CO-OPERATIVES UK

NEW INSIGHT 11

Good governance in minority investor-owned co-operatives

A review of international practice

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> "All the guidelines on corporate governance agree that the board itself should be able to present a united decision-making body. In order to do this, there is a need to orchestrate the various interests."

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Summary

The way in which the business is owned is a distinctive and defining feature of any co-operative enterprise. Co-operatives are owned by members - those involved in the business in one way or another. So what happens when co-operatives open up to a minority ownership share of external investors?

The reasons for doing this can vary. It may be an investor-owned business that is considering moving towards full co-operative, member-ownership, as in the case of the efforts of supporters trusts in football. It may be a co-operative business on the opposite path, towards demutualisation. Or it may be a hybrid model, needing to bring in new investor equity alongside existing co-operative capital.

In terms of business focus and direction, a model of mixed investor and member ownership offers a different profile of risks and opportunities. This report looks at the theory and evidence from around the world on models of this form, with close attention to the issues that arise in terms of the design of good governance for enterprises of this form.

The main case studies are to be found in the fields of agricultural and financial co-operatives, with the addition of businesses, notably in the insurance field, that are part-owned by co-operatives.

- In the last 20 years, agricultural co-operatives have faced enormous pressures to grow into large agri-food businesses, so as to compete with transnational corporations that threaten to reduce them to the – increasing unprofitable – role of a marketing co-operative.In order to move along the supply chain they have needed masses of capital, sometimes far more than they could raise from their members. Some of them, notably dairy co-operatives in Ireland and Switzerland, have put their ownership stake into a holding company and then floated the co-business on the stock market. However, most co-operatives have resisted this option and have found other ways of raising capital that do not compromise farmer ownership. Examples covered in this report include Kerry Creameries, Glanbia and Emmi.
- In financial services, Credit Agricole is the largest French mutual bank, but for historical reasons at the national level it still has a substantial private equity stake, though at the regional and local levels it consists of independent co-operative banks. Kent Reliance is a UK building society whose board and management put a great emphasis on growth, and in order to raise the capital needed for this it sidelined its member ownership stake into a holding company and floated a new company part-owned by a private investment firm. Kenya Co-operative Bank was owned by agricultural co-operatives, but it floated on the stock market and put its farmer ownership stake into a holding company.
- Some co-operatives have invited in a minority investor-ownership stake and then decided that it was a mistake – examples include the French co-operative bank, BPCE, and the American insurance provider, Nationwide Mutual.

How should minority investor-owned businesses be governed? The introduction of investor-ownership into a co-operative business, or vice-versa, will complicate its objectives and in principle make it harder to govern. It seems likely overall that it is a less stable pattern of ownership - although there are counter-examples which have endured.

If the voice and interests of members are fragmented, then the focus of investors, on financial returns to investment, can crowd out other ways of working and serve to unpick the advantages for members that a well-performing co-operative can have.

In other cases, the tensions can potentially have productive value. Tensions do not have to result in conflict and there are examples of creative governance design that can encourage good communication and the alignment of interests. These include the use of two-tier governance boards more common in other European countries and models in which co-operative members can be offered the same model of communication and dialogue that is open to investors.

“Tensions do not have to result in conflict and there are examples of creative governance design that can encourage good communication and the alignment of interests.”

There is not, it would seem, a need for any separate governance code. Rather, the analysis suggests that the tensions that are inherent in the model simply make it all the more essential that there is a focus on good governance, many elements of which are, after all, shared across both co-operative and investor-owned sectors.

Ownership is not fixed. But changes in ownership for co-operatives, with the introduction of minority investors, need to be considered with care, with an eye to the business implications and with close attention to the highest quality of governance.

Introduction

In defining co-operatives, several attributes may be seen as important, but the question of ownership comes first. In the simplest definition, a co-operative is a business owned, controlled and run for the benefit of, its members.

Ownership is the most fundamental defining characteristic, from which the others follow, and if these others are compromised – because the business is only partly controlled by the members or they do not get much benefit – then it is still a co-operative, even if it is a failing one. The International Co-operative Alliance's identity statement starts further back from the 'association of persons' who come together to meet their needs through a co-operative, but it also emphasises the importance of the enterprise being 'jointly-owned'.

This simple defining characteristic is complicated when investor-owners are allowed into the business, and the purpose of this report is to explore implications for governance of a co-operative. There are two processes by which member ownership and investor-ownership can come together. The first is uncontentious. People may buy shares in an existing business and organise together as a co-operative group to exert influence over it. When they become majority owners, the business has reached a point where it can be recognised as being a kind of co-operative. Employee share ownership schemes and football supporters' trusts are good examples.

In the field of banking, Credit Agricole is another, more complicated, example where different types of bank have merged and converted into new forms. While it used to be state owned and still has some private shareholders, it has become majority owned by co-operative banks over time.

The second process is more controversial. A co-operative business may need an injection of capital that it cannot raise from among the members (at least not as quickly as it needs). There are some good reasons for this – it may: be failing and so need to raise capital to meet business losses; be meeting stiff competition and so need to expand quickly in order to defend or capture market advantages; be looking to invest in innovation and new technology or to expand into new markets; or it may simply be required by regulator to raise levels of capital reserves. There are many advantages in being a member-owned co-operative.[1]

One of the disadvantages is that when capital is needed quickly the co-operative cannot raise it by going to the market and offering ownership shares. Sometimes this means it is tempted to take investor-owners into the business through a stock market flotation. If the co-operative consists of individual members, it takes the members' ownership stake and puts it in a holding company that then acts as an institutional investor in the business. The holding company is a kind of unseen presence behind a business that has a share price, practices 'investor-relations' and looks to all the world like a conventional investor-owned company. If the co-operative is a higher level organisation owned by other co-operatives (like some insurance co-operatives), or if it is a wholly-owned subsidiary of a co-operative (like the UK Co-operative Bank), then the owner-co-operatives already have a separate corporate structure in which to enter the new business as institutional shareholders.

The way we value these minority investor-owner co-operatives (for convenience we will now refer to them as MIOCs) depends partly on their history and current trajectory. Co-operatives that started off as investor-owned businesses but are becoming more co-operative over time have a moral advantage; nobody would argue that they are not 'real' co-operatives, even if they are not yet purely member-owned.

Co-operatives that allow investor-owners into their ownership structure are generally seen as having weakened their co-operative nature, because they are allowing a different type of ownership where voting power is weighed according to the size of shareholding and owners are remunerated as investors rather than as users of the business. It can be seen as a partial demutualisation; a part, at least, of their co-operative is now run along different lines, with different priorities and underlying principles. The governance of the business will have to be shared, with consequences that are difficult to predict.

The pressure to raise capital by changing the ownership structure

In the 1980s it was agricultural co-operatives that faced the pressure to bring investor-owners in, whereas in the last few years it has been co-operative banks and building societies that have had to consider this option. Following the banking crisis of 2008, they have been facing demands from the banking regulators to become more highly capitalised.

At the same time, low interest rates, falling profits, a long economic downturn and the need to make provision for non-performing loans, have meant they have not been able to build up their reserves through the traditional method – successful trading. Having a high level of reserves has cushioned the European co-operative banks; they tend to pursue a low-risk business strategy and to build up the reserves in the good times in order to prepare for the downturn.[2]

The same is true of Canadian credit unions, though the American credit unions have had to make good serious losses made by some of their central organisations. The UK building societies face similar pressures, though so far only one society has opted for the introduction of minority investor owners. The preferred solution for co-operative banks, credit unions and building societies has been a process of merger between capital poor and capital rich societies.

The proposed partial flotation of the UK Co-operative Bank raises some important questions. Will the governance of the Bank change, and if so, in what direction? Can the Bank continue to be a consumer champion, or will the addition of new investor-owners divert it into other purposes? Will the different types of ownership lead to conflicts of interest and if so, how will these be resolved? Will conflicts of interest prove costly, eventually leading to the Bank moving towards a more pure form of ownership, either by remutualising or becoming entirely investor-owned? Even if there are no big changes, will there be 'mission drift' towards a different business model? What will be the effect of a more mixed governance structure on business performance? Will it make the Bank more or less successful as a high street bank?

All of these questions come down to this – how can appropriate member ownership, control and benefit be assured in the governance model of an MIOC? Even so, it is difficult to answer this question. First, there are no exact precedents from which we can learn. So far, only one other co-operative bank has changed its ownership structure in this way. OVAG, the central bank for 60 Austrian local Volksbanks, made serious losses of over €1bn each year between 2009 and 2011, due to its exposure to Eastern Europe and Greece via its international subsidiary Volksbanken International. The Austrian government has taken a 43 percent ownership share. The lessons for governance are limited, since this was a part nationalisation not a privatisation, and the government expects to sell its share by 2017.

Second, the UK Co-operative Bank is not actually a co-operative bank, in the simple and accepted sense of a bank owned directly by its customers as members. In Birchall's typology of 'customer-owned banks', the UK Co-operative Bank comes under the 'other' category of banks owned by other types of co-operative.[3] There are not many of these, and none that have faced the same kind of situation the UK Bank is in at present. There are no precedents for this kind of hybridisation, and so the report will be searching for lessons from banks and other business organisations that are similar in some respects.

This report will consider three types of evidence:

1. There is recent evidence concerning the different objectives of co-operative banks compared to investor-owned banks in Europe. The co-operatives have different priorities, with more of a focus on service rather than profit, on retail rather than investment banking, on low-risk rather than high risk activities. There is evidence of a commitment to relationship banking and to local economies. The implications of this for co-operatives that become MIOCs are that the introduction of investor-ownership will complicate its objectives and make it harder to govern.
2. There is some literature on different forms of ownership, and the implications these have for governance. There are two opposite views, one that only a simple ownership structure will work and one that a multi-stakeholding approach is possible. The UK Co-operative Bank, with its proposed new hybrid ownership structure, will become a kind of natural experiment that should enable us to see which of these theories is correct.
3. There are some examples of co-operatives that have minority investor-ownership, and investor-owned businesses that are part owned by co-operatives. Case studies will be provided of the most interesting of these and lessons can be drawn for the future governance and control of MIOCs.

Evidence for the different objectives of customer- and investor-owned banks

In order to find out what a co-operative gains and loses by becoming an MIOC, it is useful to consider the evidence for the different objectives observed in the two pure types of European co-operative banks and their competitors, the investor-owned banks.

In Western Europe, the co-operative banks have around 20 percent of the market, and are competing directly, and usually successfully, against both investor-owned and savings banks.[4]

Economists have long ago identified the relationship between a bank's shareholders and its customers as an 'agency problem'. Equity shareholders tend to prefer a higher risk profile for the institution than would depositors due to the fact that they have limited liability; their potential for profit is unlimited, while the potential for losses is limited. Depositors do not share in the profits, but they do share disproportionately in the risks. In co-operative banks this particular agency problem is avoided, since the owners and customers are the same people. There is no separate shareholder interest and the banks usually work in the interests of their customers.

A recent report for Rabobank spells out what it means when co-operative banks successfully put customers at the core of the business. There is a long-term focus on customer value. Healthy profitability is necessary but it is not a goal in itself. The banks operate in local retail markets, so have access to stable sources of funding in customer deposits.

Centred on relationship banking, they produce strong local ties and networks. They have an informational advantage that makes them better equipped to assess creditworthiness, so they tend to have higher lending levels than their competitors.[5] Clearly, the introduction of investor-owners into financial co-operatives will lead to a change of focus, no longer entirely on the needs of the customer but also on the expectation of investor-owners for dividends and an increased share price.

Another way of describing the differences between ownership types is by looking at the 'bottom line'. Co-operatives have a 'dual bottom line', focusing on customer value as well as equity. They can use their comparatively low costs and (usually) abundant capital and lack of a profit maximisation constraint to pursue expansion.[6] They only need to remunerate the part of capital that is in member shares, and then not generously. Because they do not have to pay external shareholders, they can reduce the margin between the interest rates they charge to borrowers and pay to savers. They can even decide to sell products at below current market price, incorporating the anticipated profits into the products. Consequently, they are able to attract a large share of retail deposits, so experience comfortable liquidity, with high deposit to loan rations.

In good times they become net lenders in interbank markets. In bad times, they build up reserves to cushion them against poor performance; the co-operatives simply do not distribute as much dividend to members, or they adjust their prices upwards so as to extract more surplus.[7] It is true that they cannot issue shares in order to raise capital easily and quickly, nor can they rely on the limited amount of capital raised through member shares. However, they allocate virtually all their earnings to reserves that are then used to finance further growth. Their central banks are usually able to issue various forms of hybrid capital, and some of these banks can attract capital via listed subsidiaries.[8]

Unfortunately, these characteristics are only true of pure co-operative banks. They only apply in a limited way to banks owned by other types of co-operative. The UK co-operative banking and building society models are more vulnerable to shortage of capital, and they not been able to build up the level of reserves that the European co-operative banks have achieved. The introduction of investor-owners can be expected to ease the problem of lack of capital in the short term, but to make it more difficult for the MIOC to choose to build up reserves rather than pay out dividends in the long term.

With a few exceptions, co-operative banks have proved to be much less risky than the investor-owned banks. They are not under pressure to maximise profits, a pressure that in investor-owned banks often leads to insecure lending and the sale of complex products that pass the risk on. They are usually more highly capitalized than their competitors. They are under less short-term pressure and are more inclined to adopt a longer-term horizon in their business decisions and lending policies. It is less easy for them to raise external capital independent of their members, and so they avoid reliance on wholesale markets. They are not subject to the pressure from investors for immediate returns, and so a longer-term focus results.

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Their business strategy is all about relationship building; a number of studies find that co-operative banks are more willing to establish a long-term relationship with their clients, especially with SMEs.[9] They have been found to have a more stable stream of earnings than other types because they are able to use their reserves as a buffer.[10]

Unlike the ‘too big to fail’ investor-owned banks, the biggest co-operative banks have been found to be better able to smooth out their gains and losses during the peaks and troughs of the business cycle.[11]

Financial co-operatives in the UK (credit unions, building societies, the Co-operative Bank) have never had the kind of mutual insurance against risk that co-operative banking groups in Europe have been able to call on. Yet they have been generally been stable and risk-averse, and have also focused on relationship banking. The introduction of investor-owners could be expected to change this focus towards riskier investment, and diversification into other, more profitable types of banking.

Evidence from the literature on governance

Given that in an MIOC there will be tensions between the objectives of consumer and investor owners, what does the literature predict about their governance?

Hansmann gives the simplest and most powerful explanation for the success of consumer co-operatives in his book The Ownership of Enterprise.[12] He shows that the costs of ownership and the costs of market contracting are crucial to the survival of a business organisation. The co-operative business model survives when the costs of market contracting between the firm and its patrons are too high and it pays to bring one of the patrons into membership. This is what co-operatives have done.

If the costs of ownership are too high, though, this will make the co-operative ownership option less efficient than the investor-owned option, even in the presence of market failure. Hansmann defines costs broadly as 'all interests and values that might be affected by transactions between a firm and its patrons', and he makes it clear that the valuation is both subjective and objective.[13] The main source of costs in a co-operative is heterogeneity between the members, causing disagreement and increasing the difficulty of governing.

If he is right, then the introduction of two separate classes of owner in a co-operative will lead to much higher ownership costs. Eventually, the business will become uncompetitive because it has to pay costs that are higher than those of its competitors. It will either go out of business or one interest group will buy out the other; the MIOC will return to co-operative ownership or be demutualized and fully floated on the stock market. Costs will then drop and become closer to the average for the industry sector.

Hansmann chooses to focus on costs, asking 'What is the lowest-cost assignment of ownership', and he means by this 'the assignment of ownership that minimizes the total costs of transactions between the firm and all of its patrons'. However, he also suggests an alternative, 'the assignment of ownership that maximizes the total net benefits' (p21). This is the kind of approach taken by Tushaar Shah in his monumental study of agricultural co-operatives in India. In a study of several hundred agricultural co-operatives in India, Shah found that success could be explained in relation to governance. His theory is that there are three conditions for success: the purposes of the organisation are central to the members; the governance structure ensures patronage cohesiveness; and the operating system finds competitive advantage in the relationship with members. To achieve these conditions the members have to be in control of governance.[14]

In the UK Co-operative Bank the members have never been directly in control. It is only recently that its owner, the Co-operative Group, introduced a change that allowed people to become members through the Bank. They are, however, becoming members of the Group, whereas in the European co-operative banks and the North American credit unions they become members of the bank, with full rights to elect representatives to its board of directors. However, there is no doubt that there is a strong association in the minds of members between the Group and the Bank, and Shah's conditions for success have been present. The purposes of the organisation are central to the interests of the members and, with their strong endorsement of the Bank's ethical policy, to the interests of the wider group of customers. The governance structure has helped to deliver a service that has won many awards and whose quality has been endorsed in customer surveys. The 'rewards' from being a Co-operative Bank customer, if interpreted widely, include the satisfaction of supporting the ethical policy, the emphasis on sustainability and diversity, and so on. The operating model of the bank reflected a niche competitive advantage in the relationship with customers, though it has until recently neglected the idea of membership.

If Shah is right, then the introduction of a new class of owner whose interests are not aligned with those of the members will lead to a decline in performance. The purpose of the organisation will be less central to the needs of the owners, the governance structure will have to reward two classes of patron, and the competitive advantage of being a member-owned co-operative will be lost.

There is a more optimistic view derived from the idea of stakeholding. Advocates of a stakeholder view of governance take a more relaxed definition of ownership, and focus on the rights not of formal owners but of interest groups who are affected by the way the business is run. The Co-operative Bank itself took this view during the 1990s, publishing extensive annual stakeholder reports that evaluated the effects of the business on customers, staff, suppliers, the local community and the wider environment. The idea is that governance on behalf of the formal owners is not enough, and that the wider impact of the business should be measured and debated. Not many advocates of stakeholding would go so far as to suggest that all stakeholders be given voting rights, being content to leave the issue of ownership alone. Critics take a 'shareholder' view, focusing on the rights and duties of the legal owners, and rejecting claims that all stakeholders should have rights in relation to the business.[15]

When several stakeholders are taken into full ownership by way of shareholding or membership, the debate becomes more serious. Some types of co-operative are multi-stakeholding, deliberately offering different categories of membership to more than one stakeholder. The Eroski retail co-operative in Spain has employee and customer members, while the ICoop group in Korea has consumer and producer (farmer) members. The social co-operatives in Italy that provide care services to disabled and vulnerable people are, by law, required to offer membership to employees, service users and carers.

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However, multi-stakeholder co-operatives are quite rare; probably because in taking such different interest groups into membership they increase the costs of governance. They are more prevalent in sectors that rely on government funding rather than on trading in a market, because here the interests of different stakeholders are less sharply divided, and it is easier for them to agree on the organisation's objectives.

Also, it is possible to devise two-tier governance structures that provide a means by which different interest groups define their objectives and then come together in a board of directors, having reconciled their differences before issues come to the board.[16] However, the empirical evidence for this is sketchy.

In the banking sector, in the closely related sector of insurance, and in other sectors where there are large co-operatives (notably agriculture), there are examples of mixed ownership structures that may prove instructive, and it is to examples of these that we now turn.

Evidence from case studies

A search through the Global 300 listing of large co-operative businesses provided by the International Co-operative Alliance, and through the list of banks provided by the European Association of Co-operative Banks, produces four different types of hybrid organisation that may provide lessons for co-operatives considering becoming MIOCs.

There are co-operative banks that have an investor-shareholder ownership stake. Then there are other types of co-operative that have an investor-ownership stake, notably some of the bigger farmer co-operatives that have expanded globally in the agri-food business. There are conventional investor-owned companies that for various historical reasons are part owned by co-operatives. There are not many of these, since co-operatives have preferred to set up and keep their own businesses through the mechanism of federation. Finally, there are co-operatives that used to have an investor-ownership stake but have bought this back, sometimes explicitly in order to simplify their governance structure again.

Co-operative banks that have an investor-ownership stake

There are not many co-operative banks that have allowed in an investor-ownership stake. Like most agricultural co-operatives, they prefer to enter into joint ventures with investor-owned companies, or set up mixed-ownership subsidiaries, or to find ways of raising capital from their members. Here are three examples.

Credit Agricole is the largest French mutual bank, but for historical reasons at the national level it still has a substantial private equity stake, though at the regional and local levels it consists of independent co-operative banks. Kent Reliance is a UK building society whose board and management put a great emphasis on growth, and in order to raise the capital needed for this it sidelined its member ownership stake into a holding company and floated a new company part-owned by a private investment firm. Kenya Co-operative Bank was owned by agricultural co-operatives, but it floated on the stock market and put its farmer ownership stake into a holding company.

Credit Agricole

Credit Agricole is the one of the largest banks in Europe, and is the market leader in France in retail banking. With 150,000 employees and 51 million customers, it dwarfs the UK Co-operative Bank, but it has an interesting hybrid ownership structure. It was founded in the 19th century by government to meet the needs of farmers, but in 1988 it was converted to a mutual, and then recently at the national level it was converted again into a joint stock company. It has a mixed ownership: Credit Agricole's central and regionals are listed on the stock exchange, but 56.3 percent of its shares are owned by 30 regional banks through their holding company, SAS Rule La Boetie (in return, the central owns 25 percent of the share capital of the regionals). Institutional investors own another 27.9 percent, individual shareholders own 11.1 percent, and employee mutual funds own the rest.

The regionals are themselves owned by 2512 local banks. Seen from below – from the point of view of individual owners - it has 6.9 million 'mutual' shareholders and 1.2 million investor shareholders. The mutual shareholders, or members of the local banks, elect directors to the regionals and own most of their share capital. They also have a parallel democratic structure in their national federation (Fédération Nationale du Crédit Agricole), where the Group's main 'orientations' are decided.

Credit Agricole shows that it is possible to have a majority shareholding of consumers and a minority of investors. However, the consumer interest is well organized through the local and regional banks, and it ensures that the consumer voice is well orchestrated in the central bank. The individual shareholders have a shareholders' club, through which they receive regular information and can attend learning sessions designed specifically for them. They receive a newsletter four times per year, and a copy of the Shareholder's Guide on request. They may attend "Rendez vous du Club" meetings, meet management and take part in cultural and sporting events sponsored by Crédit Agricole.[17] This suggests that it would be useful for MIOCs to organize the shareholder interest in such a way that investors are engaged with the bank and understand more about it.

Kent Reliance

One of the consequences of the massive bailout of banks in the UK has been that building societies have found it difficult to raise capital for expansion. In 2008, the wholesale money market froze and then slowly began to lend again, but the massive injection of government funds into the big banks gave them for a time an unfair advantage.

At this time, Kent Reliance was the fastest growing building society. It had achieved this mainly through a subsidiary that had bought the Jersey mortgage business of a bank. It had also kept its costs down by hiving off much of its administration to two subsidiaries in India. By 2010, it was in sound condition but could not find the capital to enable it to continue to expand. In 2011 the society demutualised into a new investor-owned bank called OneSavings Bank. There are only two owners: the private investment firm, JC Flowers that has a 41 percent ownership stake, and a new Kent Reliance Provident Society that owns 59.9 percent. This means that, through the provident society, the members of the original society still have a substantial ownership share, but at one remove from the business.

The provident society has two roles: first it is the holding company for member shares in OneSavings Bank Plc. Secondly the provident society will operate its own business, taking over some of the new banks high street outlets and offering a range of its own services to its members such as KPRS rewards.[18] However, it is clear that as a holding company it is far from the active governance of the business, and has been reduced to providing members with a fairly thin offering of discounts at participating retail outlets. This is not the way to go for any co-operative wishing to preserve a member voice.

Kenya Co-operative Bank

Kenya Co-operative Bank was established in 1965, with capital raised from the agricultural co-operative sector. In 2008 it was floated on the stock market, with the ownership share of 3,800 co-operatives ring-fenced in a holding company with a 65 percent stake. This means the co-operatives are still in control. It is helped by the fact that the voice of consumers is orchestrated through their own co-operatives, and so is more like a partly owned subsidiary. The UK Co-operative Bank has always been a subsidiary, and as such is part of a large class of businesses that are wholly or part-owned by co-operatives.

Agricutural co-operatives that have an investor-ownership stake

In the last 20 years, agricultural co-operatives have faced enormous pressures to grow into large agri-food businesses, so as to compete with transnational corporations that threaten to reduce them to the –increasing unprofitable – role of a marketing co-operative. In order to move along the supply chain they have needed masses of capital, sometimes far more than they could raise from their members. Some of them, notably dairy co-operatives in Ireland and Switzerland, have put their ownership stake into a holding company and then floated the co-business on the stock market. However, most co-operatives have resisted this option and have found other ways of raising capital that do not compromise farmer ownership. Here are three examples of co-operatives that have gone down this road.

Kerry Creameries

The Kerry Group dates back to 1972 when it was set up as a private company with three shareholders; the State owned Dairy Disposal Company, a Federation of eight small farmer co-operatives in Kerry and the Erie Casein Company from the US. They all invested to finance a dairy processing facility for the manufacture of milk protein (casein) for export to the U.S.A. Ownership of the company, then known as North Kerry Milk Products Ltd, was distributed with the Dairy Disposal Company and the Federation each owning 42.5 percent and Erie Casein, 15 percent.

The linkage to the American company provided a guaranteed market for the edible casein output, which was a relatively new dairy product for Ireland. In 1986, the Group was launched as a public company quoted on the Dublin and London stock exchanges, with a market capitalisation in excess of €7 billion and some 30,000 shareholders. The farmer co-operative's share has declined, but it still has a 23.7 percent shareholding in Kerry Group. It has direct access to governance of the Group board, through a Kerry Co-operative Creameries Advisory Committee that consists of 260 farmer representatives selected on a regional basis from ten electoral areas.

Farmers elect directors to the Board of Kerry Co-operative Creameries (KCC), and then seven members of the Creameries Board go forward to the Kerry Group Board. The farmers are joined by five executive and four professional directors.

This model looks interesting, but it is complicated by the fact that the farmer interest is itself fragmented. There are three classes of shareholders in the farmer co-operative KCC: 'wet' shareholders, that is farmers supplying milk, who have with full voting rights; 'dry' shareholders, that is farmers who have previously supplied milk, also with full voting rights, and 'dry' shareholders who have inherited or bought the shares, with no voting rights. Wet shareholders hold less than half of the shares on issue.

Shares have a nominal value of €1.25 each but trade for approximately €55-€60, and traders must be approved by the KCC board. Producers of milk have the option to purchase one co-operative share per thousand litres supplied at the nominal value of €1.25 annually, based on the volume of milk they have supplied that year. This right will expire in the near future.

“Even if the member interest in an MIOC owns a majority of the shares, over time this can be eroded.”

Each co-operative share is backed by approximately seven plc shares, making the market value of the share if transferred into plc shares worth €183 at 15th January 2011.

It is interesting to note that at the original listing in 1986 there was a floor set of 50 percent, on the principle that the farmers should retain control of the Group. Yet the co-operative share has slipped to just over a quarter and the farmers have lost control. They could take back control over the Irish part of the business, which is of course the part that most concerns them. In 1996 KCC was granted the option to purchase back the Agribusiness portion of Kerry Plc. However, talks on this have not yet come to anything; the Irish dairy business is the least profitable part of the Group, and farmers are cautious about committing everything to it. They may prefer to receive dividends as shareholders in the larger international business of which the farmer co-operative is now a part. Also, since active dairy farmers are in the minority even among the farmer shareholders, the view of retired farmers is more powerful.

This example shows that, even if the member interest in an MIOC owns a majority of the shares, over time this can be eroded and, in the insatiable need for capital to expand, the company can become majority investor-owned. It also shows that the member interest itself can become fragmented. This is not such an issue in other types of co-operative; there are no ‘retired’ members as there are in a farmer co-operative.

However, there are members who act more like investors, as well as members who represent the interests of consumers. There might also be might be investors who, in having ethical motivations, act more like members, and one can imagine ethical investors finding MIOCs an attractive place to put their capital.

Glanbia

The Glanbia Group was formed in 1997 through the merger of two farmer owned co-operatives, Avonmore and Waterford that had already, in 1988, listed separately on the Dublin and London stock exchanges. The Glanbia Co-operative Society is a holding company for farmers that initially took a 54.6 percent shareholding in the Group. In 2010, there were discussions about the co-operative buying back the Irish dairy and agrifood business. For the Society and its members such a transaction offered the prospect of returning to full ownership and control of the key strategic businesses that were closely aligned with their interests. For Glanbia, it would have enabled the Group to refocus on international nutritional ingredients and cheese, significantly improving its financial flexibility and enabling it to grow. However, the vote to take back control only achieved 73 percent support when it needed 75 percent.

In fact, the co-operative holding company has become less important over time. In December 2012 a motion was approved to reduce the co-operative share holding from 51.4 percent to 41.4 percent, in order to raise equity capital. It was a tempting offer for the farmers, who were promised a distribution of €157m of plc shares. Now, the farmers' holding company owns 48.3 percent of Glanbia plc and the farmers' share is going down. This shows that, given the need for more capital in a company that already has an investor-ownership structure, it is likely that the co-operative share of ownership will decline over time. This may be a major disadvantage of MIOCs.

Emmi

Emmi is the largest Swiss milk processor and the world leader in production of Swiss cheese. It was formed by the farmer co-operative Central Swiss Milk Producers in 1993, when it was decided to form a group structure, and separate out the commercial from the associational side of their co-operative.

In 2004 it went one stage further and floated on the stock exchange. Central Switzerland Milk Producers is still the largest shareholder, with 52.1 percent of the shares. This is followed by a group of fund managers who have 9.5 percent, and then by two more co-operatives who have 4.7 percent and 3.6 percent and a welfare foundation that has 1.7 percent. That leaves just over 28 percent owned by other shareholders.[19] It is still essentially farmer-owned and controlled, though there is no mention of this on its website. Unlike the other big Swiss dairy co-operative, Fenaco, that boasts on its website of serving its 'societaires', Emmi is a shareholder-owned company that nowhere mentions that it is owned mainly by farmers. This is interesting, as it shows how, even with a majority shareholding by co-operatives, a listed company can suffer a cultural change such that it no longer has a co-operative identity, at least not one that it admits to.

What evidence is there from these three examples of the effects of a move to the MIOC model? In Ireland, Kerry and Glanbia are successful but other hybrids have failed and then been acquired by their competitors, and one, Dairygold has returned to fully co-operative ownership.[20] It has been argued that the great success of Kerry is down to its exceptionally good leadership rather than its ownership structure, and that from the dairy farmers' point of view it has not worked out well; it is the farmer-controlled co-operatives that maintain the milk price, while Kerry and Glanbia farmer are in the lowest third in the milk price league table. Tensions have been created by the mixed ownership structure, and it has been found 'extremely difficult to serve both farmer and investor interests'.[21] Despite the profitability of Kerry, it is argued that the farmers are no better off than those in the co-operative DairyGold. In Glanbia, the attempt to take back the core co-operative business also shows some dissatisfaction.

In farming, the attempt to maximise profit runs directly counter to the goal of maximising prices to the farmers. It is a 'zero-sum' game. Similarly, in banking the extraction of profit directly raises the cost to consumers (other things being equal). One of the achievements of co-operative banks in Europe has been to lower the profitability of the whole banking sector.[22]

Without co-operatives, consumers may pay more for the service they receive. Certainly, the UK Co-operative Bank and the building societies have been credited with forcing the big investor-owned banks to maintain free banking for current account holders. On the other hand, banking customers are a more fragmented interest group than are farmers, and the services banks offer matter less to them (though a mortgage on one's home, a private pension or a loan for one's business are serious commitments). With good leadership it should be possible to pursue a trade off between profit for investors and quality banking services for customers. It depends on what priorities are set for the managers by a board, and on the level of clarity in the board's view of what those priorities are.

An opposite point of view has also been put in relation to the Irish farmer co-operatives. In their governance, they have lacked a 'challenging stakeholder', an interest group that could demand clarity of aims and better performance. The introduction of outside shareholders in Kerry and Glanbia created a focus on profit margins that led to greater corporate discipline, constant innovation and ruthless cost reduction, leading to higher performance.[23] The same might happen in new MIOCs, with investor-owners being more demanding than co-operative members, and with a clearer focus on what they want from their managers and boards of directors.

Companies part-owned by co-operatives

Often, co-operatives have got together to provide services to meet needs they share and that they cannot provide for on their own. The most common type is the insurance co-operative. This works best when it has a guaranteed market and a loyal customer base, both of which conditions are fulfilled in the non-life insurance sector. Examples of such jointly owned insurance co-operatives are the Cooperators, owned by several Canadian co-operatives, and CUNA Mutual, owned by the worldwide credit union movement. There are several examples of insurance co-operatives that have a minority investor-ownership, and the trade body, International Co-operative and Mutual Insurance Federation, allows them as members providing the co-operative shareholding is in the majority. Here is one good example: Unipol.

Unipol

The Unipol Group is the second-largest insurance group operating in Italy and the largest operating in the non-life sector. As at the end of 2012, consolidated direct insurance premiums amounted to €16.8bn. The Unipol Group also operates in the banking services sector, with a banking group which includes Unipol Banca for the retail sector, and Unipol Merchant for the corporate sector. Following its recent reorganisation, all the companies belonging to the Group are now held by the financial services holding company, Unipol Gruppo Finanziario S.p.A.

The history of the Group began with Unipol Assicurazioni, founded in 1961 and subsequently acquired by several co-operatives belonging to the Lega delle Co-operative (League of Co-operatives). A Public Limited Liability Company with the Unipol brand name was purchased by a number of co-operatives belonging to the Bologna League of Co-operatives in order to bring all of their insurance portfolios under a single company.

In 1972 three trade unions also became shareholders. In 1986 it was the first Italian company belonging to the co-operative movement to be listed on the Stock Exchange, at first just with preferred shares, but then with ordinary shares. From then on, its history became one of a restless pursuit of growth and diversification. It purchased several other companies (including a bank), and aggressively attempted to takeover companies in which it had an interest. However, the penalty for this was a tendency towards fragmentation, and the company underwent something of an identity crisis when it failed in an attempted takeover. In 2011, a major rebranding project led to the reunification of the business under the 'Unipol' brand.

Now, the majority shareholder in the Group is Finsoe S.p.A., which currently holds 50.75 percent of the ordinary share capital. It in turn is 64.6 percent owned by 28 co-operatives, including the main Italian consumer, manufacturing and workers' co-operatives.

In the relentless search for growth and diversification, Unipol has moved a long way from being a 'pure' co-operative, but co-operatives still have a significant share of around a third. It may not matter that co-operatives are in the minority here, because the history of the Group is one of constant change, aggressive expansion and diversification. The co-operatives will be content to take a share in governance and to benefit from dividends in what is, after all, a major business success story. Perhaps this is the way the UK Co-operative Bank will go. If it becomes an MIOC, and then grows and diversifies to become a major high street bank with the Co-operative Group still representing consumers (albeit at a reduced level of influence), it may be a price worth paying.

Co-operatives that used to have an investor-ownership stake but have bought this back

Ownership is not fixed. It can change radically, when co-operatives and mutuals demutualise or companies mutualise. Sometimes the same company can move from one to the other and back again: a good example is Standard Life Insurance that began as an investor-owned business, mutualised and then recently demutualised again. Some co-operative boards have invited in a minority investor-ownership stake and then decided that it was a mistake. Here are two good examples: the French co-operative bank, BPCE, and the American insurance provider, Nationwide Mutual.

BPCE

BPCE is an amalgamation of two mutual banking groups: the Banques Populaires and the Caisses d'Epargne, which merged in 2009 to form France's second-largest banking group with a market share of 22 percent of deposits and 23 percent of real estate loans.[24] BP consists of 18 regional co-operative banks plus two specialist banks for the education and non-profit sectors. Together they have 7.8 million customers and 3.3 million members. CE consists of consists of 17 regional savings banks that were converted to mutual status in 1999.

When the two banks are fully merged, it is likely that BPCE will also enter the list of the top 50 largest banks in the world. Together they own an investment bank, Natixis. BPCE raised capital by issuing non-voting co-operative investment certificates to this subsidiary investment bank. Now, in order to simplify its structure, there is a plan to buy back the certificates at a total cost of €12.1bn. Once it is done, the co-operative shareholder customers will own 100 percent of their banks capital.

This example shows that it is possible for a co-operative bank to decide to buy out other interests and return to a fully mutual type of ownership. However, in this case the influence of Natixis was indirect, since the two co-operative banks wholly owned it in the first place. They simply preferred not to have their business strategies too dominated by the interest of investment banking, and to make sure that the consumer interest remained dominant.

Nationwide Mutual Insurance Company

Nationwide, based in Columbus, Ohio, is one of the largest diversified insurance and financial services organisations in the world, ranking 108th on the Fortune 500 list. The company provides a full range of insurance and financial services, including auto, motorcycle, boat, homeowners, life, commercial insurance, administrative services, annuities, mortgages, mutual funds, pensions, long-term savings plans and health and productivity services. It was always a mutual but in 1997 it floated off part of the Group, Nationwide Financial Services, on the New York Stock Exchange. Then in 2009 it made an offer to buy out the independent shareholders of NFS and remutualise it. The completion of the transaction set Nationwide apart from the competition in a deliberate marketing strategy that, its website claims, enables the Group to align its entire product and service portfolio around the customer.[25]

Nationwide Mutual shows that there is always the possibility of returning to a more pure form of co-operative business. Nationwide's board decided that the conflicts of interest between consumers and investors was not worth having, and that in the long run it was better to stick to the mutual model. Perhaps it had to go through a period in which outside investors were needed to enable it to grow and diversify so dramatically. What it has managed to achieve is a return to the pure co-operative model, fuelled of course by its ability to find enough capital to buy out the investor owner interest.

The message that Nationwide Mutual gives is clear and compelling. On its website it explains the reasoning behind its mutual status:

> Nationwide Insurance is made of members and for members. And we put our members first, because we don't have shareholders. That's how we started, how we operate today and what drives our On Your Side® service.[26]

The resulting advantage for customer-members is clearly set out in this kind of statement:

> "We can't predict when bad things will happen, but we can help protect you when they do. Last year, we paid $10.9 billion in total claims. And we paid $0 to shareholders – because we don't have any."

It emphasizes the advantages of becoming a member not just to the individual but to the collectivity of insurance customers:

> "Every member makes us stronger. And when you become a Nationwide Insurance member, you're not just a customer. You're part of a group that's millions strong."

Insurance and banking are similar, in that there is no real need for a separate group of investors provided the business can be self-financing in the long run. Just as banks recycle money, insurance mutuals recycle – or rather spread – risks, so that the idea of member-ownership becomes not just a statement of value but a real business advantage.

The internal governance of MIOCs

How should the new owners of an MIOC be brought into governance? It depends on the extent to which their ownership stake is concentrated or widely dispersed. If it is concentrated in one or more institutional investors then the voice of shareholders will be strong, whereas if it is dispersed among small investors it will be weaker.

It also depends on the mix of motives among shareholders; some may want to support the co-operative's ethical policy, but they will be unified by their desire for dividends and a higher share price. The board will have to respond to their interest, and its composition will change to reflect this. There will be a greater focus on profitability and return on equity, and the share price will provide a clear signal about performance.

All the guidelines on corporate governance agree that the board itself should be protected from factional interests – it should be able to present a united decision-making body that lives up to the highest standards as set out in codes of corporate governance. In order to do this, the MIOC's managers need to orchestrate the various interests, enabling them to express their views to the Board as part of a member/investor relations process. If this proves to be too costly then the business will suffer. If the consumer interest is stifled, it may lead to poorer business performance. The investor interest may at times lead to a more business-like and aggressively growth-oriented strategy, which could be good for a business sector as a whole. For instance, it is generally agreed that in the UK there is a need for a bank that can compete with the big investor-owned banks in the high street, driving down profits in the interests of consumers.

There is a need, also, for a more effective co-operative presence in lending to SMEs and in strengthening local economies. If the Co-operative Bank becomes bigger as a result of becoming an MIOC, it can develop a more regional presence and a large network of branches, both of which are key to the success of European co-operative banks in sustaining local economies.

Can the introduction of outside investors be seen as an opportunity for growth and diversification, while the co-operative maintains its commitment to the user-members? It depends on the effectiveness of the board, and the quality of management, but it also depends to some extent on the interaction between the two sets of interests. Under the continental system of a two-tier board, a larger supervisory board would appoint the non-executive directors to the board of management. This has the advantage that factional interests can be expressed, and conflicts played out, at a higher level, leaving the management board free from these pressures.

On the other hand, this method slows down decision-making and could, if handled badly, inflame rather than damp down factional interests. One way to gain the advantage of this model of governance would be for the MIOC to treat customer members as another type of investor – a 'mutual shareholder' as Credit Agricole calls it. The normal process of investor relations would then apply, and the interest groups could be kept informed and consulted. The board could meet with them periodically to hear their views and be called to account. This method falls short of the more directly democratic methods used in pure co-operatives to involve members (recalling, of course, that member voting rights in primary co-operatives is typically on a one-member, one-vote basis, in contrast to the constituency of external investors, which will operate on the weighting of financial investment), but it may be the most that the MIOC and its members/ investors can do to ensure that the broad range of interests are taken into account.

Options for the future ownership and governance of MIOCs

The case studies show that there are several routes that an MIOCs could go down in the future. Like BPCE or Nationwide Mutual, it could return to being a pure co-operative by buying back shares from investors when it returns to solvency, and raising capital by other means than issuing voting shares.

The giant Dutch co-operative bank, Rabobank, uses two new methods of capital raising. The first is capital securities; similar to bonds, but with no fixed term, and with interest only payable if the Bank makes a profit. The second is member certificates, which enable members to invest their capital and receive a return (again provided the Bank is in profit). Neither of these instruments infringes co-operative principles, because they do not carry voting rights. However, their growth has meant that over a third of the members have an interest in the bank's financial performance as well as in its service to customers.

An MIOC could go the other way, with the co-operative interest reducing its ownership stake over time and allowing the business to become majority investor-owned. In this case, the co-operative holding company becomes merely one institutional investor among others, and the MIOC would evolve into a joint venture, partly owned by a co-operative.

As in Unipol, governance would be relatively straightforward, with the various institutional and individual shareholders having voting rights according to their equity stake, monitoring the performance of managers, watching the share price and so on. If a majority of investors have social purposes, then their influence will be felt in the company's policies and strategies, but there is no reason to predict high governance costs because of disagreements. Unipol has had its problems; recently it failed in a takeover bid and the management had to be changed, but this is part of 'normal business'.

A third option is the middle way taken by Credit Agricole, which has both mutual and individual investors, and a mix of ownership by regional co-operative banks, institutional investors, individual investors and employee mutual funds. The system works because it is well orchestrated. The mutual voice is formed in the local banks, and expressed upwards through the regionals. The voice of individual investors is less formally expressed, through the members' club. To go down this route, an MIOC would have to strengthen the voice of customers by encouraging a higher proportion of them to become members. Again, Rabobank is instructive. In 2010, a drive to recruit members led to a fourfold increase from six percent of customers to nearly 24 percent.

However, the UK Co-operative Bank would be hampered by the fact that it does not have members of its own, but has to persuade people to join its owner, the Co-operative Group, in order to have indirect influence over the governance of the Bank. A separate membership category for the Bank would help, and this could be modelled on good practice in European co-operative banks.[27] Members would get the right to elect members of a member council that would then appoint non-executive members of the Bank board. This method of governance works very well, and there are no problems with getting people to become members and take an interest. There is tremendous goodwill towards the Co-operative Bank which, and a high level of trust. If these are not dissipated during the current resolution process, in this way member involvement could be strengthened. It is more difficult to see how the investor interest could usefully be orchestrated, but Credit Agricole's active embracing of the investor as a 'club member' is instructive.

A code of governance for MIOCs?

What would a code of governance look like for an MIOC? How far would existing codes have to be adapted to fit? These are important questions, because the consequences of getting it wrong are serious. On the one hand, the governance of MIOCs is likely to be challenging and potentially costly. On the other hand, it may also be invigorating, with unexpected synergies between member and investor interests. Most likely there will be tensions between the two sets of interests, and trade-offs will have to be made.

However, in most respects, the governance of MIOCs should not be all that different from the governance of any other large corporate entity. The code provided by Co-operatives UK for the consumer co-operative sector[28] was initially based on the Combined Code published in 2003[29] by the Financial Reporting Council for conventional businesses. There will be considerable overlap because good governance is in many respects fundamentally about the same underlying principles of the board's accountability to owners, its role in directing but not managing, its duty of due diligence, in risk management and so on.

The tables below explore some of the relevant governance issues, in an attempt to identify the implications for the governance of MIOCs. In the tables, the UK Corporate Governance Code column includes the UK Stewardship Code[30] and also, where it goes further than these, the Walker Report on governance of financial institutions.[31]

In terms of the responsibilities of a board of directors, both types of board have a fiduciary duty to act in the best interests of the company or society. The main difference is that a co-operative board has to act in accordance with the co-operative identity statement, principles and values as set out by the International Co-operative Alliance, whereas the board of an investor-owned business just has to provide entrepreneurial and responsible leadership. In an MIOC some blend of these will be needed. The co-operative board has to be accountable to its members, whereas the investor-owned board simply has to interact with shareholders and explain any deviations from the Code. It will be difficult for an MIOC to combine these principles, as the co-operative code is much more imperative. The co-operative boards also have a broader set of performance indicators to consider that take into account more than commercial indicators, though some investor-owned business boards already consider their performance in relation to stakeholders and the environment. Both types have to take into account the views of different stakeholders, though the imperative to consider institutional stakeholders' views in investor-owned business boards is not as strong as that to recognise the rights of stakeholders in the co-operative board code.

In some respects, the governance code for investor-owned businesses is stronger than that for co-operatives. This reflects the fact that the co-operative code is older. Co-operatives UK is currently revising the code for consumer co-operatives and developing one for agricultural co-operatives, so we can expect that this to change.

Table 1 summarises the responsibilities of co-operative boards to members and of investor-owned business boards to shareholders. There are strong similarities; both types have strong guidance on how to avoid boards becoming partisan, representing particular interests. As might be expected, there is a stronger emphasis in co-operative boards on active participation.

Members are encouraged to play a part in governance, shareholders merely to monitor governance by the board. The co-operative board is expected to identify active members and maintain close relations, whereas the investor-owned business board is merely to ensure dialogue with major shareholders. MIOCs will have to encourage investors to play a larger part than they are used to, if there is to be parity between the two interests. There is no way that an investor-owned business board can match the lower levels of governance found in co-operatives, though the investors' club that Credit Agricole organises is an interesting initiative that could be used to connect investors to the governance structure. The code for investor-owned business boards has a surprising emphasis on the duties of institutional investors to oversee their companies, to intervene when there are conflicts of interest, and to act collectively as 'stewards' of the company. There is no equivalent duty on co-operative members, and perhaps in the MIOC this could be spelled out.

Table 1: Responsibilities to members and shareholders

Consumer Co-operative Code	UK Corporate Governance Code	Implications for MIOCs
Board should encourage members to play a part in governance, members should hold the board to account	Boards should encourage shareholders to monitor the Code. Investors should hold the company to account	They can encourage investors (asset owners and managers) as well as members to play a part
Maintain an accurate and up to date membership register	This is done through share register	There will be two registers
Identify active members and maintain close relations	Board responsible for ensuring dialogue with shareholders. Senior NED to resolve disputes.	Close relations needed with institutional shareholders. Consideration of a senior non-executive director as a 'lightning rod' for shareholder concerns. Expect and have a policy for dealing with conflicts of interest

Consumer Co-operative Code	UK Corporate Governance Code	Implications for MIOCs
Encourage expansion of membership, involvement at level below the board (e.g. area committees).	No equivalent, unless there is a shareholder club. Keep in touch with opinion, hold meetings with major share-holders.	Some way of equalising the attention given to investors and member-owners
Ensure members are aware of their right to stand for election, ensure preparatory training is available, and elections are contested.	Nomination committee to lead on appointments, ensure orderly succession	A search committee should prepare both member and investor candidates for board membership
Monitor best practice in member participation, encourage maximum participation in elections	Encourage shareholders to monitor compliance with the Code	Develop a best practice approach to shareholder relations
Allow an advisory vote by members on remuneration packages	Chairman to ensure contact with principal shareholders on remuneration	Some blend of these two sets of principles is needed
Make sure members are in the majority on the board: professional external directors in a minority, employees limited to 33%, related people to 49%.	Except on small companies, at least half the board should be independent NEDs. An appropriate combination of exec and non-exec members so no individual or group can dominate.	Some similar rules need to be devised to keep a balance between interests, - and ensure the independence of a majority of directors from factional interests.
Members have right to vote on disposals involving 25% or more of assets	Not mentioned	Keep the co-operative principle here

Consumer Co-operative Code	UK Corporate Governance Code	Implications for MIOCs
Institutional investors are outside the scope of the code	Institutional investors are expected to manage conflicts of interest in relation to stewardship, be willing to act collectively, monitor investee companies, have a clear policy on voting etc.	This emphasis on the responsibility of member and investor owners for stewardship would be very useful

Table 2 summarises the internal workings of the board. It is not surprising that here there is a great deal of similarity between the codes for co-operative boards and for investor-owned business boards, and the implications for the governance of MIOCs are tentative:

- Perhaps the introduction of directors elected by the investor-owners would increase the skill level,
- Perhaps managers would have less understanding of the co-operative business model, or
- Perhaps there will be more co-opted professional non-executive directors.

One big point of contention would be the offer of share options to top managers, or wider staff, as part of their remuneration package. In a co-operative board this would not be possible. In an investor-owned business board, it would be expected. In an MIOC, it could be divisive. Fortunately, there are other ways of incentivising managers than giving them ownership rights.

Table 2: The internal workings of the board

Consumer Co-operative Code	UK Corporate Governance Code	Implications for MIOCs
There should be a formal schedule of matters reserved to the board	Same	Same
It needs to have the requisite skills to hold the management executive to account	The same, with Walker asking for more stringent commitment of time etc.	The introduction of directors from the investor interest may increase the skill level
It needs to ensure the integrity of financial information and have a system of risk management	The same	As above, plus greater scrutiny of the integrity of information?
It needs to appoint managers who have an affinity with the co-operative business model	Not applicable	Managers will have to have a broader understanding, but perhaps they have this already
It needs to be accountable to lower level committees, and provide them with sufficient information	Not applicable	This duty will remain, but will it become more difficult to carry out?
Election at intervals of no more than 3 years, with age rule or mandatory break in service	Same	Same
There should be a search committee for succession planning	Same	Same, but with a broader remit?
Power to co-opt professional external directors	Same	Same, but greater use of this power?

Consumer Co-operative Code	UK Corporate Governance Code	Implications for MIOCs
Ensure management training to include co-operative values and principles	Not applicable	This can be done
It should ensure training for board members, regular appraisal of performance etc.	Same	Same
The remuneration committee should approve management performance related pay	Same, should be formal and transparent, but with expectation of share options	Performance related pay is fine, but share options likely to be contentious
As above, on remuneration of directors	Avoid paying more than is necessary!	Same

Conclusion

This report began with the assertion that in defining co-operatives the question of ownership comes first. All the other characteristics of a co-operative follow on from this. However, when one looks at businesses from the outside, this is less obvious.

Institutional theorists talk of 'isomorphism'; businesses that are in the same sector look very much like each other whatever their type of ownership. Banks look like other banks, whether they are co-operatives, savings banks or investor-owned. Food retailers look just like other food retailers, whether they are family businesses, supermarket chains or consumer co-operatives. Dairies look like dairies whether or not the farmers own them. Isomorphism comes from market competition, from the need to conform to government regulation, from the need to hire professional managers who are all trained in the same way, and from the basic human desire to emulate others who are more successful. So we should not over-emphasise the differences between organisations on the basis of their ownership.

On the other hand, ownership sets limits on what a business can do, and owners have a great deal of power to stop their boards and managers from acting in ways that go against their interests. If the interests of owners and their boards and executives are not aligned, then the business will suffer. If a mixed ownership structure is chosen, with different interests pulling in different directions, then the costs of such ownership will eventually lead to either bankruptcy or conversion to a simpler, more stable ownership type.

The conversion of co-operatives into hybrids that have a minority of investor owners has uncertain outcomes, and there are few precedents to follow. The case studies presented here suggest that it is perfectly possible for co-operative banks, insurance societies and agricultural co-operatives to become MIOBs, but that some of those that do find it too difficult and move back to the pure co-operative model. Others find that the co-operative share is diluted over time so that the co-operative becomes just one institutional investor among others. When the model works, it does seem to lead to a dilution of the meaning of ownership among co-operative members.

"These issues cannot be left to chance and have to recognised and planned for."

Despite these different business trajectories, a close comparison of the governance codes of co-operative boards and investor-owned business Boards shows that there is considerable overlap. In many ways, the governance of an MIOB will be 'governance as usual'.

However, puling in one direction is the idea of membership, with boards being responsible for encouraging member participation in lower level democratic structures, and encouraging active members to stand for election. Pulling in the other direction is the idea of governance on behalf of shareholders, with boards being responsible merely for having a dialogue with major investors and, providing they are successful, being more distanced from their owners.

Yet it is possible that, if handled well, the combination of pressures from consumer members and from investors could lead to better business performance and greater accountability. The adoption of a governance code based on the different strengths of the co-operative and corporate codes could also benefit the business. One lesson that comes from the experience of existing MIOBs is that these issues cannot be left to chance and have to recognised and planned for.

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