence of relevant patents. Concerns about the

ability of farmers to make the required investment were expressed. It was still unclear whether the co-operative had the required human resources to implement the decision. The co-operative leadership was inclined to take the risks. The concept was exciting even though the final commercial details were not entirely clear. In the end, the issue of employment was decisive. The agri-business, while slowly developing, could not sustain a growing population. Additional, commercially viable sources of income and employment were absolutely necessary. The General Assembly approved the proposal to continue negotiations with Blass.

In August, 1965, Uri Weber signed an agreement on behalf of Kibbutz Hatzerim with Simcha Blass and his son. The agreement established a partnership between the kibbutz (80%) and Blass (20%) for the establishment of an industrial plant - *Netafim* - "for the production of drippers and other drip irrigation equipment and the provision of services to farmers in the field of irrigation..." The factory would be established in the kibbutz and would exclusively employ members of Hatzerim. The partners would establish a research and development department which would be headed by Yeshayahu Blass. Blass transferred the patent rights to the partnership in return for royalties on the basis of gross sales. His agreement to accept small royalties was an expression of his uncertainty about the commercial potential of his invention. The leadership of Hatzerim was less uncertain. The factory began production in January, 1966.

The cautious approach which characterized the initial decision to build the factory never the less translated into a supremely successful business strategy. From its initial stage of development, the management team of *Netafim* conceptualized its business concept as the marketing of irrigation solutions and not only the sale of a particular product based on a particular technology. As Abby Ron, one of the founding team members, explained, "We didn't build a factory to produce drippers. We built an irrigation factory. We don't sell equipment from the shelf...we sell a fully planned and equipped field meeting the growers' expectations."

This strategy not only had financial/commercial consequences but also significance in terms of human resource development. The service package offered to potential customers as part of the basic marketing strategy required the development of human resources in a wide number of professions: agronomy, planning, technical consultancy and more. All this was in addition

to the operational, marketing and managerial proficiencies required to support a rapidly growing industrial plant. Emphasis was placed on developing a new marketing approach. Abby Ron explained, "We believed we had to teach a new system of irrigation. We thought that we had to guarantee our customers a long-term relationship of training and consultancy. We discovered that this approach was not only appreciated by our customers, but was the basis for all our subsequent development! The feedback we received from the growers allowed us to develop new products and approaches..." Yearly sales increased from \$75,000 in the first year to over \$3 million by the end of the first decade. By the end of the second decade of production, yearly sales were more than \$30 million. The number of employees (co-operative members all) increased from the initial eight to 90 in the same period. Operational innovations and marketing successes created a growing volume of net profits.

The consistent application of the co-operative values which had characterized the initial search criteria and the subsequent decision to build this particular factory also had significant commercial consequences. This was particularly true of the principle of self labor which the cooperative consistently applied. Despite the large supply of relatively cheap labor available in the region, the cooperative continued to employ its own members exclusively. The management of human resources was accompanied by a successful mobilization of member enthusiasm and willingness to invest time and energy to insure the plant's success. Limitations on employment also fueled a continuous process of technical innovation in the fields of automation and (eventually) robotics. Each step forward contributed in two ways to strengthening the enterprise: the research and development enriched the teams involved and the successful implementation improved efficiency and productivity thus increasing the profitability of the enterprise.

Business success requires change

Netafim was characterized from its inception by a culture of technical and entrepreneurial innovation. The original technological invention that Blass gave to his cooperative partners was revolutionary in itself. The members of Hatzerim took the original patents and began immediately to develop new variations on the theme of drip irrigation. Two improved drippers were developed in the new factory within the first five years of production. Technical innovation and new product development has been central to *Netafim's* success from the beginning.

The business success soon outstripped even the wildest dreams of the co-operative management team. Market demand for the new irrigation system required continuous expansion of productive capacity. The co-operative leadership found itself facing a serious dilemma: despite the relatively rapid expansion of the membership base, further business expansion was constrained by a lack of human resources. There was no difficulty in finding employees from outside the co-operative. But Kibbutz Hatzerim had always carefully maintained the principle of self-labour and the non-exploitation of others. The original decisions to industrialize included a specific ban on the employment of people who were not members of the co-operative. The cooperative values of the community had become a constraint on the further development of the co-operative's most important source of income and employment.

The co-operative leadership sought a co-operative solution to the dilemma. In 1970, suggestions were raised to halt further investment in agricultural activity and concentrate all of the co-operative's resources (human and financial) in the continued development of the factory. Opponents of this approach argued that it endangered the existence of the existing enterprises and would eventually endanger efforts to expand the membership base. The alternative was to seek partnership with an additional co-operative. The initial reaction to the idea of seeking a partner for the development of *Netafim* was not positive.

But the problems in maintaining the status quo sharpened. In March, 1973, the management team of the factory proposed to the General Assembly to decide to appoint a special committee to identify an appropriate co-operative which might be suitable as a partner. In a separate discussion, search criteria were debated. One approach suggested that Hatzerim concentrate its search among the older, more established co-operatives. The assumption was that older, established co-operatives had the human resources necessary to succeed in developing an additional industrial enterprise. The other approach was to search among the younger co-operatives. The argument was that in choosing such a co-operative as a partner, Kibbutz Hatzerim would be aiding in the development of a struggling kibbutz and helping to ensure its future.

In September, 1973, the issues were debated in the General Assembly. Members expressed concern that the proposed partnership could lead to changes in the character of the enterprise and loss of control over its future development. Others were concerned that there

were few examples of successful partnerships between kibbutz co-operatives. The CEO of *Netafim* explained that the proposal was not to establish a full partnership with the additional co-operative. *Netafim* proposed to aid in the establishment of an additional factory which would deal with all the stages of production, distribution and extension services excepting the casting of the drippers themselves. This would ensure control of the product and standards. Other participants emphasized that the growth of *Netafim* and its human resource needs were hampering the development of all the other enterprises belonging to Hatzerim. The General Assembly approved the proposal to search for a partner according to the guidelines proposed by the management team.

In April, 1974, after careful deliberation, Kibbutz Hatzerim decided to transfer production rights, intellectual capital and use of the brand names to an additional co-operative: Kibbutz Magal. Hatzerim agreed to transfer up to 30% of its sales to the local market to its partner. Kibbutz Magal would assemble drip irrigation equipment; prepare fertilization and filtration equipment and offer services in planning and implementation of irrigation projects. All of these activities would be supervised by *Netafim* experts in order to ensure quality control standards. While each co-operative would retain management independence of its manufacturing and marketing process, a joint management committee would decide upon issues of pricing, customer credit and financing, marketing strategy and the general relations between the two factories. Magal was given responsibility over a specific geographical area in Israel in order to ensure effective customer service which was one of the secrets of *Netafim's* success. Magal was also promised a part of the export market in the future. Hatzerim retained complete control over the production of the drippers themselves. The leaderships of the two co-operatives pledged to maintain a relationship of mutual co-operation and coordination while jointly producing and marketing under a single brand name- *Netafim*.

The two co-operatives succeeded beyond their expectations. Despite growing competition both within Israel and in the world markets, sales continued to grow by more than 30% a year. In July, 1978 the General Assembly was convened to consider a proposal to involve a third cooperative in the enterprise. Despite the positive relationship that had been developed between the two co-operatives, members of Hatzerim were still uneasy about involving yet another potential partner. The major problem continued to be the lack of sufficient human resources to exploit the marketing opportunities the enterprise had developed.

Given the self-imposed constraint of avoiding external hired labor, the only solution seemed to be expanding the human resources through the involvement of an additional partner. But members expressed concerns about the proposed solution. While recognizing the crisis that was developing, one of the members warned that the addition of a third partner would further compromise the profitability of the enterprise from the point of view of Kibbutz Hatzerim. The entrance of new producers of drip irrigation into the Israeli market was eroding profit margins. Under these circumstances, it was imperative to carefully consider the transfer of production capabilities to yet another co-operative.

The senior managers of *Netafim* responded with unqualified support for the proposal. They argued that a failure to meet the challenges of the expanding market endangered the future of the firm. The proposal took into consideration the interests of Hatzerim by continuing the policy under which Hatzerim alone was responsible for the casting of the drippers. Members also expressed concern about the criteria to be used in identifying the appropriate partner. The CEO of *Netafim* explained that the search would concentrate on a co-operative which had the appropriate human resources and was interested in making its partnership with *Netafim* a central pillar of its business development. In addition, the co-operative would have to guarantee that the new enterprise would employ co-operative members only. The search would focus on cooperatives in northern Israel which the staff from *Netafim* found difficult to serve due to the distance from Hatzerim. In the end, the General Assembly approved the proposal by an overwhelming majority. In 1978 Kibbutz Yiftach became the third co-operative to join the *Netafim* family.

The entire process of divestment was undertaken under the initiative of the leadership of Kibbutz Hatzerim. The managers of the factory and the general co-operative management team consistently applied a policy of transparency and membership base involvement in the affairs of the enterprise. The General Assembly retained a central role in the management of the business. The management team itself was chosen by the Assembly. In addition, all significant decisions concerning business development were debated and approved in the General Assembly. But it is impossible to underestimate the influence of the ideologically motivated leadership which enjoyed significant if not total support from the membership base. In effect, the leadership managed a process in which Kibbutz Hatzerim voluntarily relinquished absolute control of its astoundingly profitable business

enterprise in order to ensure compliance with the self-imposed restrictions mandated by the co-operative's business principles. As the enterprise developed, more and more of the human resources of the co-operative were invested in *Netafim*. While this development was a natural outcome of the success of the enterprise, it would lead to some serious problems in the future.

From business success to world market leadership

Netafim developed rapidly in the three kibbutzim. In 1985, yearly sales reached \$12 million. Five years later, sales were more than \$40 million. By the end of the 1970's, export markets had become the primary source of income and growth in the enterprise. The co-operatives began to establish subsidiaries in the major markets around the world. Logistic constraints lead to building production sites in various countries and most importantly in the USA. *Netafim* became the world leader in drip irrigation and water management technologies and project development. Sales in 1996 were \$150 million. The co-operative enterprise founded as a solution to economic crisis had developed into a multi-national business.

But the astounding business success lead to a variety of new challenges that endangered the enterprise's continued growth and development. The last decade of the twentieth century was characterized by four serious problems:

- 1 The terms of trade that had allowed for the unparalleled business success began to change for the worse. The rising price of petroleum products adversely affected the cost of raw materials in the plastic industry. At the same time, economic downturns in several major markets (most especially in South America) put downward pressure on prices. Profit margins seriously eroded.
2. The development of the enterprise into a multi-national business required unprecedented investments in subsidiaries. But *Netafim* was a co-operative enterprise without access to significant capital markets. The result was a developing cash flow problem. The capital structure of the firm was no longer appropriate to its business needs.
3. *Netafim*'s major patents expired exposing the firm to even more serious competition. New entrants into the field of drip irrigation put additional pressure on prices, further eroding profit margins.
4. The gentlemen's agreement among the three co-operative owners began to dissolve. The efforts to

maintain a coordinated business policy failed as conflicts of interest developed. The vague contractual relationship which characterized the partnership was not appropriate for the management of a multi-national business.

Incorporation and its consequences

All of these developments lead to a reassessment of the structure and management of the enterprise. The desire to end the conflicts among the partners and the need to manage the multi-national business in an era of increasing competition led to a proposal to incorporate the three enterprises into one co-operative firm owned by three co-operative societies. This development led to a series of discussions in the General Assembly of Kibbutz Hatzetim in which the entire process of industrialization and its consequences was debated.

In August, 1996, Yigal Stav, the CEO of *Netafim-Hatzetim* presented the case for incorporation to the members of the co-operative. He began with a review of the existing arrangement in which three co-operatives managed independent firms while making an effort to co-operate and coordinate policy in their mutual interest. The arrangements were developed in the era in which the local Israeli market was the predominant factor and the specific geographic location of each of the co-operatives was important. Stav continued with a series of examples of the distortions and business difficulties arising from the effort to continue this business model under the significantly different circumstances that characterized the business environment in mid-1996. He summarized his presentation with an impassioned plea:

"Let me put it this way... this creation we call Netafim – we call it a group, we call it a complex, we call it all sorts of names using non-business terms. But this group of factories we call Netafim was built on the basis of personal relationships. Many of these personal relationships are historical, intimate, longstanding personal relations. They are more important than formal, legal contracts which don't really exist in our case. But this might be appropriate for the founders of the partnership, those who know each other for decades. But as we move forward and away from the origins, our reality changes and becomes more complicated. We see it today and it will only get more complicated in the future. And many things which were taken for granted by the founders are much less obvious to us today, and will be incomprehensible to those who follow us tomorrow. And we have to be aware of the fact

that family firms (and Netafim is very much like a family firm) often fall apart after two or three generations at the most...we have reached that point today. And we are investing an enormous amount of time and energy and management resources into the attempt to reach consensus, to reach mutual agreements. And as the firm continues to grow and develop this is rapidly becoming impossible!

Now this is no ordinary discussion, no ordinary decision. This is a decision which affects each and every will one of us...let no one be mistaken. The decision to incorporate will change everything. We really are a family here in Hazerim and we've been running a family business. We've always walked the thin line between running a business and solving personal and organizational problems of the co-operative (kibbutz). And we've been amazingly successful and we've built something beautiful, something that belongs to all the members. And I'm sorry to say that some of that will be lost in the process of incorporation..."

The issues that troubled many of the members were summarized by A. Yadlin, one of the founders of the co-operative:

"I believe that the strength of Kibbutz Hazerim has been in the identity we created between the co-operative and our enterprise. Once this identity is forsaken and the enterprise becomes a company owned by three cooperatives, this creates not only a social problem but an economic problem. Once we create this independent company then economic issues, even personal economic interest begin to appear...I see the proposal to incorporate as a problem and I think we need to be convinced that this is a business necessity and even if it is a necessity, sometimes we have to pay an economic price to maintain our principles because in the end they are the true source of our success..."

The debates within the co-operative continued throughout 1997. The management and the majority of the members who worked in *Netafim* strongly supported the proposal to incorporate. In December 1997 the proposal was once again presented to the General assembly. A long discussion about the voting process ensued. A small group of members demanded that the issue be decided in a referendum of the entire membership base and not only by those attending that particular session of the Assembly. Another debate ensued over the majority required to approve the

proposal. In the end the Assembly agreed to the referendum and clarified that the proposal needed to receive 60% of the votes cast. The proposal was accepted with a majority of 77% of the votes cast with over 80% of the members participating in the referendum. Hazerim retained majority control of the united firm. The decision to reorganize the three firms was much more than a question of organizational change. The consequences of the decision did effect a fundamental change in the relationship of the co-operative to the enterprise it owned. It is likely that many of the members were unaware of the significance and ramifications of the decision.

The reorganization of the firm involved some unprecedented developments from the point of view of the co-operative's members. The firm was now managed by an independent board of directors and not by the co-operative's management team and General Assembly. The members found this difficult to accept. In the beginning, the General Assembly elected a committee of 20 to act in its name as owners and to supervise the management of the firm. This arrangement lead to conflict with the firm's board and was eventually abandoned. In its place, in 2004, the General Assembly elected a small committee of seven and invested it with all of the rights accruing to Hazerim as majority owners of the firm. This new arrangement was regarded by the firm's managers and the kibbutz members as an improvement on the previous decision.

Another significant change involved the method of payment of wages by the firm to the co-operative. In accordance with traditional kibbutz principles, *Netafim* had always transferred the wages paid by its various enterprises to the communal account. Individual members then received a standard egalitarian monthly budget. There were no wage differentials of any kind. *Netafim* transferred the same wage for its CEO as it transferred for the un-skilled production floor worker. Under the reorganization, a decision was taken to adopt a differential wage scale. Sums were now transferred on the basis of the current prices in the general Israeli labor market. The enterprise continued to transfer the funds to the communal account and the members continued to receive their egalitarian budgets. But for the first time, members began to consider their individual "market value."

An even more significant change occurred in the area of human resource management. From its inception, the rapid development of the enterprise had created a problem of human resource management. Although *Netafim* eventually became the most

important asset belonging to Kibbutz Hatzerim, it was not its only asset. The kibbutz needed skilled workers and managers to work in a wide variety of additional business, educational and cultural institutions. The factory tended to attract almost all of the most competent and skilled members. But for most of the period under consideration, the central management of the kibbutz successfully implemented a human resource policy which guaranteed the checks and balances needed to manage the entire co-operative portfolio.

With incorporation into one firm and the development of an approach deemed necessary to manage a multi-national firm, it became extremely difficult to convince members to leave their jobs in *Netafim* in order to take responsibility for the management of other kibbutz institutions. This was true even if the proposal was to accept election to a 2-3 year term as a municipal leader. In addition, the extent of the firm's business empire created the need to end the ban on the use of non-member labor. The growing requirements for highly trained engineers and technicians could no longer be met by the human resources of the co-operative. It did not take long before hired labor was introduced into additional parts of the enterprise. The introduction of hired external labor meant that capitalist labor relations became part of everyday experience among the staff of *Netafim*.

From the point of view of the members of Hatzerim, the phenomenal success of their co-operative enterprise had created a growing sense of alienation of the membership base to its most impressive cooperative achievement. The General Assembly was no longer intimately involved in the management of the firm. Members developed a more restrained approach to filling the needs of the enterprise. Once the managers began hiring external labor, it became increasingly difficult to demand from members that they donate extra shifts in order to solve temporary work shortages. In light of the changing relationship between the co-operative society and its main business enterprise, some members began expressing general dissatisfaction and a lack of confidence in the firm's management and even in the central kibbutz management team.

The situation became more serious as the business results worsened. Although *Netafim* was not losing money, profit margins plunged to zero. This new situation was traumatic for a society used to ever increasing profits and a continuously rising standard of living. For many members, the psychological shock was profound. The unprecedented business crisis led to

the decision to hire McKinsey & Company, one of the world's leading consultancy firms. McKinsey analyzed the situation of *Netafim* and proposed a recovery plan for the firm. McKinsey's recommendations focused on their conclusion that the co-operative society was not capable of managing a multi-national business firm like *Netafim*. They proposed a series of additional organizational and business strategy changes including a recommendation to appoint external managers- CEO and Chair of the board of directors. The proposals were debated in the General assembly and accepted.

This stage in the development of *Netafim* had further significant consequences on the relations between the co-operative society and the enterprise it owns. The McKinsey recommendations apparently strengthened the processes of alienation that were already apparent. The economic consequences of the program have, indeed, led to a recovery of profitability and growth. Sales in 2004 approached \$350 million and profits recovered. But, the appointment of external managers, the transfer of the firm headquarters to Tel Aviv, and the application of conventional capitalist management mechanisms of governance seem to have weakened the involvement of the co-operative members in the management and development of the firm. One of the chief recommendations of the McKinsey report was to invest managerial resources in the search for a suitable private investor who would help introduce managerial standards appropriate to a successful multi-national corporation. In May, 2005, the members of Hatzerim accepted the proposal to sell 20% of the firm to an Israeli investment fund and to prepare the firm for an initial public offering on the Israeli stock exchange.

Conclusion

The case of *Netafim* demonstrates the complexities of change management in a co-operative context. In this case, co-operative values enabled the development of a world class business firm under difficult conditions. But business success fueled processes of change that seem to threaten the continued existence of *Netafim* as a co-operative enterprise. It remains to be seen whether the values and resources which characterized the members of Kibbutz Hatzerim and its co-operative management up until now will enable them to develop co-operative strategies in the future.

A Buddhist Economics Approach to Business Management: an introductory seminar paper

Wanna Prayukvong

Abstract:

Buddhist Economics, which is derived from the lessons of the Buddha on his path to enlightenment, to explain economic activities is different from mainstream economics in the paradigms of human nature.

In this presentation will cover literature review which surveyed a meaning and an issue of moral and ethics in the context of management theory, of Buddhist notion and criteria for applying to business management and the conceptual framework to study how the Buddhist Economics is applied in a business context from case studies. This framework of this study will explore not only the extent to which the Buddha's teachings can be applied but also the impediments to the application. The assessment of performance in organization and monetary and non-monetary benefits from their application will be included in this study.

Key Words

Buddhist Economics Economics, Management, Markets, Inter-faith Dialogue

Introduction

Business is an economic actor in economic system. Their role is to organize their ownership and allocate the resources by purchasing a primary and /or an intermediate product and hire labour to produce goods and services for sale in a market. These transactions generate income flow among the others economic actors which are households and government. (Mankiw, 2004). Therefore, in neoclassical economic theory the firm is viewed as an anonymous production function to bring incomes for economic growth. (Silva, Teixeira & Silva 2006)

The assumption of economic actors' behaviour in the discipline of economics is based on the rational behaviour or rational choice theory. The focus is on characterizing rationality of choice as maximization of self-interest. Human nature in mainstream economics view is of an "economic man" who is rational; he knows his own interests and chooses from a variety of means to maximize his self-interests. (Hodgson et al., 1993)

The exchange between goods, services and money is

through the price mechanism in a market system. The self-interested engagement of the firm in the market process reflects moral conduct. Therefore, the ultimate goal of an economic system producing ethical outcomes such as rising living standards and rising welfare in society, are unintended by the firm (Wagner-Tsukamoto, 2005).

While a perfectly competitive market does not exist in the real world (Friedman, 1962) due to asymmetric or incomplete information (Stiglitz, 1974). A negative externality is not included in market price. And a transaction cost is positive and large (North 1986). Market failure is an inevitable consequence. Therefore, economists present various governmental policies to intervene within the market system. These policies are never more than temporary and contingent solutions.

Today the global economy growth has expanded exponentially in terms of GDP. This wealth, however, is not spread equally across the globe. In 1997, the richest 20% of people enjoyed 86% of the world's GDP while the poorest 20% claimed only 1.3% (UNDP, 1999). More than a billion people survive on less than a dollar a day, and one fifth of the world's population live on less than two dollars a day in 2005 (UNDP, 2005) The gap in wealth distribution across the globe is increasing, not decreasing. There are two major issues arising from this uneven economic growth: the social dislocation that arises from extreme inequity (even if absolute wealth does not appear to be the issue) and absolute levels of poverty experienced by a significant proportion of the world's population (UNDP, 1999). While certain governments undertake policies attempting to correct the disparity between growth and distribution this is far from true of all governments and even those who are genuinely trying to address poverty such as the three EU Anti-Poverty programmes, the results have been modest or even negative. (EU Commission, Poverty Three. The lessons of the Poverty 3 Programme DGV/E/2, undated).

In addition to the challenge of economic justice climate change and global warming have become new dangers facing humanity at the start of the 21st Century (UNDP, 2007). The increasing emission of carbon dioxide gas seems to be the main culprit. The

industries in the unlimited economic growth paradigm consume extremely large amounts of non-renewable natural resources which include “fossil fuels” such as coal, oil and gas. The huge amount of waste from the burning of these fuels has the affect of increasing carbon dioxide emission. To correct this problem, renewable energy from sunlight, wind and geo thermal heat and clean technology are promoted. Some large corporations such as BP or GE have already invested in these new forms of energy. The potential for major global catastrophes for human and non-human life alike is considerable. (Stern, 2007)

Despite the obvious importance of State activity and, perhaps, the meta-State activity, the business sector appears to be the most prominent element of the global economy. It certainly appears to be the case that today the model for economic growth for any country is based on the model of economic liberalism that has the idea of the firm as rational agent serving a rational consumer in a free market context as its core framework. This leads some commentators to argue that the growth of firms is the primary engine of economic progress (Ghoshal & Moran, 1999).

However, the objective of business is still to achieve a level of maximized profit. Some thinkers address “self-interest” in a wider meaning. The examples are: Adam Smith who believed individualist is the influence of society that transform people into moral beings (Muller, 1993). Alexis de Tocqueville (Tocqueville, 2007) believed it should be to serve the interests of others. Moving firm motive and goal beyond narrow ideas of self-interest and profit maximization is still a difficult task to perform within modern economic literature. Within the present context of economics and management theory, it may be more difficult. (Ghoshal & Moran, 1999).

Several contemporary business approaches such as moral agency, corporate citizenship and corporate social responsibility (CSR), have been raised as alternatives. Some companies have already created many activities especially focusing on CSR. Type and level of practice, however, are still varied and not integrated to their daily practices or business strategy (Liedtka, 1998; Kotler & Lee, 2005; Porter & Kramer, 2006). Furthermore, these theories are normative which suggest that underpinning values and practices are also varied and without consensus (Porter & Karma, 2006). Perhaps, under these circumstances, we might explore the Buddhist Economics approach to explore whether it can provide an effective vehicle for shifting this existing paradigm of profit maximization to a more human centred and creation centred model of business motive and practise?

Buddhist economics approach

Buddhist Economics applies the lessons of the Buddha’s discoveries on his path to enlightenment to an analytical approach encompassing generally accepted economic concepts. It can lead to better understanding of the truths of human existence and our relationship with nature (Puntasen, 2005, p. 3).

Buddha Dhamma is a shift from faith to wisdom verified through actual experience. One of Buddha’s famous stories, “Kalamasutta,” showed the Buddha’s teaching against faith or beliefs. Once Buddha traveled to “Kalamas” village, there were several visitors who talked about their own beliefs what should they believe?

The Buddha replied, you should not believe all of what our teacher say; an authoritative tradition; upon that which has been acquired by repeated hearing; nor upon rumour; nor upon a scripture; nor upon speculative metaphysical theories, reasons and arguments; nor upon a point of view; nor upon specious reasoning; nor upon accepting a statement as true because it agrees with a theory that one is already convinced of; nor upon another’s seeming ability; nor upon the consideration ‘Our teacher says thus and so. It is proper for you, Kalamas, to doubt, to be uncertain. Uncertainty has arisen in you about what is doubtful. Come, Kalamas. Do not go up on Kalamas, when you yourselves know: ‘These things are bad; these things are blamable; these things are censured by the wise; undertaken and observed, these things lead to harm and ill’, abandon them.” [Kalama or Kesaputtiya Sutta, A.I. 188]

So the Buddha teaches us not to believe until something has been proven to be a true by personal experience through the state of mind development. Ignorance or lack knowledge consequently causes one to see a distortion or delusion causing burdens and problems in life. According to Buddha Dhamma, human beings are born in a state of ignorance (Chieng Mai Dhamma Study Group, 2007). Without accumulated wisdom or pañña, they follow their desires, struggling at the direction of craving to stay in the world. Human beings in Buddha Dhamma are different from other beings because they have the potential to practice and develop themselves through training of mental development to gain higher wisdom. So mind is a very important element to plan, lead and create all of human activities.

That all things depend on all other things for their existence is the principle of Dependant Origination (*Idappaccayata*). It refers to the law of conditionality

or law of nature discovered by the Buddha. The example is the leaf... , earth, water, heat, sea tree, clouds, sun, time, space—if any of these elements were missing, the leaf could not exist. (Thich Nhat Hanh, 1991: 169 quoted in Wheatley, 2006: 143) The progression of causes and conditions is the reality which applies to all things from the natural environment, which is an external physical condition, to the event of human society, ethical principles, life events and the happiness and suffering which are manifest in our own minds (Payutto, 1994: xi).

This is why, all the system of causal relationship based on the law “because there is this, that arise; when this ceases that ceases,” Buddha Dhamma begins with, and stresses throughout, the factors involved in the creation of suffering in individual awareness—“because there is ignorance, there are volitions formations.” Once this system is understood on the inner level, we are then in a position to see the connections between these inner factors and the causal relationships in society and the natural environment. (Payutto, 1994: xiii)

When Buddha Dhamma is applied to economics, the understanding of human nature is clearer. There is an interdependence of all things and a mutually interaction between causes and effects. This existence of anything now results from earlier factors which may be its original cause.

Nothing can exist on its own and this complies with the principle of Dependant Origination (*Idappaccayata*). So, human existence is not isolated but is related to society and nature. Without society and nature, human beings would not have survived. Self-interest in Buddhist economics has a wider meaning, which includes not only oneself but also others in society and nature. When people clearly understand the connectedness and interdependent relationship, co-operation will be a more rational behaviour.

There are two types of co-operation 1) real co-operation which is to help each other to fulfil the basic needs and achieve wellness of life together; and 2) pseudo co-operation which is to take some strong point of the competition concept as a pool-incentive. This implies group participation, or even a whole company, to put all of their co-operative effort into competing with other groups or companies, with the common target of achieving a better outcome for the group (Payutto, 1995). Therefore, compassion and true co-operation are the core values in Buddhist Economics rather than self-interest and competition in the mainstream economics.

Understanding the interdependence and mutual interaction between causes and effects is complex, and not easily comprehensible. Ignorance deludes the mind from being capable to understand this complexity. It needs a purified (calm) mind with its state of neutrality to understand such complexity. To begin with, people need to practice good conduct through *Silā*, to achieve their purified (calm) mind through *Samadhi* for having a calm mind in order to develop their “*pañña*” (ability to understand everything in its own nature without any personal bias or distortion or having a clear mind). These are not separate processes but closely related. The Buddha explained that the human mind had a potential to be developed without any limit. This has already been consistently proven by the Buddha himself, monks, laymen and laywomen by showing that human beings are capable of attaining the highest spiritual level.

The process of developing “*pañña*,” is not in current general education but it is in the Threefold Training which is the way leading to the cessation of suffering (*Dukkha*) or the Eightfold Path. The process of Threefold Training is not covered only for personal practice but also for human activities at the community and social level. These activities include the establishment of the rule, regulation and law, institution and improved activities for people to continue being in the Threefold Training environment. (Payutto, 2000: 604)

There are three parts to this development; it works in the form of spiral dynamics as shown in Fig. 1:

1. Training to develop the morality (*Silā*) is necessary to conduct one’s actions, speech, and livelihood in a moral and proper way on a personal level. On a societal level, this training addresses one’s materialistic surroundings and especially one’s social behaviour regarding rules and regulations. These are meant to protect the individual from immoral behaviour and to enhance good behaviour for societal benefit. So this training covers right speech, right action and right livelihood.
2. Training to develop the stability (*Samadhi*), or concentration of the mind, is necessary for mindfulness at a personal level. On a societal level, it builds a peaceful atmosphere in the work place, the home, and other leisure areas which encourages people to have good, positive, loving and kindness thinking. This training covers right effort, right mindfulness, and right concentration.

3. Training to develop the wisdom (*Pañña*) which is necessary to understand the nature of reality on a personal level. At the societal level, this promotes all education toward more moral and analytical thinking. Educational institutions should train people in the three aspects of morality, stability, and wisdom. This training for *Pañña* covers right view and right understanding. (Payutto, 1995)

The above development process allows us to not only to understand the theoretical concept (*Pariyatti*), but also to understand the application of the theory into practice (*Pattipatti*) and the proof of the results through practice (*Pattivedha*) (Payutto, 2000:105). Training of morality (*Silā*), mentality (*Samadhi*), and wisdom (*Pañña*) are not separate but closely related. Therefore, the Threefold Training could be considered as the development of *Pañña*.

When *Pañña* directs the way of living or behaving in the working place, it will result in optimal resource allocation in the middle way as well as wellness which are the higher level of happiness, generated from giving and sharing and doing good things for society. It also helps those who are still in need to have enough so that they will be freed from physical pain.

Pañña is a very important attribute that can be developed through the Threefold Training and can be cultivated not only at a personal but also at a social level. Business leaders can provide the atmosphere

inside the company for the employee and themselves to practice Threefold Training by:

1. Having business practice comply with the right livelihood in *Silā* which aims not only to produce a good and safe product without negative individual or social impacts but also complies with the rules and laws. The communication should be conducted with truth and good information which will provide the atmosphere for practice right speech. The motivation system including rules and regulations, should not make employees emphasize on rewards such as cash incentives and individual performance, but instead should support employees to have ethical behaviour for practice of right action.
2. To provide a peaceful atmosphere in the workplace and leisure area and support the employee volunteer activity and spiritual training to develop *Samadhi*.
3. To provide a chance for employees to develop their *Pañña* through both on and off the job training to develop *Pañña* especially for understanding the wider meaning of self and happiness.

Methodology

The objective of this study is to explore the practice and performance of a company that adopted Buddhist

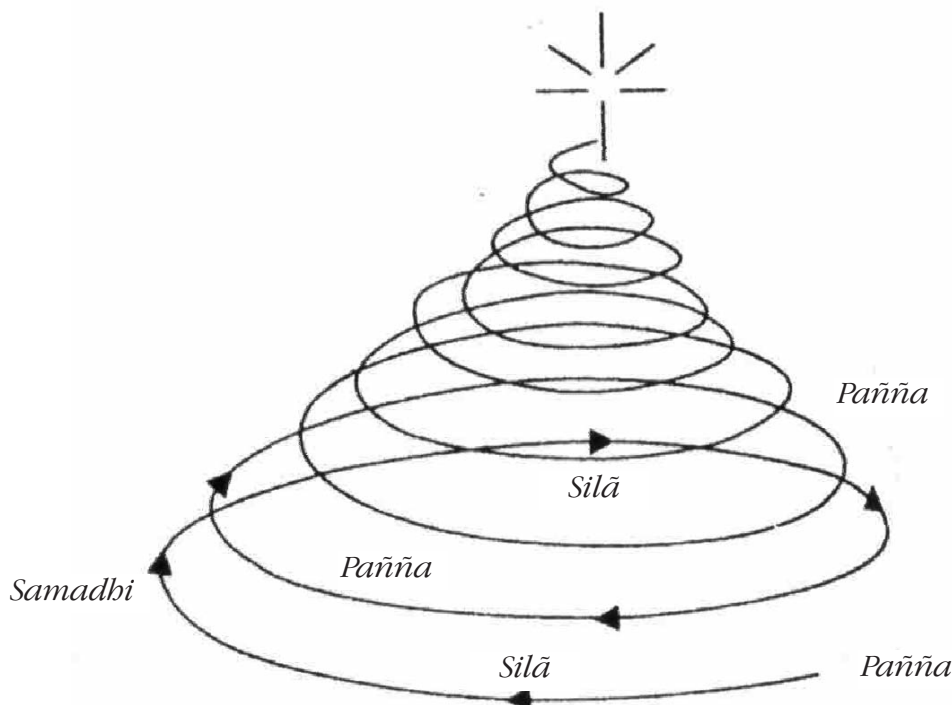


Fig. 1 Spiral dynamic of Threefold Training

Economics. This objective raises naturally exploratory research questions and suggests the case study method should be used as a research strategy. This study is only to explore from the case study while the generalization back to population like the fundamental of survey (Yin, 1994) is impossible to undertake.

Due to the complexity of data collection, the sample size should be limited to not more than 3 cases. The selection of one small, one medium, and one large business enterprises allows a multiple-cases design and should provide similar results (a literal replication) or contrasting results (a theoretical replication) predicted explicitly at the investigation (Yin, 1994:51).

The unit of analysis is the business organization and relates not only to the business management system inside the organization but also includes leaders, staff, and stakeholder of this organization.

Data will be collected from primary sources by in-depth single and group interviews and investigation by the researcher and from secondary sources by public documents, such as newspapers, and in-house documents, for example newsletters and annual reports. This collection method uses multiple sources of evidence ensuring construct validity (Yin, 1994). A case study database will be created to increase a reliability of the entire case study (Yin, 1994: 95)

A pilot case study will be used in this study. According to Yin (1995: 74), the pilot case is used more formatively, assisting an investigator to develop relevant lines of questions, possibly even providing some conceptual clarification for the research design as well.

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A comment on the paper "Buddhist Economics Approach to Business Management by Wanna Prayukvong" from an Islamic perspective.

Muhideen Adesokan, and Ibrahim Umar

The paper begins by highlighting the paradox of the 'market' intermediating the exchange of goods and services for money but yet itself requiring frequent intervention by governments on occasions due to its imperfection or outright failure. Global inequitable distribution of wealth and environmental degradation are shown to be some of the consequences of this state of affairs.

Buddhist Economics drawing on a collection of sage thoughts of the Buddha is proposed as a remedy. In particular, the principle of Dependant Origination (*idappaccayata*) is explained to mean 'effects are due to causes' and to point towards true co-operation and compassion between individuals for collective well being. *Idappaccayata* rests on three elements; *Samadhi*, a state of tranquil mind deriving from having acted for the common good *Sila*, and *Panna*, an unbiased true understanding of reality. Related to them is awareness of acting out value ideals *Pattipatti*. Taken together and imbibed these lead to *Dukkha* the elimination of economic and other forms of suffering.

Similar to the foregoing, Islam prescribes an economic order that supports the establishment of the real world implications of its law, the *shariat*. Islam calls on man to acknowledge his destiny as Allah's (God)'s *khalifah* (agent), on earth and to fulfil the terms of his agency by acting true to instructions of his principal. In the economic field, he is forbidden from charging or paying out *riba* (interest) and called upon to engage in trade and exchange for mutual benefit as well as to establish *zakah*, a state mechanism that redistributes income to the poor. The term '*umma*' or nation which connotes community, collective interest

and endeavour is used in both the Holy Qur'an and the sayings of Prophet Mohammad (SAW) in describing the Muslims.

Islam emphasises on personal accountability for one's conduct and behaviour both in this world and in the world to come. Anything one does either good or bad will ultimately benefit or harm their souls (Qur'an 41-46). This is very crucial in establishing self-restraint against immoral or unethical conduct and behaviour such as greed, amassing wealth for its own sake and selfishness. The concept of personal accountability is applicable to our modern day fictitious personality – the corporation. Destroying the environment, wasting of resources and maximization of profit for its own sake have all been condemned in the strongest terms and described as showing ingratitude to the creator of the universe. The individual, and by extension the corporation, who engages in such immoral acts are referred to as "the brothers of the devils" (Qur'an 17:26).

The Qur'an stated that no one should forbid others from enjoying the good things of this life (7:32) but its teaching on consumption emphasizes on meeting genuine needs rather than satisfying unbridled lust and incessant consumption that capitalism promotes. For instance, one of the famous teachings of Prophet Mohammad (SAW) was that if one goes for a meal, they should first of all be hungry. Then they should divide their stomach into three portions: one-third for the food, one-third for drink and the other third to be left empty for easy breathing. Any act of gluttony which leads to more intake of food or water at the expense of breathing are forbidden and akin to doing wrong to one's body and soul. This example of fundamental virtues of balance, restraint and modesty can be applied to almost every other thing. The global rat race, characterising the capitalist system, where only the fittest of the fittest shall survive, and where materialism and ardent desire to amass wealth for its sake has become the ultimate ambition is eloquently condemned:

"The mutual rivalry for piling up (the good things of this world) diverts you (from the more serious things), until ye visit the graves. But nay, ye soon shall know (the reality). Again, ye soon shall know! Nay, were ye to know with certainty of mind (ye would beware). Ye shall certainly see Hell-Fire. Again ye shall see it with certainty of sight! Then shall ye be questioned that day about the joy (ye indulged in!)" (102:1-8).¹

The main contrast between the Buddhist and Islamic perspectives is the latter's prescription of sanctions

and the establishment of courts to enforce its laws. Obviously this relates to the nature of Islam as a communal way of life with regulations for protecting the integrity of the community. Whereas some individuals will act in the common good and aim for Godly values without much prodding, the reality is that a significant group need to be coerced by community/state. Take the instance of the individual/organization as self interested profit maximising entity leading to the devastating consequences alluded to in the paper. There need to be enforceable sanctions to keep this group in check and ensure that they do not destroy the community in pursuit of their selfish interests. Lofty ideals are not enough in the real world. They need to be backed up with enforceable sanctions for businesses to act as prescribed.

A Christian response

Peter Davis

The Christian starting point is one of individual responsibility for conduct leading the individual soul, as it travels through life, to come into closer relationship with the risen Christ. During the journey of life each soul has choices in terms of its conduct towards the other souls it comes into contact with and the rest of God's creation. Right conduct rests on making productive contributions for the benefit of oneself and society whether in terms of spiritual, cultural, social or economic life but always in the context of a developing relationship with Christ.

This is not in any way to suggest there should not be any social regulation. The Holy Bible tells Jews, Christians and Muslims that God is a God who loves Justice, and the Torah lays down many explicit rules to ensure equitable treatment and the release of the poor from debt and the Qura'n also has teachings on how to regulate economic relations. I heard nothing in the presentation on Buddhist Economics to suggest that the Buddha was against regulation that leads to the public good. So it appears that all parties to this discussion recognise the need for legal regulation of the economy although we may differ over the detail to be included in such legislation.

The question comes down not to whether or not regulation is important but to whether regulation alone can be enough. So far laws, codes and independent auditors etc have not stopped corporate fraud and wrongdoing on a massive scale. Corruption can be found endemic in countries where each one of the faiths represented in this discussion pre-dominates.

Take the cases of Indonesia, the Philippines' and Thailand for example in Asia. Africa too both North and South has huge corruption problems. Thus despite regulation supported by religious cultures that are strongly entrenched corruption remains a serious problem. Even when it is less of a general problem in a given society serious cases of wrong doing like Enron (USA) and Baring Bank (UK) can occur with disastrous consequences for many stake-holders. Also, even when negligence and management failure leads to massive loss of life and personal injury, as in the tragic case in India of Union Carbide, holding the company to account and getting justice is difficult to achieve.

Nor can we with confidence suggest any one model of business ownership or governance. We have had for centuries the example of co-operative and public as well as private organizations with various ownership and governance structures all purporting to support the public good and optimise welfare. Yet poverty and injustice persist and the collapse of communism shows us that, however good the intentions of reformers is, a monopoly of power leads to corruption and injustice. As the editor of a journal promoting co-operative ideals and organizational forms focusing on problems of management and development in co-operatives I have to say that co-operatives are just as prone to corruption as any other organization.

I do not support co-operative development because I believe it to be morally superior, but because they have the purpose of serving people in their communities with ownership, rewards and governance based on labour rather than capital. It's the co-operatives' potential ability to give access to the marketplace and leverage to the poor that make co-operatives an important additional model for business. I stress an additional rather than alternative model of doing business. Co-operatives can give a wider choice and therefore counter the tendency to monopoly or oligopoly in the marketplace and empower people whose means make it hard to register their needs effectively in the market by other means.

The Buddhist critique given in Wanna's paper of the "imperfect market" is clearly justified as many of the fundamental sectors of the global economy are dominated by oligopoly; particularly in high technology, some areas of core manufacturing, communications and energy. The Buddhist emphasis on the individual focusing on reality may be significant too as it helps people to challenge accepted modes of behaviour and question patterns of personal conduct such as over-consumption and exploitative relationships. It also addresses the issue of

manipulation by advertising, which is an important issue today in its use of sexuality and the appeal to other base instincts together with the industries often unethical way children are targeted.

The Buddhist principle of non-attachment has great contemporary relevance I think. In our consumer society people are often judged by their branded fashion statement or the size and make of their car. The need for self-reflection and self-examination are important elements in the Buddhist and also Christian monastic traditions as well as being important for all believers. It is a key tenet of the Catholic scholastic tradition that faith must be in line with reason and not contradicted by it. Self-examination based on reason and reality are the foundations for the attainment of a good life and salvation beyond.

In the Jewish and Islamic traditions the emphasis is on rewards according to works or deeds based on justice under the law. In the Buddhist tradition human kind is seen as rewarded or punished in accordance with karma (results of past individual actions). Jesus, however, challenged the notion of mutuality and equity in exchange and replaced it with the more radical notion of giving without receiving. By Grace, salvation comes to an undeserving humankind, rather than by works, which for Christians arise as the fruits of God's Grace. Acts of charity are not those delivered with the thought of reward or based on how deserving a person may be but out of compassion for human frailty and need. These Christian ideas have been formulated by some secular political idealists on the left into the formula "from each according to his/her power or resources and to each according to their needs".

Certainly a gracious employer gives his workers according to their need for a living wage rather than the value of the respective productive inputs (see Mt 20:1-16) Like many of the parables there is more than one reading of the story but the traditional readings do not contradict my general point. If we focus on God and demonstrate our love of God in our service to our neighbour as we are taught by many Catholic and other saints (St Teresa of Avila for example) there will be little opportunity to be trapped by avarice, gluttony, and greed. Having too much is possibly a bigger distraction than having too little, certainly Jesus taught this (see Matt.19:24.)

No law or rule or structure is morally superior to the morality of the individuals who control it. That's not to say we should not strive for economic justice, using law to regulate organisational and individual behaviour but before God we must always in conscience account for ourselves. What we desire is, as much as what we own,

a part of that accounting. Virtue can only be practised by individuals. We can help others by good example, good teaching and good laws. In the end good managers are made not born. For the Christian, human development is impossible without grace, made possible by God's act of self-sacrifice on the cross and guaranteed by Christ's resurrection from death. The "Economy of Communion" is the Christian version of Buddhist Economics. It is an economy based on self-sacrificial love. (See book review)

The question is how do we develop people to act in accordance with justice and virtue? Aristotle, an ancient Greek philosopher who had an important influence on both Muslim and Christian thinking, wrote somewhere that excellence was the product of forming good habits. A soul who habitually seeks to open itself to communion with the risen Christ can only act in the service and interest of his neighbours benefit according to God's Will. Buddhists have a point in emphasising meditation as a habitual exercise to help reach the truth. Muslims are right to insist society has laws to protect itself. But Christians would want to add that to rely on law or human effort without God's grace cannot lead to either Truth or Justice. In the end we need an economy that is rooted as much in mercy and compassion as in justice or self-justification. In the end it comes down to the need for forming habits of self-discipline and godly behaviour by focusing on the risen Christ as our model for human behaviour and source of salvation and redemption. Without individual communion with Christ in the full confession of human frailty there cannot be any finally just economic system.

Notes

- 1 Translation from Abdullahi Yusuf Ali

The Sharing Economy. Solidarity Networks Transforming Globalisation

Lorna Gold, Ashgate, 2004. ISBN 0 7546 3345 4

This is an important book which traces the history, theology and practices in its global economic and social context of the Focolare Movement. This movement describes itself as;

".....an international movement, inspired by the gospel, working for unity in all spheres of life. For over sixty years it has drawn together people of all Christian traditions and from many of the world's religions, alongside people with no formal faith, who share the aim of building a more united world."

<http://www.focolare.org.uk/>

For a recent illustration of its interfaith dialogue see the recently held dialogue between the Focolare and the Buddhist Movement.

<http://www.focolare.org/articolo.php?codart=5776>

The idea of giving to the poor and living a celibate life in the community may seem out of tune with the individualism and materialism of the modern world yet these foundational inspirations and the principle of unity have led to a truly global movement which in many ways is a Catholic response to the movement of globalisation driven by privatisation and liberalisation of the world economy and the collapse of communism. Described by the Church as a work of Mary it is deeply committed to building solidarity and community between the peoples of the world of all faiths and none. The Focolare journal is known as New City

"New City is the magazine of the Focolare Movement, which takes as its inspiration Jesus' prayer to the Father 'May they all be one'. (John 17: 21) The Focolare Movement works to promote mutual understanding and respect through dialogue. This can take many forms, from the simple sharing of experiences between individuals, to large-scale international conferences. Whatever the level of the dialogue, the underlying principle is always love: which means openness to the other, getting to know them, and respecting them and their cultures and beliefs."

<http://www.focolare.org.uk/Newcity.htm>

Essentially Lorna Gold documents with a combination of infectious idealism and social science rigor the workings of this movement which adopts what might be described as a Christian version of a mixture of Stakeholder Management, Networking Theory and Cluster Theory (from economic geography). The results are an impressive detail and clear outline of the structural contours and performance indicators of this movement. At the level of social theory her most interesting chapter is "Ch 9. Rethinking Culture and Economy: Lessons from the EOC" (Economy of Communion) Lorna emphasises the importance of cultural values in delineating the space between the market and the domestic economies. Indeed the economic geography of the Focolare in many ways reflects the inspiration of Robert Owen's communitarian tradition where community is about more than economic co-operation but more importantly an opportunity for education in how to live co-operatively. The latest developments on this can be found on the movements website.

"There are 35 little towns in the world in various stages of development with the characteristic of the culture in which they have arisen. They are miniature towns with houses, schools, businesses and places of worship. Because of the style of life they promote they can offer a model to big cities on the way to live together."

<http://www.focolare.org/page.php?codcat1=247&lingua=ENG&titolo=focolare%20movement&tipo=focolare%20movement>

Renewal of religion was seen by the EOC founders as the way to a social revolution based on love rather than class but leading none the less to greater social and economic equality within the community. Quoting Cambon, (1999, p2) Lorna states, "In the Trinity everything is in common". Later in the chapter Lorna cites cases of business failure, however, to counter any sense of "Trinitarian Fundamentalism" as she puts it. This book should be of interest to all Christians and other people of faith who are active in the co-operative movement but perhaps also given the Focolare movement's apparent difficulty in translating itself into the world of business (see p173) the EOC should also take an interest in that very Catholic of business models,

so frequently approvingly referenced in the Social Doctrine of the Church the co-operative movement.

It is this movement that has for one and a half centuries made a solid contribution to what Lorna Gold in her conclusion considers to be “.... one of the most exciting developments within EOC to date.” Namely, the linking of the “...micro level alternative with the macro level policy issues.....” (see p194) It was Gandhi I think who first said “Think Global and act local” It is exciting to see that the practical EOC demonstration of the social - economic expression of Christian spirituality and theology has a resonance across religious and secular humanistic aspirations. I recommend co-operative managers read this book whether they believe in God or not.

The Editor



UNIVERSITY COLLEGE CORK
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**HIGHER DIPLOMA/MSc in CO-OPERATIVE ORGANISATION,
FOOD MARKETING AND RURAL DEVELOPMENT**

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**National
Association of
Co-operative Officials**

National Association of Co-operative Officials (NACO)

NACO is a Management Association and an Independent Trades Union, representing managerial and professional grades within the United Kingdom Co-operative Movement. NACO has sole representational rights for managerial and professional staff in all UK consumer co-operative societies and within the Co-operative Insurance Society Limited.

The range of services available to members encompasses collective bargaining on pay rates and terms and conditions of employment, professional advice, legal advice and individual representation – always delivered by a full-time professional official of the Association. The Association also provides ancillary services including discounted products, educational seminars and residential conferences.

NACO has grown and developed to be a major and respected professional body representing the vast majority of managers and professionals in consumer co-operatives. The Association seeks to work in partnership with co-operative societies and the excellent relationships developed help us support members individually and collectively. The Association is now looking to expand upon its traditional base, and develop relationships with members in housing co-operatives, farming co-operatives and credit unions to name but a few.

Affiliate membership opportunity

NACO also wishes to cross traditional barriers and share practices and experiences with similar minded bodies with links to the worldwide co-operative movement. In this respect, moves are in place to create an affiliate membership to allow fraternal organisations to develop links with NACO in the United Kingdom. Any parties interested in developing such a relationship should contact General Secretary Neil Buist.

Contact details: Tel - 0161 494 8693 Fax – 0161 366 6800

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