



**Trends and challenges for co-operatives  
and social enterprises in developed  
and transition countries**

edited by  
**Carlo Borzaga and Roger Spear**



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**TRENDS AND CHALLENGES FOR CO-OPERATIVES  
AND SOCIAL ENTERPRISES IN DEVELOPED  
AND TRANSITION COUNTRIES**



## 1. Introduction

by Carlo Borzaga\* and Roger Spear\*\*

Recent years have witnessed a new interest in co-operative organisations, especially as a consequence of their transformation and expansion in new fields of activity. These two phenomena are connected, since transformation appears to be the prerequisite for expanding activities in new areas and as such, are worthy of specific analysis. In particular, the capacity of co-operatives to assume a number of forms consistent with the socio-economic environment in which they are situated deserves special attention, as well as co-operative identity and the organisational and legal frameworks so far developed as a result of co-operative evolution.

The description of this evolution in a number of important countries and analysis of this process, is the aim of this volume<sup>1</sup>; more specifically, co-operatives' recent developments towards what are currently defined *social enterprises* within the co-operative framework<sup>2</sup> will be examined.

The volume takes on a wide perspective, looking at both Western and Eastern countries. On the one hand the new role of co-operatives in advanced economies is explored. As a result of the gradual withdrawal of public entities, owing to state budget constraints, co-operatives are increasingly turning into new welfare services providers in a number of countries. This has led to a number of changes at an organisational and legal level. On the other hand, co-operative development in transition

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<sup>1</sup> The volume includes the most innovative reports presented and discussed by the contributors of the International Seminar *From Co-operative to Social Enterprise*, held in Trento in December 2003. The International Seminar *From Co-operative to Social Enterprise* was jointly organised by Issan (Institute for the Development of Nonprofit Organisations - [www.issan.info](http://www.issan.info)) and the Emes Network (The Emergence of Social Enterprise - [www.emes.net](http://www.emes.net)). We want to thank the authors of this volume, sponsors and organisers for their outstanding support. In particular, we want to thank the Fondazione Cariplo and the Region Trentino Alto-Adige.

<sup>2</sup> Concerning advanced economies, the concept of "social enterprise" is used when referring to entrepreneurial entities (co-operatives, associations, etc.) explicitly pursuing a social goal. See also the Emes definition: Carlo Borzaga and Jacques Defourny, *The Emergence of Social Enterprise*, Routledge 2001. Emphasis is put on the evolution process, of which social enterprises represent the end result. With regard to transition countries, the concept of "social economy" seems to be more suited to designating the array of alternative organizational forms (among which co-operatives are here especially explored), which have so far developed.

countries is also investigated. In former socialist and communist countries, co-operatives keep showing unexpressed potentials, but they are largely underestimated as compared to other organisational models (both capitalistic companies - normally preferred in the transformation of state enterprises - and other social economy organisations, included not-for-profit organisations like foundations).

In order to tackle these issues, the volume is divided into three parts:

- *New trends in co-operative development* - devoted to both explaining co-operative evolution and increasing the readers' awareness of co-operative potentials;
- *Co-operative organizations' development paths in advanced economies* - above all addressed to investigating new co-operative forms and, more generally, social enterprises;
- *Forthcoming economic and social role of social economy organisations in transition economies* - concerning interesting evolutionary dynamics in Eastern countries.

Particular attention is drawn by the first contribution by Giulia Galera, on the specificities of the co-operative model, traced back to the ownership assets, the pursuit of goals other than profit and the governance forms. Co-operatives are described as organisational forms capable of adjusting to the changing economic, social, cultural and political conditions, owing to their ability to reduce specific transaction costs caused by market failures in several sectors. The differences concerning the development of the co-operative phenomenon at the national level, are grouped into four "co-operative models":

- the mutualistic model: characterizes co-operatives claiming a strict promotion of the members' interests;
- the sociological model: characterises co-operatives more open to the community interest;
- the in-between-model: refers to those systems where the mutuality concept, as asserted in the different legislation regulating co-operatives, has been open to different and often opposing interpretations, defending co-operative mutual nature or claiming co-operative social function;
- the quasi-public model: co-operative organisations are perceived as public enterprises and their governing rules are dictated by public authorities.

Concerning the evolution observed in the models investigated in the recent decades, the main changes that have occurred are that:

1. the social orientation has overwhelmed the mutuality orientation in a number of countries;
2. a general evolution towards the production of general-interest-services has become evident;
3. co-operative attributes towards the provision of general-interest-services have been increasingly incorporated into the new co-operative forms.

More specifically, it is the widening of the traditionally homogeneous social structure (single-stakeholder model), that is responsible for both the gradual fading of the mutualistic purpose and the enhancing of the self-help dimension embracing the community as a whole (multi-stakeholder model). Considering more generally the evolution of organisations pursuing goals other than profit (the so called “third sector”) as a whole, particular emphasis is put on the convergence of the organisational forms, specifically the associative and co-operative. While the associative form has become more productive, the co-operative form has gradually reduced its traditional goal of mutuality.

Alongside an economic investigation of the phenomenon, an interesting reflection on co-operative identity, with the values embedded and the social commitment therein is provided by Ian MacPherson. The continuity between co-operative values and the recent evolution towards the consideration of general-interest goods is shown. The author recalls the values that co-operatives are based upon: equality, equity, solidarity, self-help, self-responsibility, democracy. Moreover, he expounds upon the values that co-operative members believe in, based on the tradition of their founders: ethical values of honesty, openness, social responsibility and caring for others. The author goes then through the most relevant and interesting issues, background debates and contributions of major authors (Alexander Laidlaw, Michael Trunov, Sven Akë Bööck), that preceded the development of the ICA Identity Statement - adopted at the ICA Manchester Congress in 1995. Special attention is given to the attempts made to reconsider the relationship between the community and the co-operative movement, while facing the pressures responsible for weakening over the years co-operative communitarian perspective. The following pressures are identified: the disintegration of the centrally

planned economies of Central and Eastern Europe; the unclear roles of co-ops in many southern countries; the overpowering dominance of market ideologies and classical liberal thought; and increased global integration. Notwithstanding these pressures, the ICA Manchester Congress recaptured the social dimension of co-operatives in several ways, including the emphasis on social responsibility and member involvement, as well as an emphasis on the principles of *common capital* and sustainable communities. In MacPherson's view, co-operative communitarian tradition is now facing challenges that are intrinsic to its history and formation and that have again become topics of discussion in Central, Eastern and South Eastern Europe.

The third contributor by Hans Münkner focuses on the emergence of a new co-operative form - the multi-stakeholder organisation (MSO) – which results from the drawing together of the associative and co-operative forms. The author describes the phenomenon from a comparative legal perspective. Special regard is given to both the specific features covered by multi-stakeholder co-operatives (MSCs) and the socio-economic reasons for their development, the main ones being rapid economic, social and technological changes. Münkner also provides evidence of how the disadvantage of increased costs caused by interest harmonisation and decision making is balanced by a number of advantages of this specific organisational typology, namely better quality of services (services correspond to the users' needs) and reduced transaction costs (due to trust relations, resulting from knowledge of local conditions and stakeholders' involvement). In addition, Münkner explores MSCs as a legal form, making reference to the recent legal developments in a number of countries (Italy, Canada, Portugal, France). At the same time, he provides the arguments against special legal provisions for MSC, drawing on evidence from the legal frameworks in the United Kingdom, Belgium and Denmark.

The first part of the volume is completed by the contribution of Enzo Pezzini, who explains the importance of the Statute for the European Co-operative Society (SCE), providing co-operatives with adequate legal instruments to facilitate their cross-border and trans-national activities. He gives a general overview of the political debates that preceded the recent adoption of the SCE. This Statute is the result of ten years of effort and lobbying, involving the main European co-operative move-

ments. Its importance results from the recognition of the co-operative form by European company law. However, the SCE is defined as a mutualistic organisation and no reference is made within the Statute to the recent evolution of the co-operative form into the emerging sociological model.

Contributors to the second part put particular emphasis on the motivations behind the organizational and legal evolutions that have occurred (or are still developing). The first contribution by Roger Spear reviews some recent European experiences of legislative changes in the co-operative and social economy as well as changing usage of legal structures within the sector. It argues that there has been a strong isomorphic tendency towards conventional business structures until recent years. He then goes on to argue that in Europe we have recently seen some departures from the previous isomorphic tendencies. Firstly towards multi-stakeholder structures (though some may question whether this is truly new), and secondly towards structures that incorporate more elements of voluntary sector/non-profit organisational models. The paper continues by looking at recent UK legislation (which is scheduled to be enacted in 2005) for a Community Interest Company (CIC), which will be a new type of company, designed for enterprises who want to use their profits and assets in the public interest (social enterprises). Thus the paper considers the extent to which there is a departure from an isomorphic path towards a new regenerative trend in the co-operative form, and a development towards a new form, more properly defined social enterprise.

Presenting the Italian case, Paola Iamiceli goes through the current models of social enterprise provided by the Italian law (social co-operatives, social promotion associations, cultural foundations, etc.) in order to explain the reasons behind the adoption of comprehensive regulations concerning the social enterprise. Notwithstanding the availability of a rich number of social enterprise models - of which particularly interesting is the social co-operative model - a number of critical aspects explain, in her view, the introduction of a new legislation. Iamiceli focuses on the stakeholders' level of participation in the governance structure, on the regulations on accountability, transparency and information requirements, on the liability rules and, finally, on bankruptcy and liquidation procedures. In many cases, these delicate aspects are not properly dealt with. In other cases, regulations make reference toward company mod-

els, some of which are not always adequate. The legislative proposal on the social enterprise, currently under discussion, attempts to tackle the above-mentioned problems. The main contents of the proposal are explored by the author.

Similarly, Alix Margado examines the reasons behind the adaptation of the existing co-operative charter, in order that it provide for a new co-operative form in France (the Société Coopérative d'Intérêt Collectif - SCIC). The development of this new co-operative is described as the result of a pragmatic approach, involving associations and co-operatives. The SCIC approval procedure and the legal novelties introduced are described. Margado also makes reference to some specific aspects (social benefit, the multi-partnership envisaged, the links with the community territory in question, the limited liability), and he describes how power is distributed within the SCIC. Moreover, the author focuses on the relations between the pursuit of general-interest and public policies, and provides some examples of SCIC fields of operation.

Jean Pierre Girard focuses on the emergence of solidarity co-operatives in Canada. He singles out the following background conditions: the degeneration of small communities, community development, the development of childcare services, projects aiming to promote the reinsertion of poorly qualified individuals in the job markets, the development of home services for elderly people. Solidarity co-operatives are presented as a new option to reconcile the interests of both users and workers, while including the participation of support members. Besides providing data on solidarity co-operatives structure and growth of membership, the author also focuses on strengths and weaknesses. Despite public grants and aid offered to the start-up and for development, solidarity co-operatives keep showing a very low level of capitalization. In some sectors, dependency on public subsidies remains strong and a lack of federative or associative structures is noted except in the home service sector.

The final part of the book - *Forthcoming economic and social role of social economy organisations in transition economies* - is aimed at investigating the co-operative phenomenon in Eastern, Central and South Eastern European Countries, where an immediate challenge for co-operative organisations' expansion is raised by the disintegration of the centrally planned economies. To give a general overview of the developing role of social economy organizations in transition countries, a number of national analyses

are presented (Poland, Czech Republic, Bulgaria, Serbia). After an initial boom of co-operative development in a number of transition countries (mainly due to the way the privatisation process was carried out), a deep crisis followed. All contributions in this volume confirm the existence of a number of critical aspects which jeopardize the development of social economy and, more specifically, co-operative organizations. Moreover, positive co-operative experiences in a number of sectors - credit, housing, agriculture - are explored to provide evidence of co-operative specific capacity to replace poorly functioning markets (Lithuania, Hungary, Estonia). These experiences confirm that there is a solid basis for co-operative development.

More specifically, a brief historical analysis dating back to the roots of the co-operative movement, brings into focus the reasons behind its development, back in the XIX century. This exploration is carried out by Ewa Leś. She recalls the co-operative legal tradition which existed in the pre-World War I period and the “solidarity” trade union debates, which jointly contributed to the recent credit union re-emergence in Poland. Despite a general crisis affecting the Polish co-operative movement, credit unions and mutuals are paradoxically experiencing a renaissance phase. Similarly, Maria Kolin recalls the Yugoslavia tradition of co-operative civil service dating from the nineteenth century. She reports how old traditions have begun to re-emerge in several forms, as a result of Serbia having experienced a transition to democracy. These traditions include the development of social economy organisations. Concerning specifically the co-operative sector, Ewa Leś brings to light the reasons explaining its decline after the dramatic changes in 1989. She names the following: the transformations of existing co-operatives into other legal forms, the merging of several co-operatives into bigger entities, the negative public perception towards the co-operative movement in Poland, and the process of liquidation. In addition, deficiencies concerning the legal framework have also prevented co-operative regeneration.

Similarly, Magdalena Huncova considers the lack of a co-operative law in the Czech Republic the main obstacle to co-operative development. Czech co-operatives are currently regulated under Commercial law, which seems to obstruct the existence of authentic co-operatives. Both authors - Leś and Huncova -reiterate that co-operatives are often considered a residuum of the totalitarian regime in the public mind, therefore

their transformation into traditional companies or into associations is usually favoured.

An interesting comparison between co-operative organisations and NGOs is provided by Maria Jeliaskova, using Bulgaria as a case study. She focuses on both types of organisations as alternative models of co-operation, as far as social economy is concerned. Affinities and differences between the two models are discussed as well. Overall, differences (co-ops follow different development paths and the obstacles encountered differ too) normally prevent general consideration of the two models. Perceptions are all negative - such as common difficulties in mobilizing resources, low level of co-operation, low participation in establishing the normative framework, high competitive level and death rate, lack of long term strategies, high dependency upon donors (NGOs) and big business structures (co-operatives), high involvement in the informal economic sector and deregulated labour relations - and these models are still largely ignored. The more emphasis is put on the differences between the two models, the greater the difficulties in considering co-operative organisations as part of the social economy. There are other unfavourable conditions which have so far affected the development of social economy organisations. With respect to the Bulgarian case, Jeliaskova sites both the proliferation of transition myths and the specific ideology characterising the Bulgarian transition.

A successful co-operative experience is reported by Marit Otsing, who explores the case of housing co-operatives. The development of the co-operative movement in Estonia began in the 1990's, and they primarily concerned themselves with agriculture, housing and consumer welfare. Since its development, the co-operative sector has become an important cornerstone of the social economy. The Housing Reform programme began in 1992, when a class of private owners joined together to create an organised housing movement. Local unions formed due to the need to share information and knowledge. By 1996, five local unions created the first national union: the Estonian union of Co-operative Housing Associations. The goal of this union was to represent common interests at the local, national, and international level, promote the exchange of information and know-how, and create sustainable management and maintenance practices.

Similar areas of co-operative development can be singled out in other Baltic countries. Sigita Bubnys sites the three specific areas of development that have achieved much progress since their inception in Lithuania, which are: consumer co-operatives, agricultural co-operatives, and financial co-operatives, which have primarily taken the form of credit unions. The latter two are expounded upon in great detail. Agricultural co-operatives often take the form of agro-technical agreements, in which farmers form societies that share farming equipment in order to lower costs and ensure better usage of the equipment. The financial co-operatives are primarily credit unions that act as banks that exist to serve their members, offering better deposit and loan rates, employment opportunities, as well as other benefits. The author emphasizes the importance of social responsibility that is common practice in these credit unions. Credit unions have played a large role in offering opportunities to people who would otherwise not obtain credits under the normal banking system. The Credit Union system is still growing, it has a good level of success, and will undoubtedly contribute in the contributor's view to the recovery of Lithuania's economy.

Gabor Szabo's contribution targets the Hungarian rural co-operative sector, focusing on two case studies as examples of different routes of agricultural co-operation in Hungary. The main problems in the Hungarian agriculture regarding co-operatives are also discussed. In addition he brings to light some negative effects of the current co-operative law, which came into force in 1992.

## **Closing remarks**

From a general perspective, the chapters of the book provide evidence that the orientation of the international co-operative movement moves in the direction of revitalizing the communitarian tradition. At the national level, a number of differences characterising the single co-operative systems are highlighted, as well as the national experiences reported. Briefly, while a number of countries provide specific legal frameworks designed to incorporate the altruistic goals increasingly pursued (France, Italy for instance), other examples (United Kingdom, Belgium, Denmark) are shown that multi-stakeholder organisations can develop also without legislation specially designed for them. Different po-

litical, cultural and socio-economic circumstances at the national level explain the introduction of more flexible legal frameworks (United Kingdom with the CIC) or the adaptation of existing statutes to encourage the entrepreneurial dynamics that are part of a social project (France with the SCIC and Italy with social co-operatives).

However, situations in advanced and transition economies are extremely different.

In advanced economies, a number of features are covered by new co-operative organisations, such as a multi-stakeholder governance and the pursuit of an explicit social aim. The latter has recently been incorporated into the new co-operative forms (social co-operatives and SCIC for instance) and legal frameworks being approved (CIC in United Kingdom). Moreover, the entrance of a number of different stakeholders in the property structure has given strength to a new partnership logic, which is a precondition for success of the new membership model. The more or less strictness of the legal prescriptions concerning the multi-stakeholder character - the SCIC law, unlike the Italian law on social co-operatives prescribes the existence of a minimum of three member categories, of which workers and users are obligatory - while guaranteeing the opening of the property structure to different stakeholder categories, influences the number of new enterprises set up.

The national experiences reported confirm the need to search for new legal frameworks and governance models (Italy, United Kingdom, Canada) appropriate for encouraging the new entrepreneurial dynamics of organisations pursuing social goals. In order to improve their performance as instruments of social cohesion, delivering welfare services and generating employment, new co-operatives, and more generally social enterprises, have to face a number of challenges. To name the most relevant ones: they need to establish new modes of stakeholder participation<sup>3</sup>. The community interest needs to be harnessed into the governance structures. The concept of democracy, as traditionally understood by the co-operative tradition, has to be rethought in consideration of co-operatives' broadening social commitment. Workable mechanisms of interest harmonization, aimed at motivating the different partners and contributors to work together for the common goal, are required. Moreover, new

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<sup>3</sup> In this regard, Girard put particular emphasis on municipalities' participation and desired the future legal recognition of municipalities as a possible member of Canadian solidarity co-ops.

ways aimed at keeping the difficult balance between productive and social aims have to be specified and new social accounting and reporting tools have to be developed.

Policies aimed at sustaining co-operative development focus on two different aspects. On the one hand, the adaptation of legal forms, still in progress in a number of countries. On the other, the support to be provided for co-operative expansion still needs to be explored.

Münkner gives evidence of how governments can support the development of MSCs in different ways. Beside providing a tailor-made legal framework, they can also support their development by removing administrative obstacles and by offering incentives (Denmark). Similarly, in the United Kingdom, the legal framework provided by the Industrial and Provident Societies Act allows a wide range of autonomy in the making of by-laws. This flexibility can accommodate the creation of MSCs. Alongside the availability of appropriate legal frameworks, other aspects are considered relevant for MSCs development, such as the readiness of all concerned to co-operate and the existence of favourable framework conditions.

From an overall perspective, the situation is moving forward also in transition countries. There is a slow rediscovery of co-operative forms, though the process is hampered by a general political distrust towards co-operatives. "Transition myths" still prevail, such as that of the market, which leads to an exaggerated trust in its potentials. Meanwhile, the US model has been often imitated without reflection on the contextual differences. The traditional non-profit concept, which was developed in the US, does not seem able to fulfil the needs of these geographical areas. Like in the US, co-operatives are mostly not perceived as organisations belonging to the social economy. This normally leads to their underestimation, notwithstanding the success achieved in contexts characterised by market failures.

A number of specific weaknesses - shared by all the national experiences explored - can be identified:

- the overall lack of suitable legal frameworks. Current legislation is often not consistent and it does not favour transparency. Moreover, the complexities of the current environment demand that new organisations are developed. Generally, an improvement of the legal

system is required, in terms of both consistency and availability of legal forms;

- lack of available data on issues like the size, typologies, scope and resources of social economy organisations (especially as concerns Republics of the former Soviet Union). This deficiency prevents an objective analysis of the social economy phenomenon as a whole and it does not contribute to enhance policy makers' and practitioners' awareness of the potentials of social economy organisations;
- poor managerial skills and lack of consciousness of entrepreneurship. The development and consolidation of new managerial competencies and skills has to be sustained. Besides knowledge transfer, the transition countries' culture - as concerns the social economy specificity and potentials - has to be developed.

Notwithstanding the aforementioned obstacles to co-operative development, some positive aspects can be singled out. The limits of the traditional non-profit model are widely perceived. New models have recently emerged (for example in Hungary and Czech Republic). The general trend is towards a social enterprise model, which makes little use of the co-operative model. The co-operative form has instead regained ground in its traditional functions (credit, housing, agriculture sectors). The successful experiences reported confirm this phenomenon.

## **PART 1**

General analysis of the co-operative phenomenon



## 2. The evolution of the co-operative form: an international perspective<sup>1</sup>

by *Giulia Galera* \*

### 1. Introduction

The co-operative form, owing to both the specific ownership assets covered and the relevance of the goals other than economic pursued, is particularly suitable to assume a number of connotations, consistent with the cultural and socio-economic environment which hosts it. These specificities contribute to render the co-operative typology an organizational form flexible and capable of adjusting to the changing economic, social and political conditions.

Starting from this assumption, this paper will especially focus on co-operatives' potentials. The recent emergence of new co-operative fields of activity, which contributed to co-operative revitalization, leads in fact to reflect from a theoretical point of view on the current potential of this organizational form.

In this respect, the still topical Laidlaw's report stands out, presented in Moscow at the ICA Congress in 1980, which underlined both the evolving character of the co-operative form and sensed a crisis of the co-operative movement around the World, while it tried to maintain its distinctiveness from the private sector and as it struggled in many countries to escape the dominating influence of the State. Such concerns on co-operative role, identity and potential turned out to be increasingly well-grounded as the dismantling of most of the command economies took place in the former USSR countries and Western welfare systems entered a new reform phase (Laidlaw, 1992; MacPherson, 1995).

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<sup>1</sup> I would like to thank Professor Borzaga for his advice and unfaltering support.

## 2. Co-operative models

Before focusing on the recent evolution of the co-operative form towards fields of activities other than traditional ones, a brief overview of the main co-operative models that have developed in the different national systems is useful. Co-operative systems are brought back to the following models: the sociological model, characterizing co-operatives open to the community interest, the mutualistic model, characterizing co-operatives claiming members' interests, a third model to be placed in-between (combining both the members' and the community's interests) and finally the quasi-public co-operative model, which developed in both former socialist and communist countries.

Moreover, the most relevant difference among co-operative models regards both the opening to the collectivity and the general interest pursued as opposed to the restriction with respect to non-members. A strict classification is, however, difficult as both the main models present some features which traditionally characterize the other model. While the sociological model does include an economic component, the mutualistic model does not disregard some social aspects, whereas, for example, while pursuing a strictly mutual goal, it keeps an open membership or it attempts to take care of impoverished population groups. Rather than referring to pure theoretical models, which may not be found in the reality, it seems therefore to be more suitable to speak about co-operative systems in terms of belonging to a *fundamentally mutualistic* or *fundamentally sociological* models, as well as co-operative systems to be traced back to a sort of *in-between model*.

Differences between co-operative models reflect the ideological sources inspiring the single cultural environments and legal trends, themselves brought about by a number of cultural, political and socio-economic aspects.

### 2.1. The fundamentally mutualistic model

The fundamentally mutualistic model refers to strongly member oriented organizations, which are in their extreme version exclusively based on their economic interest. In co-operative systems characterized by the

prevalence of this model, co-operative organizations are perceived as private enterprises, differing from traditional enterprises because of their ownership rights, rather than in virtue of the social function pursued or the democratization role played in the economic system. Co-operatives are not asked to pursue social goals and their specificity is their capacity to operate in contexts of market failures.

The strict observance of the mutuality principle and the clear economic orientation are both features shared by most co-operative movements belonging to German-speaking countries (where co-operative extroversion is rejected, in the name of the so called *Selbsthilfe* and *Gegenseitiger Nutzen*), and to the USA.

Under the German Co-operative Law, co-operatives are considered private self-help associations, primarily designed to provide advantages to their members, but not as instruments of social reform (Beuthien, 1989). As the German co-operative doctrine underlines, co-operatives pursuing collective goals, as a deviation from the original co-operative model, risk losing their self-help character and are consequently destined to turn into other types of organizations intrinsically devoted to promoting others' interests<sup>2</sup>. As concerns fields of activity, the German co-operative scenario is mainly composed of *Raiffeisenbanken*, *Sparen - und Darlehenkassen*, *Volksbanken*, which carry out banking activities; purchasing co-operatives, carrying out wholesale trading activities and housing co-operatives, which still hold a position of particular importance in the field of urban social housing. On the whole, co-operative practical significance in the twentieth century with respect to the German economic life has been decreasing, if compared to both the socio-political and economic importance gained by the co-operative form in the nineteenth century (Dolce, 1993, p, 1721). In addition, unlike other European countries, as a result of their purely declared private-nature, both the Austrian and German co-operative sectors have lacked a public recognition, which generalized the economic behaviour of co-operatives. Accordingly, they are normally not perceived as alternative to the traditional companies (Ciriec, 1999). Similarly, also the USA co-operative system is mainly characterized by co-operative organizations traced back to the fundamentally mutualistic model, which are fundamentally addressed to

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<sup>2</sup> Digestus Project (Network for Laws on Social Enterprises in Europe), Germany, 1999.

replace not well functioning markets. Co-operatives under this model are like all other kinds of enterprise. They do not have any kind of social constraints and they can only be distinguished due to their property structure (profits are distributed to non-investors).

## **2.2. The fundamentally sociological model**

The fundamentally sociological model makes reference to co-operatively structured organizations which are explicitly extroverted. They can be expressly aimed at promoting the general interest of the community or they can tailor the economic system's democratization. What characterizes this model is the pure openness towards the external interests. These co-operatives have been historically used also to supply public or merit goods, with a consequent weakening of the members' centrality. Among the legal systems strongly characterized by a so called "weak mutuality" are to be placed those countries where co-operatives evolved as community enterprises, demonstrating thus an intrinsic social responsibility. There is a lack of literature on this topic and co-operatives tend to be confused with community-building organisations (popular economy). Are to be placed in this grouping a number of Latin American co-operative experiences. The development of this model was also the theoretical response to political requests, committing co-operatives the task of democratizing the economy and coping with certain social unresolved concerns.

## **2.3. The in-between model**

Beside member and community oriented co-operative systems, a third grouping is to be mentioned, which includes the majority of the European legal systems. It refers to those systems where the ambiguity of the mutuality concept, as asserted in the different legislation governing co-operatives, has been open to different, often opposed interpretations, defending co-operative mutual nature or claiming co-operative social function. To be placed under this grouping are the European co-operative legal systems which are traditionally *mainly* mutualistic, for instance the Italian and French legal systems, as well as the Belgian, Span-

ish and Portuguese ones. In these cases, the pursuing of the “member interest” does not prevent co-operatives from reaching collective goals. Nevertheless, article 2511 of the Italian *Codice Civile* judges the *scopo mutualistico* as co-operative foundation, whereas article 45 of the Italian Constitution recognizes co-operative social function. Through the addition of indivisible reserves, the *Legge Basevi*, introduces a relevant (although not total) profit distribution constraint. On the whole, both the Italian doctrine and law consider the mutualistic goal as the obligation to provide members with more favourable goods, services and working conditions with respect to those to be found in the market. Unlike the German point of view, which deliberately promotes members, the 2511 article of the Italian Code focuses on the co-operative *enterprise*, where co-operative members are only indirectly involved by means of the mutualistic principle (Grossfeld, Noelle, 1985).

Similarly, the French *Loi* n. 47-1775, 10 September 1947, while stressing co-operative self-centred nature and reasserting the concept of self-help, it affirms that *les coopératives ne peuvent admettre les tiers non sociétaires à bénéficier de leurs services, à moins que les lois particulières qui les régissent ne les y autorisent*. Such a provision, while basically confirming the French mutualistic orientation, does not deny the possible opening to non - members (Di Rienzo, 2000). Beside co-operative general structural characteristics, special laws allow indeed departures from the general law, as far as providing, for example, for the pursuing of a collective goal and allowing operations to be carried out with non members (Münkner, 1985).

#### **2.4. The quasi-public co-operative model**

According to the quasi-public co-operative model, co-operative organizations are perceived as public enterprises. Their governing rules are in fact dictated by public authorities. This model can be found - in different variants - in former socialist and communist countries.

The socialist co-operative theory - although apparently linked to the worldwide co-operative theory - was strongly influenced by the real socialism and by the socialist understanding of property. According to socialist thinking, co-operative property represented a special form of collective property and a transitional form towards state property. Co-

operatives were regarded as an instrument whereby private property was to be transformed into socialist property through the promotion of both a socialist conscience and a socialist education. Co-operatives were an integral part of the political system and planned economic system (Münkner, 1998): they implemented centrally made plans, educated members in the communist way of life and fulfilled social functions.

In the former communist countries co-operatives were mainly instruments in the hands of both the government and the ruling party, while the first private profit-oriented enterprises were allowed under the 1988 co-operative law, which legalized the establishment of new autonomous co-operatives with a minimum number of three members. The co-operative provided a suitable organizational framework for an easy business start. Even though the newly established co-operatives were allowed to operate in a limited number of sectors (service providers, restaurants) and they were supposed to be founded on the co-operative principles as recognized worldwide, they largely carried out both illegal business activities and business for financial gain (ILO, 2001, p. 20).

This trend was dictated by the USSR government's attempt to satisfy the consumer markets with new products, which could not be sufficiently supplied by the government. Consequently, co-operative organizations turned out to be the only organizational forms suited both to correct and reform the defects of the planned economy (Borzaga, Galera, 2004). The collapse of the soviet system, while accelerating the disappearance of many co-operatives, left negative cultural memories.

### **3. Co-operative models' recent evolution**

The 80s and 90s witnessed a number of changes, concerning some models more than others.

With special regard to the co-operative systems characterized by the prevalence of a *fundamentally mutualistic model*, no relevant changes have occurred in the last decades. What can be noticed is the attempt to suit the needs of large scale service co-operatives (Germany), a decrease in the importance of co-operatives and a general trend to replace co-operatives with for-profit companies.

The national systems characterized by the main recourse to a *fundamen-*

*tally sociological model* have meanwhile confirmed their community connotation. Information on this model is in general poor. Especially challenging is the role recently gained by co-operatives in the micro-credit sector, and thus in the fight against poverty and social exclusion.

Moreover, relevant changes have instead concerned co-operative systems characterized by an *in-between model*. This is particularly true in a number of European countries - namely Italy, France, Spain, Portugal - where new co-operative initiatives, that involve enhancing co-operative intrinsic social responsibility towards the entire community, have recently developed in a mainly empirical way going beyond the *mutualistic model* towards the pursuit of general-interest goals. In these countries co-operatives have turned into providers of social and personal services, once guaranteed by the Welfare State, as well as new services addressing an emerging social demand. This phenomenon has actually paved the way for a general co-operative evolution *strongly socially oriented*, characterized by a multi-stakeholder connotation. It is therefore useful to give particular attention to this specific trend.

#### **4. From co-operative to social enterprise: a European perspective**

##### **4.1. The plurality of organisational forms**

The relevance of alternative organizational forms - traced back to the so called *Third Sector*, *Social Economy* or more recently *Social Enterprise* concept, depending on the particular approach and tradition adopted - is explained by a number of socio-economic changes which have occurred. On the one hand, the globalization process which makes for-profit enterprises (multinational and small and medium-size enterprises alike, which above all represent the majority of the European enterprises) become increasingly competitive. This leads towards finding ways of reducing costs and it has generated a decreasing commitment in taking responsibility for a number of social problems (employment stability, employment of elderly and less productive workers, etc.). On the other hand, the public supply of general-interest services (especially social services) was unable to meet the increasing demand of services, owing to

public budget difficulties. From an international perspective, in some European countries new legal forms designed to encourage the entrepreneurial dynamics - that are part of a social project - have recently been introduced at national level, whereas in others traditional non profit and co-operative structures keep being the most relevant organizations. Moreover, the economic weight of these kinds of organizations is unevenly distributed throughout Europe.

Socio-political, cultural and economic circumstances at the national level explain the prevalence of one specific organizational model, namely the consolidation of the co-operative, associative and more rarely foundational models, as well as the remarkable increase of commercial enterprise experiences characterized by a social connotation.

In countries where the legal systems allow associations to carry out a significant economic activity, such as France and Belgium for instance, associations have up to now played a major socio-economic role, without changing some inherent characteristics, such as the lack of worker participation in the decision-making processes and the low levels of capitals. On the contrary, in countries where associations have been characterized by ideal purposes, the co-operative legal form is the framework mostly covered by organizations included in the aforementioned empty space. It is possible though to envisage a convergence in the organizational forms, namely the associative and the co-operative forms (Conseil Supérieur de la Coopération, 1999)<sup>3</sup>. They are increasingly drawing together; from the one side, the associative form has been gradually adapting the development of truly economic activities<sup>4</sup>. From another side, the co-operative form has been increasingly engaged in the supply of new typologies of services. More specifically, some traditional co-operative forms - such as worker co-operatives - increasingly revealed their inadequacies to supply certain services aimed at the community, owing to the limited involvement of the users in decision-making processes and the lack of voluntary participation. As a consequence, the recourse to new co-operative forms

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<sup>3</sup> This phenomenon has been taking place in other European countries as well and was first brought out by Cecop. See Cecop, *Social Enterprises: an opportunity for Europe, First European Conference on Social Cooperation, Research on social cooperation in Europe*

<sup>4</sup> This trend has been supported by the public policies. Social-health associations (of which 90,000 among 880,000 associations) obtain in France 49% of all the public funding. *Les associations en chiffres*, in *Entreprises et Carrières*, 19-25, June 2001.

adapted to meeting the community needs in a stable and continuous way was put forward in a number of countries, such as Italy, Portugal, Spain and more recently France. Meanwhile, in some Northern European countries, characterized by a major openness of the co-operative legislation to extensive interpretations, such as Sweden and England, traditional co-operatives resembling the so called social co-operative initiatives have started to be increasingly engaged in new fields, such as social service provision and work integration.

#### **4.2. A brief overview of the recent co-operative evolution which has occurred in some European countries**

The recent development of new co-operatives in EU countries is connected above all to their further engagement in the supply of educational and social services, which are carried out beyond the “boundaries” of the co-ops membership. This emerging trend undermines the traditional model of co-operatives, which is based on both a single stake-holding system and the identification of members and users, leading toward openness and readiness to have additional interested parties sharing in the duties and benefits of the organization (Levi, 1999). Similarly, the involvement of various kinds of stakeholders in the decision making process contributes to the promoting of a sense of social responsibility at local level. This new social and co-operative economy aimed at achieving general interest objectives is arising, in particular, in different European countries (Monzòn Campos, 1997); new types of co-operatives have started to emerge from the ‘80s onwards to take care of elderly people, children, disadvantaged people and to provide basic services, such as health care and other social support services. Alongside, vulnerable groups started to join workers’ co-operatives or community-based service co-operatives (ICA, 1995) and new co-operatives active in a number of different sectors (waste management and recycling, environmentally friendly tourism, etc.) have started to flourish (ILO, 2001). The aforementioned co-operatives, mainly supplying community services that benefit both members and the local community, resulted both from the changing role of the local state as regulator, rather than provider, and the emerging of new unsolved social and environmental problems. And their successful entry into public sector activities is mainly

explained by their capacity of integrating different interests, such as: those for the good of their members and for the common good, as well as personal and societal gain (Lorendahl, 1997). New co-operative solutions include: social co-operatives, community co-operatives, co-operatives for social solidarity, co-operatives d'interet collectif as multi-stakeholder co-operatives. In some cases, co-operatives have turned into a successful alternative modes of welfare delivery, such as the Swedish *co-operativization* of the public sector proves, whereas more than 66 % of private day-care centres are co-operatives (ILO, 2001, p. 52).

Interesting examples of new co-operative forms, mainly pursuing collective goals, are given also by Finnish village co-operatives, which are increasingly moving towards the production of social and health care services in the countryside and are usually formed by the majority of villagers in order to guarantee services to the local community (local shops, primary schools and social services) (Pattiniemi, 1998). Italy witnessed a remarkable development of *cooperative sociali* (social co-operatives), explicitly aimed at pursuing the general interest of the community in terms of human promotion and the social integration of citizens. In Spain, *Cooperativas de trabajo asociado* have started to provide personal services (social services, educational services, health-care services) for the local community and co-operatives with a social aim, engaged in the work integration of disadvantaged workers in the open labour market after a period of on-the-job-training. In France, a new typology of co-operative has recently emerged: *coopérative d'interet collectif*, which developed from producer co-operatives, as well as associated co-operatives (InfoScic, 2000). The United Kingdom provides another interesting experience: community businesses which have been very successful as a way of mobilizing local communities to provide collective services. This idea first developed in rural areas, but has then successfully transferred to city areas (like for example Glasgow) (Spear, 1998). More recently, a new type of company: the Community Interest Company (CIC), was designed for social enterprises eager to use their profits and assets for the public good.

Alongside the evolution from traditional services towards collective services of activity, a legal development has also occurred. Such an evolution shows relevant differences among European countries.

*Spain*<sup>5</sup>

Co-operatives with a social orientation are regulated by three local laws: mixed co-operatives of social integration in Catalan (Law 1983, art. 106); co-operatives of social integration in the Valencian Region (Law 1985, article 82) and in the Basque Region (Law 1993, article 127), where social co-operatives are mainly made up of physically, mentally or socially disabled persons. In addition, a public unit specialized in social services may join the co-operative, which can be established as consumer or provider co-operative. The general law of 1987 did not refer to this type of co-operative, while the 1999 law provides for co-operatives of social initiative, which are engaged in educational, welfare, medical and work integration services. As provided for under the three aforementioned local laws, these co-operatives are ruled by the co-operative regulations referred to the activities carried out. An additional provision specifies what the absence of a profit goal means: no results distribution, capital rate limited to the legal rate, mandate at the board of directors unpaid, employed members' and hired workers' remuneration not higher than the 150% of the remuneration of the collective bargaining.

The solidarity carried out by the Spanish social integration co-operatives is more internal than external, since it has firstly to be addressed to co-operative members, rather than to the outside. According to the circumstances, social integration co-operatives can be regarded as a sort of specialization of consumer co-operatives, worker co-operatives, or a combination of the two of them, where the co-operators are beneficiaries and sometimes employees. Consequently, social integration co-operatives fit the traditional member-oriented co-operative definition.

On the other hand, co-operatives of social initiative bring in some new elements. Their legal definition underlines their extroverted vocation. According to article 106 (Law 27/99 of the 16<sup>th</sup> July 1999), co-operative of social initiative may supply services which benefit co-operative members, through a consumer co-operative. But the same article 106 opens up to the supply of services of collective interest or public social services, as well as economic integration by work of socially excluded persons. In

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<sup>5</sup> The main reference Laws are the following: Co-operative Law n. 27/99, which replaces Law 3/87; and the different regional Laws: Catalan Law 4/83, amended by Law 13/91; Andalusian Law 2/85; Valencian Law 11/85, emended by the Law of 22 February 1995; Navarre, Law 12/89; Basque, Law 4/93.

such a perspective, the 1999 law seems to number moral persons of public law among the possible co-operative members.

### *Italy*

Law N. 381/1991 on *cooperative sociali* (social co-operative) provided the legislative framework for a well-developed existing phenomenon.

Italian social co-operatives have, indeed, not been constituted, but just recognized by the 1991 law. According to it, their goal is to “pursue the general interest of the community in promoting personal growth and in integrating people into society by providing social, welfare and educational services (A type) and carrying out different activities for the purposes of providing employment for disadvantaged people (B type)”. A type co-operatives offer a wide range of services to different population groups: the elderly, minors, the disabled, drug addicts, the homeless and immigrants from outside the European Union. B type co-operatives are required by law to hire at least 30 per cent of their staff from among disadvantaged categories of people, and disadvantaged workers may be allowed to become members. In exchange, they do not pay social security contributions and may receive government subsidies (OECD, 1999). The ownership structure is variable and it can comprise several categories of members (worker member, user members, voluntary members, subsidising members and legal entities). Volunteers can become full members, provided that they do not constitute more than 50% of the total number of members.

### *Portugal*<sup>6</sup>

Co-operatives of social solidarity were not provided by the Co-operative Code dating from 1980. The decree n. 323/81 considered “social solidarity” as a field of activity where service co-operatives were allowed to operate. In addition, “special education and integration co-operatives”, regulated by the decree n. 441-A/82, art. 3, were established as a result of the 1974 democratic revolution. These kind of co-operatives were actually used by parents of disabled children and professionals operating in the same field in order to cope with the need of special education and rehabilitation institutes. The co-operative form, beside reasons of eco-

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<sup>6</sup> The main reference laws are: the *Código Cooperativo*, published by law 51/96 and law 7/98.

conomic convenience, was chosen because of its important elements of autonomy, solidarity and economic organization. The introduction of a new form of co-operative, namely the social solidarity co-operative, was indeed meant to put all these kind of co-operatives under the same definition (do Campos, 1998). Their statute was specified by the 1998 law, which defined their goals as follows: to give support to vulnerable groups (children, teenagers, disadvantaged persons, old persons), families and socially disadvantaged communities in view of their economic integration, as well as to Portuguese emigrants in difficulty; to establish support programs; to promote both education and work integration of socially disadvantaged groups. The 1998 law differentiates regular members - beneficiaries of the services supplied, members of the family benefiting or collaborators remunerated - from voluntary members - bearers of goods and services not remunerated, donors. These do not have the right to vote and are neither electors nor eligible, but they may constitute with the social bodies a consulting committee called "general council" (articles 5 and 6). The surplus has to be assigned to the reserves, which are entirely indivisible (articles 7 and 8).

Social solidarity co-operatives, as defined by law 1998, are expected to satisfy the social needs of their members, their promotion and integration. But at the same time, social solidarity co-operatives are expected to carry out activities characterized by an extroverted connotation, such as: the support to disadvantaged groups, families and communities in difficulties, etc. (Espagne, 1999). Social Solidarity Co-operatives play an active role against social exclusion, which is not limited to the rehabilitation of disabled persons, but which covers many other forms, such as the support given to elderly people and the inclusion of both individuals and communities socially disadvantaged.

### *France*

On June 28<sup>th</sup>, 2001 the French National Assembly introduced a new co-operative form into the French system: the Co-operative Society of the Common Interest - *Société Coopérative d'Interet Collectif (SCIC)*. The legal environment in which this new form finds itself is within the overlapping legal spheres of the individual business and of the association.

The SCIC, promoted at the local level by production co-operatives

(Detilleux, 2000), has entered the wider discussion about the social enterprise in France, adding to the existing co-operative forms. This new form offers the players within the social economy a new instrument for use in fighting social exclusion and satisfying community needs.

In the absence of a legal structure adapted to meeting the community needs in a stable and continuous way, the introduction of a new co-operative form was made possible<sup>7</sup> through the adaptation of the existing legal framework<sup>8</sup>. Concerning the ownership structure, more member categories are admitted. The law prescribes the existence of the minimum of three member categories, of which workers and users are obligatory.

## **5. The emerging of new co-operatives and fields of activity in Non-European countries**

Co-operative increasing involvement in the provision of social services is to be noticed in some non European countries, such as the United States, Japan, Canada, Philippines and Latin America.

U.S. co-operatives have been increasingly involved in community development, as the National Rural Electric Co-operative Association began in the mid 1980s to advise its members - 900 electricity supply co-operatives operating in 2,600 of the 3,100 counties in the U.S., Puerto Rico and American Samoa - to become more actively involved in matters that directly affect the quality of life in rural America, notably economic development and job creation (ILO, 2001). In Japan, established and newly created co-operatives, have started to take part in the social health care sector: agricultural co-operatives provide health care services in rural communities, where aged population rates are higher. In addition, an interesting co-operative contribution in rebuilding the communities, in light of the ICA's 7<sup>th</sup> Principle, was given to the Kobe region, strongly affected by a destructive earthquake in 1995 (Kurimoto, 1997). The Kobe Coop was able to take prompt action as an organization rooted in the community and the tragic experience also helped foster closer ties

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<sup>7</sup> Alain Lipietz, *L'opportunité d'un nouveau type de société à vocation sociale, Rapport relatif à la lettre de mission du 17 septembre 1998 adressée par Madame Aubry, Ministre de l'Emploi et de la Solidarité, à A. Lipietz.*

<sup>8</sup> Law number 47/1775 of the 10th September 1947.

with various public and civil organizations. Similarly, the social and health care sector in the Quebec Region in Canada which for the last 12 years has been witnessing an original co-operative development. Starting from the ambulance transportation service, co-operatives have put down roots in a number of sectors, by making use of the whole range of co-operative typologies: consumer co-operatives, worker co-operatives, producer co-operatives and solidarity co-operatives.

During the 1990s there was a growth in number of co-operatives providing home services, particularly to elderly persons. The emergence of these kinds of co-operatives is due to different reasons, such as: the lack of resources, the will to participate in the labour organization and a wide consent to cover emerging needs. With respect to health co-operatives, their development opportunities are yet to be evaluated. Although trade unions keep opposing co-operative development, the presence of new actors, such as municipalities and popular banks, are supporting the establishment of these kinds of co-operatives, especially those particularly concerned about the survival of their belonging communities (Girard, 2001). Child-care and nursery school-co-operatives are also well developed<sup>9</sup>. These co-operatives were the first to create programmes for children with special needs. This occurred in Hamilton, Ontario in the early 1970s. By the early 1990s three such programmes, in Hamilton, London and Toronto, were in operation. They received public funding to provide consultation and support services to day care and nursery co-operatives serving children with special needs<sup>10</sup>.

Another example of the new social orientation of the co-operative form can be found in Latin America, especially within the sector of micro-credit, which has gained a leading role in the last 20 years. Such institutions are of great importance in reaching the millions of impoverished people who have no access to credit and are both socially and economically excluded. Organizations such as ACCION, which is comprised of a network of 19 groups operating in 15 countries, use micro-lending as a tool for social development. The use of microcredit co-operatives is increasing and gaining importance as a instrument for social change

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<sup>9</sup> The oldest known co-operative nursery school began operations in 1937 in central Toronto.

<sup>10</sup> International Co-operative Information Center, *Review of National Experience in Promoting and Supporting the Contribution of Co-operatives to Social Development - Co-operative Enterprise in the Health and Social Care Sectors, A global Review and Proposals for Policy Coordination*, internet : [www.wisc.edu](http://www.wisc.edu).

(Otero, 2001). Finally, in the Philippines a number of co-operatives affiliated with the National Confederation of Co-operatives (NATCCO) established daycare centres for their members. These were so successful in meeting needs within the communities in which the co-operatives operated that they were subsequently opened to non-members. This was the case, for example, in the Palompon Community Credit Co-operative, in Leyete, and in the Oyao Multi-Purpose Co-operative in Nueva Vizcaya<sup>11</sup>. What is noteworthy is co-operative evolution towards sustaining a more balanced economic development.

## 6. The co-operative scenario in transition countries

As a result of the collapse of centrally-planned economies, the next challenge was to re-establish both a co-operative identity and a new co-operative system. In the first phase of transition, governments opposed co-operatives, considering them part of the “inherited” social and economic structure. Their transformation into capitalistic companies was preferred<sup>12</sup> to the recognition of the potential of co-operatives in an emerging civil society - the creation of civil communities and economic coordination of the citizens. At the beginning of the transition, the literature on economic reform was in general critical of the potential role of employee ownership in enterprise restructuring: it was expected to promote large wage increases and inflationary pressures, a deterioration in economic performance, considerable delays in restructuring, labour hoarding, and a low propensity to carry out necessary investments. This privatisation form was rarely proposed in policy documents and its negative effects were systematically presented, while its potential advantages were completely ignored (Vaughan White-head, 1998). As compared with the alternative of external ownership of joint stock companies, employee-owned firms are instead more likely to be characterized by a focused, tightly-knit ownership group with a strong stake in the enterprise performance. In such firms, the security and stability of the enterprise and its work will weigh more heavily in decision-making. Accordingly,

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<sup>11</sup> International Co-operative Information Center, *Review of National Experience in Promoting and Supporting the Contribution of Co-operatives to Social Development - Co-operative Enterprise in the Health and Social Care Sectors, A global Review and Proposals for Policy Coordination*, internet: [www.wisc.edu](http://www.wisc.edu).

<sup>12</sup> The transformation into companies started primarily amongst the agricultural co-operatives.

insider ownership and insider control is more conducive to enterprise stability and long term relationships and thus may contribute to better economic performance (Jones, Mygind, 2000).

With the decline of communist regimes, co-operatives had to reorient their business strategy and develop entrepreneurial skills. The transition towards a market-oriented economic system took various forms:

- restitution of property to former owners (Czech Republic, former German Democratic Republic);
- privatisation by means of negotiable coupons, distributed to members, employees and former owners and sold to interested parties (Hungary, Russian Federation, Baltic States);
- dissolution and liquidation (Todev, Brazda, Schediwy, 1993)<sup>13</sup>.

Consequently, while some countries decided to dissolve all politicised unions and federations, others developed a sort of “planned transition”, also through employee ownership.

Nevertheless, recent developments show that a total disintegration of federal structures has usually led to a change of co-operatives into other legal forms and, thus, to a total de-co-operatization (Brazda, Todev, 1993).

However, the efforts to “de-politicise” co-operative unions, federations and apex organizations proved to be difficult. Not only was there a lack of leaders with experience of autonomous, market-oriented co-operatives but the primary co-operatives were weak and disoriented through the transition process.

The International Labor Organization (ILO) points out two major obstacles to the development of the co-operative sector in former socialist countries:

- first of all, a major obstacle to the establishment of new service co-operatives of farmers, traders, craftsmen and members of liberal professions was that during the first years of the new regime, there were not enough private farms, businesses and individual entrepreneurs to constitute a membership, even after decades of collectivisation;

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<sup>13</sup> The Polish law on changes in the organizations and activity of the co-operative movement from 1990, instituted the dissolution of all co-operative unions with the exception of the highest council of Polish co-operatives. Similarly, in Bulgaria in 1992 all agricultural production co-operatives were dissolved with no consideration of the fact that some had been successful even before the communist takeover in the 1940s.

- another obstacle was the lack of an adequate legislative framework regarding ownership of land, property rights and access to financial services. In addition, there was no effective administrative machinery to put the new legislation into effect. Although the economy was liberalized at high speed, reforms of government structures at national, regional and local levels lagged behind so that these structures remained largely unchanged (ILO, 2001, p. 19-23);
- an additional problem is created by the introduction of market reforms while allowing socialist structures and thought processes to still exist throughout the public administration, and of introducing private property of means of production without corresponding property rights and chances for the private owners to exercise their rights.

It has become clear that privatisation and transformation not only require legal and economic restructuring, but also create socio-psychological problems for those involved at all levels, making it more difficult to find solutions. This means that “the abolition of ideological influences upon the economy coupled with the admission of a variety of forms in the economy are mandatory requirements for the development of autonomous co-operatives” (Münkner, 1998). Prejudice towards the co-operative form in fact prevents this organizational form from developing in an environment characterized by an unregulated emergence of other types of organizations formally belonging to the third sector (voluntary organizations, self-help organizations, community organizations, religious organizations), regardless of the lack of legal provisions for organizational forms.

At present, the co-operative development paths as evident in the former communist countries are above all connected to the existence of adequate legislative frameworks that focus ownership of land, property rights and access to financial services, and the involvement of the co-operative movements in the legislative process.

However, while the traditional co-operative sectors are in decline, newly established co-operatives, such as credit unions (which were wiped out under the planned system), housing co-operatives and agricultural co-operatives are increasingly being looked upon as effective social tools, capable of fighting against social exclusion and the increasing unem-

ployment concern that resulted from the dismantling of the former industrial structure.

As many state enterprises have been closed down, new types of activities have been set up within the consumer co-operatives, such as shoe repairs, clothes sewing, photo studios, pharmacies in rural areas. Yet private firms have not replaced state enterprises, co-operatives, especially consumer co-operatives, might have a gap to fill (Sätre Ahlander, 2000).

In particular, while co-operatives are returning to their original roots, they have an important role to play in sustaining both social and economic development. And notwithstanding the apparent “co-operative vacuum”, in the long term co-operatives will surely become indispensable institutions of agricultural, rural and social development. With respect to agriculture, as a result of both the increasing competition within the global market and the lessening of support given by governments, farmers will need to look for new solutions.

In this respect, agricultural co-operatives will have an important role to play in these issues (Pattison, 2000). Co-operative action could be effective in promoting the consolidated tenure of highly fragmented landed properties, by establishing “land renting” co-operatives. Similarly, a number of services could be supplied through co-operatives. The dismantling of the former system created indeed a hiatus of service providers not replaced at present by either private or the public sectors. Transition countries could learn from the experience of European countries. This applies to social services (health, elderly and child-care, etc.) (Copac, 1999), which could be successfully supplied through co-operatives. What emerges is the potential of co-operatives as community organizations, which are increasingly showing a positive impact on both economic development and the process of democratisation. In particular, such kind of co-operatives should be considered as significant tools for social change.

As social tools, co-operatives can be used to foster social cohesion, which is threatened by a sharp rise in poverty, growing unemployment rates and high levels of inequalities, resulting in a sharp social stratification of the population.

## 7. Conclusions

To sum up, alongside the long-established co-operative enterprises (agricultural supply and marketing societies, credit societies, consumer, etc.), growing over the last decades into large-scale enterprises, behaving almost like investor-owned companies and going through a number of crises resulting in either their disappearance or reduction, new co-operative fields of development are increasingly emerging (and re-emerging) in both Western and Eastern countries. In particular, new co-operatives which are naturally addressed to the local community stand out, as they offer life-quality enhancing benefits that can both serve disadvantaged people and the community at large. The interest on co-operative evolution towards a socially oriented model arises from its strong connection with the evolution of traditional welfare models towards a “welfare community” model. However, this trend determined a number of changes of the organisational and corporate models, partly assimilated by the law.

Moreover, this is particularly interesting and relevant for “transition countries” for two different reasons: developing a private economy and co-operative system and creating a new welfare system. On the one hand, the need for traditional co-operatives is becoming apparent. On the other, the lack of public expenditure - due to cuts in budgets, following the abandon of the planned economic system - addressed to the production of personal and social services, calls for new alternative solutions, among which stands out the bottom-up supply of community care services through the means of self-help. In this respect, the co-operative model may represent an effective means both for accelerating the transition and contributing to reduce a number of problems, like low labour demand and poverty, and for providing new solutions to cope with growing social problems.

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### 3. Remembering the Big Picture: the co-operative movement and contemporary communities

by Ian MacPherson \*

#### 1. Introduction

At its Manchester Congress in 1995, the International Co-operative Alliance adopted an *Identity Page* defining the nature of co-operatives today (MacPherson, 1996)<sup>1</sup>. The page reflected issues that stretched back a century or more and echoed debates that had characterized the international co-operative movement since its beginnings. It stirred debates that had first emerged out of historic differences and contrasting understandings, for example, between Northern and Southern Europe (Watkins, 1986; Birchall, 1994, 1997; Rhodes, 1995). It brought forward perspectives from other parts of the world. It reflected the different perspectives of established co-operatives - consumer, worker, agricultural, financial, fishing and housing - and “new” co-ops - social, environmental and recreational. Beneath were longstanding tensions between co-operativism and other ideologies, including democratic socialist, Marxist, liberal, conservative and anarchist traditions. It reawakened concerns over the nature of democracy within co-ops in all parts of the world and invited debate on relationships with the state, particularly since the role of the state seemed everywhere in decline. It responded to gender issues and concerns about inclusion. It resurrected what, in the Canadian movement, was once called the “Big Picture”, the questions of fundamental purpose and commitment that should characterize co-op development and infuse co-operative institutions. It re-examined another old question: the relationship between co-ops, the co-operative movement and the communities they served - the movement’s social obligations.

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<sup>1</sup> For a copy of *The Identity Page*, a background paper on the principles, and a paper on the context within which the *Page* emerged.

The *Statement of Co-operative Identity* was a reaction to four major contemporary trends: the disintegration of the centrally planned economies of Central and Eastern Europe; the unclear roles of co-ops in many Southern countries; the overpowering dominance of market ideologies and classical liberal thought; and increased global integration through technology - the advent of what Marshall McLuhan had called *the global village*. The search for this statement unknowingly began with Alexander Laidlaw's report (1980) on *Co-operatives in the Year 2000*, prepared for the Moscow Congress of 1980. Laidlaw was a good choice for that task: he had travelled widely for someone of his generation and he knew about co-ops in many parts of the world. He was the protégé of Moses Coady, the principal founder of the Antigonish movement at St. Francis Xavier University and Canada's most profound co-operative theorist in the mid-twentieth century. Coady, in fact, was the person who popularized the term "Big Picture" in his speeches and writings (Walton, 2001; Laidlaw, 1971).

Laidlaw identified several challenges confronting co-ops: declining member commitment; weakening democratic participation; neglect of education; poor communication systems; uncertain roles for elected leaders; how they might better serve the poor; uneven employment practices; and sectoral disunity. All these problems involved the ways in which co-operatives were situated in their societies, how they encouraged member involvement, and how they responded to communities. Laidlaw anticipated four major opportunities, all of them as much social as economic: feeding a hungry world; providing productive labour; contributing to a consumer society, and building co-operative communities.

In 1984 at the Hamburg Congress Michael Trunov of the then Soviet Union prepared another paper that considered the social roles of co-operatives<sup>2</sup>. He argued that the international movement needed to take more responsibility for building global peace, encouraging new co-op development, ensuring greater food security, and counteracting environmental degradation. He ran into opposition from those who resisted the idea that the co-op movement should be "used" (as some interpreted his approach), but many were attracted to the idea that co-op should address the major issues of the time.

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<sup>2</sup> For a summary of his paper see International Co-operative Alliance (1984).

Lars Marcus (1988), the President of the ICA in 1988, built on these reports and extrapolated from his own experiences to challenge the international movement to reconsider its basic values and rethink its fundamental commitments. Marcus spoke from his efforts to expand the ICA's work beyond its North Atlantic and particularly its European base. He was also committed to expanding the ICA's base beyond its traditional consumer co-operative core to include more genuinely all kinds of co-operative enterprise. That process had begun in the 1950s through the work of several leaders, many of them, like Nils Thedin (1988), also from Scandinavia. It was demonstrated in the opening of the India Office in 1960 and the Moshi office in 1968. Marcus and the ICA Director, Bruce Thordarson, continued the process as they oversaw the opening of an office in Central America, the regionalisation of the ICA governance/managerial structure, and the beginnings of ICA international co-operative development projects.

These were big changes for the ICA, shaking old patterns of association and posing significant managerial problems, as Marcus's paper at the 1988 Stockholm Congress and subsequent events indicate. It was one thing, in the *cliché* of the times, to think globally and act locally; it was another to actually do it. The challenges, moreover, were greater than Laidlaw had anticipated and they formed a menacing background as the discussions developed. Older co-ops, in particular, were changing dramatically as they were buffeted by what became popularly called globalisation in the 1990s: the intensification of international markets; the creation of large economic blocks, like the European Common Market and the North America Free Trade Area; the rapid transformation of communications systems; the re-engineering of firms into flatter management systems; the increased mobility of capital; the "outsourcing" of labour; the declining roles of the state and entitlements; and the emphasis on economics over social policy. For many co-operators caught up in these issues, it could be a bewildering and unwelcome diversion from essential duties. For others, though, particularly outside of the North Atlantic, it was a vital exercise, one to be engaged with considerable enthusiasm.

The next step in the process was an international dialogue on co-operative values, led by Sven Akë Böök of Sweden (1992). Lasting from 1988 to 1992, it culminated in the book *Co-operative Values in a Changing*

*World*, written by Böök after extensive research and numerous meetings around the world. In it, he tried to reflect the wide, rich and diverse range of views he had found. The result is a volume that is not “an easy read,” its central arguments tending to be circular in ways more appreciated in non-Western intellectual traditions. It does not always follow the linear logic that has dominated Western thought since the eighteenth century, though it might be argued that it also reflects co-operative intellectual traditions rather well; traditions that are much more preoccupied with understanding ambiguities and shaping consensus than in finding irrefutable and permanent truth.

Böök’s study heightened discussions about community values and social obligations. He focused primarily on the movement and its institutions as he sought to make a coherent whole out of the enormously rich experiences and value systems he found within the international movement. He produced an essentially inward-looking document, recognizing the importance of new types of co-ops, particularly social co-operatives; the roles of co-ops in emancipating people from poverty and oppression; and the need for a new, broad and empowering vision.

Thus even before Manchester, there was a tendency within the international movement to reconsider the relationship between “community” and co-operatives. This was not, however, just a reaction to contemporary pressures; they were also echoes of discussions central to the movement’s origins, and they emanated from the ongoing strengths of the co-operative movement. While co-ops must constantly demonstrate their ability to meet business goals, they also function within specific contexts and historical traditions. They are steeped in the class, cultural, and ideological frameworks of their members and communities and they cannot escape them.

The Rochdale Pioneers, for example, envisioned creating colonies in the traditions of Robert Owen and his imitators; they were part of a working class culture and worldview that had been decades in formation. The consumer movements that emerged in their wake in many parts of the world, were not just concerned about purer and cheaper food, many within them were also “consumers against capitalism” (Furlough, Strikwerda, 1999). The worker co-ops that emerged in the nineteenth century, for example in France and Italy, were extensions of community activism

based on co-operative, religious or political motivations. Many early financial co-ops emerged from community concerns and the dreams of individuals, like Friederich Raiffeisen, Leone Wollenborg, Alphonse Desjardins and Roy Bergengren, seeking to ameliorate them. It is a tradition still very much evident in credit union circles, for example, in support for Community Economic Development and in contributions to education and social programmes. The agricultural co-operatives that emerged in the nineteenth and early twentieth century in Europe, more recently in other parts of the world, reflected crises in rural life as market economics transformed the ways in which rural people live; they were concerned about women's and youth issues, rural education and rural culture.

The communitarian concerns of most co-operative endeavors in the North Atlantic world, so strong in the nineteenth and early twentieth century, tended to wither in the twentieth century for many reasons, including the complexity involved in meeting both economic and social purposes. The only managerial models readily available were drawn from the military, government and private business worlds. Within the co-op world, there were remarkable searches for alternative forms of management systems; for example, in some consumer wholesales, federated structures in the community banking movement, some agricultural organisations, the network systems of Northern Italy, worker-oriented movements as Mondragon, and the "co-op corporations" of Asia. Their distinctive ways, built out from co-operative thought and practice, however, have never been fully studied or appreciated and they tended to lose their uniqueness as co-ops adapted to the market place. They tended to adopt "scissors and paste" management theory from other kinds of organisational behaviour rather than develop unique practices built out of co-operative values and principles.

The most serious challenge, in fact, came from the ascendancy of private enterprise models. A growing number of co-ops seemed content to follow the practices and conform to the values of their competitors, to be satisfied with being an "odd" variant of conventional business. Government officials, academics and business groups reinforced this trend, proclaiming consciously and unconsciously the superiority of the investor driven firm and making it the yardstick by which co-ops would be measured.

All too often, too, governments saw co-ops as agents for the implementation of their policies and forced their development or pushed them in directions useful for government purposes. Intentionally and unintentionally, they contributed to sectoral weakness by emphasizing business orientation over movement cohesion (Birchall, 1995; Laidlaw, 1980; MacPherson, 1999). They related to co-ops according to the kind of businesses they were in rather than as a sector or movement. They tended to encourage co-ops to operate in much the same way as their competitors in the market place: co-operative financial institutions like banks and insurance companies; agricultural co-ops like agribusiness; co-op housing like social housing. They de-emphasized democratic control structures and questioned the ideas and practice of “common capital” systems.

At the same time, though, many governments did encourage new types of co-operative endeavour. For a few decades in the middle of the twentieth century, many governments were influenced by the prevailing economic orthodoxies provided by Keynesian economic theory and institutional economics. Keynesian models, for example, encouraged governments to support marketing and supply co-operatives and to use co-ops in building social safety nets. That kind of economic theory tended to lose out, however, in the seminar rooms of Economics Departments and in the halls of power within governments as the twentieth century ended. Indeed, to be taken seriously, co-ops had to stress their economic roles, pointing to their financial successes more than their social contributions in order to be respected by governments.

The communitarian perspective also lost out as co-ops curtailed their educational efforts. Many co-operative movements in the later nineteenth and early twentieth centuries possessed remarkable educational programmes, embracing a wide range of the media of the day and effectively building the movement. They used educational processes to encourage diverse forms of co-operative enterprise, not just those in which they were directly engaged. As co-ops became pressed in their business activities and as their managements became increasingly “professional”, however, they reduced their educational role, converting it to marketing and institutional promotion and lessening their community emphasis.

Finally, the co-operative “communitarian tradition” never achieved suffi-

cient clarity and intellectual depth to be widely accepted, often collapsing into different kinds of socialist traditions, Marxist and Social Democrat, typically lumped together with them rather indiscriminately and unthinkingly. In a few places, it was even indistinguishable from anarchist collectivism.

Co-operative communitarianism is based on grassroots control and initiation and is committed to practicing reciprocity and mutuality. It excludes a kind of individualism that believes individual development is at least as dependent on group association as on individual initiative. Thought of institutionally, it sees enlightened individualism unfolding within a complex, often ambiguous set of relationships, including those associated with members, co-operative sectors, governments, and communities and reflected in daily management practice.

Thus, when the Manchester Congress addressed the social side of the international movement, it was resurrecting long held traditions of “community” but traditions that had faded in many established movements. It was also welcoming new co-operative forms through which people could control the social as well as the economic forces shaping their lives and their communal existence.

The Congress recaptured the social dimension of co-operatives in at least six ways: by inserting “cultural”, “social needs” and “aspirations” in the definition it accepted (the first definition ever agreed to by the international movement); by including “social responsibility” and “caring for others” in the value statement; by concretely encouraging inclusive memberships approaches; by emphasizing member involvement and control, a characteristic that would naturally broaden co-op mandates; by emphasizing “common capital” rather than continuing the tendency to think of co-ops as mere agglomerations of members; and, of course, by specifying a commitment to “sustainable communities” in the seventh principle.

Since 1995 the international movement has continued to demonstrate a growing commitment to social goals. This has coincided with recent shifts in economic thought that recognize the importance of social capital and the value of such fields as Social and Environmental Economics. Moreover, as the role of the state has declined, new co-ops have emerged meeting social needs in health, elder care and care for people

with disabilities. More generally, too, many co-ops have deepened their commitment to environmental protection, an acknowledgement of communal obligations. In almost every country, in fact, there are exciting new co-ops responding to social needs and opportunities derived from challenges facing communities.

There is, however, no simple road to enhanced social responsibility. Older, established co-operatives are significantly reflections of their traditions and are shaped by their memberships: they can expand possibilities incrementally, in a year-over-year fashion but they will not easily go through revolutionary reconstruction. The different kinds of established co-ops - consumer, farming, fishing, banking, worker and service - will identify possibilities in their own ways and according to the logic of their industries and their inheritance. New kinds of co-ops created in reaction to social possibilities will be more flexible, both in what they can do and in how they do it. There is a need to respect such diversity, not as easy as it might sound among co-operative people who can be quickly judgemental and critical of those who do things differently.

There are also challenges about how to embed commitments, in both established and new co-operatives. The history of the international movement abounds with examples of discarded priorities and weakened resolution, particularly as co-ops “mature”. Co-ops that started out with wide social visions have often become narrow in interests and limited in concerns. How can co-ops strive as they grow to retain their original commitments, to perpetuate their social concern? It is not a question easily answered.

The desire to address social and community obligations also raises issues about basic democratic practice. The mainstream co-operative movement reflects late nineteenth century concepts of democracy based on annual elections, one person/one vote and board accountability, though traditions vary dramatically with the type of co-operative and its traditional practices. They have led to well-established governance structures rooted in membership participation, either as consumers or producers. While such systems can always be improved and even modified to let other voices have access to power, they are not easily (or normally) substantially changed. The challenge is to reform them incrementally so that the social dimension is sustained, even nurtured, prudently.

There are also interesting issues involved in new co-ops, for example, harmonizing the roles of stakeholders in social co-operatives bringing together different professions and community groups as well as “traditional” members. There are uncertainties: how much power to whom and under what circumstances? How can conflicting agendas and priorities be harmonized? How can the general community interest be reflected in the governance structure? The international movement needs to study more closely the existing models that could provide some answers: the innovations of Northern Italy, other Mediterranean countries, France and Belgium; the relatively unknown (outside of the region) experiences of Latin America; the growing interests within Northern European countries, and the recent experiments in Asia and North America. Reflecting on the different ways people might organize co-operatives today is also important because our communities are changing so rapidly. Massive urbanisation (particularly in the South), the weakening of hinterland communities everywhere, increasingly mobile populations, isolation created by new technologies - all of these mean that “community”, always an ambiguous word, now has numerous definitions and understandings and, in fact, is being constantly redefined. From a co-operative perspective, perhaps that is the most important reason why the search for new forms of co-operative endeavour, within a prudent, honest and rigorous framework directly addressing community interests - and building on what the past has shown us - is a major initiative of our times, a *Big Picture* worth drawing once again.

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## 4. Multi-stakeholder co-operatives and their legal framework

by Hans-H. Münkner \*

### 1. Introduction

Central issues discussed among economists and research workers of social science are:

- mass unemployment;
- exclusion of under-qualified and disadvantaged persons;
- an aging society;
- local effects of a globalized economy;
- a new perception of the role of the state in times of democratization and decentralization;
- increasingly unaffordable systems of social security.

In these discussions a new term becomes more and more important: multi-stakeholder organisation (MSO) or multi-stakeholder co-operative (MSC), i.e. MSO with co-operative features.

According to Borzaga and Mittone, this new type of organisation is a combination of association and co-operative (Borzaga and Mittone, 1997, 12).

Interest in this new form of co-operative society has led the promulgation of new laws or the amendment of existing co-operative laws in Italy (1988, 1991), Canada (1997), Portugal (1998) and France (2001). In other countries, MSCs are established under current co-operative law (Germany), under special laws for community benefit organisations (UK), non profit associations, societies with social objectives (Belgium) or under general law (Denmark).

In the following the MSC will be presented as a form of organisation and as a legal pattern.

The MSC is not a totally new concept. It corresponds to the original mission of co-operatives to render services in all aspects of life, in order

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to cope with the consequences of rapid social, economic and technological change. In so far they differ from large modern co-operatives aiming mainly at providing economic services to members and often also to non-members.

By using MSC, problems of exclusion, unemployment and provision of social, medical and other services can be solved better than by conventional organisations:

- mobilisation of local resources for local development;
- activation of self-help potentials;
- enhancement of the inclination to cooperate and to practice mutual aid among all interested persons.

MSCs can bring about better results than public employment programmes, measures to provide work places for individuals or commercial service providers (Münkner, 1998; 2001b).

Public programs with attempts to identify job opportunities by officials must fail, if there are no vacancies. It is known from experience that paying for training programs for unemployed persons often results in teaching participants of such programs skills, which are not in demand on the labour market (Münkner, 2001b, 69 f).

MSCs can be an alternative to expensive bureaucracies for the administration of unemployment, seeking to integrate the excluded by promoting self-help and organised co-operation at local level.

From this point of view, MSC are a positive approach in line with international co-operative principles and should be supported by the established co-operative federations as one way of creating new and attractive forms of co-operation in times where the numbers of registered co-operatives are steadily shrinking as a result of mergers.

## 2. Description of the phenomenon MSC

As the name indicates, MSC is a co-operative society with a heterogeneous membership.

It is a *voluntary association* of natural and legal persons, i.e. a private self-help organisation (SHO), which does not exclude external assistance in setting up such society, public promotion and the right to participate in public tender and to take over the execution of tasks on behalf of the

community against a fee. MSC is *locally rooted*, it does not only promote the interests of its members but also works for the well-being of the community in which it operates. Accordingly, in the United Kingdom the name for such societies is “community co-operative” (Snaith, 1984, 188).

It is difficult to classify this new form of organisation in the conventional system of economic structures and legal patterns.

MSCs are:

- *organisations with economic activities, pursuing social objectives*, which brings the MSC close to non-profit associations with supplementary economic purposes. However, it is also working like an enterprise in competition with commercial firms, it has to make efficient use of scarce resources and needs professional management;
- *organisations with a special attitude towards capital and profit*. Whether MSC can be seen as non-profit organisations (NPOs) depends on the interpretation of this term. Like co-operatives, MSCs do not practice total distribution constraint, but offer limited return on share capital and may distribute part of the surplus among members in proportion to business done (patronage refund), if the by-laws so provide and the members so decide.

Borzaga and Mittone classify MSC as not-for-profit organisations with limited distribution constraint (Borzaga and Mittone, 1997, 14).

When carrying out economic activities not only as a supplementary object, provisions regarding transparency of management, accounting, reporting and audit, are not only desirable but indispensable, like in the case of co-operatives. In Germany, such organisations would be seen as economic associations without a view to profit for the organisation itself (Wirtschaftsverein).

The appropriate legal pattern for MSC can be either that of an association (e.g. in Belgium: Asbl) or of a co-operative (Italy, Canada, France).

Other special features of the MSC, like meeting conditions to qualify for participation in public promotion schemes or for participating in bidding for public tender are not matters of organisation law, but rather a matter of tax law and of regulations governing public support programs and should be better regulated there (Münkner, 2001b, 83 f).

### 3. Difference between MSC and conventional co-operative society

MSCs have *heterogeneous membership* unlike co-operatives, which usually have only one group of stakeholders. However, in savings and credit co-operatives there are also two groups of members with opposing interests: the savers/depositors, who expect high return on their savings and the borrowers, who are interested to pay the lowest possible interest on their loans. The same applies to building societies. In savings and credit co-operatives as well as in building societies, interest harmonisation between savers and borrowers is facilitated by the fact that in the course of time, most members turn from depositors to borrowers and vice versa.

In large and open (i.e. consumer based) societies, employees of the co-operative enterprise are often also members and users. This results in double representation of employees with membership in governing bodies as workers' representatives and members' representatives, giving employees/members a dominating role with the danger of turning the member-dominated co-operative enterprise into an employees' enterprise.

In MSCs members are not only of the typically co-operative users-owners-employees type, but also investor-members and promoting-members, contributing capital and knowledge, without the intention to use the services of the co-operative, representatives of enterprises, training centres, NGOs, public corporations and municipalities. Harmonisation of interests of these different stakeholders and resolution of conflicts between the different groups of stakeholders require special regulations, which allow for instance a reasonable and accepted distribution of voting rights, representation on the governing bodies and power.

Special problems may arise out of *public-private-partnership*.

When considering public authorities and private organisations as different and opposing structures, conflicts of interest appear to be unavoidable. However, in times of decentralisation, de-officialisation and growth of civil society, a trend towards partnership between citizens' organisations and the state can be observed and co-operation on equal terms based on agreements between citizens' organisations and the state have become possible, as a result of a new perception of state and community

and of a distribution of tasks between public and private organisations.

How new are MSCs?

The answer to this question depends on how two aspects are seen in the respective country.

The scope of solidarity and of the mandate of co-operatives:

- *narrow or wide range of solidarity*, i.e. solidarity only among members or solidarity beyond the membership group;
- *narrow or wide mandate of co-operatives*, promoting only or mainly the economic interests of their members or also the social and cultural interests of their members and of the community as a whole.

Perception of the relationship between state and co-operatives.

Where thinking is based on a clear separation of public and private law, with *public law* based on hierarchy and inequality of state and citizen being subject to the state and *private law* based on equality of persons, communities are part of public law and public administration and co-operatives with their principle of equality of rights (one member - one vote) belong without any doubt to the sphere of private law.

However, when seeing communities like co-operatives as *real socio-economic powers*, locally rooted and carrying out their tasks for the benefit of all citizens in the community (like Otto von Gierke in the 19<sup>th</sup> century), partnership of communities and co-operatives on the basis of equality becomes possible. In this case, for financial and other reasons, communities are looking for active participation of citizens and other stakeholders with their own resources in solving current problems of the community, which also effect the citizens. This is especially important in times where the state withdraws from economic and social tasks and leaves them to private enterprises or organised self-help of persons directly concerned. Seen from this perspective, there are no insurmountable obstacles in the way of partnership between communities (the state) and co-operatives.

Communities can resort to organised self-help in efforts to motivate citizens for active participation in solving community problems and to mobilise all locally available resources for local development, either:

- in form of establishing local development agencies or local coalitions for local development or
- in form of MSCs or community co-operatives.

## 4. Reasons for the development of MSC

Rapid economic, social and technological change has modified:

- economic structures;
- working conditions;
- social structures of family, school and community and the role of the state.

*New technologies devalue conventional knowledge and skills in agriculture, crafts, trade, industry and administration, calling for life-long learning* (Münkner, 1998, 2 f.).

Those not reacting to these challenges are left behind, loose out and join the masses of the unemployed and excluded. They are seen as useless and superfluous by those judging everything from a purely economic point of view.

When looking for ways and means to (re)integrate the excluded, NPOs not characterised by egoistic individualism but rather by solidarity could be seen as a solution, especially when in the long run solidarity is perceived as self-interested solidarity (strong individuals realising that they will depend on solidarity of others when they become weak), also referred to as *co-operative individualism* (Klemen et al., 2000).

Globalised economy has led to an almost unlimited mobility of capital, labour and knowledge. A revolution of knowledge, communication and transport technologies has initiated the transformation of industrial society into knowledge society, profoundly changing the lives of locally rooted people still working in industrial society.

Multinational firms and global players restructure their enterprises in search of best conditions for profit making, irrespective of negative side effects for others (workers, consumers, citizens), leaving the inhabitants of villages and small towns without employment and basic services (shops, banks, schools, public transport), turning workers settlements into settlements of unemployed.

These are the conditions in which MSCs become of interest, taking over the task of improving living conditions in such places, developing opportunities for reasonable occupation and employment for common benefit and aiming at integration of the excluded into social and economic life. In this context, a new concept of “work” becomes important, according

to which life-long employment in one firm and life-long work in one profession learned at the beginning of one's working-life, after leaving school, are the exception rather than the rule and part-time employment, changing employers and life-long learning in search of qualification for new fields of occupation and voluntary work during spare time become the rule.

Organisations (service providers) in which the interests of the users of services, the employees, trainees and apprentices of the enterprise offering such services, voluntary workers, local NGOs and communities can be combined are best suited to implement this new concept of work (Borzaga and Santuari, 1998).

In Canada in 1996, co-operative federations took the initiative to apply the co-operative concept to such circumstances. In discussions with government on "Economy and Work" a program for MSC was devised and a special legal framework for MSCs provided by amending the current legislation (Girard, 2001a; 2001b).

#### *Demographic changes*

Demographic development in European industrialised countries is characterised by low birth-rates and extended life-expectancy. Combined with medical progress, this leads to an aging society, turning the population pyramid into a population mushroom. This development is accompanied by growing individualism, loosening of family structures, single households of young professionals, abandoning traditional patterns of family care for the handicapped and for the elderly, relying more and more on the public social security system. However, this system comes to its limits when more and older citizens have to be supported by fewer active contributors (Münkner, 2001b, 12 f).

Women, especially single mothers, are faced with problems of combining family and work.

#### *Changing role of the state*

After decades of prosperity in an industrial society with full employment and sufficient funds to finance a comprehensive package of social security services, economic decline and reduced tax revenue coincides with increased claims of the aging society in terms of social and medical care. Such situations, where neither the state more the market offer suitable solutions, are the classical case in which solutions are sought by co-

operative activities of the people concerned. In Italy, already in article 45 of the constitution reference is made to the social role of co-operatives and to the obligation of the state to support and guide co-operatives in their work. There are special provisions, which declare collaboration between communities and co-operatives or NPOs in the field of social services to be desirable.

For instance article 44 of the community regulations of the Autonomous Region of Trentino Alto-Adige (Regional law n° 1 of January 1993) provides that:

3. "Communities may carry out their public services in the following forms:

(a) ...

(b) by using the services of third parties if this is justified for technical, economic or social reasons, provided that in case of equal conditions, co-operatives and associations, which have a legal mandate to represent the disabled, the handicapped and the disadvantaged, as well as organisations of volunteers and NPOs shall be preferred."

## 5. MSC as a model of organisation

In a very basic manner, MSCs can be defined as associations of natural and legal persons for the pursuit of common interests, irrespective of their legal form.

The *special objects* of MSCs are to improve the quality of life of the members, of beneficiaries and of the community as a whole. This goal is achieved by mobilising self-help, mutual aid, solidarity and external assistance for the promotion of self-help.

Depending on the emphasis placed on economic or social objectives, the MSC can be classified as predominantly social or predominantly economic. This classification influences the choice of the appropriate legal pattern:

- in case of predominantly social objectives, the adequate legal form is that of association;
- in case of predominantly economic objectives, the adequate legal form is that of co-operative society.

The importance of objectives can change over time so that a MSO may start as an association and later turn into a co-operative society.

During the first phase of development of a MSC, emphasis should be on:

- planning and interest representation;
- recruitment of members;
- creation of member-consciousness, wee-feeling and readiness to cooperate;
- acquisition of knowledge how to form and run a MSC, what are the rights and obligations of members.

All these are non-economic activities.

#### *Composition of membership*

The most obvious difference between MSCs and conventional co-operatives is its heterogeneous membership, essential for reaching its special objectives.

Potential members belong to the following groups:

- *the excluded* (i.e. people with low or no professional qualification, the unemployed, the disabled, the aged, former drug addicts, ex-convicts) as the direct beneficiaries of MSC;
- *volunteers*, e.g. parents and relatives of people needing care, persons in part-time employment, pensioners (“young” old);
- *employees* of the MSC and partner organisations;
- *corporate citizens*, e.g. representatives of enterprises, NGOs and other corporations;
- *representatives of public institutions* e.g. the community, local government, administrations of promotion programs.

Some or all of these groups can form or join MSCs. According to new French legislation (art. 19septies of the general co-operative law of 1947 with amendments up to 2001) at least members of three groups (the excluded, the employees of MSCs and representatives of the community) are needed for official recognition as MSC (*société coopérative d'intérêt collectif*, SCIC). According to Italian legislation at least 30 percent of members must belong to the category of the excluded (art. 2 n. 4, Regional Law n. 24, dated October 22, 1988, governing co-operatives for social solidarity).

#### *Harmonisation of interests*

One of the central problems of MSC is to focus the interests of the different members on the common objective and to avoid that one group of members dominates the organisation. The usually applied rule of “one

member - one vote” is not applicable, because it would give the most numerous group a dominating position. The solution is to give each category of members an equal number of votes, or votes in proportion to their group size, economic weight, contributions or geographical area, provided that there is a ceiling for the number of votes, which each category of members may have and a minimum number of votes securing that each group is in fact represented.

Categories of members may also consist of user-members, investor members, promoting members and corporate members.

Each category of members forms an electoral college and elects among themselves the delegates representing the interests of the category of members in the meeting of delegates of the MSC.

#### *Fundraising*

To secure a solid financial basis for MSC, neither the typical form of fundraising of associations (by annual membership dues), nor the typical form of financing co-operatives (by shares) are sufficient. The value of shares is usually determined by the financial capacity of the weakest members and therefore remains trivial, while attracting investor-members means to abandon the co-operative principle of identity of owners and users of the co-operative enterprise.

Furthermore, there is the question of distributing powers in proportion to financial contributions, which is ruled out by co-operative principles, thereby limiting the incentives for investors to gain access to power by contributing capital. The co-operative rules of limited return on capital and accumulation of surplus in indivisible reserves have the same effects on investors, but are seen as essential to qualify for participation in government support programs and to enjoy tax advantages.

#### *Qualification for public subsidies, tax advantages and public promotion programs*

To concentrate the limited public resources on promoting only genuine MSCs and to avoid sponsoring false self-help organisations (known in development aid as “self-help organisations for the acquisition of external aid”), criteria are set, which an organisation has to meet to be eligible for public support.

The German criteria are as follows (Münkner, 2001b, 84 f.):

- incorporation by registration under a law (as association, co-operative society or limited liability company);

- objects of general interest (in fields of activity listed in an annex to the law governing the official recognition as general interest organisation);
- services not only limited to the group of members but to an open group of beneficiaries;
- work at least in part with honorary office-bearers and employees with salaries not above the market rate;
- distribution constraint, i.e. no distribution of economic results or reserves among members and employees;
- being subject to internal and external audit with obligation to keep books of accounts and to issue annual reports.

Similar criteria apply in other countries.

An escape route from these strict requirements may be the establishment of daughter societies.

From this list of criteria for official recognition as organisations working in the interest of the public two reasons can be identified, why co-operatives are usually not recognised as public benefit organisations:

- their *member-orientation*, according to which transactions with non-members should be the exception rather than the rule;
- their rules regarding distribution of economic results among their members in terms of limited interest on share capital and patronage refund in proportion to business done with the co-operative enterprise, if any.

In MSCs both aspects could be regulated in their by-laws in such a way, that business with non-members could be allowed and distribution of surplus or of the reserves could be excluded.

#### *Governance and management*

In addition to the ordinary tasks of board members and managers of co-operatives, the leaders of MSCs have the tasks to keep the heterogeneous membership group together, to activate the members and to orient them towards the common objectives.

Special institutional safeguards are required to avoid that the social objectives are neglected or abandoned in the constant struggle to maintain economic viability and to cover cost and against the common trends of concentration, economisation and demutualization.

Apart from the co-operative-specific emphasis on member-relationship

management, special arrangements are needed for planning, reporting and auditing.

Advisory boards and subcommittees are needed to provide venues for meaningful active participation of users, beneficiaries and employees. A special governance structure could be introduced by setting up a management council and a social council within the co-operative society (as done in community co-operatives in the United Kingdom, where the law only provides for a board of directors or management committee and legally the social council is construed as a subcommittee of the board) (Münkner, 1995, 146).

Special precautions have to be taken to avoid that the MSC becomes dependent on powerful partners or turns into an agency of the public administration. In this regard, the co-operative principle of the ICA on autonomy and independence gives the necessary guidelines (4<sup>th</sup> ICA Co-operative Principle: Autonomy and Independence):

*Co-operatives are autonomous self-help organisations controlled by their members. If they enter into agreements with other organisations, including governments, or raise capital from external sources, they do so on terms that ensure democratic control by their members and maintain their co-operative autonomy.*

#### *Assessment of results*

To measure the success of MSC in achieving their objectives, it is not sufficient to use the instruments developed to audit investor-oriented enterprises, although institutional efficiency is also important for MSC. Like in all co-operatives, member-oriented effectiveness will have to be measured and for this the instruments of promotion plan and promotion report (Patera, 1981) could be used together with methods developed to investigate the degree of member satisfaction. In addition, development-oriented effectiveness also has to be determined and for this a new instrument developed by the French national federation of agricultural co-operatives could be used, the “bilan sociétal” (Confédération Française de la Coopération Agricole, 2001; Centre des Jeunes Dirigeants de l’Economie Sociale, 2002), which measures among other things the number of work places created, the attraction of the co-operative society as an employer, measures taken to enhance co-operative consciousness at all levels, measures taken by management to assess the quality of work, the reward system for good performance of employees and evaluation of

the effects of the co-operative society's work on the well-being of the community.

*Summary of this part*

As a form of organisation, MSCs are association-type groups of persons without a view to profit and insofar NPOs with total or limited distribution constraint.

They are characterised by their social and economic objectives, their holistic approach to development and their complex membership and decision-making structures. The disadvantage of increased cost of interest harmonisation and decision-making (democracy cost) is matched by a number of advantages:

- *better quality of services*, because the services correspond to the needs of the users and are controlled by them;
- *reduced transaction cost* due to trust in the system and in persons running the system, resulting from knowledge of local conditions and from integration of all stakeholders in planning, decision-making and control processes;
- *possibilities of mobilising human and financial resources* (voluntary work, honorary service of office-bearers, fundraising in form of donations, subsidies, tax advantages, etc., participation in public promotion programs) (Münkner, 2001a).

In an environment characterised by increasing mobility, growing individualism and progressive exclusion of disadvantaged from mainstream economic and social life, MSCs - because of their local roots in communities, towns and regions - are specially suited to establish reliable local coalitions for employment, local development programs and locally bound services close to members and users (services de proximité) on the basis of organised self-help, mutual aid and solidarity.

## **6. MSCs as a legal pattern**

During the past 20 years, the lawmakers have reacted to the growing interest in MSC, first in Italy (Regional Law n. 24 of 22 October, 1988, Autonomous Region of Trentino Alto-Adige governing co-operatives of social solidarity and national law n. 381 of 8 November, 1991), later in Canada (Co-operative Societies Act of Quebec of 5 June, 1997, Titel II 1,

articles 226.1 - 226.14 governing co-operatives of solidarity), in Portugal (Legislative decree n. 7 of 15 January 1998, governing co-operatives of social solidarity) and in France (law 2001-624 of July 2001, article 36-I amending the provisions of the general co-operative law of 1947 by adding articles 19quinquies - 19quindicies governing general interest co-operatives, sociétés coopératives d'intérêt collectif, SCIC).

New legislation for MSCs was the result of initiatives taken by representatives of co-operative federations and organisations of social economy, which were interested in facilitating the dissemination of the MSC model by giving it a special legal framework and thereby official recognition.

When analysing the new provisions for MSCs included in the co-operative legislation of Italy, Canada, Portugal and France, the following matters for special regulation can be identified:

- broadening the objects by admitting social objectives as the primary objective;
- broadening the criteria for membership by admitting not only user-members but also worker-members, voluntary members, non-using members, investor-members, promoting members and corporate members;
- allowing extension of services to non-members;
- making special provisions for the organisation of the heterogeneous membership group and the distribution of voting rights and representation on decision-making bodies;
- regulation of governance, management and control, taking the need for harmonisation of diverging interests and for safeguarding social orientation into consideration;
- regulation of eligibility of office-bearers and application of labour law to employed office-bearers;
- regulation of fundraising, accumulation of reserves and disposal of surplus according to the special co-operative perception of capital and profit;
- periodical audit of performance of management and the financial situation, including accountability for and control of success in achieving social objectives;
- regulations safeguarding independence of MSCs in case of participation of public institutions as partners.

Additional matters for regulation in tax law and programs for public promotion of MSCs, which would be best regulated outside the organisation law (because they are more frequently subject to changes than organisation law, which by nature needs to be stable) are:

- criteria for official recognition of co-operative societies including MSCs as public benefit organisations and conditions to be met, verification of compliance with these conditions regarding non-profit and public benefit orientation;
- rules regarding the participation in bidding for public tender and participation in support programs.

Arguments against special legal provisions for MSC derived from the legal framework applied in the United Kingdom, Belgium and Denmark. Whenever new models of organisations are developed in order to cope with new challenges, policy-makers, usually acting on the initiative of lobby groups, standardise such models according to criteria of best practice and lawmakers cast them into legal norms. This is how the Prussian co-operative law of 1867 was made, by using much of the by-laws of co-operatives established by Raiffeisen und Schulze-Delitzsch as direct models for legal provisions.

In the United Kingdom, Belgium and Denmark the lawmakers have reacted differently.

In the *United Kingdom* there is no special co-operative law (but efforts are under way to have such a law). Many co-operatives are registered under the Industrial and Provident Societies Act (IPSA) of 1862 with few amendments, governing bone fide (genuine) co-operatives as a type of economic association as well as associations for the benefit of the community (Bencom). Compliance with the criteria for registration as a bona fide co-operative society or as a “Bencom” are verified by a Registrar. A wide range of autonomy to make by-laws allows to accommodate MSCs in the legal framework offered by IPSA (Snaith, 2002).

In *Belgium*, a law on non-profit associations (associations sans but lucrative, asbl) of 1921 exists side by side with the coordinated laws governing business organisations in which co-operative law is contained (with amendments by a law of 20 July, 1991) and special provisions governing societies with social objectives, loi “de reparation” dated 4 April, 1995, introducing articles 164bis - 164quater governing societies with social

objectives (SFS) into the coordinated laws of business organisations, not as a new type of society but rather as a possibility to modify existing types of societies, allowing co-operatives to be officially recognised as NPOs.

*Denmark* is one of the typical examples of a country with a strong co-operative movement but without a special co-operative legislation, using the general law, freedom of association and co-operative principles. Even without a special legal framework, SMCs have developed. Partnership of communities and co-operatives is allowed under the Social Assistance Act of 1983.

The examples of the United Kingdom, Belgium and Denmark show that where there is a genuine need for this type of organisation, MSCs can develop without legislation specially designed for them.

However, governments can support the development of MSCs by providing a tailor-made legal framework, but also by removing administrative obstacles and by offering incentives. The case of Denmark shows that with independent citizens and a strong civil society, freedom of association and autonomy of self-regulation may be sufficient for this purpose.

What is most important is:

- a convincing and consistent concept;
- readiness of the persons concerned to co-operate, to practice self-help, mutual aid and solidarity.

A special legal framework can encourage the formation of MSCs and guide people so as to avoid making mistakes. Yet learning by making mistakes is a widely appreciated and effective method of learning.

## 7. Conclusions

From a German perspective, social goals and general interest orientation of co-operatives are difficult to implement in view of the clear contents of section 1 of the German Co-operative Societies Act, which contains the following definition:

*“Societies with a variable number of members, with the object of promoting their members’ income generating and economic activities by means of a jointly owned enterprise”...*

The world wide development of MSCs as a form of organisation and a legal pattern shows that conventional rules of cooperation along co-operative lines have to be reconsidered in the light of new economic, social and technological challenges, in order to maintain organised self-help as a relevant answer to current problems in times of rapid change.

New approaches developed in Belgium, Denmark, France, Portugal, the United Kingdom, Italy and Canada should cause others, e.g. the Germans, to take a fresh look at conventional patterns as far as:

- the self-help character of co-operative societies;
- the concept of work, occupation and leisure time;
- the role of the state and communities in local development;
- the responsibilities of citizens in a democratic and decentralised system of public administration, becoming increasingly dependent on private initiatives are concerned.

The SMC as a model of self-help organisation for the mobilisation of as many local forces as possible for local development is not a magic formula for the solution of the tremendous problems of mass unemployment, exclusion, undersupply of regions after withdrawal of the state and of commercial enterprises from small and mid-sized towns and of the deficiencies of social and medical services for an aging population.

While large bureaucracies such as the German labour administration obviously fail to find ways and means to deal with the problems of unemployment and exclusion, MSCs offer citizens a viable alternative to contribute their part to the resolution of local problems by organised cooperation and private initiative in communities willing to adopt innovative approaches.

Problems that will occur and will have to be solved when putting the MSC model into practice have to be openly discussed. It is known from experience that the establishment of co-operatives by persons who themselves depend on external aid and who - left on their own - are unable to help themselves, will not succeed.

Disadvantaged persons, excluded from working life, will not have chances to achieve reintegration into mainstream economic and social life, unless they work together with stronger persons, who are ready to contribute their strengths and their resources. Therefore, the heterogeneous membership group, typical for MSCs, is a precondition for success

of this model. A second success criterion is to develop a workable mechanism of interest harmonisation, in order to motivate the different partners and different contributors continuously to work together for the common goal.

It is known from development co-operation that mobilisation of self-help by external aid is a difficult task. The margin between over-promotion and under-promotion is extremely thin. Aided self-help will only succeed if certain conditions are met.

There has to be:

- a workable, consistent and convincing concept;
- informed and motivated promoters;
- self-interest of all persons concerned;
- mutual respect;
- investment in information and practice-oriented (functional) education;
- a central organisation providing the necessary services, guidance and support (Müller, 1976, 75f.).

Only when accepted in the MSC as full members with equal rights, can discouraged and frustrated persons having been excluded for some time turn into self-confident and motivated members contributing as much as they can to the improvement of their own conditions.

As shown by many examples, the community can be a crystallisation point for local development projects and local coalitions for employment. This is at the same time an old and new concept.

The concept of the co-operative society as a purely economic undertaking, which exclusively works for the benefit of its members, differs in many ways from the original co-operative idea. Co-operative goals are not exclusively of economic nature. Co-operatives aim at building people. Co-operative goals include improvement of living conditions of their members by education and training, by offering access to new skills and technologies, which make it more easy to survive in times of rapid change. Co-operatives are oriented towards member-promotion, however, by the open door principle they are ready to accept all, who are willing to take over the obligations of membership in order to qualify for membership rights and advantages.

According to their tradition, co-operative societies also show concern for

the community in which they operate. They and their members depend on the well-being of this community. This is a worldwide recognised co-operative principle.

Also legal persons like communities can take self-help action, when there is no other way to fulfil their tasks. If communities see themselves as social and economic organisations, which work for the benefit of all their inhabitants, SMCs offer an appropriate organisational and legal pattern for mobilising all local forces for long-term improvement of the living conditions of the citizens in the community. The inhabitants of the community have to realise that, in the long run, for their well-being they all depend on each other

SMCs can only succeed if - in the self-interest of each individual - egoistic individualism of the persons concerned turns into co-operative individualism (Klemen et al., 2000).

The development of MSCs does not depend essentially on an appropriate legal framework, but rather on a convincing concept, readiness of all concerned to co-operate and favourable framework conditions.

But an appropriate legal framework can help to trigger off development and to avoid mistakes. Neither the law of associations nor the law of business organisations meet the requirements of MSCs. The conventional co-operative laws as well need to be adjusted.

Co-operative federations have to decide whether to accept MSCs in their family and to support their development or whether to keep a distance from this at the same time old and new form of organised self-help.

If accepted, the MSC can develop into a future-oriented model and can open new fields of activities for co-operative self-help (Münkner, 1995, 133f.).

To conclude, four good reasons can be quoted, why services of public interest should be entrusted to MSCs or co-operatives for social solidarity:

- the members are responsible for their co-operative, they contribute the capital of their co-operative and are in charge of managing the co-operative. Those working in the co-operative are not simple employees but persons directly responsible for the continued existence of the co-operative society;
- the co-operative is part of the community. It does not consist of anonymous shareholders. The co-operative is, therefore, integrated

into the area in which the members live and work and thereby becomes an ideal partner for local organisations and for the inhabitants of the neighbourhood;

- the co-operative is not for sale. It guarantees continuity and responsibility. Shares are not transferable and the reserves are indivisible during the existence of the co-operative and even after its dissolution;
- the co-operative is subject to the same control as other enterprises and in addition to audit by a co-operative federation or by the regional administration (Infocoop, 2002, 4).

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## Appendix 1: Excerpts of texts of relevant laws

*Italy: Law on Co-operatives for Social Solidarity, Regional Law N. 24 of October 1988, Autonomous Region Trentino-Southern Tyrol*

### *Art. 1 - Goals*

Integrated production and workers' co-operatives as well as co-operatives providing social services are officially recognized and form a special category of "social co-operatives", which are at the same time production and workers' co-operatives.

### *Art. 2 - Creation of the category of social co-operatives*

(4) "Social co-operatives", which are simultaneously production and workers' co-operatives may admit as members a number of persons with special technical and administrative skills, which may not exceed 70 % of the total number of members.

### *Art. 3 - Co-operatives for social solidarity*

(1) Co-operatives for social solidarity have as their object the promotion of persons and the integration of disadvantaged persons, members as well as non-members, by efficient use of available human and material resources.

(2) Disadvantaged persons are those who for objective or subjective reasons are unable to achieve their integration into society, without appropriate physical, psychological, social (family), cultural, professional and economic help, and who due to their age and in general require social support and care.

### *Art. 4 - Membership in co-operatives for social solidarity*

1. Members of co-operatives for social solidarity are categorized as follows:

- (a) Members who contribute their labour voluntarily by their own decision and not because of specific legal obligations, free of charge and without a direct view to profit.
- (b) Members who work against payment of wages.

2. Also persons defined in the foregoing article (art. 3 (2)) and who are interested in the work of the co-operative society can become members as beneficiaries.

### *Art. 5 - Obligations and restrictions of co-operatives for social solidarity*

Obligations and restrictions of co-operatives for social solidarity include:

- (1) Distribution of profit among members for whatever reason is prohibited.
- (2) All reserves are indivisible among members. In case of withdrawal, expulsion or death of a member, the refund of shares may not exceed the amount that was actually contributed.
- (3) In case of dissolution of a co-operative, the entire assets after deduction of the paid-up share capital has to be used for purposes of general interest - preferably for other co-operatives for social solidarity.

(This is followed by rules regarding settlement of disputes)

- (4) Any amendment of the bylaws, which aims at abandoning the status of a co-operative for social solidarity, is prohibited.

(This is followed by regulations regarding sanctions for non-compliance with the provisions up to ex-officio dissolution).

*Art. 6 - Integrated producer and workers' co-operatives and relevant obligations and prohibitions*

1. The goal of these co-operatives is the sustainable integration of physically, psychologically or mentally disabled persons and other persons defined in article 3 into working life. At least 30 % of the wage earning members participating in these co-operatives must suffer from permanent reduction of their own capability to work, which has to amount to at least two thirds of normal capacity.

The following subsections of this article deal with further details and sanctions in case of non-compliance.

*Art. 7 - Co-operatives for social services*

Art. 7 deals with co-operatives for social solidarity and their obligation to collaborate with public corporations.

1. The category co-operatives for social solidarity covers all co-operatives, which have as their principal object to render social services, which have to be directed towards persons defined in art. 3 (2) of this law.
2. The members of co-operatives for social solidarity must dispose technical know how required for carrying out the activity stated in the by-laws of the co-operative.
3. Readiness to collaborate with the public corporation responsible for offering the respective services has to be indicated in the by-laws.
4. When entering the co-operative in the regional co-operative register, it is verified whether the requirements laid down in the forgoing subsection are met.

*Art. 8 - Audit of co-operatives governed by this law*

1. With regard to co-operatives governed by this law, the board of directors has to prepare an annual report, containing detailed description of achievement of the co-operative's goals and the social activities actually performed.
2. Within the delay provided for in the law regarding the deposit of documents at the register of societies, the co-operative has to submit the report referred to in the foregoing subsection together with a copy of the minutes of the general meeting and the annual report of the board of directors and of the auditors.
3. The report according to subsection 1 of this article, which is a supplement of the annual report of the co-operative, has to be audited in accordance with article 16 of the regional law n. 7 of 29 January 1954, by the auditor.

This is followed by provisions governing affiliation to a co-operative federation (art. 9), the applicability of the provisions of tax law, social law and labour law (art. 10) and transitory provisions (art. 11).

The regional law does not contain special provisions regarding the voting rights of

members, which in case of MSC are important for the harmonisation of interests between the different groups of members. According to art. 5 of the draft model by-laws it is suggested to apply the general principle of “one member - one vote”

In the model by-laws, the strict gratuity of services of office-bearers serving the co-operative is softened just as well as the categorical distribution constraint.

Art. 19 (2) of the model by-laws for co-operatives for social solidarity contains the following.

Office-bearers as such have no right to compensation. They can only claim refund of expenses incurred when executing certain activities on the account of the co-operative.

The board of directors can decide with the express approval of the supervisory committee to pay a remuneration related to work done, if the activity was expressly authorised and this restricted remuneration was paid for this activity.

As to the distribution of profit (surplus) among members, art. 10 (1) (a) of the model by-laws provides that “... shares may be charged or transferred to other members with effect on the co-operative society. No dividend on paid-up shares may be paid in excess of the dividend prescribed in special laws governing mutuality as the maximum rate and in any case not exceeding the interests paid on co-operative loans according to article 2 (6) of the model by-laws.”

*National Law 1991, law n. 381 of 8 November, 1991*

In the meantime, the provisions governing MSC have been developed further in the national law on co-operative societies.

According to Maiello (1998, 365 and 366), the legal definition in art. 1 of this law was broadened as compared to the conventional interpretation of the mutuality principle, typical for (Italian) co-operatives. In case of co-operatives for social solidarity, the entrepreneurial activity is directed towards meeting goals of solidarity, i.e. not towards meeting the needs of specific groups and categories, but of general interest for society as a whole.

Social co-operatives are created by the initiative of self-organised groups of citizens, who carry out social activities designed to meet the needs of the local community in a new participatory manner.

They try to revive the value of solidarity within co-operatives and to abandon the trends of economisation and approximation to the company model (ibid., 370). According to the self-government model represented by the Lega delle Cooperative e Mutue, social co-operatives are perceived as strong, self-governed social enterprises with professional management offering a broad spectrum of services (ibid., 373).

Co-operative societies have as their object to pursue the general interests of society in the promotion of persons and in social integration of citizens by means of:

- (a) social, health-care and educational services,
- (b) execution of different activities and provision of agricultural, industrial, economic and other services, which aim at integrating disadvantaged persons into working life (Maiello, 1998, 364).

With regard to membership, there are limitations and expansions.

Four categories of members are mentioned:

- *Active members*, i.e. members contributing labour and being warded for their work or receiving other economic advantages (e.g. boarding and lodging).
- *User-members*, i.e. disadvantaged persons and their families.
- *Voluntary members*.
- *Corporate members* (ibid, 364).

The provision that the number of voluntary members may not exceed 50 % of the total number of members is perceived by co-operators as an unnecessary restriction (ibid, 367). Furthermore, the restriction of activities to the integration of clearly disadvantaged persons with “certified” disabilities, is seen as an impediment for initiatives in favour of a broader spectrum of citizens, who also need well-being and social security.

*Canada, Co-operative Societies Act of Quebec of 5 June, 1997, Title II 1, articles 226.1 - 226.14 governing co-operatives of solidarity*

*Art. 226.1*

A co-operative for solidarity is a co-operative, which simultaneously consists of members who are users of the services offered by the co-operative and members working in the co-operative.

Furthermore, each person or organisation having an economic or social interest in achieving the goals of the co-operative can also be a member. These members are referred to in the following as promoting members.

*Art. 226.2*

The firm-name of a co-operative for solidarity has to contain the words co-operative for solidarity.

Other persons may not use this denomination in their firm-name or otherwise.

*Art. 226.3*

Each person or co-operative of the type referred to in art. 226.1 subsection 2, which has expressed its interest in achieving the objects of the co-operative by an application for membership to the pro-tem manager/secretary before the inaugural meeting, shall be invited to attend the inaugural meeting.

*Art. 226.4*

The minimum share contribution, which a member has to sign, can vary depending on whether a member belongs to the category of user-members, worker-members or promoting members.

*Art. 226.5*

The board of directors may, if the by-laws permit, issue preferred shares to promoting members.

*Art. 226.6*

User-members, worker-members and promoting members form membership groups in the meaning of article 83 and every group has the right to elect at least one board member.

The by-laws of the co-operative may provide that additional board members are elected by the general meeting.

The number of board members elected by promoting members may not exceed one third of the total number of board members.

*Art. 226.7*

The annual report of the co-operative has to indicate the number of members who are user-members, worker-members and promoting members, if any.

*Art. 226.8*

Surplus in terms of patronage refund to members and where applicable to auxiliary members shall be distributed as follows.

To user-members in proportion to the turnover with the co-operative in the preceding year.

To worker-members in proportion to work done for the co-operative in the course of the preceding year.

The volume of work done by a worker-member shall be calculated on the basis of wages received, working hours contributed or any other criterion laid down in the by-laws.

Promoting members do not receive any remuneration.

*Art. 226.9*

The minister may order any co-operative ex-officio to amend its by-laws, if the co-operative has no user-members or worker-members among its members, so as to cease to come under the provisions of this part of the law.

If the co-operative fails to comply with such order within 60 days from signing the order, the minister may amend the by-laws ex-officio.

*Art. 226.10*

In case of ex-officio amendment of the by-laws of the co-operative, the minister shall issue a certificate in three authentic copies, confirming the amendment of the by-laws.

One authentic copy of this certificate is added to the files in the ministry, one copy is sent to the co-operative. The third authentic copy is forwarded to the supervisory authority, which shall deposit it at the Co-operative Register.

The amendment of the by-laws comes into force at the date stated on the certificate.

*Art. 226.11*

When the amendment of the by-laws made by the co-operative or by the minister comes into force, promoting members lose their status as members of the co-operative.

*Art. 226.12*

If a co-operative has neither user-members nor worker-members among its members, the minister may order the dissolution and liquidation of the co-operative.

For this purpose, one member of the board of directors or two members of the co-operative can convene a special general meeting.

The minister shall forward a copy of this order to the supervisory authority, which shall be deposited at the Co-operative Register.

*Art. 226.13*

If the co-operative fails to comply with the order of the minister within 60 days from the date of its signature, the minister may order the dissolution and liquidation of the co-operative ex-officio.

The dissolution order shall be forwarded to the supervisory authority and shall be deposited at the Co-operative Register.

The order comes into force at the date of its deposit at the Co-operative Register.

*Art. 226.14*

The provisions of this title are replacing those in title II of this law.

*Portugal: Legislative decree n. 7/1998 of 15 January 1998 governing co-operatives of social solidarity*

*Art. 1 - Scope*

Co-operatives for social solidarity and their higher level organisations are governed by this legislative decree and where no provisions are contained, by the Co-operative Code (of 1996).

*Art. 2 - Concept*

(1) Co-operatives for social solidarity are those which by means of co-operation and self-help of their members, subject to co-operative principles and without a view to profit, work for the satisfaction of the common social needs and for the promotion and integration mainly of the following sectors:

- (a) Help for disadvantaged groups, in particular youths, the handicapped and the aged.
- (b) Help for disadvantaged families and communities, with the aim of improving their living conditions and their socio-economic integration.
- (c) Help for Portuguese citizens living outside of Portugal during their stay abroad and after returning to Portugal, if they are in economic difficulties.
- (d) Help for groups of persons suffering from disease, old age and serious economic hardship.
- (e) Promotion of the integration of socially excluded persons by offering access to education and training.

(2) Beyond the enumeration contained in the foregoing subsection, co-operatives for social solidarity can undertake other activities of similar nature and, within the limits

defined by the Co-operative Code, offer services to third parties.

(3) Using the co-operative form does not exempt from applying for permissions, licences and other legally required formalities, while the authorities in charge of granting such permissions have to respect the special nature and social functions of the co-operatives.

*Art. 3 - Multipurpose societies*

Co-operative societies having activities in more than one of the fields mentioned in the foregoing article may work in sections.

*Art. 4 - Effective members*

Effective members are users of the co-operative services for themselves or for their family or workers, exercising their professional activity on a voluntary basis in the co-operative society.

*Art. 5 - Honorary members*

(1) Honorary members are those persons contributing goods and services and voluntary work.

(2) Honorary members are admitted by the general meeting on proposal of the board of directors. Those admitted have the obligation to contribute goods and services towards reaching the goals of the co-operative society.

(3) Honorary members have rights of access to information to the same extent as effective members. However, they may not elect or be elected to serve as office-bearers but may attend general meetings without voting rights.

*Art. 6 - General council*

(1) Apart from the board of directors, the by-laws may provide for a general council, in which all honorary members and the office-bearers of the society participate.

(2) The general council is a consultative body with powers to move motions and to make proposals to be submitted to the general meeting.

(3) The general council may elect a representative among the honorary members, who has the right to attend the meetings of the supervisory committee, with access to all information which are given to the members of the supervisory committee.

*Art. 7 - Distribution of surplus*

In co-operatives of social solidarity all surplus has to be allocated to the reserves.

*Art. 8 - Use of the liquidated assets in case of dissolution*

Notwithstanding the provisions of article 79 of the Co-operative Code, if a co-operative in liquidation is not succeeded by another co-operative of the same type, the liquidated assets shall be transferred to another co-operative society for social solidarity, preferably in the same municipality, to be decided by the federation.

*Art. 9 - Official recognition and registration*

(1) The official recognition and registration referred to in article 87 n. 2 of the Co-operative Code shall in addition to the certification of the co-operative nature of the newly formed organisation, also certify the object of social solidarity.

(2) Of the Co-operative Code of 1996, ley 51/1996 of 7 September 1996, recognition and registration is done by the Instituto Antonio Sérgio del Sector Cooperativo IN-SCOOP with yearly renewal.

(2) Special technical and economic assistance by public authorities for activities in the fields of integration and social security depends on the official recognition referred to in the foregoing subsection.

*Art. 10 - Application of these norms to existing co-operative societies*

The present norms are also applicable to co-operatives for special education of the CERCIS type - co-operatives for education and rehabilitation of handicapped young persons.

*France, General law governing co-operatives of 1947 with amendments up until 2001*

*Art. 1*

Co-operatives are societies the essential objects of which are:

1. reduction of prices of production or sale of certain goods and services for the benefit of their members in such a way that the co-operative takes over the functions of entrepreneur or intermediary, the profits of whom would otherwise increase prices;
2. improvement of the quality of products delivered to or produced by the members and sold to consumers;
3. in general for contributing to the satisfaction of needs of their members, to the promotion of their social and economic activities and to their education.

Co-operatives operate in all spheres of human endeavour.

*Art. 3bis*

Subject to conditions to be determined in the by-laws, co-operatives may admit natural or legal persons as members, who do not make use of the services or employment opportunities of the co-operative, but contribute capital to the achievement of the objects of the co-operative.

These investor-members may under no circumstances have more than 35 % of the total of votes. The by-laws may provide that such promotion members or certain categories of members as a group may have a number of votes in proportion to the capital contributed by them, which they can subdivide among them in proportion to their capital contributions.

If co-operatives are among these members, the abovementioned limit may be increased to 49 % of the total number of votes, however, the votes of other promoting members may not exceed 35 % of the total votes.

If the percentage of capital contributed by promoting members exceeds 35 or 49 %, as the case may be, the voting rights of these members are reduced in proportion. The

maximum quota of capital contributions by promoting members is fixed in the by-laws.

*Art. 11bis*

The by-laws may provide for non-voting preferred shares, to be obtained by promoting members referred to in article 3bis or by third parties. The by-laws determine the financial advantages granted for these shares.

If the preferred reward cannot be paid out in full during three consecutive years, the holders of these shares are given votes within the limits fixed by article 3bis.

A special meeting for holders of non-voting shares will be convened according to rules to be laid down in regulations.

Every holder of non-voting shares is entitled to participate in this special meeting. Provisions in the by-laws to the contrary are void.

The special meeting may issue a statement before each decision of the (ordinary) general meeting. The statements are made by the majority of votes of shareholders present or represented. The statements are forwarded to the co-operative. They are made known in each (ordinary) general meeting and entered into the minutes.

The special meeting may appoint one or - if the by-laws so provide - more than one representative(s), the task of whom is to represent the holders of non-voting shares in the (ordinary) general meeting and to present the statements, if any, before a decision can be taken. These statements are entered in the minutes.

A decision modifying the rights of holders of non-voting preferred shares only becomes valid and legally binding, after approval of two thirds of votes cast by the shareholders present or represented in the special meeting.

In 2001, art. 36-1 governing MSC was introduced into the general co-operative law of 1947 of France by law n. 2001-624 of 27 July 2001, as

*Title IIter governing co-operatives for general interest, (sociétés cooperatives d'intérêt collectif, SCIC).*

*Art. 19quinquies – Legal definition of SCIC*

Co-operatives for general interest are companies with variable capital, which operate under commercial law subject to the provisions of this law.

They have as their object to produce goods and services in the general interest and of social utility.

*Art. 19sexies*

Third parties (non-members) may make use of these goods and services of SCIC.

*Art. 19septies*

SCIC may have the following categories of members:

1. workers of the co-operative;
2. persons normally using the goods and services of the SCIC free of charge or against pay;
3. every natural person desirous to participate voluntarily in the activities of the co-operative;
4. public corporations and their federations;
5. every natural or legal person contributing in one way or another to the activities of the co-operative.

A SCIC must have members belonging at least to three of these afore mentioned categories and in any case members belonging to the categories 1 and 2. The conditions of acquisition of membership and the conditions under which workers may be asked to apply for membership are determined in the by-laws. Public corporations and their federations may together not hold more than 20 % of the capital of an SCIC.

*Art. 19octies*

Each member has one vote in the general meeting or in the electoral colleges to which it belongs.

The by-laws may provide that the members are subdivided into three or more electoral colleges according to their participation in the co-operative or to their contribution to its continued existence.

Each electoral college has an equal number of votes in the general meeting unless the by-laws provide otherwise. In such case, the by-laws have to fix the distribution of members into electoral colleges and the number of their representatives in the general meeting in proportion to the number of members or the nature of the contribution of each member to the co-operative, provided however, that no electoral college may dispose of more than 50 % of the total of votes or of less than 10 % of the votes and provided further, that votes may not be allotted on proportion to capital contributions.

If the votes of one electoral college exceed 50 % of the total of votes or is reduced to less than 10 % of the total of votes, the number of votes shall be reduced or increased in proportion, as the case may be.

*Art. 19nonies*

Annual allocations to voluntary and legal reserves are fixed in the by-laws. These may not be less than 50 % of the available sum after allocation to the statutory reserves according to article 16<sup>1</sup>.

The total amount of interest on shares may not exceed the sum provided for by subsection 1 of this article, remaining after allocations to the voluntary and legal reserves.

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<sup>1</sup> *Article 16* (introduced in 1987, amended in 1992):

Within the limits and conditions provided for under the law and the by-laws and after allocation to the legal reserves, as well as the distributions according to articles 11bis, 14, 15, 18 and 19decies, the contributions are allocated to the reserves or given as grants either to other co-operatives, or used for co-operative or branch-specific purposes.

The general meeting may be empowered under the by-laws to convert part of the reserves into share capital with the effect of increasing the value of the shares or issuing bonus shares.

The first conversion (of reserves into share capital) may not exceed 50 % of the available resources, as they existed at the end of the financial year before convocation of a special general meeting, which has to decide on this conversion. Any further conversions can only affect one half of the increase of the above mentioned reserves, created since the preceding conversion.

When calculating the interest on shares according to article 11<sup>2</sup> and 11bis, subventions, contributions and other financial means paid by public corporations, their federations and association to the co-operative shall not be taken into account. Article 15<sup>3</sup> as well as subsections 3 and 4 article 18<sup>4</sup> do not apply.

*Art. 19duodecies*

The financial situation and the management of SCIC are subject to auditing in regular intervals. The conditions are governed by decree.

*Art. 19terdecies*

SCIC are officially recognised by the public authorities. The conditions are regulated by decree of the State Council.

*Art. 19quaterdecies*

Any decision of a society irrespective of its legal form to amend its by-laws so as to comply with the provisions of this law does not lead to the creation of a new legal person.

*Art. 19quindicies*

The SCIC can make contracts and receive licenses and permissions according to the following provisions: article L. 129-1, I and II of article L. 322-4-16, L-322-416-3 and L. 322-3-18 Labour Code, last paragraph of article L-121-2, article L-222-3, L-344-2 to

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<sup>2</sup> *Article 11:* Co-operative shares issued in the name of their holder. Their transfer is subject to the approval of the general meeting or the board of directors or management according to conditions fixed in the by-laws.

The by-laws may allow to issue shares which give the holder special advantages (preferred shares). The advantages offered to holders of these shares have to be laid down in the by-laws in accordance with co-operative principles.

Such shares can only be signed by members. They are freely transferable among members.

<sup>3</sup> *Article 15:* There may be no distribution of interest on shares among members, provided that distribution can be made in proportion to turnover with the members. Surplus resulting from transactions with third parties may not be included in such distribution.

Directors or managers may only be rewarded in proportion to turnover or surplus earned, if this kind of reward is provided for in the by-laws, which - in such case - shall prescribe that the board of directors has to fix a ceiling for annual rewards, not exceeding 5 years.

<sup>4</sup> *Article 18:* A member who withdraws from membership or is expelled, when claiming repayment of his/her shares, is entitled only to the par-value.

If the by-laws do not provide for the application of article 16, they may prescribe that a member after more than five years of membership shall have the right, in proportion to his/her capital contribution, and within the limits regarding the increase of annuities to a portion of special reserves created for this purpose.

The refund of shares to past members and the participation in the above mentioned reserves is reduced in proportion to participation of the member in losses shown in the balance sheet. However, the by-laws may provide that before such reduction, the losses incurred have to be covered first by the above mentioned reserves and only second by reserves formed under the by-laws.

L. 344-6, L. 345-1 to L. 345-3 and N. 2 of article L. 313-4 Social and Family Code, article L. 851-1 Social Insurance Code and article 140 of law n. 98-657 of 29 July 1998 to fight exclusion, may participate in bidding for public tender and in public support programs, as far as the objects laid down in the by-laws of the SCIC meet the legal requirements.

The contracts, licenses and permissions referred to in the foregoing subsection as well as direct and indirect financial support and advantages to which they entitle, are granted to SCIC under the reservation that the objects laid down in the by-laws, the rules of organisation and the methods of operation according to the laws and regulations are complied with.



## **5. The European co-operative society: a new step in European company law**

*by Enzo Pezzini\**

### **1. Introduction**

On July 22, 2003, the statute of the European co-operative society (SCE) was adopted by the Council of the Ministers of the European Union.

The adoption has been incontestably a success for the co-operative movement, which sees in this new legislation the completion of a course that lasted for 20 years of discussions with the European Commission and of negotiations within the co-operative movement.

This article will give a short and necessary background to the statute while discounting discussion of it in a strictly juridical matter. In so doing, this article will offer a more political reading of the course undertaken to reach the point of the statute's approval, the role played by the European co-operative movement, the perspectives for the statute's use and its juridical and political impact.

### **2. A brief historical framework**

The idea of a business company of a European type arose in the first years following the setting up of the European Community. In 1966, the Commission transmitted a memorandum to the Council of the Ministers underlining the importance and utility of such an idea.

Within the co-operative movement itself, the conviction that the creation of a common and juridical European tool as a means to recognize the importance of cooperation in terms of creation of occupation, of economic activity and of the role in the territorial development began to gain momentum. Furthermore, this tool had to facilitate the constitution of economic unities of suitable dimensions to the new enlarged market created.

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\* Confcooperative - Brussels Office.

In 1970, the European committee of the agricultural co-operatives (Cogeca), elaborated a project proposal of a statute of SCE which is the forerunner of the current statute. The interesting aspect of the proposal is the fact that it referred not only to agricultural co-operatives but to all co-operative forms. As early as that time, it was understood that to succeed at European level, it is necessary to overcome distinctions among sectors and professions.

From 1988, the co-ordinating committee of European co-operative organisations, the CCACE, set up a working group for the elaboration of a project of statute. Such group was coordinated by Bernard Piot<sup>1</sup>.

On the occasion of the first European conference on the social economy, held in Paris in November 1989, the European co-operative statute was created from among the common requests of the European co-operative movement (and more largely of the movement of social economy).

To be able to have at least some slight probability of success of the statute, it was necessary to find allies in the European institutions. The European Parliament and the European Economic and Social Committee have had a leading role in this operation, but it is with the creation of the Social Economy Unity in 1990 in the then DG XXIII of the European Commission (directed by Paul Ramadier<sup>2</sup>) and the constitution of the inter-group Social Economy at the European Parliament<sup>3</sup> (chaired and animated by Marie Claude Vayssade<sup>4</sup>) that a decisive step had been taken.

Thanks to the work of these various interlocutors, in 1992 the Commission presented three draft Regulations related to the statutes of co-operative, of mutual organisation and of association linked to three directives on the involvement of employees<sup>5</sup>.

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<sup>1</sup> Bernard Piot, honorary General Director of *Crédit Coopératif*, French Bank Group specialized in the financing of co-operatives and organisation of social economy. He is President of the Juridical Committee of the *Groupement National de la Coopération*, an association that represents all the co-operative organisations in France.

<sup>2</sup> Paul Ramadier has directed the Social Economy Unity at DG XXIII from its institution in 1989 to 1996.

<sup>3</sup> Members of the European Parliament can group themselves in parliamentary inter-groups on matters of common interest, in addition to political parties and Parliamentary committees.

<sup>4</sup> Marie Claude Vayssade, French Member of the European Parliament and of the socialist party, was President of the parliamentary inter-group on social economy during the legislature 1989-1994.

<sup>5</sup> Initial proposal OJ C 99 of 21.4.1992.

These proposals had been modified in 1993 in the light of the reports sent forth by the Parliament and by the Economic and Social Committee<sup>6</sup>. The document then entered the phase of the decision-making process which lasted more than 10 years.

The works at the Council were practically interrupted from 1995 and resumed during the Nice summit of December 2000 when an unexpected and pleasant surprise came - a recommencement and an acceleration of the initiative on the regulation of the Statute of the European Company (SE).

An agreement on the directive had been reached by the heads of State and government, in particular on the issues related to the involvement of employees attached to the project of Regulation of Statute of the European Company.

This political breakthrough, which was awaited for years, also paved the way for the Regulation on the European Co-operative Society.

### **3. The role of the co-operative movement**

The whole co-operative movement, represented in the CCACE, has carried out an important work of internal mutual dialogue as well as of negotiation and co-operation with the European Commission<sup>7</sup>. On 17 January 2001, the European Commission mandated the CCACE to decide on how to proceed in respect to the proposal that had been blocked for years. The question that must first be answered was whether it was opportune to proceed with the same texts or begin their re-examination. These texts were the fruit of hard-earned compromises and of a conscious and responsible approach of the European co-operative movement recognizing that it is in their interest that the statute be quickly approved rather than setting further legitimate claims which may be required by the evolution of the co-operative law in various countries or

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<sup>6</sup> Modified proposals OJ C 236 of 31.8.1993.

<sup>7</sup> The new organization chart of the European Commission resulted from the internal reform carried out by the current President, Mr. Romano Prodi, has reduced the number of Directorates General (DG) of the Commission. The Unit "Social Economy" - which inside the DG XXIII, Small and Medium Enterprises, Trade, Tourism and Social Economy which for ten years was the reference of the co-operative movement - has been dissolved. The co-operative dossiers have been allocated to the new Unit "Crafts, small business, co-operatives and mutuals" within the new DG Enterprise and under the direction of Mr. Franco Ianniello. Mr. William Neale was the officer directly responsible for co-operative matters.

sector specifications. Three subsequent presidencies of the European Union, Swedish, Belgian and Spanish were involved in the decision-making process of the draft Regulation. The revision of the text was neither simple nor swift. It was instead a deep analysis of article by article, and based on two factors: firstly, not all the Member States were part of the Union at the time the regulation was drafted; secondly, the quick approval of the Regulation 2157/2001 on the European Company on the basis of which the draft Regulation on the SCE had to be adapted.

Each presidency contributed in accordance to their respective competence in order to advance the work that made possible the final approval of the Regulation reached during the Council July, 22, 2003 (under Italian presidency).

Some juridical/political problems slowed down the process of decision:

1. the problem related to the directive on the involvement of employees, which was opposed by certain countries, particularly the United Kingdom. On the other hand, Germany considered the text insufficient as compared to the principles of co-management applied in the country and which have an almost constitutional value;
2. the problem arising from the “strategy of adoption of the statutes”. A principal strategic question herein presented concerns the fact of whether the three texts of social economy (statute of co-operative, statute of mutual organisation and statute of association) had to be adopted all together or not? After a certain period of parallel progress, it was realistically recognized that is more useful to go ahead faster with the more advanced and elaborated text on co-operatives;
3. the problem related to the juridical basis of (the article of the EC Treaty on which the Regulation is founded), which had yet to be solved. The Commission and the Parliament proposed, as a basis, articles 95 and 44 which require the adoption by qualified majority and Parliament co-decision, while the Council preferred to use art. 308 which requires the adoption by unanimity and simple consultation of the Parliament.

The choice of the second juridical basis strengthened the powers of the Council and therefore of the States. The Parliament reacted to this problem appealing to the European Court of Justice. Pending appeal the norm was not suspended.

4. Another reason for delay in the decision process may be also due to the fact that priority was given to the debate on the statute of the European Company which was adopted in 2001 with EC Regulation n. 2157<sup>8</sup>.

#### **4. The juridical form of the statute of the European co-operative**

The Statute consists in a regulation<sup>9</sup>, that defines in detail the rules of constitution and management of the SCE, and in a directive<sup>10</sup> that outlines the formalities with which the employees have to participate in the most important decisions of the enterprise through information, consultation and participation to the bodies.

#### **5. Objective of the SCE**

The objective of the Regulation is to provide a tool to co-operatives for facilitating their cross-border and trans-national activities.

Differently from the previous situation, the statute of European co-operative society gives any co-operative established in any Member State the possibility to work throughout all the 25 countries of the European Union, previously hampered by legal and administrative difficulties.

In this way, the co-operatives have the same possibilities as any European company.

On the objective of the SCE, it is interesting to read in the text of the Regulation the second “considering” which states that: “The completion of the internal market and the improvement it brings about in the economic and social situation throughout the Community mean not only that barriers to trade should be removed, but also that the structures of production should be adapted to the Community dimension. For that purpose it is essential that companies of all types the business of which is

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<sup>8</sup> OJ L 294 of 10.11.2001.

<sup>9</sup> Under European Law, a regulation has a general scope, is mandatory in all its elements and is directly applicable in every Member State.

<sup>10</sup> Under European Law, the directive is binding for Member States in so far as it concerns the result to be obtained, while it remains the competence of the national bodies to determine the form and the means to transpose it in the national legal system.

not limited to satisfying purely local needs should be able to plan and carry out the reorganisation of their business on a Community scale”.

In addition, the sixth “considering” states that: “The Community, anxious to ensure equal terms of competition and to contribute to its economic development, should provide co-operatives, which are a form of organisation generally recognised in all Member States, with adequate legal instruments capable of facilitating the development of their cross-border activities...”<sup>11</sup>.

In view of the aforementioned objectives, it can be concluded that there is a recognition at the European level of the freedom of enterprise, of the plurality of the entrepreneurial initiatives, under forms which can be different from those of traditional capital created companies.

## 6. The principal characteristics of the SCE

The SCE’s main aim is that of meeting the needs of and/or promoting the economic and social activities of its members (physical persons or legal entities), particularly through the conclusion of agreements among themselves for the supply of goods or services respecting the following principles:

- the activities of the SCE must pursue the mutual advantage of the members so that every one of them is able to take advantage of such activities on the basis of their involvement;
- there must be a correspondence between members and client/employee/supplier (according to the traditional principle of doubling quality); except as otherwise provided by a different statutory disposition. The SCE cannot admit third persons who are not partners to benefit from its activities or to participate in the realization of its own operations;
- the control of SCE must be fairly distributed among the members (on the principle of “one vote per head”), with the exception of the provision of the vote weighted in accordance with the respective members’ contribution;
- the interest on the capital invested in the societies has to be limited;

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<sup>11</sup> OJ L 207 18.8.2003.

- the final profits must be distributed according to the activities carried out by the SCE (“dividend on purchase”), or used to satisfy the needs of the members;
- there cannot be unjustified denial to the admission of new members (in respect of the open door principle);
- the net patrimony resulting from liquidation must only go to entities with altruistic goals or to other co-operatives having the same goals or having a general interest objective.

These principles are the same as those safeguarded by the International Co-operative Alliance and recognized and confirmed by international bodies (such as in the ILO recommendation n. 193 of June 2002).

In the constitution of an SCE, there are significant features in the process and requirements. Thus, an SCE can be constituted:

- by at least five individual persons, resident in at least two Member States, or by at least two juridical entities subject to the jurisdiction of at least two different Member States, or by the combination of individual and juridical persons;
- by merging two or more existing co-operatives from different Member States;
- by the transformation of an existing co-operative that for at least two years has had a branch in another Member State.

The initial capital of the SCE has to be of at least 30.000 euro. This initial capital can be variable because can be increased or diminished according to new subscription of capital share by new members or because of partial or total reimbursements of previous subscriptions. These variations do not require statutory changes nor any form of publication.

An SCE has to be registered in the Member State in which its head office is situated. It can transfer its own head office from a Member State to another without dissolution or need of new registration. This situation may create a problem resulting from the heterogeneous treatment of the SCE in the different Member States, particularly in fiscal matters that may, without doubt, play a factor in deciding where to locate the head office.

Like any other multinational company, each branch of an SCE is subject to the national fiscal regime and legislation of the country in which it is located.

The statutes of the SCE have to provide for the management structure. In this respect two possibilities exist:

- a dualistic system (management body and supervisory body);
- a monistic system (administrative body).

In addition, if permitted by the law of the Member State, the statute can provide among the members of the SCE not only customers or suppliers but, in some circumstances, a limited proportion of “investor members” who have no interest in using or producing the goods or services of the SCE. The right to vote attributed in the statute to the “investor members” has to be in compliance with the law of the State where the head office is legally located. In any case, however, “investors members” cannot have more than a quarter of the total right of vote.

## **7. The directive**

The directive, on the participation of the employees of co-operatives, aims at maintaining the rights of employees that will be implicated by the creation of SCEs.

It must be stressed that the new statute is to be adopted not for the purpose of avoiding numerous binding national obligations nor should the statute impose rules incompatible with existing employment relationships.

The solutions to protect acquired employees rights are based on negotiations between the participating companies and their workforce prior to the creation of the SCE

The directive on the participation of the employees will be transposed in the Member States legislation in accordance with their respective national juridical contexts.

The directive provides for three ways of involvement of the employees: the information, the consultation and the participation.

1. The information scheme is traditionally applied in France and Scandinavian countries. In such a scheme, representation bodies of the employees and/or representatives of the employees are informed by the competent body of the SCE on all activities carried out by the SCE or any of its branches located in any Member State. The directive specifies times, formalities and contents of the information activity, in such a way

as to allow the representatives of the employees to make an evaluation and eventually prepare consultation meetings with the competent body of the SCE.

2. The consultation scheme draws from the British tradition. It consists in a dialogue and exchange of opinions between the representation bodies of the employees and the competent body of the SCE. The directive establishes times, formalities and contents of the consultation procedure, in such a way that the representatives of the employees can present their opinion to the competent body. This opinion must be taken into account in the decision process of the SCE.

3. The participation scheme pertains to the German tradition.

The representatives of the employees of the SCE have the possibility to influence the development of the enterprise thanks to the right to appoint some members in the overseeing body or administration or by the right to oppose the designation of some or all the members of the body overseeing or administrative.

The procedural details on the participation established by the directive can, however, be disregarded by an agreement on different implementation procedures among the interested parties.

The directive fixes the general juridical framework for the negotiation, which remains the best way to determine concrete procedures regarding employees involvement. On the other side, the modalities on participation fixed by the directive become binding whenever the interested parties are not able to reach an agreement.

Every country must, therefore, transpose in its national legislation at least one of these three options and failing such, renders impossible the establishment of a registered office of a European co-operative.

## **8. The perspectives**

One element of the Statute is that it represents the first expression of society of people that finds recognition in the European company law. From an entrepreneurial point of view, this new text offers some interesting perspectives for co-operative enterprises.

The statute is of interest not only to existing co-operatives as it can be used also as a juridical tool for enterprises of other nature wishing to

group themselves so that they can operate for a common purpose, such as economies of scale, activities of research and development and access to new markets. What may attract such enterprises is the fact that the minimum capital requirement is 30,000 euro, a sum that is a quarter of the mandated sum for the European anonymous company (SE).

While an SE must be constituted from already operating companies, a SCE can be created starting from scratch.

Today around 300.000 co-operative enterprises are active in Europe and of which around 10-12% operate outside the local area. It is important that the activities of these co-operatives are able by now to develop in a certain juridical context, that guarantees their specificity at the European level.

There are some examples that confirm the existence of a real will on the part of co-operatives to commit themselves to the increasing European dimension of their activities. Others did not wait for the enactment of the statute to create alliances at the European level.

A particular case is the consumers' co-operatives of Sweden, Norway and Denmark where they have gathered their commercial activities in a sole entity called "Coop Norden" to enable them to better compete in the northern market. The ECS will formalize in an appropriate form such alliance.

The same is true in other agricultural co-operatives of North Europe such as the ARLA in Sweden and MD foods in Denmark who were waiting for the adoption of the statute to render official their alliance.

In France, various co-operative players, particularly those in agriculture, are ready to advance on some considered projects.

There are other numerous examples that can be cited.

Staying competitive and at the same time, respecting their own particularities is the opportunity offered by the SCE to the co-operatives.

## **9. The impact on accessing countries**

The co-operatives in the countries of Central and Eastern Europe are in a difficult period. Their image is not always positive and details of these can be found in other parts of this volume.

Having suffered for a long time a poor image of being a throwback to

the communist era notwithstanding their existence as long ago as one hundred and fifty years, the co-operative movements look with expectation to the statute. This expectation is rendered more urgent as attempts to re-launch co-operatives in these countries face a juridical environment that is not always favourable.

The fact that the European Union itself spells out the co-operative tool respecting the forms and options of the European company law is surely an important step forward, which can have positive effects that will push onwards co-operative legislations in the accessing countries.

Another impact that should not be underestimated is the possibility to have, in the new accessing countries, a recognized and organized co-operative movement that will bring great benefit for the whole European co-operative movement.

The attention to the co-operative dimension is not as easy today with the Council of 15. More so with a Council of the ministers of 25 and this is especially true with the new accessing countries where the co-operative experience is nonexistent or disaggregated and therefore, does not represent a strong player of political pressure or even worse, with the co-operative form being seen as residual of the past that is better done away with.

## **10. The influence on national legislations**

It has been ascertained that in 4 of the 15 countries of Europe prior to enlargement and in 5 of the countries of the enlarged Europe, co-operative legislation does not exist. This is so even if there exist some co-operatives held by hybrid systems but are not covered by a clear regulation.

The regulation on the SCE does not replace national legislations on co-operation. Rather, it can be said that numerous references to the national norms underline the value and need for reinforcing the national legislations.

An indirect harmonization may ensue as a consequence of SCE regulation.

An example is the recent reform of the Italian company law that has seen

a deep revision of the co-operative law<sup>12</sup>. During the works of the parliamentary Committee the reference to the SCE has been made, already in the Delegating Law which emanated before the conclusion of the process on the SCE.

Reading among the principles of the Delegating Law, one of the general criteria provided for by the article 1 of the delegating law, is: “to the coherence with the Community law, in which it assumes particular relevance the project of statute of European Co-operative Society, that is in advance phase of elaboration”<sup>13</sup>.

Therefore, the statute is not a tool of harmonization of the single national legal system but it goes towards a “creeping” harmonization. As always Community law lays down the foundation for the development of the national law, by contamination or capillarity.

## 11. Re-examination of the regulation

Article 79 provides for the re-examination of the Regulation within five years from its entry into force.

This must be done through a report of the Commission to the Parliament and to the Council and, if it is the case, to propose some changes. Among the elements of evaluation there will be also the effective use of the tool.

The co-operative movement, after its long insistence to have the statute, will find it opportune to activate itself by promoting the European co-operative concept. To disregard this statute as a less useful tool is indeed unfortunate.

A particular invitation must be addressed to the co-operative organizations of the cross border regions so that they may take upon themselves the promotion of the SCE.

## 12. Conclusions

If the SCE statute could be seen in the past as an additional opportunity for the development of cooperation in Europe, its adoption has now

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<sup>12</sup> Decreto Legislativo (Legislative decree) 6/2003.

<sup>13</sup> Legge delega del diritto societario (Delegating Law of reform of company law) 366/2001.

become a necessity. The realization of the single European market imposes the adaptation of the productive structures according to community dimensions and it is legitimate that such an adaptation can be achieved respecting the particularities of the co-operative enterprise.

Besides the aspect of opportunity of economic development, in this proposal there is also a symbolic dimension, which is affirmation that among the models of company law in Europe, not only the companies of capital exist, but that co-operative societies have a full right to be recognized in their specificity as important actors of the economic life of the European Union.

The co-operative movement owes this recognition from its practice of economy and its way of operating, the quest for equilibrium that brings together competitiveness and solidarity.

In the debate and in the trials of a new juridical framework for social enterprises that is being developed in various countries of Europe, it is inevitable and guaranteed that the co-operative form is seen in a privileged light.



## **PART 2**

Co-operative organisations' development paths in  
advanced economies



## 6. From co-operative to social enterprise: trends in European experience

*by Roger Spear* \*

### 1. Co-operative structures in Europe

Co-operatives in Europe use a wide range of legislative frameworks - in some countries there is law specifically for co-operatives, whilst in others co-operatives make use of traditional legal forms that have their origins in that countries development of social economy type structures. In general these forms share features that embraces the co-operative principles, but some types of co-operatives emphasise certain principles more than others. The following co-operative principles are common to all types of co-ops whether consumer, worker, producer, housing, agricultural, marketing, credit, etc.

- Voluntary and Open Membership
- Democratic Member Control
- Member Economic Participation
- Autonomy and Independence
- Education, Training and Information
- Co-operation among Co-operatives
- Concern for Community

These principle do not uniquely define co-operative structures, and in Western Europe there is considerable variety in the legal forms of democratic enterprises and this variety is increasing, particularly of hybrid forms which combine co-op and capitalist features; but in practice in a given situation the choice is much more limited by a countries legal/financial environment, the ideology of its development workers and within its support structures and other factors such as size and amount of external finance required.

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## 2. Recent trends in European co-operative structures - isomorphism

During the second half of the twentieth century, developments in the co-operative sector have frequently been marked by a tendency to change structures and practices in order to compete more effectively with conventional business in increasingly deregulated markets. A central feature of these changes has been the adoption of capitalist structures and practices, so that an isomorphic trend is apparent with co-operatives becoming more similar to capitalist business structures and practices.

There have been several major isomorphic trends in co-operative structures, firstly adaptation of the co-operative form, secondly the separation of economic and social dimensions of the co-operative organisation; thirdly hybridisation (especially increasing use of holding structures using share based legal forms); and fourthly degeneration.

*Adaptations of the co-operative form* - the post-war period in Europe has seen a number of significant legislative changes to the co-operative form in order to facilitate its operation in more competitive capital and product markets (see Monzòn Campos et al., 1996). Three in particular are noteworthy:

- issuing of non-voting shares to third-party financial partners;
- creating the capacity to change the membership base to include financial partners as members (as well as employees);
- adapting voting rights (away from the principle of equality of members) towards voting rights being weighted according to the extent of patronage.

*Separation of economic and social objectives/aspects.* This has been a strategy pursued by many co-operatives in order to allow an unhindered focusing on each aspect, for example in consumer co-operatives where member relations become rather separate from customer relations, and are linked mainly to governance requirements. Thus the consumer is treated separately from the member - the consumer becomes the focus of economic activity, whilst the membership aspect becomes marginalised and dealt with through separate social administrative structures. This results in the idea of membership being reduced more and more to a tiny minority that might be involved with AGM meetings and the occasional

social event but attempts to incorporate the idea of membership into the consumers base is neglected.

These trends can be seen in the following experiences.

In Spain legislation in 1995 allowed co-operatives to raise equity to encourage greater capital investment (through share issues) subject to some restrictions: (i) limited to no more than 33% of capital employed; (ii) a limit of 35-45% of votes for shareholders (depending on region); (iii) no limits to return on dividend.

In Sweden, which has been a bastion of co-operation internationally, from the 80s there was a change to the consumer co-operative orientation to its members - with members losing to a degree their dominant position in the co-operatives; instead, "they were only 'significant' customers among other consumers. ....and "many resources for general consumer policy have been discontinued: consumer research units, magazines and weeklies for consumer debate, consumer information and education, departments for member relations, laboratory facilities for product testing, etc." (Akë Böök and Blomqvist, 1996).

While in Swedish agricultural co-operatives trends can be seen away from solidaristic relations towards more market type relations between members and the co-operative.

Thus: although proportional financing is the norm, this is modified in practice through additional regulations, which lead to larger producers paying proportionally less than smaller ones; similarly it used to be that pricing was the same for all members, now it is more cost-based - according the costs a member causes the co-operative - this again is likely to favour larger producers.

In Quebec, the Mouvement Desjardins, a highly successful savings and credit union, has grown and developed as the markets have changed and internationalised, but as a result, creating tensions between:

- its co-operative and corporate components;
- the balance between members' internal capital and institutional investors' external capital;
- the balance between members and managers;
- the globalising of economies threatens Desjardins role in economic development of Quebec.

The outcomes of these tensions are unclear but indications are that un-

der certain conditions members interests are clearly threatened by the corporate entity:

- in Italy the 1992 reforms raised the limits on social capital that members could hold, but perhaps of more significance was the extension of the position of financial members, so that they could hold up to 33% of voting rights, and 49% of seats on the board - thus challenging traditional notions of democratic member control;
- in France, a remarkably similar 1992 Act enabled co-operatives to issue shares up to 35% of the capital base, with voting rights proportional to capital owned, but with similar risks to traditional democratic member control.

### **3. Hybridisation - the rise of holdings structures**

In many countries there was also a *hybridisation* of co-operatives (Côté, 2000) - a tendency to utilise capitalist structures either as a way of owning subsidiaries or as a way of combining activities with another society (where the shares are owned by both co-operative societies). This can be seen in a number of larger co-operatives which have wholly or partially owned share based subsidiaries. Holding structures are also used for joint ventures and merged activities; and such holding structures employ share based corporate forms so, for example, two co-operatives may hold shares in a joint venture activity. Thus the logic of capital is counterposed against the logic of members. Member influence and control becomes more difficult to exert over such structures - since control becomes indirect through the board of their co-operatives to the board of the joint venture.

The key points about this hybridisation are:

- the main form of hybrid is share based subsidiaries within social economy structures;
- there are also holding structures (share based companies) for joint ventures and merged activities; both the above have been seen increasingly as a way for co-operatives and mutuals to combat global competition;
- hybrids often involving partial member ownership and control - for example the employee stock ownership plan (the employee owned

structure: ESOP) - a “two-tier” structure, in which the workforce as a whole controls an organisation that owns (in whole or in part) the operating company (registered under conventional company law). Hybrid two-tier structure cover a wide range of possibilities for partnership between members as a collectivity and external bodies that co-invest and co-own the business. The principal draw-back of such arrangements is the additional complexity involved and usually each hybrid has to be devised almost from scratch (although in the UK bus sector, for example, employee ownership models are being developed). It ought to be possible to devise some models for such partnerships.

#### **4. “Degeneration” of the co-operative form**

There are 3 forms of degeneration. Constitutional degeneration where membership becomes restricted and employees are taken on to secure a greater proportion of the surplus to members. Organisational degeneration where the participatory structure of the co-operative becomes dominated by an elite; and goal degeneration where the goals of the co-operative change so that it becomes no different from a small capitalist business in the same sector (Cornforth et al., 1988).

The co-operative principles are intended to counter these tendencies but most recent forms of co-operatives have model rules and constitutions that make it extremely difficult for constitutional degeneration to take place. Hybrid forms - ESOPs, Employee Ownership structures, Sociedad Anonima Laboral (SALs: Spanish employee owned structures), which tend to be partially member owned enterprises - are particularly susceptible to this form of degeneration. On the other hand where the co-operative spirit only ever was skin deep, they (the members) may not see this development as a disadvantage.

#### **5. Factors influencing these trends**

*Global competition* - this puts pressure on co-operatives to match prices to consumers and producers with those of capitalist companies. In many cases this can result in copying business practices rather than using the

unique advantages of co-operatives. *Manager dominance* of social economy structures - this may not be overt, but carried out through the discourse that the needs of the corporate form must take precedence over the needs and goals of members.

*Unintended consequences*: legislation to improve the ability of co-operatives to compete or liberalising markets sometimes have unintended consequences - thus for example following the UK Building Societies Act of 1986 which made it easier to convert from mutual to limited company status, a wave of demutualisations resulted. Building Societies (savings and loans associations) have declined from 84 societies employing 83k f/t staff and 24k p/t staff in 1993 to 65 societies in 2002 employing 29k f/t staff and 9k p/t staff.

*Access to Finance* - Capitalist firms can finance growth by raising finance through share issues giving rise to equity, and by acquiring loans from financial institutions and individuals. Most co-operatives and the socially owned enterprises rely on loans and member finance as their main forms of external finance. Many co-operative argue that they have to use capitalist type structures to access financial markets for growth - drawing on the relevant financial instruments - see table below.

**Table 1 - Financial Instruments (available for business organisations)**

<i>Instrument</i>	<i>Characteristics</i>	<i>Advantages</i>	<i>Disadvantages</i>
Shares (voting)	Dividend payable	flexible	loss of control
Shares (preference, non-voting)	fixed % dividend	no loss of control	less flexible
Debentures	fixed interest, secured	no loss of control	higher interest
Commercial loans	Commercial interest rate		higher interest bank influence
Soft loans: - members - community - sympathisers	fixed and variable interest payment holidays repayment based on profit	flexible lower interest rates	goal displacement? (lender goals)

*Under-capitalisation and decapitalisation* - Most small businesses suffer from shortages of finance, and small co-operatives without access to signifi-

cant amounts of finance from owners/families may be pushed towards more capitalist/individualist forms in order to acquire sufficient finance.

## **6. A new trend - against isomorphism?**

In many European countries there have been important changes to social economy structures. In Italy since the 1980s we have seen a new co-operative structure: social co-operative, which combines elements of the non-profit (voluntary) organisation with that of the co-operative. Thus in contrast to traditional co-operatives where members are of one type (farmers, consumers, workers, etc.) members in social co-operatives may be workers, volunteers, community members, municipal representatives, parents of disadvantaged workers, users of services). But the business operates to a substantial degree in the market in a similar way to that of traditional co-operatives. Several thousand of such co-operatives have been formed. Italy, thus, has a favourable context for social co-ops (and co-ops in general) and has emerged as a leader in this form of social enterprise (Borzaga and Defourny, 2001). But the emergence of similar trends in the development of co-operatives and social enterprise can be seen in many other countries. These include the introduction of new legal status the “enterprise à finalité sociale” in Belgium (1995), the “social solidarity cooperative” in Portugal (1998), the “social initiative cooperative” in Spain (1999), the “social cooperative with limited liability” in Greece (1999), and the “société coopérative d’intérêt collectif” (SCIC) in France (2001), and the proposed “Community Interest Company” (CIC) in the UK. The replication of social co-ops in other countries has been an development that indicates there may be isomorphic trends across social economy sectors, responding to new situations in welfare systems, for example. There have also been developments of co-operatives in new sectors, such as Sweden, where social co-ops in the nursery or crèche sector take the form of parent or worker owned structures.

## **7. Social economy legal structures in the UK**

This paper now turns to examine experience in the UK. Almost all UK social economy structures are registered under Industrial and Provident

Society (I&PS) legislation or Company Law (limited by guarantee). In either of these cases the shares are of nominal value, limited liability applies, and the organisation is owned by member shareholders who may vary in number.

A company limited by guarantee (CLG) is registered under Company Law with nominal shares, limited liability, giving members democratic voting rights (1 person 1 vote). They are regulated by Company House. Many voluntary organisations and co-operatives currently use this form, since it is cheaper to register and make amendments than I&PS legislation.

An Industrial and Provident Society is an organisation that conducts a business or trade, either as a co-operative or for the benefit of the community. An Industrial and Provident Society is registered with the Registrar of Friendly Societies. Its actions and conduct will be regulated by the provisions of the Industrial and Provident Societies Acts, 1965 - 1978. A Friendly Society is a voluntary mutual organisation whose main purpose is to assist members (usually financially) during sickness, unemployment or retirement, and to provide life assurance. "Benevolent Societies" are another form of I&PS but for the benefit of the community rather than for their own members (a society "for the benefit of the community" is commonly known as a "bencom".)

From the report of the chief registrar of Friendly Societies 2000/1: "The organisations on our register range from internationally-known building societies and insurance companies to tiny village allotment societies. They include co-operative societies, housing associations, loan societies, scientific and literary societies, working men's clubs, benevolent societies, cattle insurance societies, agricultural pest clearance societies, superannuation funds, and most recently credit unions."

Thus they include the full spectrum of social economy forms of activity, from those which are club-like such as sports clubs, largely run by volunteers such as community associations, to much more commercial businesses like consumer co-operatives.

Being registered as an I&PS with the Registrar of Friendly Societies, means that there are certain requirements it has to meet, and some restrictions on its activities. The Registrar can help preserve the identity of the organisation, since he/she will not register any amendment to the

Rules that are not in accord with the democratic and community benefit principles established in the constitution.

The I&PS is required to file annual reports to the Registrar. It must appoint qualified auditors, and audited accounts have to be presented to the Annual General Meeting (AGM) as well as to the Registrar. The Constitution is crucial as it guides everything that an I&PS can do. An I&PS Constitution is often based on the Model Rules which “sponsoring bodies” such as federal bodies and development agencies supply.

Finance may be raised through members’ subscription to share capital, member loans, bank loans and the issue of loan stock (and retained earnings in future years). Outside finance must be without voting rights, although often in established co-ops “old” members (who are no longer active) continue to hold shares.

An organisation with charitable objectives can apply to the Charity Commission to become a charity or have charitable status (in addition to I&PS or Company limited by Guarantee status). A charitable trust would be appropriate as a complement to any of the above structures, if there were charitable activities (such as education) to be undertaken for others i.e. not for members. It has the advantage that donations are tax free (so tax can be reclaimed thereby increasing the original sum donated); and its activities are non-profit so not subject to tax.

*Social enterprise* - This is not a well defined category; in general people in the UK have a vague notion that it is a business with a social purpose. Experienced practitioners would generally accept that social economy legal structures (CLG and I&PS) are the most appropriate and commonly used structures for social enterprise.

## **8. New UK trends - against isomorphism?**

The UK, partly because of the large experience of de-mutualisations of mutual societies and co-operative structures, there have been several important responses to these forms of privatisation, which mark a new trend regenerating the values of mutuality and mutual practices. This has been led, to a certain extent, by activists who have formed pro-mutual groups “save our building societies”, and Mutuo (a pressure group cum think tank).

There has been a recognition by many commentators in the press and in academic communications of the value of diversity in the market (this has been particularly effectively argued in the case of Building Societies - savings and loans mutuals). And indeed it seems to be recognised to a certain extent by recent Government measures to protect Building Societies from demutualisation that they have performed an important role in giving consumers good value for money and protecting consumer rights. Several measures have been taken to give greater protection to mutuals firstly as a response by mutuals to insist on 'charitable assignment' - that is new members have to sign, giving up their rights to residual assets i.e. accepting they will not have a claim on the assets of the mutual in the event of privatisation or demutualisation; as a result the residual assets will be given to a charity or to another mutual. The second form of protection can be seen in new legislation: the Industrial and Provident Societies Acts 2002 which amends the procedure whereby such a society may convert itself into, or amalgamate with or transfer its engagements to, a company i.e. it is designed to make it more difficult to demutualise a society. The procedures have increased the percentage of people required to vote for constitutional change: 50% of members now need to vote and there needs to be a majority of 75% of the votes in favour of demutualisation. These measures have led to a refocusing by mutuals on members and membership. Another reaction or response that marks a resurgence of mutualisation can be seen in the rise of social enterprise as the embodiment or part of the embodiment of New Labour's 'third way'.

Finally, there has been some continental European influence where experience of new forms of co-operative (social co-ops) and social enterprise has seen a closer linking between the co-operative form and the voluntary organisation form and a re-assertion of the traditional social economy values.

## **9. Social enterprise and CICs**

In the UK, the Department of Trade and Industry has established a Social Enterprise Unit. Part of the motivation of promoting social enterprise is an interest in reforming public services delivery (incorporating

co-operatives and non-profit structures into the spectrum of service providers); and partly an interest in involving community/civil society stakeholders combat social exclusion. The activities of this Social Enterprise Unit have played a role in promoting a huge interest in social enterprise in the UK - this can be seen in outcomes such as the development of strategies for social enterprise and new legislation to facilitate the creation of new locally based social enterprise through the community interest company (CIC).

The Community Interest Company is about to be launched as a new legal form in the UK, and it may become an important model of social enterprise. The context for this development is a resurgence in interest in mutuality after declines in the co-operative/mutual sectors due to demutualisations and poor performance - developments that parallel similar isomorphic tendencies in other countries.

"...The Government will seek to develop further the Community Interest Company (CIC), an entirely new legal form designed for socially responsible enterprises. The Government does not intend that CICs should deliver essential public services such as schools or hospitals. However CICs have a clear role to play in complementing government services at the community level in areas such as childcare provision, community transport or leisure." HM Treasury Budget Report 2003.

The legislation for the CIC is scheduled for this parliament (2004) and so could be enacted within a few months. The legislation will establish a new type of company, the community interest company, for use by social enterprises wishing to operate as companies.

The CIC is designed to be a flexible structure facilitating entrepreneurial activity.

It has 3 main characteristics:

- non-profit;
- benefiting the community;
- asset lock.

The CIC is intended to be used by non-profit-distributing enterprises providing benefit to a community. Such enterprises are currently operating in areas such as childcare, social housing, leisure and community transport. Many of them already incorporate as companies, either as a company limited by guarantee (CLG) or a company limited by shares

(CLS). The defining characteristics of the CIC are intended to make it particularly suitable for some types of community-based social enterprise - those that wish to work for community benefit within the relative freedom of the non-charitable company form, but with a clear commitment to a non-profit-distribution status. CICs will be subject to the general framework of company law. Thus the CIC will be a new variant of existing forms of company. It can either take the form of a CLG or CLS.

The distinguishing features of the CIC will be:

- the need to satisfy a community interest test, confirming that the enterprise will pursue purposes beneficial to the community and will not serve an unduly restricted group of beneficiaries. The test is that of a reasonable person judging if the CIC's activities to benefit the community;
- exclusions from CIC status: political parties, companies controlled by political parties, and political campaigning organisations;
- charitable status: CICs will not be able to have charitable status, but charities can establish CICs as subsidiaries;
- annual reporting: CICs must produce company report containing key information relevant to CIC status, lodged with the public register of companies;
- an asset lock - CICs will be prohibited from distributing profits they make to their members;
- CICs limited by shares can pay dividends to "investor shares", subject to a cap regulated by the Regulator; but a CIC limited by guarantee, will not be to make such distributions; limits on conventional interest payments on fixed term debt will not be applied;
- a CIC's residual assets, when it is wound up, will not be distributed to its members, rather they will pass to another similar organisation with restrictions on profits distribution like another CIC or a charity;
- the Regulator approves applications for CIC status, receives copies of the community interest company reports and polices the requirements of CIC status, including compliance with the asset lock. The CIC Regulator will have close links with the Registrar of Companies.

CICs are required to provide an *additional annual community interest company report* to the registrar of companies; this covers: what the CIC has done during the year to benefit the community; the steps, if any, that the com-

pany has taken to involve in its activities its stakeholders; information about payments related to its financial instruments, and the remuneration of its directors.

## 10. Issues/concerns arising from the CIC legislation

There has been an extensive consultation on elements of the proposed legislation. The issues and concerns arising are as follows:

- the CIC legal structure facilitates small, community-based social enterprises, gain access to finance but also locks-in its assets and profits so that public interest is preserved;
- it provides a recognised vehicle for many social enterprises with improved access to finance, a stronger 'brand' and preserving assets and profits for social enterprise;
- the CIC form can be seen as a complement to Industrial and Provident Society legislation providing choice for social entrepreneurs (but not a substitute for reforming the latter which is too cumbersome); the Company Limited by Guarantee legislation impedes some entrepreneurial activities;
- if this model is to have a role delivering public services, the social enterprises will have to operate on a reasonable scale and have clear mechanisms for involving stakeholders in their governance.

On the other hand:

- the proliferation of legal forms may confuse both the wider public and social entrepreneurs setting up social enterprise. It is not clear that these difficulties could not be resolved by reforming I&PS legislation;
- this measure aims to solve the problems of the sector cosmetically; it fails to address more serious issues such as who bears the risk when these organisations deliver public services, and whether private finance should be involved;
- there are too many legal forms, it would be better to reform charity law to allow them to trade more freely;
- there will not be a clear understanding how a CIC differs from a Community Benefit Society (bencom) or from a CLG with objects beneficial to the community;

- the issue of a strong new brand might detract from the charity brand, if CICs, as non-profits, can be involved in activities that are non charitable.

## 11. Analysis of CICs prospects

The CIC is designed to be a flexible structure, however this means that it can take quite diverse forms:

- capitalist share structure (CLS) vs social economy democratic structure (CLG);
- non-profit but possibly dividend paying (capped);
- multi-stakeholder vs single owner stakeholder;
- involving stakeholder or not involving stakeholders;
- community interest report but undemanding and not sent to stakeholders.

Thus it covers both capitalist share structures and social economy democratic structures; but with a non-profit orientation, though possibly dividend paying (albeit capped). It may involve multi-stakeholder structures but alternatively could be wholly owned by a charity or other corporate entity. The CIC must produce a *community interest company report* which specifies how it involves stakeholders, but if it doesn't involve stakeholders that is acceptable. The report is sent to the company registrar and regulator, from whom any stakeholder may obtain a copy - it is not required to be sent to stakeholders (unlike annual financial reports for shareholders).

The model seems to be based on an outcome approach where community benefit, non-profit and asset preservation (via the asset lock) are emphasised while the *means* or processes for achieving those important outcomes are not considered important. Thus democratic process and social capital - which might be ways of involving stakeholders are not considered central parts of the identity of this form (or its brand). It downplays democratic structures which clearly does not fit well with traditional co-operative values. And although its common attributes fit well with the voluntary sector, its downplaying of stakeholder involvement does not fit those traditions. (As a class of entities it would not meet the European benchmark - the EMES criteria of a social enterprise,

see: [www.emes.net](http://www.emes.net). However it might fit a broad view of a social enterprise as a business with a social purpose).

It is also important to note that rather than locating a new social enterprise structure within traditional social economy legal structures of friendly societies and industrial and provident societies<sup>1</sup>, where protection of values and identity by the regulator have been stronger, the new legal structure is located within company law.

However it is difficult to predict the final outcomes, in all probability there will be a mixed result for this new sector - based on the following scenarios.

Best case scenario: its diverse flexible structure draws in entrepreneurs and capital to expand the social enterprise sector.

Worst case scenario: its diversity, undermines a clear identity and common set of values, adding little to a misunderstood social enterprise brand.

Even worse scenario: it opens a path for small business entrepreneurs to access government grants for community service provision; they don't involve stakeholders, pay poor wages, make good profits which are used by management to pay themselves above average salaries, with good perks (expenses, additional benefits, etc).

## 12. Conclusions

This paper has reviewed trends in co-operative structures in the second half of the twentieth century, noting a tendency for isomorphism with conventional business. It has detailed a number of modifications to the traditional co-operative form which were initiated to allow it to compete more effectively in global markets: through improving the access to finance, facilitating the separation of economic and social dimensions of the enterprise, and utilising corporate holding structures to achieve growth through joint venture, merger and acquisition. While competitiveness may have been enhanced, such measures may also have resulted in a move away from co-operative or social economy values, and in a number

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<sup>1</sup> Indeed there appear to be a policy of neglect of the I&PS legal framework in operation currently, since costs of registering and amending rules are higher than CLGs, and despite pressure for reforms, no progress has been made.

of sectors there have been substantial levels of demutualisations.

However in the last 20 years or so there has been a resurgence of social economy values particularly in new market sectors associated with welfare services. And new forms of social enterprise have been developed in many European countries. This raises the prospect of a resurgence of social economy values reversing the isomorphic trends seen in traditional sectors.

In the UK, new legislation for a Community Interest Company appears to fit within a similar regenerative tendency. However, despite an apparent orientation towards mutualism linked to New Labour's Third Way, it is difficult to argue that the new CIC legislation represents a resurgence of interest by policy makers in the traditional values of the social economy. Instead, it seems like a very British pragmatic approach to community development focusing on outcomes, but the risk is its neglect of process values will undermine the brand, and miss the opportunity of increasing the capabilities of communities to take part in their own development. Its flexible structure may bring new benefits to disadvantaged communities, but in this strength is its weakness - diversity and lack of identity. Time will tell which proves more important.

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## Appendix

### *Traditional Capitalism:*

You have two cows.

You sell one and buy a bull.

Your herd multiplies, and the economy grows.

You sell them and retire on the income.

### *French Capitalism:*

You have two cows.

You go on strike because you want three cows.

### *German Capitalism:*

You have two cows.

You re-engineer them so they live for 100 years, eat only once a month, and milk themselves.

### *Canadian Capitalism:*

You have two cows.

Come to think of it, they look more like a pair of moose - in fact, yes they are.

One speaks French, one speaks English.

One fights to create a new country, the other won't let it.

They both play ice hockey rather well.

### *Italian Capitalism:*

You have two cows, but you don't know where they are.

You break for lunch.

### *British Capitalism:*

You have two cows.

Both are mad.

### *Co-operative Capitalism:*

You have two cows.

Well actually you don't as the cows are indivisible assets held in common by all the members, but you do get a dividend on the milk sold.

You merge with several other co-ops to maintain competitiveness.

You have twenty cows.

Well actually you don't as the cows are indivisible assets held in common by all the members, but unfortunately no-one knows who the members are because the membership lists are lost, out of date or in different formats.

## 7. The Italian experience: a legal framework in progress

by Paola Iamiceli \*

### 1. The main questions

Do we need a specific regulation on social enterprise under Italian law? Does the whole set of laws regarding non-profit organizations and social co-operatives not constitute a sufficient or adequate legal basis for a good development of social enterprise? What is lacking?

The following analysis will mainly show that some focal profiles for the development of social enterprise are currently not covered by the massive legislation already existing. Moreover, a specific law about social enterprise might contribute to legitimate this special type of enterprise, defining its core elements and mandatory rules, if any. Finally, although the existing legislation represents an important basis to look at the multiple forms in which social enterprise is evolving today, a specific need for coordination arises: again, a special law about social enterprise should accomplish this further task<sup>1</sup>.

The issue concerning the introduction of a special regulation about social enterprise has been included in the Italian legislative agenda for some years. Also thanks to the contribution made by scholars and experts operating within the Emes network and, even more specifically, within the Digestus group, a former proposal had already been elaborated under past legislature, as also promoted by the Permanent Committee for the third sector (constituted within the Social Affairs Commission). A separate initiative aimed at reviewing the whole regulation on non-profit organisations by reforming the first book of the Italian civil code. However both attempts did not come into effect at that time.

Under the current legislature, a different proposal for the regulation of

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<sup>1</sup> On the functions of a special law on social enterprise see Cafaggi (2000, pp. 637 ss.), where four functions are examined: (1) a legitimating function; (2) a selecting function; (3) a regulative function; (4) a promoting function.

social enterprise was presented by the Government on the 19<sup>th</sup> July 2002. The proposal was approved with amendments by the Chamber of Deputies on the 20<sup>th</sup> November 2003, also on the basis of a debate involving social bodies, non-profit organisations and such like, some of which severely criticised the proposal. The text is now being examined by the Senate<sup>2</sup>.

More recently a new project concerning the reform of the first book of civil code has been elaborated by the Orlando Foundation, as also promoted by Confcommercio<sup>3</sup>. Unlike the previous one, this proposal includes a separate regulation on collective interest non-profit organisations and on non-profit enterprises (again distinguishing non-profit enterprise from collective interest non-profit enterprise).

Although the discussion is quite advanced (especially about the Government proposal), many issues still stimulate a vivid discussion among political parties, non-profit networks and civil society. Some of these will be analysed in this paper, starting from the analysis of the reasons why a law about social enterprise may help its development and proceeding on the ways in which this change might be enacted by the law.

More specifically two main questions will be examined:

- whether and why the current law about non-profit organisations and co-operatives represents (or does not represent) a valid regulation for social enterprise; in other words: why a special law about social enterprise is needed (see paragraphs 2 and 3) and
- whether the legislative proposal currently discussed at the Parliament (or others concurring proposals) can be considered a valid reply to this need (see paragraph 4).

## **2. Which social enterprise under the current law?**

The former issue requires some clarifications about the concept of social enterprise and the forms through which it can be undertaken already under the current legislation.

Indeed, as today, it does not seem possible to link the notion of social

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<sup>2</sup> See the text at: [www.parlamento.it](http://www.parlamento.it).

<sup>3</sup> See the proposal at [http://www.confcommercio.it/home/ArchivioGi/DIC-2003/Convegno-dirittosocietario.doc\\_cvt.htm](http://www.confcommercio.it/home/ArchivioGi/DIC-2003/Convegno-dirittosocietario.doc_cvt.htm). For a comment: Bassi (2003, pp. 143 ss).

enterprise to a single legal organisational form, since many organisations may appear to be eligible, although some constraints do limit or exclude the possibility of running a social enterprise by adopting certain forms. Given this, it is useful to start from a specific concept of social enterprise and then to verify which organisations are really eligible for undertaking this special purpose activity. This analysis should help reconstruct the current legal framework for social enterprise with a view to possible criticism about its adequacy and need for specific legal intervention on social enterprise as such (see paragraph 3).

For the purpose of this analysis a social enterprise can be defined as an economic activity of production and/or delivery of goods and/or services of social interest as performed according to entrepreneurial methods, which imply a permanent organisation of human and physical resources as well as the general capacity to cover the costs of the activity though not necessarily generating profits.

In this respect, three sub-issues seem quite critical: the notion of social interest; the relevance of the non-distribution constraint; the entrepreneurial core of the organisation. The analysis of these three profiles will also help to identify the typologies of social enterprise currently considered by law.

A. As to the first aspect, it is known that part of the economic literature justifies the existence of third sector looking at the ability of the organisations to produce public goods, also named as meritorious goods, or goods for which a market cannot exist due to market failures generated by positive externalities and information asymmetry between producers, patrons and beneficiaries<sup>4</sup>. Examples regard health care, education, welfare services and such like. More specifically, some authors believe that a social purpose enterprise can be distinguished for its ability of generating positive externalities<sup>5</sup>. This would be distinctive also with respect to

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<sup>4</sup> See, from different perspectives: Ben Nér and Van Hoomissen (1994, 4, pp. 393 ff); Hansmann (1980, pp. 835 ff). Within the Italian debate about social enterprise see also Giorgetti (2002, p. 36), about the importance of meritorious goods within the definition of social enterprise; Fazzi (2002, p. 28), who considers the ability of creating “common goods” the main feature of social enterprise, attaching to the notion of common goods a relational value linked with the ability of the organisation of generating trust and social capital. See also the references contained in the next footnote.

<sup>5</sup> Cafaggi (1999, p. 49 f.; 2000, p. 649). Within this debate see also Borzaga and Solari (2001, p. 296); Zamagni (2002, p. 72), who refers to the notion of social externalities to introduce the concept of civil enterprise (therein distinguished but in fact close to the notion of social enterprise as mainly intended).

cases in which the direct beneficiary voluntarily receives the goods or services (i.e. on the basis of a contract, either gratuitous or for a fee), given that additional benefits are generated by the relationship, for instance in favour of relatives or the community as such as indirect beneficiary<sup>6</sup>.

On a normative basis it is not obvious how to define a social interest activity starting from these approaches. Quite a common solution is the one which deals with sectors of activity rather than the nature of the activity itself<sup>7</sup>. More specifically the sector (e.g. health care, culture, welfare, education, etc.) is considered as a proxy for a specific nature of the activity which would be hard to observe as such. Whether this approach is really conclusive could be questioned and it seems notable that the legislation itself tends to combine the sectors with other criteria concerning the nature of the activity and its real impact on the beneficiaries<sup>8</sup>.

For the purpose of this analysis a broad approach can be taken, given that, at this stage, the intent is not to strictly define what a social enterprise is under the current law (which in fact does not include a specific regulation about social enterprise), but, rather, to what extent the current legislation may be seen as already suitable for regulating social enterprises although not specifically devoted to it. From this point of view it may be interesting to enlarge the set of relevant regulation including the laws respectively concerning: social co-operatives, voluntary organisations, non governmental organisations, social promotion organisations, non commercial associations, non-profit social purpose organisations, banking foundations, operatic foundations, cultural foundations, supplementary pension funds, to mention the most well-known ones<sup>9</sup>: indeed, in

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<sup>6</sup> F. Cafaggi (1999, p. 47).

<sup>7</sup> See the Legislative Decree n. 153/99 on banking foundations (see part. art. 2, where it is stated that these foundations exclusively pursue social goals, promote economic development and exclusively direct their activity in 'admitted' sectors and mainly operate in 'relevant' sectors, the former being defined by law, the latter by the foundation within the former; on this point, see also the decision of Italian Constitutional Court n. 301/2003 and the Ministerial Decree n. 150/2004, part. art. 2); or art. 10, Legislative Decree n. 460/97, on non-profit social purpose organisations (ONLUS), which defines the sectors in which these organisations carry out their activity; or moreover law n. 381/91 on social co-operatives, where a former type of co-operatives is defined with respect to the performed activity undertaken (health-care, social and educational services).

<sup>8</sup> See, for example, about ONLUS, art. 10, cit., where it is stated that goods and services are directed to disadvantaged persons or foreign communities (with respect to humanitarian aid).

<sup>9</sup> See: Law n. 381/91 on social co-operatives, Law n. 266/91 on voluntary organisations, Law n. 49/87 on non-governmental organisations, Law n. 383/2000 on social promotion organisations, Presidential Decree n. 917/86, art. 148, on non-commercial associations, Legislative Decree n. 460/97 on non-profit

any event, all these private organisations operate within social interest sectors.

B. The point concerning non-distribution constraint is also critical. On the one hand, nobody would doubt that an organisation which adopts this constraint may operate as a social enterprise: this means that, in order to compose the current legal framework about organisations which can run a social enterprise, the general regulation about associations, foundations and committees cannot be ignored, since all these organisations adopt a non-distribution constraint. On the other hand, the question is whether a partial non-distribution constraint (which means a constraint that limits without excluding the distribution of profits) can be accepted within the range of social enterprise features.

Recent approaches favour this solution, especially considering the need for financial resources which could be, at least partially, satisfied by the means of this slight liberalisation of the constraint, although within specific limits. Indeed a limited distribution of profits would give some (additional) incentives in investing in this type of enterprise, lowering the prospective costs of the investment without altering the nature of the activity given that the distribution would in fact be very limited<sup>10</sup>. This approach would enable the inclusion, within the range of current relevant legislation about social enterprise, of also the one concerning social co-operatives that, as it is known, which may, at least in principle, distribute limited profits<sup>11</sup>.

C. The third sub-issue (whether all the organisations so far mentioned may legally perform entrepreneurial activity) is more complex, because it involves an interpretative legal analysis concerning the specific types of organisation.

That associations and foundations in general may carry out entrepreneu-

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social purpose organisations (ONLUS), Legislative Decree n. 153/99 on banking foundations, Legislative Decree n. 367/96 on operatic foundations, Ministerial Decree November 27, 2001, on cultural foundations, Legislative Decree n. 124/93 on supplementary pension funds.

<sup>10</sup> Cafaggi (1999, p. 47); Zoppini (2000, pp. 362 ff).

<sup>11</sup> See Legislative Decree n. 1577/47, art. 26, as mentioned by Law n. 381/91, art. 3, on social co-operatives, and art. 2514, civil code, as reformed in 2003, on prevalent mutuality co-operatives. In both regulations a cap (but not a total ban) is put on distribution of profits. See on this topic Fici (2003, pp. 145 ff., part. pp. 154 ff).

rial activity is today widely accepted<sup>12</sup>, although disputed in the past<sup>13</sup>. It is notable to highlight that both the proposals already mentioned for the reform of the first book of civil code explicitly include this possibility while regulating associations and foundations<sup>14</sup>. Some doubts remain with respect to the so called committees, also regulated by the first book of the Italian civil code, given their nature that, although in absence of a legislative constraint, many describe as ‘temporary’<sup>15</sup> and then not really suitable for an entrepreneurial activity.

However, also with respect to associations and foundations, the real problem consists in the lack of regulation on organisational aspects related to entrepreneurial activity (i.e. balance sheets, reserve funds, bankruptcy and such like)<sup>16</sup>. One of the above-mentioned legislative proposals confined itself to making applicable the general regulation about (for-profit) enterprises to entities which, although different from companies, undertake economic activities, only requesting that the entrepreneurial managers do not also carry the institutional activities of the non-profit organisation<sup>17</sup>. Could this approach be effective? This issue will be discussed later.

As to the single typologies of organisations, as regulated by special laws, the approach adopted by the legislator is generally restrictive with respect to the exercise of social enterprise by non-profit organisation. With the exception of social co-operatives (whose entrepreneurial nature cannot be disputed), in many other cases the law tends to attach to the enterprise a marginal role and to reduce its relevance within certain limits.

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<sup>12</sup> Rescigno (1967, pp. 812 ff.); Costi (1968, pp. 1 ss.); Galgano (1969b, pp. 73 ff.); Zoppini (1995, pp. 164 ff.); De Giorgi (1999, pp. 387-8); Ponzanelli (2000, pp. 177 ff.); Cafaggi (2000, pp. 596 ff.); Fusaro (2002, pp. 291 ff.). In case law: App. Palermo, April 7, 1989, in «Giurisprudenza commerciale», 1992, II, pp. 64 ff.; Trib. Milan, July 16, 1998, in «Diritto fallimentare», 1999, pp. 332 ff.; Trib. Genova, April 7, 2001, in «Vita notarile», 2002, p. 683.

<sup>13</sup> For an example in case law, see App. Rome, February 9, 1981, in “Fallimento”, 1981, p. 676.

<sup>14</sup> Reference is both to the proposal of reform drafted by the commission operating within the Ministry of Justice (see art. 13) and the one drafted by the Orlando Foundation and promoted by “Confcommercio” (see art. 2.1, lett. d, and art. 8).

<sup>15</sup> See Basile (1999, p. 546) (where further references are mentioned also about case law).

<sup>16</sup> On the tendency of social enterprises to organise themselves as co-operatives rather than as associations or foundations, see Borzaga and Santuari (2001, p. 167).

<sup>17</sup> See art. 13, Italian civil code, as included in the proposal of reform drafted by the commission operating within the Ministry of Justice. By contrast, the proposal drafted by the Orlando Foundation aims at providing a specific regulation for non-profit enterprise also distinguishing between non-profit enterprises and public interest non-profit enterprises (see art. 8).

Limitations arise with special reference to two organisational and economic features: financial sources and labour relations.

With respect to the former, it is often decreed that revenues from the delivery of goods or services should be limited within certain ranges<sup>18</sup> and in any case the (productive/commercial) activity should be instrumental and auxiliary with respect to the core (or institutional) activity of the organisation<sup>19</sup>. The main assumption is that the organisation does not operate as an enterprise as such but may choose to establish an enterprise as an auxiliary means of pursuing its institutional goals. It is notable that in some cases limitations concerning revenues from delivery of goods or services are relaxed if they derive from contracts with public agencies<sup>20</sup>. This approach would favour social enterprises which are publicly funded, leaving aside others which operate independently from the public administration.

With respect to labour relations, other constraints may arise on the usage of employment contracts in organisations for which the law requires a prevalence of gratuitous activity as carried out by members<sup>21</sup>. In fact a more prominent problem regards the regulation of labour relations in non-profit organisations despite the extent to which employees can be recruited<sup>22</sup>. A law has been enacted with reference to co-operatives<sup>23</sup>, while a wider analysis should be conducted for the other organisations also considering the new perspectives created by the recent reform of labour law (Law n. 30/2003 and Legislative Decree n. 276/2003).

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<sup>18</sup> See Law n. 266/91, art. 5.1, lett. *g*, on voluntary organisations; Legislative Decree n. 460/97, art. 10, co. 2-6, on ONLUS; Presidential Decree n. 917/86, art. 148, on non commercial entities. In some cases the law does not include a prohibition, but offers fiscal incentives to comply with the rule (ONLUS); in other cases it is not clear whether, besides the different fiscal treatment, the rule also incorporates a real prohibition (voluntary organisations).

<sup>19</sup> See Law n. 383/2000, art. 4, on social promotion associations; Law n. 266/91, art. 5, on voluntary organisations; Law n. 49/87, art. 28.4, lett. *c*, on non-governmental organizations; Legislative Decree n. 153/99 on banking foundations (part. art. 3.1, where the limitation also concerns the sectors in which the enterprises may operate; on this point see Fusaro (2002, pp. 299 f.); Ministerial Decree November 27, 2001, art. 11.2, on cultural foundations.

<sup>20</sup> See Law n. 383/2000, art. 4, lett. *e*, on social promotion associations; (in the perspective of tax law) Ministerial Decree May 25, 1995, art. 1.3, on voluntary organisations,

<sup>21</sup> See, with different approaches, the law about voluntary organisations (art. 3.4, where employees and autonomous workers may be employed only if strictly necessary) and the one about social promotion associations (see article 18, where such employment is allowed in case of special necessity).

<sup>22</sup> On the special features of labour relations in non-profit sector, see in an economic perspective Borzaga and Musella (2003).

<sup>23</sup> See Legislative Decree n. 220/2002 on worker members in co-operatives.

A different approach can be distinguished with respect to other organisations. Once admitted that a limited distribution constraint is consistent with the social enterprise model, then the social co-operative pattern can be definitely considered as the main representative of social enterprise, as legally regulated in Italy. While a former type of social co-operative operates in some specific sectors, a latter type is conceived as open-ended with respect to the sectors, provided that it present a certain labour relations structure so as to include disadvantaged workers<sup>24</sup>.

Apart from social co-operatives, in some other organisations the (social) enterprise seems also to emerge as the main (not merely auxiliary) activity undertaken: according to decree n. 367/96, in order to pursue their cultural goals, operatic foundations manage their theatres and operate adopting entrepreneurial methods and efficiency standards<sup>25</sup>; in a different context, supplementary pension non-profit organisations are also recognised as (social) enterprises<sup>26</sup>. Differently from social co-operatives, both these patterns concern highly specific purpose entities. Thus, they may represent an interesting reference model along the path which leads to a more general regulation about social enterprise; however, they may not incorporate the social enterprise model as such under the Italian law, given their limited purpose.

This brief overview enables us to conclude that, in the absence of a specific law concerning social enterprises, the Italian law does include patterns of private organisations that can undertake such activity. While only few regulations consider social enterprise as the main activity of the organisation, many others tend to limit its emergence within certain ranges.

In the current political and cultural environment, in which the ability of non-profit organisations to operate as enterprises is not conclusively disputed, the major obstacle against a more open approach is represented by the lack of adequate regulation. Only when crucial aspects, like labour relations, bankruptcy, competition, accountability are legally defined with specific reference to non-profit organisations and social pur-

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<sup>24</sup> See Law n. 381/91, art. 1. For a recent view on this typology, also considering the impact of the corporate law reform, see Fici (2003).

<sup>25</sup> See Legislative Decree n. 367/96, art. 3.2.

<sup>26</sup> See Albany International BV c. Stichting Bedrijfspensioenfonds Textielindustrie, C-67/97, September 21, 1999; Pavlov c. Stichting Penzionenfonds Medische Specialisten, C-180/98, September 12, 2000.

pose entities, only then may some constraints be relaxed and the emergence of social enterprise be accompanied by a richer set of organisational forms.

### **3. What kind of regulation for social enterprises in the current legal framework should be adopted?**

The previous analysis shows to what extent social enterprise can operate today and under which legal forms according to Italian law. A distinct issue regards how social enterprise is regulated by the various laws concerning these forms and patterns. Lacking a comprehensive and consolidated legislation about social enterprise, the regulation is extremely fragmentary and incomplete.

Within the perspective of the debate concerning the nature and the governance of social enterprise, this analysis will focus on four crucial profiles, with no attempt to be exhaustive, since many others could in principle be discussed here. The selected profiles are the following:

- a) stakeholders' participation;
- b) accountability, transparency and information duties;
- c) liability rules;
- d) bankruptcy and liquidation procedures.

#### **3.1. Stakeholders' participation in the governance structure**

It is known that stakeholders' protection has been seen as one of the distinct features of social enterprises. More precisely, legal scholars and economists have highlighted the multi-stakeholder nature of social enterprise governance, thus focusing on stakeholders' participation within the organisational structure of the entity<sup>27</sup>. Others have favoured stakeholders' participation without necessarily labelling social enterprise as multi- or mono-stakeholder, but acknowledging both models<sup>28</sup>.

In fact direct participation (within general meetings, administrative body,

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<sup>27</sup> See Borzaga and Mittone (1997); Borzaga and Solari (2001, p. 296); Sacconi (2002, pp. 257 ff). With respect to the legislative proposal herein commented: Borzaga (2002, p. 10); Zamagni (2002, p. 75); Fazzi (2002, p. 31); Sacconi (2003, p. 39).

<sup>28</sup> Cafaggi (2000, p. 652).

committees, etc.) is not the only sign of stakeholders' protection within the organisation: stakeholders may be represented by other agents (either voluntarily delegated, or in any event, in charge of this duty) or different rules and standards may be applied as a means for stakeholders' protection (e.g. accountability standards may be seen in this light). This section will focus on (direct or indirect) stakeholders' participation, while the following ones will consider different profiles also affecting on stakeholders' protection.

For the purpose of this analysis stakeholders are considered as eligible interests holders with respect to the organisation. An interest is eligible when either the holder provides resources as a contribution to the organisation (these resources being financial or human capital, also consisting in know-how, skills or reputation), or he/she is (also potentially) victim of negative externalities generated by the organisation<sup>29</sup>. Interests of the first type are normally protected by contracts; interests of the second type are generally covered by mandatory laws and protected by tort law, at least in the area of private law. Those who defend a multi-stakeholder approach with respect to social enterprise also believe that all these interests can be protected by the governance of the organisation. Again, one of the main outcomes of this approach (not the only one), is the inclusion of stakeholders' participation rights within the governance structure of the organisation.

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<sup>29</sup> See, among others, the definition of stakeholder given by Sacconi, *Corporate social responsibility (csr) as a model of "extended" corporate governance. an explanation based on the economic theories of social contract, reputation and reciprocal conformism*, in [www.ssrn.com](http://www.ssrn.com): "This term denotes individuals or groups with a major stake in the running of the firm and who are able to influence it significantly (Freeman and McVea 2002). However, a distinction should be drawn between the following two categories: I) Stakeholders in the strict sense: those who have an interest at stake because they have made specific investments in the firm (in the form of human capital, financial capital, social capital or trust, physical or environmental capital, or for the development of dedicated technologies, etc.) - that is, investments which may significantly increase the total value generated by the firm (net of the costs sustained for that purpose) and which are made specifically in relation to that firm (and not in any other) so that their value is idiosyncratically related to the completion of the transactions carried out by or in relation to that firm. These stakeholders are reciprocally dependent on the firm because they influence its value but at the same time - given the specificity of their investment - depend largely upon it for satisfaction of their well-being prospects (lock-in effect). II) Stakeholders in the broad sense: those individuals or groups whose interest is involved because they undergo the 'external effects', positive or negative, of the transactions performed by the firm, even if they do not directly participate in the transaction, so that they do not contribute to, nor directly receive value from the firm."

If the above mentioned legislation about organisations that may or do, in fact, operate as social enterprises is considered, then two models seem to emerge:

- a model in which a uniformity and equality principle is stated so as to prevent differentiation between different interests within the governance structure of the entity;
- a model in which such differentiation is allowed or also favoured as a means to identify and protect different classes of stakeholders' rights within the organisation.

Organisations of the former type are social promotion associations and non-profit social purpose organisations<sup>30</sup>. Organisations of the second type are social co-operatives, banking foundations, cultural foundations, operatic foundations, pension funds<sup>31</sup>.

The co-operative model is the most complex one, also because of the impact produced by the recent reform of corporate law. Indeed, not only the assembly may include different classes of members (workers, financiers, voluntary members) but separate assemblies for separate interests may arise and also the administrative body may be composed of different directors according to the various classes of interest they may represent.

The other organisations are characterised by a simpler structure which is normally based on the 'representativeness' of eligible interests within one or more bodies: in some cases, the criterion is referred to the directing body (*organo di indirizzo*)<sup>32</sup>; in others to the administrative body<sup>33</sup> and, sometime, also to the monitoring body<sup>34</sup>; quite an important emphasis, although not exclusive, is given to the role of financiers<sup>35</sup>.

It may be worthwhile to consider how, within this scenario, associations tend to fall into the first model, co-operatives and foundations into the

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<sup>30</sup> See Legislative Decree n. 460/97, art. 10.1, lett *b* on ONLUS; Law n. 383/2000, art. 3.1, lett. *f*, on social promotion associations.

<sup>31</sup> See articles 2540, 2542, paragraph 4, civil code, on co-operative corporations, also applicable to social co-operatives; Legislative Decree n. 153/99, art. 4.1, lett. *c*, and Ministerial Decree n. 150/2004, art. 3, on banking foundations; Ministerial Decree November 27, 2001, art. 6, paragraph 3 on cultural foundations; Legislative Decree n. 367/96, art. 10, paragraph 3, on operatic foundations; Legislative Decree n. 124/93, art. 5, on pension funds.

<sup>32</sup> Thus with respect to banking foundations and cultural foundations.

<sup>33</sup> Thus with respect to operatic foundations.

<sup>34</sup> Thus with respect to pension funds.

<sup>35</sup> With the only exception of the banking foundations, where this criterion is not explicitly stated (and probably not relevant in fact), this can be said for all the organisations previously mentioned in the text.

second one<sup>36</sup>. While foundations seem to mainly consider interests of ‘financial’ and ‘knowledge capital’ providers, co-operatives offer a wider range with respect to the typology of interests.

However, no general conclusions may be inferred. Apart from the co-operative model, associations and foundations are here presented on the basis of special legislation which is not applicable to any organisation which adopts this form to operate as a social enterprise. The first book of civil code, which still represents the general legal framework for associations and foundations, does not really provide any foundation for a (multi-)stakeholder approach to non-profit entities governance.

### 3.2. Duties of information and accountability

What has just been considered above also applies to duties of information, reports and more generally to the accountability regulation of these organisations, which, as it is widely accepted, plays an important role in the enterprise regulation with some specificity for social enterprises<sup>37</sup>.

No general rule is indeed provided for associations and foundations in the Italian civil code, while social co-operatives fall under company law under this respect. This means that the regulation concerning accounts books, balance-sheets and accounts monitoring widely varies according to the company regulation which is applicable (stock company, limited liability company)<sup>38</sup>, to the administrative model which is adopted<sup>39</sup> and to the size of the firm<sup>40</sup>.

A possible (and eventually partial) integration may be represented by the general regulation concerning so called ‘commercial enterprises’ (see

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<sup>36</sup> An exception would be represented by pension funds associations, which may be included in the latter group.

<sup>37</sup> Also in a regulatory perspective, see Matacena (2002, pp. 44 ff.), *passim*.

<sup>38</sup> See art. 2519, civil code, which makes norms concerning stock and limited liability corporations applicable to co-operative corporations. While all stock corporations shall have an internal auditing body, limited corporations shall introduce this body only under certain circumstances related to size and business volume.

<sup>39</sup> If the stock corporation regime is applied, then the duty to recur to external auditing may depend on the choice of certain administrative models (part. the so called ‘dualistic’ and ‘monistic’ model); moreover or listed companies are subject to external auditing.

<sup>40</sup> In fact in many cases the regime for small enterprises will be applied, which means that the balance-sheet will be extremely lacking in information (see art. 2435-*bis*, civil code). See also art. 15, l. 59/92, which submits co-operatives which exceed certain limits in revenues, shares or other financial assets to inspection and external certification of balance-sheets.

articles 2188 ff., civil code, and articles 2214 ff. on accounts book-keeping). Indeed, these provisions would be applicable to any entrepreneurial activity, notwithstanding its nature (either lucrative or not lucrative).

The lack of regulation for associations and foundations is only partly covered by the special legislation concerning voluntary organisations<sup>41</sup>, social promotion associations<sup>42</sup> and non-profit social purpose organisations<sup>43</sup>: not just because they do not specifically regard social enterprises, but mainly because no guarantee exists that an association or a foundation which operates as social enterprise will fall into these groups. Moreover, all these norms only include the duty to adopt a balance-sheet, without providing any standard. In order to integrate this framework, self-regulation mechanisms could be hopefully activated on the part of the organisations<sup>44</sup>, although no guarantee can be offered.

Further checks may be required in case of provision of goods or services on the basis of agreements with public agencies and administration<sup>45</sup>, but the approach is again limited to a specific set of organisations and activities.

A more complex regulation regards banking foundations, cultural foundations, operatic foundations and pension funds. In all these cases the company model is adopted and, as to the balance-sheet, the one required for stock companies; in some cases external auditing and certification may be also provided at the request of public authority<sup>46</sup>.

Two other features are also noteworthy with respect to this group of entities. Firstly, for banking foundations and cultural foundations separate accounting statements are requested for entrepreneurial activity<sup>47</sup>: as seen, these organisations may operate as social enterprises (or include

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<sup>41</sup> See art. 3.4.

<sup>42</sup> See art. 3.1, lett. *b*.

<sup>43</sup> See art. 10.1, lett. *g*.

<sup>44</sup> See, also a part from any consideration of entrepreneurial activity, the Donation Charter promoted by Sodalitas (see: [www.sodalitas.it](http://www.sodalitas.it)). The organisations that subscribe the Charter commit themselves to the respect of fiduciary duties towards donors and beneficiaries.

<sup>45</sup> See, for voluntary organisations, Law n. 266/99, art. 7.2.

<sup>46</sup> See Legislative Decree n. 153/99, art. 10.3, lett. *b*, on banking foundation; Ministerial Decree of November 27, 2001, art. 13 on cultural foundation.

<sup>47</sup> See Legislative Decree n. 153/99, art. 9.3. The same distinction between entrepreneurial and institutional accountancy is included in the proposal drafted by the Orlando Foundation for the reform of foundations and associations as regulated in the first book of civil code (see art. 8.1, lett. *d*).

social enterprise within their activities) but may be not considered social enterprises as such. Then provision of separate information according to the nature of the activity seems definitely appropriate. Secondly, the law on banking foundations requires a sort of social balance sheet with the purpose of making clear what the social objectives of the organisation are and to what extent they have been accomplished throughout the year. Separate evidence with respect to the different classes of beneficiaries is also requested<sup>48</sup>.

Scholars have widely documented the relevance of social reporting by social enterprises and non-profit organisations (amongst others)<sup>49</sup>. The issue is whether the legislator should be in charge of promoting or even imposing this step while regulating social enterprises. This question will be examined later.

Accounts and social reporting and balance-sheet definitely help the organisation in reaching an adequate level of transparency, but are not the only profile to be considered. In order to be really accountable towards its stakeholders, the policy of openness should also be applied to the organisation as such. A focal point is whether and to what extent members and non-members (external stakeholders) may access information about decision-making processes or other relevant facts, activated without their participation. From this point of view some laws include general principles of openness as applied to the assets management or to organisation as such<sup>50</sup> or specific rules about access to documents<sup>51</sup>. This normative approach is not globally adopted, however, in the area of non-profit organisations and social enterprises. Again, a hint for the debate about new legislation.

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<sup>48</sup> See Legislative Decree n. 153/99, art. 9.1 and 9.5.

<sup>49</sup> Sacconi (2000); Colombo (2003). With specific reference to the proposal commented on herein: Maticena (2002); Fiorentini (2003, p. 24); Sacconi (2003, p. 48).

<sup>50</sup> Several references to this principle emerge within the law on banking foundations: see art. 3.4 (about the modes of activity in general); art. 4.1, lett. *g* (about the decision-making process within directing, administrative and monitoring bodies); art. 5.1 and 7.2 (about assets management); art. 9.5, lett. *a* (about accounts statements and balance-sheets).

<sup>51</sup> See article 2545-*bis* civil code, about co-operative members' rights of information and access to documents.

### 3.3. Liability rules

The application of liability rules towards the organisation as such as well as towards its directors is also critical. In principle, according to general contract and tort law, any organisation may be liable towards its members or third parties. Additionally, as a social enterprise, the activity may entail a higher risk of damages given that more resources and processes are probably involved. Professionalism also calls for stricter responsibility since higher standards of conduct need to be enforced accordingly in terms of liability. Furthermore, social enterprises also tend to deal with non pecuniary losses more frequently than is the case with other types of enterprise: this is because of the nature of the services provided, which in many cases are aimed at benefiting the individual, whilst at the same time having potentially detrimental effects.

This means that, on the one hand the entrepreneurial nature of the organisation may call for a stricter standard in terms of liability rules; on the other, however, the recovery may be critical if the loss is merely 'personal': then preventive measures may be preferred.

In order to analyse the regulation which is currently applicable to social enterprises, it is useful to distinguish liability of the organisation from liability on the part of its directors. In this latter case we will also distinguish between liability towards the organisation (and its members) and liability towards third parties.

As to the former, tort and contract liability rules will include a higher standard of diligence due to the organisational structure of the misfeasor or party which caused the damages. No provision is stated in these terms; however, court law often applies this criterion<sup>52</sup>. No distinction emerges between profit and non-profit organisations, but it seems quite clear that the entrepreneurial nature of the organisation matters under this respect.

Additionally, so called 'administrative liability' should be considered. It concerns the ability of private organisations (notwithstanding their profit or non-profit nature or their legal form) to prevent certain crimes by

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<sup>52</sup> See, for example, on medical liability: Cass., August 4, 1987, n. 6707; Cass., November 22, 1993, n. 11503.

adopting ethical codes or other measures<sup>53</sup>. Though not conclusive, the entrepreneurial nature of the organisation may increase the alarm for such crimes thus inducing the adoption of specific safeguards as required by law. As to directors' liability the scenario is more varied. Indeed, two models emerge: one relating to non-profit organisations regulated under the first book of civil code (mainly, associations and foundations) and one referable to companies (including co-operatives and social co-operatives).

The first model is derived from contract law. Indeed art. 18 c.c. refers to the regulation of mandate (see art. 1710 c.c.), which bases the liability rule on a duty of care, also lowering the standard in cases in which services are gratuitously provided by directors (which may be the case in many social enterprises).

The second model includes a professional liability rule, which means that the standard of conduct is higher since it considers the due skills and competence which can reasonably be expected of an entrepreneur. This standard has been already applied by the courts in the past, although an explicit norm was absent<sup>54</sup>; however, the recent reform of corporate law has incorporated this standard into the new text of art. 2392 c.c.

The same standard applies either in favour of the organisation as such and in favour of its members or third parties and creditors as single plaintiffs. Provision for this complex set of actions is only explicitly given under corporation law. However, some authors tend to extend the same regulation to non-profit organisations<sup>55</sup>. What is critical in this respect is to identify a 'qualified interest' in order to award standing to the plaintiff. When a contract between the organisation and a third party does not exist, the identification of this interest may be difficult.

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<sup>53</sup> See Legislative Decree n. 231/2001, part. art. 6, where organisational measures, also consisting of codes and disciplinary regimes, are mentioned as defences of the entity against its liability for crimes committed within the organisation and with its benefit.

<sup>54</sup> See Cass, April 4, 1998, in «Giur. it.», 1999, c. 324; Trib. Milan, February 10, 2000, in «Giur. comm.», 2001, II, p. 326; Trib. Rome, April 8, 2003, in «Giurisprudenza di merito», 2004, p. 707.

<sup>55</sup> See Galgano (1969a, pp. 263 ff.); De Giorgi (1999 p. 397).

### 3.4. Insolvency and liquidation

An adequate bankruptcy regulation supports the enterprise since it reinforces the protection of creditors and, prospectively, their willingness to award credit to the organisation by entering financial, sale, labour contracts and such like. The current Italian bankruptcy regulation applies to enterprises in general, without distinguishing between for-profit and non-profit enterprises.

The application of the general regulation to co-operatives (including social co-operatives) is not questioned. More critical might be the issue concerning social enterprises carried by associations and foundations.

Except for operatic foundations (whose regulation includes a mandatory liquidation procedure for foundations which carry out entrepreneurial activities<sup>56</sup>), no specific rule is provided for foundations and associations and the one of non-recognised associations does not even provide a rule about liquidation process. Moreover, the liquidation regulation which applies to foundations and recognised associations does not include any special reference to entrepreneurial activity and it is not clear whether (and how) a procedure might be activated (by public authority, for instance) in the event of insolvency. The law on banking foundations attributes the power of liquidating the organisation to the public monitoring agency, also including the possibility of applying the mandatory enterprise liquidation procedure (already seen for operatic foundations) as an alternative to the ordinary liquidation process generally applied to foundations<sup>57</sup>.

In dealing with a poor regulation, case law has tried to overcome some of the limits here presented. The outcome is critical however. Firstly, courts hold that, whenever non-profit organisations perform entrepreneurial activities as the sole or principal activity of the organisation, then they fall under the enterprise regulation, including bankruptcy<sup>58</sup>. Sec-

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<sup>56</sup> See Legislative Decree n. 367/96, art. 20.

<sup>57</sup> See Legislative Decree n. 153/99, art. 11.

<sup>58</sup> Cass., June 20, 2000, n. 8374; Trib. Milan, July 16, 1998, cit. This doctrine, distinguishing between principal and marginal activities, is mainly referable to Galgano (1969b, pp. 87 ff). For a different approach, calling for a wider application of the enterprise regime also with respect to 'instrumental' enterprises, see Fusaro (2002) and the proposal of reform on the first book of civil code drafted by the Orlando Foundation (see art. 8.1, lett. *e*).

ondly, they also tend to overcome the limited liability regulation which would apply to foundations and so called ‘recognised’ associations, whose creditors might levy only on the assets of the organisation, but not on the ones of members or directors. In fact, in case of bankruptcy some courts have seen in directors’ behaviour a violation of the aim of the organisation so that also the benefits of limited liability regulation, as linked with that scope, could not be retained. What follows is that courts qualify the enterprise as undertaken by the single directors as such in the form of a *de facto* company or a non-recognised association, which means that these persons are liable with their own assets, too<sup>59</sup>.

The framework is not clear indeed. It cannot be said (and courts do not imply) that, whenever the enterprise becomes the principal or sole activity of the non-profit organisation, then the non-profit scope is violated and the original legal form cannot hold anymore. However, it seems clear that, in case of non-profit enterprises (and even more in case of social enterprises) the application of a limited liability regulation (especially within the bankruptcy procedure) is critically linked with the fulfilment of the aim of the organisation. Indeed, if seen in the perspective of corporate law, either for actual lack of norms or for lack of clarity in the discipline, the law of non-profit organisations does provide a limited liability regulation (this being that of foundations and recognised associations) without imposing any severe rule which would assure the ability to solve one’s obligations towards creditors<sup>60</sup>. The uncertainty about the conditions under which the bankruptcy regulation would apply and about its extension to the single directors or managers reinforces this legal weakness.

A further issue is whether the ordinary bankruptcy regulation is anyway suitable for social enterprises or should different importance be attached to specific aspects. Examples might include the continuation of the activity as well as the effects of the procedure on pending contracts: given the nature of rights and interests involved in social enterprises’ activity and the difficulty that the workers and beneficiaries might encounter in seek-

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<sup>59</sup> App. Palermo, April 7, 1989, cit.; Cass., September 18, 1993, n. 9589; Trib. Milan, July 16, 1998, cit.

<sup>60</sup> The regulation about administrative recognition of foundations and recognised associations includes a requirement concerning the adequacy of the assets with respect to the fulfilment of the purpose (see Presidential Decree n. 361/2000). However, the requirement is quite generic and no control exists with regard to its persistence along the life of the organisation.

ing alternatives in the market, the balance between creditors' and other stakeholders' interests might be different in the case of social enterprise. Specific solutions should be sought<sup>61</sup> and special attention be given to the use of asset partitioning within insolvency procedures and, prospectively, already along the ordinary course of social enterprises<sup>62</sup>.

#### **4. The proposal of a law on social enterprise: questions and perspectives**

The above analysis has shown the weakness of the current legal framework which is applicable to organisations that may undertake or represent as such social enterprises. Sometimes the weakness is due to lack of norms, other times to lack of clarity or coordination between the various sets of regulations<sup>63</sup>. A specific regulation concerning social enterprise might help to tackle both problems, also promoting its legitimacy and its role within the law and recognising that many legal forms are already available for the purpose.

To what extent is the proposal currently being discussed by Parliament an adequate solution to the previously examined needs for regulation? Can the concurrent proposal drafted by the Orlando Foundation suggest any improvement along this path?

The core analysis will be developed with respect to the former proposal. However, some comparative remarks will be made with respect to the latter document too.

Two aspects shall be preliminarily considered.

Firstly, both the proposals aim at a law of principles and directives. If enacted, the Government will be in charge of adopting 'delegated regulations' according to these principles and directives, but some discretion might be granted to it. This means that, on the one side, the current evaluation cannot be conclusive, and, on the other, it is very important that the current drafting is very accurate.

Secondly, according to the Government proposal, the law is intended to

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<sup>61</sup> See also article 28, civil code, which states that, when the purpose of a foundation has been accomplished or has become impossible or useless, then the public authority may convert the aim of the foundation maintaining it as closely as possible to the original one.

<sup>62</sup> See Cafaggi and Iamiceli, forthcoming.

<sup>63</sup> On this latter profile see also Sestini (2002, p. 16).

complete (but not substitute) the current legislation on non-profit organisations and co-operatives, so that the Government will also be in charge of co-ordinating the various sets of regulations. In this perspective it could be advisable that the number of special (and hitherto incomplete) regulations decrease, so that the consolidated framework might also be clearer for legal practitioners, scholars and organisations themselves.

By contrast, the Orlando Foundation proposal would directly reform the first book of civil code: although not excluding the difficult task of coordinating the new regulation with the various special laws on non-profit organisations (not directly affected by the proposal), the new dispositions about “collective interests enterprise” would already be part of the general regulation about associations and foundations. This would partly help the overall understanding of the legal framework about non-profit enterprise. However, a new source of fragmentation would still concern the relationship between the associative or foundational model, on the one hand, and the co-operative model of social enterprise, on the other: an acceptable compromise? Is this the sign that the latter model is already adequate, while the former needs to catch up with the task of a modern legislation? Or does it represent an attempt of distinguishing two realities that have not (or should not have) much in common? The former approach would be more acceptable than this latter one: then a new effort of coordination would be necessary.

The Orlando Foundation proposal distinguishes itself from previous reform projects on the first book of civil code, because it differentiates between non-profit enterprise and collective or general purpose enterprise. However, it does not directly determine what “collective and general purpose” means<sup>64</sup>.

The Government proposal defines a social enterprise as a non-profit private organisation which permanently and principally carries out an economic activity aimed at the production and distribution of social

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<sup>64</sup> In fact art. 2.1, lett. *c*, does draw an explanatory (and exemplary) list of features that, in any case, attach a collective or general purpose label to the organisation. To carry out a collective or general purpose enterprise is already one of these features as such. Other features (that are presented as alternative but may also help to understand what collective or general purpose means, operating as crossing references) include receiving public or community contributions, mainly relying on voluntary human resources to achieve social goals, to manage assets which were donated to pursue social goals.

benefit goods and services, and pursuing general interest goals.

It also states that the social feature of the enterprise shall be defined with respect to:

- special social value of interest areas in which the organisation operates in order to provide goods and services to beneficiaries with no exclusion for non-members;
- non-distribution constraint (also covering indirect distribution) so not to allow any speculative connotation of the participation in the enterprise;
- a duty to reinvest profits or residual revenues in the institutional activity or to integrate the assets;
- capital and governance structure: public and for-profit entities cannot 'control' the organisation, also considering the power of appointing the majority of directors.

Focusing on this introductory definition, it seems clear that the legislator is opting for a functionalist approach rather than selecting (or even introducing) a specific organisational form to define what a social enterprise is under Italian law: then the focus is on the general interest goals pursued by the entity and the economic activity in the sense of the production and distribution of social benefit goods and services. What is critical, however, is that the criteria to be adopted in defining the social function and the social benefits goods and services are not stated, except for a general reference to 'areas' (which ones in fact?)<sup>65</sup> and a negative statement about the exclusion of non-members, which indirectly and not conclusively sheds some light on the idea of organisations also aimed at producing positive external effects. A form of path dependence from current legislation about non-profit social organisations and bank foundations (which, among others, define the organisations in terms of areas of interest) will be quite likely in fact. This approach is not censurable as such but it is definitively not sufficient to assure the social nature of the organisation and of the goods or services provided. In this respect a more direct link between the function and its modes should be drawn: principles like equal treatment or general rules like transparency or accountancy methods like social balance sheets seem much more meaning-

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<sup>65</sup> For a critical view on this solution: Borzaga (2002, p. 12).

ful than the areas of interest as such. Also a more specific definition of social goals, maybe considering social inclusion or benefits for disadvantaged people, might help to clarify what social enterprise should be.

Also the exclusion of any minimum distribution of profit is critical. Indeed it might limit the opportunity of collecting financial resources from people who, although not involved into the governance and the running of the enterprise, are willing to redirect part of their savings or investments in social benefit goals though not giving up any expectation of reimbursement or remuneration, however low. This different approach would not attach any speculative connotation to the entity while enlarging the set of possible financing stakeholders of the organisation<sup>66</sup>.

Moreover, a closer look at the recent regulation of financial markets and corporations would suggest that the distinction between equity and debt (only the former giving right to profits) has become more and more blurred: then it could be ineffective and contradictory to prohibit distribution of profits and to allow other forms of financing through the issue of debt, while to exclude these latter ones, too, does not seem appropriate given the problems faced by many social enterprises in financing their activity<sup>67</sup>. In fact this is a profile on which the current proposal does not make any effort either to clarify to what extent social enterprises may access to the new forms of corporate financing and (which would be even more appropriate) to promote specific financial means for these organisations<sup>68</sup>.

The focus of the non-profit feature is also confirmed as regards the capital structure, thus prohibiting for-profit and public entities from 'controlling' the social enterprise. Again, a sort of 'purity' of the model is defended, considering that a so-called 'control' by diverse entities could itself alter the nature of the social enterprise<sup>69</sup>. In fact it might be questioned whether other measures than an outright ban could avoid that a

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<sup>66</sup> See also Fazzi (2002, p. 31), on the importance of attracting financial capital on the basis of a fiduciary relation with the financier which incorporates the (social) mission of the enterprise.

<sup>67</sup> See, for a general and up-to-date view on non-profit financing, also with a view to the promotion of capital financing, Centro Ricerche sulla Cooperazione (2004).

<sup>68</sup> See, for a critical note on this profile, Cafaggi (2003, p. 11).

<sup>69</sup> A different but related limitation is drawn by the Orlando Foundation proposal with respect to the additional and marginal enterprises that can be undertaken by the association or foundation operating as social enterprise and also regarding the (for-profit) companies in which the same association or foundation may have shares.

social enterprise pursued the interests of a for-profit organisation or a public administration rather than the ones of its stakeholders. In fact, if asset partitioning was strictly enforced<sup>70</sup> and specific policies on conflict of interests were enacted, a more flexible approach could be taken, also favouring a broader intervention by for-profit organisations in general interest areas<sup>71</sup>.

The issue is also linked with a further question covered by the proposal concerning 'groups' of social enterprises. In a context in which it is already clear that entities do not operate as autonomous entities, but more often are included or even generated within networks characterised by various levels of hierarchy, it could be difficult to interpret and regulate the entity assuming a sharp distinction between for-profit and non-profit networks or groups<sup>72</sup>. The need for a more complex and comprehensive approach might become even higher if the concept of social enterprise is enlarged so as to include not only entities as such but segregated assets within the assets of one or more entities<sup>73</sup>.

Whatever the approach, an important issue is on the table, although it is not clear whether and how it will be tackled by the legislator: how to define 'control' with respect to social enterprises. The origin of the assets (pertaining to the so-called 'controller') may be one of the criteria, especially where it is concentrated in one or few entities, but it seems clear that, despite this 'origin', the control may be elsewhere. Other aspects have to be considered then: the power of appointing directors, as the proposal already states, but also the power of changing the articles of the organisation, the power of liquidating it, the power of approving budgets and balance sheets and other pivotal rights.

Given the nature of the law of principles and directives, the proposal does not go deep enough into many of the above-mentioned issues un-

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<sup>70</sup> See Cafaggi and Iamiceli, forthcoming.

<sup>71</sup> See also Travaglini (2002, p. 65 f.), who favours the participation of public and for-profit entities in social enterprise networks, even if these are controlled by non-profit entities; Fazzi (2002, p. 33), who, without questioning the *ratio* of the proposal under this profile, doubts about its effectiveness, provided that for-profit organisations may directly operate in social interest areas.

<sup>72</sup> On the tendency of non-profit organisations to be part of groups or networks, see Cafaggi (2003, p. 9). On groups of social enterprises, see article 1.1, lett. *f*, where principles of transparency and minority protection are stated and policies on conflicts of interest and abuse of dominant position are also mentioned as topics due to be covered by forthcoming legislation.

<sup>73</sup> See Cafaggi and Iamiceli, forthcoming.

der the four selected profiles. Some suggestions can already be made, however, at this stage.

1. One of the focal point of regulation regards the participation of the stakeholders in the governance of the enterprise, although it is not clear which forms will be introduced by the legislator or only promoted and then eventually adopted by the organisations.

This participation is not limited to but is especially requested as regards workers and beneficiaries (as customers or recipients of goods or services provided). It seems that a broader approach could hopefully be adopted, also considering donors or other financiers, especially regarding ethical financing. A broader notion of the beneficiary could also be considered, especially when the social enterprise benefits the community at large and not single (classes of) individuals.

This is probably a field in which self-regulation should be promoted without imposing specific forms of participation or standard definition of stakeholders. Important measures should be requested however, in order to make such self-regulation effective; among which: that the organisation explicitly states what the forms of participation are and how they can be accessed; that the organisation provides all the information in order to exercise these rights; that specific procedures are enacted in order to prevent or regulate conflicts among stakeholders and between the stakeholders and the organisation. It is not clear whether the prospective regulation will entail all this. Some ideas can also be gleaned from the Orlando Foundation initiative, although not specifically related to social enterprises<sup>74</sup>.

2. The issue related to transparency and accountability is also considered by the proposal. Then, besides economic balance sheets, social balance sheets are also required and other forms of accountancy and social monitoring. As seen before, it would not be the first time that social accoun-

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<sup>74</sup> Concerning associations or foundations that pursue collective or general interest goals see, art. 4.3 (second paragraph), lett. *d* (on separate assemblies in associations), art. 6.4 (on the composition of a mandatory directing body - *organo di indirizzo* - which represents the different classes of interests involved into the activity of the foundation) and art. 6.3, second paragraph, lett. *b* (which states that at least one third of the directors should be appointed taking into consideration the type of interests involved into the activity of the foundation).

tancy is imposed by law<sup>75</sup>; however, a substantial effort by organisations needs to be made in order to develop adequate systems in practice, given their delay on both levels.

By contrast the Governmental proposal does not adopt the rule of separation between entrepreneurial and not-entrepreneurial accountancy, as already seen regarding banking foundations<sup>76</sup>. In fact this solution could enhance the transparency level of the organisation in cases in which the enterprise is the main, but not the only, activity carried out by the entity. Within the forms of monitoring favoured by accountability, the duty of establishing a monitoring body should also be mentioned<sup>77</sup>. Especially in the absence of an assembly or where forms of direct participation for the different classes of stakeholders are lacking, this feature helps to create some balance within the organisation and itself increases the accountability of the enterprise. Individual access to information could also be a critical point, while it is not mentioned under the Government proposal<sup>78</sup>.

3. The list of topics due to be regulated by the Government also includes directors' liability (towards members and third parties). Given the fact that a monitoring body is also mandatory, it seems that the same (or a different) regulation should be provided also for (at least internal) auditors. No specific criterion is given by the proposal, but it is possible (and in any event preferable), that a reference regulation be the one already in force for corporations, where a professional standard has been applied to directors' liability. A lower standard would, in fact, delay the 'professionalisation' of social enterprises.

Again, however, the new regulation (as examined through the Government proposal), does not seem to consider the important case of directors' (or auditors') liability towards the entity as such, which means its

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<sup>75</sup> See also, in the Orlando Foundation proposal, but again with respect to general interest organisations (though not entrepreneurial), art. 4.5, lett. *a* (on social mission statement and reporting by associations; the disposition is strangely not repeated with respect to foundations).

<sup>76</sup> See § 3.2. This is the solution proposed by the Orlando Foundation (see art. 8.1, lett. *c*).

<sup>77</sup> See by contrast, for the Orlando Foundation proposal, artt. 4.2, lett. *c*, and 6.3, second paragraph, lett. *c* (on a mandatory monitoring body, also solicited to operate by association members or foundation beneficiaries).

<sup>78</sup> See, by contrast, the Orlando Foundation proposal, which mentions this right at art. 4.3, lett. *c* and art. 4. 5, lett. *c* (with respect to members and non-members information rights) and 6.5.1 (with respect to foundation beneficiaries).

stakeholders collectively intended. In some types of organisation this hypothesis might be covered by liability towards members (considered not as individuals but as part of the collective body which represents the entity interests). In non-membership organisations or in multi-stakeholders organisations, where the interests of the entity may not coincide with the interests of the members, that coverage is not guaranteed. A different way to interpret this issue is whether third parties may sue the directors for collective damages rather than for individual ones.

On this profile the proposal drafted by the Orlando Foundation is more accurate. It includes both professional requisites for directors and a directors' liability regulation, which incorporates special standing for minority members of associations and, in the case of associations and foundations, the power of third parties to report severe violations to a monitoring public authority<sup>79</sup>.

4. A fourth question examined above regards assets liability and bankruptcy regulation. On the former, the Government proposal chooses the limited liability regulation; on the latter, it delegates the power to define such procedures to the Government, thus clarifying that special procedures have to be enacted in the event of insolvency.

The limited liability solution is quite acceptable if read in the light of the law and economic debate: asset partitioning would indeed promote investments also protecting creditors (especially voluntary creditors), and would allow a better monitoring of directors' behaviour by circumscribing the extent of assets on which either enterprise risk and management choices have an impact<sup>80</sup>. What is less clear is whether this solution entails the adoption of specific legal forms of organisation in order to undertake social enterprise (for example, only recognised associations would be allowed and non-recognised associations would be excluded) - which seems in contrast with the open approach adopted by the proposal regarding the legal forms of social enterprise - or other measures will be defined by the legislator, like forms of asset partitioning for social enterprises.

As regards insolvency procedures, the reference included in the proposal is definitely insufficient, this also being a critical and complex regulation

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<sup>79</sup> See art. 4.3, second paragraph, lett. *a*; art. 4.5, lett. *d*; art. 6.5.3.

<sup>80</sup> See Cafaggi and Iamiceli, forthcoming; in more general terms, see also Iamiceli (2003, part. pp. 148 ff).

to be delegated to the Government with no directive at all. However, a general reform of bankruptcy law is also being discussed at this moment. Although it does not specifically consider the case of social or non-profit enterprise, a major co-ordination (or even inclusion) of this discipline with(in) the more general one could be appropriate.

Many other issues are on the table, some included or indirectly linked with the contents of the proposal, others neglected (labour law issues and the competition law perspective can be mentioned among the latter). One important question is how private organisations will react and whether social enterprise will in fact be promoted by means of a new regulation. Considering the European context makes the need for a new regulation even stronger, given that many countries are moving in this direction<sup>81</sup>; however, only the concrete application of the different legal regulation will suggest which model/s might be preferred and, possibly, whether European intervention might be expected: a challenging issue, which remains beyond the boundaries of these pages.

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<sup>81</sup> See in Belgium, Law, April 13, 1995 on the *société a finalité sociale*; in France, Law, July 17, 2001, n. 624, on Société Co-opératif d'Intérêt Collectif (SCIC); in Portugal, Law, December 22, 1997, on the Cooperativa di solidarietà sociale; in the United Kingdom, the proposal drafted by the Department of Trade and Industry, HM Treasury in March 2003, on the Community Interest Company; see an updated version of the proposal at <http://www.dti.gov.uk/cics/index.htm>. For a legal framework regarding these and other models, see Digestus (1999).

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## 8. A new co-operative form in France: Société Coopérative d'Intérêt Collectif (SCIC)

by *Alix Margado* \*

SCIC is the French acronym for “General interest co-operatives”. It is a new private, general interest co-operative allowing anyone (employees, users, volunteers, public bodies, companies, associations, etc.), wishing to act together in the framework of the same lasting local development project, to do so.

### 1. Was a new charter in French law really necessary?

The context and the stakes vary according to the regions and the countries. However, one notes that everywhere in Europe (and beyond), social and economic players are thinking about and experimenting with new types of companies which adapt to the two-fold need of creating new activities and employment, as well as protecting the interest of the parties involved and their environment in the best possible manner. The general term used to define this type of structure is a “company with a social objective” (*entreprise à but social* or EBS in French). The EBS contain and affirm what true economists call *development* which they qualify as being both *economic and social*. Unfortunately, it is well-known that the term *social* has been gradually forgotten by mainstream economic thinking and that liberalism in its caricature has limited it simply to “social works”.

Differently from the Italians who introduced a law on two types<sup>1</sup> of “social co-operatives” in 1991, or the Belgians who created “companies having a social objective” (*société à finalité sociale* or SFS for short), a type of label which could be applied to any type of business activity (company or association) in 1995, France opted to simply adapt the existing co-

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<sup>1</sup> An A-type social co-operative for those co-operatives having a social activity and B-type for those co-operatives which have any type of activity and whose personnel includes at least 30% of disabled people.

operative charter established with the law dated September 10, 1947 and create the SCIC. This position is in line with the one adopted by Alain Lipietz who in his report in response to Martine Aubri's question in 1998 on the opportunity in France of adopting a new company charter for companies having social objectives<sup>2</sup> simply stated: No!

Why is the need felt to create or adapt company charters? If one thinks about it, the needs are not new. The novelty lies in the evolution of the post-industrial context, in a global economy which together lead to changes in social organisation. The combination of these parameters requires an adaptation of the procedures and a legal and tax framework for production companies.

For the players in the social economy the importance attached to values such as solidarity, the pre-eminence of the individual over capital, etc. which emerged during the nineteenth and twentieth centuries, remains basically unchanged. At the beginning of the twenty-first century taking into account the afore-mentioned social changes, the need was felt to adapt existing legislation so as to better meet, in some cases, their needs. SCICs are the result of a pragmatic approach. It was indeed those involved in associations and/or co-operatives who asked legislators to adapt the texts, extend the existing provisions so as to ensure that they were better adapted to their objectives and their work. The laws and rules sometimes oblige them to look the other way on certain drifts which occur or require energy-consuming legal contortions. All of us are aware of associations in which a phantom General Assembly leaves important decisions in the hands of their paid director, whereas it is the Chairman who is actually responsible from the legal point of view. There are also cases in which to keep its "association project" while carrying out business activities, one, two, three branches have been created thus multiplying the management costs and confusion concerning who decides what whereas for those co-operatives seeking to integrate their customers, employees or other people it is impossible! Each type of co-operative only groups together the same category of individuals sharing the same type of objective, i.e. purchases for consumer co-operatives,

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<sup>2</sup> Lipietz Report : A report concerning the mission letter dated September 17, 1998 sent by the Employment and Solidarity Ministry Mrs. Aubry to Alain Lipietz on the need for a new type of social company - final report published at the beginning of 2000. It can be consulted on internet.

work and the possession of the production tools for the workers production co-operatives (*société co-operatives de production* or Scop); the use of materials for Agricultural co-operatives - (*co-operatives d'utilisation de materiel agricole* or Cuma), etc.

The preparation of a bill on SCICs has been exemplary in terms of pragmatism and the search for the best possible response taking into account expectations. The players in the field (17 projects followed for a period of 18 months in the framework of the *Demarche Collective d'Innovation* or DCI; the co-operative networks and associations involved; the human resources (universities, foundations, etc.)<sup>3</sup>, and the public bodies (Dies; Dgefp/Mpe, then Sees after their creation), closely collaborated to amend and validate the text which was voted by the MPs in 2001.

## 2. The laws<sup>1</sup>

*Scic legal basis :*

Law n. 47-1775 dated September 1947 establishing the statute of co-operatives (the articles concerning the SCIC are articles 19.5 to 19.15)  
articles 1832 to 1844-17 of the Civil Code which set down the general legal basis of companies.  
Articles L. 231-1 to L. 231-8 concerning the variability of capital in Commercial Law (Law dated July 24, 1867),  
Law 66-537 dated July 24, 1966 of Commercial Law,  
Law 78-763 dated July 19, 1978 (art 1 1°§, and art. 2),  
Law 84-578 dated July 9, 1984 art. 10 on the development of economic initiatives (Official Journal dated July 11),  
Law 85-703 dated July 12, 1985 (Official Journal dated July 13), decree 87-544 dated July 17, 1987 (Official Journal dated July 18),  
Law 92-643 dated July 13, 1992 (Official Journal dated July 14).

*Law 2001-624 published on July 17, 2001 - Official Journal dated July 18, 2001*

On June 28, 2001 the National Assembly during the last reading passed article 36 of a law called DDOSEC (different social, economic and cultural provisions).

<sup>3</sup> The list of the DCI projects, the members of the reflection group and the summary of the work carried out can be found on the internet site: [www.resoscope.org/scic](http://www.resoscope.org/scic).

<sup>1</sup> The law and the decree are available on the internet site: [www.resoscope.org/scic](http://www.resoscope.org/scic).

The article includes:

1. 10 articles defining SCICs;
2. they have been placed in Title II c) of Law n. 47-1775 dated September 10, 1947, after Title II b) dealing with the Union of Social Economy (Ues). These two titles stem from article 19 of Law n. 47 (articles 19.5 to 19.15);
3. the addition of article 28 to the law dated September 10, 1947 allows a “declared association” (Law 1901 or 1908 for Alsace) to transform itself in a co-operative without changing its legal status (valid for all the co-operatives);
4. The change of paragraph one of article L. 228-36 of the Commercial Law which grants access to non voting shares in the limited liability companies co-operatives (Sarl). Until the present they were limited solely to co-operatives which were joint stock companies (Sa).

*Decree 2002-241 dated February 21, 2002 - Official Journal dated February 23, 2002.*

The decree examined by the Council of State in December 2001 and published on February 21, 2001 meets the law on three points:

1. The SCIC approval procedure (articles 1 to 7):
  - the Prefect of the Department where the co-operative is located gives his approval for a five-year period; possibility of withdrawal or non-renewal of the approval if it doesn't evolve in conformity with the law or the SCIC objectives; following the request for the approval registration, if no reply is given by the Prefect's office within two months it is to be construed as an acceptance;
  - approval of the formal aspects: conformity of the charters with the law, minimum capital<sup>5</sup> and the presence of at least three categories of members, of which there must be the wage earners and the users; correctly appointed managers, pre-registration at the Registrar of Companies; a change in the Kbis form<sup>6</sup> for existing registered companies that carry out a change; if any change is made to an association the commitment to set aside the reserves and the association funds previously created into the indivisible reserves of the SCIC; if there is a renewal supply the co-operative review report;

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<sup>5</sup> Minimum capital of 3750 euro for a limited liability company co-operative and 18.500,00 euro for a joint-stock co-operative company.

<sup>6</sup> A form identifying the company issued by the Commercial Court Registrar.

- opportunity: assessment of the general interest by means of a note stating the objectives, the means and the organisation of the co-operative. Such note is compulsory and must be placed in the file containing the approval request;
  - registration in a yearly ministerial list published in the Official Journal;
  - obligation to inform the Prefect in case of a change in the statutes or subject-matter and for any other request of the Prefect concerning; the approvals, qualifications, agreements and financing, etc.
2. The conditions for the granting of subsidies (articles 8 to 12):
- conformity with CE Regulation n. 69/2001 concerning subsidies to territorial bodies granted for the development of the SCIC;
  - conformity with CE Regulation n. 70/2001 for subsidies to territorial bodies granted for SCIC investments;
  - conformity with CE Regulation n. 68/2001 for subsidies to territorial bodies granted for SCIC training activities;
  - state the areas eligible for certain subsidies;
  - state the obligations (state the object, amounts, conditions of use, list and minimum amounts collected in the last three years - reimbursement in the case of improper use).
3. Co-operative review obligation (article 13): the decree dated November 23, 1984 concerning co-operative review applies to SCICs.

*Ministerial circular*

The circular dated April 18, 2002 sent to the Departmental Prefects offers some explanations on the three points of the decree: approval, subsidies and co-operative review.

### **3. Legal novelties of the SCICs**

We have already stated that the SCIC is not a new legal charter fundamentally different from the many existing charters. It is simply the adaptation of the Law dated September 10, 1947 concerning the co-operation charter. Consequently, it adopts all the prerogatives and it shares with all the co-operatives the same type of structure, constraints and opportunities. However, to meet the expectations which were outlined and simultaneously grant them a regulatory framework, the SCIC introduces some

important legal novelties in the co-operative world and special provisions which differentiate it from all other companies.

*Special SCIC provisions:*

1. the SCIC definition once again highlights the link between economic development and social development: article 19.5 - The SCICs are limited liability companies or joint-stock companies with a variable capital governed, by the provisions of this law, and by Commercial Law. Their objective is the production or the supply of goods and services having a general interest and offering a social benefit;
2. non-profit aspect of the SCIC: the law imposes the setting aside of at least 57.50% of the profit to the indivisible reserves and no derogation whatsoever is permitted to the above. Any public aid is not taken into account in calculating the interest paid to the social partners (article 19.9 of the law);
3. the Departmental Prefect where the SCIC is located must issue an approval before the commencement of any activity. The approval has a duration of five years, is renewable and can be withdrawn (article 19.13 of the law and articles 1 to 7 of the decree);
4. any declared associations can be transformed into a SCIC without changing its legal status (art. 19.14 of the law concerning companies and article 28 a) concerning associations);
5. the co-operative review is compulsory (article 19.20 of the law, specified in article 13 of the decree);
6. public bodies can, if they wish, and if the assembly of the members agree, take some of the share capital of the co-operative without the need of the approval and examination in the Council of State - differently from what is required for other private companies - maximum of 20% of the capital for all the local community organisations (article 19.7 of the law);
7. SCICs may receive subsidies from the local community organisations (article 19.10 of the law). The conditions for the granting of such subsidies are set down in the European regulations dated January 2001 (articles 8 to 12 of the decree);
8. an employee who is appointed manager or CEO maintains his statute of wage earner as occurs in the Scop. However, if the person appointed manager did not previously have an employment contract

with the co-operative, the classic regime of social proxies is applied (article 19.11 of the law);

9. a certain number of approvals, qualifications and agreements which had previously been solely limited to associations are now accessible to the SCICs. For example the CES, employment laws for young people (article 19.15 of the law).

*Novelties for co-operatives:*

1. opening up of the entire activity to third parties, non-members of the co-operative (article 19.6 of the law);
2. multi-partner aspect of the SCICs: the members of a SCIC must include at least three different categories of people (natural and/or legal); having a different relationship with the activity being carried out. Such minimum number must compulsorily include the users (clients, beneficiaries) and the wage-earners of the co-operative. Beyond the minimum of three categories the multi-partner aspect of the SCIC is open to any natural person and any private and/or public legal person (article 19.7 of the law);
3. colleges of members can be created to govern the General Assembly, as long as the principle of “one man one vote” in the College Assembly is complied with. However, the votes of the members must be weighed when there is the report on the results of the vote of the different colleges in the General Assembly (article 19.8 of the law).

#### **4. Social benefit, multi-partner aspect and territory**

The social benefit is not defined by the law on the SCICs. It is a concept which goes beyond it, it doesn't belong to it, but it fits perfectly in it. Social benefit can only be considered with reference to a specific environment and taking into account human, geographic, cultural, political, economic parameters, otherwise who would benefit, who would be interested in it and on what basis would it be qualified?

The multi-partner aspect of the SCIC, its capacity to enhance co-decision taking by people having a different relationship to the same activity, no matter what its activity, is the cornerstone of this new type of co-operative. It is its trademark and the guarantee that the SCIC's activity is well-rooted in the territory in which it operates.

The SCIC is a production co-operative, a trading company. It turns to its customers. It is a partner to its suppliers. It uses the services of those who fund it. It organises a production process. It reaches agreements with public political bodies, and it can enter tenders or sub-tenders with other social and economic players. It prepares a sales strategy. It is well-rooted, it has an impact on a clearly identifiable economic and social environment. This is the SCICs area of intervention which thus comprises concepts such as customer catchment area, customer target, etc. and it is in and on this territory that the analysis of the needs and resources according to which the SCIC shall propose and organise its activity is carried out.

The appreciation of its social benefit depends among other things on:

- the product or service offered;
- its production organisation;
- ease of access of its products by the greatest number of people;
- its capacity to mobilise different categories of players;
- its degree of democracy and transparency in management;
- the quality of the positive effects on its environment (the economists call it “positive externalisation”).

Make the greatest number of people be present and become players. They will first exchange views on their special interests and then finally decide to act together - what a public spirit ideal! In the SCIC, in a given territory and for a given activity this ideal must be attained.

This explains why the participation of different partners is envisaged.

This also explains why there must always be a minimum of three categories. The producers and the consumers are deeply involved.

Whereby the possibility (not the obligation) to bring together public bodies which by their very nature are very attentive to any activity concerning the greatest possible number of people, the general public and the area.

The SCIC is indeed the entire community. It is not merely a self-centred group involving solely its members. Every co-operative and association legitimately has this type of self-centred objective vis-à-vis its associate members. It is part of their logic and reason of being. In the world of associations however there are many groups which have set down for themselves completely altruistic objectives (associations operating for the

public benefit; charitable, humanitarian, human rights associations, etc.). Consequently, we tend to have the idea whereby collective altruism can only be brought forward by associations. We adorn “association projects” of all the virtues whereas a company which states it wishes to “offer its services to the community” is looked upon with suspicion.

The preamble of the law before the National Assembly voted during its first reading on May 10, 2001 speaks about “... the altruistic ends of this new co-operative society which distinguishes itself from a classic co-operative in the fact that its objective is not simply to satisfy its own members but also a wider public for whom it wishes to satisfy the needs”. The co-operative exception envisaged in article 19.6 meets this altruistic objective. Indeed, it authorises the SCIC to deal with third parties with no limitations whatsoever, differently from all the other types of co-operatives in which the activity mainly concerns its members. This is one of the reasons justifying the need for an approval and the five-yearly review of the co-operative approval. The shared reflection with other networks on the results of these co-operatives shall give the SCIC evaluation instruments of communication and transparency on their altruistic vocation (as well as on other social benefit aspects which have already been mentioned).

The SCIC is thus a company, a trade company whose business is that of carrying out an economic activity capable of creating employment in a manner and with objectives which shall satisfy the needs of a territory which is identified by the players of the SCIC themselves.

The clearer and the more consistent the project, the greater the number of people willing to adhere to it. The greater the number, the more the needs of the territory have the possibility of being better represented.

The consequence of being deeply rooted in the territory enabling the real expression of each one's opinion is the limit to the SCIC's territorial development. To act and understand what is happening in the co-operative each member must be able to see its boundaries, position each interest group, be able to listen to the voice of its collaborators. There is no absolute limit. Each SCIC project must however ask itself: starting from what point does the SCIC risk endangering its real internal democracy, its capacity to be “in touch” with the evolution in the needs of the territory instead of privileging no matter what the price the existing activity?

Is it justified to extend one's customer catchment area instead of setting up another SCIC project in a nearby area and transfer to the local players some of the knowledge acquired with the first SCIC? The Italians use the image of a strawberry field, of the layering and spreading to explain how the company having a social objective must develop. The crossed participation, the establishment of second-level co-operatives thus result in greater economies of scale, investments and market shares.

Consequently, under the pretext of being close to its territory the SCIC is not condemned to remain in the micro-economy. It is simply intended to be cloned and to create a network to ensure a development which is consistent with its objectives.

## **5. Power in the SCIC**

If the SCIC is characterised by its partnership aspect and its roots in a territory, so as to best ensure the general interest, the result is an obligation to manage such partnership in a dynamic manner: a phantom-like Board of Directors should not exist in a SCIC. The presence of at least three categories of members is one of the pre-conditions for its very existence. The SCIC cannot do without promoting the interest of the wage earners, customers, etc. If one of the three categories envisaged were to disappear the SCIC too would disappear.

The transfer of information and the training of its members are absolute necessities (and expenses which are to be put in the SCICs budget).

The co-operative principle of "one man one vote" ensures that everyone has their say. It is the system which applies by default in the SCIC. Why then authorise the introduction of "colleges" as per article 19.8 of the law? The reason is that we all know that an individual's opinion varies according to the group in which he speaks. As for the general interest, it is interesting to put forward principles of democracy which are not simply the arithmetic sum according to which the numerical majority decides and the decision is thus considered to express the interest of the majority.

The fact that each individual within a group can express his opinion and that discussions among the groups are stimulated is a clear indication that each group exists beyond the simple numerical sum of the individu-

als it represents. The expression of a group is an important element of democracy which does not cancel individual opinions. The decisions taken by a General Assembly of an association or a company are a case in point as are more or less spontaneous, more or less short-lived protest marches in the streets.

The college introduces an intermediary between the individual member and the General Assembly. It is an additional stage in learning the collective decision-taking process. The co-operation between individuals is experimented and it benefits from the mental or symbolic representations found in our society. Group-to-group co-operation is more difficult to circumscribe. It shall express itself in the SCIC among other places but at present at a time in which the first approved SCICs are appearing it is yet too soon to pass a judgement.

The creation of colleges, intermediate stages in the collective decision-taking process appears to be complicated to some. The players who participated in the DCI see it as a wise instrument for power management and the legislator has agreed. In the philosophy behind the law dated July 1901 on associations, the law dated July 2001 on the SCICs gives those who formulate the charter great freedom in adapting the power organisation within the company. Granting the same vote percentage to colleges having different numbers of members or giving them a weighted average through unequal percentages set down in the charter implies rationing the decision-taking power.

According to which criteria? Here too, the legislator has granted those formulating SCIC charters full freedom as far as the creation of colleges and their relative weight are concerned.

The only obligation is that if colleges are created (it is an option) they must be at least three in number. Moreover, if different percentages are envisaged for the report on the results of the college assembly votes in the General Assembly they must be between a minimum of 10% and a maximum of 50%.

The only limitation: above the discriminatory criteria of common law the criterion for the creation of a college cannot be based on a consideration linked to the capital possessed by the members.

The SCICs which have been or are being established show that there are different ways to tackle this issue. The solutions chosen can be modified.

An extraordinary General Assembly can change the number of colleges, the vote percentage and the establishment criteria. After the issuing of the decree in the public meetings organised in the entire territory and in meetings with those executing the research projects after having overcome the initial surprise, the infatuation for the freedom to organise power as one wishes through the colleges is confirmed.

The legislative framework is also a guarantee against instrumentalisation or the take-over of power by a single college (unless everyone unanimously agrees since the provisions creating the colleges and their duties are voted by an Ordinary General Assembly in which all the members' votes are equal).

Warning. One must however organise power structure within the co-operative. The college is not a working committee or an exchange group. It is one of the moments of the General Assembly and it must therefore express the opinion of a certain group to contribute to increasing the efficiency of the company. The establishment criteria must take into account the need of reaction imposed by the trade and entrepreneurial nature of the SCIC.

## **6. Very limited profitability**

The considerations concerning companies with a social objective shared with our European neighbours in the Digestus European Framework by the Cecop<sup>7</sup> and the Italian co-operation in 1998-99 had initially concluded on the need for such companies not to have any profitability whatsoever.

The non redistribution of profits and their total reinvestment in the business activity are a part of the afore-mentioned altruism. However, when the firm with a social objective takes the form of a company albeit a co-operative company as is the case of the SCIC one cannot hide and overlook the notion of capital. In co-operatives the individual is pre-eminent to capital. Capital thus ranks second, however it is not secondary. Capital is necessary for the establishment and the existence of a co-operative company.

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<sup>7</sup> Cecop: European confederation of production and associated work co-operatives, social co-operatives and participating companies.

It commits, on the basis of one's contributions, the responsibility of each individual member be it a natural person or a legal entity. This is why, as is the case in other types of co-operatives in France, the SCIC can pay a share in the profits to the capital shares. The law dated September 10, 1947 puts a ceiling on the interest paid to the quotas at the average yield rate of bonds of private companies which is set yearly by the Economics and Finance Ministry (TMRO). In the SCIC the possibility of paying part of the surpluses has been subjected to strict limitations. The law sets down that at least 57.5% of the net management surpluses must be set aside in the reserves which constitute the real collective and indivisible wealth of the co-operative.

The law authorising the SCIC to receive public aid (under regulated conditions) admits that the surplus obtained thanks to the aid can be granted to the collective property of the company. On the other hand, it does not admit that such public aid may be used for personal gain. Consequently, after having directed 57.5% of the surpluses to the reserves, the SCIC General Assembly cannot decide to pay interest to the shares unless it has previously removed from the balance 42.5% of the surpluses corresponding to the public aid received by the SCIC.

This is the only exception to non-profitability. It allows for the recognition of the capital instrument, and in some ways allows it to be kept like a maintenance contract for industrial or computer instruments. This exception to the total non-profitability rule enjoyed by the SCIC, is to be compared to the authorisation, which associations considered as being non-profit making, to pay their administrators or integrate salaries in the Board of Directors (authorisation which is governed by the law). One can thus speak of non-profit SCICs.

The charters and the yearly General Assembly set the interest rate paid to the shares within the limits set by the TMRO. If the charters envisage it the General Assembly may decide to pay 0%. This last possibility and the restrictions imposed by the law also have a downside: it shall be difficult for a SCIC to attract the capital it may need during an investment or development period. As is the case in other types of co-operatives, this inconvenient, which is even greater in SCICs owing to their "non-profitability" must be counterbalanced by the creation of specific financial instruments (such as the Socoden in the SCOPs, for example) and by

granting investors some advantages. The non-profitability must not be ignored by those wanting to transform an association or a company into a SCIC. The same holds true for those who accuse the SCIC of unfair competition. Not only is the interest paid to the shares limited or non-existent; not only are the shares not revaluated taking into account the company's profits (as is the case in other co-operatives), but if the company terminates its activity, the liquidation surplus shall be granted to another co-operative, association or public body. Personal gain is totally excluded from a SCIC. Should the approval be withdrawn by the Prefect, the company must remain a co-operative<sup>8</sup> since it cannot grant anyone the reserves<sup>9</sup> it has accumulated, otherwise it must terminate its activity.

## 7. General interest and public policies

A SCIC located in a territory shall most presumably not ignore the existing public policies or those which can be created in that territory (employment creation, innovation, insertion, agglomeration contract, etc.).

On the other hand, policy-makers too may express interest in a SCIC capable of taking over and carrying out their activity. However SCICs remain a private initiative. It sets for itself a common objective but its aim is to be as autonomous as possible to attain such objective as is the case for any trade company worthy of its name. Consequently if a local community is interested in a SCICs activity it can subsidise, reach agreements, conclude friendly deals or invite it to take part in public tenders. It can even acquire part of the capital and take part in the management. In such case it is responsible as is the case for any other member only according to its contribution. However, a SCIC cannot be financed using public funds: no more than 20% of the co-operative capital detained by all the territorial bodies and their groupings together.

The SCIC can have both public and private resources belonging to both individuals and groups. This is part of its nature of having as its objective

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<sup>8</sup> With changes in the charter by removing the specific elements of the SCIC and adapting those of the SCOPs if the wage-earners are volunteers and if the General Assembly agrees, or the simpler ones envisaged in co-operatives set up in conformity with law 47.

<sup>9</sup> This prevents it from becoming a limited company or a joint-stock company unless it exits the co-operative charter, a possibility which in some cases may be examined and accepted. However, the reserves remain indivisible for a ten-year period.

a social benefit. However, it is done in a business logic seeking independent management and the consolidation of the company (and of employment). As far as the power detained by the community if it has a share of the capital it shall be what is set down by the charters (no more than 50% if the community constitutes a college on its own).

The links, the exchanges or lack of exchanges between the different SCICs, shall be good criteria to assess the freedom of movement of each SCIC and its capacity to promote each individual instead of policies imposed from above.

## **8. Types of SCIC**

SCICs can operate in many different sectors.

Between the approval of the decree on February 21, 2002 and the end of October 2003, 26 SCICs have been approved. As of today the SCIC projects on the entire territory include:

- maintenance and enhancement of natural spaces, eco-sites;
- waste recovery, enhancement and management;
- culture (art restoration, creation, shows, animations, radio, television, theatre);
- sport (sport and social and ecological environment);
- local services (crafts, furnishings, assistance, hairdressers);
- education (risk prevention, enhance memory);
- training (professional, popular education, long term development, etc.);
- agriculture (gardening, forestry, masonry, wood);
- scientific research, test laboratories for industry;
- health (healthcare, old age homes);
- social (nursery schools, shelters, protected shelters, insertion companies, etc.);
- justice (reinsertion and mediation services);
- service platforms, means co-operatives, activity co-operatives;
- housing co-operatives (Special SCIC law HLM - August 2003);
- trade, distribution (association cafés, organic trade, fair and equal trade shops);
- social tourism (entertainment, lodging, trips, holidays).

This type of list however does not give an exhaustive overview of the existing SCIC projects. The real drive behind SCICs which is highlighted most of the time is the will to act in favour of:

- local development, synergy of the different players on a territory;
- citizen training and education, how to live better together;
- insertion, creation of new jobs;
- environmental protection and enhancement;
- know-how maintenance and/or development;
- long-term development.

What the SCIC produces may help qualify it, but one must avoid using a single criterion. It is easy for example to state that a given SCIC is going to protect a certain skill in the forestry industry which risks disappearing and which is going to make its production more remunerative through hybrid partners and an ad-hoc marketing. However a nursery school which transforms itself in a SCIC has as its interest not simply that of caring for children something which it has been doing well for many years. Its real drive is to be found elsewhere. Its social benefit shall be confirmed by its SCIC approval since in addition to caring for children it shall organise other activities which in turn shall lead to new and different partnerships, etc.

It seems difficult to classify the SCIC projects in a pertinent manner, capable of translating the twofold social aspect of the SCICs. Indeed, it must not be forgotten that it is part and parcel of its legal definition: economic and social. The type of activity gives us a classification from the economic point of view. In the future when some time has elapsed from their creation and after the fine-tuning on the social aspect mentioned above has been carried out it will be possible to set down the criteria for a social classification.

The circular sent to the Prefects by the Ministry concerning the SCICs offers, among other things, some indications on the assessment of the *social benefit*. In this framework it quotes the November 30, 1973 judgement (Delmas-Marsalet, government commissioner) concerning a clinic managed by an association: “The social benefit of an institution is not determined by the sector in which it operates but by the conditions with which it operates. Any social and economic sector of activity be it healthcare, education, culture or in the future environmental protection,

can carry out a social activity”. Many of the questions raised by the creation of the SCICs still have to be fine-tuned and solved with the participation of all the players and by all the future SCICs, issues such as the fiscal aspects, links with public bodies, own resources, European harmonisation, etc. The greatest challenge in the entrepreneurial context is that of learning how to take decisions collectively.



## 9. Solidarity co-operatives in Quebec (Canada): overview<sup>1</sup>

by *Jean-Pierre Girard* \*

### 1. Introduction

Since 1997, Quebec legislation has allowed for multi-membership co-operatives, also known as solidarity co-operatives, to be created. To the best of our knowledge, such co-operatives are the first of their kind in North America. To date, very little has been written on this subject, which can be explained by the embryonic status of the concept. However, in barely seven years (1997-2004), more than two thousand and fifty of these co-operatives have been created. They operate in a wide variety of branches of industry. Given their associative nature, they offer new avenues for partnerships to emerge between civil society, parapublic organizations and various local forces. In the example of social co-operatives in Italy the issue centres around an original re-articulation of the link between the economic and the social. The association of workers and users within the same organization makes it possible for a joint construction of supply and demand to emerge. This structure is proving to be a new means of applying the contributions offered by volunteer and activist resources, thereby reinforcing the value of donations and reciprocity. Finally, as it is the last model to arrive on the scene of the Quebec co-operative landscape, the solidarity co-operative needs to find its bearings among the large co-operative family in which homogeneity regulates membership.

This article aims to portray the solidarity co-operative's level of devel-

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<sup>1</sup> The latter part of this paper is essentially an excerpt from Girard, De Bortoli (2004). The author would like to thank Jocelyne Chagnon from the Co-operatives Branch of the Government of Quebec for having made available updated data relating to solidarity co-operatives and Geneviève Langlois, research assistant at CRISES/UQAM, for having provided very valuable feedback. The author alone assumes responsibility for the text.

opment in Quebec. After a brief summary of the genesis of the idea behind the solidarity co-operative, we will present the legal provisions which define the concept and which prescribe its policies. Our analysis will be pursued by a short portrait of the development of the formula since its legal act, which set the bases for the creation of solidarity co-operatives in 1997. We will then formulate several observations on the appreciation of the solidarity co-operative and its perspectives in terms of future development. Finally, we will present a brief overview covering our three years current research concerning the potential impact of solidarity co-operatives on social cohesion.

## 2. Origin

Quebec, over many decades, has been the scene of a major co-operative development, thus imitating the phenomenon which took place in many other areas of the world. This particular diffusion of the co-operative concept results from a declination of single ownership. Hence, the very well-known network of Desjardins financial services co-operatives is made up of consumer co-operatives. Agricultural co-operatives, as important players in the domestic agri-food industry, are rather producer co-operatives. On a more reduced scale, we have contributed for approximately thirty years to the development of self-managed companies which adhere to the model of worker co-operatives. Forestry co-operatives are a good example of this phenomenon. Although embracing a model of unique partnership, these different types of co-operatives are not sheltered from the tensions brewing between members who may hold different, or opposing, interests. Therefore, in financial services co-operatives, the investing member seeks to maximize the return on his deposits. On the contrary, the borrowing member looks for the lowest interest rate at which to borrow money. However, it remains that this group of co-operatives, contrary to the mutual responsibility co-operative, respond to a single line of reasoning: consumption, (producer) distribution and work.

The origin of the concept of solidarity co-operatives stems from different sources. We are able to identify four major issues which have variable levels and have contributed, over a period of approximately ten years

(1986-1996), in encouraging reflection on what has developed into the solidarity co-operative. These matters are: the question of local development, that of the closing of villages, the development of daycares (nursery schools) and the issue of insertion. A fifth theme and the occasion on which its debate took place gave the process its final élan: home services and the Quebec Economic and Job Summit (1996).

In Quebec, if eventually community development came to be known as regional development, as in the 1980s, it is in fact the concept of local development that would be referred to. In this sense, groups of citizens and representatives of institutional players from the community, such as municipalities, credit unions, etc. will seek to associate themselves with organizations promoting discussion, implementation of development strategies and the initial support for new businesses. Notwithstanding the fact that democratic operating rules are being established, these structures, which balance various interests, should have adhered to the legal form of the non-profit organization (NPO), since the provisions set by the *Cooperatives Act* (uniqueness of owner) do not promote choosing the co-operative model. Related to the issue of local development, in small villages, the closing of essential services such as the post office, grocery store, gas station and others, demonstrates a serious threat to the community's survival. The idea of consolidating all concerned organizations and persons within a co-operative able to offer a basic minimum of services is gaining ground. In other respects, the increased presence of women in the job market has given rise to a peaked demand for the development of childcare services. Again, the impracticability for the co-operative to consolidate like family members and workers has led to the NPO model being favoured in this area. Finally, concerning the fourth issue, we must consider the increased number of projects aiming to promote the reinsertion of disqualified individuals in the job market since the beginning of the 1990s. These initiatives have often taken the form of apprenticeships in home working supervised by a structure aiming to accommodate the interests of the trainee, the beneficiary of the service and the supervising organizations, as is the case with the Local Community Health Centres (LCHC)<sup>2</sup>.

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<sup>2</sup> Parapublic organizations reconciling health and social services. Hence, they are funded by the health and social care ministries. They cover all the concerned territory.

These new social and economic realities and the demands imposed by local development have fuelled reflection on the co-operative movement to discover means of adapting the co-operative model to the new situation. One event in particular provided the opportunity to bring this reflection to fruition. The Government of Quebec's initiative to conduct the Economic and Job Summit<sup>3</sup> in 1996 generated numerous actions likely to improve Quebec's performance in the areas of job creation and maintenance. Among these issues, that of home-care service needs to be raised. Following the example of other Western countries, Quebec must come to terms with its noticeable aging population. Sheltering those who are aging and losing their autonomy in a public environment is considerably expensive; consequently, the government has decided to encourage elderly people to remain at home. In this context, through the network of LCHC, the government is able, in principle, to ensure a delivery service of assistance and care to these persons, but not to ensure work and domestic help. Since a significant portion of these custodial services were carried out under the table (black market), the government decided, within the 1996 Economic and Job Summit, to support the creation of Homecare Social Economy Enterprises, using the NPO model or co-operatives considered as non-profit organizations<sup>4</sup>. In doing so, it is seeking on the one hand to bring this service delivery out of the informal economy, and on the other hand to promote job creation, especially for persons excluded from the job market (measures enabling re-entry into the labour force). Government support for Homecare Social Economy Enterprises has first of all taken on the form of a financial aid program at the request of users, who wish to override domestic help services, and from elderly people, who are in the process of losing their autonomy and require regular housekeeping. This initiative is known as *Programme d'exonération financière en services à domicile* (PEFSAD). Second of all, following the representations from the general organization consolidating all of the co-operative sectors in Quebec, the Conseil de la coopération du Québec (CCQ), the Province accepted to expand the *Cooperatives Act* by

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<sup>3</sup> Summit gathering different socio-economic actors such as employers associations, important trade unions, environmental and community base representatives, co-operative leaders, etc.

<sup>4</sup> This notion of the profit-making co-operative implies that the co-operative agrees to include in its positions a provision to the effect that the surplus will be reinvested in the co-operative and not returned to the members in the form of patronage returns.

adding new provisions allowing the creation of solidarity co-operatives. For the co-operative movement, the opportunity to develop co-operatives within the niche of home services provided an excellent opportunity for more openness towards the form of multi-member co-operatives. Indeed, it granted them the opportunity to establish a legal basis allowing for interests to be expressed by the various actors affected by these co-operatives' lines of activities. We are therefore speaking about the interest of the user, who seeks to satisfy his need for home services as much on the level of cost as on the quality of the service, of the worker, in terms of work and salary conditions, and of organizations or individuals which, without being directly involved in offering these services, share the same objectives of the organization. Over a period of a few months, a close collaboration between the CCQ and the government department responsible for administering the *Cooperatives Act*, the Direction des coopératives, enabled the amendments to the act's text to be completed, all of which formed the subject of a sanction made by the Quebec parliament in June 1997.

### 3. Provisions relating to the solidarity co-operative<sup>5</sup>

Paragraph 226 from the *Cooperatives Act* therefore provides substance to the concept of the solidarity co-operative. The main provisions are associated with four elements: definition, capitalization, formation of the board of directors, and patronage returns.

According to the Act, the solidarity co-operative concurrently consolidates members who are users, services offered by the co-operative, and members who are workers employed within this co-operative. Moreover, any other person or company who has an economic or social interest in attaining the objective of the co-operative may also be a member of the co-operative. This member is hereafter named a "supporting member" (see "Loi sur les coopératives", chapitre C-67.2). In Quebec, the initial mechanism of capitalization takes the name of parts (shares) of qualification composed according to the choice of the co-operative, of social parts exclusively, or of both social parts and preferential parts. For the solidarity co-operative, it is specified that the number of these parts that

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<sup>5</sup> It is expected that the *Cooperatives Act* will be changed in some part during 2004.

a member must hold can vary according to whether the member is a user, a worker, or a supporting member. During these activities, in the same way as is seen in other types of co-operatives, the solidarity co-operative can use another mechanism of capitalization, which consists of issuing preferential parts according to categories which have not been included in the qualification parts. Furthermore, if a policy authorizes such, the Act specifies that the solidarity co-operative has the freedom to issue, to the supporting members, another capitalization title, that of participating preferential shares. Each category of members (user, worker, supporting member) forms a group for the election of the directors. The Act ensures that each of these groups has a minimum of one representative serving on the board of directors. It is at the co-operative's discretion to determine the number of members per group, however the Act stipulates a maximum of a third of the directors can originate from the group of supporting members. Under the hypothesis that the co-operative pays patronage returns, the Act specifies that such returns occur for user members on a pro rata basis with operations carried out with the co-operative during the previous fiscal year. In the case of the working member, this payment is established according to the volume of work carried out during the previous fiscal year. This volume can be determined according to the number of working hours, the member's revenue, or any other measure as set by the policy. Attributing patronage returns to supporting members is prohibited.

#### **4. Development of solidarity co-operatives**

The limited existence of solidarity co-operatives in Quebec allows only for the distribution of incomplete, fragmented information. We must wait a few more years before being able to paint a more accurate portrait. At the constitutional level, the very large majority of solidarity co-operatives are *ex-nihilo* creations, while some result from the transformation of NPO's. Furthermore, a few co-operatives of another type have modified their positions to embrace this form of co-operative. One must be aware that this development, a relatively quick result ensuing from the solidarity co-operative model, was able to benefit from the support of different government programs. Besides the cases of co-operatives in the

home service sector, and those in the area of childcare services, which to date are very small in number, several others have been able to sustain themselves with the assistance of the financial aid program provided to co-operative development from a Government organization, Investissement-Quebec. This program offers mainly loan guarantees. Furthermore, another program developed by the ministère des Régions<sup>6</sup> proposes subsidies for the start-up of so-called social economy companies. It is used for initial financing. Managed by organizations called local development centres, which also use resources to supplement the start-up of social economy companies, this program has significantly stimulated the development of solidarity co-operatives.

**Table 1 - Evolution of the number of solidarity co-operatives in Quebec: period from 1997 to 2003**

<i>Year of constitution</i>	<i>Number of co-operatives</i>	<i>Co-operatives remaining in operation</i>	<i>% of co-operatives remaining in operation</i>
1997	18	17	94,4
1998	32	23	71,9
1999	45	29	64,4
2000	46	28	60,9
2001	30	25	83,3
2002	35	34	97,1
2003	49	49	100,0
<i>Total</i>	<i>255</i>	<i>205</i>	<i>80,4</i>

*Source: Direction des coopératives, 2003, MDER.*

Solidarity co-operatives are present in various lines of activities with a dominant presence in the so-called area of personal home services. This result is not surprising considering the resources allocated since 1997 to promote the development of this type of organization. Table 2 exposes the portrait dating from December 2003.

On a financial level, we must deal with limited data, considering the number of solidarity co-operatives that have submitted their annual balance sheet to the Co-operative Branch. In this sense, we have at our disposal a reduced range of samples

<sup>6</sup> Since the election of a new provincial Government in April 2003, this program has been terminated.

**Table 2 - Main lines of activity of solidarity co-operatives in Quebec.  
Based upon constitution chart: 2003**

	<i>Total**</i> N	<i>Total</i> %
<b>Primary</b>		
Agriculture	10	
Others	6	
<i>Sub-total</i>	<i>16</i>	<i>6,3</i>
<b>Secondary</b>		
Printing, editing	6	
Others	10	
<i>Sub-total</i>	<i>16</i>	<i>6,3</i>
<b>Tertiary</b>		
Personnal services	38	
Recreational-tourism	29	
Social services	19	
Grocery, specialised stores	17	
Arts and scene performance	15	
Services to enterprises	13	
Accommodation and food services	12	
Others	80	
<i>Sub-total</i>	<i>223</i>	<i>87,5</i>
<b>Total</b>	<b>255</b>	<b>100,0</b>

Source: *Direction des coopératives, 2003, MDER.*

\*Based upon classification des activités économiques du Québec code.

\*\* On December 31, 2003.

According to table 3, we learn that on average, a solidarity co-operative has assets of \$250K<sup>7</sup>, a level of debt of 120K\$ and equity of 130K\$. The annual average turnover is 511K\$ with an annual % of growth of 19,6.

**Table 3 - Solidarity co-operatives in Quebec: (partial results: 72 co-operatives). Financial data on December 31, 2002: average**

<i>Variable</i>	<i>Total</i>
Assets	250K\$
Debt	120K\$
Equity	130K\$

Reference: *Direction des coopératives, Gouvernement du Québec.*

The average membership of a solidarity co-operative is established at 351 members, broken down into 315 user members, 24 worker members,

<sup>7</sup> On April 30 2004, 1\$CDN=0,62 euro.

and the balance, 12, in supporting members. Among these supporting members, the corporate member category is mainly composed of local development centres, Local Community Health Centres, financial co-operatives (Desjardins), and other community organizations.

## 5. Assessment: development perspectives

The accelerated development of solidarity co-operatives in Quebec since the 1997 adoption of the decree acknowledging their existence is definitely not a coincidence. First of all, the co-operative formula is part of the economic development model in Quebec. In the image of French language and culture, it is a model of development which distinguishes itself from the rest of Canada, and more generally speaking, North America.

In Quebec, there exists a presence of large capital stock companies such as Bombardier, Québecor, Jean Coutu and others, but through capital equity participation, there is a very large influence of major public corporations including the very impressive Caisse de dépôt et de placement (assets exceeding \$110G), the Société générale de financement and Investissement-Quebec. Workers' funds (Fonds de solidarité des travailleurs et travailleuses du Quebec: asset of 5G\$) are then earmarked for risk capital within companies including co-operatives and large co-operative organizations, which at the forefront are Desjardins (asset of 100G\$), Agropur and the Coopérative Fédérée de Quebec.

Therefore the co-operative option, contrary to the prevailing situation in other Canadian provinces, forms a clear part of the choices of economic and social development. On another level, major resources are allocated to promote this development, not only on a financial level, such as illustrated previously, but also concerning support, aid offered to the start-up process and to development. The determining role of the local development centres and regional development co-operatives<sup>8</sup> must thus be taken into account. The acknowledgement of solidarity co-operatives did not arise from a sole government initiative, but from years of representa-

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<sup>8</sup> The main activity of regional development co-operatives, which consists of assistance to the start-up of new co-ops whatever the sector of activity, is supported by a subsidies program from the Government of Quebec.

tion by the spokesperson for the co-operative movement, the Conseil de la coopération du Québec, an organism which facilitates the integration of the model into the larger co-operative family. To this day, there does not exist an association of co-operatives in a federation or consortium as is the case, for example, for the social co-operatives in Italy. Being present in a multitude of sectors, there is no sufficient critical mass to justify such groupings, but there is also the question of the model, such as Italy's consortium, being unknown. In the sector of home services, a Federation was created in 1996, however it brings together the group of co-operatives independently from their form. Cohabiting as such in the Fédération des coopératives de services à domicile du Québec are solidarity co-operatives, user co-operatives and even some worker co-operatives. Elsewhere, solidarity co-operatives generally adhere to organizations which often supported their development, the regional development co-operative, which enables networks or co-operatives also associated with regional development centres to join forces with more institutionalized co-operative networks.

How is arbitration carried out among the various interests within these co-operatives? The information available does not allow for a firm judgement to be pronounced. Various indications lead us to believe that until the present time, things have been progressing relatively well. Therefore, according to the Co-operative Branch, telephone surveys indicate that the sharing of positions on the board of directors is generally administered according to the rule of equality between group members. Furthermore, these co-operatives do not seem to have appealed more than the others to significant interventions between the actors, involving mediation. One must however keep in mind that they are still, in the great majority of cases, under the influence of the enthusiasm for a merge from the outset, a favourable élan of compromises. They seem overall well entrenched in their environment, proposing responses which are flexible and adapted to the various needs.

In prospective terms, certain stakes must be closely monitored. To this day, solidarity co-operatives have been very active in areas mainly affecting social issues. In certain cases, including home services, there has been saturation. Although in this world of local community-based services or so-called *relational* services, which includes the recreational-tourism sector

(for example, managing an outdoor activities Centre), the model has not yet reached full maturity. It goes without saying that there is nothing preventing us from thinking that there would be cause for envisaging development in sectors increasingly regulated by the market. For example, in the food-processing industry, a co-operative would group together non-traditional livestock breeders (bison, emu, ostrich, etc.), slaughterhouse employees and consumers. The solidarity co-operative formula could also find a place in the already established networks of consumer co-operatives. Whether it be in the academic environment (colleges and universities), in food consumption, or even in funeral services, the solidarity co-operative, out of all the networks of consumer co-operatives, would provide an original approach to motivate participants other than the users, the most important being the workers.

These new areas of development may lead us to rethink capitalization strategies. To this day, we have no choice but to notice that solidarity co-operatives have benefited reasonably from public grants, which explains in many cases why co-operatives have adopted the so-called non-profit status (impossibility of returning the surplus) which also implies exemption of tax. One can even think that in certain cases, these incentives were able to produce a perverse effect by inciting people to adopt this formula for the sake of this very end result. What cannot be doubted is that the height of start-up grants serving as capital outlay had a discouraging effect, where members are concerned, in regards to capitalization. By taking into account individuals' financial limits, let us consider the lower wage earners: one nevertheless agrees that for the formula to be viable over the long term, greater financial involvement by the members through self-capitalization would certainly be welcome. One is entitled to imagine that this may be the path that new co-operatives will follow, particularly those exposed to the games of supply and demand, thus evolving in less protected markets.

## **6. Solidarity co-operatives and social cohesion: a research project**

By their nature as associations, solidarity co-ops have the potential to offer new kinds of partnership and governance among civil society,

parapublic organizations, and various local actors in seeking solutions to needs that are not met or not met sufficiently. Joining workers and users in the same organization allows mutual balance of supply and demand. This structure is also a new way to use volunteer and activist resources, which reinforces the values of altruism and reciprocity. Like social co-operatives in Italy, solidarity co-ops are an original means of reconstructing the link between the economic and the social spheres (Girard et al., 2000).

These remarks demonstrate the value of attempting to understand the impact of this kind of co-operative on social cohesion. The solidarity co-op is an original way of mobilizing various actors; it is a customized response to unmet needs and it can serve as a unifying force.

As part of the research project entitled “Co-operative Membership and Globalization: Creating Social Cohesion through Market Relations”<sup>9</sup>, the Centre de recherche sur les innovations sociales dans l'économie sociale, les entreprises et les syndicats (CRISES) of the Université du Québec à Montréal (UQAM) will undertake a series of studies and analyses on the topic of solidarity co-operatives and social cohesion, which will be carried out between 2002 and 2005<sup>10</sup>.

From 2000 to 2002, CRISES took part in a variety of research activities concerning social cohesion and financial service co-operatives, which led to the publication of a series of monographs<sup>11</sup> and of a synthesis<sup>12</sup>. Co-

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<sup>9</sup> This Canadian research project was lead by the Centre for the Study of Co-operatives of the University of Saskatchewan: <http://www.socialcohesion.coop/>.

<sup>10</sup> Updated information at <http://www.unites.uqam.ca/crises/e/projetsocietariat.htm> (in French only).

<sup>11</sup> Mager Lucie, sous la direction de Marie-Claire Malo et B. Lévesque (2001), «Coopératives financières cohésion sociale et territoire: la Caisse populaire Desjardins Saint-Patrice de Magog issue de fusions de caisses dans la MRC Memphrémagog», Montréal: UQAM, Centre de recherche sur les innovations sociales dans l'économie sociale, les entreprises et les syndicats, *Collection études de cas d'entreprises d'économie sociale*, n. ES0104; Huot Geneviève, sous la direction de Marie-Claire Malo et B. Lévesque (2001), «Coopératives financières, cohésion sociale et territoire: La Caisse populaire Desjardins de Kildare issue de fusions de caisses dans Lanaudière», Montréal: UQAM, Centre de recherche sur les innovations sociales dans l'économie sociale, les entreprises et les syndicats, *Collection études de cas d'entreprises d'économie sociale*, n. ES0105; Camus Annie, sous la direction de Marie-Claire Malo et B. Lévesque (2001), «Coopératives financières, cohésion sociale et territoire: La Caisse populaire Desjardins Allard-St-Paul issue de fusions de caisses dans l'arrondissement Sud-Ouest (Montréal)», Montréal: UQAM, Centre de recherche sur les innovations sociales dans l'économie sociale, les entreprises et les syndicats, *Collection études de cas d'entreprises d'économie sociale*, n. ES0106; Chouinard Omer, P. M. Desjardins, É. Forgues, et U. de Montigny (2001), «Coopératives financières, cohésion sociale et territoire: La Caisse populaire Moncton-Beauséjour et la Caisse populaire de Néguauc issues de fusions de caisses milieux urbain et rural», Montréal: UQAM, Centre de recherche sur les innovations sociales dans l'économie sociale, les entreprises et les syndicats, *Collection études de cas d'entreprises d'économie sociale*, n. ES0107.

operative organizations have been studied in the light of five concepts: *territoriality*, *accessibility*, *employability*, *democrativity*, and *networking*. For the current research project, we will define each of these dimensions and raise different key questions.

## 7. Territoriality

As elsewhere in Canada, territory is being defined in new ways. In the past in Quebec, the parish of the local Catholic Church, with a more or less homogeneous population, was central. It is now being replaced by a wider territory corresponding to *Municipalités régionales de comté* (MRCs)<sup>13</sup> with a heterogeneous population. To what extent do solidarity co-operatives fit into this new division with regard to the membership's understanding of the three member categories, the structure or representatives of the board of directors, and the field of activity? Do the development projects of these co-ops correspond to this new geographic frame of reference?

## 8. Accessibility

The level of accessibility of the solidarity co-ops' services is a central element of this research. Starting from Vienney's (1994) view that co-operatives are intended to be a response to needs that are not met or not adequately met, and are aimed at actors with relatively little power, the research seeks to describe this accessibility.

As accessibility is directly related to the services provided, one must consider the nature and the effectiveness of these services in direct relation to the urgency of the needs of the population - the one hand (nature), how well the co-ops meet the need itself, and on the other (effectiveness), how well they are able to meet the demand quantitatively.

It is also worthwhile to see how these organizations develop new services, not from the perspective of doing business with non-members, but, as described in the typology of Desforges (1980), to broaden the

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<sup>12</sup> See Malo et al., 2002.

<sup>13</sup> This is a new territorial division created by the Government of Quebec in the 1980s, mainly to facilitate regional development.

range of services offered to members, and thus strengthen their ties to the co-op. A good example is the case of personal and home services co-ops, which at the instigation of their members have begun to own and run residential centres. As aging members can no longer remain in their own homes despite the assistance services offer by the co-op and must move into group homes, they would have to leave their area if there were no such resources present. The action of the co-operative in this sector allows people to remain in their community, which seems at first sight to have a direct and positive effect on social cohesion or as a way of fighting against exclusion.

Correlating accessibility with networking, we can analyse it by observing the effect of the introduction of co-operatives on already-existing services in the area - in the case of personal and home services, for example, or public health clinics (LCHCs), in relation to the accessibility of their services. We can also attempt to measure the impact of the relations of these co-ops with the other organizations on the accessibility of the services of the co-op itself, by seeing, for example, how accessibility of the co-op's services is increased or diminished according to whether it is or is not strongly connected to local community organizations. Finally, we can study how accessibility of services is affected by compromises (if any exist) among the individual interests of members, the interests of members as part of the group, and the general interest of the population, in relation to accessibility of services.

## **9. Employability**

The concept of employability can be interpreted differently depending on the solidarity co-op's sector of activity. In certain cases, this element is secondary - the solidarity co-op offering a number of services to a community that does not possess a grocery store, post office, or bank, for example. Here, accessibility is the crucial value. In other cases, employability is central - a co-op working under programs of reintegrating marginal populations into the workforce, for example.

Indicators include the degree to which the jobs created are comparable, in terms of work conditions, to similar jobs in other organizations. The socio-economic characteristics of the personnel hired could also show

the influence of co-ops on social cohesion (employment of people who are poor, unemployed, young or old, men or women, with or without training, etc.). A comparison of these data with other organizations would allow us to measure the co-ops' contribution to social cohesion relative to other similar organizations.

## **10. Democrativity (or simply, democracy)**

The notion of democrativity refers, on the one hand, to the nature of the democratic process in the enterprise (namely the choice of representative, direct, or deliberative democracy) and on the other, to the institutional or composite form of its structure, understood by means of concepts such as “social democracy” and “plural democracy”. The distinction between the two, though unclear at first glance, is fundamental. The “nature of the democratic process” refers to the practice of democracy in the operational and dynamic sense of the term, thus to the idea of process. The “institutional or composite form of its structure” refers to the composition of the democratic structure of the enterprise - that is, the composition of its board of directors, the existence of special committees, the socio-economic characteristics of this composition, etc. In this second aspect we find the concepts of plural democracy, which refers to the territorial, institutional (other local organizations), and socio-economic origins of the members of the board, and other instances of the democratic structure of the enterprise; and the concept of social democracy, which refers to the symmetrical representation of local or larger groups in this structure. All these concepts can be studied in light of the development and evolution of co-ops.

## **11. Networking**

Networking is defined as the links among various individual or collective participants, forming networks, which at the same time use and generate social capital (the values of confidence and reciprocity), which favours co-operation and contributes to the construction of social cohesion. Studying this aspect will allow us to see how the relative connectedness of participants initiating projects influences their success. We will then be

speaking of a stock of social capital. We will also study these ties to see whether they constitute what Granovetter (1985) refers to as “strong ties” or “weak ties,” and to what extent they influence social cohesion in one or the other case. Then, in an area where connectedness and degree of democracy overlap, we will look at the influence of the “charismatic personality” on the creation of social ties that increase the potential of success for the project. In other words, we will see how local participants, possessing strong symbolic capital (director general of a financial services co-op, mayor, recognized institution, etc.) are able to form social ties that favour the success of a solidarity co-op’s project. At the same time, we will take into account the role of such influence on the process and components of the democratic structure of the enterprise.

As seen above in the discussion of territoriality, this dimension will also allow us to explore the extent to which the connectedness of the enterprise is favoured by whether or not it adopted the new institutional territory of local development - in this case that of the new municipalités régionales de comté - as the LCHCs in particular have done. In the same way, the correlation between the degree of accessibility of services (quantitatively) and the degree of connectedness of the enterprise could be analysed (see accessibility). Finally, we will emphasize the presence of various participants who traditionally play an unobtrusive role or only become involved when forced to do so, those who have directly and voluntarily contributed to the successful development of solidarity co-ops.

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## **PART 3**

Developing economic and social role of social economy organisations in transition economies



# 10. Co-operatives in Poland: from state-controlled institutions to new trends in co-operative development

by *Ewa Leś*\*

## 1. Introduction

In Poland during the transition period, the co-operative sector has not been put “on the table”, neither as a privatisation form that combines economic and social benefits nor has its development been stimulated as a strategy for the prevention and reduction of high unemployment and poverty, reforming public service delivery and developing the local economy. In the transition process there have not been significant policy initiatives, except for the credit co-operatives, which would stimulate co-operative sector reforms, moving it away from the negative definition as relic of the old regime and adjusting the co-operative sector to the new and complex conditions of the liberal market economy. The necessary legislative framework and fiscal incentives have not been provided. As a result, most of the co-operative sector has undergone a dramatic depression that has been reflected in a scale of decline of the co-operative labour force without precedent in the history of the Polish co-operative movement. Since the beginning of the transition the neo-liberal ideology and strategy for socio-economic reform in Poland well-known as “shock therapy” has been highly critical of all forms of collective property - State or co-operative. Consequently, the economic and social advantages of the co-operative form have remained untapped in the process of transition, likewise its role in promoting economic democracy, economic self-reliance and creating a new framework for redistributive justice.

In the paper, I will describe briefly the past developments of the co-operative sector in Poland and its impact on the present status of the sector. I will analyse the legal conditions and a scale of the co-operative

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movement and then, the phenomenon of the movement of new wave co-operatives, describing the main drawbacks in its development. The aim of this paper is also to indicate, among other functions, the potential of the co-operatives as a socio-economic reintegration instrument and as a producer of general interest services. One of the main conclusions of this paper is that while co-operative sector is obviously no panacea for all the social and economic problems of the transition, its strength is that it often does play a considerable role in increasing employability and living standards of low-income groups and strengthening community regeneration and development. Although empirical evidence so far is not extensive, what is available is encouraging, showing co-operatives' viability, both economically and socially and, therefore, indicating the need for government action reforming and fostering the co-operative sector as a permanent form of ownership and organisational structure with the capacities of mitigating market failures, strengthening economic democracy and civil society.

## **2. Traditions of the co-operative movement**

The Polish co-operative movement has been shaped by a long history. During the nineteenth century its role was of utmost importance for Poland because the country had been deprived of its sovereignty. As a consequence, co-operatives became a mechanism of economic development as well as assuming the roles of non-existent public institutions, bolstering the national spirit and furnishing educational and social support. Among the founding-fathers of the Polish co-operative movement especial mention should be made of Stanisław Staszic, Fryderyk Skarbek, Karol Marcinkowski, the priests Augustyn Smarzewski and Piotr Wawrzyniak and most famous of them all, Stefczyk the founder of the credit unions known as 'Stefczyk co-operatives' based on the Raiffeisen model and popular among poor farmers. After Poland regained its sovereignty in 1918, co-operative institutions once again played an important role in the country's socio-economic life.

### 3. The co-operative movement under communist rule

Under communist rule, Polish co-operative institutions, like other organizations of civil society, could neither set goals nor undertake activities independently of the communist state. Between 1948 and 1989 co-operatives in Poland were neither autonomous nor independent socio-economic players, nor were they institutions in which sound social and economic relations existed between a co-operative and its members. During the communist period, co-operatives existed as quasi-state agencies and were a part of the so called 'socialised ownership' together with the public sector and the non-profit sector (Leś, Piekara, 1988).

Under the nationalised economy they were an integral part of the planned economic system, although formally co-operatives have maintained different property status than public enterprises. Co-operative private ownership was liquidated and instead a kind of joint property has been introduced where co-operative property belonged to the whole membership (Piechowski, 1995). As happened to many associations and foundations in the late 1940s and early 1950s, numerous assets and properties held by co-operatives were taken over by the state. "In the centrally planned economy the co-operatives monopolized some branches of economic activity, such as food supply and processing, agricultural marketing and production, and housing" (Piechowski, 1995). They were incorporated into the national economic policies and their economic activity was subjected to central and regional economic plans. During the communist era the state administration appointed its own people (the so called nomenclature) to key positions in a co-operative. Staffing policies in the Polish co-operative sector have been often based on "know-whom" principle instead of "know-how", paraphrasing Hans Münkner's terminology. Bureaucratisation and centralization of co-operative organizations, as well as subordination to the totalitarian state and monopolistic position that co-operatives enjoyed under communism in some areas of national economy and negative selection to the jobs in co-operatives - all those factors have contributed heavily to the rather bad reputation that co-operatives have developed in Polish society.

#### **4. An outline of co-operative organizations in Poland after the breakthrough of 1989**

In contrast to the remarkable proliferation of foundations and associations since 1989, the Polish co-operative movement has not experienced vigorous growth. The legacy of communism has had a profound impact on the public perception of the co-operative sector in Poland, and it continues to weigh heavily on the position and prospects of the co-operative movement in the country. The Polish co-operative movement, in spite of its long-lasting and successful history, became totally discredited in public opinion at the beginning of the 1990s. This included not only co-operatives as existing organizations, but even the notion of ‘cooperation’ (Piechowski, 1999). However, the reason why most of the co-operative sector in Poland has not experienced a significant growth after 1989 is not only due to the communist legacy. The neo-liberal ideology adopted during transition has favoured market-led economic reforms and commercial privatization over other forms of property, including a co-operative type of ownership. Although since 1989, formally, the co-operative sector has become a part of the private sector, it has not received political recognition, except for credit co-operatives.

As a result, no legislation and sound policy measures were introduced in order to reform and strengthen co-operative institutions during transition. It has de-motivated different players potentially interested in engagement in co-operative movement and had laid to a persistent uncertainty among members of the existing co-operatives. As one analyst has put it, co-ops’ leaders “...were conscious that state authorities and most political forces had neglected the role and importance of the co-operatives in transforming the national economy and had sometimes even assumed a hostile attitude towards the movement” (Piechowski, 1995). As a result, until now the co-operative sector has been almost entirely overlooked as an instrument that could contribute to the local economy and transform the Polish public welfare system. The co-operative sector thus found itself unprepared for the conditions of a market economy.

There were three main problems:

- a. a shortage or complete lack of capital (co-operatives were weakest in terms of capital);
- b. a low-skilled labour force;
- c. low-skilled managements unable to run co-operatives in free-market conditions (Sztanderska, 1997).

This is why, that which Münkner described as the triple crisis of the co-operative movement identified by the crisis of identity, performance and environment, still finds clear evidence in the Polish co-operative sector.

The co-operative sector in Poland consists of 16 branches and, according to the National Council of Co-operatives, has a membership of 8 million individuals, the dominant subsectors being: housing, rural consumer co-operatives, and labour co-ops. (see table 1).

As for discerning the pattern of co-operative development I find a classification proposed by Borzaga useful: that of 4 major co-operative model, i.e. the mutualistic model, the sociological model, the in-between model and quasi-public model (Borzaga, 2003). According to this pattern, most of the Polish co-operative sector still belongs to the quasi-public model, though formally located in the private sector of economy.

Unlike civil society organizations in Poland, which proliferated after 1989, co-operative enterprises underwent a process of decline: indeed, between 1992 and 2004 the number of the co-operatives decreased from 19,372 to 13,000. In the years of transition (1989-1995) employment in co-operative sector has dropped off by over 72 %, much more than in the public sector. For example, in the years 1990-2002 there was a severe decline of employment, in particular in rural co-operatives, i.e. from 350 thousand to 150 thousand employees (Ministry of Economy, Labour and Social Policy, 2004) and in co-operatives for the handicapped. In 1992 co-operatives for the handicapped were the only category of shelter enterprise, while in 2001 only 12% of the shelter enterprises were co-ops. The majority were transferred into various forms of companies and some have been closed down.

The decline in the size of the co-operative sector was caused by the following three main factors:

1. transformation of existing co-operatives into other legal forms such as foundations (co-operatives for the disabled, farmers' co-operatives) and private firms (including so called 'wild privatisation');

2. the merging of several co-operatives into a larger co-operative entity;
3. liquidation.

One of the few Polish co-operative sub-sectors that is undergoing a remarkable renaissance since the transition is that of credit co-operatives (*Spółdzielcze Kasy Oszczędnościowo-Kredytowe* - SKOK). These did not exist under communism and were introduced in the early years of the 1990. The main sources of inspiration for the renaissance of the credit co-operatives are rooted in the “solidarity” trade union debates of the early 1980s and the active role played by the union in the early 1990s in their introduction. By March 2004 they had over 1 million members. There are some 13 thousand branches all over the country and their network has overtaken that of the biggest Polish retail Bank - PKO BP in size. The credit co-operatives offer various financial services to individual employees and retired consumers in a form of savings and credits and provide credits to small enterprises (Dunajski, 2003). Their share in the credit market for small enterprises amounted to 5 % in 2001.

**Table 1 – Sectors and enterprises**

<i>Sectors, enterprises</i>						
<i>a. numbers of units</i>		<i>31.12.1995</i>	<i>31.12.1996</i>	<i>31.12.1997</i>	<i>31.12.1998</i>	<i>31.12.1999</i>
<i>b. dynamics</i>						
Total	a	2.110.710	2.412.022	2.595.890	2.842.278	3.039.451
	b	99,5	114,3	107,7	109,4	106,9
Public sector	a	49.419	55.528	57.247	69.729	83.306
	b	99,7	112,4	103,1	121,8	119,5
Private sector	a	2.061.291	2.356.494	2.539.643	2.772.549	2.956.145
	b	99,5	114,3	107,8	109,2	106,6
Nationalized Enterprises	a	4.357	3.847	3.369	2.906	2.599
	b	87,9	88,3	87,6	86,3	89,4
Municipality Enterprises	a	481	444	265	-	-
	b	85,3	92,3	59,7	-	-
Commercial Companies	a	104.922	115.739	126.465	136.497	146.859
	b	110,4	110,3	109,3	107,9	107,6
Companies	a	207.021	223.113	245.374	272.008	288.956
	b	100,6	107,8	110,0	110,8	106,2
Other Companies	a	1.031	1.237	1.385	1.507	1.561
	b	103,7	120,0	112,0	108,8	103,6
Co-operatives	a	19.822	19.868	19.775	19.638	19.328
	b	100,0	100,2	99,5	99,3	98,4
Joint Private Economic Activity	a	1.693.427	1.949.986	2.090.013	2.274.493	2.417.737
	b	98,5	115,2	107,2	108,8	106,3

**Table 2 - Cooperative sector in Poland**

<i>Co-operative sector (30.12.2002)</i>	<i>Numbers of co-operatives</i>
Alimentary co-operatives	382
Village co-operative "Peasants' Self-Help"	1588
Co-operative creamery	234
Bee-keeping and horticulture co-operatives	121
Collective farm co-operatives	955
Farmers' co-operatives	967
Co-operative banks	630
Housing co-operatives	3074
Work and services co-operatives	1114
Building co-operatives	36
Co-operatives for the handicapped	293
Co-operatives for the blind	28
Handcraft co-operative "Cepelia"	298
Credit unions	118
Other co-operatives	44
Audit unions and their subsidiaries	72
	9954

## 5. The emergence of new-wave co-operatives

The new wave co-operatives generally develop in areas, where traditional co-operative structure are absent, (general interest services [educational services, nursery services, childcare] and socio-economic services for the long-term unemployed and low employability groups). In Poland, new co-operatives consist of credit co-operatives and mutuals, non-public schools, farmers' groups as well as social co-operatives and other social enterprises involving the unemployed and low-income and low-employability groups. Among new or alternative co-operatives are credit unions, non-public (civic) schools run by the Civic Educational Society and agricultural produce marketing groups. According to Piechowski, there are some 143 farmers' marketing groups with various legal forms: most of them are associations, followed by co-operatives and limited or joint-stock companies and joint private economic activities registered with the local authorities (Piechowski, 1999, p. 53).

The new wave co-ops are a result of the initiatives undertaken by the leaders of civil society grass-roots organizations and some local co-operative sector leaders. Their emergence has occurred mainly in conjunction with the crisis of the post communist welfare state as well as

massive unemployment and poverty being the result of economic transformation. Growing institutional and administrative vacuums in the social welfare system and the decline in public service coverage during the transition have made civic-minded local leaders establish new citizens' organizations and institutions, such as foundations and associations and set up new programmes to bridge the post-communist welfare gap. At the beginning they were mainly aimed at addressing the social/material needs of the weakest social groups and have gradually expanded the range of activities seeking more effective modes of assisting the low-employability groups, including skills training, job creation services and the development of local economy. In addition, to cope with the problems of social exclusion, the potential of new co-ops and civil society organizations are utilized for citizen-led privatisation of local public services. Co-ops running schools managed by parents and teachers, associations running small village-based schools managed by parents are some of the latest examples of the phenomena in question.

However, there have not been so many new co-ops so far. Many are just foundations and associations operating socio-economic programmes, such as ecological farms and second-hand stores, and services in renovation-construction work, gardening, sewing, bookbinding, carpentry for firms and private residents (The Barka Foundation). A second example is provided by the social enterprises for the mentally disordered. The "U Pana Cogito" Hotel in Cracow employs five healthy staff members and fifteen persons with mental disorders who, after consumer service courses, work as chambermaids and reception clerks. The hotel thus performs the function of an occupational activity establishment and is co-financed by the Fund for the Rehabilitation of People with Disabilities (Leś, Nałęcz, 2003).

Further examples of new co-operatives are the recent socio-economic schemes undertaken in the north-eastern part of Poland, which is affected by high unemployment. The activities of the three newly-created co-operatives include basket-making, computer services and catering (Leś, Nałęcz, 2003).

These activities receive financial support from the National Co-operative Council and the Swedish Co-operative Development Agency. In 1999 the first Polish institution promoting and supporting new co-operative

initiatives at the local level - Co-operative Development and Local Entrepreneurship Association in Olsztyn (WAMA-COOP) - was established. With the new co-operatives carrying out a social and economic function in the field of social exclusion, unemployment, general interest services and local development, the problem today seems to be that of how to give them the means to survive in the long run. The most serious operational difficulties these co-ops face are the inadequate legal and fiscal regulations, often with a lack of public support for the public services they provide. In addition, the lack of capital and extreme difficulties gaining access to loans and credits. The present experience clearly shows that financial support schemes both public and private are required, in particular by the availability of co-operative credit fund, social security incentives.

## **6. Conditions for re-development of the co-operative enterprises in Poland. What is needed for boosting the co-operative sector?**

Legal conditions for the co-operative sector after 1989.

The necessary legislative framework and fiscal incentives are needed to reform and develop the Polish co-operative system. I would like to emphasise the legitimating role of legislation. It is particularly important vis à vis banks, credit institutions and investors. Experience shows that the adoption of active policy measures and legislation are necessary to the sector re-building, ensuring long-term survival and development of the co-operative form of property in Poland.

The legislative changes introduced during the 1990s in the form of amendments to the co-operative law in force since 1982 served to "...overcome the prejudice against co-operatives, to restore confidence in co-operative ownership, and to create awareness that members can be effective owners of the co-operative, thus establishing strong economic and social links between co-operatives and their members" (Piechowski, 1995). However, these legislative changes, although important, have not reintroduced private ownership into co-operatives, which is the crucial element for full and genuine restoration of the concept, values and principles of the co-operative movement. Particularly noteworthy in this

regard is the initiative concerning the parliamentary bill on co-operatives which, among other changes, proposes a different definition of co-operatives that stresses the subjectivity of their members. The bill states that “one goal of associating the members of a co-operative is to jointly run the enterprise in order to meet their economic, cultural and social aspirations and needs”<sup>1</sup>.

In this context, particularly noteworthy is the recent legal initiative, jointly undertaken by the Presidential Office and the Polish National Council of Co-operatives. The proposed bill, among other changes, differently defines a notion of co-operation stressing self-determined objectives by the members. The bill also replaces the principle of “joint social ownership” and re-introduces private ownership in a co-operative. It seems to provide a sound basis for the co-operative sector, legitimizing co-operatives as an integral part of the Polish economy.

Improving legal, fiscal, economic and institutional conditions for new co-operatives.

The newly emerging small co-operatives and co-operative-like entities need innovative legislative framework and fiscal incentives, including new financial instruments and more active position of the public sector, potential private partners, as well as promoting community finance through, among other forms, community trusts, community social economy funds and, tapping on informal finance existing within communities and social networks, developing micro credits and micro loans programmes.

A significant step forward towards elaborating specific legislation on social co-operatives is the recent Act on Social Employment, which became effective in January 2004. This law introduced social integration centres and social co-operatives filling the gaps in government policies on social exclusion and long-term unemployment, ensuring social education, career training, temporary and permanent jobs. Independently from the government legal initiative, the National Council of Co-operatives has proposed two other pieces of legislation on social co-operatives performing general interest services and co-operatives for school-graduates. Both legal incentives in question are at an early stage of elaboration.

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<sup>1</sup> J. Jankowski, *Czas na dobre prawo* (It is time for a good law), [www.krs.pl](http://www.krs.pl).

## 7. Conclusions

There are some prerequisites for paving the way to further development of new wave co-operatives. The first is the need to develop a suitable legal framework, funding mechanisms, management structures and an enabling infrastructure that will bring back and promote the main co-operative values and principles such as solidarity, cooperation, self-help and participation.

In view of the aforementioned analysis, the relatively small size of the co-operative sector at present is due to two historical factors: the drastically altered role of co-operative institutions under communism, and policies unfavourable to the co-operative sector since 1989. The recovery of the co-operative sector has been slow because the liberal government policies of the 1990s were much more oriented towards privatisation, commercialization, and individual entrepreneurship than towards private co-operative ownership and other collective forms of ownership.

As a result, the role of the Polish co-operative sector in the political and socio-economic system is undefined, fragile and unstable. Nevertheless, some sub-sectors of the Polish co-operative sector have been gradually overcoming the obstacles against their growth and are on their way up (credit unions, mutuals and new-wave co-operatives).

At the beginning of the twenty-first century the main challenges confronting the co-operative sector in Poland seem to be:

- establishing itself within the broader political system;
- establishing itself as an independent agent articulating local issues, needs, interests and concerns, and as a tool of local solidarity and socio-economic development;
- establishing itself in the emerging welfare mix;
- counterbalancing tendencies towards the individualization and privatization of behaviour in Polish society;
- mitigating the institutional crises and social conflicts of the transition period;
- fostering capacity through self-regulation;
- capacity building and sustainability.

To conclude, it should be stressed that no systematic research has been

conducted on the role of the co-operative sector in Poland during the transition period. Co-operative institutions have received little analytical attention and there has been a gap in empirical evidence on the potential and economic and social effects of co-operatives during the transition. This also concerns research on new co-operatives in the country, which are still 'terra incognita' in terms of their size, composition, financing, needs, effectiveness, main functions and drawbacks.

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# 11. The evolution of co-operative principles and the emerging Third Sector activities in Serbia

*by Marija Kolin* \*

## 1. Introduction

### 1.1. Overall socio-economic situation

General and long-term social decline and the dissolution of Yugoslavia following wars and other dramatic events during the past decade have had a negative impact on socio-economic development in Serbia. Turbulent political circumstances and severe economic deterioration have caused a general decline in living standards, uncertainty and pessimism in broad sectors of the population. According to experts, the disastrous decline in production, gross domestic product and the standard of living have pushed Serbia back three or four decades. At the end of the last century, transition in the country lagged behind that of other countries in the region as regards the openness of the economy, the amount of investments, the international relations established, technological cooperation, the decentralization of economic decision-making, and the extent of privatization. After the change of government in October 2000, despite pressing political issues and social turbulence which still hinder the modernization process, the priority of reform has been the social and economic system. In a new environment, where openness and democratic freedom prevail, the Serbian authorities have concentrated on macroeconomic reforms, while the necessary institutional and sectoral reforms have been given secondary importance. In 2003, the still collapsing economy produced salaries which were on average less than 200US\$, a GDP coefficient of 2,000 US\$, and a life expectancy at birth of 73 years for both sexes, while the classic 'socialist welfare system' was undergoing reform. As long as Serbia remains less

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attractive to foreign investors, social stability and employment will be problematic. As a consequence, it is all the more important to promote new forms of effective partnership and to increase the capacity of various alternative employment measures to foster social cohesion (Kolin, 2003).

## **1.2. Poverty and unemployment**

As a result of drastic economic decline during the last decade, the middle social strata have almost disappeared, while the majority of the population has been exposed to mass poverty and pauperization. According to research and statistics, such as for example the European Agency for Reconstruction's documents (Multi-Annual Indicative Program 2002), one quarter of the country's eight million people (excluding Kosovo) are poor, while an additional 20% constitute the 'near-poor'. Analysis of poverty according to social and economic category shows that urban worker households are most severely affected, but employees in non-productive branches of the economy (education, science, culture, judiciary, state agencies) are also victims of the drastic decline in the standard of living. The newly-impooverished population comprises the unemployed as well as employees and urban families.

Besides the traditional groups at risk - the sick, the elderly and the disabled - the bottom of the social ladder is occupied by other vulnerable groups, among them, according to the Serbian Ministry of Social Affairs are pensioners (1.5 million) and the unemployed (850,000).

Serbia has a persistently high unemployment rate of around 30% of the labor force. This concerns mainly long-term unemployment, with high proportions of young people, women and low-skill and unskilled workers. In the next few years, owing to restructuring and privatization, an additional million people are expected to lose their jobs. And unemployment is accompanied by a decline in individual and social standards, increased poverty, and a return to obsolete ways to satisfy the needs of the population, pronounced economic insecurity, uncertainty and pessimism. As a result, some studies suggest (Kolin, 2000) that poverty and social exclusion are serious obstacles against Serbia's transition to democracy and a market economy. At present, the social situation in

Serbia is complicated especially by an estimated 600,000 refugees who fled from war-stricken areas in 1991-1995 and 1999 after the NATO intervention. Their principal problems are unemployment and emotional stress, which especially affects refugee women and children, destroyed families, the elderly refugee population, the disabled, and the ailing.

### **1.3. Combating poverty and unemployment**

Since the change of government, one of the most important strategies has been the creation of a framework for secure economic and social growth which will be reflected in an improved standard of living and a reduction in the gap between average incomes in Serbia and in the EU member states. One priority has been the development of SMEs and other opportunities for new job creation. The main focus of the strategy is on generating economic growth and more employment, especially in food processing, manufacturing, tourism, and e-business. Institutional support and advocacy for the SME strategy have been provided by the newly-established Ministry of Economy and Privatisation, the Republic Agency for the Development of Small and Medium-Sized Enterprises and Entrepreneurship, Regional Agencies and Centres for SME Development, while the removal of legal and regulatory constraints on enterprises and a new legal and regulatory environment is intended to foster the development of new opportunities.

In parallel with employment creation strategies, since the beginning of the reform process, the government has sought to combat poverty and unemployment by means of other actions as well. The Poverty Reduction Strategy (PRSP), as a joint effort by the UNDP, the World Bank, the IMF and the Serbian government, is one of the main instruments with which poverty and unemployment are combated. The PRSP is based on a modern approach which recognizes the multidimensional nature of poverty and stresses social inclusion and equal opportunities in protecting the rights of poor people and other vulnerable groups. The main components of the PRSP strategy are a broader conception and policies to create new productive jobs for redundant workers in state-owned enterprises, and social instruments targeted on vulnerable groups through better social assistance, education

and health services intended to prevent social exclusion. Great changes are taking place in governmental policy in the field of employment and social programs for redundant workers during the period of privatization and economic reconstruction. The Labor Market Bureau (LMB) is the main governmental institution concerned with active labor market programmes, and it offers a full range of measures and initiatives tailored to the needs of beneficiaries. In similar manner to the programmes of international agencies such as EAR and the UNDP Rapid Employment Programme in South-Eastern Serbia, recently-established labor market projects include a number of innovative initiatives to provide employment in local communities. The best examples are pilot programs like the 'Job Clubs' which motivate the unemployed to look for work, or programs for disabled persons which provide job subsidies, services in job training and interacting with employers, and other programs in line with active labor market policy measures. These and other programmes targeted on poverty and unemployment are still in their conceptual phases, or in their early phases of implementation, and their impact is still to be felt by vulnerable groups in Serbia.

Taken as a whole, in the future transitional period, as Serbian society awaits the jobs which will arise from these economic changes, a more innovative approach will be needed to support other schemes for job-seekers. Such approaches should recognize the potential of social co-operatives, credit unions or mutual support societies in fostering employment and social cohesion.

## **2. Co-operative evolution**

### **2.1. History**

Serbia has a long tradition of co-operative enterprise which is closely connected with traditional family patterns, and with mutuality and solidarity as among the basic values and principles of the family way of life. Looking back, (The History of the Co-operative Movement, 2000) the co-operative movements that began in the middle of the nineteenth century in most countries in the world, and whereby people organized themselves in pursuit of a common goal, usually economic, had great

influence in Serbia. Because Serbia was a mainly rural country, the history of its co-operative movement centered on the agricultural collective farms and credit unions created at the end of the nineteenth century. The Association of Co-operative Farms of Serbia was established in 1895 as an independent interest and expert-business association of co-operative farms and other organizations. Through regional associations, membership of the association amounted to 995 co-operatives which organized production on the farms of both members and other farmers, supplied tools and equipment, processed agricultural products and sold them on domestic and foreign markets. In 1895, the Head Alliance of Serbian Co-operative Farms was established after enactment of the first Law on Agricultural and Artisanal Collectives in 1898.

During the Kingdom of Serbs, Croats and Slovenians (1918-1941), considering the level of economic development of the country, the collective movement was well developed: indeed farms constituted 82.7% of the total number of collectives. The majority of agriculture co-operatives were organized as credit and purchase collectives, while specialized production collectives (specialized in grain, dairy products, and wine, fruit, and apiculture products) were also established. These performed an important role in the processing and marketing of produce and in the purchase of agricultural equipment and supplies, but also in dealing with the social problems of communities.

After the Second World War, evolution of the co-operative movement was strongly influenced by the communist endeavor to collectivize the private sector of agriculture. The co-operatives became an integral part of the political system and the planned economy when their ownership was transformed into so-called 'public' enterprises without compensation, so that a significant amount of agricultural property came under government ownership.

The period since 1989 has been a new phase in the development of agricultural co-operatives in Serbia. The former legal regulation has been replaced by a set of new laws, most notably the new legislation (Law on Associations in Serbia, 1989 and the Law on Co-operatives and the Law on Co-operatives, 1996). According to the new legal framework, co-operatives are organizations of their members while their material basis

is collective ownership. Their task is to strengthen farming households as economic subjects and enable them to develop market relations.

## **2.2. New co-operative initiatives**

The program of economic restructuring since the democratic turnover has emphasized the revival of co-operatives as one of the main means with which to achieve an open labor market and the integration of disadvantaged workers. Whilst the Serbian public is not sufficiently well-informed about the significance of the co-operative movement and its importance in the contemporary economies of the developed countries, neither has Serbia adopted a proper legal framework within which co-operatives can flourish, nor have co-operatives been recognized or are present on the Serbian socio-economic scene (Kolin, 2002). Therefore, the scope of the modern co-operative movement (Ecological Co-operatives in Serbia, 2002), consists of agricultural and ecological co-operatives, and some initiatives by women, while still needed are promotion and an appropriate legal framework to regulate new co-operative forms. The following types of initiative are oriented to the development of the contemporary co-operative movement in Serbia.

### *2.2.1. Agriculture network of co-operatives*

The new co-operative movement in Serbia is mainly connected with the agro-economy modernization process that began with revitalization of the previous idea of co-operatives. The Association of Co-operative Farms of Serbia is a non-governmental business association established as an independent interests and expert association which fosters farm production and a modern business approach in agriculture. The association furnishes a wide variety of services in expert assistance, the protection of interests, representation and negotiations with government, and improvements in the legal regulation of agricultural production. An agro network has been established which comprises NGOs, associations, academic institutions co-operatives as well as prominent experts in the field to provide training, counseling, good practice exchange opportunities and other activities intended to promote entrepreneurship

in the Serbian agro economy during transformation. The new approach to cooperation in the agro economy often comprises programmes to revive local arts and crafts, hand-printed textiles, pottery and similar traditional activities. Work within co-operatives is mainly directed toward new products inspired by an artistic tradition which although ancient is adapted to contemporary needs and tastes. For example, co-operative unions of collective farms also promote cooperation in various fields of agriculture craftsmen guilds, consumer unions and other co-operatives.

### *2.2.2. Ecological co-operatives*

A special type of agricultural co-operative comprises ecological co-operatives as independent for-profit organizations usually with 10 to 20 members. These are small stock companies involved in organic farming and producing health food on democratic principles. The basis of organic agriculture is the use of natural fertilizers, biological and other natural remedies for plant and animal protection, and environmentally safe technologies proven to yield the best results. The goal is to achieve the global advantages of organic production development, to introduce and to educate people, and to show them the advantages of organic farming. These co-operatives also promote potential resources such as non-polluted fertile soil and clean water for organic production and for the development of profitable business.

These kinds of co-operative also provide the basis for other related activities, such as tourism, industry, education, science, and a large number of crafts, or they organize seminars and educate co-operative members and also members of their families on how to switch from conventional to organic production.

### *2.2.3. Co-operative initiatives in the women's movement*

Co-operatives have been recognized as improving the position of women in regard to political, economic and social development. The contemporary gender movement in Serbia is seeking to revitalize co-operatives as a creative means to achieve gender equality in the country's new circumstances. Given the current situation, where women are the

main losers from marketization during the transition process, the Association for Women's Initiatives has launched a project for co-operative promotion as a significant strategy to improve the social position of women. The initiative reflects the history of the cooperation movement, into which women were integrated from its beginning in the nineteenth century through international co-operative alliances. Given that people of various professions and qualifications are becoming unemployed, and that among them there is a large number of women, the 'Women's Co-operatives - A Challenge and an Opportunity' project focuses on the promotion of the new co-operatives as one of the most efficient ways to combat unemployment on the principles of equality, democracy and independence (Vujatovic-Zakic, 2001).

#### *2.2.4. Current international co-operative initiatives*

The donor programs in Serbia, such as USAID, European Union programs, UN agencies and the World Bank, that have followed the change of the government encourage political and economic change by focusing on poverty reduction and alternative solutions within the social economy framework as a core dimension in supporting national recovery.

Some of the new initiatives promoting alternative ways to achieve social and economic sustainability in Serbia after the democratic turnover start from the fact that the co-operative movement has a long history in the region and those co-operatives can become significant tools of social change which will foster social cohesion. For example, the USAID program implemented through six US based NGOs like American Development Foundation (ADF) and Community Revitalization through Democratic Action (CRDA) have started to promote co-operatives and long-term economic development through micro-credits and other schemes intended to increase economic power and income-generating opportunities primarily in agriculture-based communities. The community revitalization project implemented under the ADF/CRDA program in Vojvodina is currently operating in seventy communities located in twelve municipalities which comprise more than half of the two million population of Vojvodina. The project concerns not only

civic participation, infrastructure reconstruction and economic development but also the organization of farmer co-operatives and associations and assistance to small and medium-sized enterprises, thus providing substantial support for multi-ethnic Vojvodina. The similar CRDA program has started up in central Serbia with micro-finance, micro-enterprise and income generating projects mainly targeted on the most vulnerable social groups (Kolin, 2002).

With Serbia's transition to democracy, the EU has acted rapidly to support the population and the new authorities with various programs which target vulnerable groups and foster co-operative relations between government and non-governmental organizations. The EU has supported a number of projects directly or indirectly related to poverty alleviation through economic growth and enterprise development. For example, the support provided by the EU for reform of labor and social policy or involvement in the Poverty Reduction Strategy can be related to the activities of co-operatives. The European Agency for Reconstruction (EAR) as the European Community's main support agency has promoted a wide range of projects concerning the rural economy, privatization, enterprise development, and vocational education and training as part of the VET programme. Although the VET reform is still at an early phase of development, it is expected that vocational education and training will furnish various sectors of the economy with a skilled labor force by fostering employability. In this regard, co-operatives are a very promising option.

The current documents (Support of Civil Society in Serbia, 2003) pointed out that some international agencies as the EAR will cover key gaps in the protection of the most vulnerable groups in Serbia and provide a framework for the creation of synergies and social partnerships among social actors at the local level. It will provide more opportunities for NGOs to build capacity and implement direct services, furnish advocacy, promote participation by vulnerable groups, and mobilize volunteers. The program will also create subsidized employment within the social sector and other actions needed for social cohesion.

### *2.2.5. Main problems and prospects*

If the co-operative movement is to play an important role in the future open labor market, the work integration of disadvantaged workers, and the entire process of economic recovery in Serbia, the following issues must be addressed:

- establishing a coordination organization or clearing house for co-operative activities which maintains relation with the government and the international community and serves as a collective voice and catalyst for a whole range of issues regarding promotion of the co-operative movement;
- promoting a suitable legal framework and regulatory initiatives harmonized with solutions in the countries of the European Community or the advanced Central-Eastern European post-communist countries;
- facilitating a range of educational and training programs, seminars and courses to enhance understanding of co-operative forms of business and mutual societies for social services and to provide a solid foundation upon which the co-operative movement can be revitalized;
- publishing a specialized monthly magazine or bulletin for co-operative members and the wider public and disseminating reliable information useful for the understanding and promotion of new experiences and practices in the various fields in which the co-operative movement is active in Serbia, the region and the world.

In conclusion, then, reaffirmation of co-operative movement must start with building of the organizational and legal concept so that co-operatives can become powerful actors and catalysts for social reform, especially in regard to poverty, marginalization and unemployment. Moreover, not only must co-operatives be recognized as means with which to combat unemployment but the revival of the co-operative movement must generate new potential in co-operative enterprises by enabling them to deliver direct social services, and other types of non-traditional co-operative activity.

#### *2.2.6. Co-operative promotion in the third sector*

A starting point for the promotion of co-operatives could be the third-sector organizations already established in Serbia, especially through welfare programmes or community development NGOs providing protection for the most vulnerable groups in society (Kolin, 2000). It will be possible to achieve this with a comprehensive set of activities when the NGO sector has obtained better understanding of the co-operative movement, its legal and administrative framework, and the opportunities offered by non-traditional, social types of co-operative activity. Programmes organized among new co-operatives established by NGOs could be effective instruments with which not only to integrate disadvantaged workers into the open labor market but also to provide collective social services and other activities comprising a whole range of social and community-based actions.

#### *2.2.7. Third sector developments during the 1990s*

According to the NGO database compiled by the Center for Non-Profit Sector Development, a think tank organization established in 1996 by the Soros Foundation, there are more than 2000 alternative, autonomous, and innovative organizations in Serbia, and their number has rapidly increased since the political change (Directory of the nongovernmental, nonprofit organizations in FR Yugoslavia, 2000). The database also demonstrates the diverse fields in which the various NGOs are active: community services, education, culture, science, the arts, research, ecological groups, local community development, human rights and women's organizations.

As an important means to foster the values of democracy, the newly emerging third sector has laid the foundations for social change and has played a direct political role. Together with political forces, by organizing and channeling popular demands for change, Serbian civil society contributed to the political changes of October 2000. Following the shift to social transition and development, the Serbian third sector has attempted to mobilise its organizational capacity so that it can respond to the human costs of transition, combat poverty and unemployment, and

promote innovative programs for vulnerable groups. Owing to the dramatic increase of poverty and vulnerability during the transition process, civil society organizations have begun to realize their potential in improving the overall social situation, helping to provide welfare services, various kinds of psycho-social assistance, legal aid, counseling, occupational therapy, job creation activities, advocacy and other supplementary and innovative programs (Kolin, 2003).

#### *2.2.8. Social co-operatives initiatives*

##### *1. The work integration of the unemployed or the recently laid-off*

One can expect the main outcome of innovative employment through newly established co-operatives to be the work integration of disadvantaged workers in the open labor market. In a context of widespread unemployment - around 30% of the labor force (mainly low-skilled, semi-skilled and unskilled workers) is registered as unemployed, and around one million more are expected to become unemployed in the next few years due to restructuring - co-operative entities could offer alternative solutions by implementing integration through the social economy. NGOs in co-operative partnerships could assist with business incubator programs where already-existing organizations educate and stimulate business activities, offer training, provide counseling and undertake many other initiatives to encourage employment and profit-making activities in a socially inclusive society.

##### *2. Work integration of the vulnerable*

The integration of the most vulnerable groups in the society is a major indicator of social cohesion. With almost one-third of Serbia's population currently living below the poverty line, the programme of cooperation activities could encourage initiatives that promote equality of rights and opportunities for all citizens. Such a programme would be especially concerned with reducing widespread and chronic poverty and unemployment in various sectors of the population. Above all, different opportunities for job creation could be implemented through co-operatives that will foster the social integration of people with mental or social handicaps into active life.

### *3. Social services to the most vulnerable groups*

Despite the efforts at poverty reduction undertaken by the Serbian government and the international programmes targeted on vulnerable groups, a large part of the population in Serbia will need more welfare services tailored to their specific social needs or additional social safety nets to satisfy their basic needs and support social inclusion. Two types of co-operative - the member-oriented self-help co-operative or another type of co-operative which provides help to users - could be effective for those social groups at greatest risk. Co-operatives as social tools which foster social cohesion could be oriented towards the most vulnerable groups, namely:

*The elderly.* Owing to the increasing number of elderly people and the limited resources of the governmental institutions to meet their needs, it is important to increase the delivery of social services through new co-operatives offering various community social services, especially to the 'oldest-old' living alone in isolated rural areas without kin or an extended family.

*The disabled.* Social actions and community development programs are needed for the disabled, immobile or semi-immobile persons without family support. Physical, health, social and other types of home-care welfare services organized at the local level, personal assistance, day care centers, occupational therapy or socio-economic activities fostering self-esteem and inclusion could be provided by co-operatives. These could organize self-help groups or direct services to users provided by professionals and trained volunteers. Such activities should not be based on economic criteria alone but should also increase self-confidence and personal development, social cohesion and solidarity.

*The chronically ill.* Owing to the increasing risk of social deprivation during the transition period, chronically ill persons with weak family support may become extremely marginalized and isolated. Care-giving programmes involving day-care centers, volunteer activities and services delivered at home, different kinds of psycho-social counseling and other forms of support would be provided on the local level as supplements, innovations or alternatives to governmental programmes

Such a comprehensive programme for the future development of the co-operative movement should address the problem of the present

unfavourable legal and fiscal environment and strengthen the professional competence and reliability of the emerging organizations in Serbia. In addressing these problems, information or educational centers could be established to collect, evaluate and distribute the experiences and best practices that can help the social actions and welfare programs implemented in the new co-operative forms.

A social co-operative national information center could collect information on different types of socio-economic activity and provide counseling, education, training courses and other learning opportunities for volunteers and professionals as the main protagonists so that they may learn the meaning of the new approach in social policy. Co-operatives with social protection functions like those in care services, health care, education, environmental protection, as well as other fields of activity where these organizations demonstrate remarkable social responsibility, could be also promoted by future social policy in Serbia.

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## 12. The Czech co-operative reality and its social aspects

*by Magdalena Hunčová \**

### 1. Introduction

I start by recounting my experience of research on co-operatives. I began my doctoral research on ‘analysis of the co-operative’s position in the transition economy’ five years ago. When I first addressed the theme of co-operatives, my questions were:

- what is a co-operative?
- what is a Czech co-operative?
- what are the nature and role of co-operatives generally?
- what is the role of co-operatives in a transition economy?
- are co-operatives still modern?

The motto of my research could be: “The cultural appeal of co-operatives and mutual bodies to European researchers is found in the fact that they practise direct grass-roots economic democracy” (Pestoff, 1995).

I greatly agree with the authors of the International Joint Project on Co-operative Democracy when they write: “If we aim at citizens seeking cooperation, however, we must recognize the limits to the role of the public sector and the private sector and explain the role of the social sector ... It cannot be formed and function solely through representative democracy. ... The present can be seen as a period of transition ... to a different or new society... based on the initiative of individual citizens in their communities” (Centre for the Study of Co-operatives, 1995).

Much of the knowledge presented as outcomes of my doctoral research (conducted at the Masaryk University of Brno at the beginning of 2003) seems unknown in the Czech Republic of today.

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## 2. Some details of my research on the co-operative phenomenon

The first stage of my research consisted in a bibliographical search conducted in order to define the co-operative phenomenon and make some operational definitions. Some differences between Czech co-operatives and others were identified.

The second step was to analyse co-operatives in light of a theory of public economics and its thesis of a public good and common one, namely the Pestoff 'welfare mix triangle' scheme (Appendix 1), the purpose being to determine the position of the co-operative within the socio-economic space in general, and to identify the operational field of co-operatives as well as an area of their fluctuation. The ICA 1995 Co-operative Identity Declaration was used as an international standard for the authentic co-operative and as a measure of the Czech co-operative reality.

World-wide debates on co-operative legislation helped me understand some limitations in current 'co-operative' law in the Czech Republic, where co-operatives are regulated by the Czech Commercial Code. My research drew a map of co-operatives both in the Czech Republic and externally to it. It provided a clear and understandable picture of the nature of co-operatives, their activities, abilities, and their role in the transition period.

The operational field of co-operative bodies was found to lie on the border between the non-profit and commercial sectors, and its extremes in the public sector, commercial sector, and the informal sector of communities, within the area of fluctuation depicted by the Pestoff welfare triangle<sup>1</sup>.

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<sup>1</sup> There are three interfaces in this triangle. The first line divides the non-profit/commercial sectors; the second the public/private sectors; and the third the formal/informal sectors. There are three sectors at the corners: commercial, public and communities plus the third (non-governmental non-profit) sector in the middle. The third sector of European provenance includes not only NGOs but also many organizations heterogeneous in their activities and relationship subjects. The feature shared by them all is the self-governance of 'associations and symmetries of interest'. This is the 'self-governed civil mix sector' depicted as a circle within the welfare triangle - see Appendix 1.

The authentic co-operative is both an association and an enterprise controlled by the members which operates in accordance with international co-operative identity standards (ICA, 1995)<sup>2</sup>. Hence, an authentic co-operative is a *binary subject* funded as a *symmetry of interest*. Because of its binary nature, the operational field of a co-operative's identity and activity comprises for-profit and commercial sectors.

Co-operatives fluctuate within their operational field and may tend towards its extremes:

- when a co-operative shifts too far towards the commerce sector, it tends to change its legal form into that of a company and to *lose its mutuality and self-help dimension*. Moreover, such co-operatives may lose their property (capital) in the Czech transition economy, and this applies to housing co-operatives as well;
- when a co-operative body shifts too far towards the public sector, it tends to lose its *autonomy and voluntariness*. When a co-operative is used as a tool for social policy, its autonomy and voluntariness cannot be preserved sufficiently and it is at risk of the corruption present in any social state;
- when a co-operative body shifts too far towards the community sector, it may encounter a crisis of communities. But co-operatives are 'at home' in this sector because of co-operative mutuality and their self-help grass roots. Social co-operatives naturally operate in this sector.

Consequently, an authentic co-operative is a binary non-profit organization, a mutual self-help symmetry of interests. A co-operative usually produces socially positive externalities, this being the nature of co-operatives. It is a democracy of economy as a part of a civil direct democracy. It is (a small) business controlled democratically by co-operative members, and its 'capital is employed by labour'. This binary dimension comprises both the strength and weakness of co-operatives. Co-operative symmetry is a legal element of a civil society.

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<sup>2</sup> See: [www.coop.org](http://www.coop.org)

### 3. Worker co-operatives and consumer co-operatives

- A worker co-operative is an authentic co-operative whose capital is employed by its labour. The members of this type of co-operative are both employees and employers (and perhaps also consumers). Such co-operatives usually associate their member's work or produce products or services to ensure their members *employment*. The interest of their members is economic, social or cultural assistance for themselves, their families and their communities; but *employment* is the primary interest and benefit of mutuality. The consumers of any co-operative product or service may be members and their families, as well as communities as an extra and beneficial side-effect;
- A consumer co-operative is an authentic co-operative with its capital managed by labour. Members of this type of co-operative may be both customers and producers and simultaneously have employment positions within it. The interest and benefit of members is usually economic, social or cultural assistance for themselves, their families and their communities. Their benefit may consist of good cheap foodstuffs and other products of daily use (consumer co-operatives and producer co-operatives), good cheap services (service co-operatives, social co-operatives) or cheaper loans (credit unions and saving co-operatives), competitiveness (traders, stocks and sales co-operatives) or quality and easy-to-get housing (housing co-operatives), etc.

The social co-operative also seems to be an authentic form, although it serves not only its members but their community. A social co-operative is a consumer co-operative which mutuality weakens and self-help strengthens.

As noted before, the operational field of co-operatives extends through the non-profit and profit sectors. Authentic co-operatives usually fluctuate on the border of these sectors.

- Consumer co-operatives are usually under pressure by market competition and globalisation to change their position from the border between sectors to the market sector. Co-operative members may lose their mutuality through the action of co-operative managements as their positions grows stronger. Co-operative

property tends to become capital (which means ‘labour managed by capital’), and the co-operative tends to change its form into that of a company. To safeguard the co-operative identity and the social role of co-operatives it is necessary to protect their mutuality and non-risk capital by law in order to preserve the human dimension of the market furnished by co-operatives.

- Moreover, housing co-operatives and social co-operatives<sup>3</sup> are under pressure from public social policies and public finances. They may lose their autonomy and voluntary principles and move into the public sector. The Legislative Commission of ICA<sup>4</sup> has reported a number of such manoeuvres. Governments in Asia and Oceania had promoted the co-operative movement in order to develop their countries: co-operatives were established, ruled and financed by government and they consequently lost their self-governance, autonomy, voluntarism and mutuality. Co-operatives were thus unable to perform their role in regional development and a pro-corruption environment was encouraged. If co-operative identity and self-governance and autonomy are to be protected, it is necessary to support them only initially with public funding or fiscal exemptions, for only authentic co-operatives can play a role in citizen empowerment.

#### 4. An outline of Czech co-operative history

The Czech co-operative movement thrived under the Austro-Hungarian monarchy and in the Czechoslovakian Republic from 1847 until 1938. The Prague Foodstuff and Saving Fellowship (*Prager Viktualien- and Sparverein*) appeared as the first co-operative in 1847. In the following ninety years, the co-operative movement flourished as co-operatives wove together a rich network, with credit co-operatives<sup>5</sup> as the middlemen.

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<sup>3</sup> Social co-operatives furnish health services, daily assistance services, services for the excluded (handicapped), etc.

<sup>4</sup> Paez (2000), as member of the ICA Legislative Commission for the region of Asia and the Pacific.

<sup>5</sup> There were two types of credit union in the Czech area: Schulz-Delitsch and Reiffeissen-Kampelik.

For example: In 1920 there were 3,820 credit unions with 409 thousand members in the Czech region.

**Table 1 - Number of credit unions (1925-1947)**

1925	4,006	506
1930	4,269	646
1945	3,625	1,070
1947	4,248	1,306

Co-operatives were regulated by a specific law of 1873 which was subsequently revised in 1903. Every type of co-operative was a binary, autonomous, self-governed, voluntary, mutual, self-help, open, etc. body. Co-operatives worked in networks centred on credit-saving and store co-operatives. Czechoslovakian co-operatives lost their autonomy in 1938 when they were brought compulsorily under the management of unions controlled by the state.

After 1948, the previous co-operative law was abolished and co-operative ownership became socialist. Co-operatives lost their democracy (the managers were installed by the Communist Party), mutuality and self-help (under a centrally planned economy), voluntariness (duty of fields and property collecting and duty of membership) and autonomy (under total politics). Credit-and-saving co-operatives with all their assets and liabilities were taken over by the state savings bank in 1954. Only housing co-operatives preserved some of their self-help dimension during the totalitarian period, in that members had built their flats with their own hands as a collective effort with a state financial endowment. The ownership of flats was corporate.

The government once again obstructed Czech co-operatives after 1992. Co-operatives became enterprises owned by their members under the Czech Commercial Code. They then lost their mutual and self-help dimension next and almost that of binarity, as well as their social dimension. Co-operative ownership (essentially collective private) was transformed into (individual) private ownership by the Transformation Law. Moreover, privatisation deprived co-operatives of many useful shop and service outlets. Transformation costs have been estimated as

amounting to nearly 40% for agricultural co-operatives, for example. Many co-operatives have now changed their legal form or have collapsed.

Czech co-operatives continue to be open legal bodies with by-laws and some democratic principles in the control of capital. They may be established by a minimum of five physical persons or two legal bodies. However, we may view Czech co-operatives as being social enterprises. Some examples follow.

1. Housing co-operatives have been transformed by the Housing Law of 1994, which states that an occupier of a state-owned or co-operative flat is entitled to buy it as his/her own individual property, and that the co-operative is obliged to sell it. Czech housing co-operatives as legal 'profit' entrepreneurs now often associate their occupier-members and occupier-owners (both members and non-members) by means of a concordat.

New flat-owners are allowed to leave a co-operative and make themselves independent when the block of flats is full. Many separate blocks of flats have divided in order to create new housing co-operatives or citizens associations, or to remain extraneous to the legal form. But problems with the maintenance of such houses has led to new 'chop-logic' legislation set within the housing law of 2000: new flat-owners are legally obliged to establish a housing society and likewise when they constitute a citizens association. A housing society has been defined as a non-profit organization since October 2002. There is only one legal non-profit 'co-operative' at present<sup>6</sup>.

Under the Commercial Code, a housing co-operative is now an entrepreneurial and for-profit body. But an entrepreneurship property may sometimes be 'privatised through bankruptcy'<sup>7</sup>. Consequently, flat owner-occupiers as well as member-occupiers may lose their flats entirely or they may have to purchase them again. These are flats which they have built with their own hands and bought. The problem arises because members' property, like that of NGOs, is not protected by law, nor by

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<sup>6</sup> Some positive changes are expected to be introduced in 2004.

<sup>7</sup> Co-operative managements sometimes do not pay co-operatives liability caused by bankruptcy in order to buy up the property.

membership and mutuality. The new law on credit unions came into force in 1995. Many credit unions were created prior to 1998 and this sector of the financial industry grew to remarkable size. To attract new members, the interest on deposits was set unusually high. But then in 1998 the Czech Minister of Finance spoke on television about the low credibility of credit unions, with the consequence that many of their members withdrew their deposits and credit unions collapsed; now only truly mutual credit unions remain. The state savings bank was privatised at the same time. Today's credit unions do not create networks with other co-operatives. To stabilize the sector a law of 2000 has established new conditions for credit security funds held by the state.

Historically, the co-operative movement was a response to the failure of the market mechanism in the first half of the nineteenth-century. This response was based on a new combination of production factors (*capital managed by labour*), and the solution for the problem was devised at the micro-economic level. Social or welfare states have instead sought to solve the same problem at the macro level. It is therefore understandable that co-operatives are still inappropriate and strange to both socialism and capitalism in the Central and Eastern European countries.

On the other hand, this thesis may explain why co-operatives are involved in European social policy (welfare mix) and why the expectations of co-operatives concern prosperity.

## **5. Co-operatives and transition**

The research discussed demonstrates the precarious condition of Czech co-operative enterprises and highlights the confusion of the legislation that currently regulates them. Czech co-operatives have lost their elements of association and mutuality and become only worker/consumer-owner co-operative enterprises. Czech law has freed co-operatives from their identity twice, in 1948 and in 1992. No specific co-operative law now exists in the Czech Republic, so that there is a very narrow area for labour to associate itself (capital employed by labour) or democracy to arise in the economy (capital managed by labour). The state and the market still predominate in the economy, although civil

society is developing. Moreover, the market increasingly overflows into the social area under state budget deficits.

Co-operatives as symmetries of interest could perform a specific role in the transformation of the economy and society as a school for democracy, as a school for business and as a bearer of ethics. Authentic co-operatives could sustain the development of human, work and social capital in that co-operatives build citizens' solidarity capital and their independence and responsibility. Co-operatives could be an important element in the social economy and participate in policies for employment, social cohesion and regional development. Nevertheless, Czech law and policy have not to date given co-operatives a chance to perform these roles. Czech social policy does not take co-operatives or other symmetries of interest into account. The civil direct democracy and economic democracy are lacking in the Czech Republic. But the transition is ongoing.

Some transfer of responsibility to lower levels has been achieved by the reform of the Czech public administration in 2000. The Czech public sector still predominantly delivers social assistance; apart from assigning a subsidiary social role to the market (and to certain alternatives). The municipality has been a traditional welfare provider at the Czech local level since the reign of Maria-Therese in the second half of the eighteenth century. The social state today has not relinquished its welfare decision role. In parallel, some other forms of NGOs have taken over the social role of social co-operatives. It is consequently difficult to develop any social co-operative under such conditions; even if the special law for social co-operatives is in place.

On the other hand, it is possible to recognise quasi social co-operatives (as social enterprises) when examining some of the Czech producer co-operatives. In the 1950s, co-operatives of handicapped workers were established and financed by the Czechoslovakian totalitarian state. Some of these co-operatives survived the co-operative transformation and still employ handicapped persons (members included). They operate in a difficult environment of market competition without, in principle, any support in the form of public funding, but only have the endowment of pro-employment policies as protected workshops.

## 6. Conclusions

- A co-operative is a socio-economic body operating on the border between the profit and non-profit socio-economic sectors with extremes in the commerce, public, and community sectors.
- A co-operative is a self-help mutual symmetry, which means a binary body combining the non-profit association of members with the enterprise democratically controlled by those members.
- The co-operative movement was the response to the market failure of the nineteenth century; a response which took the form of a new combination of production factors: 'capital employed by labour' at the microeconomic level.
- Cooperation is expected to be a school of economic democracy, of small business and a bearer of morality. Co-operatives could be serious partners in a welfare mix.
- The dimensions of a co-operative are notably autonomy, self-government, self-help, mutuality, binarity, civility, non-profitness, voluntariness and solidarity.
- The positive externalities produced by co-operatives are factors in community and regional development, social cohesion, and employment as an element of social economy.
- Co-operatives are now operating and spreading throughout the world. Cooperation is a typical form of economic activity and association.
- Co-operatives are usually of two types: (a) worker co-operatives with working members, (b) consumer co-operatives with member-customers or clients.
- Both the development of the co-operative movement and trust in society may, as the opposites of a pro-corruption climate, be measures of the success of a transition economy.
- The Czech co-operative movement became 'unwelcome by politics' and suppressed by law in 1948 and again in 1992. It thus lost its main dimensions of autonomy and voluntariness.

- The Czech co-operative became an 'enterprise owned by its members' and tended to change its form into that of a company. It lost its non-profit character, mutuality and self-help.
- Citizens associations and foundations on the one hand, and municipalities and the state on the other, took over the co-operative's social role at the local and regional levels.
- Government social policy now prefers public agencies in community social care for reasons of expertise (as regards abandoned baby day care, for example). The socio-economic sphere is diversified between public power and the market.
- Direct civil democracy is undeveloped. Mutual and self-help principles do not work. Non-risk capital wants to be protected. There is no specific law on co-operatives. Practically no association is active except for chambers of professionals. It is necessary to promote the co-operative phenomenon and empower citizens in respect of governments, politicians and the law. A specific co-operative law is necessary to this end.
- Some social co-operatives (social enterprises) can today be recognised as producer co-operatives of handicapped persons employed in protected workshops. These were all established in the 1950s, none of them recently. Other social enterprises have different legal form and are not co-operatives.

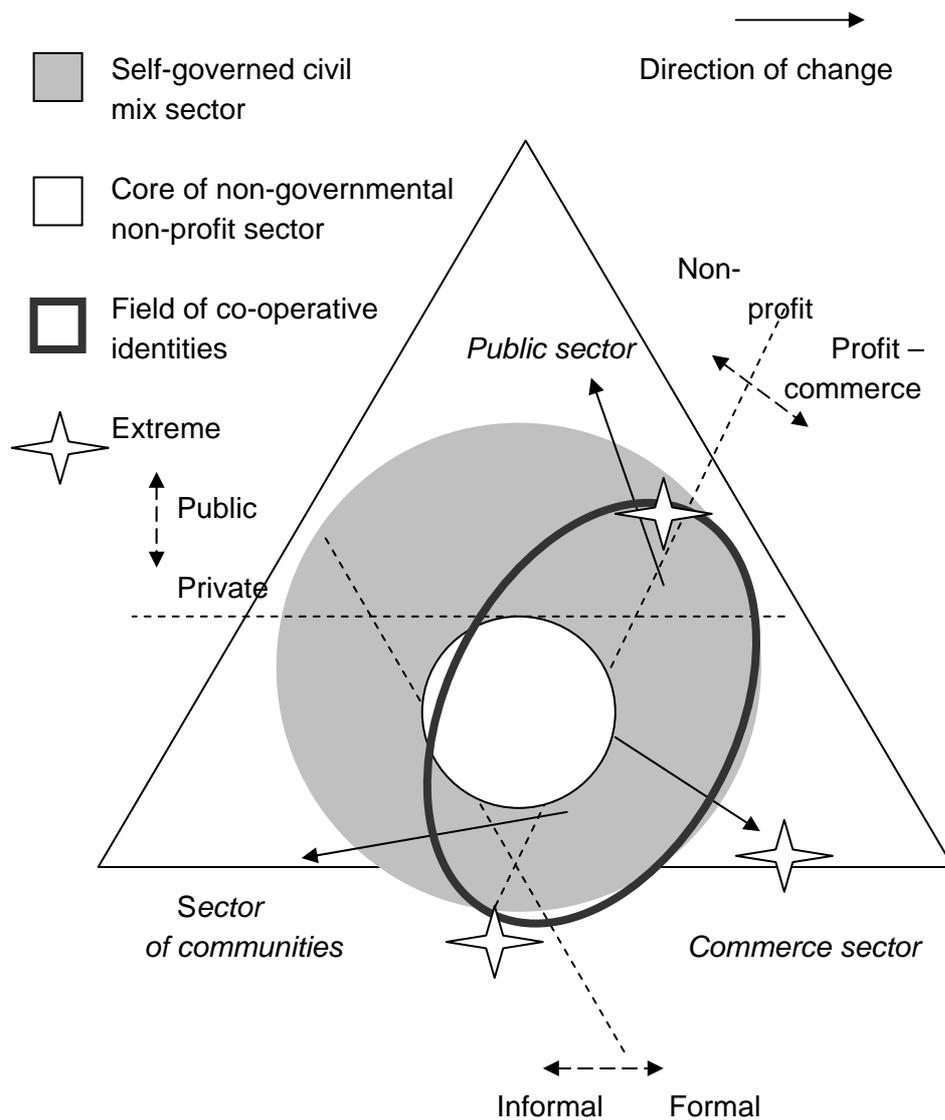
The research set out in this paper should be continued in order to sustain the process of cultivating the Czech socio-economic environment at the gateway to Europe.

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## Appendix 1

### Field of co-operative identities within the balanced civil mix sector and directions of change



Source: Hunčová, M. (created the Pestoff "Welfare Triangle")

## Appendix 2

### Some figures on co-operatives in the Czech Republic (1997, 1998, 2002)<sup>8</sup>

a) As of 31 December 1998:

	Housing co-operatives	Consumer co-operatives	Producer co-operatives	Agricultural co-operatives	Credit co-operatives
Unions and associations	SČMBD	SČMSD	SČMVD	SZDS	ČAZ
Number of co-operatives	1,045	69	402	827	75
Number of members	*	517,657	23,700 and 53 other bodies by law	*	62,300
Number of employees	*	23,549	34,200	75,979	*

b) As of 31 December 2002:

Unions and associations	SČMSD SMBD SDLBD	SČMSD	SČMVD	ZDS	ČAZ
Number of co- operatives	764	63	335	698	46
Number of members	*	397.031	14,400 and 40 other bodies by law	*	14,200
Number of employees	*	17,184	27.500	45,000	*

\*) Not monitored

<sup>8</sup> *Briefing about Czech co-operative movement in 1998*, The Czech Co-operative Association, Prague 1999, and *Briefing about Czech co-operative movement in 2002*, The Czech Co-operative Association, Prague 2003.

Housing co-operative system (SČMBD, SMBD, SDLBD)

	1997	1998	2002
Number of members	*	*	*
Number of co-operatives	996 <sup>9)</sup>	1,045 <sup>10)</sup>	1,764
Number of commenced flats	366	363	1,246
Number of flats under construction	756	771	2,195
Number of completed flats	168	152	807
Total number of flats	801,530	718,511	733,851

\*) not stated

Credit co-operative system<sup>11)</sup>

	1997	1998	2002
Number of credit unions	70	75	46
Number of members	25,533	62,300	14,200
Total of deposits (savings) of members in mil, Kc	1,126	4,200	959
Total of provided credits to members in mil, Kc	372	1,900	576

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<sup>9</sup> Consisting of 437 small housing co-operatives created by means of separation of part of a bigger co-operative or, as a new possibility, by the sale of municipal flats and houses – these data constantly change given the privatisation of co-operatives and municipal housing and house-holding property. At the same time, some newly created co-operatives or societies do not join a Union.

<sup>10</sup> Including 500 small housing co-operatives, likewise.

<sup>11</sup> Out of 75 credit unions in 1998, 38 were members of the Czech Association of Credit Unions.

## Agricultural co-operative system

	1997	1998	2002
Number of co-operatives	1,011	827	698
Number of workers	89,480	75,979	45,000
Agricultural land in hectares	1,364,000	1,234,455	988,000
Number of member organizations of SZDS*)	1,090	1,020	1,018
including: agricultural co-operatives	795	617	510
joint-stock companies	167	237	456
limited companies	113	126	52
the others etc.)	15	40	1,349

\*) And agricultural enterprises united in Association including

## Producer co-operative system

	1997	1998	2002
Number of members	30,000	23,700	14,400
Number of co-operatives	419	402	335
Number of workers	40,000	34,200	27,500
Number of non-co-operative bodies	0	53	40
Wage resources	3,940 mil, Kč	3,673 mil, Kč	3,785 mil, Kč
Average monthly earnings in Kč	8,208	9,000	11,500
Economic result	680 mil, Kč	430 mil, Kč	394 mil, Kč
Turnover	21,000 mil, Kč	19,007 mil, Kč	21,100 mil, Kč
Volume of exports	3,900 mil, Kč	3,674 mil, Kč	4,780 mil, Kč
Value added	*	5,758 mil, Kč	5,942 mil, Kč

## Apprenticeship education system of producer co-operatives

	96/97	97/98	00/01	02/03
Number of apprentices	996	863	297	250
Number of training institutions	31	29	6	5

Consumer co-operative system

	1997	1998	2002
Number of members	555,499	517,657	397,031
Number of co-operatives	69	69	63
Number of employees	24,932	23,549	17,184
Total retail trade turnover in mil, Kč of current prices	27,932	28,866	26,887
Including: total number of shops	27,810	27,735	26,826
Catering establishments	164	131	61
Number of retail shops	4,004	3,834	3,062
Including: supermarkets	49	60	138
Department stores	7	4	3
Shopping centres	170	126	34
Grocery shops	3,060	2,942	2,544
Discount shops	76	90	50
Number of catering establishments	76	55	28
Wholesale turnover in mil, Kč of current prices	13,887	13,378	11,246
Number of wholesale warehouses	90	64	39
Gross storage capacity in m <sup>2</sup>	256,537	228,895	138,002
Volume of grocer's production in mil, Kč	532	549	375

Educational system of SCMSD and co-operatives

	No: of schools			No: of students			No: of employees		
	1997	1998	2002	1997	1998	2002	1997	1998	2002
SOU, SOŠ, and OŠ	16	15	11	6.181	4.322	4869	706	605	584

SOU = Co-operatives apprenticeship Training School

SOŠ = Co-operatives professional High School

OŠ = Co- ops professional School

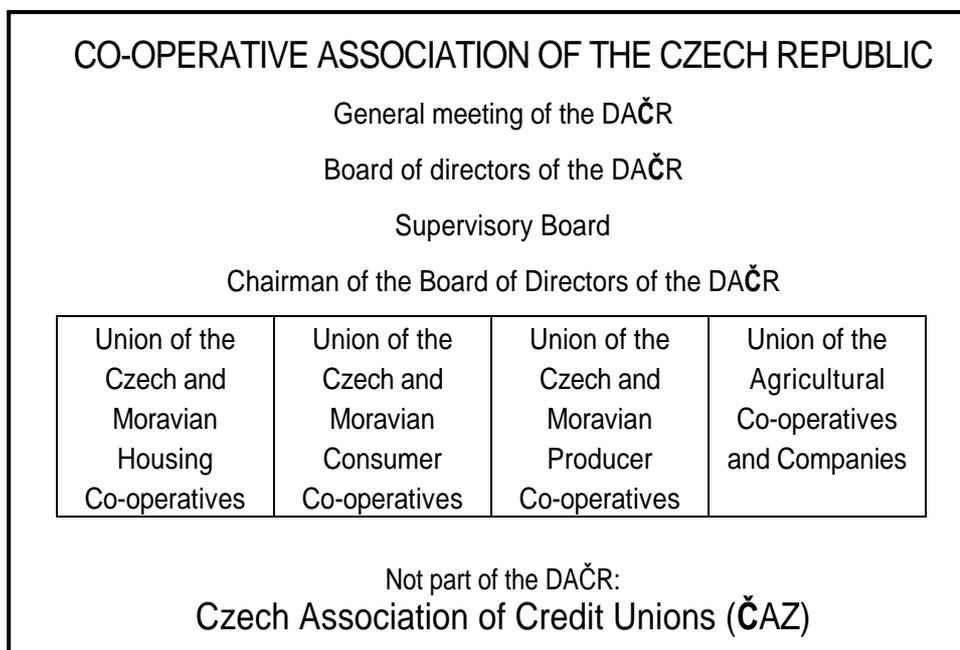
*Comment:*

- Czech credit unions association (ČAZ) is not a member of the Czech co-operative association (DAČR), and some credit unions are not members of the CAZ.
- Czech Co-operatives Association (DAČR) is an association of co-operative unions of all types except for credit co-operatives; some housing bodies are also separate.
- Co-operatives schools are established as Ltd. (s.r.o.)

*Abbreviations:*

- SČMBD – Czech-Moravian Housing Co-operatives Union
- SMBD – Union of Small Housing Co-operatives
- SDLBD – Union of ‘Folk’ Housing Co-operatives
- SČMSD – Czech-Moravian Consumers’ Co-operatives Union
- SČMVD – Czech-Moravian Producers’ Co-operatives Union
- SZDS – Agricultural Co-operatives and Societies Union
- ČAZ – Czech Association of Credit Unions

Framework of the Czech Co-operative Association (DAČR)



# 13. The co-operative model in Bulgaria: Prospects and problems of the social economy

*by Maria Jeliazkova\**

## 1. Introduction

The years of transition in Bulgaria have been accompanied by a contradictory development of the social economy, periodic and irregular political interest in it, as well as a certain amount of research on its various forms. The specific model of economic restructuring has resulted in the social exclusion of large groups, forcing them outside the normal mechanisms of market exchange, and especially outside the labor market. The growing risks and restricted access to basic services for increasing groups of people, the privatizing of social security systems, the pressure on basic social and economic rights (labor, health, insurance, educational, etc.), the decrease in state social costs and the deregulation of social services have made coping mechanisms urgently necessary.

In this situation the opportunities for survival of vulnerable groups depend on a narrow range of strategies: notably, reliance on the safety nets of social policy, migration, and inclusion in the gray and black economy. There are numerous data indicating that all these strategies are widespread in the country.

The social economy is another way to provide people with an economic niche and help them cope with risks and crisis through mobilization and cooperation. As a collective strategy it represents social entrepreneurship, and it is a spontaneous business incubator which provides opportunities for economic freedom for groups in the population which cannot satisfy their basic needs within the framework of the formal market mechanism. “Research on European nations has already demonstrated that the waves of growth in the social economy have arisen primarily during major transformations...” (Defourny, Develtere, Fonteneau, 2000). Thus social

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economy-type enterprises in Bulgaria have emerged in response to the current economic and social crisis. They tend to shape a segment in the national economy which functions in a specific economic regime. Functionally, the social economy provides socio-economic initiatives for particular groups in the population whose basic resources are social and human capital. The organizational specific is linked with the mechanisms of collective decision-taking based on internal solidarity, collective identity, a feeling of belonging, confidence and voluntary participation. “Generally speaking, we are referring to collective socioeconomic initiatives for the creation of enterprises or productive organizations, whose distinguishing feature is a capacity to find innovative, dynamic solutions to the problems of unemployment and social exclusion and to contribute to the type of economic development that enhances social cohesion, which is one of the facets of sustainable development... The emphasis is on economic enterprise with a social content...” (Maciel, 2003).

The distinctive features of this kind of enterprise are the following: a) financial profit is not the main criterion for efficiency; b) the intensity of accumulation is comparatively low because the technologies applied are more labor intensive than capital intensive; c) ‘free’ market exchanges are restricted and consequently the level of competitiveness is comparatively low; d) the enterprise provides jobs and broadens access to goods and services, often delineating the border between providers and users; e) the result is an increase in opportunities for income-generating activities and the life chances of socially excluded groups; f) one effect is the more even distribution of income.

Accordingly, co-operatives and NGOs in Bulgaria can be considered forms of development of the social economy. Both perform this role by cooperating on available resources (human, financial and material), uniting social and collective principles and entrepreneurial features. Member-oriented organizations prevail in the rural model (mainly in the form of agricultural co-operatives), while structured organizations supplying public goods are spreading in urban areas. The development of both forms has encountered serious difficulties as the country adjusts to a market economy.

## 2. Forms of social economy

### 2.1. Non Governmental Organizations (NGOs)

It can be stated that NGOs in Bulgaria are closer to the social economy as conceptualized by most authors. There are around 10,000 registered NGOs, and according to rough estimates half of them are effectively in operation and around one third have a declared social orientation. Two important factors have driven the large increase in the numbers of NGOs during the transition period: 1) the availability of various donor programs which have invested in projects characterized by social aims; 2) high rates of unemployment and strong pressure on the salaries and wages of the employed.

**Table 1 - Trends in NGOs' development**

<i>Capacity:</i>	<i>Positives</i>	<i>Negatives</i>	<i>Outcomes</i>
Rapid development during the years of transition (around 10 000 NGOs);	Numerous projects	Isolated improvements	Safety net for incomes and employment for highly qualified personnel
Large share of highly educated people	Gradual capacity building	Lack of sustainability - more than 70% of the projects end when the financing ceases	Alleviation of poverty
Second employment	Provision of social services in various spheres (health care; education; anti-poverty; employment) and for different vulnerable groups	Excessive dependency on donor programs	On the margin between the formal and informal economy
High concentration in the capital and cities	Development of some good practices	Low negotiating power	Danger of establishing para-state and para-business NGOs
		Lack of transparency	Contradictory effect on inequalities

The enormous fall (by 70%) in the living standards of the highly-qualified employed as well as the uncertainty of employment have been and continue to be stimuli for NGO establishment. Correspondingly, highly educated people have established NGOs mainly in the capital and the large cities. According to financial streams, NGOs work with different vulnerable groups to develop anti-poverty activities. Highly qualified labor in the NGOs is a precondition for participation in decision taking. Also to be observed is a trend towards the conversion of NGOs into social service providers<sup>1</sup>.

## 2.2. Agricultural co-operatives

There are around 6500 registered co-operatives in the country, and the majority of them are rural co-operatives. They adhere to the traditional model of agricultural production and represent a strategy for survival of rural communities. Agricultural co-operatives are set up to cooperate available resources, and their social and collectivist orientation is secondary and greatly subordinate to economic ends. A very thin segment of the personnel, forming the managerial staff and providing more qualified labor, is decisive for decision-making in co-operatives. Thus member participation in management is seldom to be observed, and dissatisfaction results in workers leaving the co-operative and joining another co-operative in the same village, if one exists. Rural co-operatives cultivate more than 40% of arable land in the country and annually provide employment for 29,4 thousand people. A recent survey (Jelyu, 2003) has shown that in 1999-2001 agricultural co-operatives were the most unsuccessful unit in agriculture. All the basic indicators were reported as diminishing (decreases of 34.5% in the number of employed; 30.2% in the volume of production; 17.9% in long term assets; 23.8% in productivity; 31.7% in the market share; and 18.1% in technological innovation). At the same time the dependency of co-operatives on outside monopolistic business structures is increasing.

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<sup>1</sup> Survey on NGOs in Bulgaria, Anti-Poverty Information Centre, Sofia, 2002; National Report on Social Services, ILO, Budapest, 2004.

**Table 2 - Trends in development of agricultural co-operatives**

<i>Capacity</i>	<i>Positives</i>	<i>Negatives</i>	<i>Outcomes</i>
Around 3000 co-operatives	Long (more than a century) tradition in providing opportunities in economic crises	Low market orientation	Income generating strategy for people in rural and urban areas
Agriculture is the main source of employment for 368 500 people and the secondary source of income for around 1000000 people	Spontaneous use of social capital	Market failures (the proportion of unsuccessful co-operatives has increased in the last three years from 26% to 44%);	Increases the incomes of retirees
Around 60% of co-operative members are aged over 60	High share in employment of rural population	Low negotiating power	Decreases poverty depth
Provides some opportunities for the inclusion of ethnic minorities	Development in new fields (for example, environmental production, child care)	Low access to credit	Supports informal economy
		Inadequate legal framework	Scant effect on inequalities

### 2.3. Specialized enterprises for the disabled

Restricted opportunities for the inclusion of the disabled in the competitive labor market and the need to provide them with economic niches are often basic arguments in support of social economy development. A further benefit of the co-operative model is its ability to neutralize the danger of labor market segmentation and to counteract attempts to profit from the illegitimate use of disabled labor.

Data show that in the period 1990-1996 (Centre for Vocational Training and Rehabilitation, 1997) in Bulgaria the number of the disabled employed in specialized enterprises, registered as both companies and co-operatives, decreased by 50%. In 2002 there were 91 specialized enterprises for disabled workers in the country employing 14,573 people, among them 7,920 disabled<sup>2</sup>.

<sup>2</sup> Data from the "Rehabilitation and Social inclusion" Fund.

Studies show an enormous decrease in the activities of the specialized enterprises engaged in specific productions before transition (plug industry, suitcase industry, tailoring, shoemaking, etc.). Obviously, when they were subordinated to the general institutional framework and forced to participate in 'free' market competitiveness, such enterprises could hardly survive. Analyses have pointed to pressure by mega structures (different unions) on specialized enterprises; attempts to neutralize collective decision-taking mechanisms and their replacement with hierarchies; attempts to use state budgets earmarked for the disabled in non-legitimate ways; extremely weak opportunities for the disabled to influence policies, especially when they do not cooperate with each other.

Urgently required is a coherent national strategy for the employment of the disabled which comprises close protection of their labor, subsidized and sheltered production, a special normative framework with tax exemptions, clear state engagements in the field, and the enhancement of cooperation.

### **3. Divergence and convergence of different forms of social economy**

#### **3.1. Differences**

At first sight it seems that aside from their correspondence to the broad definitions of social economy, NGOs and co-operatives differ in many substantial respects, follow different paths of development, and face different obstacles. The most important of these differences can be summarized as follows:

- a) officially declared guiding principles: general/private interest for NGOs and mutual interest for co-operatives;
- b) normative framework: law on non-profit juridical persons for NGOs and co-operative law for co-operatives;
- c) human capital: highly qualified labor in NGOs and low qualified labor in co-operatives;
- d) area of activity: urban for NGOs and rural for the majority of co-operatives;

- e) form of development: modern as regards NGOs and traditional in the case of co-operatives.

As a result of these differences NGOs and co-operatives are seldom considered together, and theoretical and practical difficulties have arisen in the rare attempts made to discuss them simultaneously<sup>3</sup>.

However, there are grounds for believing that behind the differences lie common characteristics and trends that may prove to be more important.

### 3.2. Similarities

There is clear tendency for NGOs and co-operatives to grow increasingly similar, particularly as regards:

- a) intensive involvement in new fields of activity (health care, tourism, ecology, child care, etc.);
- b) diversification, broadening of specialization and social functions;
- c) cooperation, networking and bridging;
- d) low participation in the establishment of the normative framework - only around 4% of NGOs projects have to do with the normative framework, and co-operatives play hardly any role in its establishment;
- e) restricted group solidarity, difficulties in mobilizing resources and a low level of cooperation, which can be measured by the intensity of internal conflicts;
- f) high competitiveness within both forms, accompanied by fragmentation and segmentation into a small number of successes and large numbers of failures for both forms. The result is a high death rate;
- g) strong pressure to turn into for-profit activities: in many cases NGO is only the organizational form in which for-profit activity takes place, and an increasing number of co-operatives are officially converting into for-profit companies;
- h) lack of long-term strategies, with a dominance of survival strategies, short-term aims and a high diversification of activities with low

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<sup>3</sup> Even research studies on different forms of social economy are mechanical sums of different themes rather than monographs.

- economic and social success and the corresponding unsustainable development. Over two years 400 co-operatives are reported to have gone into liquidation. Data show that more than 70% of NGO projects do not continue beyond the financing timetable;
- i) little economic freedom and the consequent centralization of internal power relations: NGOs are closely conditioned by donor programs, and co-operatives are highly dependent on mega business structures;
  - j) close involvement in the non-official economy and a lack of labor contracts due to the extremely high burden of the social insurance reform are constantly reported for both forms. Employment relationships are often unregulated and extraneous to the official economy.

Similarities between the forms are intensively 'produced' by the need to provide social space on the one hand, and by the inadequacy of the existing institutional framework on the other.

#### **4. The boundaries of the social economy**

Social economy initiatives in Bulgaria are dependent on and restricted by five basic factors:

*1. Social policy.* Social policy provides individual social protection in two basic ways: a) by redistributing incomes towards the most vulnerable groups; b) by providing opportunities for employment through inclusion in the official labor market and enhancing employment in business organizations. Functionally, it provides temporary shelter for excluded groups and/or prepares them for entry into the labor market. Organizationally, it adopts centralized and hierarchical models of interaction. The social economy is shaped by the effectiveness and limitations of social policy.

During the first ten years of transition in Bulgaria social policy was practically non-existent. By contrast, energetic and proactive social policy measures have been introduced in the past two to three years: most notably, changes in the legislation; active employment measures; the de-institutionalization and deregulation of social services; the fixing of an official relative poverty line. These measures have to a certain extent enhanced the activities of NGOs and developed the social economy,

giving rise to a number of good practices. However, some tendencies in these developments are contrary to the principles of the social economy: a) the proactive policies for employment adhere to the model of strong state intervention, instead of supporting spontaneous social economy developments; b) the basic principles are subsidies for employers and pressure on the unemployed, thereby continuing the logic of ‘making capitalists without capitalism’ as defined by Szelenyi (2002); c) the departmental approach concentrated in the Ministry of Labor and Social Policies has little chance of reversing the trend towards impoverishment. On the contrary, development of the social economy requires a broad and clear vision of national development.

2. *The market and its efficiency.* It may be that the presence of a highly developed market segment in the economy, one which needs highly qualified and specialized labour, is a precondition for social economy development, given that some groups of people (for example, the low-skilled, the disabled, immigrants, etc.) are unable to compete in a labour market of this kind. For these categories, development of the social economy is an important source of income-generating activities which furnish a safety net and may lead to future inclusion in the official labour market. However, this particular market segment is very thin in Bulgaria. By contrast, underdeveloped and ineffective markets predominate in the Bulgarian economy: output and profits are low and the price of labor is extremely low (the minimum wage is 60 euros and an average salary is 120 euros). Consequently, many ‘market’ enterprises are mixed forms of market and social economy. The result is a lack of clear boundaries between the market segment and the segment of the social economy. Mainly responsible for this development in Bulgaria seems to be the cost of labor, for which reason the official labor market is not an inclusive mechanism. Then, market enterprises and social economy enterprises to a great extent pay similar prices for labor. The basic differences between them reside in the different price levels for goods and services and the fact that the social economy, based on reciprocity, provides broader access to goods and services. It thus seems that the social economy is a specific compensating mechanism for market dysfunctions, and it endeavors to restore market ‘normality’ to the basic economy. Delineating the border, social economy organizations tend to turn into

semi-market organizations, while some market agents turn into semi-social economy organizations.

However, if the social economy occupies the middle place between market and state, a question linked with Coase's theorem<sup>4</sup> arises. It may be suggested that the social economy is a coordinating mechanism whose significance increases when, owing to the ineffectiveness of the institutional framework, the costs of coordination (official and unofficial transaction costs) both through hierarchies and markets are rather high (at least for some stakeholders). Douglas North (2000) writes, "When we compare the cost of transacting in a Third World country with that in an advanced industrial economy, the costs per exchange in the former are much greater" and he goes on to say that transaction costs are the most vivid dimension of the institutional framework. Thus cooperation in the social economy can be regarded as a strategy for economizing on transaction costs. For example, it saves that proportion of coordination costs linked with "chains of interdependence that become more differentiated and grow longer; consequently they become more opaque and, for any single group or individual, more uncontrollable" (Elias, 1978). Cooperation makes it possible to avoid some external chains of interdependency and replace them with cheaper internal ones. As a mechanism coordinating economic activity, the social economy simultaneously supports and questions the two other mechanisms, 'normalizing' the market and reducing the pressure on social policy.

However, to a great extent, similar functions are performed by the informal economy in its capacity as a 'shock absorber'.

3. *Informal economy.* There are nevertheless important differences between the social economy and the informal economy: a) whereas the informal economy only expands current income, the social economy is a developmental model; b) whereas the former often sacrifices rights and entitlements for financial results, the latter interrelates economic, social, cultural and political problems. It combines different types and classes of rights: civil (belonging), political (right to associate and democratic decision-making), economic (economic freedom), social (in the broad sense the right to protection and insurance), and it contributes to the

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<sup>4</sup> Economizing on transaction costs involves the choice between two coordinating mechanisms: market or hierarchy.

collective enforcement of individual rights; c) whereas the informal economy comprises only support activities, the social economy acts as a spontaneous business incubator and if successful enables transition to other inclusion mechanisms: labor market, business organizations, etc.; d) whereas the informal economy obscures macroeconomic indicators and hinders economic management, the social economy may reinforce national development.

There is little doubt that the deregulatory climate of the years of transition has greatly increased the magnitude of informal economies in the transition countries. Expert evaluations for Bulgaria calculate that the informal economy produces more than 25% of the Gross Domestic Product and comprises more than 30% of employment relationships. Moreover, the institutional framework (and its rigidity) is a decisive factor in determining whether the social economy becomes a formal and official segment of the economy or whether it is swallowed by the informal sector.

4. *The third sector and civil society.* External funds and non-negotiable donor programs have largely predominated in the intensive establishment of the third sector in Bulgaria. In early years especially, this development was clearly dominated by the charity model and the charity 'industry' which, like passive social policy measures, merely distributed the means to support survival and the *status quo*, rather than promoting the social economy as a developmental model.<sup>5</sup> As a consequence, third-sector development was and still is largely oriented towards the non-profit model, rather than responding to co-operative principles based on economic democracy. One result has been the low level of participation by civil society in current reforms.

By contrast, the social economy needs clearly defined values based on principles of democratic, equable and sustainable development and linked with 'development through participation', dispersion of power, and opportunities to regenerate social capital.

5. *The frame of reference: transition myths and ideologies.* The social economy depends closely on the concepts of economic and social development. "It is also clear that local initiative projects can fit into a variety of

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<sup>5</sup> Preference for one of these two rather different strategies continues to be an important basis for political and scientific discussion.

different scenarios for national development” [...]In strong neo-liberal economies, the social economy may be nothing more than a palliative, and end up as part of the informal economy. In economies where State intervention is fairly strong, the social economy may complement conventional social policies, which nonetheless resist significant transformation themselves. Lastly in economies that are fundamentally re-defining themselves, the social economy may serve as the ‘architect’ of a solidarity-based society with strong potential for creating new, democratically based relations between the social sphere and the economic sphere. Thus, the scope of these initiatives varies according to the economic scenario.” (Favreau, 2000).

The development of a social economy simultaneously requires economic freedom and support for community economic initiatives. Transition in Bulgaria is a contradictory mixture of a highly interventionist state and ‘over liberalized’ values, which means a low level of economic freedom simultaneously with an excessive individualization that can hardly support the development of a social economy. Whether explicitly defined or implicitly adopted, the frames of reference define the forms, characteristics and the success of the social economy and can support or neutralize the basic resources of the social economy: social and human capital, internal solidarity, collective identity, feeling of belonging and confidence, formation of group identities.

Of fundamental importance in this regard are the following ‘myths’ of the transitional ideology which have been responsible for Bulgaria’s rather unsuccessful transition.

1. *Privatization is a universal panacea.* This is the main explanation for the uncritical undertaking of massive waves of privatization in very different areas, social security included (for example health care reform, pension reform, social services reform, educational reform, etc.) without open public discussion on these developments. As a consequence, the public good is considered to be merely a mechanical sum of private goods. And the model of privatization has largely undermined broad-based property rights.

2. *Those responsible are distant in either time or space.* Transition has greatly developed the ideology of non-responsibility, hampering public

discussion and encouraging the growth of administrative (bureaucratic) hierarchies.

3. *If we had more money everything would be fine.* A lack of financial resources is constantly cited as the main obstacle against development. The grounds for the assertion are dubious: first because “the capacity for technological and social innovation is configured by social conditions existing in the cultural and institutional environment, more than by the availability of material resources” (Maciel, 2003, p. 1039-1040); second because data often show entirely the opposite phenomenon: for example, the increase in funding for the integration of Roma minorities has been accompanied by the growing impoverishment of the Roma people; and third because it is officially declared that it is impossible to use pre-accession funds (ISPA, SAPARD, etc.). Rather, financial hierarchies undermine economic effectiveness.

4. *Freedom and social security are antithetical. More freedom means less social security and vice versa.* Hierarchies of basic needs and rights can easily be reformulated into hierarchies of groups instead of into empowerment. This transitional ideology supports different kinds of hierarchies, and the results are increasingly contrary to the intentions. The anti-solidarity spirit of these myths results in deep social fragmentation and undermines the roots themselves of cooperating. Fragmented societies, characterized by anomie and ‘broken’ social links, ‘produce’ redundant people instead of enhancing social entrepreneurship. An over-individualized and fragmented society offers few opportunities for collective action. The social economy is obstructed by “a number of factors increasingly undermining social cohesion...These include pervasive individualism and the weakening of the unifying power traditionally provided by religion, moral standards and trade unions.....Unemployment... and the new poverty also play a role in destroying the social fabric...” (Defourny et al., 2000).

What is more, anti-solidarity and the fragmentation of society increase the divergence between NGOs and co-operatives. By contrast, a revival of solidarity would reveal their similarities. The embeddedness of the two forms in the economic and social context reinforces their differences by keeping them at a distance which is not profitable to either of them.

## 5. Prospects

The foregoing analysis of organizational forms of social economy in Bulgaria prompts the following conclusions:

1. it seems that there are differences among the various forms of social economy in the country. Co-operatives and NGOs follow different principles (general/private interest for NGOs, mutualistic for the co-operatives); they are subject to different normative frameworks (they are established under different laws); they have human capital of differing quality (higher-educated personnel in NGOs and low-qualified labor in co-operatives); they develop predominantly in different settings (urban for NGOs and rural for co-operatives); and they sustain different relations between modernity and tradition;
2. however, significant similarities are emerging and are perhaps more important than the differences. Co-operatives and NGOs provide opportunities for employment and income-generating activities for excluded and vulnerable groups of people. They generate opportunities to mobilize resources (human, communal, financial and material) and through cooperation to increase social and economic efficiency. They thus represent important but under-utilized mechanisms for social inclusion. This is extremely important for Bulgaria, because the labor market, with the extremely low price of labor, does not function sufficiently as an inclusive mechanism;
3. bulgarian co-operatives and NGOs are characterized by a lack of long-term strategies, little economic freedom, and scant access to credit. By sustaining short-term objectives and the marked diversification of activities, they achieve little economic and social success, with the consequent unsustainable development;
4. the existing forms of social economy are under strong institutional pressure as the existing institutional framework is adjusted to another type of economic actor. As a consequence, co-operatives and NGOs have high death rates, restricted opportunities for development, and tend to turn into para-market agents;
5. simultaneously, these forms of social economy are subject to strong non-institutionalized pressure which intensifies internal conflicts and struggles for resources, and results in fragmentation and

segmentation rather than mobilization for successful development. “Informality as a leading coordinating mechanism of economic life”<sup>6</sup> supports the functioning of both co-operatives and NGOs at the margin of the official economy, and rather often as part of the informal economy owing to the well-known lack of labor contracts (due to the high burden of the insurance reform) and de-regulated labor relations. These conditions undermine the very existence of the co-operative principle as a coordinating mechanism;

6. co-operatives and NGOs in Bulgaria are embedded in the economic and social context. Although there are some parallels with developments in the European Union (for example intensive entry into new fields), they remain on the boundary of the social economy, providing strategies for survival instead of becoming powerful generators of development. To reverse this tendency, the social economy must be included in a national strategy for development as a clear political priority.

In light of these conclusions, various scenarios can be developed in outlining the prospects for NGOs and co-operatives in Bulgaria. Whatever the case may be, the successful development of both forms requires identical measures and policies:

- a) *legislation*. There is an evident need to enact new legislation for the social economy. More than 64% of co-operative representatives consider the current legislation to be an obstacle against the development of the social economy: it should be harmonized with European-level legislation, especially with regard to the laws on social enterprises. A social economy ‘space’ should be clearly regulated and enhanced;
- b) *European Social Model*. It seems odd that the concept of a European Social Model is so under-developed. What is more, many commentators declare that, owing to the diversity of the European Union countries, there is no such phenomenon, and they remain silent when expressions such as ‘market economy’ and/or ‘political democracy’ are used. However, there are fundamentals that are clearly conceptualized as European: a degree of control on

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<sup>6</sup> Minev D., Project “From Social Assistance to Employment”, financed by EU Commission and MLSP.

- inequalities; an emphasis of participation, empowerment, solidarity principles and justice, broad-based anti-poverty programs regulated by the state; denial that poverty is purely an income problem; basic standards of social security; holistic approach; growing awareness that poverty problems are not problems of economic growth alone; the current development of National Action Plans, anti-poverty strategies, etc. It is inappropriate that failures or poor results in some of these areas are considered to refute the entire model. In the transition countries especially, there is a vital need to develop the concept of the European social model, and especially so in the field of the social economy;
- c) *networking with the European communities*. Besides knowledge transfer, cooperation on skills, etc. there are further advantages to such networking: 1) the European social model, although unpronounced and unrecognized, is spontaneously involved; 2) networking reinforces the 'open society', an important feature of which is the decline of national hierarchies. This is advantageous to both NGOs and co-operatives;
- d) *becoming influential actors*. Although there are attempts by NGOs to act simultaneously as pressure groups and social service providers, these activities clearly require the involvement of other stakeholders which embrace the solidarity co-operative principle. Enhancing community action will reinforce partnerships among different stakeholders - NGOs and co-operatives included. A basic requirement in this regard is the creation of social investment funds, which could support cooperation and sustain social links, and thereby regenerate social capital.

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# 14. How to develop the co-operative movement: the case of housing in Estonia

*by Marit Otsing\**

## 1. Introduction

Estonia - a new member state of the European Union - is situated in the north-eastern part of Europe. Its territory is 45.227 square kilometers and its population is 1.370.000. The capital is Tallinn with 415.000 inhabitants.

Estonia, as well as other Eastern and Central European states, has been rapidly moving from the left - socialism and a planned economy - to the right and to a free-market economy and liberalism.

In the early 1990s, Estonia entered a period of state-wide privatisation. Buildings, real estate and enterprises previously owned by the state were designated for privatisation. For this purpose, individual privatisation vouchers were issued, the value of which depended on the number of work years of the person concerned. 98% of the entire apartment housing stock was privatised on the basis of these vouchers, and the inhabitants of flats became their owners. State enterprises were also designated for privatisation.

At the end of the 1980s, with the advent of 'perestroika', the formation of new cooperatives began in Estonia. At the time this was the only possible form of private enterprise. By the beginning of 1990 there were already 2000 such new cooperatives registered in Estonia; by August 1993, the number had risen to 3000. As a consequence of legislative changes, in the following period the majority of these cooperatives were re-registered as other juridical forms of enterprise.

The process of privatisation and the founding of new enterprises marked only the beginning of the development of new ownership structures.

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\* Estonian Union of Co-operative Association.

## **2. The cooperative housing movement**

Housing reform in Estonia began in 1992; since then 98% of all apartments have been privatised, and 75% of the population now lives in apartment buildings. The reform has moved through three stages:

1. the privatisation of apartments;
2. the establishment of housing cooperatives;
3. privatisation of the land for housing co-operatives.

As of 2004 there are 7.500 housing cooperatives in Estonia and 337.500 apartments with 776.250 occupiers. Each year, 1000 new housing cooperatives are founded: 55% of the Estonian population lives in housing cooperatives.

## **3. Estonian Union of Cooperative Housing Associations (EKL)**

The Estonian Union of Cooperative Housing Associations (EKL) is an organisation which unites Estonian housing cooperatives and associations and defends and develops the interests of its members at the local, state and international authority levels. It was established on 17 April 1996 in Rakvere to comprehend, assist and protect the interests of flat-owner associations and housing cooperatives. The Union has nine bureaus in various towns throughout the country which furnish information on organising the activities of flat-owner associations and housing cooperatives. Today EKL has 1.100 member cooperatives with 100.000 members.

The main goals of the Union's activities are the following:

- to develop and publicise the flat and housing association movement;
- to assist members in fulfilment of tasks such as the management and administration of their housing;
- to gather and disseminate current information among members, and to publish relevant leaflets and materials;
- to influence and participate in legislation; observe and contribute to the development of legislative and other acts of law;
- to provide help with the establishment of associations and other management and administration structures;

- to devise and implement development projects and training programs concerned with joint housing management and of nationwide as well as local and regional importance;
- to offer members a universal professional, high-quality service.

Housing cooperatives and associations in Estonia are today the most widespread and recognized form of cooperating and managing accommodation. About 50% of the Estonian population lives in housing cooperatives, which play an important role in society and represent an enormous, stable and secure resource. Indeed, Estonia has become a republic of housing cooperatives.

The EKL is headed by a 23-member Council which is elected on 'Union Day' and appoints the board, the task of which is to supervise and implement the Union's everyday activities in accordance with decisions approved on Union Day and by the Council.

EKL organises training courses, seminars and information days for the boards, bookkeepers and executive directors of housing cooperatives and associations throughout Estonia. In addition to short-term training sessions, EKL also organises 160-hour supplementary courses for senior managers based on the Licence issued by the Ministry of Education, with official certificates awarded to graduates.

Also of assistance in problem-solving and information exchange are the Round Table meetings held in twelve different towns in Estonia and six different areas in the Tallin municipality.

Regular study visits are made to Finland in cooperation with the Finnish Real Estate Union. EKL has also organised similar visits to Sweden, Norway, the Czech Republic, and other countries.

The annual Estonian Forums for Flat Associations and Housing Cooperatives provide opportunities to discuss practical issues and to keep abreast of the latest developments in state housing policies. The purpose of these forums is to share information and to draw the government's attention to the problems of housing associations.

The EKL collaborates with companies in providing important services and products to associations at discount prices. The member card has been recognized by both firms and associations, because the reliability and quality of products and services, guarantees, and reasonable prices

have an important role in contemporary life. The list of the companies offering discounts is constantly growing.

In order to furnish its members with current and relevant information, EKL publishes the magazine ELAMU, which reports on the activities of flat and housing associations in Estonia and abroad. Each issue provides expert information in the following areas: legislation, cooperation, training, the economy, and renovation. The magazine is free for members of the EKL.

The EKL has published several books in its *Guidebooks for Housing Associations* series on the management of associations, bookkeeping, and legal issues, as well as on cooperation. In order to help associations find firms providing the services that they require of the best quality, the Union has issued a catalogue entitled *Information about Housing*.

The EKL represents Estonian flat associations and housing cooperatives in the following international organisations: ICA Housing, CECODHAS; and the Baltic Union of Cooperative Housing Associations (BUCHA). It also cooperates with the Finnish Real Estate Union, the Norwegian Union of Cooperative Housing Associations (NBBL), the Swedish Union of Cooperative Housing Associations (HSB), the Canadian Union of Cooperative Housing Associations, and The European Organisation of Social Economy Cecop.

Since 1999 the EKL has had its own website, which is constantly expanding and now has more than 2000 regular users. The website is popular because it provides current information on a daily basis: every morning it displays news on housing associations from the Estonian press. Furthermore, an EKL lawyer can be consulted at the website on recurrent questions, and there is a forum where the leaders of the unions can express their opinions. Recent statistics on the website can be found at: [www.ekyl.ee](http://www.ekyl.ee).

The Estonian Union of Cooperative Housing Associations embraces the universal principles of cooperation: voluntary and open-minded membership, democratic government and control, the economic involvement of members, independence and freedom, training and information, cooperation at the local, regional and international levels, and interest in the development of the community. The EKL has affirmed that its values are trust, cooperation, honesty, competence, and

development, and it has stated its mission as being “a satisfied resident of a well-managed housing cooperative”.

#### **4. Housing co-operatives create social capital**

Francis Fukuyama has stressed the importance of social capital in society. On Fukuyama’s definition, social capital is one of the three types of capital besides physical and human capital. It is the ability, based on shared value orientations and unofficial norms of behaviour, to work together in pursuit of common goals and with mutual trust, together with such virtues as honesty and a sense of duty.

Fukuyama states that it is easier to create social capital in an organisation with certain borders than it is in society as a whole. Social capital means the sharing of norms and values, a feature also characteristic of organisational culture. Study of effectively-managed organisations reveals that their management relies not on formal bureaucracy but on value orientations shared by management, employees and members which enable them to communicate effectively. When people trust one another and act as a team, the results of their work improve.

Social capital plays a vital role in both politics and the economy. Every economic system is based to a large extent on cooperation. While acknowledging the strong individualism of enterprises, it should still be borne in mind that every business arises from a group of people who have begun to cooperate. Amongst other things, social capital based on common values enables the avoidance of transaction costs and reduces bureaucracy and legal expenses.

An organisation whose members have a shared interest in moving it forward is the best carrier of social capital. In this respect the post-socialist states are no different from the countries of Western Europe. Estonia and other Eastern and Central European states may be different in terms of their recent history but they face the same challenges: urbanisation, globalisation, and the rapid depletion of energy resources. The spread of ideas on social economy throughout Europe has played an important role in strengthening enterprises, especially on their social side, in every country.



# 15. Development of co-operative enterprises in Lithuania

*By Sigitas Bubnys\* and Dalia Kanpelyte\*\**

## 1. Introduction

Lithuania is the southernmost and largest of the three Baltic Republics on the eastern shore of the Baltic Sea, with a territory of 65,200 sq. kilometres and a population of 3.7 million. Lithuania's economy was transformed by its incorporation into the Soviet Union at the end of World War II. Rapid industrialization took place, particularly in metalworking and machine building which became Lithuania's prime exports. The textile and leather industries were also important. The agricultural sector was among the best developed in the Soviet Union so large-scale food exports were made to Soviet republics.

With the collapse of the Soviet Union, Lithuania regained its independence on 11 March 1990. Its economy, along with those of the other former Soviet republics, was thrown into turmoil. Closely interdependent industries and trade partnerships collapsed, closing many factories. The agricultural sector faced swift and severe reforms with the dismantling of collective farms and the distribution of equipment and land to former kolkhoz workers. With the decrease of jobs in the industrial sector, many returned to farming as a source of income or, minimally, as a source of food for their families, often without the necessary equipment to work their land effectively.

In the years following the redistribution of the land, it has become clear that co-operation in agricultural sector is necessary in order to increase both production and profitability. For now, this co-operation primarily takes the form of joint ownership of farm equipment and the renting of adjoining land. The lack of further co-operative development in Lithuania, which has a strong history of many types of co-operatives, could be

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blamed on the lack of effective legislation, the mistrust of people in one another, as well as a certain fear of a return to the kolkhoz or collective farm.

With the advent of independence, followed by the collapse of the majority of large factories, the privatization of State property and the possibilities of quick riches for the enterprising - readily available short-term credit became a big necessity. In the agricultural sector, the dismantling of collective farms had left many former agricultural workers with land, but no equipment to work it and no access to capital for investment in their new sphere of private enterprise. Here, the need was for co-operation and longer term credit which is covered by the banks only in very small part (a tedious bureaucratic procedure, taking only immovable property as collateral) along with limited government subsidies and loans, while the numerous commercial and State banks were primarily oriented towards business loans.

The aim of this article is to review the co-operation system in Lithuania as well as to analyse the pre-conditions of further successful development of co-operation. As the characteristics of economy in transition and the historical background could play the key role, the specific features for social co-operatives could be identified.

## **2. The cooperation system in Lithuania**

### **2.1. The history of cooperation**

It is interesting to note that credit co-operatives “taupmenu skolinimosi bendroves” (“Societies for borrowing of savings”) first started in Lithuania in 1871. By 1939, at the start of World War II, there were 310 such “people’s banks” with 119,000 members and some 85 million litas in assets. The 1939 credit co-operatives held 37.0% of the market share of deposits and 37.5% of all loans in the country. At the end of last century the first consumer co-operatives were established, at the beginning of the 20<sup>th</sup> century co-operatives for dairies.

The Soviet regime terminated this very strong movement. The powerful State and the Communist party took control of the development of the co-operative sector and made decisions concerning the form and type of

co-operatives. They supported the co-operatives organizationally and financially and exerted strong influence as far as the structure of the co-operative bodies of all levels and the individual members of these bodies were concerned. The democratic principles of the co-operative movement were disregarded and the co-operatives became important means of socialization of agriculture, crafts and trade.

## **2.2. The current cooperation situation**

Nowadays in Lithuania mostly there are 3 types of co-operatives:

- 1) consumer;
- 2) agricultural;
- 3) financial (credit unions).

### *2.2.1. Consumer co-operatives*

According to statistics of the Lithuanian Consumers' Co-operative Society, this society unites 96 co-operative societies with over 190 thousand members. The consumer co-operative companies employ 9 thousand people. Co-operative stores and catering enterprises sell goods for more than 130 million euro, bakeries bake 40.0% of the bread produced in Lithuania. In addition to its general activities, such as trade, baking and the canning industry, the Lithuanian consumers' co-operation deals with the purchase of agricultural products and second hand materials, the processing of fruits and vegetables, catering, the production of national beverages, fur farming, construction, transport and other activities.

The numbers are mistrustful in this case, because these co-operatives are not co-operatives anymore. They are closed stock companies and nothing more. There are some co-operatives with a co-operative structure, but only with some members, others are "dead souls". Really nothing has changed from Soviet times, but instead of the State these co-operatives are "privatized" by some members, former soviet system officials, as usual.

### 2.2.2. *Agricultural co-operatives*

For the year 2000, 341 agricultural co-operatives were registered. One third of them are no longer operating. Most of active ones are agro-technical (40.0% from the total number of agricultural co-operatives), industrial (30.6%), trade (13.0%), dairy (7.1%) and other (9.3%). Most of them are newly re-registered the same collective farms from Soviet times, with some exceptions. There are some real agricultural co-operatives with true co-operative principals. Most popular form of farmers co-operation are mutual technical help of farmers “one neighbour - to another neighbour” and the societies of users of technical equipment.

*Mutual technical help* is the most popular and mostly applied form of usage of technical equipment between farms. The usage of technical equipment is very simple in organizational form and also very effective. One may name the economical and organizational advantages of farmers mutual technical help:

- lower need for investments. Usually it costs about 50-35% less to share technical equipment between farms than to use it in one farm. This is very important to farmers, because investment capacity of farmers is very low, and the use of loan funding is not always available. While decrease in the investments on technical equipment, new possibilities to form other elements of material base (buildings, stock herds of animals, stock seed, etc.) arise;
- the decrease in the annual fixed costs of technical equipment maintenance. While using technical equipment not on one single farm, one can increase its seasonal usage. At the same time fixed costs for depreciation, insurance, etc. decreases;
- the maintenance of added value created by farmers;
- the decrease in costs for buying mechanical services;
- the decrease in the need for working capital;
- more rational and qualified usage of technical equipment.

The *societies of users of technical equipment* are quite common in small, medium (30-50 ha) and even large farms. Separate farmers only buy the most often-used universal technical equipment and one or two specialized machines. For those jobs for which a farmer doesn't have equipment, he borrows machines from other farmers. To gain revenues, farm-

ers try to use their technical equipment as best as possible in order to provide services to other farmers. In this way a system of technical services provision is formed, where the farmer is a customer and at the same time a provider of technical services. Usually a manager acts as an intermediary. Farmers, agricultural enterprises and providers of technical services may join the societies of users of technical equipment. The more members there are in the society, the opportunity to use technical equipment from inside increases, at the same time the costs of buying technical services from outside decreases, as the prices to buy technical services from outside are higher. It is necessary to register the society of users of technical equipment according to the law. It can be registered as society or as farmer's co-operative.

### *2.2.3. Financial co-operatives - credit unions*

A credit union in Lithuania is a co-operative financial institution, owned and controlled by the members who use its services. Credit unions serve groups that share a common bond. Membership of credit unions in Lithuania is based on the following criteria:

- employment in the same enterprise or institution;
- membership of the same professional group;
- belonging to a certain formal registered association;
- residing in the same location: town or village.

In credit unions the members are the owners. Benefits of ownership include better rates on deposits and loans and better service. Regardless of their size or field of membership, credit unions are different than for-profit financial institutions. Credit unions exist to serve their members. Banks and other financial institutions exist to make money for their stockholders. Credit unions are member-owned, co-operative financial institutions that provide many of the same financial services that banks do, savings and current accounts, youth and senior accounts, loans for a variety of purposes, convenient services to access and send funds and more. In essence they are mutual organizations operated entirely by and for their members. Credit unions are also not-for-profit and exist to provide a safe, convenient place for members to save money and to get loans and other financial services at reasonable rates.

Credit unions in Lithuania are organizations with high social responsibility - continuing the ideals and beliefs of the co-operative pioneers, credit unions seek to bring about human and social development. Their vision of social justice extends both to the individual members and to the larger community in which they work and reside. The credit union ideal is to extend service to all who need and can use it. Every person is either a member or a potential member and appropriately part of the credit union sphere of interest and concern. Decisions should be taken with full regard for the interest of the broader community within which the credit union and its members reside.

### **3. Credit unions as an example of good co-operative practise in Lithuania**

Credit unions - microfinance co-operative community banks - started their activities in Lithuania in 1995, when the Credit Union Law was passed in the Lithuanian Parliament. At the end of September 2003 there were 57 credit unions operating in Lithuania with total assets of over 31,395,000 euros, and total membership over 30,000 people (the total population in Lithuania is - 3,500,000 people). For the last three years credit unions have shown over 100% growth annually in assets and members. Credit Unions take approx. 0.5% of the market share in assets.

Credit unions in Lithuania are very active in microfinancing the agricultural sector (farmers) and small business activities. From the start of credit unions activities in Lithuania, over 39,200 credits amounting to over euros 51,000,000 were granted to finance different types of activities. Credit unions are active in community development. Through financial support to their members, who at the same time are owners of credit unions, they help to increase the welfare of community, to create new jobs, to start businesses, to develop the production of goods and services in rural areas.

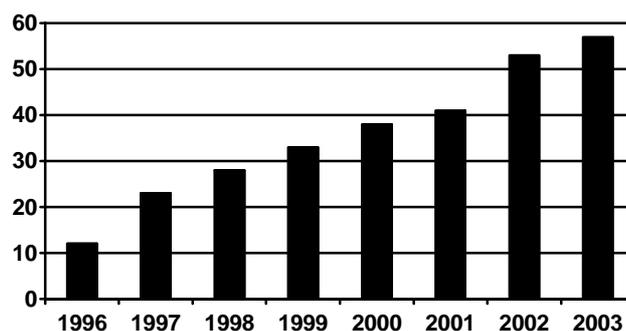
In November 1997, 11 credit unions joined the Association of Lithuanian Credit Unions. This is a team of young professionals who organize central marketing, training activities, give consultations on legal and financial issues, provide technical assistance and develop the common computer accounting program KUBAS, organize the foundation of new

credit unions, promote credit unions in national and international, financial and governmental institutions. In May 2000 the new law for Lithuanian central credit union was passed in the Lithuanian Parliament. The need to found a central credit union facility arose in light of the rapid expansion of the credit unions network. The Lithuanian central credit union is strengthening the credit union network financially and is helping to manage liquidity and stability of the network. The model of the Lithuanian central credit union was designed according the examples of the Central credit co-operative institution models in Netherlands (Rabobank Netherlands), Poland (Kasa Krajowa), Canada (Desjardins Caisse Central) and others. Founded in November 2002 the Lithuanian Central credit union manages credit unions Liquidity and stabilization funds, grants loans to credit unions, manages external credit lines and also acts as a clearing center for all credit unions.

#### 4. Overview of credit unions' activities

From the start of the activities of credit unions in 1995, credit unions have shown impressive growth results.

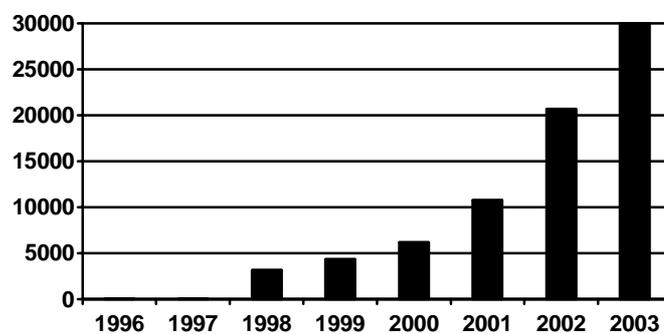
Figure 1 - Number of credit unions



In an average each year 6 credit unions receive licenses. In year 2002-2003 the growth of the number of credit unions was very high. The main reason for that is the closing of Lithuanian Savings Bank branches in rural areas. This caused great demand for financial services in rural areas.

Credit union members are mostly individual persons (98%). Until the second edition of the Law on Credit Unions legal persons had no right to become credit union members. Now enterprises owned by credit unions members can also join credit unions. Credit unions serve only small and medium enterprises which employ no more than 49 people annually

Figure 2 - Membership growth in credit unions



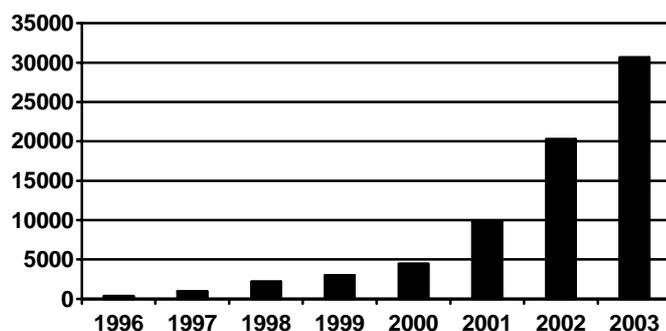
## 5. Services in credit unions

Lithuanian credit unions provide saving services and loan products to members and also make transfer payments. Saving products are - current accounts, savings accounts, children savings accounts, retirement savings accounts, also short term and long term deposits.

In addition, credit unions give loans to their members. Loans are mortgage loans, business loans, consumer loans, fast loans and loans for studies. Credit unions also collect taxes for commodity enterprises, such as electricity, gas, water. A member in a credit union can also make different payments for goods, services or receive money from other persons.

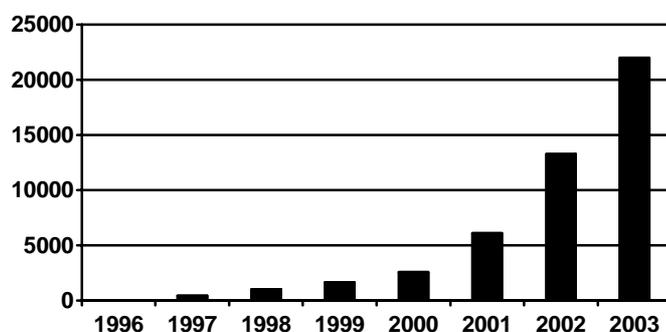
On the whole credit unions serve individual persons. Savings of business enterprises and loans to enterprises make up not more than 2% of the whole credit unions savings and loan portfolio.

Figure 3 - Assets of credit unions, in thousands euro



Average assets growth in credit unions during the last five years exceeds 100 %. The largest part of all assets is invested in loans, for example, 65% of all assets in December 2002 were invested in loans to credit union members. The total amount of loans granted out of total assets has increased since 1997. In 1997 total loans made up 42% of all credit union assets.

Figure 4 - Loans outstanding in credit unions, in thousands of euro



In peak periods - spring and summer - when farmers and small businesses begin major activities, credit unions start to lack resources for granting loans. At this moment extra credit lines from the Lithuanian Central Credit Union are used to increase assets size and the financing capacities of credit unions.

## 6. Credit unions' role in regional development and social economy in Lithuania

Credit unions are known in Lithuania as community banks. They are helping to develop local communities by providing financial services to those people who have no access or have poor access to financial services provided by banks. Most people working in rural areas have very low income. Banks refuse to provide financial services to those people as they consider them to be a high-risk segment. Credit unions unite people from the same community. As community representatives are elected to the governing bodies of credit union, they know the situation a lot better and can grant loans with low risk to low income people - farmers, entrepreneurs, small and medium businessmen. In such a way, credit unions influence the economy of the community as the money lent from credit unions is used for business development in the same community or improvement of social welfare.

Though the market share of credit unions (0.5%) in Lithuania is small, credit unions play an important role in regional development as they serve people in the regions. After privatization, starting from 2001, the major retail bank Hansa-LTB closed its branches due to the changes in national and international financial markets, which forced banks to increase their profitability. People living in rural areas were left with no access to financial services, though they must be provided with pensions, salaries, possibilities to make payments for public utilities, as well as to be able to save and receive credits.

The need for credit unions services rapidly grew in place of closed branches of Hansa bank. In these areas new credit unions were founded or old credit unions opened their own branches. Credit unions can operate in the regions because they perform a major role for the utility of their members - that is to provide necessary banking services at compatible prices. As credit unions are not profit seeking, they can perform in those areas where the profitability of performance is very low.

Integration into the European Union opens new possibilities for farmers and entrepreneurs to receive funding from Structural funds of the European Union. Credit unions could be the institutions which could provide small businesses in the regions with consultations on the development of

investment projects to receive funds. Today credit unions in Lithuania are still too small to provide financial support for businesses themselves (the average assets of a credit union aren't more than 500 thousand euro). As credit unions grow bigger, they will be ready to finance large-scale investment projects.

## **7. Conclusions**

The Soviet regime from 1940-1990 had a severe impact on the development of co-operation traditions in Lithuania. The concept of consumer co-operatives as well as agricultural co-operatives was perverted, co-operation in the financial sector was destroyed. Nevertheless, co-operation as a social dimension has not disappeared from the national arena. Economic and social development stimulate the recovery of co-operation. Good examples of the development of co-operation in social economy are some agricultural co-operatives and credit unions - whose growth and amplification of co-operative principles destines co-operation recovery as a part of the social economy.



# 16. Economic substance and legal regulation of agricultural co-operatives in Hungary<sup>1</sup>

by Gabor Szabó\* and Alexandra Kiss\*\*

## 1. Introduction

The main goal of the paper is to show briefly the new Hungarian co-operative laws and regulation and to analyse their impact on agricultural co-operatives. Two case studies are also presented as two examples of different routes of agricultural co-operation in Hungary.

The study consists of two main parts. First, the new laws and legislation on agricultural co-operatives will be discussed. After analysing the main conflicts and different interest groups in the co-ops, a case study on a transformed co-operative will try to find out reasons which led the examined co-operative to transform itself into an Investment Oriented Firm (IOF) in the form of a joint stock company.

In the second part of the study the recent legislation and regulation regarding Hungarian agricultural co-operatives will be discussed, then we are going to analyse a second case study on the Hungarian Mórakert Purchasing and Service Co-operative, Mórahalom, which is an active and successful marketing co-operative in the fruit and vegetables sector. Although the so-termed conversion process into Investment Oriented Firms or conventional firms (mainly caused by political and state support

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uncertainties in the Hungarian case) is taking place in Hungary as well as in other European countries, the Mórakert co-op still preserves its legal status and organisational structure.

Main methods used to carry out present research were: literature review, collecting secondary (statistical) data, interviews and case study analyses. According to the Hungarian Central Statistical Office (CSO), on 30 September in the year 2003 the number of co-operatives in the Hungarian economy were 5,561, of which 1,561 co-ops work in agriculture and forestry. This is the second largest number, after real estate, renting and business activity sectors (1,939). Co-operatives also exist in relatively great numbers in the wholesale and retailing sector (1,036).

## **2. Appearance of different interest groups in the transformation process of the Hungarian agricultural co-operatives due to legislation on co-operatives which came into force in 1992<sup>2</sup>**

The former Hungarian legislation on co-operatives (which came into force in 1992) established the institution of ‘co-operative business share’ in the agricultural co-ops. Different interests still exist in the Hungarian co-operatives nowadays, such as was the case in the transformed and converted co-op analysed in this paper (see section 4).

These opposite internal interests can basically be divided into long term-short term and personal contribution-capital divisions. In addition to these two basic groups there are three main types of totally different interests (Kalmár, 1996; Módos, 1993). The first is between the active members and the so-termed retired members.

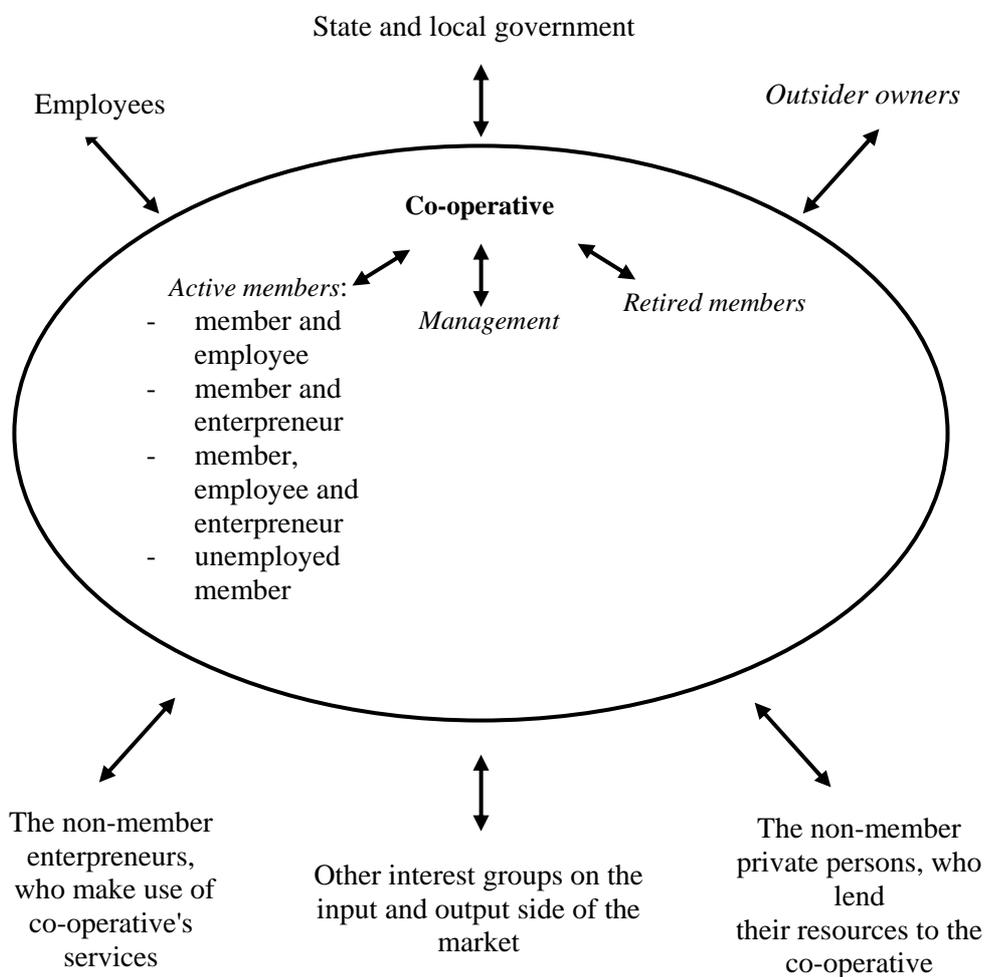
Secondly, there are different interests between the (active) members and the outsider owners (as investors). The retired members and outsider owners are interested mainly in the short-term advantages of ‘their’ co-operatives, and because they have special shares in the co-operative they would like to obtain dividends on these shares as quickly as possible. They are not concerned with the long-term advantages of the active members. Finally, there exist some other misunderstandings between the members/employees group and the ‘new owners’.

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<sup>2</sup> This section is based on Szabó et al. (2000) and Kiss (2000).

There are more different stakeholders in an average co-operative in Hungary as can be seen in figure 1. However, it is necessary to underline the role of the management governing the co-operative. The leaders of the co-op have the ability to control the main transformation process, due to their key position in the business and governance matters of the co-operative.

Figure 1 - Different stakeholders in Hungarian agricultural co-operatives after 1992



They have plenty of information and very important connections to members and to organisations and authorities, which are playing an outstanding role in the life of the co-op. Active members can be divided into more groups on the basis whether they are working/earning additional income other than in the co-operative. There are some members who just have special entrepreneurial business connections to the co-operative, they are not working in the co-op. And there are some who are employees of the co-operative and entrepreneurs at the same time.

### **3. Changes in the life of agricultural co-operatives in 2000-2001 and the Law CXLI on the agricultural co-operative business shares (2000)**

There were significant changes in the Hungarian agricultural co-operative life at the end of year 2000, because of the proposed law on the settlement (arrangement) of the so-termed 'business co-operative shares'. The government had planned to oblige the agricultural co-operatives to buy the business co-operative shares from outsider owners at their nominal (face) value. That was a real fear for the co-operative, since they did not have enough property to fulfil their obligation. It was clear for most co-operatives that the government prefers the western-type ("complementary") co-operation to the existing agricultural production type co-ops. Connected to the previous opinion, some of the co-operative leaders have thought that the government would like to strengthen the family farm model, rather than to support the collective type production of the agricultural co-operatives.

There were hard disputes between the government and the representatives on behalf of the agricultural producers and co-operatives, and some of the co-operatives had decided to transform themselves partially or fully into (limited liability or joint-stock) companies. There were 952 remaining agricultural co-operatives on 1<sup>st</sup> January 2001 from the 1,049 which had existed a year earlier. From the 97 co-operatives which were to be wound up, 45 transformed themselves into an IOF company, in the last two months of year 2000. According to some opinions the latter cases were mainly due to the political atmosphere.

Law CXLIV/2000 on co-operative business shares (MK, 2000a) come

into force from 1<sup>st</sup> of January 2001. The law obliged the agricultural co-operatives to buy the business co-operative shares from outsider owners with “subjective right”, at their nominal value. According to the legislation, if the co-ops did not have enough property to pay off the full price, the state would provide interest-free loans to cover the margin. According to the law mentioned above, the deadline to apply for the pay-off was 15 April 2001, however, the Constitutional Court (hereafter CC) failed to approve the above mentioned law (MK, 2001b).

Despite the decision of the CC, the procedure of collecting requests for the pay-off had started and 363 thousand applications had arrived by 15 April 2001. In May 2001 the government made it clear that they would continue to arrange the co-operative business shares and extend it towards the retired members, a process which began in 2002. In order to be able to carry out the above mentioned activity, the government entrusted the Hungarian Development Bank Ltd. (“Magyar Fejlesztési Bank”) with the foundation of a Ltd. company for the utilisation of the co-operative business shares. The pay off has been carried out by that Ltd. co. entirely from the governments’ budget. Subsequently, the process of collecting applications was carried out in the regional offices of the Hungarian Ministry for Agriculture and Rural Development. In the 5/2002 (MK, 2002b) decree the Government made it clear that it is not an obstacle for the pay-off if, in a co-operative, there is a winding-up or liquidation process, or even when the co-op is close to bankruptcy. The state guaranteed the loans connected to the pay-off procedures up to 2 billion HUF in the Government’s decree 1025/2002 (MK, 2002a).

Due to the above mentioned procedures the state has been getting property rights in the agricultural co-operatives in proportion to the co-operative business shares. There were and still are a number of questions regarding state ownership in the agricultural co-operatives due to the abovementioned legislative procedures, such as: what about the possible voting right(s) of the state or the rent which has to be paid after the property (assets) has been used by the co-operative, etc. However, it is clear that a long time will pass in the arrangement process before the situation will be solid and stabile.

## 4. Case study N. 1 on the “doubly” transformed Kapostáj Agricultural Co-operative<sup>3</sup>

### 4.1. Transformation of the former agricultural production co-operative according to the laws which came into force in 1992<sup>4</sup>

The former *Kapostáj Agricultural Co-operative* was a ‘traditional’ production co-operative located in Kaposvár-Toponár in the south-western part of Hungary. The main aim of the co-operative was above all being able to give the so-termed active members the opportunity to work and therefore to earn a living from agricultural production.

Worthy of note is that, unlike members of other co-operatives during their transition after 1992, those of the Kapostáj Co-operative stayed together: none decided to leave the co-operative and/or withdraw assets or property, despite this being easily possible due to the legislation. There was no option to change into company form at that time, although that would have been easier to operate.

As can be seen in table 1, the ownership structure was very complex in 1999, and became a great source of problems in recent years.

**Table 1 - Share of the total co-operative property in 1999**

	Number	Co-operative shares in HUF	Business shares in HUF	Property in total in HUF	Division in %
Members	96	960,000	70,321,104	71,281,104	34
Retired members	219	2,415,000	83,304,811	85,719,811	40
Inheritance matters	25	25,000	3,937,374	3,962,374	2
Members in total	340	3,400,000	157,563,289	160,963,289	76
Employees	3	-	1,711,022	1,711,022	1
Outsiders	430	-	48,679,907	48,679,907	23
<i>Total</i>	<i>773</i>	<i>3,400,000</i>	<i>207,954,218</i>	<i>211,354,218</i>	<i>100</i>

In the case of the co-operative examined, interest problems (see section 2) occurred from day to day; however, the situation had become harder, since the number of the outsiders was increasing year by year. They did not have control or decision rights, so they could not influence the busi-

<sup>3</sup> See a more extended version of the case study in Szabó et al. (2000) and Szabó and Kiss (2002).

<sup>4</sup> See more details on laws which came into force in 1992 in Szabó et al. (2000) and NCC (1992).

ness of the co-operative. As was stated earlier, no dividend had been paid on the co-operative business shares since 1992.

#### **4.2. The transformation the co-op into a joint stock company in December 2000<sup>5</sup>**

The General Assembly of the 'Kapostáj' Co-operative decided to partially transform the co-operative into a joint stock company in December 2000.

The main reasons for the conversation were the following:

- they wanted to operate their properties in a solid (stabile) legal form;
- it would be possible to dissolve the tensions emerging due to the different entitlement (residual claims) of the owners;
- in the new organisational form a new organisational, governance and incentive structure would be established which would enable the running of a more efficient operation;
- the joint stock company as a company (IOF) structure would make it easier to absorb additional risk-bearing capital and loans;
- the joint stock company as such, has a better image towards to the business partners compared to the co-operative form.

However, it was a strong desire on behalf of the co-op to preserve or even to increase members' allowances in the new legal form as well. It is the reason why members thought the transformation would not be against their interests. The additional risk-bearing capital will make possible for the company to access to new markets, to obtain a modern equipment park and therefore to enlarge their scope of services, all in all: to farm more efficiently.

It is clear from the numbers of table 2 that more than half of the owners of the co-operative were outsiders and they held the 26% of the total property. One can imagine that the compulsory buying up (pay-off) of the co-operative business shares would lead to a bankruptcy of the co-operative.

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<sup>5</sup> This section is based on Györke (2001).

**Table 2 - Share of the total co-operative property in September 2000**

	<i>Headcount</i>	<i>Co-operative shares in HUF</i>	<i>Business shares in HUF</i>	<i>Property in total in HUF</i>	<i>Division in %</i>
Co-operative members	295	2,950,000	153,180,812	156,130,812	74
Outsider owners of the co-operative business shares	365	-	54,773,406	54,773,406	26
<i>Total</i>	<i>660</i>	<i>2,950,000</i>	<i>207,954,218</i>	<i>210,904,218</i>	<i>100</i>

*Source: Györke, 2001.*

As we have mentioned earlier, there were different interests even between the various types of members, not just among the members and outsider owners, therefore it was hard to adjust the different interests (see figure 1). The form of a joint stock company enabled every stakeholder to exercise an influence on the operation of the company. That was a successful project on solving the interest tension among the different types of stakeholders. Recently, it has been in the interest of every owner to run the company efficiently and to get the results for their investments. However, the biggest disadvantage for them is the fact that everybody is just a business partner for the company, therefore the rent for their land is lower and the prices of the services offered by the company are higher.

## **5. Recent legislation and regulation regarding Hungarian agricultural co-operatives**

The definition of the co-operative, incorporated into the new (CXLI/2000) co-operative law (MK, 2000b), is very complex, however it is in accordance with the international theory and definition(s) of the co-operatives. The co-operative is an economic organisation and a legal entity, with open membership and variable capital, aiming to meet the requirement of promoting (complementing) the members' business (farming) or the consumption in a case of natural persons, and in certain cases to meet the demands of membership according to their cultural,

educational and social needs. It is clear from the definition that the main aim is to promote/help the farming of the members, however the law does not exclude the possibility of the collective (agricultural) production in the co-operatives. It is very interesting that the law makes possible for the co-operative to require agricultural land to be offered for rent to the co-operative or personal contribution from the potential members applying for membership. However, it is interesting that agricultural co-operatives use less and less land compared to corporations and private farmers. Thanks to the uncertainty (mentioned above) and other economic disadvantages, the arable land used by co-ops has decreased over the last 12 years (see table 3).

**Table 3 - Distribution of arable land by types of farms<sup>a)</sup> in %**

<i>Denomination</i>	<i>1990</i>	<i>1998</i>	<i>1999</i>	<i>2000</i>	<i>2001</i>	<i>2002</i>
Corporations	14,2	17,4	19,2	24,4	26,6	27,4
Co-operatives	73,1	26,8	24,3	20,5	14,9	11,5
Private farmers	12,7	55,8	56,5	55,1	58,5	61,1
<i>Total</i>	<i>100,0</i>	<i>100,0</i>	<i>100,0</i>	<i>100,0</i>	<i>100,0</i>	<i>100,0</i>

a) Land area in use.

Source: AKII-CSO, 2003.

According to the financial basis for co-operatives, it is very important, that the co-operative must have at least 3 million HUF (proximately 11,500 euro in 2003) as property of co-operatives shares. In the case of secondary co-operatives the minimum amount is 10 million HUF (proximately 38,500 euro in 2003). The members get co-operative shares in exchange for their investments and they are eligible for earnings per share according to the results of the farming of the co-op. The liability of the members is limited, it is only up to their financial contribution.

Altruism appears in more paragraphs in the law. According to those parts, the co-operation between the members and the co-operative is not businesslike. However, as part of the co-operative's activity the co-operative has also business activities undertaken for third persons or parties. The co-operative is operating on business at cost principle, it does not aim to gain profits from the economic relations with members. The institutions of the self-governance (democratic decision-making) are still the same as in the past. The one member - one vote principle is still valid, everybody in the General Assembly has one vote (democratic con-

trol), however the earnings per share depends on the transactions with the co-operative or on the personal contribution in the period. It is a significant change, that according to the new law, the leaders and officers of the co-operative can be outsiders, non-members as well, not just members as before. They can even participate in the general assembly and they have the right to make a proposal there.

The law fixed the common rules for the organisational changes, like merger, transformation into (joint stock or limited liability) company, demerger, etc. It is a very new rule that in a case of merger, the result has to be in accordance with the relevant regulation of the competition policy. This regulation is aiming to avoid the monopoly position (Kiss and Szabó, 2001) by certain co-operatives on the domestic market.

The last paragraph of the law mentioned above contains the rule that every co-operative has to be transformed into a new type of co-operative according to Law CXLI/2000 (MK, 2000b) or into a (joint stock or limited liability) company in five years. The most important difference is the fact that the new co-operatives do not possess the so-termed co-operative business shares.

The government (Government's decree 326/2001) has supported family farms and the reorganisation of the agricultural production according to the Western-European model: (MK, 2001a). The farmer who owns a family farm and meets some requirements, is eligible to apply for support to buy modern machinery or land, to invest into (re)constructing his (premises) buildings, etc. The government also supports the so-termed integrators to give chances for family farmers against the big market players.

There is a great significance of different (marketing) organisations of agricultural producers in the agri-food economy of the European Union, like agricultural co-operatives and Producers' Organisations (PO), which are active in the fruit and vegetable sector. POs exist in other legal forms as well, like joint stock companies, Ltd. Co.s, etc., they have to only fulfil certain requirements. The Hungarian regulation (25/1999 Decree of Ministry of Agriculture and Rural Development) takes over the European Union's one (Regulation (EC) N. 2200/96 on the common organisation of the market in fruit and vegetables) concerning POs. According to the above mentioned decree, the POs (in the Hungarian regulation the

abbreviation is: TЭСZ) organise production; store, grade, process and market products and are set up by producers of a certain product or (sub)region. A significant advantage of the organisation, that the fruit and vegetable producers could afford the support of the EU solely through their POs. In the next part of our study we will briefly show a case study on the development of the first officially acknowledged Hungarian TЭСZ (Mórákert Beszerző, Értékesítő és Szolgáltató Szövetkezet), which works as a very successful (e.g. in terms of increasing annual turnover and membership) co-operative in the fruit and vegetable sector.

## 6. Hungarian case study N. 2 on the mórákert purchasing and service co-operative<sup>6</sup>

The *Common Agricultural and Entrepreneurial Society, Móráhalom* was established in January 1994 with the aim of organising small-holders within a loose network. It is a non-profit organisation. Noteworthy is that, due to the existence of the former co-operatives in Móráhalom, people were reluctant to use the word co-operative. Therefore they established an intermediate form, to co-ordinate certain parts of members' activities. The basic principle of setting up this society was to co-operate, to enable members to step forward, particularly in the input and output market. The number of founding members was 35, but by October 1999 membership had increased to 1996. The main activity, in addition to organising joint projects, was the organising of collective purchasing activities. This type of co-ordination was successful, and in some cases savings of 18 or 20 % of the purchase cost were achieved.

A countervailing power was thus established, and due to the greater volumes involved and cash payment it was possible to buy seeds and chemical fertiliser much more cheaply than would have been possible for the small-holders individually.

Because the society was financed from membership fees the revolving fund proved insufficient to finance purchases. Consequently, in practice, the members put together amongst themselves the sums required for the quantities to be purchased. Members were informed of delivery dates, and they transported the input materials by means of their own vehicles

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<sup>6</sup> See more details on the case study co-operative in Szabó (2002b).

and stored them on their sites. As mentioned above, these joint purchasing activities were extremely successful. However, the main problem was rather to co-ordinate the marketing of the small-holders' produce. Therefore, the next step was to set up the Mórakert Purchasing and Service Co-operative, Mórahalom in April 1995.

The Mórakert Purchasing and Service Co-operative, Mórahalom, a successful so-termed new type co-operative, is a co-operative of a type built on the Danish model. The co-operative itself has no machinery or land capacity connected with agricultural production. The main (in fact, the only) aim of the co-operative is to co-ordinate purchasing and selling activities. The input side of the members' activities was organised first, as this was a simpler task. Co-ordination of sales began later. The co-operative had 52 founding members in April 1995; by April 1998 membership had increased to 66, by October 1999 the number of members was 134 and in the year 2002 the co-op had 289 members. All members have their own land property and assets for farming.

The co-operative employs a staff of 64 throughout the year, which is of great significance, since work is otherwise rather sparse and co-operative employees enjoy relatively high salaries in comparison with the local average.

The main aim of the co-operative is to purchase input materials and to sell vegetable and fruit products produced by the members. In line with this main aim the co-operative is endeavouring to establish secure markets for the long term. It offers services and organises the buying of input materials and the functioning of selling outlets in a more co-ordinated way, therefore promoting farming for the small-holders through better market prices.

Providing information is also very important with respect to the success of the co-operation between the co-operative enterprise and its members. Another basic aim is for the co-operative to be a kind of non-profit organisation, so it runs according to the business at cost principle. After the subtraction of deposits and cost from the surplus made annually the co-operative reimburses members in proportion to their turnover with the co-operative.

The co-operative follows wholesale market prices, collecting data on a daily basis from the two major prices indexes. Members can obtain in-

formation from a published circular, which provides practical details such as when and how input materials ordered can be delivered.

One of the main steps enabling competitiveness to be achieved on saturated markets is for the co-operative to differentiate its products from those of other producers. The co-operative sells potatoes and onions in different packaging bearing its name, which makes it easier for the consumer to remember and recognise its produce. Bar codes are also used, and a registration system is being developed to enable the co-operative to control its selling parameters on computer. The system allows those operating it to distinguish which member's vegetables are being sold to a specific market, and therefore the farmer can be tracked down if problems arise. This facilitates the work of the two purchasers, particularly at peak times, when vast quantities of vegetables and fruit have to be procured within hours.

70% of the produce purchased from members is sold on the domestic market and 30% abroad (Estonia, Latvia, Lithuania, The Czech Republic, Slovakia, Slovenia). The co-operative marks the onions, potatoes and peppers it sells with its own label, and is now attempting to increase the range of products sold in packaging showing its name.

About 90% of the products distributed on domestic markets by the co-operative are sold to retail chains (Tesco, Metro, Spar, etc.); wholesale markets are avoided where possible, in order to shorten the marketing chain. Some products are sold on a contractual basis according to weekly prices. The co-operative is attempting to increase the proportion of export sales, but it presently uses exporters to sell its produce abroad. However, the aim is to export as part of co-operative activity.

Various marketing channels are being used, from individual shopkeepers through wholesale markets to retail chain networks. In accordance with the trends in Europe and the US, the importance and share of the retail chain networks is increasing year by year. It is very difficult to achieve a foothold in one of the chains, but such a foothold is a secure position if the co-operative can deliver the entire range of produce to the network, while also guaranteeing top quality and a high degree of flexibility.

To achieve competitiveness, in certain cases the co-operative works on the basis of so-called production contracts, which involve the co-operative detailing the requirements for the producer to ensure that the

necessary quantity is produced. At the same time efforts are made always to purchase input materials of the same type, to enable members to accomplish excellent, balanced quality in their production. The co-operative also deals with produce derived from non-members, in the interest of achieving better exploitation of its capacity, but its activity does not extent to purchasing on behalf of non-members.

They reinvest the surplus made in the co-operative annually. The biggest plan is to establish a so-called secondary or regional type co-operative which would be a good institution to secure markets for the members, to increase product's prices and in the meantime to reduce transaction costs.

## **7. Conclusions: different routes in the Hungarian agricultural cooperation**

Although the so-termed conversion process analysed in the first part of the paper (and mainly caused by political and state support uncertainties in the Hungarian case), is taking place in Hungary as well, some co-operatives (like the Mórakert co-op) still preserve their legal status and organisational structure. There are a number of reasons, why members have still loyalty to their co-op. The organised trust connected to relational connections in the co-op are crucial factors to solve the first hold-up problem, e.g. prevent post harvest hold-ups (Hendrikse and Veerman, 2001), at least at the relatively low level of product differentiation. The Mórakert co-operative is very good example, how an agricultural (marketing) co-operative can achieve some of the potential advantages (Ihrig, 1937; Spear, 1999; Szabó, 2002a), solving many "traditional" TCE and agency problems (Borgen, 1999; Szabó, 2002b) and serving its members with a continuing growth. However, due to oligopolistic and monopolistic power in several industries, there are now only a few sectors and branches in which co-operatives are able to achieve success. In the case of the 'doubly' transformed Kapostáj Agricultural Co-operative it can be stated that the former co-operative, with its leaders, is a strong economic centre in the micro-region and has the capacity to adapt to different conditions and the changing economic and social environment with a high degree of flexibility. And that is the reason why the Kapostáj

co-op transformed into an IOF form. However, according to Ihrig (1929), one has to bear in mind, that only the careful examination the threefold (product, capital, control) connection between the members and the co-operative will show whether an organisation is still a co-operative or ‘just’ an IOF firm, not the external-legal form...

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