



POLICY STATEMENT ON COOPERATIVE ENTERPRISE

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1. INTRODUCTION

Cooperative enterprises – producer, consumer, agricultural, service, and banking – form the core of a PROUT economy, in which the majority of manufacturing and service enterprises would be organized as worker owned and managed cooperatives.

Cooperatives are the preferred form of enterprise in the PROUT economy because they are considered the best arrangements for human beings to work together. According to PROUT founder, P.R. Sarkar, "In society human beings have to work jointly with others so that everyone can move forward collectively." Only those things that cannot be done collectively should be done individually. If individuality dominates human life, it will "adversely affect the environment, the welfare of different groups and even the continued existence of humanity" (P.R. Sarkar, *PROUT in a Nutshell*, vol. 16, p. 38).

The core value of a cooperative enterprise system is "coordinated cooperation," in which free human beings with equal rights and mutual respect work together for the welfare of each other. This differs from "subordinated cooperation," where people work individually or collectively but are under other people's supervision. Subordinated cooperation occurred in state socialist communes that were formed through forced collectivization. True coordinated cooperation does not exist as a prevailing value in any present economic system.

The cooperative system cannot function effectively in an environment of exploitation, corruption, and materialism, nor where they are forced to compete with large corporations for markets and supplies. For cooperatives to succeed, they must have morality among the worker-members, strong management of the enterprise, and community support for the cooperative system. Furthermore, cooperatives need ready access to suppliers and markets for their goods and services. And the members of a cooperative must be able to work in a collective spirit and must share similar material aspirations.

In sum, developing a well-functioning cooperative sector requires moral people with cooperative values, similar material needs, and mutual respect for each other; appropriate organizational and management structures; and a conducive political, social, and economic environment to support small and medium scale cooperative industry and the development of a local economy.

In attempting to establish a viable cooperative economy, it must be considered whether cooperatives can develop in the absence of a sufficient moral base. In other words, must strong moral values first be prevalent for cooperatives to flourish, or do cooperative enterprises themselves help create moral and cooperative values among those participating in the cooperative?

This paper offers a PROUTist perspective for developing worker cooperatives. It examines their principles, advantages, internal organizational structures, supportive infrastructure, and wider environmental factors necessary for their development. It then addresses difficult questions of strategic priorities.

2. PRINCIPLES OF COOPERATIVE ENTERPRISE

Worker cooperatives are firms that are controlled and owned by their members, who are the workers. PROUT cooperatives find affinity with the following principles established by the International Cooperative Alliance:

1. Membership is open and voluntary. Workers are able to become members, usually by nominal holdings of share capital.
2. There is democratic control at all levels of the enterprise, on the basis of one member, one vote.
3. Interest paid on share capital is limited.
4. Workers share in any surplus, usually in proportion to each member's work contribution.
5. Some part of cooperatives' surpluses is devoted to worker education.
6. Cooperatives cooperate among themselves.

Thus, PROUT cooperatives differ fundamentally from private firms. Control of the firm is based on rights derived from a worker's labor contribution, rather than on property rights established by capital investment.

3. ADVANTAGES OF COOPERATIVES

In addition to fostering collective cooperation, cooperatives have the following advantages.

1. Cooperatives are inherently just enterprises: they broaden the base of property ownership and distribution of wealth. This is particularly important for creating democratic institutions and true political equality. Otherwise, those who have the wealth control access to resources, the media, and political power, which acts to corrupt democracy.

2. Cooperatives have demonstrated that they can outperform comparable private sector firms if they have access to sufficient means of production – i.e., capital, labor, and entrepreneurial and managerial talent. Productivity increases for two reasons. First, workers have greater motivation and morale because of greater individual rewards and because of elimination of the conflict between labor and management. Second, there is greater flow and use of information concerning production efficiency and there is greater scope to bring forward and use workers' insights for improving production.

3. Cooperatives enhance worker satisfaction and job fulfillment because of participation in decision-making, equitable sharing of profits, greater opportunity for self-expression and dignity, and an environment of mutual respect and social equity. Cooperatives are one component of what is known as "psycho-economy", a branch of economics recognized in PROUT that is concerned (among other things) with increasing the psychic rewards of individual and collective work activity.

4. Cooperatives provide greater job security than private enterprise. In cooperatives, when it becomes necessary to cut back on production, workers are not immediately fired or laid off. Cooperative members can collectively arrange to reduce work hours or wages in order to maintain the employment of all members of the enterprise.

5. Cooperatives are one component of PROUT's economic system that contributes to local control of the economy. Worker-controlled businesses stay where workers live and are locally owned. This eliminates problems of outside ownership and of profits flowing out of the local economy to outside owners, as occurs in capitalist economies.

4. INTERNAL STRUCTURE AND PROCESS

Membership and Control

Membership in a worker cooperative is open only to those who work in the enterprise. The right of control of the firm and the right to any residual assets and profits is

based on the labor contribution rather than the value of capital or property holdings. Control is based on the principle of one member, one vote, and not on the number of shares or amount of a person's investment in the cooperative. If non-worker shareholders are allowed to become members, it introduces conflicts of interest that can dilute the worker incentive system.

New workers enter the cooperative on a trial basis before they become full members.

Ownership

Several forms of ownership have been used in worker cooperatives:

1. conventional ownership through share capital;
2. social ownership where workers have operation control or usufructuary rights, as was true in Yugoslavia; and
3. collective ownership with workers' having the right to the residual assets of the firm through a system of internal capital accounts.

The last form of collective ownership is practiced in the highly successful Mondragon cooperative federation in the Basque region of Spain.

Worker cooperatives that are structured on a share basis invariably revert to capitalist owned firms if they are at all successful. Workers have an incentive to sell their shares for the best price. Often people interested in become a working member cannot afford the appreciated value of the share, and the share is sold to an outside owner. At the other extreme are cooperatives in England and former Yugoslavia where workers have no ownership stake but merely control the operations of the firm. The assets are socially owned, and workers have no claim on any increases in the net value of the assets. This system encourages workers (particularly older workers with a shorter time horizon in the cooperative) to take out profits or surpluses immediately as wages and finance any long-term investments through debt.

Experience in structuring worker cooperatives shows that in addition to their wages, workers must participate in the growth or decline of the firm's net worth in order to have sufficient incentive for long-term investment in the firm. They do not necessarily need total ownership or control over the assets. Thus, PROUT cooperatives would be structured according to the Mondragon's model of collective ownership that provides a balance of incentives.

Members are required to purchase a share in the cooperative and make an equity investment. It is important that all members have a financial stake in the cooperative. The cost of the share depends on the valuation of the cooperative. In a new cooperative startup, it would depend on the need for equity investment to leverage outside capital. If a new member cannot afford the price up front, it may be possible for the person to pay over time from wages, assuming the cooperative can afford this payout, or to arrange for an equity loan to the member from a cooperative support organization (as discussed below).

A PROUT cooperative system should adopt the innovative Mondragon system of internal capital accounts that spread gains or losses in the net worth of the cooperative to individual workers' capital accounts. In Mondragon the cooperative restricts workers from taking out their balances at will so that it can use the assets for reinvestment in the cooperative. The cooperative pays yearly interest on each account. The balances on each member's account are eventually paid out either on a rollover basis at a designated period of time (for example, five years), or when a worker leaves the cooperative.

Members must sell their shares back to the cooperative in order for control to remain with worker members. Thus, inheritance of shares is not permitted.

Although the Mondragon system is widely considered the best existing model, its steep reserve requirements and policies that restrict members' ability to withdraw their balances until retirement contradict members' rights to their residual assets. Forced savings may work in isolated rural settings but not in highly mobile urban environments.

Diversifying Risk and Ownership

One of the primary barriers cooperatives have had in attracting talented people and capital is that workers are poor, risk adverse, and do not want to concentrate both their savings and source of income in one firm. However, if a cooperative attempts to sell outside shares in order to raise capital and diversify risk, it must then give voting rights to shareholders. This contradicts the principle of control based on a person's labor contribution rather than capital contribution.

A cooperative also has difficulty offering preferred stock that gives first right to a dividend to the preferred stockholder, but without any vote. In a cooperative, there are no outside shareholders who have a vested interest in declaring dividends for preferred stockholders. The workers, who make all decisions, can decide to divide all surpluses as wages and not declare any dividends at all.

Professor Jaroslav Vanek, an internationally known scholar on economic democracy at Cornell University in the United States, has suggested ways of diversifying risk in worker cooperatives through new financial instruments in order to make cooperatives more adaptable in contemporary settings. Ideally workers and managers should own 10 percent of the company. Other interests, including the cooperative support structure, banks, government, the community at large, and outside investors, should hold the other 90 percent.

Outside investors would buy fixed interest rate bonds or variable rate debentures. Variable rate debentures would diversify the risk. Part of investors' return would be paid at a fixed rate; the other part would vary with the profits of the firm so that the investor is sharing the risk. However, the investor would not have a vote. Voting rights would still be based on labor and not capital contribution according to one

person, one vote.

Workers would be required legally to pay out a return to investors based on some percentage of their own income. This would avoid the problem described above whereby workers can take out potential surpluses from value added as wages rather than declaring any profits.

Another investment option is a mutual fund that diversified its investments in various worker-controlled companies. Vanek also sees a potential role for foreign investment through cooperative support structures, particularly in underdeveloped economies. Foreign investors could have some vote in support organizations, or if they were providing technical assistance as well as capital, then they may have a vote at the enterprise level. The vote would be based on their labor participation in the enterprise.

If Vanek's model, while not yet tested, is capable of attracting outside capital without compromising fundamental principles of worker control, it would be a major contribution to economic democracy.

Incentives and Rewards

The incentive system for pay and profit sharing must be fair and at the same time be able to attract competent people to the cooperatives. PROUT advocates rewarding workers' performance according to their skill and contribution but within a minimum and maximum income range. Rewards can also be in-kind payments – such as equipment, education and training, foreign travel – that encourage more productive work. Cooperatives often establish wages according to a ratio between the highest and lowest paid members. The ratio is determined according to time, place, and person. The wage differential would be greater under present conditions than would be anticipated in a fully established PROUT economy.

In addition to wages, cooperatives pay returns on individual capital accounts in proportion to a member's contribution to the growth of the assets. However, this long-term incentive may not be strong enough, particularly in cooperatives with younger members. Cooperatives should also look at annual gain-sharing plans as a more immediate incentive to reward worker performance. These plans devise a bonus formula for performance gains in specific areas of a firm's operations such as labor productivity, cutting costs, improved quality of services or products, or increased customer satisfaction.

Cooperatives must operate as businesses and reflect business performance in their incentive and reward systems. If a cooperative is performing poorly, wages must be set accordingly even if it means that workers do not meet their minimum necessities. The problem of providing a safety net for workers is an issue for the economic or cooperative system as a whole and not for an individual enterprise. However, cooperatives have the choice of reducing all workers' hours rather than laying off

members so that losses are spread equally among the membership.

Hired Labor

Worker cooperatives should discourage the use of hired labor unless it is critical for the business' survival. A dual structure of worker owners and hired labor contradicts the principle of worker control and self-management. Some cooperatives resort to hired labor because the structure of the industry requires seasonal or part-time labor. Where possible, cooperatives should offer hired labor bonuses for productive work even if they do not permit voting rights.

Governance and Management

The degree of collective decision-making depends on the size of the cooperative. Members can make most key decisions in a small collective (maximum of 10 to 12 people). Larger cooperatives elect boards which make policy decisions. Boards select a manager who is a member of the cooperative. The manager is in charge of day-to-day operations. Each cooperative, according to the realities of its business, must decide which decisions are made, respectively, by the manager, the board, or by the entire membership. Guidelines are available from other cooperatives' experience.

To the extent possible workers should participate in all levels of decision making through work teams. The concept of coordinated cooperation means that workers should participate as equal members. Their interests should not be subordinated to those of managers, who often possess greater technical knowledge of the firm and are in a strategic position to control information. Workers build their capacity and confidence to participate effectively in policy decisions through initial involvement in day to day decisions involving routine production tasks.

Ultimately coordinated cooperation requires that members and management possess mutual respect and trust for each other. Where cooperatives have been the most successful, managers serve as educators to develop workers' understanding of the cooperative and the management function.

Formal structures and processes of the cooperative can also help check the power of management. Workers must have access to records and information about the cooperative and must learn how to interpret that information.

Grievance procedures and processes for dispute resolution must be in place. Resolving disputes depends on clear guidelines of behavior and expectations of members, which must be set out in the operating rules of the cooperative and in the performance appraisal process that evaluates each member's work contribution. In grievance processes, unions have represented the interests of cooperative members as workers (as opposed to their interests as owners). A cooperative board or union may resort to an outside mediator to resolve conflicts. A cooperative support organization could possibly undertake the mediation role.

Social Goals

Cooperatives should make a continuous effort to raise the education level and moral standard of all members. In addition, cooperatives can choose or be mandated by law or by cooperative support organizations to set aside a percentage of any surpluses for community and social purposes. Whether mandated externally or voted internally, social goals must be secondary to the primary goal of maintaining the cooperative's economic viability.

Dissolution of the Cooperative

Any surplus of assets after paying the value of the shares can either be distributed to the current members, to current and past members who can be located, or to another cooperative. Some cooperative laws require that assets be distributed to another cooperative in recognition of the role that the state plays in developing cooperatives and the social goal of maintaining a strong cooperative sector.

The suggested PROUT policy on dissolution is to assess the context in which cooperatives are established and determine what is the best practice for establishing a strong cooperative sector.

In some contexts, a policy that prohibits distribution of surplus assets to members may discourage talented people from entering the cooperative sector.

5. SUPPORTIVE INFRASTRUCTURE

Experience in Western economies shows that cooperatives do not survive as isolated enterprises. They must operate together as a system of enterprises with a supportive infrastructure. These cooperative support institutions provide cooperative enterprises with financing, technical and management assistance, joint marketing and purchasing of supplies and services, research and development of new products, cooperative education and training, and lobbying and public relations services. Cooperatives tend to be relatively small enterprises in order to function democratically. The only way they can afford these services that larger companies can provide internally is through mutual cooperation.

The design of appropriate structures and functions of the supportive infrastructure should be based on local capacity and context. From existing experience, two issues deserve particular attention: (1) whether support organizations develop bottom up or top down, and (2) how much control support organizations have over cooperatives.

The strongest cooperative systems have developed bottom-up. For example, in Mondragon and the kibbutzim in Israel, a base of cooperative enterprises first formed and then created their own support organizations according to their needs. These

support organizations later took on proactive roles of developing and supporting new cooperative startups or converting existing businesses to cooperatives.

In a number of Western countries with few existing worker cooperatives, support organizations have been established top down through government, foundations, unions, and other private sector interests in order to accelerate cooperative development. These efforts are relatively new with less dramatic results. Nonetheless, they have had some success in starting cooperatives and providing visible cooperative models.

A second important issue is the degree of control a support organization takes during early stages of developing new cooperatives. Ideally a cooperative should be totally worker controlled. However, if a support organization puts up financing and technical assistance resources, it has a stake in the cooperative's success, both in terms of its economic viability and its ability to function democratically. A new cooperative often requires strong guidance and oversight in the first few years. Some cooperative support organizations have placed their own staff as the manager until the cooperative members learn to manage democratically. Others retain a seat on the board of directors and have a controlling vote over hiring or firing the manager and over the ability to change the cooperative constitution. Once the cooperative is functioning well, the support organization turns over its control to the cooperative members.

The Mondragon system maintains control over new cooperatives by requiring each cooperative to sign a contract of association with the cooperative system's bank. The cooperatives agree to adopt Mondragon's bylaws that establish various operating principles. Mondragon has the power to do this because the cooperatives need financing from its bank. In this way, Mondragon is able to replicate basic cooperative principles and structures throughout the cooperative system.

6. CONDUCIVE SOCIAL ENVIRONMENT FOR COOPERATIVES

Cooperative models serve a useful role of awakening consciousness and showing that there is an alternative way to organize economic activity. However, successful models are few and far between in an environment hostile to cooperatives. For cooperatives to develop on any scale, changes are needed in society's values, political support, and the economic system.

Cooperative Values

Cooperative structures and models are very difficult to create if there is no commitment to cooperative principles or values. The experience of working in a cooperative may help to develop those values, but it is far more difficult for those values to develop at a late stage of a person's adult life rather than during their formative years. Successful cooperative structures require socialization towards

cooperative modes of behavior and thinking at an early stage of life. Family, educational, and social institutions are all potential vehicles for cooperative socialization. Possibly the strongest leverage for intervention is in the school system. Children need to be exposed at an early age to teamwork and rewards for cooperative behavior.

Political Support

The government can implement policies that either encourage or mandate cooperatives. In a PROUTist economy, economic democracy should be a constitutional right. Laws would be passed mandating that cooperatives would be formed in medium scale industries that were not key industries. However, mandatory legislation is only viable if an ethical foundation is already established. Legislation itself does not create the value base. Otherwise forced collectivization is likely to dampen productivity and innovation as occurred in command economies. In absence of full-scale support for cooperatives, government can still "privilege" a cooperative sector through subsidies to develop cooperative infrastructure, tax incentives or preferential bidding to cooperatives for government contracts (i.e. sheltering their markets).

However, if incentives are not designed properly, they can lead to exploiting the cooperative structure for private gain. This has happened in the so-called cooperatives that received some leeway for private gain in command economies.

Decentralized Economy

External economic systems affect the design and behavior of economic enterprises. Increasing internationalization and monopolization of the economy undermines the viability of cooperatives. If they are to operate democratically, cooperatives must be relatively small (not more than 500 people). They do not usually have the scale of operations or resources to compete successfully in highly volatile global markets. Global competition also requires fast response time to changing market conditions.

Cooperatives can adapt to some extent to global markets through mutual cooperation and federated support structures. Yet the more cooperatives are entrenched in global markets, the more they must adopt the behavior of capitalist firms. For cooperatives to maintain democratic processes and create desirable work environments, they need greater economic certainty for marketing goods produced and procuring supplies.

Decentralized, self-reliant economies reduce market uncertainties by minimizing dependence on external markets and exposure to market shocks. The availability of local raw materials guarantees constant supplies to cooperatives. If cooperatives produce for local needs, their goods are easily sold in local markets. Economic certainty creates a positive environment for increasing interest and involvement among cooperative members and fostering acceptance of the cooperative system among local people.