A co-operative must be run as a business and needs an intergenerational strategic focus to match that of its members.

The meaning of being a 'co-operative'

BY: **NICOLA SHADBOLT**

Recent announcements by Fonterra on how they will reward/penalise their owners for sustainability practices generated a range of responses including some saying they are not 'being co-operative'.

This raises the question of what does being co-operative really mean? The answer is, as with so many similar complex questions, that it depends! What might seem right in one cooperative will be greeted with scorn in another, it all depends on the history of each co-operative, the legislation they have evolved and exist under and the expectations of the owners that have built up over time.

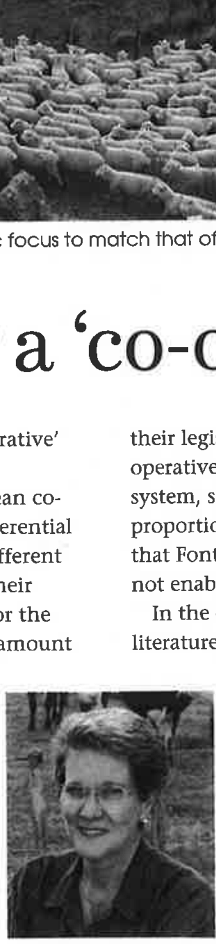
These differences were brought home to me when I was invited to a Co-operative Leaders' workshop in Missouri just after I stepped off the Fonterra board in late 2018.

Attendees came from a wide range of countries and as we worked together on Professor Mike Cook's co-operative life-cycle framework it became obvious that there were quite different 'co-operative' systems in place.

For example, one of the European co-operatives not only deducted differential freight charges they also had a different price for the milk that supplied their premium products to that used for the lower-priced products. Once the amount of milk supplied went over a predetermined amount the price dropped. They also paid premiums for differing levels of quality and approved on-farm practices.

For that cooperative it was highly unlikely that each member received the same price for their milk. So, while some may say that is not treating everyone the same, it is not being 'co-operative', their response was that they were just running a good business by costing their inputs according to what they are worth to ensure the co-operative can be profitable and to align their members with market demand.

It was interesting to note that under their legislation members control their co-operative through a one member/one vote system, so they were very critical of votes proportionate to participation (wet shares) that Fonterra has, and argued that it did not enable democratic control.



Nicola Shadbolt.

In the co-operative business research literature, there are examples where paying the same price to everyone has led to discontent from those who have better quality or higher specification products that they know is worth more. This has often led to members selling the better product elsewhere and the co-operative then receiving only the poorer quality product. Not as easy to do with a product like milk, but always a risk if the end market is prepared to pay a premium for quality product.

For nearly a decade now we've been running a postgraduate course at Massey University on co-operative governance and management. The first assignment we ask students to do is to determine the difference between corporates and co-operatives. It always generates interesting debate because there are many ways in which a co-operative is very similar to a corporate, and in other ways it is quite different. And, just to confuse things further, there are many ways in which the co-operative business model has evolved throughout the world so there is no one typical model to compare against.

However, most co-operatives do deliver to a very similar set of principles that are based on the rationale for collective action, although the how of delivery will differ, as with the democratic control discussion above, but they are generally understood as being key to the success of all co-operatives.

As identified by Cook and others the co-operative business model can create some challenges. One commonly mentioned is the free-rider problem when new users join and reap the benefit others have built up over many years. The free-rider risk also exists if co-operatives undervalue their membership fee. This particularly becomes an issue if the co-operative expands and if the fee is insufficient to cover the capital cost of that expansion. We have had a very real example of this in NZ and one that led to the demise of a co-operative. The other one is agency risk; this is very important as it has led to the demise or upset of a number of co-operatives. This is the risk that appears once you delegate the running of your business to someone else.

The rules around how you select/elect those people and how well they then deliver to your needs are fundamental to minimising this risk. How well they are held to account is probably the most telling as an out-of-control board/ management can also do great damage. There are various examples from around the world of how this is addressed, the most novel I have observed is an Indonesian collective that rotates the role of chair in the board to contain the power imbalance that can lead to dysfunctional boards. A commonly used definition of co-operatives is that they are user-owned, user-controlled and that they are there to benefit the users. A simple test then is to what extent are they user-owned, that is only those who participate in the co-operative (sell to/buy from it) have provided the capital through membership fees/shares and retained earnings. Then, to what extent they control the co-operative is a measure of how they use their ownership rights, who gets to vote on critical issues? Finally, how are the profits/ rewards of membership distributed among the members, is it an equal amount to each member, based on how much they participate, or on how much they own?

The benefits are also not always profit as they often include technical assistance, training, social programmes to name but a few. There is a belief that the co-operative is not just there to provide money, there is a strong membership expectation of more.

When I am asked to describe a co-operative, I reflect on my many years as a member of several co-operatives, as an academic researcher and teacher of co-operatives and as a governor of a co-operative and come up with this simple definition: A co-operative is a socialist construct in a capitalist skin.

Essentially a co-operative must get the collective action, the 'core' right, we are in this together, we are stronger together than apart, we matter to each other.

The term 'socialist construct' is a bit off-putting for some but I use it purposely to reflect that it is about people and what matters to them and their families and communities. However, without a capitalist skin the co-operative becomes redundant, like the ones that only receive the poor-quality product, as their members have moved their better-quality product elsewhere. The capitalist skin dictates that the co-operative must be run as a business but not just with a short-term corporate focus, it needs an intergenerational strategic focus to match that of its members. This requires strong governance with appropriate accountability to minimise agency risk.

When I shared this definition recently the response I got was enlightening – so the shareholders' council looks after the socialist construct (reinforced by the fact that they are elected on a one-farm one-vote basis) and the Fonterra board looks after the capitalist skin. Neither body is independent of the other, both work together with mutual respect to deliver overall success.

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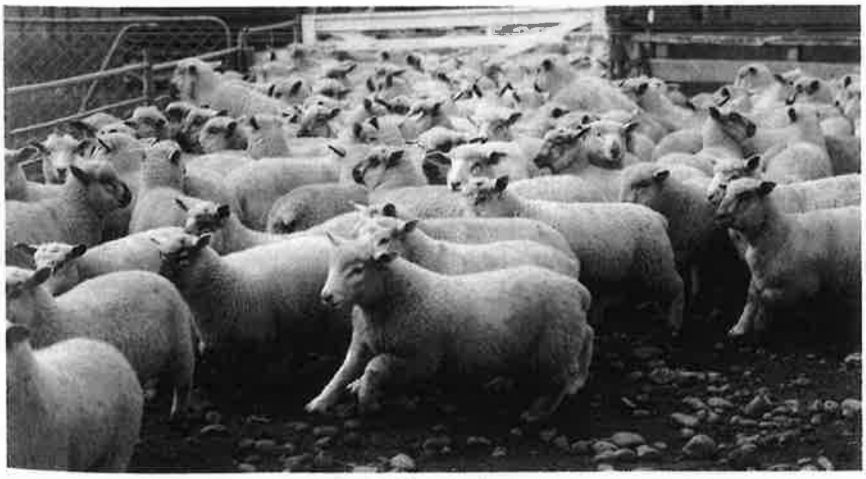
COLLECTIVE ACTION:

Principles for Co-operatives:

1. Voluntary and Open Membership
2. Democratic Member Control
3. Member Economic Participation
4. Autonomy and Independence
5. Education, Training, and Information
6. Co-operation among Co-operatives
7. Concern for Community

From: International Cooperative Alliance (ICA)



Paying the same price to everyone has led to members selling their better lambs elsewhere and the co-op receiving only the poorer quality product.