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The Conversion Syndrome

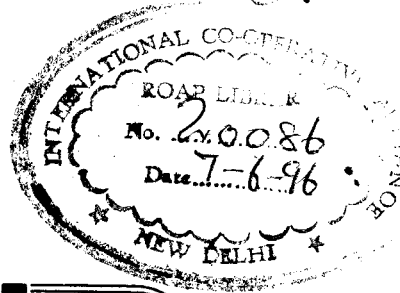
A Review of the Conversion of Australia
Cooperatives into Investor Owned Firms

by

Garry Cronan

Manager, Cooperatives Development
Department of Local Government & Cooperatives
Registry of Cooperatives
NSW 2200, Australia

334(94)
C80



International Cooperative Alliance

Regional office for Asia and the Pacific

"Bonow House", 43 Friends Colony (E),
New Delhi - 110065

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The Conversion Syndrome

A Review of the Conversion of Australia Cooperatives into Investor Owned Firms¹

In June this year, Australia's leading business newspaper, "The Financial Review" carried the story that one of the country's largest and most successful cooperatives was on track to be listed public company by the first half of 1995. Namoi Cotton Cooperative is the nation's largest cotton ginner and marketer, with an annual turnover of almost \$400M (AUS) and exports of approximately \$280M (AUS).

Such news items are not unfamiliar in the history of the cooperative movement in Australia.

The rate of conversion of some of the country's leading cooperatives into company structures has quickened, as competition and deregulation of the nation's economy intensify. The cooperative sector has lost million of dollars of turnover to the world of investor owned firms. Many thousands of Australians have lost their direct association with the cooperative movement.

The cooperatives that have companies have not necessarily been the failures of cooperation but rather some of its successes. In particular, agricultural cooperatives and Building Societies have been those most likely to convert.

The paper will examine the experience of general cooperative which have converted into companies, such as agriculture marketing and supply cooperatives. Reference will be made where appropriate to Building Societies, Credit Unions and other mutual financial cooperatives. The theme of the paper is that Australian Cooperatives have tended to convert to investor owned firms in the absence of alternative integrated and supportive cooperative structures and networks. Such structures and networks if present could well provide cooperatives with greater flexibility to deal effectively with the challenges of a competitive market place, without recourse to changes in identity.

Relevance of Experience

Is the Australian Cooperative Movement's experience relevant when considering the wider issues of cooperatives structural adaptation and transformation occurring in the Asia Pacific region?

Much can be learnt from an understanding of why, in the context of an economy such as Australia's and as a response to competitive pressures, some cooperatives would choose the option of converting to a company structure. Such an understanding may be of interest to other countries and movements in the region dealing with similar challenges.

The Structure of the Australian Cooperative Movement

Does the structure of the Australian cooperative movement, by its very nature, make cooperatives prone to conversion to investor owned firms.

In examining this I would like to use a metaphor to describe the structure of the cooperative sector in my country compared to that of many cooperative movements overseas.

It strikes me that best description of this situation is summarised in the metaphor.

“ The forest versus the paddak”.

For those of you who may be unsure of what I mean by the expression paddack, in the Australian context it normally means a fenced field or piece of land, generally with a scattering of trees.

Let me explain.

In Australia we have quite a few large well-developed primary cooperatives such as the cotton cooperative I mentioned at the start of my paper. We don't however, have any developed second or third tier cooperative structures. As a result of the absence of these unifying secondary and tertiary levels, we lack the integration and synergy that characteristics more developed cooperative sector overseas. As Dr Gary Lewis observes in his comprehensive study of Rochdale Cooperation in Australia, “there has never been a cooperative movement, as such in Australia”.

This situation can be best visualised in the “forest versus the paddock” metaphor. In Australia we have a few large mature primary cooperatives (trees) generally isolated (in paddocks) but no developed movement (forest).

Extending my metaphor, we can equate the competitive forces of deregulation, privatisation and globalisation, with the winds of change blowing through the various types of cooperative movements-paddocks and forests. It is apparent which cooperatives are best able to survive the force of the wind. The forest helps support the trees within it; the paddock provides no such protection.

The significance of Cooperative Networks

The layers of cooperative activity in the more developed overseas movements clearly give those cooperatives greater opportunity to respond to the competitive forces they face. The Australian cooperatives, generally isolated, are far less likely to be able to resist these forces - one manifestation of which is the conversion syndrome.

I contend that if Australian cooperatives had alternative integrated, supportive structures and networks, the option of conversion to investor owned firms would not have been so readily considered, and embraced by some cooperatives. Such structures and networks could have provided solutions for some of the structural deficiencies of cooperatives, offered precedents in management approaches and practices for dealing with competitive challenges, focused education and advisory services as well as encouraged greater governmental support and understanding for the sector.

The absence of integrated supportive networks for a sizeable portion of the movement in Australia, has meant that cooperatives have often had to deal with these competitive challenges at the level of either:

- * the individual organisation, that often resorted to prevailing corporate culture, with its supportive infrastructure for solutions; and/or
- * within the context of a broader industry response, that may not necessarily be concerned with cooperative sustainability.

Regional Context

Mr. Robby Tulus, Senior Policy Adviser, International Cooperative Alliance, Regional Office for Asia and the Pacific (ICAROAP), although not dealing directly with the conversion factor I am addressing, makes a relevant point in his background paper "Cooperative Competitive Strength: Positioning Cooperatives in the Market Oriented Economy". prepare for this Cooperative Ministers' Conference over 26-30 July, 1994, in Sri Lanka. When discussing the question of structural adaptation and transformation of cooperatives Mr. Tulus writes:

"Transforming cooperative structure is a vital aspect in the context of economic liberalisation. This includes identification of the gaps and superfluous links within the existing structure. In order to ensure organisational strength and efficiency of the whole system, the structural gaps should be covered, and superfluous units eliminated The aim should be to improve the operational efficiency of the entire structure both vertically and horizontally, and hence build a working system".

The wisdom of these words is borne out by the Australian experience. There is an undoubted need for more vertical and horizontal integration in the cooperative movement, if it is to successfully respond to competitive challenges. We need to nurture a "working system" in Australia.

The Australian Economy

The challenge to cooperatives are taking place against a background of significant adjustment and what amounts to a gradual restructuring of the Australian economy.

Australian Governments, both State and Federal irrespective of political allegiance are all committed, in varying degrees, to policies of deregulating the economy and increasing competition, both domestic and international. Such policies include the removal of regulatory restriction in the financial and rural industries, and the removal of barriers to the importation of many products, thereby, exposing Australian industry to full international competition.

Many previously government owned services or utilities have been, or are being, privatised Government supported agricultural marketing arrangements are being removed, and producers are now expected to make their way in an increasingly competitive environment.

There have been efforts by both Government and industry to link Australia's future development with the fast growing economies of countries in the Asia Pacific area, and to focus policy makers, corporations and individuals on the opportunities in the region.

Various Governments within Australia have developed programs designed to encourage industry to adopt practices to become world competitive. Included among these initiatives are: best practice programs, total quality management, export, trade and value adding enhancements, industry restructuring packages, major new job training programs and innovative investment schemes to mention just a few.

As the Australian economy has become more competitive the position of cooperatives in some industries has been challenged. Many of Australia's more successful cooperatives have developed in industries which in the past have had a large degree of regulation. As these industries are deregulated cooperatives are facing threats to their market share not only from domestic but international competitors. In the face of such challenges, questions are being asked about the sustainability of the cooperative structure.

Extent of Conversion

The current wave of conversion of cooperatives into investor owned firms, follows on from the period of the late 1950s to the 1980s when as documented by Dr. Gary Lewis "much of the traditional Australian cooperative movement was lost". In particular, Dr. Lewis records that during the 1970s "the backbone of the rural cooperative movement had gone, subsumed within capital" as cooperatives converted to company structures.

In the terms of my metaphor, the trees in paddock had begun to fall.

The conversion syndrome has occurred in almost all Austra-

lian States irrespective of the legislative arrangements existing at the time.

A list (incomplete) of Australian cooperatives, which have in recent years converted into company structures is attached (see Appendix 1). This list of 49 cooperatives (including Building Societies) represents hundreds of millions of dollars of annual turnover.

The 39 general Australian cooperatives (excluding Building Societies) included on the list may not appear numerically significant in the context of the overall number of cooperatives in Australia. It is hard to determine the exact number, no national database exists at present, however, it would appear that (excluding Building Societies, Credit Unions and other financial cooperatives), there are approximately 2300 registered general cooperatives in Australia.

Why the concern about the conversion syndrome, if only 39 of the 2300 have recently decided to convert?

The answer lies not in the actual number but in the size and strategic nature of those cooperatives that have either already converted or are thinking about doing so. As Mr. David Williams, Executive Director, Hambros Australia, a merchant banker with considerable experience dealing with cooperatives recently noted in an article in a national dairy industry journal:

"In the past two years there has been a revolution in the Australian bush. There is hardly....a significant cooperative that hasn't considered its corporate structure or the adequacy of its capital structure".²

The problem for the cooperative movement is that it could well represent a trend that will be difficult to stop.

I would like to briefly consider some statistics in relation to New South Wales, which has probably the largest number of commercial cooperatives incorporated under discrete cooperative legislation in Australia, to demonstrate the fragility of the movement.

If the aforementioned cotton cooperative was to decide after a vote of members to convert approximately 16% of the turnover of the New South Wales cooperatives sector would be lost in that

one conversion alone. The top four of the eight hundred cooperatives in New South Wales account for over 50% of the \$2.5B (AUS) turnover within the State's sector annually. The top twenty five cooperatives in the state account for 75% of the turnover annually. In other words the New South Wales sector consists of around twenty five comparatively large primary cooperatives with a much greater number of smaller less commercially significant cooperatives. Clearly if larger primary cooperatives are going to convert into investor owned firms, as is periodically suggested in the media, then the cooperative sector in New South Wales will be greatly weakened by such actions. A similar situation exists in other Australian States.

Apart from conversions generated from within, a number of major cooperatives, such as New South Wales' largest, Australian Cooperative Foods have resisted concerted corporate takeover attempts, during the last few years. These examples are additional to those listed in this paper.

Future Studies

As far as I am aware, no detailed comparative study has been done within Australia on the subsequent financial results of these converted organisations. Such a study might determine if there has been an improvement in performance as a consequence of the change of ownership and governance structure. Other important questions to be considered might include:- What is the relationship of the former members with the new corporate entity? Do they now have any control over their former cooperative? Does the new company structure continue to serve their interests, or has it gone on to focus on other, perhaps more profitable, pursuits? Has it retained anything of its cooperative heritage?

Such a study is beyond the scope of this paper but has the potential to objectively evaluate the merits or otherwise of conversion.

Factors Contributing to the Conversion Syndrome

I hope through the metaphor of the "paddock versus the forest" you will gain an impression of the structure of the Australian Cooperative Movement, and from the listing provided

with this paper and appreciation of the extent to which it is prone (at least in part) to the conversion syndrome.

I have identified twelve specific factors that have helped shape the landscape of the Australian cooperative movement. These factors illustrate the vulnerability of cooperatives and highlight some of the weaknesses inherent in the Australian cooperative sector. They all in some way affect the achievement of the supportive cooperative structures and networks that I suggest are necessary to offer cooperatives greater flexibility in dealing with competitive challenges. If we were addresses it would strengthen and enhance the ability of the cooperative model to withstand the winds of change, as manifest by the conversion syndrome.

The identified factors are grouped under four headings:

- # Structural
- # Management
- # Education and Advice
- # Government Facilitation

Structural

I have identified seven factors in the structural area relating to the overall shape and nature of movement in Australia. Some of the factors may be unique to Australia, other factors will be common to most cooperative movements throughout the world.

1. Cooperative Capital

Australian cooperatives like their counterparts throughout the world are trying to reconcile the de-emphasised role of capital within cooperatives with the need to obtain sufficient funds to remain competitive.

Cooperative fundraising was the subject of at least two major national conferences in recent years. In particular, the Cooperatives 2000³ Capital Conference in Sydney in late 1993 dealt extensively with this issue. This Conference focused on the options available to cooperatives to raise additional capital while retaining their cooperative character.

The lack of options available for cooperatives to raise sufficient equity funds is often given as the main reason for a

public listing in Australia. A spokesperson for Gresham Partners, the advisers to Namoi Cotton, is quoted as saying “**What Namoi is about is responding to the competitive environment, getting more flexibility in its funding so that it can compete on an equal basis with the corporate processors**”⁴.

While it is true cooperatives have less fund raising options than investor owned firms, it is also true that Australian cooperatives have not been sufficiently innovative in encouraging their members to view the “investment” of funds in their own organisations as worthwhile.

Equity Features of Australian Cooperatives

It has been noted that there is a wide range of equity structures in Australian cooperatives. Mr. Ian Langdon, Chairman of Australian Cooperative Foods, in a paper to the 1992 Agricultural Cooperative Capital Update Conference in Queensland, points out that apart from normal commercial pressures the varying application of cooperative principles has resulted in a range of capital structures in agricultural cooperatives in this country. He reports that :

“There are a number of cooperatives that have a nil or close to nil share capital base and there are a small number who have adopted quasi revolving funds or reserves. These are very much in the minority. The dominant equity feature of Australian agricultural cooperatives is their use of a base share capital plan and extensive use of unallocated reserves”.⁵

Legislative Options for Fundraising

General cooperative legislation varies throughout Australian in regard to the options available for fund raising. The New South Wales Cooperatives Act, 1992 provides probably the greatest range of available alternatives among the Australian States. The main options include : Members shares; entry fees for membership; periodic charges payable by members; loans by members, the new Cooperative Capital Units; and external borrowing⁶. There is no provision within any discrete State cooperative legislation for a second class of share, whether issued to members or non members.

In spite of the fact that a range of alternatives has existed in the legislation, cooperatives have not maximised the opportunity to raise funds from their members. Within New South Wales, during the ten year period 1982-1992, only approximately 50 cooperatives made use of the compulsory share and loan mechanisms available under the legislation, to raise around \$38M (AUS) in equity and \$6M (AUS) in loan funds from members.⁷

The new cooperative legislation in New South Wales now allows for the issuing of a financial instrument called a Cooperative Capital Unit, (CCU) which may have some of the character of either debt or in some limited sense equity. CCU's can be issued to members and non-members alike. The first issue of CCU's to the public has recently been made by Norco Cooperative Limited, a regional based dairy cooperative. The Chairperson of Norco in the information statement for the CCU issue says "For 100 years Norco has been proving the value of cooperative ownership within the agricultural and food industries. Your investment in Norco Capital Units will help Norco grow even more strongly as it moves into its second century of service to rural Australia".⁸ It is the dairy industry and others like it, which have a strong cooperative presence, but are facing major competitive forces, that are seeking fundraising solutions consistent with cooperative principles.

Growth and Cooperative Philosophy

Mr. Langdon, in a paper delivered at the 1993 Capital Conference makes the point "the challenge is to find a practical response to the current commercial pressure to grow and to **fund that growth in a manner that is compatible with both survival and cooperative philosophy**".⁹

If cooperatives wait until there is an urgent need for funds then in all probability it is too late to have their needs met by members alone... external equity raises the threat of loss of control"¹⁰. I have previously noted "the dilemma for cooperatives is that by basically restricting their fund raising to their membership, they maintain control but members are often either unwilling or unable to contribute sufficient funds - either directly, or by way of retained surpluses - for the cooperative to be competitive".¹¹

A number of Australian cooperatives particularly in the dairy industry are closely examining the model of the Irish dairy cooperatives that have introduced external equity. Fast rates of growth are achievable using similar hybrid models but if control is to be maintained in the hands of the members they will need, over time, to fund their share of that growth.

It is also worth making the point that general cooperatives in Australia are not very experienced in dealing with external equity. If equity CCU's are, for example, to become popular, cooperatives will need to avoid the conflict of competing interests developing between the members and external equity holds. Ironically one of the outcomes of such conflict may be pressure to convert.

Value for Members

Cooperatives need to offer value to their members. Mr. David Williams, when discussing the issue of cooperative members' reluctance to contribute capital and the related problem of the conversion of agricultural cooperatives into companies, draws the following conclusions in regard to Australia “

“Properly advised, I have found cooperative members to be more than willing to contribute additional capital where this can be shown to provide them in adequate return. Treating them better requires communication, equitable treatment and redeemable shares. In achieving equitable treatment, cooperatives shares need to reflect their realisable value. If they do not, farmers cannot be blamed for saying they have no value. Moreover, unallocated reserves and asset value changes will encourage takeovers or restructuring which would be otherwise not justifiable”¹².

Limited Return

The issue of limited return on capital in a cooperative is a core consideration for members contemplating a change from the cooperative model to an investor owned firm. As Mr. Langdon notes in his paper “Valuation of Cooperative Shares - Do They Have a Value” also prepared for the 1992 Conference in Queensland :

“It is difficult for cooperatives to raise equity funds if there is limited reward for investment of capital. The prohibition of capital appreciation is a significant deterrent for members to invest in equity.....The challenge for cooperatives is to devise member based equity structures that link share ownership and patronage so that returns on capital do not breach the equitable distributions of surpluses principle. Such returns could be either in the form of allocations of operating profits or in the form of capital appreciation of shares through bonus issues, but only if shares were held on a patronage basis”.¹³

Shares in Australian cooperatives are normally redeemed at par value. Combining this with the fact that share registers of cooperatives have often contained a majority of inactive members can mean that a conversion will sometimes be supported simply to unlock the “real” value of the shares.

Active membership requirements have been introduced into New South Wales cooperative legislation to ensure that it is only active members who will vote in cooperatives on questions such as conversions. This however, only addresses one side of the problem. There is still a need to ensure that current and past members receive value from their participation and “investment” in the cooperative. To do otherwise in the Australian context is to ignore one of the major motivations for members to convert their cooperative into an investor owned firm.

Summary

The combination of deregulatory forces, and increased competition has meant that cooperatives, particularly in some of their traditional industries such as dairying, are no longer able to operate without competitively managing their capital. Their problem is that they may lack a viable capital structure, at the very time they face their most competitive challenge - often in the form of adequately funded investor owned firms, who incidentally may have been previously locked out of these markets by regulation. They can be restricted from quickly accessing adequate funds from either their members or the market because of the operation of cooperative principles.

The nature of cooperative capital and the past practices of cooperatives in this area are often proffered as the main explanations for the conversion syndrome. The resolution of this issue for cooperatives remains central to the long term survival of the movement in Australia.

2. Representative Cooperative Organisations

The recent history of representative national general cooperative organisations in Australia has not been encouraging for the long term development of an integrated movement (forest). It has appeared that for one reason or another the national structures which have been created in this country have not been sustainable in the longer term. There is a sense in which its history has been of a stop start nature. Considerable effort has been expended by the movement, but in the end, the national organisations have not been able to effectively build either lasting support from within the movement or broaden their base so that they gain wider community support for their activities.

Within the last two years the peak national organisation the Australian Association of Cooperatives, (AAC) has gone into liquidation. AAC in effect replaced the earlier Cooperative Federation of Australia, (CFA) as the peak national organisation for general cooperatives in the mid 1980's. Both AAC and CFA had themselves sought to develop links with the ICA.

Following AAC's collapse, (due in part to the failure of a banking operation for general cooperatives) a new national structure was established. The new structure was build upon some of the remaining State Cooperative Federations which had not become part of AAC, and newly formed Stat organisations. This organisation known as the National Cooperative Council of Australia (NCCA) has as its only members five State Cooperative Federations. Primary cooperatives cannot belong to the NCCA, rather they join their respective State Cooperative Federations. The NCCA has at this stage decided to focus more on issues of national concern rather than seeking to build and develop contacts with the international cooperative movement.

The NCCA and State Cooperative Federations are also not likely at this stage to pursue a similar commercial course to that of AAC. As a consequence their activities will be restricted to

mainly representing the sector to Government. Services such as insurance, legal advice, trade facilitation will not be undertaken.

Apart from financial cooperatives, like Credit Unions and Building Societies, the general cooperative sector's representative organisations are organised not on industry groupings but on geographical regions, specifically, the Australian States. Within the regional State Cooperative organisations there may be some industry sub-groupings.

The failure of AAC and the need for regrouping within the NCCA/State Federation structure has represented a considerable setback for the movement in Australia. At the very time when competitive pressures on the cooperative model are increasing the movement as represented by its national apex organisation is probably at its most vulnerable point for many years.

The collapse of AAC and the subsequent need for New South Wales Government assistance to smaller community cooperatives affected by the fallout, as well as the recent demise of Letona Cooperative, a large fruit and vegetable cannery and the failure of major Victorian Building Society, have not helped the public perception of cooperatives. In the last couple of years, there had been no apex general cooperative organisation able to go to the media to argue the case of the retention of the cooperative model. This is at the first time the financial and business media are reporting the increasing number of cooperatives contemplating conversion.

3. Cooperation Among Cooperatives

The forest of my metaphor requires multi-layered interaction between cooperatives not only in a representative sense but in truly commercial one. For this to be achieved it requires cooperatives to believe that they can obtain real commercial advantage for their members from active cooperation among cooperatives. Such strong links can ultimately lead, in the previously quoted words of Mr. Tulus, "the improvement of the operational efficiency of the entire cooperative structure both vertically and horizontally, and hence build a working system"¹⁴

The history of general cooperation in Australian demonstrates the we have so such working system. The trees in paddock don't connect. There is no sense in which the growth of one assists

with the development of other cooperative organisations. Indeed in some cases cooperatives have seen other cooperatives as their major competitors, rather than organisations they may have interests in common with. While there have been some notable exceptions (particularly in the credit union movement), the general experience has been that any attempt at commercial cooperation among cooperatives has been short lived.

By way of contrast the American agricultural cooperative system shows the advantage of doing business the cooperative way. Cooperatives both cooperate and compete with each other at various levels throughout the system. It represents unique blend of cooperation and competition. There are local cooperatives which may be either supply or marketing cooperatives. These locals then combine together to form regional, which then combine together to form inter-regional.

For example the local cooperative agricultural store may sell fertiliser which it obtains from its regional cooperative. The regional is able to offer a good price for this product because it buys in bulk for all its member cooperatives. The regional cooperatives may have come together to form an inter-regional cooperative to bulk produce the fertiliser. Cooperatives at various levels in the system are free to choose whether they will purchase the product from their affiliated cooperatives. It makes sense however, if the price and service is reasonable, to support the cooperative group they are a part of. The system benefits in a competitive sense from these economies of scale, while retaining and building a market presence for cooperatives to build a competitive working system.¹⁵

The American system enjoys some protection from the legislative effects of anti trust or anti-competitive regulation. To this extent American agricultural cooperative had time to develop these working cooperative systems, and so be in a somewhat stronger position, to competitively respond to market challenges such as the conversion syndrome.

Nevertheless, even given that qualification, Australian cooperatives are still not embracing the idea that one of their available competitive responses is far greater cooperation among cooperatives. This is at the time that business literature and government programs are showing corporate Australia the commercial ben-

efits of collaborative or networking strategies.

4. *Cooperative Culture*

If economic considerations are finely balanced, cooperative cultural values may be the deciding factor in determining whether an organisation remains as a cooperative or converts into an investor owned firm.

In this context I have taken the term cooperative culture to mean the sum of experience, history, values and principles of cooperation, both in theory and in practice.

It would seem that there is only a limited sense of cooperative culture within the general cooperative movement in Australia and little appreciation of such values in the broader community. What historical perceptions may have existed appear to be diminishing as the pace of societal and economic change quickens.

Cooperative Character

Prof. Hans-H. Munkner in a background paper "Structural Changes in Cooperative Movements and Consequences for Cooperative Legislation in Western Europe" prepared for a cooperative meeting in Marburg, Germany in July last year, points out that cooperatives can be seen as basically either "predominantly economic structures,... or movement for socio-economic reform."¹⁶ Dr Garry Lewis has characterised the history of the Australian Cooperative Movement, similarly as a struggle between pragmatists and idealists.¹⁷ His verdict was that the idealists were defeated and that the pragmatists achieved some limited success.

Cooperatives in Australia whatever their past history now appear to be predominantly economic structures, as Munkner says "concentrating their efforts exclusively or mainly on the promotion of the economic interests of their members."¹⁸

One of the consequences of this is that "in large scale cooperative enterprise with professional management the features resulting from the historical roots of cooperatives and the ethical and moral foundations of the cooperative way of doing business are often considered more to be burden of the past than a source of strength for the future"¹⁹

The challenge for the general cooperative movement in Australia is to draw from its neglected history those distinctive cooperative features which have enduring value, and to marry them with best international cooperative practice to create a relevant and vigorous cooperative culture.

The Demutualisation Process

If the history and culture of cooperatives is fully understood within the movement, there is even less appreciation of the role of mutual organisations, including co-operatives, in the broader Australian Community. To this extent the cooperative movement is not alone in Australia in facing the conversion syndrome.

Media attention in New South Wales has recently been focused on a large mutual motorists organisation, which is considering a public listing. This organisation which was originally started to provide roadside vehicle service to motorists, now has many hundreds of thousands of members. As part of the services offered to members the organisation developed insurance, travel and associated capacities. The insurance business has grown to such a size that it is now one of the State's largest businesses.

The current board and management of the organisation are presently seeking member support for conversion from the mutual structure into what they propose as a more appropriate business arrangement. There has been considerable debate in the media as to the merits of such a change. Many of the points raised in the debate mirror the issues for general cooperatives. It is symptomatic of the general demutualisation of business which has been proceeding not only within the cooperative sector, but in other areas including the insurance industry.

The Cooperative model needs to be able to compete in the marketplace of ideas-mutual organisations generally need to address the challenges represented by other ways of doing business. Cooperatives do have a lasting, legitimate and worthwhile role to play in the new internationally competitive environment. However, unless this articulated and supported by cooperatives themselves, it will be hard for the broader community to see the demutualisation process, as anything other than a historical inevitability.

5. Funding Organisations

General Cooperatives in Australia do not have, as do some of their overseas counterparts funding organisations specifically established to support them.

As a result cooperatives need to access funds from normal commercial sources. This has sometimes led to the suggestion that they are disadvantaged because such lenders don't really understand cooperatives. Whatever the veracity of these claims, it is clear that cooperative in this country when compared to say American agricultural cooperatives are the poorer, in terms of choice, for not having organisations such as the Farm Credit Administration and the various cooperative banks, lending funds to either individual farmers or more directly to cooperatives.

Effective long term cooperative development, almost by necessity requires a cooperative bank or equivalent organisation. Often these cooperatives lending organisations have grown out of the agricultural cooperative movements. This has not been in case in Australia-this vital piece of the forest has been missing.

For a variety of reasons including legislative restrictions, financial cooperative as represented by the Credit Unions and Building Societies are not able to lend to cooperatives in any commercially significant way. There has been a recent offer to develop a cooperative bank in Australia based on the credit union movement, however this has as yet been unsuccessful.

In a number of overseas countries the supporting infrastructure of dedicated cooperative lending institutions, whether established by the movement or the Government, have acted as a disincentive for cooperatives to convert to investor owned firms. In Australia in general no such disincentive exists. Exceptions to this are certain taxation entitlements available to agricultural cooperatives for the repayment of Government loans. However, these loans are only effectively being made in one State (Queensland) and are therefore not available to the bulk of Australian cooperatives.

6. Meagre Strategy

One of the strategic responses adopted by Australian Cooperative to competitive forces has been, not surprisingly, to merge

with other cooperatives in a similar position in an attempt to gain the advantages of greater market power. In both the dairy industry and the Building Society Industry such strategies have produced far more effective and efficient organisations.

However, given the absence of developed and integrated second and third tier cooperative structural options in this country, the process of amalgamation has meant that we have ended up with larger and fewer primary cooperative organisations. The larger cooperatives have tended to soak up the smaller cooperatives around them as they strive to become more competitive. Such a strategy is something of a mixed blessing for the longer term development of a more integrated cooperative movement. The result is fewer and larger cooperatives which may convert into companies upon reaching a certain size, or dominance their particular market.

Limitation on the overall size of any one cooperatives and the establishment of linkage between cooperatives are strategies which have been pursued by movements in some countries to combat tendencies.

7. Regulated Industries

I have already noted that many of Australia's most successful cooperatives have developed in the shadow of regulation, the Building Societies and the dairy and sugar cooperatives probably being the best examples. To this extent deregulation has represented a challenge to the sustainability of the cooperative model because the most successful examples of individual cooperatives, or industry cooperative groupings, are also probably the most vulnerable to conversion.

If cooperatives in growing industries which traditionally have a strong cooperative presence are converting or giving consideration to conversions, then it can create an image that the organisation has outgrown the cooperative way of doing business. That there is somehow an upper limit to the size of cooperatives, given certain market characteristics and accompanying deregulatory government policies.

Nevertheless, deregulation has also represented an opportunity for cooperatives. Some of the most interesting and innovative new cooperative formations have occurred in industries which

have been previously heavily regulated. Members in these cooperatives are looking, in particular, for new ways of marketing their products. Deregulation has also hastened the movement from a purely production focus to a more market oriented perspective for many cooperatives.

All Australian governments whether state or federal are considering deregulating the Statutory Marketing Authorities (SMA's). These organisations have previously had responsibility for marketing many agricultural commodities. A number of SMA's are or have considered converting into cooperative structures. The deregulatory process presents an opportunity for the general cooperative movement in Australia to develop a comprehensive strategy to establish through new cooperative organisations the necessary building blocks for a working, integrated cooperative system in this country. Such a system would be an alternative to industries dominated by large investor owned firms.

Management

I have identified two features of cooperative operation in Australia which may be relevant when considering the conversion syndrome.

8. Directors and Managers Skills

Directors

General cooperatives are sometimes criticised for what some in the financial media regarding less than optimum performance. This lack of performance is often coupled with concern about the skills of directors and managers of cooperatives. Such criticisms often end by suggesting that solution to this problems lies in gaining additional skills for board by converting into company thereby accessing a greater pool of experienced directors.

Directors of cooperatives in Australia have been drawn almost exclusively from within the ranks of the membership of the cooperative. There has not been a tradition in this country of independent, non-active member directors serving on the boards of cooperatives. As a result the boards have reflected the underlying skills of the membership.

Being a director has involved an element of voluntary service on the part of members of cooperatives. For many the remuneration for the service provided has been very low or non-existent.

Often the member will have no previous experience as a director, prior to being elected. There have been very few cooperatives which have offered formal training programmes for the new directors. The movement itself is only now once again starting to address the issue of director training.

The expectation of performance for cooperative directors is increasing. Not only are cooperatives becoming larger, more diversified and complex business organisations requiring a greater range of skills to effectively manage them, but government now requires a higher level of accountability and responsibility from directors. The new cooperative legislation in New South Wales has provided cooperatives with greater commercial freedom but has also increased their level of accountability and responsibility.

Provision has been made in the New South Wales legislation for non-member independent directors. Such positions are limited to one in four directors. It is hoped that a pool of experienced cooperative directors can be established, so cooperatives which lack the necessary skills from within their own ranks can have access to experienced directors who will be able to bring a broader vision to the management of the cooperative.

Managers

It has been suggested that because cooperatives have not had a good image in the business community in Australia, they have had trouble attracting professional and experienced managers to work with them. If such a claim is true, it is probably because cooperatives have not been in a position to match the salaries offered by the private sector. Cooperatives have also had difficulty in knowing how to effectively recruit managers. Given such a situation the management of some cooperatives may conclude that their interests would be better accommodated if the organisation converted to a company structure.

9. Management Driven/IOF Background

There has been a tendency within some of the larger

cooperatives for management to appear to capture the agenda on the future direction of the organisation, without sufficient communication with, or support of the members. It is not surprising in a complex, diversified cooperative that some directors would defer to management in terms of the strategic direction of the organisation. On some occasions this strategic direction has involved the cooperative converting into some other form of organisation.

There are many more corporations in Australia than there are cooperatives. If a cooperative is seeking to recruit new and competent staff it will more than likely find the person seeking currently employed in a similarly sized or larger corporation. If recruited the managers will bring a completely new and different perspective to the role of running the cooperative. Some will make the transition to the cooperative way of operating more easily than others. For some the temptation will be to have the organisation, rather than themselves change to something they are more familiar with.

This situation is not helped by the fact that cooperatives cannot normally include their employees as members. If these employees could identify as part owners of the cooperative they may not be so ready to convert it to another structure.

The issues I have been addressing in regard to directors and managers have also been considered by Mr. David Williams. He has summarised his views in the following words :

“All of this is not meant as a dissertation to stamp out public listings of cooperatives restructuring of cooperatives into corporate entities or external equity raising. Rather, it is an attempt to discourage the practice of changing the corporate form of cooperatives for no good reason behind the shield of illogical and unsubstantiated claims by management and directors as an excuse for a corporate vehicle with perpetual capital and less direct shareholder accountability than that offered by the cooperative”²⁰.

Education and Advice

The absence of these two factors have been of particular significance for the cooperative movement in this country.

10. Lack of Educational Facilities and Commitment

A well known American writer on cooperation has expressed his views on the importance of cooperative education in the following terms :

“Cooperatives were started by people who believed in them. They were carried through the years of early growth by people who believed in them They will only be built into the strength and significance our country desperately needs by people who believe in them. However, efficient, cooperative business can never achieve success without the active , daily assistance of its essential companion - cooperative education”²¹

The ICA have recognised the importance of the role of cooperative education by making it one of the six international principles of cooperation. It has been said that a cooperative will only last for a generation and a half without a commitment to cooperative education.

Despite several attempts to create organisations in Australia devoted to cooperative education, no lasting progress has been made. Within the last two years a new organisation the Asia Pacific Cooperative Education Centre, has been established in Australia. This organisation will be focused on providing education and training not only to directors and managers of cooperatives in Australia, but throughout the Asia Pacific region. It is welcome and timely initiative and deserves to be successful.

The absence of effective and continuing cooperative education in Australia has meant that the current generation of cooperative directors and managers have operated to some extent a cooperative cultural wilderness - returning briefly to may metaphor, in a paddock without a forest in sight. The lack of effective cooperative education over the last ten to fifteen years in Australia should not be underestimated when looking for the reason why some cooperatives have had a tendency to convert into investor owned firms.

11. Lack of Supporting Information and Advice

For the cooperative movement to grow and develop it needs a supporting infrastructure service providers who can provide

objective and independent advice and information. As from a few government departments and to a limited extent State cooperative federations and one or two cooperative development and education organisations, no established network currently exists. Where and from whom cooperatives get their advice, particularly for major decisions like conversions, will often influence the final decision.

Large accounting and legal firms as well as merchant banks and other business advisers generally do not know a great deal about the operation of cooperatives. It is natural that they should on occasions recommend corporate structures they are more familiar with to their cooperative clients.

Government Facilitation

12. Separation of Governmental Responsibilities

As I have already stated the responsibility for the regulation and administration of general cooperatives in Australia resides with the various State Governments. The national Government has no direct responsibility and as a result there is no national Minister responsible for cooperatives.

One of the consequences of the States being responsible for cooperative legislation has been that the legislation is not consistent throughout the country. The lack of a national cooperative framework is increasingly being given as a reason why some of the large more nationally or internationally focused cooperatives would seek to convert into companies. As companies they could operate under Corporations Law which is the national company law framework. There are currently moves under way to address the question of the inconsistency of cooperative legislation. At least a partial solution to this problem is expected within the next twelve months.

The commitment of government resources to cooperative regulation and development vary throughout the States. If major cooperatives continue to convert into other forms of incorporation it may be that the critical mass of the sector is lost as far as government involvement is concerned and resources currently available to support the sector and withdrawn by one or more governments.

Financial Cooperative Regulation

Following the failure of a major Victorian Building Society a new state based national regulatory system was developed for Building Societies and Credit Unions. Previously, these financial cooperatives were, like the general cooperatives, regulated by the various State Government Registries' of Cooperatives. The new financial institutions arrangements have meant that in most States the previous Registries have been split between the new financial regulator and the former Registries of Cooperatives.

These new arrangements represent a historical break as far as government is concerned. The varying types of cooperative organisations are now the responsibility of different government departments and organisations. The policy driving the development of the various sectors of cooperative activity in this country are no longer connected at departmental level. This now also reflects the situation between the sectors on the ground where it appears that there is not any systematic attempt being made to encourage cooperation between Building Societies, Credit Unions or general cooperatives. The forest is not being nurtured.

Not All Bad News

The explanations provided in this paper for the tendency of some cooperatives to convert into corporate structures may read like a bad report card on the cooperative movement in this country. In some ways it is - but this is not the whole story. There have been examples within Australian context, where the forest of my metaphor has developed.

The Credit Union movement such an area. It is one of the success stories of the cooperative movement in Australia.

Credit Unions are very competitive with other organisations offering financial services in Australia. Their industry organisations have built strong representative and commercial structures to serve and assist their members throughout the whole country. This has been achieved in an industry which has been very competitive and one subject to major deregulatory changes. Credit Unions have also been at the forefront of many technological advances in the area of customer service. There has been a commitment by the industry to education and training. Of special

interest is the fact that they still stress not only to their members and employees but the general public, their cooperative character.

The experience of the Credit Union industry demonstrates that strong cooperative movement can be nurtured and developed in Australia.

Apart from the Credit Union experience a number of recent initiatives for general cooperatives have been commenced, particularly in New South Wales, which have the prospect of addressing many of the factors contributing to the vulnerability of the sector to the conversion syndrome. The cooperatives 2000 strategic plan has identified the key issues affecting cooperative development in this country to the turn of the century. These issues are remarkably similar to the factors I have identified as contributing to the conversion syndrome.

The Cooperatives 2000 Strategic Plan is currently being implemented. Other initiatives such as the current ICA/New South Wales Registry of Cooperatives international trade project offers some opportunity to demonstrate to Australian cooperatives the Advantage of commercial cooperation among cooperatives.

Again in New South Wales we have new legislation which has made the cooperative structure much more competitive with other forms of incorporation. Over the last few years a record number of new cooperatives have been formed, perhaps the start of the forest.

Conclusion

This paper has sought to provide an explanation as to why some cooperatives in Australia have decided to change their corporate identity from that of cooperative to an investor owned firm. I have not attempted to mount an argument that these conversions should not happen, rather to consider the underlying reasons why they occur.

I have pointed out that although Australia is a developed country with a high standard of living its general cooperative movement has not reach the same level of development. A number of factors have been identified as missing from the

structure of the general cooperative movement which has made it prone at least in part to the conversion syndrome.

The clear lesson for the cooperative movement is that, if it is to successfully respond to the challenges of an increasingly competitive world environment than it will need to maximise its strength as a movement through much greater integration. To do otherwise is not to learn from the Australian experience which has shown that cooperatives are very vulnerable when they are not a part of the forest

Thank you.

List of Recent Conversions

The State by State list included:²²

Queensland

- * Tully Cooperative Sugar Milling Assoc
- * South Johnston Cooperative Sugar Milling
- * Babinda Cooperative Sugar Milling Assoc
- * Atherton Table and Dairy Cooperatives
- * Buderim Ginger Growers Cooperative Assoc
- * Queensland Cotton Producers Cooperative
- * Queensland Independent Wholesalers Cooperative
- * The Associated Newsagents Cooperative
- * Master Builders' Cooperative
- * Plumbing Materials Cooperative
- * Associated Milk Service Cooperative
- * Master Butchers Cooperatives

Building Societies

- * Permanent Building Society

South Australia

- * Berri Fruit Juices Cooperative
- * Berri Cooperative Winery and Distillery
- * Renmark Cooperative Winery and Distillery
- * Vitor Citrus Cooperative
- * Red Comb Egg Cooperative
- * Associated Grocers Cooperative
- * Eudinda Farmers Cooperative
- * South Australian Fishermen's Cooperative (SAFCOL)
- * Southern Farmers Cooperative

Building Societies

- * Cooperative Building Society of South Australia

Western Australia

- * Teachers Credit Society
- * Plumbers Cooperative

Building Societies

- * Perth Building Society
- * Town and Country Building Society

Victoria

- * Autobarn Cooperative
- * Drouin Cooperative Butter Factory

Building Societies

- * Victoria Building Society
- * Permanent Building Society

New South Wales

- * Wyong Cooperative Dairy
- * Farmers Grazcos Cooperative

- * Wollondilly Abattoirs Cooperative Ltd.
- * Griffith Growers' Cooperative Society Limited
- * Australian Mushroom Growers Cooperative Society Ltd.
- * Cooperative Insurance Co. (CIC)
- * Cumberland Cabs Cooperative Limited
- * Western Districts Taxi Cooperative

Building Societies

- * NSW Permanent Building Society
- * United Permanent Building Society
- * St. George Building Society

Footnotes :

- ¹ Mr. Garry Cronan, Manager, Cooperatives Development, Department of Local Governments and Cooperatives, Registry of Cooperatives, NSW 3300, Australia
- ² Williams David, "Raising Cooperative Capital". Why members Resist, Australian Dairy Foods Journal April, 1994
- ³ Cooperatives 2000 is a joint Cooperative/Government initiative in New South Wales, designed to develop a strategic plan for cooperative development up to the year 2000. See Capital Conference Papers for full details of proceedings.
- ⁴ Australian Financial Review op.cit.p.27
- ⁵ Langdon, Ian "Australian Agricultural Cooperatives - A Current Perspective", 1992, A paper presented to the Agricultural Cooperative Update Conference, September 17-18, 1992, Queensland, Australia.
- ⁶ Magarey, Donald, "Guide to the NSW Cooperatives Law", CCH Australia Limited, 1994, p.93.
- ⁷ Cronan, Garry, "Policy Underpinning NSW Cooperative Legislation" 1993, A paper presented at the 1993 Capital Conference, November 1993, Sydney, Australia.
- ⁸ Information Statement Norco Cooperative Limited, Invitation to Invest in Norco Capital Units"
- ⁹ Langdon, Ian "Capital Fund Raising Options for Cooperatives" reproduced in the New South Wales Registry of Cooperatives newsletter "Cooperation", Special Edition, January 1994, p.2. Mr. Langdon is also a director with Phosphate Cooperative Co. of Australia Ltd. and a former Dean, Faculty of Business Studies, Griffith University.
- ¹⁰ *ibid*, p.5
- ¹¹ Cronan, Garry "The USA/Australian Experience" Australian Dairy Foods Journal, June, 1994.

- ¹² Williams, op.cit.p.50
- ¹³ Langdon, Ian, "Valuation of Cooperative Shares - Do They Have a Value", 1992. A paper presented to the Agricultural Cooperative Update Conference, September 17-18, 1992, Queensland, Australia.
- ¹⁴ Tulus, op. cit.,p25
- ¹⁵ Tgese features of the USA cooperative system were observed, when I was member of a study tour of American agricultural cooperatives, in late 1993. The tour was organised by Monash University, Melbourne, Australia.
- ¹⁶ Munkner Hans " Structural Changes in Cooperative Movements and Consequences for Cooperative Legislation in Western Europe", reproduced in a Report of a Colloquium held at Marburg, 2-3 July 1993, Enterprise and Cooperative Development Department, International Labour Office, Geneva.
- ¹⁷ Lewis op dt p 233
- ¹⁸ Munkner Op.cit,p59
- ¹⁹ Munkner, op. cit, p.60
- ²⁰ Williams, op.cit.p.50
- ²¹ Webb, Glen "Its a Long Way from Toad Line", American Cooperation 1991, p.21. In this article Dr. Webb quotes a 1954 editorial by Jerry Voorhis.
- ²² 1. Assistance in compiling this list was provided by Mr. Jim Manwaring and Mr Jayo Wickremarachchi, senior staff members of the Development Branch, New South Wales Registry of Cooperatives

